Ethics Code for Insolvency Practitioners

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1. The new code came into force on 1 January 2009 and had been long time in the making, work began in 2005. It is based on and follows the format of Code of Ethics for Professional Accountants produced by the International Federation of Accountants ("IFAC").

2. This in itself created an inherent problem in that not all IP's are members of an accountancy body, but nonetheless follows the structure of the IFAC.

3. The Code is not a set of rules, although referred to as a Code, but sets out a series of directing principles and base standards to which all insolvency practitioners must adhere. The code itself suggests contacting the relevant authorising body – see paragraph 25(b) if there is any doubt as to the implementation of the Code. The ICAEW operates an Ethics Helpline where insolvency practitioners regulated by the ICAEW can seek guidance – helpline staff are exempt from the duty to report misconduct.

4. The Guide mirrors the framework approach of the IFAC Code and sets out the five fundamental principles to which all practitioners must adhere:-

   4.1. Integrity;

   4.2. Objectivity;

   4.3. Professional competence and due care;

   4.4. Confidentiality;

   4.5. Professional behaviour.

5. Integrity, this in reality goes without saying. An insolvency practitioner should be straightforward and honest in all professional and business dealings.

6. Objectivity – an insolvency practitioner should not allow:-

   6.1. Bias;

   6.2. Conflict of interests, or;

   6.3. Undue influence of others;

   to override his business or professional judgment.

7. Professional competence and due care, an insolvency practitioner should keep up to date with all developments and ensure up to date advice is provided, continuing education.

8. Confidentiality – keep information obtained as a result of professional and business relationships and not to be used to the personal advantage of the IP. As drafted, the fundamental principle of confidentiality makes it clear that where an insolvency practitioner has a legal or professional right or duty to disclose he may do so.

9. Professional behaviour- requires compliance with relevant laws and regulations and avoidance of any action which brings the profession into disrepute. Courtesy has been added to this principle – the only difference from the IFAC principles. This is as a result of feedback received from insolvency practitioners during consultation on the code.

Identification and categories of threats

10. An insolvency practitioner needs to take reasonable steps to identify possible threats and in particular threats in existence at the time of or immediately preceding the acceptance of an appointment. In reality this means having in place systems to ensure that any threat to the fundamental principles are identified and evaluated.

11. Those threats fall into five broad categories:-

    11.1. Self-interest, resulting from the financial or other interests of the insolvency practitioner, his or her practice or of the close or immediate family member of an individual in the practice. By way of example:

        11.1.1. An individual within the practice having a claim as a creditor which would require evaluation;

        11.1.2. Concerns about damaging a possible business relationship;

        11.1.3. Concerns about potential future employment.

    11.2. Self-review threats, which occur where a previous judgment made by an individual within the practice will need to be reviewed by the insolvency practitioner. Examples, which may diminish over time, are:

        11.2.1. Acceptance of an appointment over an entity which employed an individual within the practice or to which such an individual was seconded.

        11.2.2. Where the insolvency practitioner has carried professional work of any description (including an IBR) and sequential appointments.

    11.3. Advocacy threats – where an individual within a practice promotes a position to a point where there subsequent objectivity may be compromised. Examples are:

        11.3.1. Acting in an advisory capacity for the creditor;

        11.3.2. Acting as an advocate for a client in litigation or a dispute.

    11.4. Familiarity threats which may occur where, because of a close relationship an individual becomes too sympathetic or antagonistic to the interests of others. Examples are:-

        11.4.1. Where an individual within a practice has a close relationship with anybody having a financial interest in the insolvent entity;

        11.4.2. Where an individual within a practice has a close relationship with the potential purchaser of an insolvent entity.

    11.5. Intimidation threats – which may occur when an IP may be deterred from acting objectively. Examples are:-

        11.5.1. Pressure being exerted by an employer over an employed IP;

        11.5.2. Threatened with litigation;

        11.5.3. Threatened with a professional complaint.

12. An insolvency practitioner should take reasonable steps to evaluate any threat to the fundamental principles and put in place appropriate safeguards. In particular they should consider whether a reasonable and informed third party in possession of all the relevant information, including the significance of the threat would consider any safeguards acceptable.

Safeguards

13. What safeguards should be applied is fact specific to each case. Generally they fall into two broad categories:-

    13.1. Safeguards created by the profession, legislation or regulation and;

    13.2. Safeguards in the work environment.

14. The safeguards seek to create a work environment where the threats are indentified and the introduction of appropriate safeguards. Examples include:-

    14.1. Leadership which stresses the importance of compliance;

    14.2. Monitoring and quality control of engagements;

    14.3. Documented policies;

    14.4. Policies and procedures:-

        14.4.1. requiring the consideration of the fundamental principles of the code before the acceptance of an appointment:

        14.4.2. concerning the identification of potential personal and third party conflicts;

        14.4.3. prohibiting non insolvency team members from inappropriately influencing the outcome of an insolvency appointment.

    14.5. Training and education;

    14.6. Senior manager specifically appointed to oversee the adequate functioning of the safeguarding system.

Application to insolvency profession

15. The second part of the code deals with its specific application to insolvency appointments and emphasises the overriding requirements to act in accordance with insolvency legislation and his role as an officer of the court (where appropriate). The starting point is that before accepting an insolvency appointment an insolvency practitioner should consider whether that acceptance would create threats to the fundamental principles and if it does whether appropriate safeguards could be put in place to reduce the threats to an acceptable level.

16. The code then suggests various safeguards which might be considered, including:-

    16.1. Involving another insolvency practitioner within the practice to review work done:-

    16.2. Consulting independent third parties, such as the creditors committee;

    16.3. Joint appointments it is worth noting that where a practitioner is specifically prohibited from accepting an appointment taking a joint appointment is not an adequate safeguard;

    16.4. Legal advice;

    16.5. Chinese walls;

    16.6. Application to the court for directions.

17. Where the threat cannot be reduced to an acceptable level then the insolvency practitioner should not accept the appointment. The code emphasises that in all cases the insolvency

practitioner will need to exercise his judgement to consider what a reasonable fully informed third party would consider reasonable.

18. Again before accepting an appointment an insolvency practitioner should take reasonable steps to identify circumstances which could pose a conflict of interests and in particular where:-

    18.1. He has to deal with competing claims from separate entities over which he is appointed;

    18.2. Sequential appointments;

    18.3. A significant relationship has existed with the entity or someone connected with it.

19. Further an insolvency practitioner should ensure that the following matters have been considered pre-appointment;

    19.1. Obtaining an understanding of the entity, its business and managers

    19.2. General industry knowledge;

    19.3. Assigning sufficient experienced staff;

    19.4. Using experts where necessary.

20. An insolvency practitioner should also ensure that he or she only accepts appointments where they have sufficient expertise or can acquire the necessary competencies.

21. Significant professional relationships can be a threat to the fundamental principle of objectivity. The concept of a significant relationship differs from the previous test of "material professional relationship", but in reality it is unlikely to differ a great deal from the previous test When applied to a potential appointment. Often for accountants, material suggests something quantifiable, something that has a monetary value like a fee or a shareholding. In insolvency, relationships are often about more than financial matters, it's about who the insolvency practitioner knows as well. In the former guide a personal relationship was given as an example of a self interest threat. That is why the concept of significant professional or personal relationship was introduced. It is about looking at more than the financial and quantifiable aspects of a relationship, but also the "softer" side. Often these aspects of a relationship will only be within the knowledge of the insolvency practitioner or the insolvency team – that is why assessment of the relationship is important.

22. Professional and personal relationships include relations with:-

    22.1. The entity, its directors, shareholders and employees; it is worth noting that the entity also includes a bankrupt or the debtor subject to an IVA.

    22.2. Any business partner, subsidiary or associated companies of the entity;

    22.3. Secured or unsecured creditors;

    22.4. Close or immediate family of officers of the entity.

23. In assessing whether the relationship is a significant to the conduct of the insolvency appointment the Code gives examples of the matters which should be taken into account including:-

    23.1. The nature of any previous relationship with the entity;

    23.2. The impact of that work on the insolvency of the entity;

    23.3. The level of the fee;

24. How recently the work was carried out, the more recent the more likely that there will be a threat to the fundamental principles. The carrying out of audit work within the previous three years will amount to a significant professional relationship. There is however a carve out for members' voluntary liquidations.

25. If safeguards cannot be introduced to protect against the treats to the fundamental principles then a significant personal or professional relationship exists and the insolvency practitioner should not take the appointment.

26. In dealing with the assets of the entity the insolvency practitioner should not acquire directly or indirectly, any assets of the entity nor knowingly permit any individual within the practice to do so. The prohibition extends to family members of the insolvency practitioner or individual.

27. In the case of a pre-pack the threat to objectivity can be addressed by independent valuations. Any decision making process must be transparent, understandable and readily identifiable to all third parties affected by the sale.

28. The code also provides for:-

    28.1. Referral fees and commission payments, which should not be accepted unless there are sufficient safeguards in place to reduce the threats to an acceptable level, which may include disclosure in advance of any arrangement and to creditors.

    28.2. The payment of commission remains prohibited;

    28.3. Guidelines as to advertising;

    28.4. Gifts and hospitality.

Record keeping

29. Towards the end of the code there is one of the most important provisions. It states that an insolvency practitioner will always have to justify his actions and be able to demonstrate the steps that he took and the conclusions he reached in identifying and responding to any threats, both leading up to and during the appointment by reference to written contemporaneous records.

30. These records should be sufficient to enable a reasonable and informed third party to reach a view on the appropriateness of his actions.

Conclusions

31. Overall the code does little more than codify what should have been best practice in any event, but it is nonetheless important that regard is had to it in both word and spirirt.

32. This is important to insolvency practitioners, not only within the context of the conduct of any insolvency event, but also because of the potential consequences of any breach.

33. The courts have made it clear that the breach of the code will not in itself be actionable it will be a factor which can be taken into account (see SISU CAPITAL FUND LIMITED V TUCKER [2006] BPIR 154). In addition any breach is a cheap and easy way for a disgruntled creditor or bankrupt to make a complaint, the response to which may be time consuming and costly.

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