



Fair Business
Banking

Resolving Insolvency: Restoring confidence in the system

*A report by the APPG on Fair Business Banking
produced with the support of City law firm Humphries Kerstetter*

September 2021

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Foreword

The production of this report has been a sobering experience. We started out aware of a number of complaints about Insolvency Practitioners (IPs). However, it was only when we put out a call for evidence that we became aware of the volume and severity of the complaints in this area. We were presented with evidence of intimidation, deception, dishonesty and even misappropriation of assets, all involving IPs supposedly performing their court appointed functions.

Some of the cases we looked into are well known, Silentnight, Comet, HBOS Reading. All different in their own ways, but also all containing the same underlying characteristics. Perhaps the most important of these characteristics was the willingness of IPs to sell their independence, and their considerable powers, in return for an appointment to an insolvency case. As the cases below demonstrate, far too many IPs view their court appointed powers as little more than a commodity to be sold to the highest bidder.

Another defining characteristic of the insolvency industry that emerged from our work is how far IPs have departed from the core principles of the Insolvency Act, that rescuing a business should be the primary goal of their work. As defined by the Act, Objective One of any administration should be to rescue a company as a going concern, if at all possible. How many administrations result in Objective One? No one could tell us. None of the firms or their regulators compile this data. Any experienced IP can tell what the answer is likely to be though. Pretty much no administrations achieve Objective One.

We accept that any call for evidence, such as the one we made back in January, will be self-selecting. Only people with grievances will come forward, but even viewed in the knowledge of this obvious distortion, the evidence was startling. As the Comet and Silentnight cases demon-

strate, even the most senior IPs, from the most well-regarded firms in the country, will break the rules when large fees are on offer.

What is anyone doing about this? Very little is the depressing truth. True there have been one or two high profile regulatory sanctions in recent years. But dig deeper into the data on fines handed out under the current self-regulation regime and it becomes readily apparent there is very little jeopardy for an IP who is prepared to break the rules. Over the last 10 years just five IPs have had their licences removed as a result of a complaint¹. To put that into perspective, over the same period there were close to 8,000 complaints. Where fines are handed out, they are generally derisory, rarely exceeding four figures.

Should we expect more from the Recognised Professional Bodies (RPBs) that self-regulate the industry? The real-world answer to this must be no. These are bodies that were set up to represent their members, not to regulate them. They get their funding from membership fees in what is effectively a competitive market. It doesn't require much insight to work out what would happen to membership numbers if one of the four RPBs were suddenly to take a tougher approach to regulation and sanction than the others. Their members would simply migrate to a more friendly 'regulator'.

As legislators we have to be realistic about incentives and outcomes. There is a lot of money to be made in insolvency. This is, of itself, not necessarily a bad thing. But the outcomes this situation is currently producing are contrary to natural justice and our goal of building a fairer, more efficient economy. As our report details the industry is currently beset by opaque appointment processes, secret panel agreements with powerful creditors, IPs failing to bring legitimate claims for the benefit of wider interests, secondments to the same powerful creditors to generate business, a weak system which blesses

1 Insolvency Service figures 2010 - 2019

an IP's conflict of interest once it is disclosed and inadequate regulatory oversight.

Insolvencies happen for many reasons and rescue is too often ignored. The time is over for a default position which implicitly blames management and sanctions a private contractor to help the strongest creditor collect what they can. We have put forward five simple changes to the current regulatory and legal system that govern administrations. We believe that these changes could have a profoundly positive impact on how the industry conducts itself which, over the longer term, will inevitably benefit the wider economy. We look forward to discussing these recommendations with the industry and debating them in Parliament.

Kevin Hollinrake MP, Co-Chair of the
APPG on Fair Business Banking

Executive Summary

Insolvencies directly impact up to 1% of national turnover, roughly £23bn each year, and in the UK in 2019 over 120,000 businesses were made insolvent. There is universal acceptance that a well-functioning insolvency regime is a vital part of the economy, giving firms a place to turn when things aren't going well. Since the APPG on Fair Business Banking was formed, however, it has received a steady stream of complaints about the insolvency profession, prompting an investigation into practices, any issues and potential solutions.

Insolvencies are carried out under the watchful eye of 1,600 practising and licensed Insolvency Practitioners (IPs) in the UK. IPs wield considerable economic and legal power with the ability to compel people to attend interviews, seize and sell assets and remove directors from their posts. This power comes with a responsibility to think beyond their own self-interest as set out in the Code of Ethics. A common theme in complaints received by the APPG is that IPs protect the interests of the party with the power to appoint them, generally the secured creditor or bank, rather than promoting the interests of the company facing insolvency. While many IPs act professionally and ethically, the complaints remain an area of concern.

Due to a lack of a public tender or formal process for appointing IPs, creditors are able to make improper requests of IPs. Many pre-administration appointments are carried out in relative secrecy - understandably - to avoid public knowledge of an imminent insolvency. As a result, there is a lack of available detail on negotiations taking place prior to an insolvency, more specifically, what was agreed between the IP and appointing party. In an individual case, IPs published and presented a leaflet aimed to increase business by explaining how the administration process can be adapted so the creditor can retain 'maximum control' over the administration.

There is an unfortunate lack of transparency surrounding panel agreements between banks and IPs due to commercial confidentiality. These panel agreements have been claimed to grant IPs, in return for signing up to agreed terms on costs and service delivery, a steady stream of work from the bank. In fact, no IP on a panel, from what we found, would litigate against the bank that had appointed them. An email from a former partner at a major accounting firm confirmed 'if it came to a case where litigation is appropriate, we would have to decline to act given our panel status with all the major Banks'.

The question of conflicts of interest arose again in cases that flowed from the 2008 crash. It emerged that it was standard practice for banks concerned to require their borrowers to undertake an Independent Business Review ('IBR') for their security. IBRs were paid for by the business but undertaken by an IP from the bank's panel, therefore the IPs contractual relationship was with the bank rather than the business. The reports would advise on the viability of the company and provide advice on bank proceedings. In many cases the IP not only advised that the company should go into insolvency but was then rewarded with the appointment.

The current regulatory regime requires IPs to be a member of Recognised Professional Bodies (RPBs), there are currently four such organisations in England and Wales. RPBs are subject to oversight from the Insolvency Service (IS) who acts on behalf of Government. Evidence shows that self-regulation fails to sanction many misconducts, is slow and has a lack of transparency. As of 1 January 2019, 200 complaints remained unresolved after 12 months despite RPB's aim to complete investigations within six months. Over the last seven years, only three IPs have suffered the ultimate punishment of having their licences removed. Moreover, RPBs can only regulate their own members. The APPG has received examples where IPs move RPBs to avoid sanctions.

Evidence shows clear conflicts of interest, and a

failure of the current system of self-regulation to address problems in the profession. As a result, we propose the following five recommendations:

A conflict of interests ban: We recommend a ban on taking appointment as IP where the IP has personally been involved in pre-appointment work for any interested party in the 2 years before the appointment. This creates true independence, ensures outcomes are not skewed by conflicts of interest and would prevent administrators and creditors discussing pre-administration strategies.

A single regulator with an Ombudsman: The 2019 Insolvency Service Call for Evidence resulted in the creation of a power for the Secretary of State to create a single regulator in place of current RPBs, a power which expires in October 2022. Using this power would improve consistency and confidence in the profession and avoid the conflicts of interests that arise within RPBs, namely the tension between protecting reputation and being awarded work. Meanwhile, an Ombudsman would offer dispute resolution to complainants and professionals, bringing greater fairness and transparency to the sector.

Placing the Code of Ethics on a statutory

footing: During investigation, IPs and RPBs repeatedly discussed the importance of the Code of Ethics in holding them to acceptable standards, despite the lack of force of law it holds. By placing the Code on a statutory footing, with provision for reliance on breaches by shareholders and creditors, it would increase enforcement of ethical behaviour in the profession.

A centralised database recording the

outcomes of administrations: In years since the Enterprise Act, no proper assessment of the effectiveness of the statutory objective of rescue has been possible because of a lack of tracking of whether the first, second or third statutory objective has been achieved. This also leads to a lack of accountability within the profession. We

propose that the new regulator maintains a centralised database to encourage rescue culture to be taken more seriously. Moreover, this would increase transparency in the appointment of IPs, allowing the monitoring of links and potential conflicts of interests between creditors and IPs.

Further rule changes in support: In order to provide more clarity on procedures, legislative amendments should be made, including prohibiting administrators from discussing pre-agreed administration strategies with appointing creditors, removal of lenders' right of veto in appointing IPs, encouraging IPs to document and demonstrate that all practical avenues to rescue have been explored to emphasise rescue as the primary objective, extending the evaluator process to cover asset sales over £5 million, and re-consideration of extending the CIGA moratorium to financial contracts.

Report on findings

Whichever end of the telescope you choose to view the UK economy through, insolvency looms large. Study the big picture and the macro-economic impact is enormous. In England and Wales insolvencies directly impact up to 1% of national turnover, roughly £23bn², each year. These figures relate to 18,000 companies employing 187,000 people. Not all of these jobs will be lost, some insolvencies result in businesses being saved and jobs preserved. Nonetheless the impact on the national exchequer, on confidence and on communities is vast.

Although the number of individual insolvencies is huge, the impact just one insolvent company can have on the broader landscape is dramatic. In 2017 the 10 largest insolvencies accounted for over 40% of the economic value by revenue of all 18,000 companies that ran into trouble. Mistakes, deliberate or otherwise, made during the insolvency of these companies can have a significant impact on the economic landscape occupied by us all.

Focus in on the detail of each insolvency and their relative importance balloons. Every corporate insolvency, no matter how small, will come with its own tale of personal dreams shattered, jobs, homes and families all put at risk. The subject of this paper is corporate insolvencies and their effect on the economy as a whole, however we should never forget that what really matters here, whichever way one looks at the subject, is the impact on the individual.

It is against this background that there is universal acceptance that a well-functioning insolvency regime is a vital part of the economy. The responsibility for this work is entrusted to 1,553 licensed Insolvency Practitioners (IPs) in England and Wales, of which 1,236 are actively

practicing³. These individuals wield considerable economic and legal power. Each one acts as an Officer of the Court when taking on insolvency work. They can compel people to attend interviews, seize and sell assets and remove directors from their posts. Their powers are extensive, but entirely necessary if an IP is to fulfil their role. With that power comes responsibility. As officers of the court, IPs have a duty⁴ to act honourably and fairly. More than this, as part of the wider accountancy profession they also have a responsibility to think beyond their own, or their clients' self-interest. As set out in the accountancy Code of Ethics⁵:

A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. A professional accountant's responsibility is not exclusively to satisfy the needs of an individual client or employing organisation.

The work of insolvency practitioners has been subject to sustained and ongoing examination by authorities in recent years. However much of the work that has gone into exploring the regulation and legislation surrounding the insolvency industry has focussed on the conduct and behaviour of directors and companies in the period leading up to administration. This work has included introducing changes in 2020 to support businesses struggling due to the coronavirus pandemic. Longer-term the Department for Business, Energy and Industrial Strategy has published numerous briefing papers, including in May 2016 A Review of the Corporate Insolvency Framework: A consultation on options

2. Figures for England and Wales, 2017, as produced by the Insolvency Service. Figures for Scotland are assumed to be of similar scale

3. Insolvency Service figures for 01/01/20 - <https://www.gov.uk/government/publications/insolvency-practitioner-regulation-process-review-2019/annual-review-of-insolvency-practitioner-regulation-2019#fnref:4>

4. As set out in Ex parte James (1874)

5. <https://www.icaew.com/-/media/corporate/files/members/regulations-standards-and-guidance/ethics/icaew-code-of-ethics-2020.ashx?la=en> Note that this is not the same code as the insolvency code of ethics discussed below.

for reform⁶ and in March 2018 Insolvency and Corporate Governance⁷. More recently, in July 2019 the Insolvency Service produced a call for evidence as part of its examination of Regulation of insolvency practitioners, Review of current regulatory landscape⁸.

This work is welcome, however it does not directly address all of the concerns raised with the APPG on Fair Business Banking. In the years since the APPG was established to promote better standards in the banking industry, we have been presented with a steady stream of case studies about troubling behaviour in the world of insolvency. Of course, these reports are by definition concerned with cases where something has gone wrong. It should be recognised from the outset that while the focus of this paper is on the how, when and why things go wrong, we accept that in many cases IPs act professionally and ethically, often in difficult circumstances. That said, the complaints remain. This paper examines the insolvency profession as a whole, assessing whether issues raised with the APPG and elsewhere are part of a wider pattern and then suggests changes to address any failings identified.

It would be impossible to produce a paper such as this without identifying certain individuals and companies. Where this has happened, it is primarily because their names are already in the public domain. However, our interest is not in naming and shaming any individuals, but rather examining the system, and whether there are structural problems in the insolvency regime in England and Wales, which allow, or even encourage, wrongdoing to flourish.

6. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/525523/A_Review_of_the_Corporate_Insolvency_Framework.pdf

7. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/691857/Condoc_-_Insolvency_and_Corporate_Governance_FINAL_.pdf

8. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/816560/Call_for_Evidence_Final_Proofed_Versionrev.pdf

As part of our work, we have contacted all the major accountancy firms, the regulators and the Insolvency Service with a series of questions and an open invitation to respond to the general theme of our investigation. By and large we had a positive response to our questions, and we are grateful to all those who responded. Parties who responded included eight of the largest accountancy firms⁹, the Insolvency Service, the IPA and the ICAEW. Some of the responses were detailed and considered, and therefore more helpful. Other firms chose to respond to the questionnaire by means of a narrative setting out their view of the standards and practices in the industry. Where responses to the questionnaire are directly relevant to the findings of this report they have been included in the relevant section below. However, it is worth recording that most of the industry participants who responded to our questions were positive about their industry, said standards were high and considered that in many ways the UK leads the world in the provision of insolvency services.

The narrative

Complaints about IPs started to come into the APPG on Fair Business Banking almost as soon as it was set up in 2012. Time and again we heard similar stories from company owners.

'My bank mis-sold me a financial product that caused my business to go under, yet the IP who is now running the show is refusing to investigate the matter.'

'I am having to fight tooth and nail to get the IPs interested in pursuing redress against the bank.'

'The IP is refusing to even contemplate litigation.'

The common theme was that instead of promoting the interests of the company and all parties to the insolvency, the IP was protecting the in-

9. PricewaterhouseCoopers, Deloitte, EY, KPMG, Grant Thornton, BDO, PKF and RSM

terests of the party with the power to appoint them, generally the secured creditor or bank. Of course, each complaint had its own features, some concerned more obviously egregious behaviour, others felt as if they were rooted in sour grapes and the inability of a company owner to accept the bitter sting of failure. But well-founded or not, the complaints have kept coming. Given the passage of time and the change in lending practices many of the complaints we now hear no longer have mis-sold financial products at their core. However almost all of them do seem to turn on the same axis, the relationship between the IP and the party, often a secured creditor, who has appointed them.

Controlling the process

The process by which IPs get appointed is opaque by design. There is no public tender, or formal process. The market is not made aware an opportunity exists. Appointments are carried out in relative secrecy and in private. To a large extent this is unavoidable. No one wants to advertise the imminent insolvency of a company. There would be a very rapid and highly detrimental effect on the company's trading and prospects. However the nature of these appointments will often come as a shock to the company owners or directors at the heart of the action. To many the process feels like a bilateral negotiation involving only the secured creditor and their chosen IP. Any party outside this bilateral negotiation has no insight into how the appointment process unfolds, what is asked for by the appointing party, or offered by the IP. Working papers produced by IPs during this period are not available to stakeholders. Often this failure to engage more broadly with the body of creditors extends to the holding of a creditors' meeting, which are often only held if interested creditors agree to pay for it.

Complaints were made to the APPG about the lack of any publicly available detail on the negotiation that takes place prior to an insolvency. The complainants almost universally had concerns about what was agreed between the IP and the

appointing party prior to the insolvency. What conflicts had arisen and how were they dealt with? As part of our work in undertaking this report we also tried to establish what information exists about this process and came to the same, or similar, conclusion finding little transparency or disclosure.

The only well documented case studies we could find were in the rare instances where IPs have set out their 'offer' in marketing material or when the process breaks down, litigation ensues and information is made public through disclosure required by the court.

An inappropriate offer

One such case where information about the appointment process was made public stemmed from 2011 and the decision by Swiss insurance giant Zurich to close down its specialist property lender Dunbar Assets Plc. The bank was a small, but highly regarded relationship bank. It lent to a small number of commercial borrowers, almost all of whom were prepared to risk everything, via personal guarantees, largely because they had trust in themselves, the bank and the system. In banking terms Dunbar was tiny, with something like 200 borrowers owing just over £1bn when the decision was taken to pull the plug.

In the months following the decision to close Dunbar loans were called in, demands were made under the associated personal guarantees¹⁰ and scores of people¹¹, possibly as much as 50% of its customer base, made bankrupt. Various case studies relating to the demise of Dunbar were presented to the APPG as part of this work. Unfortunately, many of these centred on personal rather than corporate insolvencies, something that largely sits outside the scope of this report. However, one case study did prove relevant, a civil action brought against Dunbar and the BDO IPs appointed over a company

10. <https://www.thetimes.co.uk/article/dunbar-faces-challenge-over-bankruptcy-policy-6xbgdbbf06f>

11. <https://www.thisismoney.co.uk/money/news/article-5642105/Bankrupted-customers-007-bank-Dunbar-call-new-tribunal.html>

called Angel House Developments. In May 2016 the High Court in London heard the claims of misfeasance and negligence against the BDO IPs, and an associated conspiracy claim against Dunbar. While the claim ultimately failed, it offered an extremely detailed insight into the appointment process and the tone and content of the interactions that take place between IP and secured creditor prior to appointment.

It was presented to the court that during the pre-appointment negotiation process the insolvency practitioner made what was described in court as ‘improper’ offers to the bank. No doubt aware that independently of the insolvency process the bank wanted to pursue the shareholder and director of the company, Ms Davey, under her personal guarantee, the IP sent his counterpart at Dunbar an email¹² in which he offered to lend them his ‘powers’:

Would you benefit from having an Administrator, with his associated powers, as part of your strategy in pursuing the director / shareholder?

Cross-examined on this point during the trial it became clear that what the BDO administrator was offering was to use his court appointed powers to obtain information from Ms Davey that might aid Dunbar in pursuing her under the personal guarantee. The presiding judge may not have liked the claim against BDO, ultimately ruling against it, but neither did he like this behaviour. Evidence was presented to the court showing that not only did the BDO administrator offer an ‘improper’ service to Dunbar, but he also delivered on his promise, providing personal information about Ms Davey to the bank as well as helping it serve proceedings against her. Ruling on the case the judge made this comment:

...assisting Dunbar to serve the Guarantee proceedings upon Ms. Davey and providing

Dunbar with personal information concerning Ms. Davey were actions which were not designed to further the purposes of the administration. To that extent, these actions were not part of the proper functions of the Administrators, and they should not have happened.

In his ruling on this aspect of the case the Judge focused on the delivery of the ‘improper’ service. His interest was not just that an improper service was offered, but that it was delivered. The judge found that a senior IP, from a respected firm such as BDO, had been prepared to offer his court appointed powers, not for the benefit of the administration, but to assist the party who had the power to appoint him.

Inappropriate demand

The example above centres on the question of whether there exists a willingness by certain IPs to ‘hire out’ their powers to a creditor, in exchange for their appointment. A similar, more recent, legal case examines the converse question whether or not there is an equal and matching desire by creditors to recruit and control those powers.

This question was examined during the 2020 civil trial of insolvency practitioners involved in the administration of a company and property development known as One Blackfriars. The case was broadly similar to the Dunbar case above in that the administrators, coincidentally also from BDO, were accused of negligence in the performance of their duties, a willingness to prefer the interests of the secured creditor over other parties and therefore, a conflict of interest.

During the trial¹³ the insolvency practitioner at the heart of the dispute was asked by the judge, Mr Kimbell QC, whether the appointing bank, Royal Bank of Scotland, ‘wanted to guide the administration’. Summing up the witness’s reply,

12. Julia Anne Davey v James Money & Jim Stewart-Koster, 16/05/16

13. Hyde v Bannon, day six

the Judge stated:

So your answer is not just that they [RBS] wanted to do it [guide the administration] pre-appointment, but they wanted to do this after appointment as well, but it was up to you to exercise your duties to prevent that.

The witness was unequivocal in her answer: *That's correct, my Lord*

As with the Dunbar / BDO case above, the One Blackfriars case was rejected at the High Court. Despite this the case study still appears relevant in answering the second part of the question, whether it is the case that secured creditors - even mainstream ones such as Royal Bank of Scotland - will try and control the administration process.

Maximising Control

The nature of the appointment process for insolvencies means it is rare for firms to publicly market their services. However one example of such marketing, from one of the smaller players in the market, Moorfields Corporate Recovery, did offer an insight into the power dynamic that exists between banks and insolvency professionals. In June 2013 Moorfields published a leaflet aimed at drumming up business by exploiting provisions for 'Light Touch Administrations' contained in the Insolvency Act 1986. The two-page document titled *Light Touch Administrations, Low Cost Strategy, Maximum Control*¹⁴ sets out to explain how the administration process can be adapted so that the creditor can retain 'maximum control' over the administration. This point is reinforced in a sub-heading which reads *So how does a lender secure a low-cost strategy whilst maximising control?* The answer, according to Moorfields, is for creditors to use a particular subset of insolvency law known as Light Touch Administration. The document explains:

...where full control is required, the appointment of an Administrator will be a more robust tool. Not only can an Administrator use their statutory powers to assume control of a company and its assets, records, employees and directors (forcing cooperation if need be), they enjoy a wider range of additional powers

The discussion of how to gain "control" in an insolvency is tempered by a line towards the end of the document which states the importance of *"ensuring the interests of creditors as a whole are treated appropriately"*. Other than that, the document would appear to pull no punches in what it is offering banks - control.

This question of control, or who is in charge of an insolvency - particularly an administration - is one that crops up over and over again in discussions the APPG has had with company owners and directors whose businesses have gone into administration or another insolvency process. A central theme of the complaints received by the APPG was that IPs were allowing their powers to be 'weaponised' against certain parties in an insolvency and for the benefit of others.

Of course, it is not always the secured creditor who might benefit from this kind of misconduct. Another example of this kind of behaviour presented to the APPG during our investigation involved a property dispute where the IPs had been appointed by the director of the company. In a judgement¹⁵ handed down on 11 December 2019 the presiding judge found that Insolvency Practitioners had been appointed by the company director *"...so as to influence the insolvency procedure and the course of the administration."* In his preliminary findings the Judge then goes on to state the director's *"...motive was to obtain a collateral advantage in connection with this process [the administration] to which he would not otherwise have been entitled. In the sense originally envisaged, this advantage was achieved."*

14. <https://www.moorfieldscr.com/media/1135/june-2013-light-touch-administration.pdf>

15. In the matter of C A & T Developments, 2019 EWHC 3455

The case studies above are a handful of the cases presented to the APPG that demonstrate how parties appointing IPs - notably secured creditors - were prepared to make improper requests of IPs, and / or, of IPs allowing their powers to be abused. These are individual examples of a potential problem. However, a more generic issue was also presented to us of what individuals inside and outside the industry consider to be a systemic problem - the insolvency panel agreement.

Panel agreements

All large corporates will operate panel agreements with their professional service providers. The practice is normal, and for the most part uncontroversial. It allows the buyer of a service to control costs and set standards for products or services they are purchasing. The buying power of large corporates can sometimes give rise to complaints that panel agreements can be repressive or overly controlling but it's generally, and quite rightly, left to the market to regulate such matters.

The same framework is in place for insolvency practitioners and banks. Banks will negotiate panel agreements with the large accountancy firms. These are normally, but not always, restricted to the larger players in the market such as the big four accountants plus perhaps BDO and Grant Thornton. In responses to our questionnaires the bulk of these firms confirmed they were on bank panels for insolvency work, some on as many as six. One firm gave some detail on how panels operated, stating that they contain provisions stipulating costs such as the hourly rates that can be charged. However the bulk of the firms refused to be drawn on the nature and content of their agreements, or even which bank panels they were appointed to, citing commercial confidentiality.

To some extent then we are operating in the dark when considering panel agreements. However their basic purpose would appear to be fairly self-evident. In return for signing up to agreed terms on costs, service delivery and various oth-

er matters, the accountancy firm can expect a steady stream of work from the bank. They are therefore an important driver of work. After all, directly or indirectly, the banking sector is possibly the largest single route¹⁶ by which IPs are appointed to insolvencies, particularly higher value appointments such as administrations.

But are panel agreements appropriate in the world of insolvency? Should banks be stipulating how IPs work, what they get paid and the standards they should work to when insolvencies are not undertaken solely for the benefit of a secured creditor? Concerns about the relationship, and potential conflicts created by panel agreements were put to us by a number of parties, including the European Association of Certified Turnaround Professionals (EACTP) which described panel agreements starkly as an “*abuse of the close relationship between secured creditors and professional advisors*”. In their submission to the APPG the EACTP stated:

The existence of bank panels of advisors creates conflict, it being too easy for professionals recommended by a bank to forget that their obligations are to their distressed clients and not to the secured lender who will be their next referral source. The separation of IPs from firms that practice corporate rescue advisory work is recommended.

The point made to the APPG was that insolvency work is very different from any other kind of professional service provided for under a panel agreement. If a lawyer, an insurance company or property advisor is contracted to work for a large corporate under the terms of its panel agreement, their legal and professional responsibilities will be to that corporate. The duties imposed on IPs are very different. They have responsibilities to the state, for example to report misconduct by directors; they have responsibili-

16. The APPG asked the major accountancy firms what percentage of appointments came directly or indirectly from secured creditors. While most firms declined to answer the question, one of the firms stated the figure was around 22%.

ties to the company and then they have responsibilities to creditors and to a lesser extent to shareholders. The bank is just one among many parties who have an interest, something to gain or lose, out of an administration. The problem is the interests of the parties are by no means the same. Far from it. The interests of the various parties will often be in direct conflict, with each party trying to maximise their returns from a pot of funds that, by definition, is limited and quite possibly deficient.

Neither is it possible to argue, as it would be in standard commercial relationships, that 'he who pays the piper, calls the tune'. A secured creditor has the power to appoint an IP, but they don't pay for the work directly. Other than in the rare occasions when a creditor might fund an administration, IPs will be paid out of the funds available to the company they have been appointed over. Even when an insolvency is funded by a creditor the responsibilities of the IP, their duties and obligations, remain broadly the same.

So, we are left with a situation where Insolvency Practitioners working, often on high value insolvencies with multiple interested parties, will be operating under a panel agreement, the terms of which are confidential and known only to the IPs and one of the creditors. The APPG asked accountancy firms to share details of their panel agreements, including the names of the banks who had appointed them and key aspects of the agreements. As stated above, all declined, citing commercial confidentiality.

This is the telling point about panel agreements. It is impossible to know whether they are in general terms benign, or even beneficial to the wider creditor community, or whether they unfairly, possibly improperly, benefit the author of the agreements, the banks. What we do know is that they raise very loud alarm bells with people who contacted us as part of this work.

While we cannot know for sure what constraints or demands Panel Agreements place on IPs, we were given a flavour of their contents through

information presented to us as part of this work. We were repeatedly told by industry insiders and others that formally or informally banks have extracted undertakings from accountancy firms in return for being placed on their panels. Perhaps the most telling of these alleged undertakings was that no IP on a panel would litigate against the bank that had appointed them.

While no-one could provide us with firm evidence of this 'no-litigation' practice, evidence to suggest this understanding is more than speculative can be found in various sources. The APPG has been shown an email from a former partner at a major accounting firm in which he explains his firm's policy on taking on insolvency appointments where there is a threat of litigation against the secured creditor:

...if it came to a case where litigation is appropriate, we would have to decline to act given our panel status with all the major Banks and thus our perceived or actual conflict of interest.

This reticence to bring a claim against the secured creditors with whom the accountancy firm has a panel agreement is mirrored in two further cases. In both cases the IPs stepped down from their appointment rather than be involved in a claim against the bank. The decisions to walk away from these appointments were recorded in documents on Companies House. The first was in the insolvency of a company called Bold Hotel (Southport) Limited, undertaken by IPs from BDO. The liquidators filed an update to creditors on 19 May 2015 explaining their decision to step down because the directors of the company were pressing for them to bring a claim against the secured creditor, Royal Bank of Scotland, on behalf of the company. The update stated:

The directors believe that there is a substantial claim for consequential losses [against RBS]... This may involve litigation in the future and, in that event, the current liqui-

dators are likely to be conflicted, therefore it has been agreed that we will vacate office to permit an alternative liquidator to consider these matters.

Similarly in the insolvency of The Delivery Specialists Limited another pair of BDO IPs stepped down from their appointments rather than get involved in litigation against the secured creditor, again RBS. Their update to creditors on 9 August 2016 stated:

The directors believe that there is a substantial claim for consequential losses... This may involve litigation and as a consequence we as joint liquidators of the company are now in a position whereby we have a perceived conflict of interest. It has been agreed with the directors that the joint liquidators will vacate office to permit an alternative liquidator to be appointed to consider these matters.

The problem with both these examples is it is very hard to see how the spectre of litigation against the secured creditor could give rise to a conflict. Insolvency professionals must be in a position to take action against any party to an insolvency, if a claim exists that might return funds to the company. This must include the secured creditor.

This question of whether there are 'no litigation' agreements between the restructuring divisions of accountancy firms and the major banks has been explored in court in another case that was brought to the attention of the APPG. In the High Court action of *Ventra v Lloyds Banking Group*, the bank was ordered by the court to search for and disclose its panel agreement, again, with BDO. As was reported¹⁷ in *The Times* on 26 August 2019:

17. <https://www.thetimes.co.uk/article/lloyds-banking-group-under-scrutiny-for-insolvency-ties-67q0nxb2>

A High Court judge said Lloyds must reveal details of its insolvency agreement with BDO, the accountancy firm, in light of claims that the "impartiality and independence" of insolvency practitioners may have been undermined by their relationship with the bank.

The *Times* story went on to explain that the company bringing the claim against Lloyds was arguing that:

...BDO's position on the Lloyds "panel", essentially a preferred status enjoyed by certain firms who win regular work from the bank, meant that it was unlikely to sue the lender should legal issues come to light.

It is understood the *Ventra* claim against Lloyds settled shortly after the disclosure order was made. As such no details of the panel agreement, and what terms¹⁸ it held BDO to were ever put into the public domain.

The fact that the examples above all involve BDO should be seen as no more than coincidence. The APPG has been provided with examples of similar conduct that involve other major accountancy firms, however as they weren't formally documented in the same way as the examples above they have proved more difficult to present. Detail from one such example involving another member of the top six firms - not BDO - is worth recording. The APPG was told that the panel agreements with this particular firm do not carry a condition stipulating that the IPs cannot bring litigation against the bank. As was explained to us, it was felt that introducing such a condition would be too much of a blunt instrument. Instead the agreement accepts that IPs are free to bring litigation but stipulates that for

18. It should be noted that in the *Times* story about the BDO / Lloyds panel agreement a spokesperson for the bank denied Lloyds ever "imposed restrictions on pursuing claims against the group or any other parties when appointing insolvency professionals".

the duration of any such claim the IP - or more importantly their firm - would not receive any appointments from the bank. It has not been possible to verify this claim. However, if true, it is self-evident that such condition would amount to a bar against litigation in any practical, real world, sense.

Conflicts, but no claims

Whatever the terms of panel agreements may, or may not be, remains an unknown. With no transparency around the documents it is not possible to know exactly what conflicts the agreements introduce and to what extent they protect creditors from litigation. Only slightly less opaque is the day-to-day practice of IPs when it comes to litigation against banks. The APPG conducted its own research as part of this project, analysing claims filed at court, asking accountancy firms, lawyers and other experts about claims brought by IPs against secured creditors involved in their appointment. We did not identify a single example. We asked all the major accountancy firms whether their IPs had brought a claim against a secured creditor and if so to provide examples. Only one firm said they had brought any claims, but said these were procedural matters relating to the disclosure of documents that banks would not otherwise be able to share for reasons of confidentiality.

Of course, claims have been brought by IPs against banks, the case above of Ventra against Lloyds is one such example. But in each case identified by the APPG the original IPs appointed by, or with the approval of the secured creditor had to be replaced or removed before a claim could be brought. The APPG is still interested in hearing from any parties, IP or otherwise, who have details of any claim brought by an IP against a secured creditor directly involved in their appointment.

Act or omission

Of course, a failure to bring a claim may be no more than that - a failure to act. If, as might be suggested in the cases of Bold Hotel and Deliv-

ery Specialists above, the IPs did no more than decline to act, allowing someone else to step into their roles, it would suggest a problem may exist, however the damage would be limited as the IPs were prepared to walk away from the insolvency.

Two other cases presented to the APPG raised a different scenario. The cases are similar in that both were brought against Administrators from Deloitte, alleging the IPs failed to act independently, preferring the interests of the secured creditor who had appointed them, Barclays in both cases, against those of the company and the wider creditors. In each case it was alleged that the IPs failed to bring legitimate, high value claims against Barclays relating to the mis-selling of swaps and manipulation of interest rates. The strength of the claims against Deloitte appears to be strengthened in both cases by the simple fact that after the Deloitte IPs had stepped down from their positions, multi-million pound claims were brought against the bank. Both claims settled, one on confidential terms, the other for in excess of £10m.

The litigation against the Deloitte IPs for failing to bring claims against Barclays, goes further than simply alleging a failure to act against the bank. The claims make a case that the Deloitte IPs acted to protect the interests of the bank, shielding it from legitimate high value claims. Unfortunately for the purposes of this report, neither claim has been resolved in court so it is not possible to rely on any ruling as to the merits of the allegations and whether the court agrees that misconduct did take place. One of the claims, brought by Paul Holgate in relation to the administration of his family's caravan park, Arthur Holgate & Son, was settled on confidential terms in 2019. The second claim, brought by property company Rhino Enterprise Holdings remains active with no date set for trial.

Hired gun

While the two Deloitte cases above remain unresolved, and therefore must be treated as such,

other cases have resulted in judicial or regulatory rulings. In recent months cases have been brought against two of the most senior Insolvency Practitioners in the UK, one formerly of Deloitte, the other formerly of KPMG. In both cases the core allegation is one of conflict of interest between the IP and parties who appointed them. In both cases the evidence suggests the misconduct goes far beyond a failure to conduct proper conflict checks when taking on new work. In February 2020, the ICAEW levied¹⁹ a £1m fine against Deloitte and £50,000 against Neville Kahn²⁰, formerly head of Deloitte's restructuring division. The sanctions were brought in relation to work done on the 2012 restructuring and subsequent administration of electrical retailer Comet. The Consent Order²¹ published by the ICAEW details a litany of failings by Deloitte and Kahn. Almost all of these failings stem from the relationship Kahn had established with the private equity backers of Comet prior to the administration and then how Kahn allowed that relationship to affect his judgement. What was not clearly set out in the disciplinary documents was the extent and the severity of the misconduct that took place under Kahn's watch by the private equity backers of Comet. As reported by the *Financial Times*,²² the private equity backers of Comet managed to net a profit of £100m during the 12 months they owned the chain, without putting a pound of their own money at risk. At the same time, the taxman was left £50m out of pocket and 7,000 people lost their jobs.

The ruling by the ICAEW and related reporting makes clear the extent of the failings by Kahn and his team at Deloitte. Checks on the legality of the complicated financial structure created by Comet's private equity backers, OpCapita,

Greybull and Elliot, should have been the subject of an in-depth investigation by Deloitte administrators. This wasn't done. Connected party transactions that should have been declared were covered up. The acquisition of Comet by the private equity trio should have been investigated, but wasn't. The role of various parties and whether they were acting as shadow directors should have been looked into. Again, this didn't happen.

The list of failings in the ICAEW disciplinary notice is extensive. Of course, the incentives to engage to bend the rules in this way is pretty clear. Commercial organisations such as banks and private equity companies are not bound by the same rules as IPs. As our examples above demonstrate, inevitable pressure will be brought to bear on IPs to favour the interests of one party over another. At the same time the fees at play are not insignificant. In the first 12 months of the Comet administration Deloitte earned fees of over £10m of which they had paid themselves nearly £5m.

Another case study displaying similar characteristics to Comet and Deloitte has very recently been pursued by the ICAEW and the Financial Reporting Council (FRC) against KPMG. The case revolves around the pre-pack administration of furniture manufacturer Silentnight. The FRC alleges that KPMG and its insolvency partner David Costley-Wood were hopelessly conflicted when they took on the appointment and should never have accepted the work. These conflicts contributed to the failure of the administrators to act in the interests of all creditors and allowed Silentnight to offload £100m of pension liabilities on to the UK taxpayer, while HIG, the US private equity group that appointed KPMG, walked away with a highly valuable company free of its largest liability. The alleged misconduct by the KPMG IPs stretched to assisting the company in misleading the Pension Protection Fund and the Pension Regulator about the cause of Silentnight's problems and the role of HIG as a so-called white knight.

19. <https://www.icaew.com/insights/viewpoints-on-the-news/2020/feb-2020/icaew-issues-1m-comet-fine>

20. A smaller fine of £25,000 was levied against Deloitte partner Christopher Farrington for his part in the insolvency of Comet

21. <https://www.icaew.com/-/media/corporate/files/about-icaew/what-we-do/protecting-the-public/disciplinary-orders/30-january-2020.ashx?la=en>

22. <https://www.ft.com/content/329317ae-48cc-11ea-aeb3-955839e06441>

The regulators submitted their preliminary findings to the tribunal in June this year and made public their sanctions on 5 August, including a £13m fine against KPMG and £500,000 against Costley-Wood. Both parties were severely reprimanded, particularly with respect to the conflicts of interest they allowed to go unchecked. The Tribunal found that Costley-Wood “assisted in a process that was designed to drive Silentnight into an insolvency process... [providing] advice and assistance to HIG so that it could acquire Silentnight as an otherwise profitable business without the burden of the Pension Scheme Liabilities”. The Tribunal went as far as to find that Costley-Wood acted dishonestly “in order to assist HIG in its efforts to enable Silentnight to shed its liability under the Pension Scheme as cheaply as possible”.

What is striking in the rulings against KPMG and Costley-Wood is not just the detail of the specific findings against both parties, but how they reflect many of the trends that have been reported back to the APPG by other parties. Taking a step back, these accounts appear to provide the following template: An Insolvency Practitioner seeking work offers advice to a creditor concerned about their security. The advice involves the IP guiding the creditor on how best to protect their position, how to ensure they get paid back in full, or perhaps - as appears to have been the case with Comet and Silentnight - how to make a profit from the situation. That advice being well received the IP is appointed to the administration and the secured creditor sees their plan come to fruition. To many of the outsiders who spoke to the APPG this situation seems extraordinary, not dissimilar to asking a football manager to referee the game, or a lawyer representing one party in litigation to preside over the case as the judge.

Independent Business Reviews

The dual role of IPs, how they can advise one party prior to an insolvency and then, upon the gift of appointment by that party, shed previous affiliations and manage the insolvency on be-

half of all parties, is one that was brought into sharp focus following the financial crisis. As has been repeatedly presented to the APPG, in the wave of insolvencies that flowed from the 2008 crash, it emerged that it was standard practice for banks concerned for their security to require their borrowers to undertake an Independent Business Review (‘IBR’). These reviews were paid for by the business, but undertaken by an IP from the bank’s panel. More importantly, the IPs’ contractual relationship was with the bank rather than the business that was paying for their services. Their duty of care, in other words, lay with the bank.

In the case studies presented to us it was clear that in some instances the businesses would see the report that emerged from the review; in others, they saw a summary of the report; in many cases they saw nothing. As well as advising on the viability of the company, the reports would also provide advice on how the bank should proceed and whether insolvency was required. In many cases the author of the report not only advised that the company should go into insolvency, but was then rewarded with the appointment.

In every case we examined this situation gave rise, at the very least, to a perceived conflict of interest. To some extent this has been recognised by the industry. The APPG was told that some time prior to the financial crisis Royal Bank of Scotland introduced a policy preventing parties who had conducted IBRs from being appointed as IPs (other than in certain defined circumstances). The other major banks were not as cautious and allowed the practice to flourish. It is quite likely that hundreds, possibly thousands, of insolvencies were triggered off the back of the IBR model outlined above. This in turn led to a wave of complaints and, very quietly, the practice was dropped by many of the major banks and some IPs, although it has never been barred.

The major accountancy firms were asked in the APPG questionnaire whether they would consider taking an insolvency appointment when

they had previously conducted an IBR or similar pre-insolvency advisory work. None of the accountancy firms considered the issue to represent a clear conflict. All of the firms which answered the question directly said they do conduct IBRs on behalf of banks and would consider a subsequent insolvency appointment, subject to the usual conflict checks. The universally accepted position was summed up by one of the firms in the following way:

We do undertake Independent Business Reviews (“IBRs”) of companies at the request of their secured creditor... As the work has been delivered for a creditor there is no prohibition under the Insolvency Act and Rules or the current Code of Ethics on accepting a subsequent insolvency appointment. However, the officeholder should, and in our case would, undertake a consideration of the threats of taking such an appointment and consider whether any appropriate safeguards should be applied.

While the use of IBRs in the industry is seen as normal practice and uncontroversial, it was an area that consistently surprised outsiders. The fact that at least one bank has clearly identified the potential conflict of interest and acted to put a stop to it, while the rest of the industry and the regulators have carried on regardless was something that many people we spoke to found hard to understand. The secrecy and lack of disclosure around IBRs only added to the frustration felt by people who came forward to us. The questions they were left asking themselves was whether, and to what extent, the conflict inherent in these IBRs corrupted the insolvency process. Was it the case that IPs recommended insolvency when there were other viable options? Did the creditor push the IP into producing a recommendation that favoured insolvency over other outcomes? Or, conversely was the conflict professionally and ethically negotiated, so that the best outcome for all parties was achieved?

In many ways the issue around IBRs goes to the heart of the question the APPG has been looking to answer. The fact that conflicts exist in the industry is indisputable. The question is, has the industry risen to this challenge and defended itself against these conflicts; or has the power dynamic between secured creditors and IPs corrupted the relationship to such an extent that radical change is now required?

Business review as a business opportunity

Another case study relating to the conduct of finance professionals at one of the Big Four firms sheds further light on how conflicts are managed at the very top of the industry. This case study has been anonymised at the request of the party who supplied it to us, however the APPG has reviewed the relevant documents and is content that the narrative below is accurate.

Shortly after the financial crisis a commercial property company with assets of circa £1bn was in detailed negotiations with its lender about restructuring its loans. The negotiations had reached a critical point. On one side the bank was threatening administration and refusing to extend credit beyond the term of the existing loans. On the other side the company was asking for forbearance and time to trade its way out of its financial position.

As a last throw of the dice the company was persuaded by its lender to spend a significant sum of money, roughly £500,000, to get restructuring advice from one of the big four accountants. Unlike the IBRs detailed above, in this instance the accountancy firm was working directly for the property company. Its relationship and duties were solely to the company, not to the bank. The advice was presented by way of series of slides. They were cogent and compelling, mapping out a path by which the company could sell certain assets, pay down debt and trade its way out of its difficulties without being placed into administration.

The advice failed and the company ended up in administration. But the directors of the property company had no complaints with the work of the accountants. They considered it had been undertaken professionally, diligently and in good faith and were content with that part of the process.

A few months after the companies had been put into administration the directors of the property company asked the accountancy firm to resend the slide presentation. What they were sent surprised them. Presumably by mistake they were sent a completely different document. It was a shorter presentation, prepared at the same time as the original roadmap and with the same codename, but one that charted a route to a completely different destination. The document marked 'private and confidential' had been prepared solely for the bank. It was essentially a pitch document, presenting the bank with five options through which the accountancy firm could assist in recouping the bank's loans. Two of the options involved the property company going into administration, all of the options involved significant downsides for the property company. 'Loss of income', 'equity reduced to zero', 'loss of control of the portfolio', 'failure of the overall group' are just some of the 'cons' for the property company listed in tables summarising each option. The upsides for the bank include 'taking control', 'eliminating corporate liabilities through administration process' and 'extracting higher prices'.

In many ways the two documents are very similar. The intended audience is the same in both cases, the bank. The subject matter is the same, the future of the property company. The author is the same, the accountancy firm. However the intention of the two documents is utterly opposed. One works in the interests of the property company, to save it from administration and protect shareholder value. The second document is designed solely and exclusively to promote the interests of the accountancy firm and the bank. As was explained to the APPG by the directors of the property company, they felt that

despite being the client they were being treated as little more than a commodity to be traded for the benefit of the creditor and their chosen accountancy firm.

Two further examples are interesting, one for its pandemic-era aspects.

A prestigious and award-winning London-based business had been in the process of raising growth capital to expand and at the end of this process, an investment fund with whom terms had been agreed withdrew at the eleventh hour without explanation. It was not long before the company faced significant cashflow pressure including expensive debt from a tertiary lender who had secured a debenture over the business. The director identified and approached a new potential investor as a white knight but the secured creditor did a deal behind the company's back with this third party to take over the business jointly. The acquisition was presided over by a well-known mid-market accountancy firm with a restructuring practice which had also acted for the secured lender funding the business in the first place. On the orders of the secured lender, it had subsequently been appointed to advise the business, agreeing to monitor, support and oversee the fundraising efforts. The same firm ultimately assisted the directors in placing the company into an insolvency process. Prior to this, the secured lender had expressed a desire to take a majority ownership stake as a condition of advancing any further funding and management suspected that the lender was pursuing a "loan-to-own" strategy. Upon appointment as administrators, the firm stated that it was not aware of any conflict of interest. A rescue of the Company might have been achievable with a restructuring of debt and renegotiation of rents (which the director knew landlords would be receptive to and which in fact happened following its acquisition out of administration). However, instead of attempting a restructuring to rescue the Company, the firm presided over a pre-ordained and exclusive sales process in which the Company was quickly sold to a special purpose

vehicle 50% owned by the secured creditor and 50% owned by the white knight investor identified by the company prior to administration.

In another case, the bank appointed a large (not top 6) accountancy practice to conduct an IBR in the context of cashflow difficulties which the company was experiencing as a consequence of the COVID pandemic. The instructions did not require the firm to address whether or not to recommend the advancement of a further CBIL to the company, but the IBR nonetheless recommended that the bank should not advance another CBIL, but rather that an insolvency process should be considered if the shareholder was not prepared to advance further funds. That recommendation was made in a version of the report which was not shared with the company, despite the IBR having been performed on the basis of a dual instruction from the company and the bank. There was no record explaining why CBILs had been issued previously but then not made available. As a consequence of the IBR the bank refused to support a further CBIL application, which had a knock-on effect for the company in closing down other avenues of finance, forcing the director to resort to high interest, personally secured borrowings. The bank, perhaps unwittingly, was implicated in the possible insolvency by not supporting the company's access to CBIL lending when that is what would have enabled the survival of the business at low relative risk to the bank given the government-backed element.

Secondments

During our research, concerns were raised with the APPG about the close relationship between banks and the IPs they used. This can manifest itself in different ways however one area of particular concern is the use of secondments, whereby insolvency professionals from the major accountancy firms will spend significant periods of time working for banks - often for free. The secondments are presented as a tool of professional development, a way in which the two sides can learn more about how each other works. However research by the APPG suggests that the

majority of secondments take place in one direction only, with insolvency professionals from the accountancy firms placed to work for the banks. Rarely if ever do the bankers go to work at accountancy firms. Moreover, the secondments are almost always at the expense of the accountancy firm. Banks generally pay nothing for the labour they receive from the accountants. They get it for free. The argument made to the APPG was that this practice was not about professional development of the individual, but about the commercial development of the accountancy firm's insolvency work; the secondments should be seen as either a method of developing close personal relationships between bank employees and the IPs, or simply as a quid pro quo, the gift of free labour in return for the future appointments of highly lucrative insolvency work.

Regulation

The current regulatory regime was introduced by the Insolvency Act 1986, which required IPs to be regulated by their own members. Professional Associations were granted a statutory regulatory function allowing them to become Recognised Professional Bodies (RPBs) with a duty to licence, regulate and censor their members. All Insolvency Practitioners must be a member of an RPB and can only act by or under the rules of that body. There are currently four such organisations, the two largest being the Institute of Chartered Accountants in England and Wales and the Insolvency Practitioners Association.²³

RPBs are, in turn, subject to the oversight of the Insolvency Service (IS), which acts on behalf of the Secretary of State for Business, Energy and Industrial Strategy. The IS has powers of sanction, the power to give directions, to impose financial penalties and to issue reprimands to RPBs which fail to meet or ensure adherence by members to the regulatory objectives. The IS is therefore an oversight regulator, or the regulators' regulator.

23. Insolvency Practitioners Association / Institute of Chartered Accountants in England & Wales / Institute of Chartered Accountants in Scotland / Institute of Chartered Accountants in Ireland.

This system was strengthened in 2015 with the introduction of the Small Business Enterprise and Employment Act. For the industry, the main change was the introduction of *regulatory objectives* for RPBs including the fair treatment for persons affected by an IPs' acts and omissions and protecting the public interest.

The Code of Ethics that has resulted from this regulatory framework is, on paper, very hard to pick holes in. The five fundamental principles are:

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- Integrity - to be straightforward and honest in all professional and business relationships
 - Objectivity - not to compromise professional or business judgments because of bias, conflict of interest or undue influence of others
 - Professional competence and due care
 - Confidentiality
 - Professional Behaviour - to comply with relevant laws and regulations and avoid any conduct that the insolvency practitioner knows or should know might discredit the profession
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The underlying principle of the code is that insolvency practitioners should identify, evaluate and address threats to compliance with these fundamental principles. If a threat is identified, steps must be taken to mitigate its effect or the practitioner must decline the appointment.

Is disclosure adequate disinfection for conflicts?

A widely held concern raised to the APPG was the use of the disclosure regime to mitigate perceived or real conflicts of interest. Industry experts brought multiple case studies to our attention in which IPs had accepted work despite there being a real or perceived conflict of interest. The concern was not just that IPs were ac-

cepting roles where there was a potential conflict but that when this was challenged through the regulatory regime nothing was done. The fact that the conflict was disclosed was presented as an all encompassing cure, neutralising any potential problems.

One such case study arose in November 2018 when IPs from Grant Thornton were appointed as administrators to the payday loan company Wonga Group. The appointment was highly significant given the size of the company, the nature of the business and the number of creditors and debtors involved. Shortly after GT was appointed it emerged that the firm had been involved with Wonga on multiple levels prior to the administration. These were detailed in the Statement of Administrators' Proposals issued by the GT administrators on 24 October 2018. The disclosure detailed how GT had been involved with Wonga in the following capacities in the three years prior to the appointment:

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- Offering restructuring advice to Wonga UK and then Wonga Group Limited from April 2018
 - Providing internal audit services to Wonga Group Limited for an unspecified period from December 2014 onwards
 - Providing advice on how the company should classify and measure financial assets, liabilities and contracts under IFRS 924 from March 2018 onwards
-

Having disclosed the potential conflicts in headline form, the GT Administrators went on to state in their Proposals:

Having reviewed each of the fundamental principles set out in the Code of Ethics, we did not consider there was a threat to

24. IFRS 9 is defined as "how an entity should classify and measure financial assets, financial liabilities, and some contracts to buy or sell non-financial items."

our ability to comply with those principles any potential role as an insolvency practitioner if there should need to be such an appointment. The administrators carefully re-examined the position in August 2018 prior to accepting the appointment to the Companies and considered there were no circumstances preventing them from being Administrators to the companies or their associated companies in the UK.

As was reported by The Times²⁵ in May this year, the position adopted by GT led to at least one complaint being made to the relevant RPB, in this case the Insolvency Practitioners Association (IPA). The core of the complaint was that GT's previous involvement with Wonga clearly amounted to a material professional engagement and therefore gave rise to a conflict. GT and the IPA disagreed and the complaint was rejected, allowing the work to continue.

A similar situation arose earlier this year. Just months after the IPA dismissed the Wonga complaint, Grant Thornton insolvency practitioners took on another high-profile administration, this time of the financing group Greensill Capital. Within weeks it emerged²⁶ that again GT had multiple previous professional engagements that at the very least gave rise to a perception of a conflict. In this case the prior engagement was with Greensill Capital's largest creditor Sanjeev Gupta's steel empire. It emerged first in the press and then disclosed in company filings that GT had advised Mr Gupta's companies on deals worth in excess of £1bn, all backed by Greensill. These were the kinds of transactions that would be expected to be investigated during an administration. The question that arose was whether the GT administrators would be able to conduct these investigations impartially and independently.

25. <https://www.thetimes.co.uk/article/conflict-inquiry-in-to-grant-thornton-and-wonga-reopens-wzlnjp7rz>

26. <https://www.thetimes.co.uk/article/audit-giant-grant-thornton-accused-of-conflict-over-role-in-sanjeev-guptas-takeovers-fgn527ksj>

Once again disclosure was presented as the panacea to the perception of any conflict. In a statement the company said:

Prior to accepting our appointment as administrators to Greensill Capital (UK) Limited, we gave careful consideration to the code of ethics relating to such matters and satisfied ourselves that there is no threat to our independence as a result of any prior relationships.

Moreover, in line with the administrators' statutory obligations and standard reporting processes, any relevant prior relationships will be disclosed to creditors in due course.

The APPG is not aware of any formal complaint being made in relation to the Greensill appointment, however it has raised concerns in the industry. One senior Insolvency Practitioner who spoke to the APPG under condition of anonymity explained the problem.

These roles, internal auditor and advisor on such significant deals, clearly amount to a material prior relationship. How can creditors know that these things won't influence an administrator's decision making? The disclosure isn't even sufficient. On the Wonga case we don't know what fees GT were paid for the audit work. Clearly it would make a significant difference if the fee was a few thousand pounds or a few millions pounds. But we just don't know. It's frankly outrageous that this situation has been allowed to go ahead unchecked. It does no-one any favours.

It would appear that the Insolvency Service may agree with this position. According to the story in the Times, the regulators' regulator, did not accept the IPA's position on the Wonga complaint and reopened an investigation into GT's appointment.

This problem with the current regulatory system, described to the APPG unkindly as 'the chaps

regulating the chaps' can lead to the perception of other problems. Under the current rules RPBs only regulate their own members. They have no power to take action against non-members, making it easy for an IP facing regulatory scrutiny to avoid censorship by simply moving to a firm covered by a different RPB. The APPG has been presented with a number of case studies where this appears to have taken place. In one instance an IP moved from one of the big four accountants, where IPs were regulated by the ICAEW to a smaller practice, where it was the norm to be regulated by the IPA. The move came after it was widely reported that the individual's conduct in relation to a particular insolvency was under investigation. The move away from the ICAEW is thought to have stymied the original investigation. This matter only came to the APPG's attention because a second complaint was brought against the individual in relation to their work with their new firm.

HBOS Reading

While the scandal of HBOS Reading is generally and quite rightly seen as a failure of the banking industry, it was also presented to the APPG as an issue that has rested, unresolved, at the door of the insolvency profession ever since it first came to light. The background to the case is well known. Former HBOS banker Lynden Scourfield abused his position of power at the bank using the insolvency process and other methods to misappropriate tens, even hundreds of millions of pounds from a slew of small businesses and HBOS. The case resulted in the jailing of six people for a combined sentence just shy of 50 years. The mechanics of the crime were relatively simple. Businesses that had the misfortune to end up under the supervision of Scourfield were showered with loans on the condition that they used business consultants whose purported role was to help turn the businesses turn around. In reality, once in position these individuals set about plundering the businesses of money and assets. The fraud went on for seven years, involved anywhere between £300m and £1bn and destroyed scores of otherwise successful businesses. At

sentencing the judge described Scourfield as an "utterly corrupt bank manager" who, driven by "rapacious greed... got his tentacles into the businesses of ordinary and honest people and ripped them apart without a thought for those affected".

While the misconduct of Scourfield and his co-conspirators was thoroughly and forensically examined by the court, other parties to the scandal came in for less scrutiny. Information presented to the APPG would suggest that one such group was the IPs appointed by Scourfield and HBOS over the companies he had targeted. The exact number of companies that suffered at Scourfield's hands has never been identified, however evidence used by the investigating police force, Thames Valley, suggests that at least 70 companies were victims. Analysis of these companies by the APPG shows that roughly half went through some kind of insolvency process, with IPs appointed from major firms including KPMG and PwC.

Of course, each of these HBOS Reading insolvencies were different. In some cases the corporate theft was very brazen. Companies were made to pay for holidays, prostitutes and drugs for the HBOS gang - or simply handed over bundles of cash. In other cases the crimes were more traditionally white collar, money was siphoned off through payment of outsized fees, assets were sold to related parties and transactions were conducted at substantial undervalue.

What is striking however is that none of the cases involving IPs resulted in any regulatory intervention by one of the RPBs. This is despite extensive evidence existing in the public domain about the role played by IPs in each case and their apparent failure to identify the ongoing fraud.

The APPG was given the example of angling supplies group Keenets Limited, also known as Speyside Angling and Sharpes Limited. While this case did not feature in the criminal trial

there is no debate that it was one of the companies that suffered at the hands of Scourfield's gang. Analysis of corporate filings for these companies show they were repeatedly provided with debt funding by HBOS, then placed into administration, then sold on to further companies that were, again, funded by the bank and Scourfield. However, at no point do the administrators register any concern. Indeed, at one point they appear to give these transactions a clean bill of health finding that none of the parties involved in buying and selling these assets were related or conflicted.

These matters were drawn to the attention of the regulators. In 2018 a report by a forensic accountant (and trained Insolvency Practitioner) at HBOS was made public. The Lord Turnbull report²⁷ by Sally Masterton explored in extensive detail the misconduct at HBOS Reading. The report also contained a 12-page chapter entitled *Insolvency Practitioners and Investigating Accountants*. Masterton names firms including PwC, KPMG and two of the smaller operations as being among those that have "breached reporting obligations and been involved in serious misconduct". Her report states:

Insolvency Practitioners, investigating accountants and accountants providing other accountancy services appointed from January 2007 either knew, ought reasonably to have known or should have strongly suspected fraud and/or money laundering.

Despite compelling and factual evidence or suspicious evidence of a very serious nature not one of the Insolvency Practitioners appointed during 2007 and 2008 duly reported to SOCA [Serious Organised Crime Agency] their suspicions or evidence of director fraud or appointed liquidators to investing misfeasance by, or delinquency of, directors.

The report, and particularly its findings with respect to Insolvency Practitioners, was raised with the regulators as part of an official complaint²⁸ that was submitted to the Insolvency Service in 2019. In addition to the findings in the Lord Turnbull report the complaint, seen by the APPG, supplied first-hand information of how Scourfield operated and concluded that "IPs and law firms were the oil that kept it [the fraud] running".

The response from the ICAEW reads:

I have fully reviewed the Turnbull report and the list of concerns raised [in the Lord Turnbull report] about the actions of IPs, unfortunately there is no documentary evidence to support any of the comments/allegations made in the report. Additionally, the events in question took place between 2002 and 2010 and it names a small number of IPs, particularly at PwC, it is also very vague in respect of IPs at KPMG and other firms.

I confirm that despite a number of emails to members of the insolvency practitioners regulation section at the insolvency service I have not received any confirmation from them that the insolvency service has undertaken any investigation themselves into the matters referred to in the Turnbull report.

Following my assessment of your complaint I have concluded that there is currently insufficient evidence to demonstrate that any ICAEW member would be potentially liable to disciplinary action. Unfortunately due to the lack of evidence I am not in a position to take this matter forward to investigation.

The complainant, someone with first-hand knowledge of standards and ethics in the industry, was disappointed. They followed up on the letter pressing the ICAEW to launch a full-blown investigation into the matter. This resulted with

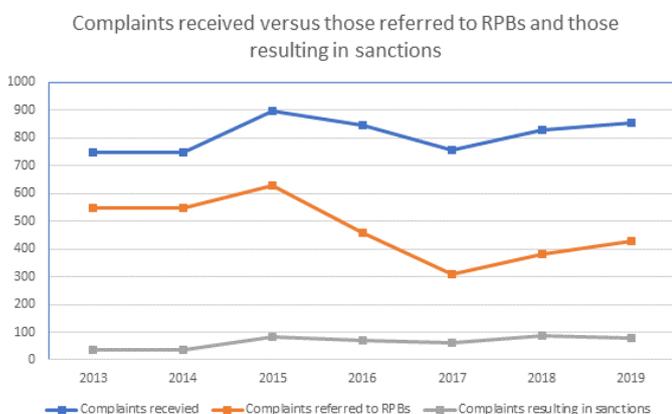
27. <https://www.appgbanking.org.uk/wp-content/uploads/2018/06/draft-Project-Lord-Turnbull-Report-part-1.pdf>

28. The APPG has been asked to keep the identity of the complainant confidential, however we have been shown correspondence between the individual and the regulatory bodies confirming all the details supplied above

an undertaking by the ICAEW that they would keep ‘the complaint open’. No disciplinary action has materialised. Nor, as far as the APPG can discern has there been any effort made by any of the RPBs to conduct any kind of lessons learned exercise to understand what went wrong with HBOS Reading and whether failures by IPs contributed to the situation.

Disciplinary Action

Of course the RPBs can and do intervene. Official figures show fines are regularly levied by the bodies. According to the Insolvency Service, around 800 complaints about IPs are received each year, of which roughly half meet the criteria to be passed on to the relevant RPBs. In 2019, the last year for which data is available, there were 856 complaints in total, 428 of which were passed on to the RPBs. In 2018 the respective figures were 830 and 381. These complaints are then assessed by the RPBs who decide whether they should be investigated and, then upon investigation, whether any sanction is appropriate.



Two things emerge immediately from the data. One is the system is slow. The goal of the RPBs is to ‘substantially complete the investigation of a complaint within six months’. As of 1 January 2019 the number of complaints that remained unresolved after 12 months was 200. Nearly half of these complaints were lodged in the previous year, the others stretched back over the last five years. Twenty of the open complaints are classified as ‘pre-2015’ making it unclear exactly how long they remained unresolved, other than for a very long time.

The suggestion that the RPBs lack urgency in dealing with complaints is backed up by a monitoring report²⁹ issued by the Insolvency Service in respect of the IPA in October 2020. The report is part of an ongoing review of the work of the IPA. The report states:

Of the 35 files reviewed, there was evidence in 22 cases of significant periods of inactivity, such as no contact being made with either the complainant or the insolvency practitioner. In some of these cases, there were periods of three to six months from receipt of the complaint prior to any substantial correspondence with either party. While all complaints were acknowledged, in seven cases the complainant was not initially provided with information about the process, the matters being considered for the next steps.

The other thing that emerges from the data is the simple point about the number of sanctions levied against members of the RPBs. Of the 800 complaints received each year, we know that roughly half fall at the first hurdle, ie with the Insolvency Service. The remainder get passed on to the RPBs. Whether all or just a proportion of these cases are accepted for investigation by the RPBs is not known. What is revealed by the data is the number of sanctions handed down each year. These suggest it is very rare for IPs to suffer the ultimate punishment of being excluded by their regulators. Over the last seven years just three IPs have had their licences removed. Fines are more common. Something like 30 IPs are sanctioned by way of a fine, reprimand or agreeing to some kind of undertaking each year. However the fines are not generally significant, coming in the range of £500 to £2,000, with the occasional larger sum as an outlier.

These fines come with some form of public censure, normally in the form a Regulatory Notice,

29. <https://www.gov.uk/government/publications/the-insolvency-practitioners-association-ipa-monitoring-report-2020/ipa-monitoring-report>

published on the RPBs website. The vast bulk of the sanctions relate to work carried out by IPs on individual insolvency cases such as personal bankruptcies or Individual Voluntary Arrangements. Very few relate to corporate work that is the subject of this report.

Courts

The approach of the courts to scrutinizing IPs' conduct has been hands-off. IPs are institutionally assumed to be scrupulous officers of the court. The legal bar for a challenge is set high, akin to perversity in decision-making. Coupled with the difficulty of raising the litigation finance and insurance needed to start a claim against an IP through the court system, this route is all but out of the question for most practical purposes. This deference by the courts – a hands-off approach – might be acceptable when the IP is fully independent, but not in the real world where there is every chance that the office holder has a relationship with the senior secured creditor or, if not, actively seeks their work. The impression understandably given to the weaker parties is that the system inherently pushes them aside.

Rescue or recovery?

Ultimately the question this report has set out to ask is whether the insolvency system in the UK is working efficiently and fairly for all those involved, not least the wider economy. The findings above suggest there is a problem. While it may not always be the case, the examples presented to the APPG suggest that the interests of certain parties are being preferred against those of others. The gift of appointment is being abused, leading to skewed priorities and therefore skewed outcomes.

There is a very real possibility that the manipulation of the system has a tangible outcome and that the insolvency industry in the UK is not doing what it was set up to do, which is to prioritise the rescue of businesses over the recovery of assets. Companies are broken up, assets are sold off and creditors repaid, but almost none of them are saved. This is despite rescue being

a statutory priority under the 1986 Insolvency Act. The legislation, together with subsequent law, such as the Enterprise Act makes it clear that IPs should rescue companies where possible. This is spelled out perhaps most clearly in the three objectives³⁰ for Administrations set out in the 1986 Act, the first of which is to save the company as a going concern.

Within the insolvency industry it is widely accepted that Objective One is almost never achieved. This is in large part because it is not easy. Rescuing a company takes time, involves a lot of uncertainty and ultimately may fail. We also heard evidence of a general over-leveraging, making rescue more difficult and asset realisation more attractive (with ready enforcement of contractual personal guarantees, for example). For these reasons it is rarely, if ever, in the interests of a secured creditor to pursue Objective One, particularly if there is the option of a guaranteed return from pursuing a recovery strategy.

As part of the research stage of this project we tried to establish how successful the insolvency industry was in achieving Objective One outcomes in administrations. What was disturbing, and possibly revealing, was no one collates this data. We asked the firms, the RPBs and the Insolvency Service if they could provide us with data breaking down the outcomes that are pursued and achieved in administrations. The universal answer was that this data is not collected.

This seems extraordinary. All the accountancy firms and the RPBs accepted that a key aim of Government legislation was to encourage corporate rescue. All of the firms said that rescue was hardwired into their DNA. However not one firm, RPB or even the Insolvency Service, monitors the outcomes of their work, to ascertain if

30. The full wording of the Act reads: the administrator of a company must perform his functions with the objective of (a) rescuing the company as a going concern, or (b) achieving a better result for the company's creditors as a whole than would be likely if the company were wound up (without first being in administration), or (c) realising property in order to make a distribution to one or more secured or preferential creditors.

they are actually achieving the desired outcome. This failure might be seen as a small point. We would say it isn't. It addresses the fundamental problem in the industry, which is not just one of a breakdown in process, but also of outcomes. There is a sense that the industry has lost sight of what matters, which is driving economic growth by saving companies and saving jobs. Protecting creditors' positions is important. But it was never envisaged as the singular goal of insolvency legislation. It is this situation that must now be addressed through changes to legislation and regulation, as we address below.

Recommendations

The 5 recommendations

Our 5 recommendations, designed to tackle the issues clearly laid out in the body of this report, are as follows:

1. A conflict of interests ban
2. A single regulator with an ombudsman
3. Placing the Code of Ethics on a statutory footing
4. A centralised database recording the outcomes of administrations
5. Further rule changes in support

Overview

Introducing the 2016 review of the corporate insolvency framework, the Secretary of State at the Department for Business, Innovation and Skills said:

"An increasing international focus on company rescue has helped to shift the perceptions of what constitutes best practice; the UK needs to reflect this if our businesses, investors and creditors are to remain confident that the best outcomes can be achieved when things go wrong."

We agree. For that reason "Objective 1", intro-

duced in 2002, has to be better supported than currently. The insolvency profession universally accepts that this primary intention of the Enterprise Act in promoting corporate rescue is neither achieved nor even attempted in almost all cases in practice. There are many reasons for this, but our recommendations aim to lay the ground for a rebalancing in favour of jobs, wealth protection and long-termism.

Our recommendations also aim to redress the connected problem of a widespread view of inherent bias in the system. Judges, arbitrators, experts, referees and umpires on the sports field all have to be, and be seen to be, independent of the parties. IPs taking over control of a business are not and are in fact regularly put in place by the secured lender, leaving other stakeholders effectively out in the cold. Even if the secured lender's interest is served by an attempt at rescue, the IP's interest is in the fees for this insolvency job and the fees for the next job from the same source. Constructive support from other stakeholders is discouraged. These factors militate against rescue.

In formulating the 5 recommendations, we have been guided by the conclusions of our investigations. The unavoidable conclusion from the present review is that unbalanced outcomes over the last 20 years are the structural result of the current regime, largely due to the profession seeking lucrative repeat work from institutional lenders when such lenders are only one stakeholder in each insolvent business.

The authors of *Insolvent Abuse*³¹ presciently stated some 20 years ago:

In a perfect world, it might be hoped that individually and collectively, accountants would act ethically. However, we do not live in that perfect world, but in a world dominated by market pressures in which accountants, just like other sellers of labour, are

31. *Insolvent Abuse: Regulating the Insolvency Industry* <http://visar.csustan.edu/aaba/INSOLVNTABUSE.pdf>

competing for business and are accountable for their contribution to the performance of the firms for which they work.

The expectation that IPs can stand firm at all times to (often unconscious) influence within this system is not a real-world expectation, less still where the statutory framework grants the IP extreme discretion to determine to whom they owe their duties. The irrefutable evidence we have seen is that firms have intentionally permitted their officeholders' powers to be hired out to their institutional clients. These are not isolated cases. Far from rescue culture, the system permits a lucrative vulture culture. As can be seen from the case studies, the powers of administration have been bent to suit creditor needs across a spectrum of behaviours, ranging from disguised pre-pack sales to parties connected to the secured creditor to "light touch" administrations in the form of receiverships by another name. Rescue is as far as it could be from the minds of these powerful interests in the insolvency industry; indeed, one IP at a top firm told us that the market had moved further away from rescue culture since the Enterprise Act.

A common thread running through the case studies brought to the attention of the review was the perception of bias on the part of IPs appointed by secured creditors where an institutional or panel relationship existed. We saw frequent evidence of the IP being sceptical or dismissive of directors and shareholders on the one hand, and overly close to the appointing creditor on the other.

We saw strong evidence that a pre-appointment engagement of the IP by the secured creditor was an aggravating factor in these cases. Such engagements were documented as a company appointment, or a dual appointment, but the reality was they were made with a view to the secured creditor making a formal appointment at the end of the engagement period. In certain

cases brought to our attention it was clear that the apparent appointment by the company was no more than window-dressing for a period of due diligence on behalf of the secured creditor intended to justify the administration and inform the subsequent administration strategy. This is particularly the case with IBRs, which the review found were still being performed by large accountancy firms, including in the context of government-backed CBIL lending. One IP commented to us that they were "leant on" by a bank during the course of an IBR and asked to prepare a confidential schedule to the report which would not be shared with management for their comment. The IP refused and was not instructed again by the bank in question.

Another IP commented to us that it is common for the course of an administration to be "meticulously planned" prior to appointment. Often these discussions take place informally, or alongside pre-appointment work, in the context of an appointing creditor dangling the carrot of a mandate. Even where all parties act with the best of intentions, important decisions can be made on the basis of early and imperfect information from which an IP would find it hard to row back at a later stage of the administration if new information or developments came to light from sources outside this early stage private conversation between one creditor and the prospective IP.

Pre-appointment strategizing between the IP and the secured creditor is a matter of significant concern to the APPG. Courts have been inconsistent on this point, on the one hand holding that there is nothing improper in and of itself in an IP agreeing an outline strategy with an appointing creditor prior to appointment (*Re One Blackfriars*), on the other that insolvency courts do not have jurisdiction to investigate such pre-appointment dealings because they occur prior to the commencement of insolvency (*Re Coniston Hotel*).

The practice of pre-appointment engagements

can lead to a self-fulfilling justification for proceeding to appoint a party who is in reality (or has been) the creditor's advisor as the independent officeholder, namely the argument that it would be more efficient and less expensive than passing the baton on to a new IP. This was a common observation made by IPs who undertake pre-appointment work for creditors. The countervailing argument is that a truly independent appointment would bring a fresh perspective and set of eyes to an insolvency. There is also no prohibition - now or proposed - on a creditor's advisor presenting their information and view to an independent administrator, who would in any event have a duty to make enquiries of parties with potentially relevant information. Although one suggestion was to accept pre-existing relationships where the directors and secured creditor agree upon the identity of an IP, this could only work with careful safeguards and risks leaving company representatives put under greater pressure to accede to the lender's requirements. Any such exception to the ban would need to withstand real world pressures.

Pre-appointment engagements are justifiably expressly identified as threats to objectivity as defined under the ethical code but it is clear from discussions with practitioners that such appointments are common practice and many IPs do not perceive an issue. Those that do perceive an issue tend to work for smaller, independent, firms. Their views tend to be strongly opposed to the idea of IPs performing any material pre-appointment engagement.

In our view the spread of opinion on the topic of pre-appointment work itself suggests that self-regulation is not appropriate as it is liable to lead to inconsistent outcomes with many IPs taking appointments in circumstances which would be criticised by others. That inconsistency is in itself a threat to the requirement for IPs not just to act independently, but to be seen to act independently. Indeed, certain firms we spoke to positively encouraged the mandatory prohibition on pre-appointment engagements on the

basis that they disagreed with the judgment calls taken by other firms in the market. The point raised was that allowing IPs to decide is leading to inconsistent outcomes which put firms with a more ethical approach at a competitive disadvantage.

Notwithstanding the courts' inconsistent approach to what goes on in the "twilight zone", one thing is clear: IPs advising creditors in this period do not owe wider statutory duties and have been known to disclaim duties to the company, or to obtain the contractual right to prefer the creditor's interests (*Re Coniston Hotel*).

We consider that there are clear ethical threats arising from this market practice. Creditors want to know the intended course and outcome of an administration prior to appointing IPs. Whilst a dialogue with prospective administrators might be less problematic where there is a clear and obvious course, or where the creditors and management are fully aligned, often this is not the case and there is certainly no basis for a presumption that it is.

Our review accordingly demonstrates the need to right a wrong very widely perceived by the business community and thinly defended by the insolvency industry, being the extent and depth of the relationships between institutional lenders and the large accountancy firms. Institutional relationships are affecting (or being perceived to affect) personal, fiduciary, appointments.

It is our clear conclusion that reform is needed. We consider that the objective of that reform should be to re-balance the regime with narrow, but deep, regulatory and legal change to better protect entrepreneurial investment and support long-term solutions while continuing to facilitate the efficient allocation and reallocation of capital in our economy.

Recommendation 1 - the ban

The insolvency regime in the UK today carries an unwarranted risk of outcomes skewed by the current commercial dynamic described above. Effective regulatory intervention is rare and the deference with which courts have both traditionally and increasingly treated IPs has led to ineffective civil redress.

We therefore recommend a ban on taking appointment as IP where the IP has personally been involved in pre-appointment work for any interested party in the 2 years before the appointment. This introduces true independence.

The aim of the proposed ban is to reinforce independence and better protect the 'safe space' represented by administration. We recognise that this change may mean lenders will put more pressure on directors to agree deals before any insolvency procedure and to avoid the insolvency procedures at all. The state cannot aim to police every aspect of insolvency practice and the large firms will continue to earn significantly from long-term relationships with lenders by performing pre-insolvency advisory and restructuring work. On the other hand, companies will become aware that they have the option to hold out against the lender's pre-insolvency pressure if they prefer to take their chances with an independent, unrelated IP. In the same way that parties appointing arbitrators to determine their disputes expect independence, stakeholders in insolvency deserve the same. This is a key requirement of a cleaner regime. Practitioners themselves asked that any rule changes were clear and easy to apply and these proposals meet those concerns.

The limited proposed ban addresses the perception of bias on the part of IPs appointed by secured creditors where an institutional or panel relationship existed. An alternative is a wider ban, covering situations where the IP's firm had been involved. There is no doubt that this would

better protect against conflicts of interest. But it comes with practical hurdles. We consider that a ban on this wider basis should be a longer-term aim. At the risk of rewarding the very behaviour in the spotlight, at present the wider version of the ban risks making appointments unworkable given the wide-ranging relationships between the banks and the big accountancy practices where many IPs are currently housed.

Recommendation 2 - a single regulator with an ombudsman

The 2019 Insolvency Service Call for Evidence sought views on the creation of a single regulator in place of the current RPBs, for which a power was created for the Secretary of State in the Small Business Enterprise and Employment Act 2015. This power expires in October 2022.

In light of our experience since the financial crisis and of the findings of our study we see the attraction of introducing a single regulator for reasons of consistency and confidence. We also consider that there may be objections if an existing body (especially one of the RPBs) were to become the single regulator. We consider a conflict of interest sits at the heart of the RPBs: a tension between promoting the reputation and interests of an industry and also calling out and censuring poor behaviour. There is therefore also merit in structuring the new regulator so as to create independent oversight, including a two-tier board, oversight by individuals unconnected to the major insolvency industry interests and systems for financial penalties to benefit the victims rather than the regulator.

In addition, we recommend the creation of an ombudsman to assist in the swift, low-cost resolution of certain disputes. This should be available both during and after an insolvency and provide access to an independent service to investigate and decide facts, offer dispute resolution to complainants and professionals (including the determination of rights and obligations

in relation to complaints within their remit) and report to government on systemic issues. The design of such a scheme will require detailed discussion and scheme rules but the essential service is to provide free access, at the option of the complainant, to an independent determination of a complaint by users of the services of insolvency practitioners, as an alternative to court action. This is an important mechanism to bring greater fairness and transparency to bear on the sector in circumstances where the practical reality is that redress through the courts is out of reach financially for almost all, too late and unlikely to succeed. It also offers policymakers insights into the functioning of this market in ways which courts are not set up to provide, through analysis of trends in complaints and recommendations for change.

R3 said of proposals to create a new regulator: “A key question is not just how the regulatory framework is structured, but what it achieves. From our perspective, regulation should be fair and proportionate, transparent, effective at addressing shortcomings, efficient in reaching decisions, flexible enough to keep pace with innovation, and, above all, consistent. The existing regulatory framework is well-established and the insolvency and restructuring profession is subject to close scrutiny by its regulators.”

The tension between promoting the reputation and interests of an industry and also calling out and censuring poor behaviour is a clear conflict of interest. Recent developments aimed at putting distance between the regulatory and non-regulatory functions of RPBs are not sufficient in our view. The problem is not so much the ethical guidance, which has recently been reinforced and is based on international accounting guidance, but the fact that disclosure appears to be seen as the panacea to all potential ethical threats which are not simply accepted as matters of market practice. This then shifts the onus on to shareholders and directors either to make expensive and often fruitless legal challenges, or to await a tardy regulatory complaint which is

statistically unlikely to be successful.

Further, the statistics do not support the RPBs in arguing for the satisfactory investigation, prosecution and resolution of complaints under current arrangements. We propose that steps are taken to consolidate regulation into the hands of a sole statutory regulator funded by an industry levy.

Recommendation 3 - placing the Code of Ethics on a statutory footing

IPs and RPBs repeatedly relied in discussions with us on the Code of Ethics as holding them to acceptable standards, but it has no force of law and no teeth without sanction which is currently effectively absent. The Code of Ethics should be placed on a statutory footing, with provision for reliance on breaches by shareholders and creditors.

Recommendation 4 - a centralised database recording the outcomes of administrations

Impact assessments are common in other areas of public policy. In the years since the Enterprise Act, no proper assessment of the effectiveness of the statutory objective of rescue has been possible because nobody tracks whether the first, second or third statutory objective has been achieved. We propose that the new regulator maintains a centralized database and hope that rescue culture is taken more seriously as a result.

Recommendation 5 - rule changes in support

We also recommend, **first**, that legislative amendments should make it clear that administrators should not discuss or pre-agree adminis-

tration strategies with appointing creditors before an administration because of the risk that doing so will undermine the integrity of the subsequent appointment.

Second, even with our recommended ban in place (recommendation 1 above), the secured lender still legally holds all the cards as to the appointment of IP, with a right to 5 days' notice of the directors' choice of IP and an accompanying veto which inevitably grants the lender the ultimate right to choose in practice.

We consider that the secured creditor's right to appoint an administrator of their choice is an unnecessary power in light of the requirement of an IP to ensure that they have the necessary skill and experience, or the ability to obtain the same, to perform an appointment. If the profession behaves in the way to be expected it is our view that there is no justification for this trump card.

Secured creditors perceive some advantage in having the company appoint the candidates of their choice and the review was presented with numerous examples of appointments of individuals notionally by the company but where the directors had no effective say in the matter in light of the primacy of the secured creditor's right of appointment. The ultimate right of veto is thus also a disincentive for management, who are frequently criticised for not making appointments themselves at an earlier stage. Removal of this privilege will give companies more opportunity to take decisive action and make their own appointment, particularly if they do not agree with the views of a creditor or its advisors. That option will in turn rebalance pre-appointment discussions between creditors and management ensuring a greater equality of arms. The secured lender would still retain the ability to manage the assets and appoint an IP under a fixed charge.

We consider such a "first past the post" system would be an appropriate way to determine appointments. This would ensure management had an incentive to act swiftly and naturally re-

distribute a proportion of work away from firms with long-standing lender relationships.

We recognise that administrators have a duty to investigate the actions of management upon appointment and for that reason there needs to be a safety check to ensure that directors do not appoint IPs with whom they themselves might have a close relationship, even if not caught by the proposed ban. A streamlined court application process should be made available to management and creditors to uphold the principles of the ban and to challenge a proposed appointment on the grounds of independence only within a short period. Finally, as part of these supporting measures, rule changes should be made to prevent administrators going on to become liquidators and to expedite section 236 applications to make former officeholders' files available to a subsequent liquidator. These rules permit proper enforcement of the primary ban and oversight of appointments.

Third, we consider that the obligation for an IP to seek solvent rescue as the primary objective of administration is given teeth through legislative amendments which put the onus on IPs to document and demonstrate that all practical avenues to rescue have been explored and considered post appointment, including negotiations with appointing creditors. This way, IPs will remain responsible for decisions and a reverse burden of proof will apply where a course of action calls into question ethical matters. Connected to this, there should be rule clarification on the extent to which IPs are permitted to delegate their functions to agents. The deferential standard of court review of administrators' decisions should be removed so that the courts feel able to scrutinise IP conduct, decision-making and delegation more thoroughly and effectively. A docketed and inquisitorial approach to insolvency applications to court during the insolvency, with a costs-neutral regime, should be introduced to rules of court so that references can be made swiftly on ethical and these other key ongoing issues during an administration.

Fourth, the new evaluator process should be extended to cover asset sales over £5 million, drawing on developments in relation to pre-pack sales. Many of the cases considered in the course of our review suggest more could have been done to maximise the return to secondary or unsecured lenders on the sale of assets, both business and property. In certain cases, the valuation of the asset(s) in question has been one of the key disputed issues in the administration. Complaints have repeatedly been made where IPs have relied upon valuation evidence obtained by or provided to the appointing creditor.

Recent changes to the law in relation to pre-pack sales out of administration have introduced the need for an evaluator to provide a report supporting the proposed sale and the evaluator must be suitably independent. This is intended to act as a safety-check and in our view has wider potential application to the sale of a substantial part of a company's assets out of administration. In many cases the evaluator would either be an independent valuer or they would engage a third party with the relevant expertise. Where there had been a sales and marketing process they would review and report on the adequacy of the steps taken. Interested parties would be entitled to raise matters for the evaluator's consideration. If the evaluator approved the terms of sale the IP would have a strong prima facie defence to any subsequent claim which would bring certainty to all concerned.

We recommend that the sale price of all individual or connected assets in excess of £5 million out of administration be supported in this way by an independent evaluator's report confirming the basis of sale and consideration achieved.

Fifth, we also recommend that the government re-consider extending the CIGA moratorium to financial contracts and consider a statutory first charge or levy over a small part - we propose 5% - of an insolvent company's assets. The latter is intended to combat over-leverage in the market and the development of 'loan-to-own' lending,

and to provide administrators with access to funds to enable consideration of a rescue, drawing on a number of comments received in the course of this review.



The APPG on Fair Business Banking is a platform through which businesses, professionals and trade bodies can discuss issues regarding commercial banking and its role in the life cycle of a business, and through which parliamentarians can access information on banking, finance and related issues, including business rescue and insolvency, on behalf of constituents. As a cross-party group, the APPG is an effective vehicle to effect meaningful change via the Parliamentary system. The Group's status is that of an APPG is bound by the rules set out by The Office of the Parliamentary Commissioner for Standards. It does not have charitable status, or official status in the House, nor is it funded by Parliament. It relies wholly on the participation and contribution of parliamentarians, industry members and stakeholders committed to creating a strong platform for business in the UK to thrive. The APPG is coordinated and administered via the APPG on Fair Business Banking Secretariat. An All Party Parliamentary Group (APPG) is an interest group that occupies a strategic and effective position within Parliament. It is cross-party, with a minimum number of parliamentarians from the Government and the official opposition, and cross-house, made up of both peers and MPs.



Humphries Kerstetter LLP is a London law firm specialising in investigations and the resolution of complex commercial disputes by litigation and arbitration. Humphries Kerstetter has supported the APPG in the production of this report, including factual and legal investigatory work and assistance in consideration of the APPG's recommendations.