



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

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

Question 1.4

Commented [JL1]: TOTAL:40 out of 50
Well done!

Commented [JL2]: 10 out of 10

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]: 6 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?

In an insolvency context the principle of fair dealing, which relates to fair or equitable treatment, requires like categories of stakeholders (e.g. unsecured creditors) to be treated equally. It will not be possible to treat all stakeholders equally, since the applicable insolvency laws will usually require some classes of creditor (e.g. those with preferential debts) to be preferred over other classes.

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 two prongs of the duty to act with independence and impartiality might be classified as “internal” (connected with the IP him/herself) and “external” (connected with other people). The former requires the IP not to have any conflicts of interest. The latter requires the IP not to allow another party to exercise undue influence so as to override his or her professional and/or business judgment in the execution of his or her duties.

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This question required a discussion of independence in fact and independence in appearance.

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.

A contingency fee arrangement (CFA) is a form of results-based payment, colloquially known as a success fee. The IP’s fee will depend on whether he or she achieves particular outcomes (contingencies) for the debtor company.

CFAs are controversial in many areas, not just for IPs, because they are often regarded as giving rise to a conflict between the fee earner’s desire to get paid and the best interests of the paying party and any third parties concerned. In the case of an IP, the IP should always be seeking to act in the best interests of the creditors (although the IP may take into account the interests of other stakeholders). The IP should not require any financial incentive to act in the creditors’ interests and should not be incentivised to achieve any outcomes other than those which are in the interests of the creditors. For this reason, CFAs should not only be unnecessary, but might in some circumstances conflict with the IP’s obligations to creditors. Issues might also arise if the contingencies on which the CFA is predicated divert the IP’s focus away from a holistic approach to the insolvency.

A CFA might be permissible or even desirable, however, where it is predicated on a really extraordinary outcome, or where it is blended with e.g. a reduced hourly rate in order to mitigate the potential distortion of the IP's objectives in the insolvency.

Where an IP thinks there is a risk that a CFA might prevent him or her from properly discharging the duties and responsibilities of an IP, the CFA should be rejected and an alternative fee agreement reached.

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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.

The duty of professional and technical competence is the third duty in the INSOL International Ethical Principles document. It is also reflected in the UNCITRAL Legislative Guide on Insolvency Law (p. 174 para. 35) and the World Bank's Principles and Guidelines for Effective Insolvency and Creditor Rights Systems (principle 35, *Competence and Integrity of Insolvency Administrators*). Further, it is likely that the contract pursuant to which the IP performs his or her role will contain a contractual duty of care, whether express or implied, and the IP might be personally liable for a breach of that duty.

The INSOL Ethical Principles document explains that the duty of professional and technical competence may be complied with by (1) keeping abreast of legislative/regulatory changes; (2) undertaking CPD; and (3) undertaking sufficient case work to remain experienced. This might be regarded as too focused on knowledge, but the INSOL commentary clarifies that the duty also covers practical matters such as sufficient time and attention to devote to a case.

The duty requires the IP to reflect on his or her own skills, knowledge and expertise, and to consider whether any new instruction falls within their competence.

The close relationship between the duty of professional and technical competence and the duty of care, skill and diligence assumes particular importance because of the financial distress of the debtor company. The IP must act with due care and the creditors and other stakeholders must be able to rely upon that if the insolvency system is to be effective.

Applying ordinary principles of professional negligence, the yardstick in England and Wales of whether an IP acted with the necessary care, skill and diligence is that of the ordinary, skilled IP. Specifically, an IP is not to be judged "by the standards of the most meticulous and conscientious of his profession. In order to succeed the claimant must establish that the [IP] has made an error which a reasonably skilled and careful [IP] would not have made" (*Re Charnley Davies Ltd* [1990] BCC 605, 618). That case concerned an administrator, but the same standard applies to a liquidator (*Re Mama Milla* [2014] EWHC 2753 [28]).

In assessing the objective standard of an ordinary, skilled practitioner, no allowance will be made for lack of seniority (cf *Nettleship v Weston* [1971] 2 QB 691). The test, which can be read across from professional negligence generally, is whether the defendant "has acted in accordance with a practice accepted as proper by a responsible body of professional people skills in that particular art" (*Bolam v Friern Hospital Management Committee* [1957] 1 WLR 582). In reaching its decision, the court may have regard to codes of practice and guidelines from industry bodies like [INSOL](#).

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?

The primary points for the IP to bear in mind are (1) his or her competence – the IP may not be legally qualified and points of law may arise, for example, about whether certain sums fall within or outside the estate, in relation to which legal advice may well be required; and (2) the value which the IP is providing to creditors. The IP owes a fiduciary duty to act in the best interests of the creditors. As such, the IP should act prudently and certainly not waste money on duplicated professional services or exorbitant legal fees. That may be a particular challenge in cities like London or New York, where legal fees are notoriously high. To mitigate the risk of excessive legal fees diminishing the funds available to return to creditors, the IP should exercise his or her judgment as to what would be prudent, and monitor the fees claimed by professionals working on the transaction (see e.g. the Australian case of *Re Korda; in the matter of Stockford Ltd* (2004) 140 FCR 424, 443 at paragraph 51).

In England and Wales, rules and advice for the procurement of specialist advice and services are provided by the regulator for chartered accountants, the ICAEW. While not all IPs are chartered accountants, the document could also be of assistance as guidance to non-chartered accountant IPs who are seeking to instruct (or advising the debtor company to instruct) a legal professional in relation to an insolvency. The rules and advice are contained in the ICAEW Code of Ethics 2020. The relevant provisions of the Code of Ethics include the following:

R2320.3: When an insolvency practitioner intends to rely on the advice or work of another, from within the firm or by a third party, the insolvency practitioner shall evaluate whether such advice or work is warranted.

R2320.4: Any advice or work contracted shall reflect best value and service for the work undertaken.

The supporting advice (2320.4 A) explains that relevant factors in assessing value and service include cost, expertise and experience of the advisor, regulatory authorisation of the advisor and the professional and ethical standards applicable to the advisor. In the case of legal professionals practising in English and Welsh law, all will be bound by the SRA/BSB professional and ethical standards and all will be regulated, so the latter two points of advice might be of little practical use in the appointment of legal professionals.

R2320.5 The Insolvency practitioner shall review arrangements periodically to ensure that best value and service continue to be obtained in relation to each insolvency appointment.

R2320.6 The insolvency practitioner shall document the reasons for choosing a particular service provider. This rule must surely have been written by a lawyer, but it reflects the important duties of record keeping and transparency on an IP.

It may also be the case that the IP and legal professional regularly work together. Where that is the case, the IP should consider whether he or she is in fact able to maintain independence, and also whether he or she will be perceived as properly independent of the legal professional.

This question might arise particularly in situations where the “Big Four” UK audit and accountancy firms provide insolvency services and also provide in-house legal services on the same transaction (this point is hinted at by the ICAEW Code of Ethics advice at 2320.6 A1).

Commented [JL9]: 7

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

Commented [JL10]: 9 out of 15

WeBuild Ltd is a private company registered in Eurafriodia. 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.

Directors trading in financial difficulty without taking action to remedy the company's finances

In many jurisdictions it is unlawful to trade once insolvency becomes likely. At any rate, directors will owe a range of fiduciary duties to act reasonably carefully in the best interests of the company. On the face of it, there seems to be a credible case that, by taking no action to remedy the company's dire financial position and reputational issues, the directors breached those duties and, as a result, have driven the company into insolvency.

There may be remedies against the directors under the insolvency law of Euraficlia to restore some or all of the value lost by the directors' misconduct to the estate. Remedies might include setting aside voidable transactions. There may also be claims against the directors personally in the non-insolvency law of Euraficlia, e.g. for breach of the directors' fiduciary duties.

Independence and impartiality of Mr Relation

Perhaps the most glaring ethical issue are the questions which hang over Mr Relation's independence and impartiality. Independence and impartiality are core responsibilities of any IP which are essential to maintain creditor and public confidence in the insolvency system. The duty of objectivity, independence and impartiality is principle 2 of INSOL's Ethical Principles for IPs. It is also the subject of rules and advice by the ICAEW (R2311.1 and following).

Questions initially arise over Mr Relation's independence because of the family relationship between Mr Relation and Mr Inlaw. There is also the quasi-familial godparent relationship with Mr Inlaw's daughter. The INSOL commentary on the Ethical Principles explains that a family connection will generally give rise to concerns about independence. Although Mr Relation declared the relationship and came to the view that he was able to act independently and impartially, his approach to the directors meeting (dealt with in section 3 below) in which he assured the directors that they would not be the focus of his work, must surely call into question whether Mr Relation is in fact able to act independently and impartially. As is often said of the courts, justice must not only be done but seen to be done. The same sentiment applies forcefully to IPs. In my view, Mr Relation would be better advised to decline the instruction. That response would probably be reinforced if Mr Relation asked himself, why have I been asked to advise? Why have I been appointed, when there are thousands of IPs who could have done the job? In all likelihood, he would conclude that he had been asked because of his personal relationship with Mr Inlaw.

Commented [JL11]: This is irrelevant to the question of the IP's ethical conduct.

Commented [JL12]: What about his declaration of independence?

In addition, Mrs Keeneye has reasonably raised a question over Mr Relation's impartiality. Given Mr Relation's television interview in which Mr Relation expressed the view 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), a reasonable person might have legitimate doubts about whether Mr Relation would approach an insolvency in which a financial institution was a major creditor with the requisite impartiality and dispassionate objectivity demanded of an IP by the duty of fair dealing. Having said this, we have no instructions about when that interview was or what the circumstances were, and it is not impermissible for IPs to give broadcast interviews or express views in the media, as long as they do not break client confidentiality.

Assurance at the "planning" meeting between the directors and Mr Relation

A third issue is the lack of transparency around the "planning" meeting. Transparency is an essential aspect of the fiduciary role. The question does not state whether a record was kept of the meeting and/or whether the shareholders were subsequently informed of the meeting, but the thrust of the question seems to be that the meeting was surreptitiously conducted behind the backs of shareholders and creditors.

The assurance that the directors would not be Mr Relation's focus was given before Mr Relation had informed himself (or properly or adequately informed himself) of the company's affairs. Given that he and/or the company might have claims against the directors which, if successful, could increase the money in the estate which is available for distribution to the creditors, it is inexplicable that Mr Relation gave this assurance.

More concerning, the assurance appears to be borne out because Mr Relation informed the creditors that he had found no evidence of wrongdoing or maladministration by the company's directors – an assertion which seems improbable on the limited facts available. Overall, it appears that Mr Relation has failed adequately or diligently to discharge his duties to the creditors.

Commented [JL13]: Which ethical norm or duty does this relate to? Isn't it also independence and impartiality?

Commented [JL14]: A reasonable attempt at identifying and discussing the issues. Not all the facts are correctly linked to the ethical norms. Other issues that could have been mentioned pertain to professional competence and the duty of care as well as the subsequent appointment as liquidator.

*** End of Assessment ***