



SUMMATIVE (FORMAL) ASSESSMENT: MODULE 9

ETHICS AND PROFESSIONAL PRACTICE

This is the **summative (formal) assessment** for **Module 9** of this course and is compulsory for all candidates who **selected this module as one of their elective modules**.

The mark awarded for this assessment will determine your final mark for Module 9. In order to pass this module, you need to obtain a mark of 50% or more for this assessment.

INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT

Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.
2. All assessments must be submitted electronically in **Microsoft Word format**, using a standard A4 size page and an 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way. DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.
3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).
4. You must save this document using the following format: **[studentnumber.assessment9]**. An example would be something along the following lines: 202021IFU-314.assessment9. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words “studentnumber” with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked.**
5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words.**
6. The final submission date for this assessment is **31 July 2021**. The assessment submission portal will close at **23:00 (11 pm) GMT on 31 July 2021**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.
7. Prior to being populated with your answers, this assessment consists of **8 pages**.

Commented [DB1]: Please read and then follow the instructions!

ANSWER ALL THE QUESTIONS

QUESTION 1 (multiple-choice questions) [10 marks in total]

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and **mark your selection on the answer sheet by highlighting the relevant paragraph in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

Question 1.1

Please choose the **most correct answer** from the options below.

INSOL International's *Ethical Principles for Insolvency Professionals*

- (a) are mandatory and apply to all its members.
- (b) creates a set of rules which all jurisdictions have to incorporate into their insolvency frameworks.
- (c) creates a set of rules by which stakeholders and the public in most jurisdictions would be able to determine whether insolvency practitioners are acting in accordance with ethical principles.
- (d) creates a set of best practice principles to inform and educate insolvency practitioners and stakeholders by providing ethical and professional guidance on issues of importance.**

Question 1.2

The "Enlightened Creditor Value" approach to insolvency proposes the following with regard to the protection of competing interests in insolvency proceedings:

- (a) creditors' interests are of paramount importance and as such only these interests should be protected in insolvency.
- (b) The interests of stakeholders should be regarded in the same manner as those of creditors.
- (c) Creditors' interests are of paramount importance, however, the interests of other stakeholders should also be considered where this would be in the creditors' interests.**
- (d) Only the shareholders of the company and the creditors of the company should be protected by the insolvency law (and in that order).

Question 1.3

All insolvency professionals are fiduciaries.

- (a) True**
- (b) False

Commented [JL2]: TOTAL: 42 out of 50
Well done!

Commented [JL3]: 7 out of 10

Commented [JL4]: b
Although most IPs are regarded as fiduciaries not all are e.g. Supervisors in a CVA. See section 3.2 of the GT.

Question 1.4

Being truthful and being honest is **not** the same thing.

(a) True

(b) False

Question 1.5

Tony has been appointed as a liquidator of Company X. Company X has several major creditors, including ABC Bank. A year prior to the liquidation of the Company, Tony was acting in an advisory capacity for ABC Bank in litigation against Company X where he attempted to advance ABC's position as a creditor.

This situation is an example of a/an _____ threat.

(a) self-review

(b) self-interest

(c) advocacy

(d) intimidation

Commented [JL5]: c

Question 1.6

A lack of independence and impartiality due to a prohibited relationship with a stakeholder can always be remedied by disclosing the relevant relationship to the relevant parties and issuing a declaration of independence.

(a) True

(b) False

Question 1.7

Julie is a well-known insolvency practitioner and is often sought out for her knowledge and expertise. She currently has ten ongoing insolvency matters (most of them quite complex) and has been feeling somewhat overwhelmed. Due to her impressive *curriculum vitae* she is contacted by a very large designer company in distress inquiring whether she would be able to take an appointment as an administrator. Julie should:

(a) Accept the appointment as it will boost her career even further.

(b) Accept the appointment as she can get one of her junior associates to take over all her other cases.

(c) Accept the appointment because as a professional she will have the ability to give all of the cases she is involved in some attention, although some of them will now only be overseen by her.

(d) Refuse the appointment as she will not be able to give all of the cases she is involved in the requisite level of attention.

Question 1.8

Johnson has been appointed as a new associate at the firm where he is employed. In his new role he has to meet certain targets in relation to the fees he earns for taking appointments. Johnson is currently appointed as a liquidator for a small company. He realises that he will not meet the firm's target for fees. The most ethical thing for Johnson to do would be to:

- (a) Call a creditors' meeting requesting an adjustment to his agreed fees due to unforeseen circumstances.
- (b) Ask his administrative assistant to invoice the estate for the use of the firm's conference venue for meetings held there at a 50% increased fee.
- (c) Carry out his duties in a timely fashion and complete the appointment efficiently and without undue delay, only invoicing for work properly performed.
- (d) Ask his administrative assistant to double check all the calculations in the case file and then bill the hours as part of his invoice.

Question 1.9

Please choose the **most correct answer** from the options below.

An insolvency practitioner using a fixed fee calculation method for determining the amount of remuneration owed to him, will receive a fair amount of remuneration.

- (a) This statement is true since jurisdictions always allow for an adjustment of fees where it is necessary.
- (b) This statement is false since the practitioner might have carried out more work and invested more resources than is reflected in the fee.
- (c) This statement is false since the practitioner will always receive more remuneration than what is reflected in the work carried out.
- (d) This statement is false since the only way to receive a fair amount of remuneration is to calculate the remuneration on an hourly rate.

Commented [JL6]: b

Question 1.10

Please choose the **most correct answer** from the options below.

Fathima has just completed Module 9 of INSOL International's Foundation Certificate. She works as a junior insolvency practitioner at a large firm. Her firm is contemplating the acquisition of a new information technology system to help ease the administrative burdens of the practitioners at the firm. This new system will digitise all of the documents in relation to insolvency appointments. All the practitioners and administrative personnel employed by the firm will have access to these files as long as they have access to an internet connection. Fathima should advise someone in the office to implement procedures and policies on _____ in relation to this proposed new system.

- (a) quality Control
- (b) risk Management

(c) compliance management

(d) fidelity insurance

QUESTION 2 (direct questions) [10 marks]

Commented [JL7]: 10 out of 10

Question 2.1 [maximum 4 marks]

What are the main fiduciary and other duties usually associated with insolvency professionals?

The main fiduciary duties of the insolvency professionals are as follows:

- (i) the duty to act in good faith – this duty implies honesty and fair dealing;
- (ii) the duty to act in the best interest of the beneficiary of the fiduciary duties;
- (iii) 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;
- (iv) a duty which is usually not regarded as being fiduciary in nature, the duty to act with care, skill and diligence.

Commented [JL8]: 4

Question 2.2 [maximum 4 marks]

Briefly explain the two-pronged nature of the duty to act with independence and impartiality.

The IP would be able to carry out his/her function in the best interest of the beneficiaries only if he is independent and impartial. It aims at removing bias, conflicting interest and undue influence of others from overriding the IP's professional judgements in performance of his/her duties. Independence and impartiality would be looked at a matter of fact and from the perspective of an informed observer, therefore the IP should refrain from matters that involve any stakeholders with whom he has an existing relationship with. IP must be factually free of any influences that could compromise his judgement and must on the other hand also avoid such circumstances that would lead a reasonably informed third party to conclude that the IP's integrity, independence and impartiality have been compromised.

Commented [JL9]: 4

Question 2.3 [maximum 2 marks]

What is the preferred method of calculation of insolvency practitioner remuneration? Name one ethical issue in relation to this method of calculation.

Time-based fees remains the most widely used method of calculation of the insolvency practitioner's remuneration. The biggest ethical issue relating to this method of calculation is that this system might incentivise time spent on the administration without necessarily achieving any outcome and it might not be reflective of the actual work done.

Commented [JL10]: 2

QUESTION 3 (essay-type questions) [15 marks in total]

Commented [JL11]: 14 out of 15

Question 3.1 [maximum 8 marks]

Which elements of insolvency proceedings are especially prone to create or give rise to threats to independence and impartiality? Please elaborate.

The following circumstances in an insolvency proceeding often pose a threat to the insolvency and impartiality of the IP:

- (i) **Pre-commencement/appointment involvement:** Consultation prior to the commencement of the insolvency process often take place between the IP, company or other stakeholders. Not all types of such contact would dilute the independence and impartiality but it may leave an impression of the lack of it. However, the consultation should not be of a material nature and should be limited to the company's financial position, company's solvency, effects of potential insolvency. This question arose in the matter of *Re Korda, Ten Network Holdings Ltd* wherein the firm was involved with the company to review their financial position before their appointment as the administrator. The court held that it was in the intrinsic character of corporate restructuring, that the companies engage administrator firms to gauge the financial position of the company before the actual commencement of any insolvency or insolvency like process. So long as certain safeguards like the administrator being engaged in limited capacity with no interaction or absolutely necessary interaction with the management of the company and declaration to the effect that if the company in fact enters into an insolvency process they might be the potential administrator and thus their work must be done at an arms length basis currently.
- (ii) **Appointment of CIPs:** Several jurisdictions allow the petitioner of an insolvency application to also suggest the name of the IP to be appointed as the CIP. This could lead to the particular stakeholder thinking that the CIP must automatically act in their favour. The practitioner must make it clear that he/she is an independent entity who must act in a manner to balance the interests of all the stakeholders and not any one particular class of stakeholders.
- (iii) **Subsequent appointments:** This is a scenario wherein the same CIP is allowed to act in different insolvency capacities in relation to the same debtor company. Subsequent appointments therefore pose a problem in relation to independence and impartiality due to self-review and self-interest threats that is creates. The self-review threat refers to a situation where a CIP who was involved in decision making at the earlier stages of the process would not be able to evaluate the results of previous judgements made or services rendered. The self-interest threat relates to the issue of remuneration of the CIP.
- (iv) **Secret monies and personal transactions with the company:** CIP must never place themselves in a position where they stand to gain against and such a situation creates a conflict with his duties. The CIP's duty to act with independence and impartiality therefore encapsulates the same values as the no-profit and no-conflict 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 and thereby be unjustly enriched by secret kick-backs or commissions. The no-conflict rule determines that a fiduciary may not allow a conflict to arise between his duties and the interests of the beneficiary, for eg. transacting with the debtor company in his personal capacity. This issue was interpreted in the matter of *Commonwealth Bank of Australia v. Irving*, wherein the chartered accountant Mr. Irving had a long-standing relationship with one of the erstwhile directors of the company Mr. Townsend. Mr. Irving had also provided consultation services to the company regarding its financial position. Although, Mr. Irving had disclosed his prior relationship to the directors of the company and there was no factual evidence to prove any impropriety but the situation was exacerbated by Mr. Townsend's law firm acting as Mr. Irving's legal counsels in the matter. Therefore, although individually the facts do not seem to affect the independence and impartiality of Mr. Irving but any informed observer may come to an alternate

conclusion due to the longstanding personal and professional relationship that strikes at the root of the matter between Mr. Irving and Mr. Townsend.

Commented [JL12]: 8

Question 3.2 [maximum 7 marks]

As insolvency appointments often involve complex legal issues, it is common practice for insolvency practitioners to rely on the advice and services of legal professionals. What ethical considerations should be borne in mind, especially regarding the fees of these legal professionals?

It is common practice for CIPs to rely on legal professionals across jurisdictions. In South Africa and England and Wales, the CIPs are generally not trained in law and therefore in almost all cases it becomes paramount that they rely on legal professionals. The Insolvency Code of Ethics by the Institute of Chartered Accountants of England and Wales addresses this issue with remarkable clarity. It puts the onus on the CIP in every matter to as a first step assess whether appointment of a legal professional is required and document the reasons found in support of the same. It also mandates disclosure with regards to any personal or professional relationship that exists between the CIP and the legal professional. Moreover it mandates a three-pronged approach to decide the appointment:

- (i) Cost of services;
- (ii) Whether the service provider has the requisite regulatory approval;
- (iii) The professional and ethical standards applicable to the service provider.

Legal fees are the most controversial administrative costs. The Singaporean Kao case illustrated that the legal fees could be paid out as disbursements or third party costs. The court was of the opinion that the fees could be made part of the IP's fees or could be separately billed in favour of the company. When it is included as part of disbursements, it has been held in Re Korda that it would be the IP's onus to use their commercial judgment to assess if the fees claimed are reasonable or not. However when they are directly charges to the company the level of scrutiny and issues relating to assessing whether there is any duplication of work for which legal fees is charged remains. In the Dovechem case, the court was confronted with a question as to whether there was duplication of work on the liquidator's side as they had charged 4 times the fees charged by the solicitors appointed in the matter. The onus then fell on the CIP to prove that there was no duplication of work and they were successful in the same.

Commented [JL13]: Reasonable attempt. Some elements missing – relationships/ familiarity between service provider and IP.
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QUESTION 4 (fact-based application-type question) [15 marks in total]

Commented [JL14]: 11 out of 15

WeBuild Ltd is a private company registered in Eurafriolia. The company specialises in construction and property development and is well known in the area where it conducts business. Mr B Inlaw, Dr I Dontcare and Mrs I Relevant are the directors of the company. The company has ten shareholders, with Mr B Inlaw and Dr I Dontcare also holding shares in the company.

The company traded profitably for the last 10 years but recently started to experience financial difficulties. One of the main reasons for the decline is the fact that several of the company's employees have instituted a class action claim against WeBuild for workplace related injuries due to faulty machinery. This also resulted in bad publicity that led to a decline in contracts. The directors of the company were made aware of the issues relating to the machinery but chose not to take any action to remedy the situation. When the company's financial position started to decline the directors continued to trade as if nothing was amiss and even made several large payments to themselves by way of performance bonuses. When they received a letter of demand from the company's major secured creditor, ABC

Bank, the directors decided to call a shareholders' meeting to discuss the company's options.

Present at this meeting were the shareholders, the directors and Mr Relation, a lawyer, to provide them with information and advice in relation to their options. Some of the shareholders recognised Mr Relation as Mr B Inlaw's brother-in-law and godfather to his daughter. During the meeting, Mr Relation suggests that the company enter into a voluntary administration procedure. Mr B Inlaw suggests that the company appoint Mr Relation as administrator. He accepts the appointment, ensuring that he discloses his relationship with Mr B Inlaw and says that he will declare that he believes that he will still be able to act with the required independence and impartiality.

After the meeting adjourns, Mr B Inlaw requests the other directors and Mr Relation to stay behind for a brief "planning" meeting. During this subsequent meeting the directors inform Mr Relation that they are concerned about their personal liability for breach of duty. Moreover, they are worried that they might land in hot water due to their decision to continue trading when the company was clearly in dire financial straits. Mr Relation assures them that his focus will not be on them but on trying to rescue the company.

In the weeks that follow, Mr Relation conducts a superficial investigation into the affairs of the company and the circumstances leading to the financial difficulty of the company. He relies on detailed reports drafted by Mr B Inlaw regarding the company's business and drafts a strategic plan for recovery based on his investigation and the reports he received.

At a meeting of creditors to consider the plan, Mr Relation states that he has found no evidence of any wrongdoing or maladministration by the company's directors. Mrs Keeneye, a lawyer attending the meeting on behalf of ABC Bank, the major secured creditor, recognises Mr Relation from a television interview where Mr Relation expressed the opinion that banks should be more accommodating in restructuring proceedings and that he thinks that the interests of lower ranking creditors should sometimes outweigh "big money" (referring to financial institutions). She immediately feels uncomfortable with his appointment as administrator.

Several months later the administration fails due to a "lack of funding" to finance the rescue. The administration is subsequently converted to liquidation proceedings and Mr Relation is appointed as the liquidator.

INSTRUCTIONS

There are at least THREE major ethical issues in this factual scenario.

Please identify these ethical issues and explain in detail why they are in fact ethical issues. Your answer should include reference to the ethical principles and the commentary thereon. Where appropriate and suitable, you should also endeavour to elaborate on possible remedies or safeguarding mechanisms to minimise or remove the ethical threats.

You may also make use of case law and secondary sources to substantiate your answer.

There are several ethical issues in the given facts. A CIP has to function in accordance with the cardinal principles of integrity impartiality, independence and good management. However, the following ethical issues have marred the functioning of Mr. Relations:

- (i) Pre-commencement/appointment involvement: In the given factual scenario, Mr. Relations was acting as an adviser prior to the commencement of the

commencement of the insolvency process and infact is the key proponent for the company entering into voluntary administration process. Not all types consultation prior to the commencement of the insolvency process would dilute the independence and impartiality of the CIP unless the consultation is of a material nature. This question arose in the matter of Re Korda, Ten Network Holdings Ltd wherein the firm was involved with the company to review their financial position before their appointment as the administrator. The court held that it was in the intrinsic character of corporate restructuring, that the companies engage administrator firms to gauge the financial position of the company before the actual commencement of any insolvency or insolvency like process. So long as certain safeguards like the administrator being engaged in limited capacity with no interaction or absolutely necessary interaction with the management of the company and declaration to the effect that if the company infact enters into an insolvency process they might be the potential administrator and thus their work must be done at an arms-length basis currently. The consultation therefore must be limited to the extent of assessment of the company's financial position, company's solvency, effects of potential insolvency. However, in the given case the consultation was not at an arms length basis and was certainly not limited to the financial position of the company.

- (ii) Appointment of CIPs: In the present case Mr. Relations has along standing person relationship with the directors and moreover has expressly stated that he would act in the interest of shareholders over the interest of the creditors. The CIP must at all times operate as an independent entity who must act in a manner to balance the interests of all the stakeholders and not any one particular class of stakeholders. However, in this case Mr. Relation has deliberately covered up the malfeasance of the existing management of the company and thereby aided in the diversion of funds that could've been used to repay or even rescue the company. Moreover, considering the deliberate concealing of facts in the given factual matrix, the fact that a declaration of the interest of the CIP was given is not enough to attest to his independence and impartiality. This was discussed at length in the matter of Commonwealth Bank of Australia v. Irving, wherein the chartered accountant Mr. Irving had a long-standing relationship with one of the erstwhile directors of the company Mr. Townsend. Mr. Irving had also provided consultation services to the company regarding its financial position. Although, Mr. Irving had disclosed his prior relationship to the directors of the company and there was no factual evidence to prove any impropriety but the situation was exacerbated by Mr. Townsend's law firm acting as Mr. Irving's legal counsels in the matter. Therefore, although individually the facts do not seem to affect the independence and impartiality of Mr. Irving but any informed observer may come to an alternate conclusion due to the longstanding personal and professional relationship that strikes at the root of the matter between Mr. Irving and Mr. Townsend.
- (iii) Subsequent appointments: This is a scenario wherein the same CIP is allowed to act in different insolvency capacities in relation to the same debtor company. In the present case Mr. Relation is also proposed to be appointed as the liquidator. Subsequent appointments pose a problem in relation to independence and impartiality due to self-review and self-interest threats that is creates. The self-review threat refers to a situation where a CIP who was involved in decision making at the earlier stages of the process would not be able to evaluate the results of previous judgements made or services rendered. In this case, the the cover-up by Mr. Relation by aiding the directors from any liability for breach of duty shall not be rectified even at the liquidation stage. The self-interest threat relates to the issue of remuneration of the CIP. Since Mr. Relation has been

involved in the matter from the very inception and since he took substantial risk in covering up the malfeasance of the directors, there is a high likelihood of him claiming an unscrupulous amount as his professional fees.

Commented [JL15]: A good answer with three issues correctly identified. I would have liked to see a little more detail with regard to the application of the principles and also why the issues are in fact ethical issues.
Respectable answer nonetheless.
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*** End of Assessment ***