INSOL International

Module 9

Guidance Text

Ethics and Professional Practice

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1. INTRODUCTION TO ETHICS AND PROFESSIONAL PRACTICE

Welcome to **Module 9**, dealing with E**thics and Professional Practice**. This Module is a standalone elective module choice for the Foundation Certificate. The purpose of this guidance text is to provide:

- an overview of the importance of the role played by insolvency professionals (IPs);
- an evaluation of the nature of the responsibilities of the IP and the ethical conduct expected from IPs; and
- a detailed discussion and commentary on the best practice guidance as contained in INSOL International's publication, *Ethical Principles for Insolvency Professionals*.

This guidance text is all that is required to be consulted for the completion of the assessment for this module. You are not required to look beyond the guidance text for the answers to the assessment questions, although bonus marks will be awarded if you do refer to materials beyond this guidance text when submitting your assessment. For the purpose of self-assessment, you may be required to conduct research beyond the scope of this guidance text.

Please note that the formal assessment for this module must be submitted by **11 pm (23:00) BST on 31 July 2021**. Please consult the web pages for the Foundation Certificate in International Insolvency Law for both the assessment and the instructions for submitting the assessment. **Please note that no extensions for the submission of assessments beyond 31 July 2020 will be considered**.

For general guidance on what is expected of you on the course generally, and more specifically in respect of each module, please consult the course handbook which you will find on the web pages for the Foundation Certificate in International Insolvency Law on the INSOL International website.

2. AIMS AND OUTCOMES OF THIS MODULE

After having completed this module you should have a good understanding of the following aspects of ethics and professional practice:

- the role of the IP in the insolvency system;
- the nature of the duties owed by IPs to their beneficiaries;
- the identity of the beneficiaries of the IP's duties;
- the ethical standards to be expected of IPs;

- the threats to ethical behaviour by IPs;
- aspects relating to proper practice management.

After having completed this module you should be able to:

- explain the duties owed by IPs and the nature of such duties;
- understand the *nexus* between the ethical norms expected from IPs and their fiduciary duties;
- identify threats to ethical conduct by IPs;
- recommend safeguards for ethical conduct;
- understand the policies and procedures in relation to practice management as well as to formulate and utilise them.

Throughout the guidance text you will find a number of self-assessment questions. These are designed to assist you in ensuring that you understand the work being covered as you progress through the text. In order to assist you further, the suggested answers to the self-assessment questions are provided to you in **Appendix A**.

3. AN INTRODUCTION TO ETHICS AND PROFESSIONAL PRACTICE

3.1 The importance of ethical behaviour by insolvency professionals

The role of the Insolvency Practitioner (IP) is one of great importance. IPs play a "significant role in lubricating the wheels of commerce".[1] The success and outcome of an insolvency procedure will to a large extent depend on the IP's attributes, qualifications and experience and, of course, his ethics and morals. The trust and confidence that the stakeholders in an insolvency proceeding (and the public at large) place in the IP is equally important. A lack of trust and confidence in the profession erodes its efficacy in bringing about successful rescues and / or ensuring that returns to creditors for failed companies can be maximised.

The role of the IP is brought into greater focus in the event of corporate insolvency, where more stakeholders stand to be affected by the demise or threatened demise of the debtor. The Corporate Insolvency Practitioner (CIP) operates in difficult and daunting circumstances, involving distressed parties, competing demands, strict deadlines and complex legal, financial and factual issues. Their tasks are therefore not only overwhelming at times, but also involve a great deal of responsibility.

The consequences of financial distress on debtors and all the stakeholders involved make for a chaotic, difficult and volatile situation, often leaving many parties vulnerable and at the "mercy" of the appointed IP. It is therefore not surprising that the parties involved tend to look to the IP to enforce the rules and bring about some

[1] *Re Econ Corp Ltd (No 2)* [2004] SGHC 49, 266 [Singapore].

much needed clarity and order. IPs are relied upon to do these tasks with the utmost professionalism, being mindful of the fact that he is engaged in activities that will have a real impact on people's lives and livelihoods. His conduct should therefore reflect the seriousness of the circumstance and reflect the highest standards of ethical behaviour.

Evidently the public and stakeholders in insolvency will scrutinise the IP and, based on his conduct, form an opinion not only of him and the insolvency profession but also the entire insolvency system. How would people be able to trust the system if they cannot trust the people who administer it?

In this text the abbreviation "IP" will be used in relation to Insolvency Practitioners in general and "CIP" to elaborate on principles of specific importance for Corporate Insolvency Practitioners.

3.2 The nature of an insolvency appointment

IPs are regarded as experts in the administration of insolvent estates and restructuring strategies. They are given a large number of extensive powers to utilise their expertise and experience in relation to the objectives of their appointment. However, if an IP has extensive powers and responsibilities, yet lacks integrity, ethics and basic morality, it will not be of much benefit to the debtor, its stakeholders or society at large. To this end, many jurisdictions have imposed fiduciary norms to govern the conduct of IPs.

A fiduciary is largely accepted to be a person who:

(a) undertakes to act on behalf of another, and

(b) has discretion and power over the interests of the other.[2]

A further element of vulnerability is sometimes added as an indicator for the existence of a fiduciary relationship.[3] It is, therefore, not surprising that most IPs are regarded as fiduciaries.[4]

The word "fiduciary" is, however, not definitive of a single class of relationships to which a fixed set of rules and principles apply; it is necessary to determine the rules that govern each class of fiduciary relationship.[5] Many types of relationships are

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[2] R Nimmer and R Feinberg, "Chapter 11 Business Governance: Fiduciary Duties, Business Judgment, Trustees and Exclusivity" (1989) 6 Bankr Dev J 1, 34 – "The idea of treating one person as a fiduciary of another thus rests on the fact that the discretionary judgment of the one controls the destiny of the other."; R Valsan, "Fiduciary Duties, Conflict of Interest and Proper Exercise of Judgment" [2016] 62 McGill LJ 1, 7. See also J Velasco, "Delimiting fiduciary status" in D Smith and A Gold (eds), *Research Handbook on Fiduciary Law* (Edward Elgar 2018) at 78 – "It is fair to say that power, trust, and vulnerability are the key terms used to describe fiduciary relationships generally." J Glover and J Duns, "Insolvency Administrations at General Law: Fiduciary Obligations of Company Receivers, Voluntary Administrators and Liquidators" (2001) 9 Insolv LJ 137 – "Are voluntary administrators fiduciaries? In the scheme of Pt 5.3A, administrators are acting for the benefit of others and the powers and discretions that they possess are held in representative capacities. These are standard indicia of fiduciary status."

[3] R Valsan, "Fiduciary Duties, Conflict of Interest and Proper Exercise of Judgment" (2016) 62 McGill LJ 1, 7.

[4] J Glover and J Duns, "Insolvency Administrations at General Law: Fiduciary Obligations of Company Receivers, Voluntary Administrators and Liquidators" (2001) 9 Insolv LJ 137; D Milman, *Governance of Distressed Firms* (Edward Elgar 2013) – "…can office-holders be classed as fiduciaries? The answer to this in all cases (whether or not 'officer of the court' status applies) would appear to be in the affirmative."

[5] M Havenga, *Fiduciary Duties of Company Directors with specific regard to Corporate Opportunities* (Transactions of the Centre for Business Law, University of the Free State 1998) 10.

classed as fiduciary in nature and are frequently described as relationships of trust.[6] Lawyers, accountants, agents, trustees, doctors, and directors of companies are but examples of a number of recognised fiduciaries. Evidently, the fiduciary norms applicable to doctors cannot be applied to IPs as their roles and the objectives of their office differ in a number of respects. It is imperative that the fiduciary norms as applicable to IPs are developed and sufficiently nuanced so as to provide better clarity for the insolvency profession and the community in which they operate, including the public at large.

Much ambiguity as to their role is created by jurisdictions that have differing approaches in regard to the duties and obligations that IPs owe. Moreover, jurisdictions have divergent ideas as to the exact nature of the IP's role in different types of insolvency proceedings. This inevitably leads to some confusion as to the role of the profession. IPs, of course, have their own thoughts regarding their role and given the fact that they are appointed from the ranks of several different professions, such as lawyers, accountants, auditors and business managers, the further inevitability of even more confusion is a certainty. This is due to the fact that some of these professions are regarded as fiduciaries in their own right and this will influence their behaviour in accordance with different sets of fiduciary norms, which may be related but not similar. In other words, lawyers and accountants might not have similar approaches to similar situations, purely based on the fact that their frame of reference is different. As an example it could be noted that most lawyers as fiduciaries have a special relationship with the law and the administration of justice which might influence the way in which they deal with a specific situation where elements of dishonesty and fraud have been detected. A much clearer and more definitive approach as to the nature and extent of an IP's *sui generis* fiduciary role is needed. This statement is even more accurate in the case of Corporate Insolvency Practitioners (CIPs), due to the number of interested parties.

Depending on the type of appointment, whether it is a turnaround / rescue or liquidation, the CIP enters the scene and usually takes control of the affairs and business of the debtor company.[7] The extent of an IP's powers and discretion are often far-reaching and without any personal liability. In many jurisdictions the CIP becomes an "officer" of the company and is also required to adhere to the duties and obligations that are normally attributed to company officers.[8] In addition, in many jurisdictions the CIP will be regarded as an officer of the court.[9] These combine to create an intricate net of unique fiduciary responsibilities.

3.2.1 The duties

In accepting an appointment as an IP, the IP gives a voluntary undertaking to abide by the rules and responsibilities that defines that type of fiduciary relationship and thereby encourages the trust of the stakeholders involved.[10] What these rules and

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6 R Flannigan, "The Fiduciary Obligation" (1989) 9 Oxf J Leg Studies 285,286 – "It is a 'deferential' kind of trust in the sense that the trusting person will defer to the judgment of the trusted person. The deference may be total, or it may be only partial or situational. It is accompanied, in some cases, by elements of necessity, dependence or submission."

7 Bearing the distinction between debtor-in-possession and practitioner-in-possession in mind, this statement refers to instances where a form of management displacement does take place.

8 The UK and Australia are good examples here.

9 Examples: South Africa, Scotland, England and Wales (limited instances), Canada, Australia and Germany.

10 M Harding, "Fiduciary relationships, fiduciary law and trust" in D Smith and A Gold (eds), *Research Handbook on Fiduciary Law* (Edward Elgar 2018) 64 – "…fiduciary law's greatest contribution to facilitating a principal's trust-based reliance is perhaps seen in its recognition of voluntary undertakings to abide by the norms that, distinctively, characterise fiduciary relationships."

responsibilities are should therefore be clearly identifiable to ensure the IP's compliance and thereby the trust of the parties.

Although the exact fiduciary duties of IPs in various jurisdictions might differ, the following main duties can broadly be agreed upon as being applicable:

- the duty to act in good faith – this duty implies honesty and fair dealing;
- the duty to act in the best interest of the beneficiary of the fiduciary duties;
- the duty to exercise the powers of the office in an independent and impartial manner – this duty includes the duty to avoid a conflict of interest; and
- a duty which is usually not regarded as being fiduciary in nature, the duty to act with care, skill and diligence.

The duty to act with care, although not fiduciary in nature, is of extreme importance in insolvency situations given the already dire circumstances of the debtor. Furthermore, it is inextricably linked to fiduciary duties for it cannot be said that a fiduciary who acts in a negligent manner has complied with his duty to act in the best interest of the beneficiaries of his duties. The duty to act with care becomes even more important given the qualifications and skills of Ips, effectively rendering them experts and thereby holding them to a higher degree of care.[11]

3.2.2 The beneficiaries

When it is accepted that an IP is a fiduciary, the next question would be to whom the fiduciary duties are owed.

The task of determining the beneficiaries of fiduciary duties in insolvency proceedings is not straightforward or easy. It has already been mentioned that the debtor's demise will have a profound impact on a large number of stakeholders. Various factors should be considered, including:

(a) the extent of financial difficulty of the corporation;

(b) the procedure entered into;[12]

(c) the rights afforded to stakeholders; and

(d) the theories underpinning corporate (in the case of corporate insolvency) and insolvency law.

Most jurisdictions follow a creditor-oriented approach to insolvency and as such it has become widely accepted that the main beneficiaries of an IP's duties are the creditors. However, it is not the only approach to be taken.

Several academics have developed insolvency theories in an attempt to answer the question as to whose benefit the insolvency law should be formulated. For purposes

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[11] L Jacobs and J Neethling, "*Die sorgsame ondernemingsreddingspraktisyn: 'n ondersoek na die gepaste maatstaf*" (2016) 13 LitNet Akademies 3, 773 (English title: "The careful business rescue practitioner: a search for the proper yardstick". Available at https://www.litnet.co.za/careful-business-rescue-practitioner-search-proper-yardstick/.

[12] D Milman, *Governance of Distressed Firms* (Edward Elgar 2013) 92.

of this module, the main theories of insolvency and corporate law will be identified and explained in a condensed form.

3.2.2.1 Contractarian theories

The "contractarian theory" is generally based on wealth maximisation and the idea that the law should maximise the collective return to creditors.[13] This theory is also in line with the "proceduralist" approach to insolvency which contends that insolvency law should address issues that only arise out of insolvency and believe that non-insolvency claims and entitlements should not be protected by the insolvency law unless this would result in a greater return for creditors.[14] A recognised branch of the contractarian theory is the "creditors' bargain theory" (CBT), developed by Jackson in the early 1980s.[15] CBT is based on the premise that creditors enter into a bargain with the debtor company during negotiations for credit and thereby establish their position and possible remedies upon default by the company, such as insolvency.[16] Upon the debtor company's insolvency, the creditors with an interest will try to recover their debt and will enter into a frenzied race with other creditors to enforce their private contractual agreements with the company. This could cause depreciation in value of the business assets, creating uncertainty of returns for all creditors. The CBT proposes to solve this problem by replacing individual enforcement rights with a collective right to share in the proceeds of the insolvency proceeding, giving rise to the "collectivist approach".[17] "…the Creditors' Bargain was essentially a bargain that in the event of bankruptcy, the creditors would get everything."[18] The CBT therefore does not support any redistribution of wealth or consequences in insolvency.[19]

Another contractarian theory can be found in the "team production theory" (TPT) of corporate law.[20] This theory is based on social contract and is much more inclusive in nature than the wealth maximisation ideals of the CBT. This theory builds on the ideology that shareholders are not the only party that contribute to the production process of a company. Other parties, such as trade suppliers and the workforce, all contribute towards the end product.[21] The TPT, therefore, promotes the inclusivity of

13 P Walton, "When is Pre-packaged Administration appropriate? – A Theoretical Consideration" (2011) 20 *Nottingham LJ* 1, 3-4.

14 D Baird, "Loss Distribution, Forum Shopping, and Bankruptcy: A Reply to Warren" (1987) 54 *U Chi L Rev* 54 815; H Nsubuga, "Corporate Insolvency and Employment protection: A Theoretical Perspective" (2016) 4(1) *NIBLeJ* para 2.

15 P Walton, "When is Pre-packaged Administration appropriate? – A Theoretical Consideration" (2011) 20 *Nottingham LJ* 1, 4; H Nsubuga, "Corporate Insolvency and Employment protection: A Theoretical Perspective" 4(1) *NIBLeJ* 4 (2016), para 58.

16 H Nsubuga, "Corporate Insolvency and Employment protection: A Theoretical Perspective" (2016) 4(1) *NIBLeJ* 4 para 58. Walton is of the opinion that one of the shortcomings of the CBT is the fact that it only considers "hypothetical contract creditors". P Walton, "When is Pre-packaged Administration appropriate? – A Theoretical Consideration" (2011) 20 *Nottingham LJ* 1, 5.

17 E Warren, "Bankruptcy Policy" (1987) 54 *U Chi L Rev* 775, 797-799. The Collectivists believe the single justification for bankruptcy to be the enhancement of the collective return to the creditors. See also H Nsubuga, "Corporate Insolvency and Employment protection: A Theoretical Perspective" (2016) 4(1) *NIBLeJ* 4 para 61; P Walton, "When is Pre-packaged Administration appropriate? – A Theoretical Consideration" (2011) 20 *Nottingham LJ* 1, 5.

18 L LoPucki, "A Team Production Theory of Bankruptcy Reorganization" (2004) 57 *Vand L Rev* 741, 748.

19 *Ibid*.

20 L LoPucki, "A Team Production Theory of Bankruptcy Reorganization" (2004) 57 *Vand L Rev* 741, 744; H Nsubuga, "Corporate Insolvency and Employment protection: A Theoretical Perspective" (2016) 4(1) *NIBLeJ* 4 para 72.

21 L LoPucki, "A Team Production Theory of Bankruptcy Reorganization" (2004) 57 *Vand L Rev* 741, 749 – "The team members include all who make firm-specific investments but are unable to protect those investments by direct contracting, personal trust or reputation. Team members may include stockholders, creditors, executives, other employees, suppliers, customers, local governments, regulatory agencies, and others." See

all stakeholders during insolvency proceedings and supports the idea of redistribution of some of the interest of one stakeholder (team member) to another.[22] The problem with the TPT might be that it is too wide and includes too many stakeholders (team members) who cannot realistically nor economically always benefit from the insolvency proceeding.[23] This theory closely resembles some of the "traditionalist" theories on insolvency.

3.2.2.2 Traditionalist theories

Traditionalist theories on insolvency law are against the idea that the law should exist only to serve creditors' interests and are consequently also inclusive in nature.[24] Communitarianism looks to balance a wide range of different stakeholders in the insolvency of the debtor and even to consider the welfare of the community at large.[25] It "considers limiting the rights of high ranking creditors to give way to some extent to others including the community at large."[26] It subscribes to the notion of redistribution, that is, to redistribute the consequences of the debtor's default.[27] Communitarian theorists seek to focus on the fact that those involved in and dealing with companies are humans and corporate law should not be de-personalised.[28] The Cork Report also seems to validate at least some aspects of the Communitarian Theory. [29]

Criticism levelled against this theory relates to the difficulty of defining the community and determining how far it may stretch and is cumbersome.[30] Also, articulating the community's needs in legislative form may prove to be problematic.[31] The communitarian theory has a lot in common with Warren's "multi value approach", or "eclectic approach".[32] In a corporate insolvency context this approach requires recognition of those who are not directly "creditors".[33] Warren refers to the notion that it was intended that insolvency law address concerns that are broader than just the debtor's immediate problems and that of its creditors.[34] It should involve considering other internal or external stakeholders such as employees, suppliers or tax authorities and in some instances to "protect interests that have no other

also H Nsubuga, "Corporate Insolvency and Employment protection: A Theoretical Perspective" (2016) 4(1) *NIBLeJ* 4 para 73.

22 H Nsubuga, "Corporate Insolvency and Employment protection: A Theoretical Perspective" (2016) 4(1) *NIBLeJ* 4 para 77 – "The TPT being an inclusive theory, advocates honouring all team members' interests on the insolvency of the company, whether in terms of financial gain or losses."

23 LoPucki contends that TPT entitlements are entitlements to "rents and surpluses" and it goes without saying much that there will not be a lot of surplus in the case of insolvency.

24 J Wood, "Corporate Rescue: A Critical Analysis of its Fundamentals and Existence" (PhD thesis, University of Leeds 2013) – "Contrary to proceduralists, traditionalists believe that insolvency law is not a tool solely reserved for the creditors in which they can pursue their own interests." at 88; H Nsubuga, "Corporate Insolvency and Employment protection: A Theoretical Perspective" (2016) 4(1) *NIBLeJ* 4 para 3.

25 P Walton, "When is Pre-packaged Administration appropriate? – A Theoretical Consideration" (2011) 20 *Nottingham LJ* 1, 7.

26 *Ibid*.

27 E Warren, "Bankruptcy Policy" (1987) 54 *U Chi L Rev* 775, 777.

28 A Keay, "Tackling the Issue of the Corporate Objective: An Analysis of the United Kingdom's 'Enlightened Shareholder Value Approach'" (2007) 29 *Sydney L Rev* 577, 586.

29 Cork Report on Insolvency Law and Practice, Cmnd 8558 [1982]: p 56 para 204. "The chain reaction consequent upon any given failure can potentially be so disastrous to creditors, employees and the community that it must not be overlooked."

30 P Walton, "When is Pre-packaged Administration appropriate? – A Theoretical Consideration" (2011) 20 *Nottingham LJ* 1, 7.

31 *Idem*, at 9.

32 *Idem*, at 10.

33 E Warren, "Bankruptcy Policy" 54 (1987) *U Chi L Rev* 775; P Walton, "When is Pre-packaged Administration appropriate? – A Theoretical Consideration" (2011) 20 *Nottingham LJ* 1, 10.

34 E Warren, "Bankruptcy Policy" (1987) 54 *U Chi L Rev* 775, 788.

protection".[35] It is, however, criticised as "too widely expressed to be of much specific assistance in developing policy."[36] It does not provide enough guidance as to the weight that has to be afforded to each of the interests and priorities that come into play in an insolvency context. As Walton states, "[i]t is not clear which principles are to be seen as core and which are of peripheral relevance."[37] Baird criticises Warren's approach by asking the reasonable question of why stakeholders should be given special rights in insolvency if they don't have the same rights outside of insolvency?[38]

3.2.2.3 The "enlightened creditor value" approach

As part of a recent research project, I developed my own theory of insolvency law: the "enlightened creditor value" (ECV) approach.

Like its solvent brother, the ESV approach,[39] the ECV sets out to strike a balance between the competing interests of differing stakeholders in order to benefit creditors in the long run. It can be seen as a compromise between the creditor theories and stakeholder theories.

This theory encourages the CIP to achieve the best outcome for creditors by taking into account all the relevant considerations for that purpose; this involves the taking of a proper balanced view of the short and long term – the interests of the shareholders and employees, customers, suppliers, financiers and others – as well as to consider the impact of the company's possible demise on the community. The basic position is that CIPs are required to treat creditors' interests as paramount, that is, "creditors first", not "creditors only". The interests of employees or other stakeholders should be considered in performing these duties – but only where this would be in the creditors' interest. A practical example of this theory could be something along the following lines: If a CIP faces the decision of whether or not to lay-off the employees of the company during rescue proceedings, the decision to delay termination of their employment contracts, at least to some extent, would involve a consideration of the employees' interests but ultimately should hold some benefit for the creditors in that the employees' continuous employment will contribute to the generation of revenue or the retention of goodwill that will lead to a better outcome for creditors in the long run.

This approach can be further qualified by stating that the extent to which a CIP would have to exercise his duties for the benefit of other stakeholders, should depend on the nature of the proceedings and the scope of the financial difficulty the debtor company is facing:

(a) During rescue proceedings the CIP, having regard to the financial situation of the debtor, ought to weigh up the competing interests of the stakeholders involved. If the financial difficulty of the debtor has not reached the stage of "doubtful solvency", as Hawke states,[40] then the CIP should take greater care to act in the

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35 E Warren, "Bankruptcy Policy" (1987) 54 *U Chi L Rev* 775, 788; P Walton, "When is Pre-packaged Administration appropriate? – A Theoretical Consideration" (2011) 20 *Nottingham LJ* 1, 10.

36 P Walton, "When is Pre-packaged Administration appropriate? – A Theoretical Consideration" (2011) 20 *Nottingham LJ* 1, 11.

37 *Ibid*.

38 D Baird, "Loss Distribution, Forum Shopping, and Bankruptcy: A Reply to Warren" (1987) 54 *U Chi L Rev* 54 815, 817-818 – "Whenever we must have a legal rule to distribute losses in bankruptcy, we must also have a legal rule that distributes the same loss outside of bankruptcy", at 822.

39 The enlightened shareholder value approach.

40 N Hawke, "Creditors' Interest in Solvent and Insolvent Companies" [1989] *JBL* 54, 59.

interests of the company and its shareholders.[41] Where the company is, however, beyond that point and where it conversely enters the "twilight zone", the CIP should keep the interests of the creditors at the fore;

(b) Where the CIP is appointed as the liquidator of the company he or she owes fiduciary duties to the creditors of the company but also to the company itself.[42] Liquidators, therefore, exercise their duties for the benefit of the creditors in the first instance and then for the benefit of the shareholders.

3.3 INSOL International's *Ethical Principles for Insolvency Professionals*

In 2016 INSOL International[43] took the initiative of drafting "Ethical Principles for Insolvency Professionals" to address the ethical foundation that underpins the insolvency profession. The drafting of the principles was undertaken by Working Group 10 of INSOL's Task Force 2021. This Working Group considered an extensive range of ethical issues in drafting the principles that are meant to be used as best practice guidance to members as well as to jurisdictions and recognised professional bodies that do not have ethical guidelines that apply to IPs. As trust and confidence are essential to the efficacy of an insolvency regime, the goal in establishing the Principles is to enhance and protect the integrity of the insolvency profession and to create a framework that is fair, effective, practical and readily understood.

The members of the Working Group were representative of the diverse community that work in insolvency; from practitioners with a legal or accounting background, members of professional bodies to academics focusing on ethics in insolvency. Several jurisdictions were represented by those involved, contributing to the final product providing a global overview of ethical considerations for the insolvency profession.

The Principles are therefore generic in nature in order to set out the most basic ethical standards expected of IPs. It could be viewed as a quasi-"model code" that can be adapted as needed and incorporated into a jurisdiction's provisions relating to the regulation of IPs.

The Principles are therefore not meant to replace the ethical obligations of IPs in terms of a specific jurisdiction's legislation, regulations or other forms of professional standards and are not mandatory. As stated, they are meant to provide a guide to best practice while allowing for the differing nature of legislation and insolvency practice in different jurisdictions.

The Principles provide guidance based on international standards of conduct and consequently some of the principles may impose a higher standard than existing jurisdictional legal requirements. Where the law in a jurisdiction is silent, or ambiguous, the Principles aim to provide clarity and guidance as to what is regarded as best practice.

In the event that the Principles in some way conflict with existing local rules or laws, they are not intended to supersede such rules or laws. The majority of the content of this Guidance Text is based on the INSOL Principles.

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41 *Ibid* – "…as long as the company remains on the right side of 'doubtful solvency,' any consideration for creditors' interests need only be minimal."

42 A Keay and P Walton, *Insolvency Law Corporate and Personal* (4th ed, LexisNexis, 2017) 299.

43 International Association of Restructuring, Insolvency and Bankruptcy Professionals.

3.4 Other sources of guidance on ethical behaviour

There are also other documents that provide guidance on the qualities and the behaviour that is to be expected of IPs that will be important for this module.

3.4.1 UNCITRAL Legislative Guide on Insolvency Law

The purpose of the United Nations Commission on International Trade Law (UNCITRAL) *Legislative Guide on Insolvency Law* (UNCITRAL Guide or the Guide) is to aid in establishing an efficient and effective legal framework for addressing the financial difficulty of debtors.[44] It is intended to act as a point of reference for national authorities and legislative bodies when preparing new insolvency laws and regulations, or for the purpose of reviewing the adequacy of existing insolvency laws and regulations.[45] To this end, the UNCITRAL Guide provides guidance on the role of the insolvency representative or IP, his tasks and rights and duties. The Guide states that due to the important role of the CIP and the extensive powers bestowed on him, it is essential that he is appropriately qualified and possesses the knowledge, experience and **personal qualities** that will ensure not only the effective and efficient conduct of the proceedings, but also that there is confidence in the insolvency regime.[46] The most important qualities mentioned by the Guide for purposes of this module are: integrity, impartiality, independence and good management skills.[47]

Where relevant, mention will also be made of this document in the discussion of the INSOL Principles below.

3.4.2 The World Bank Principles

The World Bank's Principles and Guidelines for Effective Insolvency and Creditor Rights Systems (World Bank Principles),[48] much like the UNCITRAL Legislative Guide, are to be used to guide system reform and benchmarking. The principles and guidelines are a distillation of international best practice on the design aspects of insolvency systems. The principles touch on a wide array of important aspects regarding the insolvency process.

Relevant to the discussion on ethics and practitioner behaviour are:

(1) **Principle 33**, which refers to the integrity of participants in the insolvency system. It provides that rules should be provided to prevent abuse of the insolvency system and that these rules in turn instil public confidence in the insolvency system.[49] Even though the principles do not mention IPs specifically, they are included by implication as one of the main participants in the proceedings. This principle highlights (by implication) the integrity of the IP and touches on the prevention of abuse of the insolvency system; and

(2) **Principle 35**, which refers to the competence and integrity of insolvency administrators and provides that IPs should be competent to exercise the powers

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44 UNCITRAL Legislative Guide on Insolvency Law, 2004, available online at http://www.uncitral.org/pdf/english/texts/insolven/05-80722_Ebook.pdf, p 1, para 1.

45 *Idem*, p 1, para 1.

46 *Idem*, p 174, para 35. Emphasis added.

47 *Idem*, p 174-175, para 41.

48 World Bank Group, *Principles and Guidelines for Effective Insolvency and Creditor Rights Systems*, April 2001.

49 *Idem*, p 60, para 220-221.

given to them and should act with integrity, impartiality and independence.[50] This principle states that those who administer insolvencies are given powers over debtors and their assets and have a duty to protect them and their value.[51]

3.4.3 European Bank for Reconstruction and Development (EBRD) Office Holder Principles

The EBRD Insolvency Office Holder Principles[52] (EBRD Principles) build on the World Bank Principles and Guidelines and the UNCITRAL Legislative Guide, by providing greater detail and guidance on the application of the standards and practices advanced by those institutions in relation to insolvency professionals.

The EBRD Principles provide guidance on several aspects of the role of the IP in an insolvency regime and promote ethical norms such as honesty, integrity, independence and impartiality, as well as the duty to stay abreast of important legal and technical developments in the field and to act with care.

Principle 12 recommends that local laws should encourage and facilitate the development of a code of ethics.[53] Moreover, it suggests that the law should compel the application of the code by ensuring that it is enforced and binding on IPs.

Where applicable, reference will also be made to the EBRD Principles in the text below.

4. CODES OF CONDUCT

IPs can often stumble into a breach of their fiduciary duties, not necessarily because they are unethical but because they sometimes fail to understand the extent of what is expected of them in the role of IP. One way in which an attempt can be made to remedy this, is for jurisdictions to draft a code of professional conduct and ethics specifically aimed at IPs. This will not only provide IPs with the opportunity to examine the nature and goals of their work, it also offers information to others (the stakeholders and general public) about what can be expected from members of the insolvency profession.

Not only will this enable IPs to better navigate the ethical conundrums of insolvency appointments relating to remuneration, but will also provide a rare opportunity to educate stakeholders and members of the public who are often too keen to believe the worst of the insolvency profession.

A code of conduct should incorporate the guidance and best practice principles provided by the standard-setting bodies for insolvency (UNCITRAL and the World Bank Group) as well as other international organisations.

50 *Idem*, p 61, para 226.
51 *Idem*, p 61, para 227.
52 *EBRD Principles in Respect of the Qualifications, Appointment, Conduct, Supervision, and Regulation of Office Holders in Insolvency Cases*, June 2007, available online at: file://prs- tore2.unv.wlv.ac.uk/home0$/u22982/home/Profile/Downloads/ioh_principles%20(1).pdf.
53 *Idem*, p 11.

5. THE PRINCIPLES

5.1 Introduction

As stated above, a code of conduct can be seen as a sensible way of educating IPs and the general public as to the ethical standards expected of officeholders in a specific jurisdiction. There are various approaches to drafting a code of conduct.

Some codes of conduct are **rules-based**. A rules-based code usually includes a set of detailed rules to govern professional conduct and to serve as a foundation for resolving grievances.[54] It is a type of code that sets out the do's and don'ts of the profession and are usually binding and enforced throughout the system.

Other codes follow a **principles-based** approach. A principles-based approach usually sets out certain ideals to which practitioners should strive and makes use of lofty language about what "should" be done in regard to certain themes. Instead of focusing on what is right or wrong, it places an emphasis on self-realisation as to what the best approach in a situation might be.

As the title suggests, the INSOL Principles follow a principles-based approach. As noted earlier, the INSOL Principles are not mandatory and are meant to set out international best-practice ethical behaviour whilst not being bound to any specific jurisdiction. Moreover, it can be argued that a principles-based approach to ethics further encourages ethical behaviour by compelling IPs to consider whether their conduct meets the ideals set out in the principles, in effect also compelling the IPs to think about what the ethical thing is to do.

5.2 Integrity

Principle 1 – Integrity
Integrity In addition to complying with applicable law, Members should endeavour to demonstrate the highest levels of integrity by being straightforward, honest, and truthful; and by adhering to high moral and ethical principles in all aspects of their professional practice.
Commentary Integrity implies fair dealing, honesty and truthfulness.

The IP is deemed to act in good faith if he acts with honesty, integrity and confidentiality. On account of his membership of a particular profession,[55] the IP is in most instances already required to demonstrate impeccable probity and honesty.

[54] M Frankel, "Professional Codes: Why, How, and with What Impact?" (1989) 8 *J Bus Ethics* 109, 111.
[55] Lawyers, accountants, auditors.

The beneficiaries in the insolvency proceedings are at "at the mercy of" of the IP's discretionary powers;[56] they have to trust and / or rely on the IP to protect their interests. This reliance and trust in the practitioner demands honesty, truthfulness and transparency on the part of the IP. It is crucial for the IP to be honest and truthful with the beneficiaries and to act with integrity towards them at all times. Honesty implies that the IP should refrain from lying, while truthfulness means that the IP should not conceal any facts from parties with an interest in the outcome of the insolvency. Honesty further implies that the IP should be open and transparent in his decision-making and should not conceal or misrepresent any information. The IP should be honest and truthful when negotiating on behalf of the beneficiaries as well as when reporting on his acts and dealings.

The IP must refrain from misleading a creditor, employee or shareholder of the company through any act or omission. Honesty and frankness by the IP may also help neutralise any negative emotions during the insolvency proceeding. An honest and transparent approach to the procedure would instil confidence among beneficiaries and the public and facilitate better co-operation. In restructuring proceedings, this duty will include honesty and truthfulness regarding the prospects of success.

Self-Assessment Exercise 1

Question 1

What are the most common elements associated with the existence of a fiduciary relationship?

Question 2

Identify the key fiduciary duties linked to Insolvency Professionals

Question 3

True or False? All Insolvency Professionals owe fiduciary duties.

Question 4

Identify the sources of ethical guidance available to jurisdictions when considering frameworks for addressing the behaviour of Insolvency professionals

Question 5

True or False? Being truthful and being honest amounts to the same thing.

For commentary and feedback on self-assessment exercise 1, please see APPENDIX A

[56] F Cassim *et al, Contemporary Company Law* (2nd ed, Juta 2012) 512 – "Typically, in fiduciary relationships, one party is vulnerable to, or is at the mercy of, another party's discretion."

5.3 Objectivity, independence and impartiality

Principle 2 – Objectivity, Independence and Impartiality
Objectivity, Independence and Impartiality Members should exhibit the highest levels of objectivity, independence and impartiality in the exercise of their powers and duties. Members should avoid circumstances likely to result in a conflict of interest. Members appointed over an estate should not acquire or remove any assets or cash from the estate except as prescribed or as properly authorised remuneration. Members should not be unjustly enriched, for example, by receiving secret kick-backs or commissions.
Commentary Independence should be considered both as a matter of fact and from the perspective of an informed observer. It should be considered with reference to jurisdictional guidance, whether legislative, professional or code-based, but the key tenet underlying the principle of independence should be ensuring that a Member's conduct is, and is seen to be, not unfairly or improperly biased towards any party, including Members themselves or their associates. A Member should not accept an appointment in connection with the estate if his (or a related party's) relationship with the directors of the company or any of the stakeholders would give rise to a possible or perceived lack of independence. Threats to objectivity, independence and impartiality may include any of the following, singly or in combination: • Self - interest; • Self - review; • Advocacy; • Familiarity; and • Intimidation. Lack of independence cannot necessarily be cured by disclosure or by appointment of an independent joint practitioner or officeholder, although both options may be considered and may be appropriate in certain circumstances. Where a Member purchases or removes assets or cash from the estate (excluding appropriately approved remuneration and disbursements payments), it is likely that there will be a **perception** that independence, objectivity and / or impartiality has been breached, even if it has **not** in fact been breached. Such action may erode trust in the integrity of such Member and the process.

> Where a Member appointed over the estate of a commercial retailer is purchasing goods or services from a commercial retailer that sells to the public, it should generally be permissible for such Member to purchase such items from the retailer in the ordinary course of business (for example, buying food in a retailer on the same terms as every other purchaser). However, Members should not take advantage of staff discounts or special payment terms, as doing so may impair, or be perceived to impair, independence.
>
> Bribery or payment or receipt of secret commissions in order to receive work or provide work to others should be unacceptable.
>
> Acquisitions by close connections, e.g. family, connected / related parties, will generally give rise to the same concerns as acquisitions by Members themselves. Therefore, immediate relatives and close business connections should be subject to the same restrictions as Members.
>
> Jurisdictions may wish to permit a Member (or relative or connection) to purchase assets where the stakeholders have given explicit permission in advance.

The IP will only be able to exercise his discretion and powers in the best interest of the beneficiaries if he is independent and impartial. This is especially true given the balancing act he has to perform in considering and dealing with the competing interests of the stakeholders.[57]

The call to independence and impartiality of the IP aims to ensure that the IP does not allow bias, a conflicting interest, or the undue influence of others to override his professional and / or business judgements in the execution of his duties and obligations. It is worth noting that many jurisdictions have strict legislative provisions dealing with this aspect.[58] IPs should not take appointments where their independence and impartiality will be called into question by the existence of a relationship with a stakeholder. In the event that such a relationship precludes an IP form accepting an insolvency appointment, a joint appointment does not necessarily constitute a proper safeguard.

Independence is two-fold. IPs must be independent in fact and also be seen or perceived to be independent. Independence in fact requires that the IP be factually free from any influences that could compromise his judgement. IPs must, therefore, avoid all personal and professional relationships and direct or indirect interests that will adversely influence, impair or threaten their integrity and ability to make decisions. Independence in perception, on the other hand, includes the avoidance of circumstances that would lead a reasonably informed third party to conclude that the IP's integrity, independence and impartiality have been compromised.

57 C Anderson, "Miracle Workers or Ambulance Chasers? The Role of Administrators in the Part 5.3A Process" (2004) 12 *Insolv LJ* 238, 248.

58 Australia in particular has extensive provisions dealing with the independence and impartiality of CIPs. See eg s 448C of the Corporations Act 50 of 2001 and the Australian Restructuring, Insolvency and Turnaround Association (ARITA) Code of Professional Practice. Australia's firm approach to independence and impartiality stems from the well-known Harmer Report (Australian Law Reform Commission General Insolvency Inquiry Report No 45 (1988)), which emphasised that impartiality is one of the nine fundamental principles for an efficient insolvency regime – "An insolvency administration should be impartial, efficient and expeditious".

Being seen or perceived to be independent and impartial is of extreme importance in the context of insolvency proceedings. If the stakeholders involved in the proceedings perceive the IP to be biased, or to lack independence (even though it might be untrue), it would negate the trust and reliance that they have placed in him. Without trust and reliance, the stakeholders and beneficiaries will no longer believe that the IP is bound to act in their best interest,[59] which could lead to a discontinuance of their co-operation with the IP and the insolvency process. This could be particularly cumbersome in rescue proceedings where the co-operation of certain parties is essential to the success of implementing a rescue plan or strategy. In other words, a perceived lack of independence could undermine the success of an entire rescue proceeding.

In the pursuit of ensuring the independence of IPs, jurisdictions usually identify certain personal and professional relationships or situations that might give rise to a lack of independence. These might include any professional or personal association with the company or a company director,[60] a company shareholder, a company employee, company business partners, other firms or entities controlled by the company, either secured or unsecured company creditors, company debtors, or even the relatives of company officials. As the aforementioned list does not purport to be a *numerus clausus* of relationships, each instance of alleged lack of independence would have to be assessed against the prevailing circumstances.

In order to address threats to independence and impartiality, some jurisdictions provide for the disclosure of the relationship and a declaration of independence. In this document an IP would be required to truthfully disclose any and all relationships that he might have with any stakeholders in the insolvency proceeding, as well as the nature of said relationship and the level of interaction with the stakeholder. The IP would also be expected to state that despite the existence of a relationship with a stakeholder he would still be able to perform his duties independently and impartially. However, disclosure of such a relationships does not suddenly render them harmless. If the relationship is not substantial and of a merely superficial nature, disclosing it and declaring independence might remedy the situation. However, it will be a much harder task convincing stakeholders of independence and impartiality when the IP has had a longstanding professional or personal relationship with someone related to the proceedings or one of the stakeholders. The mere disclosure of any relationship as a solution, is flawed. No disclosure serves as a guarantee of impartial and objective conduct. Instead, the declaration by the IP should be seen as a disclosure of those relationships that do not pose any risk to the practitioner's independence.

The elements of the insolvency proceedings dealt with below are particularly cumbersome and often give rise to threats to the independence and impartiality of the IP and specifically the CIP.

5.3.1 Nature of pre-commencement / appointment involvement

In practice, prior consultations often occur between the CIP and the company or stakeholders. These consultations may also create the impression of a lack of independence and impartiality on the part of the CIP. Yet the prior consultations need not result in the disqualification of that person as practitioner and may in fact

[59] *Bovis Lend Lease Pty Ltd v Wily* [2003] 45 ACSR 612: 139 [Australia].

[60] See, eg, *Bovis Lend Lease Pty Ltd v Wily* [2003] 45 ACSR 612 – in this case the CIP had previously acted as an advisor to one of the company's directors; *African Banking Corporation of Botswana v Kariba Furniture Manufacturers and others (228/2014)* [2015] ZASCA 69; 2015 (5) SA 192 (SCA); [2015] 3 All SA 10 (SCA) – in this case the CIP had previously acted as an attorney for the company.

constitute a crucial part of the insolvency process. Therefore, not all forms of contact between the CIP and stakeholder parties prior to the practitioner's appointment would necessarily result in a lack of independence. Nevertheless, there should be limits to what would be deemed acceptable engagement during such consultations. Should the consultation involve material engagement by any of the stakeholder parties, the CIP would no longer be independent and should therefore not be appointed as practitioner. The advice provided by the practitioner in the prior consultation should be limited to the company's financial position, the company's solvency, the effects of potential insolvency, and any alternatives to insolvency. It would also make sense for the CIP to set out the nature and extent of prior consultations in a disclosure statement. This would facilitate improved transparency and help prevent accusations of a lack of independence.

CASE STUDY

***Re Korda, Ten Network Holdings Ltd (Admn Apptd) (Recs and Mgrs Apptd)* [2017] FCA 914 [AUSTRALIA]**

In this case the administrators' firm had been involved in reviewing the company's financial position for several months prior to their appointment. The question before the court was whether they should be allowed to continue to act as administrators given their "long-term, substantial and remunerative involvement" with the company.

It is a longstanding practice and especially commonplace for large and complex companies to engage CIPs to undertake a contingency plan in the event that it becomes necessary to appoint a CIP. Such a practitioner is usually referred to as a "potential" or "putative" practitioner. It is assumed that the potential CIP would be able to quickly step into their role and be able to commence it seamlessly, or that they would be able to "hit the ground running".

In the matter of *Korda* the court elaborated on the nature of modern day corporate restructuring and the importance of early intervention and being prepared to act when and if necessary.

In hearing evidence it was generally accepted that the administrators' firm in this case refrained from providing advice to the board of directors, the creditors or any other stakeholders. The nature of the work done by the firm related to deposing the management in order to form an understanding of the company's operations, financial position, legal and contractual obligations and cash flow. Based on this information a transformation plan could be developed and, in the event of it being unsuccessful, a draft administration plan. It was noted also that neither of the appointed administrators were involved in any of the work described above. Nor did either of them meet with any of the board members or management of the debtor prior to their appointment.

The Australian Securities and Investments Commission (ASIC), appearing as *amicus curiae*, submitted the following statement (with which the court concurred):

"Directors contemplating potential insolvency should be encouraged to engage with appropriately-qualified professionals early to develop restructuring plans which will maximise the chance of rescuing a viable business or returning as much value as possible to the relevant stakeholders should a later appointment prove

necessary. A reasonable fair-minded observer would appreciate that as a common characteristic of large and complex corporate distress situations. Provided that appropriate safeguards are put in place to avoid the existence or appearance of conflict should an appointment subsequently prove necessary, significant, long-term and consequently remunerative work undertaken for such purposes should not of itself preclude the practitioner from taking a formal appointment (subject of course to consideration of the facts and circumstances of each particular case).“

The court held that these “safeguards” could include: that the potential administrator makes it clear to the board of directors and executives that she or he is the person who might become the actual administrator if other measures to fix the company’s finances do not succeed as well as proper record keeping of all of the meetings held and tasks performed

In this case the court did not find actual or apprehended bias or conflict (despite the substantial pre-appointment work) as the administrators work in this regard was limited to certain aspects and the engagement did not involve any advice to the company or its directors.

5.3.2 Appointment

In many jurisdictions the CIP can be appointed by either the board of directors or a stakeholder (usually a shareholder or creditor). This may lead the appointee to expect that the practitioner would prioritise their interests. In some instances, these persons, being the “principal”, even believe that it is within their power to influence the CIP. Thus, it is vitally important for the CIP to be aware of his responsibilities in this regard. The practitioner should not make any promises to those who appointed him and should make it very clear that he is expected to act in the interests of all the beneficiaries. The duty of independence also obliges the CIP to scrutinise each given situation prior to accepting an appointment. Such scrutiny would include reasonable steps to determine any possible association or conflict of interest with any stakeholder.

5.3.3 Subsequent appointments

Subsequent appointments refer to a scenario where the same CIP is allowed to act in different insolvency capacities in relation to the same debtor company. In some jurisdictions, such as England and Wales, CIPs are allowed to be appointed in this manner.[61] Subsequent appointments pose problems in relation to independence and impartiality due to the self-review and self-interest threat it creates. The Insolvency Code of Ethics of the Institute of Chartered Accountants of England and Wales (ICAEW) recognises the potential conflict of interest in this regard and utilised the scenario “sequential insolvency appointments” as an example of circumstances that might lead to a self-review threat being created.[62] A self-review threat refers to a situation where a CIP, due to being involved in prior decision-making, will not be able to appropriately evaluate the results of previous judgements made or services rendered.[63]

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[61] In South Africa this is prohibited by statute.
[62] ICAEW Insolvency Code of Ethics, 2114.1 A5(b)(ii), available at https://www.icaew.com/-/media/corporate/files/technical/ethics/insolvency-code-of-ethics.ashx?la=en.
[63] *Idem*, 2114.1 A4(b).

The self-interest threat relates to the issue of remuneration of the CIP. The reason subsequent appointments might pose an issue in relation to the remuneration of the CIP, is that the CIP will be remunerated twice for work done in relation to the same company. A self-interest threat refers to a situation where the interests (including financial interests) of the CIP might inappropriately influence his judgement or behaviour.[64] An example of a way in which a subsequent appointment and the corresponding subsequent remuneration might influence the behaviour of the CIP, could be that a rescue or turnaround practitioner might not put his best effort into saving the debtor from liquidation due to the fact that he knows he would subsequently be appointed as the liquidator and be paid again. CIPs who engage in subsequent appointments often hold the view that the previous appointment does hold some benefits and advantages in the subsequent appointment (such as institutional knowledge) and as professionals have the opinion that they are able to act with independence and impartiality. In jurisdictions where subsequent appointments are allowed, the opinion is held that the benefits outweigh the risks.

In certain jurisdictions subsequent appointments in relation to the same debtor company are prohibited due to the threats expressed above. South Africa is a good example of this. The South African Companies Act of 2008 provides that a business rescue practitioner may not be appointed as the liquidator of the debtor in subsequent liquidation proceedings.[65] As already mentioned, other jurisdictions such as England and Wales[66] and New Zealand[67] permit subsequent appointments.

5.3.4 Secret monies and personal transactions with the company

The CIP should act in the best interests of the beneficiaries of his duties at all times and in all transactions. As a fiduciary, a CIP is not allowed to make a secret profit at the expense of the beneficiaries, or place himself in a position where his personal interests (or that of parties related or connected to him) conflict with his duties. If his judgement was influenced by the fact that he stands to gain personally from a decision, it cannot be said that he was acting in the best interests of the beneficiaries of his duties. This is of particular importance in situations where the CIP (or family / friend of the CIP) would like to purchase assets from the company. This could in effect place the CIP at both ends of the contract, which may cause a strong suspicion that the practitioner, being a fiduciary, is serving his own interests instead of those of the beneficiaries.[68] There are also a number of ways in which the CIP would be able to manipulate such a transaction for his own benefit, for example fixing an advantageous price, as the CIP would have knowledge of the bare minimum the company would accept and drafting (or having input into the drafting of) a contract with favourable clauses.[69] To this end it is important that a CIP follows the necessary procedural steps (disclosure) and obtains the necessary informed consent where a jurisdiction permits transactions between the CIP and the company.

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64 *Idem*, 2114.1 A4(a). See also INSOL Principles, p 10 for a definition of "self-interest" – "A situation in which a Member has, or is perceived to have, a direct interest in obtaining a particular outcome: for example, where such Member (or a close associate) is also a creditor or shareholder of the insolvent estate."

65 Companies Act 71 of 2008, s 140(4).

66 An example can be found in the Insolvency Act 1986, Sch B1, para 83(7)(b), which allows for an administrator to be a liquidator in a subsequent appointment.

67 Companies Act 2003, s 239ABY provides that the administrator is to be the default liquidator. This section was inserted into the Act by the Companies Amendment Act of 2006.

68 J Shepherd, *The Law of Fiduciaries* (Carswell 1981), 157 – "Put another way, the rule could be expressed: there is a heavy presumption that a person who has acted on both sides of a transaction, on one side as a fiduciary and on the other side in his individual capacity, has used his fiduciary powers to benefit himself."

69 *Ibid*.

The CIP's duty to act with independence and impartiality therefore encapsulates the same values as the familiar "no-profit" and "no-conflict" rules in Corporate Law and underpins his duty of undivided loyalty to the beneficiaries.

The no-profit rule determines that a fiduciary may not profit from his position of trust (his position as CIP) and thereby be unjustly enriched, for example by receiving secret kick-backs or commissions.

The no-conflict rule determines that a fiduciary my not allow a conflict to arise between his duty and the interests of the beneficiaries, for example transacting with the debtor company in his personal capacity.

CASE STUDIES

Commonwealth Bank of Australia v Irving **[1996] 65 FCR 291 [AUSTRALIA]**

This case perfectly illustrates that even without any actual bias shown, personal relationships with stakeholders can result in a lack of independence due to the perception created thereby.

The CIP (Mr Irving), a chartered accountant, was appointment as the administrator in terms of the Australian Corporations Act Pt5.3A for the debtor company, NPC. At that time the company had only one director, Mr Roberts. Approximately two weeks prior to the commencement of the proceedings, Mr Townsend and Mr Shergold had resigned as directors of the company.

Mr Irving and Mr Townsend had known one another for 16 years. Mr Townsend, a legal practitioner, had at numerous times acted as legal adviser to Mr Irving in his practice as a chartered accountant. The two also partook in the same charity events and sport activities in relation thereto. These charity events were also widely publicised.

Moreover, prior to commencement of the insolvency proceedings Mr Irving had provided consultation services to the company regarding its financial position. As part of his services he had also engaged in discussions with one of the company's major secured creditors (a bank).

Two of the company's creditors sought the removal of Mr Irving as administrator of the company due to his lack of independence.

It is important to note the following:

(a) Mr Irving had disclosed his relationship with the directors and the company before taking the appointment and stated therein that he believed that he would still be able to act in an independent manner;

(b) There was no factual evidence of any impropriety by Mr Irving as administrator and no party suggested anything to the contrary;

(c) the situation was somewhat exacerbated by the fact that the law firm where Mr Townsend was employed acted as solicitors for Mr Irving in this matter.

Important comments made by the court:

As the administrator of the company, Mr Irving would have had to investigate the affairs of the company and also the conduct of the directors, including that of Mr Townsend, to determine whether or not any action should be taken against them or any of them. His relationship with Mr Townsend created the perception that Mr Irving held Mr Townsend's judgment in high regard and relied on his professional advice and judgment. In the court's view a reasonable person would have trouble believing that (despite Mr Irving's assertions to the contrary) he would be able to conduct said investigation without any bias.

The court noted that although nobody had made any allegations against the propriety of Mr Irving's conduct, the mere fact that he had a longstanding friendly and professional relationship with Mr Townsend would create doubt with a fair-minded person that he would be able to perform his duties in an independent manner and therefore it would not be appropriate for Mr Irving to continue as the administrator of the company. There must not be any bias and there must not be any appearance or perception of bias. This relationship created a familiarity threat for the CIP.[70]

The involvement of Mr Irving as an advisor in the pre-commencement business of the company was also mentioned. It is fairly common place for companies and their management to meet with advisors who are ultimately appointed in an official capacity as CIPs. The court mentioned that not all prior involvement would lead to a lack of independence but that in this case it was capable of giving rise to questions of a possible lack of independence. Substantial involvement with a company prior to its administration will disqualify a person from appointment as that company's administrator. Such involvement will be seen to detract from the ability of the person to act fairly and impartially during the course of an administration. Substantial involvement prior to commencement of the proceedings could create both advocacy[71] and self-review[72] threats for the CIP.

Comments:

Mention was also made of Mr Irving's disclosure of the relationship, yet it did not influence the outcome of the proceedings. This is indicative of the belief that declaring an interest does not remedy the situation.

Ventra Investments Ltd v Bank of Scotland Plc [2019] EWHC 2058 (Comm) [ENGLAND AND WALES]

This case brought renewed scrutiny to the practice of accountancy firms that enter into relationships with lenders as part of the lender's "insolvency panel".

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70 A situation in which a Member's relationship to a stakeholder impairs (or is perceived to impair) such Member's impartiality and objectivity owing to the Member being too sympathetic or antagonistic to the interests of others. See the glossary of terms in **Appendix B** for a description.

71 A situation in which a Member promotes a position or opinion to the point that subsequent objectivity may be compromised (eg, the Member has acted on behalf of a significant creditor to advance such creditor's position). In such a case, it is unlikely that other creditors would consider the Member to be impartial.

72 A situation in which actions taken by a Member, such Member's firm, a close associate, or a close associate's firm is (or is perceived to be) subject to review only by such Member (eg, where a Member's firm carried out the disposal of certain assets of the insolvent estate prior to insolvency, and there are suspicions that the disposal is in some way improper).

The case is complex in as far as facts and legal issues are concerned and consequently this case study will focus only on the facts and legal issues relevant to the CIPs' duties of independence and impartiality.[73]

The relationship giving rise to an issue in this case was based on Ventra Investments' Administrative Receivers' firm (BDO) being on the Lloyds "insolvency panel", which is essentially a preferred status enjoyed by certain firms that then win regular work from the bank. This became a troublesome issue when a subsidiary of Lloyds, the Bank of Scotland, became embroiled in a legal battle with the debtor company, Ventra Investments, in a case concerning among other things certain transactions made at an undervalue.

According to the liquidators of Ventra Investments, there were issues relating to the independence and impartiality of the administrative receivers taking an appointment when they were so closely linked to one of the stakeholders. The liquidators also claimed that the administrative receivers were "effectively under the control" of the bank and therefore unduly favoured the lender. They believed the relationship influenced the administrative receivers to exhibit a reluctance to take legal action against the bank.

An unwillingness legally to challenge wrongdoing by a creditor is an obstacle to performing their duties as CIPs in the best interest of the creditors as a whole. Although the administrative receivers' firm denied that their relationship with the bank would cause a lack of independence and impartiality, the perception created by this relationship (and some facts) could lead to an informed observer forming the opinion that the CIPs might not be objective in the performance of their duties.

Comments:

Great care should be taken to assess appointment opportunities in order to avoid taking an appointment where an actual or perceived conflict of interest might arise.

Self-Assessment Exercise 2

In order to learn more about your own jurisdiction's requirements in relation to independence and impartiality and to educate yourself as to what is expected of you in this regard, investigate whether your own jurisdiction provides for this duty or, alternatively, what any regulatory or recognised professional body in your jurisdiction advises in this regard. Be specifically on the lookout for provisions in relation to prohibited or worrying relationships and the test for compliance.

For commentary and feedback on self-assessment exercise 2, please see APPENDIX A

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[73] You can investigate the finer details of this case and read some interesting media reports by visiting: https://www.casemine.com/judgement/uk/5d43fad72c94e04a9677bf66; https://www.bmmagazine.co.uk/news/lloyds-banking-group-ordered-to-explain-relationship-with-insolvency-firms/; https://www.thetimes.co.uk/article/lloyds-banking-group-under-scrutiny-for-insolvency-ties-67q0nxrb2?wgu=270525_73669_1597751206018_d2f08448a2&wgexpiry=1605527205&utm_source=planit&utm_medium=affiliate&utm_content=30828.

5.4 Professional / technical competence

Principle 3 – Professional / Technical Competence
Professional / Technical Competence Members and their firms should maintain an acceptable level of professional competency. This may be achieved by: • keeping current with legislative / regulatory changes; • undertaking continuing professional education; and • undertaking sufficient case work to remain experienced
Commentary Members and their firms should be sufficiently and appropriately experienced and resourced to deal with the engagements and cases they accept or can call upon specialists or further resources as required. Accepting cases where a Member cannot give them the level of attention or technical expertise required to deliver the best result for stakeholders may bring such Member and the profession into disrepute. Even where there may not be continuing education or qualification requirements, Members should endeavour to maintain a high level of competency in their field in order to deliver the services they are engaged to perform and in accordance with any statutory duties.

IPs are often regarded as experts in turnaround, restructuring and liquidation. As such, members of the public and more specifically stakeholders in an insolvency expect that IPs have the requisite experience and technical competence to perform the duties associated with their appointments. This expectation is further emphasised by the fact that IPs are remunerated as skilled professionals.

This ethical principle is one that requires an exceptional level of self-realisation and introspection by the IP. It is important that professionals know the limitations of their own knowledge, skills and experience (and diaries). As such, when an area of deficiency is identified it is of paramount importance that the IP, as fiduciary, ensures that he educates himself in order to enable him to act in the best interest of his beneficiaries. The principle of professional and technical competence and the duty of care placed on the IP require that an IP should only accept insolvency appointments when the IP has or can acquire sufficient expertise. Moreover, IPs should not accept appointments when they are already under a heavy case load and would not be able to provide the level of attention required by the appointment.

It is also trite that the Law is dynamic and often changes to accommodate changes in practice, politics, culture and the environment. IPs should endeavour to keep abreast of changes to the law or practice in their field. Many jurisdictions provide

opportunities for continued professional development and arrange short courses and conferences for IPs to brush up on the latest developments.[74]

This ethical principle is also closely related to the duty of care, skill and diligence. When a company is in financial distress, it is extremely important that the person who is appointed as CIP does not act recklessly with regard to the affairs and property of the company. It is possible that the objectives of the insolvency proceedings (to protect the interests of stakeholders) can be frustrated through the incompetence and carelessness of the practitioner. It is clear from these statements that a practitioner who undertakes too many case appointments, or one who fails to meticulously perform his duties, might be in breach of the duty to act with care, skill and diligence and may be held personally liable for any loss due to his actions or omissions.

In this regard it could be useful to utilise the recognised two-fold test in relation to the duty of care skill and diligence.[75] The CIP's conduct should be measured against that of a reasonable CIP.[76] This implies that it should be established whether he acted with the same degree of care, skill and diligence that may reasonably be expected of a reasonable practitioner in the same circumstances, having regard also to his personal attributes and qualifications.

A CIP can, however, be regarded as an expert in insolvency practice as a result of his experience and training and hence an even higher standard is to be met with regard to the subjective test. As an expert, a CIP should to a certain extent be able to be subjected to the test of a reasonable expert.[77] Due to the fact that CIPs will have varying degrees of experience and training, the subjective elements of the test are important and ought to be applied on a case-by-case basis in order to determine whether there was any breach in duty.

This approach seems to be aligned with the guidance provided by UNCITRAL:[78]

> "One approach may be to require the insolvency representative to observe a standard no more stringent than would be expected to apply to the debtor in undertaking its normal business activities in a state of solvency, that of a prudent person in that position. Some States, however, may require a higher standard of prudence in such a case because the insolvency representative is not dealing with its own assets, but with assets belonging to another person."

A professionally competent CIP will act with the necessary care, should obtain an adequate degree of understanding of the nature of the company's business in order

[74] For information regarding educational course offered by INSOL International, see www.insol.org/education. For information regarding the technical content of conferences, seminar and webinars presented by INSOL International, see www.insol.org/events.

[75] An objective test is to be applied in order to determine what the reasonable person would have done in the same situation, as well as a subjective test that takes into account the general knowledge, skill and experience of that specific person.

[76] *Re Charnley Davies Ltd* 1990 BCC 605 at 618 – "An administrator must be a professional insolvency practitioner. A complaint that he has failed to take reasonable care in the sale of the company's assets is, therefore, a complaint of professional negligence and in my judgment the established principles applicable to cases of professional negligence are equally applicable in such a case. It follows that the administrator is to be judged, not by the standards of the most meticulous and conscientious member of his profession but by those of an ordinary, skilled practitioner. In order to succeed the claimant must establish that the administrator has made an error which a reasonably skilled and careful insolvency practitioner would not have made."

[77] R Bradstreet, "The leak in the Chapter 6 lifeboat: Inadequate regulation of Business Rescue Practitioners may adversely affect lenders' willingness and growth of the economy" [2010] 22 SAMLJ 195 at 209.

[78] UNCITRAL Guide, p 184, para 61.

to understand how the business functions and exactly what is expected of him/her.[79] The CIP should also acquire knowledge of the industry in which the company operates.

Self-Assessment Exercise 3

Julie is a well-known insolvency practitioner and is often sought out for her knowledge and expertise, especially in relation to retail insolvency. She currently has 10 ongoing insolvency matters (most of them quite complex) relating to retail insolvency and has almost exclusively only dealt with retail insolvencies for the last 5 years.

Due to her impressive *curriculum vitae*, she is contacted by a very large mining company in distress inquiring whether she would be able to take the appointment as an administrator. Julie does not feel like she has the level of expertise to accept this appointment.

Question 1

What would you advise Julie to do in these circumstances?

Question 2

If Julie was to accept the appointment and something went wrong, could she be held liable for a breach of her duty of care?

For commentary and feedback on self-assessment exercise 3, please see APPENDIX A

5.5 Professional behaviour

Principle 4 – Professional Behaviour

Professional Behaviour

Communication with stakeholders should be used to inform and educate them on the progress of a case. Members should strive to be accurate, honest, clear, succinct and timely.

[79] R Mokal and J Armour, "The new UK Corporate Rescue Procedure – The Administrator's Duty to Act Rationally" [2004] 1 *International Corporate Rescue* 1, 6 – "So for example, not to take into account reasonably discoverable factors relevant to determining whether the continuation of the company as a going concern (by preserving for its benefit the specific skills and knowledge of the local market of its pre-distress shareholder-managers, say) would result in better expected returns for its creditors than if the company's business were to be sold off to another company (with little knowledge of and enjoying no goodwill in market), would be to ignore considerations relevant to serving the creditors' interests, and would thus constitute a breach of duty."

It is in the best interests of all parties for Members to co-operate and communicate in a professional manner with other Members and adjudicating bodies. Nonetheless, a Member's duty is to the estate.

When promoting themselves, or their firm, or when competing for work, Members should act with integrity and should avoid bringing the profession into disrepute.

Commentary

It is important to provide information about the progress of, and potential recoveries in, the proceedings to those parties with any tangible interest in such proceedings (including but not limited to creditors and shareholders). This does not mean that Members can or should be expected to respond to every query raised. Disseminating information should be balanced with maintaining commercial and other confidentiality obligations, and Members should consider the cost of preparing the response against the benefit of such response.

In a high-profile case, many persons without a tangible interest in the case might demand information. Members should weigh the advantages of providing the information against the associated cost and disruption to the company or estate. Decisions should be made in the best interests of the estate and its stakeholders. Duties should be carried out in a timely fashion, respecting legislative time limits. Members should strive to complete cases efficiently, without undue delay.

Although Members are naturally in competition for engagements, Members have a common interest in upholding standards for the insolvency profession. Members should not allow their personal relationships with other Members (or the hope of obtaining work) to unduly influence or adversely affect their dealings with the estate. In particular, where different Members are appointed over different estates or divisions of a company group, a Member should act in the interests of their allotted portion of the estate and its stakeholders, which should prevail over the interests of the collective group in the event of a conflict. For example, agreeing to a collective settlement that would leave the individual estate to which a Member is appointed in a worse position than could be obtained by another course of action would be contrary to such duty.

As part of a profession that is often the subject of public scrutiny, it is important that an IP always conducts himself in a manner that reflects the standards and customs associated with the profession.

Due to the nature of insolvency proceedings and the impact on the immediate community and society, IPs are often asked to comment on ongoing procedures whether informally by colleagues, friends and family or formally by media outlets. In this regard IPs should take care not to divulge any confidential information. Confidentiality forms part of the fiduciary duty to act in good faith. The IP will acquire a vast amount of sensitive information, sometimes even before being formally appointed. Client lists, trade secrets, confidential business discussions and internal financial statements constitute examples of information and sources of information that will be disclosed to the IP. The fact that corporate information can in modern times be regarded as one of a company's most valuable commodities, makes confidentiality a significant obligation of the restructuring CIP in the context of a

struggling company.[80] The IP must, therefore, be careful not to disclose (even inadvertently) any confidential information to third parties. An IP may also not use any information gleaned from his position as fiduciary to facilitate a personal benefit or benefit for a person related to the CIP and should be careful not to be guilty of insider trading or using information to compete with the company. It is also essential that the IP refrains from divulging sensitive information lest it damages the goodwill and reputation of the company. Clearly, therefore, the IP's duty to good faith has a significant impact on the success of the insolvency proceedings.

The principle of confidentiality therefore imposes an obligation on IPs to refrain from:

- disclosing confidential information acquired as a result of professional and business relationships without proper and specific authority, unless there is a legal or professional right or duty to disclose;

- making improper use of confidential information acquired as a result of professional and business relationships to their personal advantage or the advantage of third parties; and

- publishing or divulging without just cause to any person any confidential information or details concerning the business, affairs, trade secrets, patents, technical methods or processes of any estate in respect of which they hold an appointment.

An IP must maintain confidentiality, including in a social environment, being alert to the possibility of inadvertent disclosure, particularly to a close business associate or a close or immediate family member.

Another important aspect of the IP's duties to the beneficiaries is to communicate with the stakeholders in a timely fashion and, as stated earlier, this should be done in an honest and truthful matter. The stakeholders in the insolvency proceedings will have varying degrees of knowledge and understanding of how the procedure works.[81] This sometimes leads to conflicts between parties as not everyone has the same clear understanding of what the process involves. The IP, as fiduciary, should make use of the opportunities presented to him to not only inform the stakeholders of relevant issues but also to educate them. As such, transparency forms an integral part during the IP's appointment. Transparency and fiduciary duties are inextricably linked. As fiduciaries, IPs have a duty to account.[82]

Dickfos reflects on the fact that the type of information and comprehensiveness thereof is extremely important. She notes that often "too much" information is provided for the average unsecured creditor; she further questions whether the information provided is meaningful and able to be understood and states that stakeholders tend not to read documents that are too lengthy.[83] Communication with the stakeholders provides an excellent opportunity to manage their expectations.

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[80] J Shepherd, *The Law of Fiduciaries* (Carswell 1981) 326-327 – "Like other intellectual property, information must be treated as property because it exhibits so many of the characteristics of property. Money is spent to acquire it, and both the possessors and those who want it consider it very valuable. Like other assets, information is bought, sold, and protected in many of the same ways."

[81] J Dickfos, "The Costs and Benefits of Regulating the Market for Corporate Insolvency Practitioner Remuneration" (2016) 25 *Int Insolv Rev*, 56. Dickfos refers to the lack of practical knowledge, experience and judgement of stakeholders that contribute to "information asymmetry".

[82] *Kao Chai-Chau Linda v Fong Wai Lyn Carolyn* [2015] SGHC 260, [2016] 1 SLR 21, 31 [24] [Singapore]; *Mirror Group Newspapers plc v Maxwell (No 2)* [1998] I BCLC 638, 648 [England].

[83] J Dickfos, "The Costs and Benefits of Regulating the Market for Corporate Insolvency Practitioner Remuneration", (2016) 25 *Int Insolv Rev*, 61.

They have unrealistic views[84] as to what the IP will do and what the outcomes of the procedure will be. If these expectations are not met by the IP, stakeholders might feel that the he “failed” and did not do his job properly. The IP should make use of the opportunity to educate stakeholders as to his role and the tasks to be performed in order to minimise any possible disputes. This would, however, only be feasible if the stakeholders have trust and confidence in the IP.

Self-Assessment Exercise 4

Question 1

Jason, as the administrator of a large construction company with several government contracts, has been asked to give a television interview on the progress of the proceedings. What are the factors that Jason should consider when deciding to grant the interview?

Question 2

It is only risky to provide media interviews and not when you are having a social gathering with family and friends. True or false?

For commentary and feedback on self-assessment exercise 4, please see APPENDIX A

5.6 Remuneration and disbursements

Principle 5 – Remuneration

Remuneration

Members are entitled to remuneration for their work (necessary or beneficial, and properly performed). Members should maintain and provide sufficient information to the body approving such remuneration (where applicable) in order to allow an informed decision on whether the remuneration is reasonable. Remuneration should only be drawn in accordance with the approval obtained (if applicable).

Commentary

Remuneration is a very sensitive subject. Where applicable law does not provide procedures or standards for remuneration, it is important to carefully consider the manner in which Members request and provide justification for remuneration (or pay themselves where no approvals are required by law or professional guidance). Acceptable methods of calculating remuneration may include but are not limited to:

[84] *Ibid*.

- Fixed fee;
- Percentage of the value of the assets realised and / or the value of distributions made;
- Hourly, or otherwise based on the time properly spent on attending to the case;
- Contingent fee arrangement; and
- Combination of the above methods.

The terms of any contingent fee arrangement (including remuneration based on realised value) should be transparent, objectively measurable, and if applicable agreed or approved by the proper authority or stakeholders.

Members should be able to justify the work performed, for example, by demonstrating that it is required by law (for example, certain jurisdictions may require reports to regulators, which do not benefit stakeholders, but which serve a public interest), or that such work is reasonable in light of the:

- complexity of the case;
- degree of responsibility falling upon Members;
- effectiveness of Members in carrying out their duties;
- value and nature of the estate assets and liabilities; and
- benefit therefrom accruing to the estate.

It is helpful to distinguish between disbursements, remuneration, and third-party costs billed to the estate.

Disbursements which are a direct recovery of costs paid by Members or their firms to a third party (e.g., travel costs) should be disclosed.

Disbursements that may arise from a recharge or allocation of costs incurred by Members or their firms and contain a profit element (e.g., a charge for use of a meeting room to hold a statutory meeting) should be approved, where applicable, in the same way as remuneration.

Third party costs are not considered remuneration or disbursements and, accordingly, should be disclosed separately in accordance with local law and regulation.

5.6.1 Remuneration

One of the biggest culprits in reducing the public's confidence and trust in the insolvency profession, is the issue of remuneration.[85] This is exacerbated by the media and others placing an emphasis on seemingly excessive remuneration claims by CIPs. For example, shortly after the collapse of the English construction giant Carillion, the right honourable Frank Field MP, the chair of the UK House of Commons' Work and Pensions Committee, commented on the GBP 44.2 million to be paid in fees to PwC in relation to one year's Insolvency work on Carillion as "milking the cash cow".[86]

Despite the controversies often related to remuneration, it remains a crucial part of any insolvency regime. CIPs are entitled to receive reasonable remuneration that is commensurate with their qualifications, experience, and the risks involved in the particular case. Due to the fact that the duties of IPs are sometimes daunting and their appointment involves a great degree of risk, it is important that a balance is struck between risk and reward in order to attract appropriately qualified professionals to perform these tasks.[87]

The various methods for calculating remuneration are dealt with below.

5.6.1.1 Fixed fees

As the name suggests, this fee is based on an amount that has been fixed by legislation or the profession. The UNCITRAL Legislative Guide mentions that CIP remuneration may be fixed, but it does not elaborate or provide further guidance on how this could be incorporated into the laws of a specific jurisdiction.[88] In most jurisdictions that allow for a fixed fee to be charged it can be, or is, used in combination with other methods of calculation.

An issue with a fixed fee element awarded to an IP in relation to work carried out in the performance of his duties, is that it might not be representative of the value of the work done. It is possible for an IP to receive remuneration based on this method of calculation, but it may be that the IP invested more time and resources to complete the work than is reflected in the fee and therefore his remuneration is not commensurate with his efforts and the work performed. On the other hand, an IP might have to do very little work in a particular case and would be be paid the same amount.

A fixed fee cannot be said to represent a fair method of calculating remuneration, unless the remuneration framework allows for the adjustment of the fee in cases where it proves necessary.

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[85] D Brown and C Symes, "Submission to Senate Inquiry into Liquidators and Administrators" [2009] 1-7; J Dickfos, "The Costs and Benefits of Regulating the Market for Corporate Insolvency Practitioner Remuneration" (2016) 25 *Int Insolv Rev* 56,57. Even in 1998, when the seminal remuneration case of *Mirror Group Newspapers plc v Maxwell (No 2)* [1998] I BCLC 638 [England] was decided, Ferris J noted that "[i]n recent years there has been a good deal of concern as the result of a fairly general perception that costs in insolvency cases have reached an unacceptably high level."

[86] The Times, 7 February 2019. Referring to the insolvency practitioners' fees, he commented: "In this they are ably assisted by a merry little bank of advisors and auditors, conflicted at every turn and with every incentive to milk the cash cow dry." There are many more examples of global headlines casting CIPs in a very dim light, eg, "Rangers liquidators rack up £5m fees as creditors offered 3p in the pound" – Daily Record, 27 January 2020 – https://www.dailyrecord.co.uk/news/scottish-news/rangers-liquidators-rack-up-5m-21366070.

[87] UNCITRAL Guide, p 181, para 53.

[88] *Ibid* – "It may be fixed by reference to an approved scale of fees set by a government agency or professional association".

5.6.1.2 Percentage-based fees

Percentage-based remuneration can be based on either a percentage of realisations of assets or on a percentage of distributions to creditors.

The strongest criticism against a percentage-based approach relates to proportionality. The UNCITRAL Guide states that IPs often find this to be an uncertain method to calculate remuneration, as the amount of work involved in the administration will not necessarily be in proportion to the value of the distributable assets.[89] This again means that the possibility exists that the IP would do more work than what he will be remunerated for. However, this method of fee calculation does provide some incentive for IPs to ensure that assets will be sold for the highest possible price – the higher the price assets are sold for, the higher the fee. It also provides creditors with some form of certainty as to the fee that will be claimed by the IP, which makes the calculation of risk a lot easier.

5.6.1.3 Time-based fees

Perhaps one of the most contentious ethical issues in relation to the remuneration of IPs is the profession's partiality for charging on the basis of time. Despite the contentiousness of the issue it remains the preferred method for calculating the remuneration of IPs in many jurisdictions, as it is believed to provide for a fair compensation for work done.[90]

It is accepted that IPs making use of this calculation method are to be remunerated only for "time properly spent on attending to the case".[91]

The rate of calculation on which the remuneration is to be based could be the IP's own hourly or daily rate, or a rate prescribed by legislation or the profession to which the IP belongs.

The UNCITRAL Guide submits that this system might operate to incentivise time spent on the administration without necessarily achieving any outcome.[92] Moreover, that it is also possible that this method of calculating remuneration might not be reflective of actual work done by the IP.[93]

Time-based fees were considered in the seminal case of *Mirror Group Newspapers plc v Maxwell*,[94] where Ferris J stated three important principles in relation to time-based costing. He stated that:

(a) time spent represents the cost of rendering services, not the value of the service rendered;

(b) time spent should be only one of a number of relevant factors to assess value; and

(c) it follows from the first two that the real task is to assess value and not cost.[95]

89 *Idem*, p 181, para 55.
90 *Idem*, p 181, para 54.
91 INSOL Principles, Principle 5, p 7.
92 UNCITRAL Guide, p 181, para 54.
93 This implies that a practitioner might be getting more or less than what he deserves in terms of performance.
94 *Mirror Group Newspapers plc v Maxwell (No 2)* [1998] I BCLC 638 [England].
95 *Idem*, at 652.

However, it will only be possible to make an assessment regarding the value of the services *ex post facto*. The case also addressed the issue of time-based costing not being reflective of work that was performed.[96] This is especially true of prescribed fees. It is quite possible for an IP to do more work than what the prescribed hourly / daily rate allows; equally so, it might be the case that an IP is remunerated for more than the actual work performed. IPs often criticise the amount prescribed for hourly rates as they believe it does not clearly represent the full account of the costs of running an insolvency procedure.

5.6.1.4 Contingency fees

Contingency fee arrangements have long been a bone of contention in the insolvency world. These arrangements are also known as "success fees" or in some jurisdictions as "conditional fees". As the name suggests, these are fee arrangements which determine that the IP would be entitled to receive remuneration based on a specific outcome or condition being met. The outcome or condition usually pertains to a favourable outcome for stakeholders, for example the successful implementation of a rescue plan. One reason for the controversy surrounding contingency fee arrangements is that the conditions and outcomes on which the fee is payable are arguably conditions and outcomes that IPs, as fiduciaries, should aspire to anyway and would therefore form part of their remit. Another issue can be found in the diverting of an IP's focus to a singular task that will benefit his fee arrangement, instead of allowing his approach to be holistic. There would not be an ethical issue in the event of a contingency fee being paid for the achievement of a truly remarkable outcome and these outcomes should always be objectively measurable. It should not merely be an achievement in the eyes of the IP.

5.6.1.5 Combination fees

Many jurisdictions allow for a combination of the abovementioned methods to be utilised in the determination of the quantum of IP remuneration.[97] Each of the methods have advantages and disadvantages. Allowing for a combination of methods provides the opportunity to utilise the best of each whilst the drawbacks, in as far as ethical behaviour is concerned, can be avoided. In most jurisdictions the decision regarding how the fee is constituted rests with the IP. In some cases it might be predetermined.[98]

It is imperative that the IP is able to justify his remuneration and that the remuneration that he claims is fair, reasonable and proportionate in the circumstances. In order to determine whether the remuneration is reasonable, the following factors are usually considered: the complexity of the case; whether any aspects of the case creates any responsibility of an exceptional kind or degree for the officeholder; the effectiveness with which the officeholder carried out the duties of the office; and the value and nature of the property with which the officeholder had to deal.[99]

In order to place the IP in the best possible position to justify his remuneration, the IP must be able to account. As fiduciaries, IPs have a duty to account.[100] Transparency is a key component to ethical behaviour by the CIP. Moreover, transparency and

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96 *Ibid*.
97 Australia, England and Wales and Russia, by way of example.
98 In Russia, eg, the combination is predetermined.
99 Variations of these factors can be found in several jurisdictions.
100 *Kao Chai-Chau Linda v Fong Wai Lyn Carolyn* [2015] SGHC 260, [2016] 1 SLR 21, 31 [24] [Singapore]; *Mirror Group Newspapers plc v Maxwell (No 2)* [1998] I BCLC 638, 648 [England].

fiduciary duties are inextricably linked. In the case of *Mirror Group Newspapers plc v Maxwell*,[101] Ferris J emphasised the fiduciary nature of the CIP's office and related this effectively to remuneration and the duty to account. Ferris J stated that, as fiduciaries, IPs have a duty to protect, get in, realise and pass on to others assets and property that do not belong to themselves but to their beneficiaries.[102] What an IP retains for himself out of the property which he controls as an officeholder will no longer be available for those towards whom he is a fiduciary.[103] Because an IP is not expected to act gratuitously, he cannot account for the retention by paying it over. The only way in which to account for it is by showing that he ought to be allowed to retain it. This duty to account brings about an obligation to justify expenses incurred, including an obligation to justify and explain the remuneration claimed in exercising the duties of the office.[104]

It is important that an IP be transparent regarding his fees and the cost of proceedings from the outset. The level of detail required should be proportionate to the complexity of the appointment.[105] Understanding the steps to be taken in a case with a complex set of facts or legal issues, would necessarily require a more detailed explanation in order to place parties in the best position to appreciate what steps are required.

5.6.2 Disbursements and expenses

5.6.2.1 Generally

Both the UNCITRAL Guide and the INSOL Principles elaborate on the fact that an IP will invariably come across the need to incur certain expenses during the course of the administration of the estate (administrative costs).[106]

Although the remuneration claimed by IPs tends to be a contentious issue, the disbursements and expenses can also have a significant impact on the value of the estate. It would, therefore, be fair to say that in light of the fiduciary nature of his position the IP has a duty to minimise the extent of the impact of these administrative costs. Moreover, incurring these expenses is dependent upon the IP's commercial judgement, reasonably exercised.

The need for record keeping[107] and the duty to account[108] prevail in the case of administrative costs and the IP's transparency should continue when disclosing payment of these costs.

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[101] *Mirror Group Newspapers plc v Maxwell (No 2)* [1998] I BCLC 638 [England].
[102] *Idem*, at 648.
[103] *Ibid*.
[104] *Mirror Group Newspapers plc v Maxwell (No 2)* [1998] I BCLC 638, 648 [England]; *Re Peregrine Investments Holdings Ltd* [1998] 3 HKC 1 [Hong Kong]; *Kao Chai-Chau Linda v Fong Wai Lyn Carolyn* [2015] SGHC 260, [2016] 1 SLR 21, 31 [24] [Singapore]; S Steele, M Wee and I Ramsay, "Remunerating Corporate Insolvency Practitioners in the United Kingdom, Australia and Singapore: The Roles of Courts" (2018) 13 *AsJCL* 141,147.
[105] *Kao Chai-Chau Linda v Fong Wai Lyn Carolyn* [2015] SGHC 260, [2016] 1 SLR 21, 32 [27] [Singapore].
[106] UNCITRAL Guide, p 4, a. "…claims that include costs and expenses of the proceedings, such as remuneration of the insolvency representative and any professionals employed by the insolvency representative, expenses for the continued operation of the debtor, debts arising from the exercise of the insolvency representative's functions and powers, costs arising from continuing contractual and legal obligations and costs of proceedings".
[107] *Mirror Group Newspapers plc v Maxwell (No 2)* [1998] I BCLC 638, 649 [England]; INSOL Principles, p 8 – "It is in Members' (and their agents and service providers) interests to implement policies, procedures and systems to ensure reasonable and proper: record-keeping…"
[108] *Mirror Group Newspapers plc v Maxwell (No 2)* [1998] I BCLC 638, 648 [England].

The INSOL Principles defines disbursements and third-party costs as follows:

> "Disbursements – Sums paid by a Member or its firm to third parties or a recharge or allocation of costs incurred by Members or their firms which is charged to the estate."[109]

Disbursements thus referring to monies paid by the IP for expenses incurred by the IP as part of the discharge of his duties. This serves to reimburse the IP. Costs pertaining to travel are an example of this.

Third-party costs are defined by the INSOL Principles as follows:[110]

> "Third-party costs – Sums paid directly from the estate to a third-party supplier. The third-party supplier invoices the estate."

Third-party costs therefore consist of payments made to parties who rendered services to the estate and which were not paid by the IP or his firm. Utility bills and costs pertaining to continued trade are examples of this.

5.6.2.2 Disbursements

As part of the IP's duty to account, he should be able to justify payments to third parties and should take responsibility for subjecting the bills of third parties to scrutiny.[111]

The difficulty in quantifying disbursements made to professionals (other than legal professionals) was highlighted in *Mirror Group Newspapers plc v Maxwell*,[112] where the court was confronted with an unusual expense paid to a firm of public relations consultants. The court stated that it did not have the kind of information it needed in order to form a judgement on the matter and identified the consequential need for a proper explanation by the officeholders.[113] In such cases, where insufficient information regarding somewhat obscure disbursements has been given, practitioners should expect the disbursement to be subjected to careful scrutiny.[114] As part of his fiduciary duty to account, an IP should still be able to provide transparent and full disclosure as to the nature and need of the expenses incurred.

In Singapore, Rajah J stated that "some measure of restraint and discipline"[115] is needed in recouping disbursements. The court touched on the seemingly innocuous disbursement of photocopying charges, which could be very substantial in major matters. The court confirmed the principle laid out in *Mirror Group Newspapers plc v Maxwell,*[116] by stating that an IP would still need to provide sufficient particulars in order to establish whether these expenses were reasonably necessary.[117]

In Australia, Finkelstein J stated that a practitioner should act with the same care as a prudent businessman would act in his own affairs when dealing with disbursements.[118] He mentions that a prudent businessman will only litigate as a last

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[109] INSOL Principles, p 9.
[110] *Idem*, p.10.
[111] *Mirror Group Newspapers plc v Maxwell (No 2)* [1998] I BCLC 638, 639 [England].
[112] *Idem*, at 662.
[113] *Ibid*.
[114] *Ibid*.
[115] *Re Econ Corp Ltd (No 2)* [2004] SGHC 49, 264, 286 [59] [Singapore].
[116] *Mirror Group Newspapers plc v Maxwell (No 2)* [1998] I BCLC 638 [England].
[117] *Re Econ Corp Ltd (No 2)* [2004] SGHC 49, 264, 287 [59] [Singapore].
[118] *Re Korda; in the matter of Stockford Ltd* (2004) 140 FCR 424, 443 [51] [Australia].

resort and, if it is unavoidable, will keep it under close scrutiny. A prudent businessman will shop around to ensure the best legal advice at the best rates by negotiating for the best fees and monitoring the fees incurred.[119] "Personal relationships should not obscure the practitioner's duty. The sole selection criteria should be the benefit to him as litigant. So he will avoid cosy relationships with solicitors and counsel."[120] Here an important ethical issue regarding the use of service providers comes to the fore. The nature of their professional work might lead to familiarity issues being created between IPs and certain service providers. The familiarity issues give rise to a lack of independence, creating a conflict of interest. This is to be avoided in order to enhance the trust and confidence in the IP and the insolvency regime.

In the Singaporean *Kao* case, the court identified two further issues in relation to disbursements:

(a) allegations of over-servicing, referring to all instances in which unnecessary work was performed; and

(b) allegations that work was duplicative, particularly where other professionals (such as lawyers) were engaged.[121]

Both of these issues to some extent relate back to the duty of the practitioner to act with care. A careful IP would make sure that no unnecessary tasks are performed and would be careful to not do work that has already been done, or allow service providers to charge for work already performed.

As fiduciaries, IPs do not have an automatic right to recover all expenses (not even if they were incurred in good faith) unless the expenses were reasonably incurred in the discharge of their stewardship.[122]

5.6.2.3 Third-party costs

Third-party costs are paid directly from the debtor's estate and therefore also have an effect on beneficiaries' interests by diminishing the estate. These administrative expenses, although paid directly from the estate of the debtor, are still executed by the IP or under his supervision.

These expenses might relate to the payment of utilities or suppliers in the case of continued trade.

5.6.2.4 Legal professionals

One of the most contentious administrative costs is those paid to legal professionals. This is due to the fact that multiple sets of professionals (IPs and legal professionals) translate to multiple sets of professional fees and disbursements.

It is possible that the services of legal professionals (lawyers and counsel) can be paid as disbursements or third-party costs. This was carefully illustrated in the Singaporean *Kao* case by Chong J.[123] The court explained that the costs of legal

[119] *Ibid*.
[120] *Re Korda; in the matter of Stockford Ltd* (2004) 140 FCR 424, 443 [51] [Australia]; *Kao Chai-Chau Linda v Fong Wai Lyn Carolyn* [2015] SGHC 260, [2016] 1 SLR 21, 44 [58] [Singapore].
[121] *Kao Chai-Chau Linda v Fong Wai Lyn Carolyn* [2015] SGHC 260, [2016] 1 SLR 21, 23 [Singapore].
[122] *Idem*, at 35 [32].
[123] *Idem*, at 44.

professionals can be claimed i) as part of the IP's disbursements,[124] or ii) the costs can be billed separately and directly to the debtor company.[125]

When the costs are claimed as disbursements, the onus is on the IP, as the party responsible for the payment, to consider whether the bill is reasonable and appropriate given the circumstances.[126] This reasoning is reminiscent of that expressed in Australia by Finkelstein J in *Korda,*[127] where it was stated that the IP should exercise his commercial judgement when hiring legal professionals and that a prudent IP would monitor the fees claimed by these professionals.[128]

When the costs of legal professionals are not claimed as disbursements but billed to the company, the issues relating to the monitoring of the fees and scrutiny of the bill prevail. A new issue in relation to this type of administrative costs is the one of duplication of work done by the legal professional.[129] In such a situation the burden rests on the CIP to justify claims for work performed when there are other professionals instructed on the same matter.[130] In the *Dovechem*[131] case, the court was confronted with a complaint by the majority shareholders of the company that the liquidators had charged four times more than the solicitors that were instructed to institute action on behalf of the company. At first glance it would appear that the liquidators in the case had duplicated the work done by the legal professionals, but the liquidators successfully proved that the work done by them in relation to the case was very different from that of the solicitors.[132]

In certain jurisdictions, such as South Africa and England and Wales, the CIP appointed to perform a rescue or turnaround of a debtor might not be trained in law or have specialised legal knowledge and as such would at times have to rely on expert advice at a certain cost. That is why it is sensible to include guidance on engaging legal professionals in codes of conduct.

The new Insolvency Code of Ethics by the Institute for Chartered Accountants of England and Wales (ICAEW) addresses this issue with remarkable clarity and sensible advice.[133] In a section dealing with the specialist advice and services, the ICAEW Code requires that when an IP intends to rely on the advice or work of a third party the IP should evaluate whether such advice or work is warranted.[134] The Code

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[124] *Kao Chai-Chau Linda v Fong Wai Lyn Carolyn* [2015] SGHC 260, [2016] 1 SLR 21, 44 [57] [Singapore]. As was the case in *Mirror Group Newspapers plc v Maxwell (No 2)* [1998] I BCLC 638, 660 [England] – Ferris J stated that where the solicitors were engaged in providing legal services in connection with the CIP's appointment there is a contract between the parties and CIPs will be personally bound to pay solicitors for work done in accordance with that contract.

[125] *Kao Chai-Chau Linda v Fong Wai Lyn Carolyn* [2015] SGHC 260, [2016] 1 SLR 21, 44 [59] [Singapore].

[126] *Idem*, 44 [57].

[127] *Re Korda; in the matter of Stockford Ltd* (2004) 140 FCR 424, 443 [51] [Australia].

[128] *Re Korda; in the matter of Stockford Ltd* (2004) 140 FCR 424, 443 [51] [Australia]; *Kao Chai-Chau Linda v Fong Wai Lyn Carolyn* [2015] SGHC 260, [2016] 1 SLR 21, 44 [57] [Singapore].

[129] *Kao Chai-Chau Linda v Fong Wai Lyn Carolyn* [2015] SGHC 260, [2016] 1 SLR 21, 44 [59] [Singapore].

[130] *Ibid*.

[131] *Liquidators of Dovechem Holdings Pte Ltd v Dovechem Holdings Pte Ltd* [2015] 4 SLR 955 [Singapore].

[132] *Idem*, at [46] – "The Liquidators had to establish the facts and find the documents supporting those facts in order to instruct the lawyers and to obtain legal advice on how the statement of claim should be amended. It is not surprising that the work of the Liquidators involved checking many boxes of documents since Suit 833 involved several years of the plaintiff's operations (it related to the employment of an allegedly phantom employee) and the Liquidators had not run the Company or the plaintiff at the material time. In this case, the time spent by the Liquidators and that spent by the lawyers cannot be compared and the fees of the Liquidators cannot be assessed by reference to the lawyers' fees."

[133] The ICAEW Insolvency Code of Ethics is based on the International Ethics Standards Board for Accountants Code, effective from 1 May 2020 and is available at https://www.icaew.com/-/media/corporate/files/technical/ethics/insolvency-code-of-ethics.ashx?la=en.

[134] ICAEW Insolvency Code of Ethics, R2320.3.

also requires an IP to document the reasons for choosing a specific service provider.[135] Additionally, where a professional or personal relationship exists between the IP and the service provider, the Code suggests full disclosure of the relevant relationship and the process be undertaken to evaluate whether the service will be the best value for the creditors.[136] In order to establish whether the service provider will be offering best value and service, the IP would have to consider:[137]

(a) the cost of the service, the expertise and experience of the provider;

(b) whether the provider holds appropriate regulatory authorisation; and

(c) the professional and ethical standards applicable to the service provider.

The requirements and guidance set out in the Code could be applied effectively to the use of legal professionals. Where an IP requires the advice and services of a legal professional he should be able to show that it is indeed necessary and should be able to explain why he chose a specific legal professional. Where he has a relationship that could create the perception that he is not independent from the legal professional, he should disclose the relationship to the stakeholders. He should also be able to provide details of the process he followed to make sure the service provider would offer the best value for the beneficiaries.

Self-Assessment Exercise 5

Many jurisdictions allow for contingency fees or conditional fee arrangements. What does this remuneration method entail? What are the main ethical issues associated with the use of this method of remuneration and are there any safeguards for the use thereof?

For commentary and feedback on self-assessment exercise 5, please see APPENDIX A

5.7 Practice management

Principle 6 – Practice Management

Practice Management

It is in Members' (and their agents and service providers) interests to implement policies, procedures and systems to ensure reasonable and proper:

- record-keeping;
- quality control;

[135] *Idem*, R2320.4.
[136] *Idem*, R2320.6 A6(b).
[137] *Idem*, R2320.4 A.

- risk management;
- compliance management;
- complaints management; and
- professional indemnity / fidelity insurance (where available).

Commentary

Members should endeavour to perform their duties in a timely fashion, respecting legislative time limits.

Members should consider and obtain, where required or reasonably available, appropriate professional indemnity and / or fidelity insurance in keeping with the best interests of stakeholders.

Professional indemnity insurance provides redress to stakeholders in the event a Member acts negligently.

Fidelity insurance protects stakeholders in the event a Member (or a Member's staff) defrauds the estate.

5.7.1 General

The manner in which an IP manages his practice will reflect his commitment to performing his fiduciary duties and his concern for the interests of the beneficiaries of those duties.

It is not expected of IPs to perform all the duties and obligations of their appointment personally and as such they often make use of administrative and other forms of assistance in administering the estate. The IP should therefore ensure that there are policies, procedures and systems in place in order to facilitate an efficient service delivery by all involved in the process. The policies and procedures will usually entail guidance on the aspects dealt with below.

5.7.2 Record-keeping

Not only is it important to keep proper records for remuneration and disbursement purposes but it is also good practice for IPs to keep records in order to justify their decisions should they be challenged or reviewed at a later stage. An IP might be expected to demonstrate the steps taken and the conclusions reached in identifying, evaluating and responding to any circumstance. The records the practitioner maintains in relation to the steps taken and the conclusions reached should be sufficient to enable the courts and a reasonable and informed third party to form an opinion on the appropriateness of the IP's actions. IPs should keep a record of the facts pertaining to the case, who they had interactions with as well as any communications with parties involved in the matter. It would also be sensible for the IP to note his thoughts on the courses of action he considered as well as the reasons why he ultimately chose a particular course of action. This type of record-keeping will act as a safety measure should his decisions be questioned.

5.7.3 Quality control

The IP should ensure that there are policies and procedures to apply and monitor quality control of engagements. Quality standards are often set by the profession itself as well as recognised professional bodies that aim to regulate the profession. It could also be set by the IP's firm. These are important measures to ensure that the profession is not brought into disrepute by the negligent and shoddy work of IPs and also to ensure that the remuneration claimed by the IP is for work properly undertaken. It is imperative that the personnel assisting the IP also adhere to these standards and, most importantly, that the IP oversees that work done by people other than himself adhere to the standards.

5.7.4 Risk management

The process of risk management entails the identification, assessment and control of threats to the IP's practice and / or appointment. Threats could be caused by various different sources, including but not limited to: Information Technology threats and data-related breaches (IPs hold a great deal of sensitive information), financial security, legal liabilities and of course accidents and natural disasters. These types of threats can cost the IP or his practice / firm money, or cause it to permanently close. Risk management policies and procedures aim to minimise the risks and costs involved before they transpire by allowing the IP / firm to make plans for unexpected eventualities. It will help to protect the IP, his firm and its assets, as well as the IP's clients, from potential harm. In being able to identify certain threats it will allow the IP to make sure that his and the firm's insurance needs are met (see the discussion on indemnity and fidelity insurance below).

5.7.5 Compliance management

Many aspects of an insolvency appointment are governed by legislation or secondary legislation, as well as soft law in some places (such as codes of conduct). IPs should take care to comply with the provisions of these sources where a specific aspect is dealt with. Compliance provision could, for example, relate to the performance of certain duties within a specified time. Policies and procedures should be put in place to ensure that the IP complies with the standards and regulations that apply to the profession. The people assisting the IP will thereby also be informed of what is expected of the IP.

5.7.6 Complaints management

As circumstances in insolvency can at times be difficult and even volatile for stakeholders, it would be sensible if the IP allowed for complaints to be lodged. This would enable the IP to more effectively deal with the anxieties of parties involved in the process and perhaps even resolve matters before they escalate. A serious complaint could also inform the IP that he would need to consult the body of creditors, the court, or, in some cases, a legal advisor.

5.7.7 Professional indemnity / fidelity insurance

In many jurisdictions IPs are required to obtain insurance (professional indemnity or fidelity) in protecting the best interests of the stakeholders. Indemnity insurance covers against the risk of stakeholders instituting action against the IP for acting negligently (without reasonable care). Fidelity insurance protects stakeholders in the event of the IP (or someone working for him) acting dishonestly or defrauding the

estate. Fraud in this sense does not necessarily refer to criminal fraud.[138] Given the extensive duties owed by IPs, it would be sensible for IPs to obtain professional and fidelity insurance to protect themselves as well as the stakeholders in the estate.

Self-Assessment Exercise 6

Explain the difference between professional and fidelity insurance and elaborate on why it is of particular importance for IPs to obtain this type of insurance.

For commentary and feedback on self-assessment exercise 6, please see APPENDIX A

6. CONCLUSION

From the above discussion it is clear that the IP profession is one that requires the IP to act honestly and in the best interest of the beneficiaries of his duties and with the necessary care and skill at all times; all this while performing the intricate and complex tasks associated with the administration of the insolvent estate. Moreover, IPs have to perform these duties and tasks while undergoing immense public scrutiny. This is of course to be expected as they are the skilled professionals who give themselves out as helpers in times of chaos and they get paid really well to do so. Most IPs perform their duties with the standard of behaviour expected of them but, due to the vast collection of duties and the differing backgrounds of IPs, they may quite often fail in this endeavour.

Codes of professional conduct could be a helpful tool to remedy this situation. A code has the ability to help the IP to understand what is expected of him and to be properly informed about what can be done when a potential problem arises. INSOL International's Ethical Principles for Insolvency Professionals does an excellent job of explaining and elaborating on what is commonly accepted as best practice ethical behaviour. One hopes that jurisdictions across the world will make use of this resource and draft their own codes or principles.

Having a sound framework to ensure the ethical behaviour of members of the insolvency profession will contribute to the public's trust and confidence in the profession and in turn strengthen the entire insolvency regime.

A final word of advice to bear in mind: A person who accepts the office of a fiduciary undertakes the responsibility of ensuring that he or she understands the nature of the duty a fiduciary is called upon to perform.[139] Make sure that you know!

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[138] Fraud in this sense refers to instances of equitable or civil fraud relating to conduct which, having regard to some special relationship between the two parties concerned, is an unconscionable thing for the one to do towards the other. It might also refer to common law fraud which depends on dishonesty. In both cases the action or conduct will fall short of the conduct expected to be prosecuted in criminal proceedings and might not even relate to deceit.

[139] *Daniels v Anderson* [1995] 13 ACLC 614 [Australia].

APPENDIX A: COMMENTARY AND FEEDBACK ON SELF-ASSESSMENT EXERCISES

Self-Assessment Exercise 1

Question 1

What are the most common elements associated with the existence of a fiduciary relationship?

Question 2

Identify the key fiduciary duties linked to Insolvency Professionals

Question 3

True or False? All Insolvency Professionals owe fiduciary duties.

Question 4

Identify the sources of ethical guidance available to jurisdictions when considering frameworks for addressing the behaviour of Insolvency professionals

Question 5

True or False? Being truthful and being honest amount to the same thing.

Commentary and Feedback on Self-Assessment Exercise 1

Question 1

What are the most common elements associated with the existence of a fiduciary relationship?

A fiduciary is largely accepted to be a person i) who undertakes to act on behalf of another, and ii) who has discretion and power over the interests of the other. A further element of vulnerability is sometimes added as an indicator for the existence of a fiduciary relationship

Question 2

Identify the key fiduciary duties linked to Insolvency Professionals.

- The duty to act in good faith, this duty implies honesty and fair dealing;
- The duty to act in the best interest of the beneficiary of the fiduciary duties,
- The duty to exercise the powers of the office in an independent and impartial manner, this duty includes the duty to avoid a conflict of interest

(The duty of care is not fiduciary in nature and should not be mentioned in answer to this question.)

Question 3

True or False? All Insolvency Professionals owe fiduciary duties.

False, Not all Insolvency Professionals are regarded as fiduciaries as some appointments do not comply with the elements that would normally characterise fiduciary relationships.

Question 4

Identify the sources of ethical guidance available to jurisdictions when considering frameworks for addressing the behaviour of Insolvency professionals.

The INSOL International Ethical Principles for Insolvency Professionals; UNCITRAL Legislative Guide on Insolvency Law; The World Bank's Principles and Guidelines for Effective Insolvency and Creditor Rights Systems; European Bank for Reconstruction and Development (EBRD) Office Holder Principles.

Question 5

True or False? Being truthful and being honest are the same thing.

False, it would be possible for someone to be completely honest but not divulge all the information at his disposal thereby being untruthful.

Self-Assessment Exercise 2

In order to learn more about your own jurisdiction's requirements in relation to independence and impartiality and to educate yourself as to what is expected of you in this regard, investigate whether your own jurisdiction provides for this duty or alternatively what any regulatory or recognised professional body in your jurisdiction advises in this regard. Be specifically on the lookout for provisions in relation to prohibited or worrying relationships and the test for compliance.

Commentary and Feedback on Self-Assessment Exercise 2

This exercise is for enlightenment and to educate yourself on the rules that might apply to you or that would apply to you in relation to performing your insolvency related duties in an independent and impartial matter. You should look for relationships that might be prohibited or even certain actions. Knowing what would get you in trouble is the first step of staying out of it!

Self-Assessment Exercise 3

Julie is a well-known Insolvency Practitioner and is often sought out for her knowledge and expertise especially in relation to retail insolvency. She currently has ten ongoing insolvency matters (most of them quite complex) relating to retail insolvency and have almost exclusively only dealt with retail insolvencies for the last 5 years.

Due to her impressive curriculum vitae she is contacted by a very large mining company in distress inquiring whether she would be able to take an appointment as an administrator. Julie does not feel like she has the level of expertise to accept this appointment.

Question 1

What would you advise Julie to do in these circumstances?

Question 2

If Julie was to accept the appointment and something went wrong, could she be held liable for a breach of her duty of care?

Commentary and Feedback on Self-Assessment Exercise 3

Question 1

The principle of professional and technical competence is one that requires an exceptional level of self-realisation and introspection by the IP. Well done to Julie for knowing her limits!

It is important that professionals know the limitations of their own knowledge, skills and experience (and diaries). As such, when an area of deficiency is identified it is of paramount importance that the IP, as fiduciary, ensures that she educates herself in order to enable her to act in the best interest of her beneficiaries.

The principle of professional and technical competence and the duty of care placed on the IP require that an IP should only accept insolvency appointments when the IP has or can acquire sufficient expertise.

In Julie's case it might be possible for her to brush up on some knowledge of the mining industry, given her current case load it might be difficult for her to administer all those estates while taking on a new client in an area she does not know a lot about. She is allowed to make use of the advice and services of other professionals as IPs are not required to be experts on everything. However, the cost of using these professionals should be carefully considered. Julie would have to consider all of

these factors before making a decision on whether she would be best placed to serve the interests of her beneficiaries should she decide to accept the appointment.

Question 2

The two-fold test for breach of the duty of care would have to be applied in the case (explain the test and apply it).

Self-Assessment Exercise 4

Question 1

Jason, as the administrator of a large construction company with several government contracts, has been asked to give a television interview on the progress of the proceedings. What are the factors that Jason should consider when deciding to grant the interview?

Question 2

It is only risky to provide media interviews and not when you are having a social gathering with family and friends. True or false?

Commentary and Feedback on Self-Assessment Exercise 4

Question 1

Jason should be mindful that giving information should be balanced with maintaining commercial and other confidentiality obligations, and he should also consider the cost of preparing the response against the benefit of such response. In other words what would be gained and lost by divulging certain information. It is normal that in a high-profile case, many persons without a tangible interest in the case might demand information. Again Jason should weigh the advantages of providing the information against the associated cost and disruption to the company or estate. Decisions should be made in the best interests of the estate and its stakeholders. He should be mindful of his duty of confidentiality: not disclosing confidential information acquired as a result of professional and business relationships, without proper and specific authority, unless there is a legal or professional right or duty to disclose; making improper use of confidential information acquired as a result of professional and business relationships to their personal advantage or the advantage of third parties; and publishing or divulging without just cause to any person any confidential information or details concerning the business, affairs, trade secrets, patents, technical methods or processes of any estate in respect of which they hold appointment.

Question 2

False. An IP shall maintain confidentiality, including in a social environment, being alert to the possibility of inadvertent disclosure, particularly to a close business associate or a close or immediate family member.

Self-Assessment Exercise 5

Many jurisdictions allow for contingency fee or conditional fee arrangements. What does this remuneration method entail? What are the main ethical issues associated with the use of this method of remuneration and are there any safeguards for the use thereof?

Commentary and Feedback on Self-Assessment Exercise 5

As the name suggests these are fee arrangements which determine that the IP would be entitled to receive remuneration based on a specific outcome or condition being met. The outcome or condition usually pertains to a favourable outcome for stakeholders. One reason for the controversy surrounding contingency fee arrangements is that the conditions and outcomes on which the fee is payable are arguably conditions and outcomes that IPs, as fiduciaries, should aspire to anyway and would therefore form part of their remit. Another issue can be found in the diverting of an IP’s focus to a singular task that will benefit his fee arrangement instead of allowing his approach to be holistic. There would not be an ethical issue in the event of a contingency fee being paid for the achievement of a truly remarkable outcome and these outcomes should always be objectively measurable.

Self-Assessment Exercise 6

Explain the difference between professional and fidelity insurance and elaborate on why it is of particular importance for IPs to obtain this type of insurance.

Commentary and Feedback on Self-Assessment Exercise 6

Indemnity or professional insurance covers against the risk of stakeholders instituting action against the IP for acting negligently (without the reasonable care). Fidelity insurance protects stakeholders in the event of the IP (or someone working for him) acting dishonestly or defrauding the estate. Fraud in this sense does not necessarily refer to criminal fraud.

Given the extensive (and sometimes confusing) duties owed by IPs it would be sensible for IPs to obtain professional and fidelity insurance to protect themselves as well as the stakeholders in the estate.

APPENDIX B: GLOSSARY OF TERMS[140]

Advocacy	A situation in which a Member promotes a position or opinion to the point that subsequent objectivity may be compromised (e.g., the Member has acted on behalf of a significant creditor to advance such creditor's position). In such case, it is unlikely that other creditors would consider the Member to be impartial.
Agent	A person / firm employed under an engagement letter by the insolvent estate (acting by a Member) to perform a task or provide a service: for example, the employment of legal counsel.
Associate	Persons connected to the Member in the capacity of (for example) a personal friend or acquaintance, spouse, partner, civil partner, employee, employer, colleague, a relative of the Member or the Member's spouse or civil partner, the spouse or civil partner of a relative of the Member or the Member's spouse or civil partner.
Close business associate	Persons connected to the Member through professional means, including via employment, partnership, directorships of or shareholding in corporate entities or corporate trust arrangements.
Creditor	A person who is, or claims to be, owed money by the insolvent estate, whether or not such claim is ascertained, liquidated or contingent.
Disbursements	Sums paid by a Member or its firm to third parties or a recharge or allocation of costs incurred by Members or their firms which is charged to the estate.
Estate	The insolvent entity or its assets over which the Member has been appointed insolvency practitioner in accordance with applicable law.
Familiarity	A situation in which a Member's relationship to a stakeholder impairs (or is perceived to impair) such Member's impartiality and objectivity owing to the Member being too sympathetic or antagonistic to the interests of certain others (e.g., where the Member is a close relative of a significant creditor or shareholder, or of a director of the insolvent estate).

[140] The glossary of terms included in this appendix has been reproduced from the INSOL International publication *Ethical Principles for Insolvency Professionals*, published in June 2019.

Family	Lineal ancestors / descendants (including step-parents). Dependent relations-by- marriage in lineal relationship. Any other dependents living within the household (adult or children). A Member is related to another individual if they - (i) are married, or live together in a relationship similar to a marriage; or (ii) are separated by no more than two degrees of natural or adopted consanguinity or affinity. A Member is related to a corporation, partnership or other juristic person or entity if the individual directly or indirectly controls such juristic person or entity.
Insolvency and Restructuring Officeholders	Officeholders include formal and informal appointments such as Liquidator, Provisional Liquidator, Insolvency Administrator, Insolvency Trustee, Receiver, Restructuring Officer, and Insolvency Resolution Professional.
Insolvency and Restructuring Professionals ("IPs")	IPs include professionals engaged in insolvency administration, restructuring and turnaround practice areas, and the advisers to those engaged in these practice areas.
Intimidation	A situation in which a Member is, or may be, threatened or pressured (e.g., with litigation, unfounded complaints, or even physical harm).
Member	Individual member of INSOL International authorised in accordance with applicable law, practice and regulation to accept an engagement or appointment in respect of an estate.
Regulator(s)	Any recognised professional body charged with regulating the profession of insolvency practitioners (whether solely or as part of a wider body of professional regulation) in accordance with local law and guidance.
Self-interest	A situation in which a Member has, or is perceived to have, a direct interest in obtaining a particular outcome: for example, where such Member (or a close associate) is also a creditor or shareholder of the insolvent estate.
Self-review	A situation in which actions taken by a Member, such Member's firm, a close associate, or a close associate's firm is (or is perceived to be) subject to review only by such Member (e.g., where a Member's firm carried out the disposal of certain assets of the insolvent estate prior to

	insolvency, and there are suspicions that the disposal is in some way improper).
Shareholder	A person having an equity interest in the insolvent estate (ordinary, preferred, restricted) as defined by local law and accounting standards.
Stakeholder	A person having a tangible interest in the insolvent estate.
Tangible interest	Financial (monetary or economic) interest, whether direct or indirect (e.g., loss of employment).
Third party costs	Sums paid directly from the estate to a third party supplier. The third party supplier invoices the estate.

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