



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: **[studentID.assessment9]**. An example would be something along the following lines: 202122-336.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 2022**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2022**. 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**.

ANSWER ALL THE QUESTIONS

Commented [JL1]: TOTAL 43 out of 50
Well done.

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

Commented [JL2]: 10 out of 10

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**

Question 1.4

Being truthful and being honest is the same thing.

(a) True

(b) False

Question 1.5

Select the **correct** answer:

Tony has been appointed as a liquidator of Company X. Company X has several major creditors, including ABC Supplies. Tony owns 30% of the shares in ABC supplies.

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

(a) self-review

(b) self-interest

(c) advocacy

(d) intimidation

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

Select the **correct** answer:

Thembi 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. Thembi 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

Select the **correct** answer:

Rajesh 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. Rajesh 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 Rajesh 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

Select the **most correct answer** from the options below.

An insolvency practitioner using a percentage-based 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 the value of the realisable or distributable assets.

(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.

Question 1.10

Select 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 [JL3]: 10 out of 10

Question 2.1 [maximum 2 marks]

The ethical principle of integrity implies "fair dealing". How would this apply in an insolvency context?

Fair dealing relates to the treatment of people in a fair and equitable manner. In an insolvency context, due to the nature of insolvency, it is not possible to treat all stakeholders fairly, as the system is designed to favour only certain stakeholders. For example, some jurisdiction is more creditor friendly and treats creditors more favourable. Nonetheless, in an insolvency context, fair dealing will involve treating similar stakeholders in an equitable manner.

Commented [JL4]: 2

Question 2.2 [maximum 4 marks]

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

The duty to act with independence and impartiality is a duty of the Insolvency Practitioner ("IP") to not allow bias, conflict of interest, or undue influence of others which will impair his professional and/or business judgements in the execution of his duties and obligations.

Firstly, independence and impartiality go hand in hand and refers to ensuring that the IP is separate and not prejudiced or biased towards any stakeholders or parties.

It is important, that independence and impartiality are adhered to both in fact and in appearance. That is, the IP should be factually independent, and his actions should also give the perception that he is indeed independent. The IP should ensure that his conduct does not appear to be unfairly biased to any parties.

Some indications of a threat to independence and impartiality include self-interest, self-review, advocacy, familiarity and intimidation.

For the IP to be independent in fact requires the IP to be free from any influences that can compromise his judgement, including avoiding all professional and personal relationships, direct and indirect interests, and other actions that may influence, impair or threaten his integrity. Similarly, perception includes avoiding situations that will give the perception to reasonably informed third parties to conclude that the IP's integrity, independence and impartiality is compromised.

Commented [JL5]: 4

High importance is placed on this duty to avoid erosion of the trust and reliance that stakeholders place on IPs.

Question 2.3 [maximum 4 marks]

Contingency fee arrangements have been a controversial issue in relation to insolvency practitioners and their remuneration. Briefly reflect on this practice and the possible ethical issues in relation to this method of calculation.

Contingency fee arrangement refers to a fee arrangement that is reliant on some outcome, usually based on realised value condition being met.

These arrangements are controversial to insolvency practitioners as this method is seen as a means for encouraging IPs to achieve a specific favourable outcome, such as a very successful sale of an asset for the benefit of the creditors. That is, the IP will be incentivized to achieve the best outcome possible as his fee is reliant on this outcome.

However, the cause for concern with this arrangement is that the IP owes a duty to aspire to achieve this outcome irrespective of his fee arrangement. Similarly, due to being incentivized to obtaining the best outcome from this one action, resources and attention will be geared towards this achievement, rather than taking a holistic approach.

However, it should be noted that there will not be ethical issues in the event of a contingency fee paid based on a truly remarkable outcome, and these outcomes should always be objectively measurable.

Commented [JL6]: 4

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

Commented [JL7]: 15 out of 15

Question 3.1 [maximum 8 marks]

The ethical principle that requires insolvency practitioners to act with and maintain professional and technical competence is often linked to the duty of care. Elaborate on this duty and on the yardstick that would be used when determining whether a practitioner acted with the necessary care, skill and diligence.

IPs are required to act with and maintain a duty of care. While the duty of care is not fiduciary in nature, it refers to adherence to a standard of reasonable care while performing his actions, especially as IPs are responsible for the impact on many stakeholders.

This duty of care covers many aspects of an IP's roles and actions and commences even before an IP takes an appointment. For instance, an IP should ensure that he has the necessary time, resources, experience and attention before taking an appointment to ensure that adequate attention is given.

Furthermore, the duty of care further extends to the IP ensuring sufficient understanding of the business and its industry to ensure that he understands what is expected of him.

The ethical principle that requires insolvency practitioner to act with and maintain professional and technical competence is often linked to the duty of care highlighted above. This is because of the level of responsibility and accountability that the IPs have towards

stakeholders, including vulnerable stakeholders such as creditors who may be in a distressed situation.

The principle holds that IPs should maintain an acceptable level of professional competence by, as noted above, keeping current with legislative/regulatory changes; undertaking continued professional education; and undertaking sufficient case work which allows for the IP to remain experienced. This includes maintaining competence in the IPs field of work in order to deliver the highest quality of work for the benefit of the stakeholders involved.

The principle of professional and technical competence is closely linked to the duty of care, skill and diligence as IPs operate in distressed and contentious situations while holding the affairs and assets of others in their hand. The insolvency proceedings, while already challenging, can be further frustrated by the incompetence and carelessness of IPs. This carelessness can result in loss which the IP may become personally liable for.

A two-fold test can be applied to an IP to determine whether the duty of care, skill and diligence is met. This is an objective test to determine what a reasonable person would have done in the same situation, along with a subjective test, taking into consideration the general knowledge, skill and experience of that specific person. A conclusion will be made on whether the IP acted with the same degree of care, skill and diligence that may reasonably be expected of a reasonable IP in the same circumstances, while having regard to his personal attributes and qualifications.

Due to the nature of the work in which the IP performs, a higher regard is held for IPs in relation to the subjective test, in light of the fact that the IP is seen as an expert in his field.

Commented [JL8]: 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?

IPs should keep ethical considerations surrounding remuneration in mind when dealing with all appointments. This extends to situations which involve complex legal issues and the remuneration of the legal practitioners employed to provide advice to the IPs.

There is a difference between remuneration, disbursements and third-party costs that are billed to the estate. Firstly, remuneration refers to the compensation that the IP receives for taking their appointment and conducting their work. Secondly, disbursements are sums paid by IPs or their firms to third parties or a recharge or allocation of costs incurred by IPs or their firms which are charged to the estate.

Finally, third-party costs are sums paid directly from the estate to a third-party supplier. These suppliers invoice the estate.

Before engaging solicitors, as there is a duty to be independent in fact and appearance, the IP should avoid engaging solicitors based on close relationships, but rather engage on the sole criteria that the solicitor is indeed needed to solve a purpose.

Once a solicitor is engaged, other issues surrounding legal fees include that of over-servicing by providing services for unnecessary work; and to avoid duplicating the work of other professionals.

IPs will want to scrutinize the work of the legal practitioners to ensure unnecessary tasks are not performed and it is not for work already done.

Whether or not the legal fees are classified as a disbursement (paid by the IP and recovered), or as a third-party cost (billed to the estate), they are under the supervision of the IP and as such, the IP has a duty of care to ensure that they are reasonably incurred.

Where the cost is incurred as disbursements, the IP should ensure that, given the circumstances for involving the legal professionals, the costs are reasonable and appropriate. When the costs are billed to the estate, the IP should extend the same care, however the additional concern of duplication of work is added. The IP will need to justify the claims for work performed especially when other professionals are engaged in the same matter.

Under the New Insolvency Code of Ethics for Chartered Accountants of England and Wales, the code requires that where an IP intends to rely on advice of third parties, the IP will need to determine that the work was indeed warranted. The IP should further document the decision for choosing the service provider and for the work they will perform.

Furthermore, a prudent IP will shop around to obtain the best value when it comes to legal professionals. When considering the service of the legal professionals, the IP would consider the cost, expertise and experience of the service provider; whether they hold appropriate regulatory authorisation; and the professional and ethical standards applicable to the service provider.

Commented [JL9]: 7
A very good answer.

QUESTION 4 (fact-based application-type question) [15 marks in total]

Commented [JL10]: 7 out of 15

WeBuild Ltd is a private company registered in Eurafriclia. The company specialises in construction and property development and is well known in the area where it conducts its 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 financial 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 difficulties 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.

You are required to 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 identified in the scenario.

Breach of Fiduciary Duty

The first ethical issue to be considered is that of a breach of a fiduciary duty. This occurs on both the side of the directors and on Mr. Relation, acting as an IP in his role as administrator and liquidator.

A director owes a fiduciary duty to act in the best interest of the company and its stakeholders, including the safety of its employees.

In the case, it was identified that there were several workplace-related injuries due to faulty equipment which the directors ignored.

Secondly, Mr. Relation, acting as an administrator and later as a liquidator has breached his duty to the Company and its stakeholders for reasons outlined below under Conflict of

Commented [JL11]: this is not relevant to the question in this way.

Interest and Independence, to properly investigate the affairs of the Company to remedy the situation at hand.

Commented [JL12]: This creates a self-interest and self-review threat and does not necessarily constitute a breach

Mr. Relation has ignored the breaches of fiduciary duty on the part of the directors, including the director's decision to trade while the Company was insolvent and/or transactions which may have caused the company to become insolvent, including the directors' bonuses, which may be considered a voidable transaction in insolvency.

Conflict of Interest

The first instance of a conflict of interest relate to some directors also owning shares of the Company. This is an issue as the ultimate goal of a shareholder is to ensure the Company is profitable to gain a return on their investment. Meanwhile, the duty of the director is to properly run the Company in the best interest of its stakeholders.

Commented [JL13]: This is irrelevant to the question, moreover, it is commonplace in private companies to have several director-shareholders. It does not constitute a conflict of interest.

It appears that Mr. B Inlaw and Dr I Dontcare may have put their interests as shareholders before their duties as directors by ignoring faults with the Company, its equipment and the needs of creditors in an effort to cut costs, and by default, cut corners. Based on the case, this cost cutting was at the expense of the employees' safety.

Integrity

The ethical principle of Integrity appears to have been violated.

A fiduciary should act with the highest level of integrity by being straight forward, honest, and truthful; and by adhering to high moral and ethical principles in all aspects of their professional practise.

As outlined above under Breach of Fiduciary Duty, both the directors violate this duty to their employees and to the Company; and Mr. Relation has violated his integrity as highlighted under Conflicts of Interest.

Under this principle, the directors have failed to treat all parties fairly, namely the employees. Similarly, they have defrauded the creditors by continuing to trade while in difficulty, employing an IP that is not independent, and issuing bonuses to themselves.

This has the adverse impact of eroding the estate at the expense of creditors and other shareholders who are not also directors.

Objectivity, Independence and Impartiality

The next ethical principle that seems to have been breached is that of Objectivity, Independence and Impartiality.

Under this principle, an IP must be independent in fact and in appearance and avoid situations that will likely result in a conflict of interest.

It is clear that Mr. Relation is not an independent party due to his relationship with Mr. B Inlaw – he is the brother-in-law of Mr. B. Inlaw and the godfather to his daughter. Similarly, Mr. Relation has represented the directors and the Company in the past.

Commented [JL14]: Familiarity threat

Commented [JL15]: Not in the facts.

By hiring Mr. Relations, and in light of their relationship, Mr. Relation will be inclined to 'bury' evidence of any breach of fiduciary duty on the part of the directors. Any actions available to an administrator or liquidator against the directors to recover funds for the estate will undoubtedly be avoided.

Additionally, a breach of this principle has resulted in issues, namely, self-interest, self-review, and familiarity.

By taking the further appointment as liquidator, Mr. Relations will review the work that he performed as administrator which does not allow for a fair assessment of the Company. This will result in the consequences of the director and of the administrator going unchecked, and potential future losses to the estate. For example, an independent liquidator may raise the issue of the improper trading and payments performed by the directors and seek recoveries for the benefit of the creditors. The self-interest issue arises as Mr. Relation will be compensated twice for work done on the same Company, which will influence his behaviour. This behaviour may not be in the best interest of the creditors and Mr. Relations may be liable for the actions he takes.

Similarly, Mr. Relations have allowed and may even allow further transactions to the directors causing an unfair preference to be given.

Further evidence of this impartiality is seen in the way Mr. Relation expressed the opinion that banks should be more accommodating to restructuring proceedings and that the interest of lower ranking creditors should be preferred. In this regard, Mr. Relations is already biased even prior to his appointment as the interest of the bank will not be considered on a similar basis to the other stakeholders.

Commented [JL16]: This is an advocacy threat.

It should be noted that making a declaration, as Mr. Relation claims he will endeavor, on its own is not sufficient to resolve this issue.

Professional Behaviour

The next principle that may have been breached is that of Professional Behaviour.

Under this principle, the IP should strive to be accurate, honest, clear, succinct and timely. Due to the other issues identified above, Mr. Relations is biased in favour of the directors and has resulted in financial harm on the estate along with hiding evidence of this harm by failing to properly investigate and report any mismanagement and breaches by the directors.

Commented [JL17]: This is more care and integrity than professional behaviour.

Remuneration

As already touched on above, the principle of remuneration is affected by Mr. Relation taking both appointments – that is, Mr. Relations can be remunerated twice for the same duties. He may also not be stringent in reviewing the services of professionals.

Remediation

Some ways of remediating the issues identified above would be to:

- 1) Adopt independent directors, separate from the shareholders
- 2) Appointing an administrator that is not closely related to the Company or its directors
- 3) Appointing a liquidator that is not the same administrator
- 4) Appointing an independent liquidator to act jointly

Commented [JL18]: You have identified some of the facts that would give rise to the ethical issues but do not always link the facts to the ethical mischief. Moreover, your answer is slightly confused as you reference the conduct of the directors and not that of the CIP.

7

*** End of Assessment ***