



## TPE 2023 – Case Study Part 2

Erskine

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## Case Study

Last Friday evening, one month since you completed the assignment on Erskine, you were in the pub across from the office enjoying a light refreshment after a busy week. Brian arrived, entered and you caught each other's eye. He looked a little embarrassed to see you but it was Friday evening and even a newly-qualified CA has to rest sometimes! Brian came over, greeted you and introduced his partner as Patricia Erskine. He said that you might know her former husband – Dave – but that they didn't have much time to chat as they were there for a quick drink before going out for a meal at a luxury gourmet restaurant. With that, they headed out to a waiting taxi. Brian has been doing a lot of fine dining over the last couple of months and you had wondered how he does that on a manager's salary.

The weekend has passed, and it is now Tuesday morning. You are at your desk reading the morning paper and one story in particular gets your attention. Interestingly, it concerns the electronics industry. Kelvin Vision Technologies Ltd ('KVT') is in financial distress. Claire Minnow, a partner in another accountancy practice has been asked to convene a meeting of creditors with a view to appointing a liquidator. Could this be an opportunity for Erskine, you wonder? Both companies operate in similar fields. You don't wonder for long as Brian comes over to tell you that Colin has just phoned and has requested a meeting this morning on an urgent matter. You suggest to Brian that it might be linked to KVT. Brian agrees but not for the reason that you thought. KVT is a large trade debtor of Erskine and Brian thinks that Colin's visit may well be in relation to that.

Colin arrives and the three of you meet in Brian's office. Colin is clearly agitated and speaks quite fast.

"I have received a letter from Claire Minnow & Co stating that one of Erskine's customers, KVT, is in creditors voluntary liquidation and that unsecured creditors are unlikely to receive a pay-out. I've been lucky enough to avoid this type of situation with my other business ventures so far but I've been in business for a long time and I understand the basics about what a liquidation is. What I need is for you to clarify for me the specific impact of this on Erskine and any immediate actions we as directors should take."

"At the last year end – 30 June Yr 45 – KVT owed Erskine £432k. They have made no payments since then and the balance outstanding is currently £486k. I have been somewhat concerned at the high level of indebtedness and have phoned around the main Erskine customers and am shocked to discover that most are owed money by KVT. A number of them are unsure if they will survive if they don't receive payment of their debt. Plus, I'm not sure how much of the true picture they are actually telling me. What would be really useful is if you can summarise the impact of all this on Erskine in a few slides so that I can present them to Pete and Dave."

Colin hands you a schedule with the results of his phone calls (Appendix 1). Brian suggests providing a few slides on this for Colin covering the specific implications for Erskine. You write that down as you are confident that it will be you preparing the slides!

"That is not the only bad news I have this morning," continues Colin. "Following your report and valuation of Dave's shareholding, I insisted the directors commission an independent property assessment and valuation of the second unused factory unit." He hands you the covering letter received from the surveyors (Appendix 2). "It is in such poor condition that it may have to be demolished."

“Erskine is generally a sound business, which is why I invested in it 10 years ago. However, I need some advice as to the current position. A lot has happened in the last month since you prepared your report. I am still keen to consider a further investment in the company. As you will remember, Dave wants out. If Pete can be persuaded to stay on and drive through the ideas from your report for improving efficiency and profitability, I think he and I could run the company very successfully. Of course, I would have to get more involved in the day-to-day operations but I relish a challenge.”

Brian concludes the conversation by indicating that he will get you to draft a report outlining Colin’s options for the future of Erskine, in which you will include recommendations for how Colin should proceed, considering his responsibilities as a director.

The meeting concludes and Colin leaves, but Brian indicates that you should stay behind for some further instruction.

“I think that the best way to move things forward will be to have someone else in the team – Cerys Roberts – construct a Statement of Affairs for Erskine and provide it to you. Cerys has some experience in this area, so her work can be taken as being reliable and accurate for your purposes. I know you likely haven’t seen a Statement of Affairs in much detail before, but I trust you should be able to make appropriate conclusions from it based on your training. You should be able to use this Statement of Affairs, once drafted, as a key ingredient in writing the report requested by Colin. Cerys is pretty quick at drafting these things, she may even have got it finished by the time you sit back at your desk! I’ll just phone her now.”

You go straight back to your desk after the meeting and see an email from Cerys with the Statement of Affairs completed (Appendix 3). “Cerys surely does deserve her reputation of being unrealistically fast in a narratively convenient way”, you think to yourself.

As you begin to get started, you make a mental note to keep your firm’s compliance partner informed of any other issues you encounter when preparing the various documents.

### **Required:**

- Create the draft content and speaker notes for a brief presentation suitable for Colin to deliver to Pete and Dave, covering the specific implications for Erskine of KVT going into liquidation;
- Draft the report to Colin outlining his options for the future of Erskine; and
- Prepare a note of any other issues you consider to be relevant to your firm’s compliance partner.

## Appendix 1

### Colin's note from phoning around Erskine's customers

Name of debtor	Amount owed to Erskine £'000	Comments
Allander Components	143	Has a large exposure to KVT – wouldn't say how much – directors very worried that they might not be able to continue.
Blane Peripherals	76	KVT cleared their account last month – very lucky escape! KVT does account for 20% of their turnover.
Carron Computers	23	Small outstanding debt with KVT inconvenient but not too problematic.
Dualt Components	117	Thinks they should be able to recover their goods at KVT under the retention of title terms in their contracts.
Endrick Engineering	68	Does not use KVT so should be no problems here.
Finglen	<u>75</u>	Could not reach any of the directors by phone. Have left message asking them to call back.
<b>TOTAL</b>	<b><u>502</u></b>	

## Appendix 2

### Covering letter received from Ivy & Co Chartered Surveyors

Ivy & Co Chartered Surveyors  
27 Prince John Street  
Edinburgh  
EH1 1IV

The Directors  
Erskine Electronics Ltd  
Clyde Business Park  
Port Glasgow  
Inverclyde

Date as postmark

Dear Sirs,

#### **Empty Factory Premises**

We refer to your instructions to provide an open market valuation for your factory premises near Port Glasgow.

We understand that the subjects were purchased in Yr 37 for the sum of £150,000 and have lain empty since that time except for a short period when they were used to store excess inventories.

On the day of our visit, the weather was poor and excessive water ingress was noted. This has clearly been ongoing for some time. There was evidence that entry had been obtained forcibly to the premises and arson had been attempted.

Elements of the steel structure were misshapen, and, upon close inspection, we found considerable evidence of rust and other degradation of the supporting structure. We strongly recommend obtaining a specialist structural engineer's report.

In light of the above problems, we are not in a position to provide an open market valuation as we are of the opinion that the market for such subjects in their current condition would be extremely limited. The value of the land might be in the region of £20,000.

Yours faithfully,

Ivy & Co Chartered Surveyors

## Appendix 3

### Draft Statement of Affairs of Erskine and notes from Cerys

#### Estimated Statement of Affairs of Erskine Electronics Ltd.

	Estimated Realisable Value	Notes
<b>Assets</b>	<b>£</b>	
Assets not specifically secured (List A)	2,008,300	
Assets specifically secured (List B)	<u>2,976</u>	1
Estimated total assets available for preferential creditors, holders of floating charges and unsecured creditors	2,011,276	
<b>Liabilities</b>		
Preferential Creditors (List C)	<u>(55,000)</u>	2
Estimated balance of assets available for holders of floating charges and unsecured creditors	1,956,276	
Estimated prescribed part of Net Property	(394,255)	3
Holders of Floating Charges (List D)	<u>(1,165,000)</u>	
Estimated surplus as regards holders of floating charges	397,021	
Add: Estimated prescribed part of Net Property	394,255	3
Unsecured Creditors (List E)	<u>(1,326,000)</u>	
Estimated deficiency as regards creditors	(534,724)	
Issued and called up share capital	<u>(100,000)</u>	
Estimated deficiency as regards members	<u>(634,724)</u>	

#### Notes from Cerys

- 1) As the motor vehicles are owned subject to a hire purchase arrangement, this figure is reached after deducting the outstanding liability from the estimated realisable value of the vehicles.
- 2) This amount sees all employee claims satisfied.
- 3) The calculation of the 'prescribed part' is complicated and I see no reason to go into it here. It should suffice to say this figure is not available to holders of floating charges, and is instead distributed to unsecured creditors. You should see it being deducted and then added back later, as it is 'removed' as far as the floating charge holder sees, but then 'reintroduced' for the unsecured creditors.

**END OF PAPER**