



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]: 8 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?

The concept of fair dealing relates to treating everyone equitably so as to have a fair outcome. Insolvency does not treat all stakeholders in the same way, in fact it deliberately distinguishes between stakeholders depending on their ranking in the insolvency waterfall. However the IP is required to deal fairly between members of the same class and should also deal fairly as between classes so as to be open and honest with all stakeholders.

Commented [JL4]: 2

Question 2.2 [maximum 4 marks]

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

An IP should be under a duty to ensure that he has high levels of independence and impartiality. He should not allow any bias or conflict of interest or influence from any source to compromise the discharge of his duty as IP.

Impartiality has two aspects, in fact and in perception. The IP must ensure that he is not influenced in any improper way by any relationship he has either from work or personal life, that he has no actual interest in any connected party or entity that might relate to the IP's appointment so as to avoid any influence that might possibly change any action he undertakes as IP. Secondly, and as importantly, he must be perceived by all stakeholders to have independence of judgement irrespective of whether, de facto, he is influenced by something. If a reasonable person could believe that the IP is influenced by a factor outside his professional judgement then that would undermine the perception of impartiality of the IP and therefore the trust in that process to which the IP is appointed. Any actual or perceived undue influence on the IP would result in the stakeholders losing faith and probably cooperation in the process. This would result in any rescue proceeding being compromised to unworkability and the risk of challenge to any rescue or liquidation by a stakeholder high. For this reason many jurisdictions prescribe in their professional IP standards or rules Ips taking appointments in circumstances where certain connections exist between the IP and the parties connected to the IP appointment.

Commented [JL5]: 4

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 arrangements are an arrangement whereby you are paid in relation to your success. What 'success' equals is something that needs to be considered in the context of the appointment however it is usually related to a threshold outcome and then there is an element of 'success fee' ties to the amount of access achieved. For many years these type of arrangements were prohibited in the remuneration of lawyers in disputes because it was considered ethically unaligned to achieving the duty to the court to act in the best interests of your client because your client's interest may not result in the best outcome for the fee arrangement (for example a settlement may not result in a contingent fee arrangement being triggered or may result in a lower fee than the lawyer may consider it would achieve by a successful damages award at trial, nonetheless not going to trial may be in the interests of the client in the context of lower legal fees, less stress and less risk).

The issue of contingency fee arrangements in the insolvency context are even more difficult, unlike litigation the IP is appointed to act in the best interests of the community of stakeholders albeit in a ranked manner. Therefore achieving the best restructuring or maximising the insolvent estate is the essence of the appointment of the IP anyway. How you can quantify an outcome that is for the benefit of all beyond maximising the recovery of the estate (which is the general duty of the IP in any case) is therefore very difficult. Even a fee that includes an uplift for a rescue may not necessarily be in the best interests of the population because it occludes the perspective of the IP from taking a truly objective perspective of what is in the best interest of the community of stakeholders. For that reason I am not in favour of success fees in the context of an IP appointment (however I can see that they may have a use in the context of a secured lenders appointment of a receiver over assets).

Commented [JL6]: Are there any circumstances when it would be appropriate?
2

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

Commented [JL7]: 13 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 ethical principal of professional and technical competence means that an IP should have the relevant levels of technical expertise and relevant experience to perform their appointment properly. This is expressed in Principle 3 of the INSOL Principles for IPs.

The INSOL Principles are drafted to reflect the generally held consensus that Ips hold a role that is at least akin to being a fiduciary (see J Glover & J Duns 'Insolvency at General Law: Fiduciary Obligations of Company Receivers, Voluntary Administrators and Liquidators' or D Milman 'Governance of Distressed Firms'). In many jurisdictions IPs have had fiduciary status imposed on them by local laws or regulations. As a general rule fiduciaries must carry out their role in the best interests of the beneficiary and to discharge that standard must apply to themselves a high standard of behaviour in order to discharge their duty of care. In courts of equity (i.e. those who take origin from the English common law) the duty of care is generally measured in two ways, objectively and subjectively. Objectively would mean that the IP carried out its functions in a manner that an objective standard is met. In a sense this

provides a floor to the standard of the duty of care, it can be no lower than that of an objective view of an IP carrying out its duty. Often the concept of reasonableness is applied in this context, would a reasonable IP carrying out this role do. The subjective standard is to look at the specific context and abilities of that IP and judge whether the IP has discharged his or her particular skills to a standard that is at least the skills he or she possess. In that context factors such as the support of any organisation that they are a member of (such as an accountancy firm) would be relevant.

In essence the INSOL Principals are an attempt to document what the duty of care means in the context of an IP and its role. In judging the discharge of a role by an IP against the INSOL Principals both an objective and a subject standard should be used as relevant.

Without relevant knowledge and experience an IP will be unable to perform the role properly. This expectation is reinforced by the fact that IPs are paid as specialist experts not as laymen. Therefore, INSOL have incorporated Principal 3 to reflect that an IP must have the requisite level of skill and knowledge in order for it to meet an objective threshold to discharge the duty of care of a fiduciary. This is something that is similarly imposed on other professional relationships where a fiduciary duty is present, so accountants and lawyers are required to undergo continuing professional development once qualified in order to maintain the appropriate levels of skill and knowledge to properly discharge their duties to their clients.

Therefore, as a part of discharging their duty of care to the stakeholders, it is entirely correct that an IP be held to an objective minimum standard of competence for role of this level of complexity and responsibility. It is also proper that the IP should be judged against his or her own levels of particular experience and expertise, not least because many IPs are appointed to particular insolvency situations on the basis of a need to have a particularly deep understanding of the type of industry or the particular insolvency process being used. Therefore it is appropriate to ensure that they apply the high levels of technical expertise that they should possess for that role.

Commented [JL8]: A complete answer would have referenced the UNCITRAL legislative guide as well as case law on the topic. A good attempt.
6

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 can be lawyers by training and practice but frequently are not. Most frequently they come from the accountancy profession. Insolvency processes to which IPs take roles are by their nature laid down in law. They also frequently require a legal advisor either to assist with the legal process of an insolvency (whether that be a pre-pack using a scheme of arrangement or a liquidation involving issues of claim or ranking) or to assist with interpreting the law in a particular fact situation. This is even more acute in the common law world where a deep understanding of legal precedent is required on top of an understanding of the statute. Clearly a failure by an IP to apply the law to a situation would be a abrogation of his duty of care to stakeholders and may well give rise to personal liability. It is therefore proper that, with good judgement as to necessity, cost and appropriateness, an IP should be able to rely on legal advice in the discharge of his or her role.

Having established that there are situations in which it is perfectly reasonable for an IP to retain lawyers and for that to be a cost of the insolvency process it is necessary to consider where it may be problematic.

Firstly there is the issue of whether to engage lawyers or not in the first place. The IP, from its own personal perspective, may find having legal advice attractive because it offers a way to demonstrate, through a third party, that the IP is discharging his duty properly. However such legal advice is not generally for the benefit of the stakeholders of the insolvency process but in the interests of the IP in its own capacity. As such it is important for the IP to distinguish situations where it is in its own interest to have legal advice from those in which it is in the interests of the stakeholders. Of course there may be situations where it is in both interests and in that situation the IP may proceed to get legal advice recognising it is primarily for the benefit of the stakeholders.

Secondly, care must be taken to ensure that the work of the lawyers is not duplicative of work done by any other person (in particular the IP) involved in the process. This was the issue examined in the *Dovechem* case in Singapore. The important outcome of that case was that the IP had to demonstrate that the solicitors to the IP's work was not duplicative to that of the IP. In that case that was shown to be so. In England and Wales the Insolvency Code of Ethics issued by the Institute for Chartered Accountants of England and Wales deals specifically with this issue. This Code required the IP to keep a record of why it chose a specific service provider. It sets out a threefold test to consider:

- (a) It needs to examine the cost of the service, the expertise of the provider and the experience of the provider;
- (b) Consider whether or not the provider has necessary regulatory approvals to carry out the work; and
- (c) Consider what professional and ethical standards must be applied by the service provider.

This test is useful for an IP to consider when it comes to appointment of lawyers.

The most contentious issue in relation to instructing lawyers is likely to be their cost. These can either be claimed as a disbursement for the IP's own role or as a cost directly to the debtor estate. Either way they are a cost on the estate and therefore must be considered carefully. When instructing lawyers the IP must ensure that they are the appropriate lawyers for the case, that their costs are reasonable to the market and that they are properly monitored for their incurrence. Finkelstein J discussed this issue in the *Korda* case. Finkelstein J discussed this issue in the *Korda* case when he said an IP should exercise commercial judgement in the choice of lawyers and, if he is prudent, monitor the fees claimed.

In summary, legal advice is reasonable in many insolvency situations. However, a prudent IP would follow the advice laid out in the Insolvency Code of Ethics and be able to demonstrate the reasons the legal advice was needed and why he choose the lawyer he choose. The IP should also keep records of how he monitored the legal fees to ensure that they offer good value.

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

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

Commented [JL9]: 7
An excellent answer, thank you.

Commented [JL10]: 12 out of 15

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.

This scenario raises a number of ethical issues to consider. There are a few pertinent facts worth drawing out. Firstly the directors

Firstly, at the initial meeting the facts state that Mr Relation, a lawyer, was there to provide the shareholders and the directors legal advice in relation to their options. At this point Mr R is not acting in any way as an IP. Nonetheless as a lawyer he shares similar fiduciary obligations to an IP and it is not clear who he client is in this situation. The interests of the Company when insolvent are generally those of its creditors, as a rule the board needs its own advice as to the position of the directors in this insolvent situation and lastly the shareholders may want their own advice as to any recover or recourse actions they may (or may not) have. Who he is advising will have a bearing on his appointment at IP as it could create a conflict of interest.

If Mr R has been advising the company at the meeting there is no absolute bar on his going on to be the IP in an insolvency process but must ensure his objectivity, independence and impartiality and must avoid conflicts of interest (Principle 2 INSOL). This, for example was the issue in the *Re Korda* litigation in Australia where the court recognised that pre-appointment work, subject to the safeguards it set out, may be entirely in the interests of the overall stakeholders. However, if this is the case then, as the court in *Korda* held, it is important that the pre-appointment work was general in nature and did not involve advice to any particular stakeholders (to which I refer to my comments above on Mr R's role as solicitor).

The duty to avoid actual or perceived conflict of interest is clearly brought into play in this situation because of the familial relationship between Mr R and Mr B Inlaw. The presence of a familial relationship at least raises a presumption of a lack of impartiality and should be avoided if you wish to remain in compliance with the INSOL Principal 2. The fact that a relationship is declared does not cure any actual conflict of interest nor would it cure the perception of a lack of impartiality on behalf of stakeholders. In the circumstances where his brother in law may behaved in a way so as to cause personal liability to himself, Mr R should have recognised the potential for a conflict of interest and not taken the appointment.

Having been appointed the next action taken by Mr R was to attend a meeting with the directors at their request. Clearly Mr R is now administrator owing duties to all the stakeholders and, depending on the jurisdiction, the courts. This meeting appears to be in breach of a number of the INSOL principals, Clearly meeting with one group behind closed doors is not acting within Principal 2's obligation to act with impartiality. Further more his suggestion that he would focus on the rescue and not director liability also falls out with Principal 2 as it is not acting with impartiality, objectively or independence. Principle 1 of the INSOL principals requires IPS to be straightforward, honest and to demonstrate the highest levels of integrity. Meeting with the directors in this way and making them promises without considering the wider stakeholder group's interest is not acting with high levels of integrity as integrity in this context puts an onus on Mr R to acting fairly.

Mr R is acting as a fiduciary in his role at IP to the stakeholders in the insolvency process. As a fiduciary he has a high burden of care towards the stakeholders and must discharge that duty with care, diligence and skill. Failure to do that would compromise his integrity under Principal 1. Mr R fails to adequately investigate the affairs of the company and relies upon the report given to him by his brother in law. This has elements of a failure to discharge his duty of care to the stakeholders combined with a conflict of interests as discussed above.

Mr R states that he has found no evidence of maladministration by the directors. We know from the fact pattern that that is because he has failed to adequately or independently investigate the behaviour of the directors as referred to in the last paragraph. Making this

statement is also a breach of Principal 1 on integrity as no reasonable man would agree that he has discharged his duty of care in a manner to give rise to his being able to make this statement.

Mrs Keeneye has concerns relating to this previous statements on big banks. This also gives rise to the presumption of a conflict of interest under Principal 2. In this case it is the perception of a conflict of interest that has arisen and one that he should have considered prior to taking any appointment.

Lastly Mr R should not have been appointed as a liquidator. There is a clear potential for a conflict of interest that arises when a company goes into liquidation after a rescue process and it is fair and reasonable to expect that any liquidator would need to assess the actions of the rescue administrator in managing the business and drawing up a rescue plan when considering his obligations towards the liquidation estate. Clearly that cannot happen if the same person holds both roles.

Commented [JL11]: A clear and well-reasoned answer. I would have liked to see clearer explanations as to why there are breaches in some instances, but an overall solid attempt.
12

*** End of Assessment ***