

Winding Down Your Architecture Practice

Key Considerations

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We are frequently approached by architects looking to wind down their practices, because either (i) they want to retire, (ii) they want to close down because of economic uncertainty, or (iii) they simply do not want to carry on with their practice and they will gain little value in selling it. However, in winding down a practice, we recommend the following key issues are considered:

1. Your contractual and professional obligations as an architect to maintain professional indemnity insurance run-off cover; and
2. the appropriate method of closing down your architecture practice.

1. **Obligation to maintain professional indemnity insurance run-off cover**

In winding down your practice, one important issue is whether or not you have an obligation to take out professional indemnity run-off cover insurance.

Run-off is a form of professional indemnity insurance that covers the historic liabilities of a practice after it has been wound down. This cover is important as professional indemnity insurance is provided on a claims made basis. This means that if a claim is made and you want cover to be provided, professional indemnity insurance needs to be held on the date the claim is made against your practice, rather than the date of the incident itself.

In considering whether or not to take out run-off cover, it is necessary to consider your contractual obligations and professional obligations as an architect.

Contractual obligations

With regards to your contractual obligations, your practice may have contractual liabilities that last for 6 or 12 years (from the date of breach of contract) depending on whether your contracts have been entered into as simple contracts or deeds. In addition, such contracts may contain contractual obligations to maintain insurance for 6 or 12 years from completion of the services or practical completion. It is therefore prudent to take out professional indemnity run-off cover insurance.

If you enter into a contract knowing that you will be closing down your practice and that you will not have run-off cover in place, then you risk a potential claimant bringing a personal claim against you (see the decision in *Merrett v Babb*). In that scenario, a court might well have sympathy with the claimant.

Professional obligations

In addition to your contractual obligations, you are likely to also have professional obligations to maintain run-off cover, as a member of your professional body. In particular, as a registered architect in the UK you will have professional obligations to maintain run off in accordance with the Architects Registration Board (**ARB**) and/or as a member of the Royal Institute of British Architects (**RIBA**).

ARB

The ARB has identified the standards of professional conduct and practice that are expected of persons registered as architects (under the Architects Act 1997). The Architects Code: Standard of Conduct and Practice (the **Code**) provides that architects are expected to have adequate and appropriate professional indemnity insurance cover for their practice, including an expectation that architects will maintain a minimum level of run-off cover.

Upon the dissolution of your practice, the ARB expects you to ensure that adequate run-off provisions are put in place to cover any outstanding liabilities. The ARB recommends that architectural practices should acquire a minimum of six years of run-off cover. In relation to the amount of cover required, the ARB advises that the cover should be held at the same amount as the highest level of cover maintained for the three years preceding the date you ceased practice. Once the run-off cover expires, it is recommended by the ARB that you continue to monitor any risk you have of a claim being made against you.

As a registered architect, you are therefore under a professional obligation to maintain run-off cover in order to ensure compliance with the Code. Any breach of the Code may be taken into account in any disciplinary proceedings before ARB's Professional Conduct Committee.

RIBA

The RIBA's Code of Professional Conduct sets out the standard of professional conduct and practice required of all RIBA members. Therefore, if you are a member of the RIBA, it is important to be aware of the professional obligations relating to run-off insurance.

The RIBA stipulates that members must have in place adequate run-off cover when they cease practising. The RIBA's guidance mirrors the ARB's Code by stating that a minimum of 6 years' worth of run-off cover should be maintained. The RIBA similarly advises that you should continue to monitor any risk of a claim being made against your practice after this time. The amount of run-off cover required by the RIBA is also consistent with the ARB Code,

i.e. the same amount at the highest level cover maintained for the three years prior to the cessation of practice.

Therefore, from a professional perspective, you have a professional obligation to maintain an adequate level of professional indemnity insurance run-off cover after you have wound down your practice.

2. Methods of closing down a practice

In terms of how to wind down your practice, there are various methods available. In this article we will assume the practice is solvent at the time of closure.

Strike-off

You may choose to voluntarily strike your architecture firm off the Companies House register using the method known as "voluntary strike-off" (in accordance with section 1003 of the Companies Act 2006). Note that you will need to distribute all cash and assets in the company before the company is dissolved as otherwise such assets will vest *bona vacantia* i.e. belong to the Crown.

This method of dissolution is often an attractive procedure as it is relatively quick, straightforward and cost-effective. Once a company is struck off the Companies House register it is deemed to be dissolved and there is no longer a legal entity (and therefore there is no one to sue).

However, note that despite the company's strike-off and dissolution, future claimants may apply to restore the company to the Companies' House register at any time, if they have claims against the company.

Although a company does not have to formally discharge all of its liabilities before it is struck off, it must however notify all contingent and prospective creditors (which would include a party to whom an existing obligation is owed but in respect of which a present liability has not arisen and may never arise e.g. a potential claim). Note that failure to inform such creditors would constitute an offence under the Companies Act 2006. It will be an aggravated offence punishable by a term of imprisonment if the person's failure to perform this duty is with the intention of concealing the application.

Solvent liquidation

Another method of dissolution is via voluntary liquidation, which is the most costly procedure. There are two main types of liquidation – creditors' voluntary liquidation (**CVL**) and members' voluntary liquidation (**MVL**). A CVL is entered into when a company is insolvent (which we will not be discussing in this article) and an MVL is entered into when a company is solvent.

To initiate an MVL, you must make a Declaration of Solvency (for English and Welsh companies). You will need to review your company's assets and liabilities before making a declaration.

To make a declaration of solvency you must produce a written statement stating that the directors have assessed the company and that they believe it can pay its debts in full together with any interest within a specified period, not exceeding 12 months from the commencement of the winding up of the company (pursuant to section 89 of the Insolvency Act 1986 and the Insolvency (England and Wales) Rules 2016). You will also need to include the statement of your company's assets and liabilities. Once this has been confirmed, a shareholders'/members' meeting is convened to appoint a liquidator to wind down your company.

It is important when making a statutory declaration of solvency that the directors assess the actual and contingent liabilities of your company (including pending or potential claims) and have reasonable grounds for the opinion that your company would be able to pay its debts in full within the period specified in the declaration (which must not exceed 12 months from the commencement of liquidation).

Should a declaration of solvency be made falsely or if it is found to be inaccurate the repercussions for the directors can be very severe, including an unlimited fine and up to 2 years imprisonment. It is therefore prudent to ensure that the company holds adequate professional indemnity insurance to capture any potential liabilities that arise in the period specified in the declaration of solvency.

Key Take Away Points

If you are considering closing your practice, we recommend that you give careful consideration to your ongoing contractual liabilities and obligations. You are obliged to maintain appropriate run-off cover, to ensure that you can meet any future contractual liabilities and also that you comply with your professional obligations as an architect.

Whether you choose voluntary strike-off or a MVL, you will need to consider any actual and contingent liabilities (and again maintain adequate run-off insurance cover).

We appreciate that many architects are finding it difficult to purchase run-off cover at an affordable price and on a basis which does not require annual renewal, leaving the risk that it might not be available in the future. It is therefore essential that you speak to your insurance broker about what options are available for run-off cover. You should also seek financial advice from an accountant/insolvency practitioner about what closure process is most appropriate and take legal advice on any potential liabilities and obligations your practice may have.

Should you have any queries or are seeking advice on the matters raised in this article, please do not hesitate to contact James Hutchinson (J.Hutchinson@beale-law.com) or Madeleine Kelly (M.Kelly@beale-law.com).

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