Association of Business Recovery Professionals

8th Floor
120 Aldersgate Street
London
EC1A 4JQ

T: 020 7566 4200
F: 020 7566 4224

E: association@r3.org.uk
www.r3.org.uk

Rescue
Recovery
Renewal

Professor Prem Sikka
Emeritus Professor of Accounting
University of Essex
Wivenhoe Park
Colchester
CO4 3SQ

6th September 2018

Dear Professor Sikka,

Independent review of the UK's corporate audit and accounting framework

I write as President of the insolvency and restructuring trade body R3, to provide a response to your independent review of the UK's corporate audit and accounting framework. Our enclosed submission sets out some facts and our views on a number of issues you are keen to address; we would be happy to provide more detail on any specific section. We're keen to be as open and helpful to you as possible, answering any questions you have about our profession and its framework.

By way of background, R3 is the trade association for the UK's insolvency, restructuring, advisory, and turnaround professionals. We represent licensed insolvency practitioners, lawyers, turnaround and restructuring experts, students, and others in the profession. Our members work across the spectrum of the profession, from the global legal and accountancy firms through to smaller, local practices. Our members have direct experience of insolvencies and their impact on the UK economy and insolvent companies' stakeholders.

The insolvency, restructuring and turnaround framework and profession is a vital part of the UK economy. The profession rescues businesses and jobs, creates the confidence to trade and lend by returning money to creditors after insolvencies, investigates and disrupts fraud, and helps indebted individuals get back on their feet. The World Bank ranks the UK's insolvency and restructuring framework as one of the best in the world.

R3 recognises the considerable public interest, following a number of high profile business failures over recent years, in the ability of the UK's corporate audit and accounting framework to provide employees, shareholders, stakeholders, government and the public with confidence that businesses accurately report financial performance and justify decisions taken by directors. The insolvency and restructuring framework is a key part of that debate and as such we're very keen to assist with your review over the coming months. We have also been meeting regularly with the APPG on Fair Business Banking, which as you know has raised concerns about the insolvency framework.

We would be happy to arrange a roundtable discussion between you and a small number of senior insolvency and restructuring professionals if you would find it helpful during the review, or would welcome a one to one meeting if that would be of more use.

We hope that this response is helpful to your review and would be very happy to discuss these matters further. Please contact R3's Public Affairs and Policy Officer, James Jeffreys, at james.jeffreys@r3.org.uk or 020 7566 4220, for further information.

We look forward to meeting and working with you over the coming months.

Yours sincerely,

Stuart Frith
R3 President

Enc.

Contents

Introduction and overview

Given that your review intends to make recommendations for wider reform of the UK's corporate audit and accounting framework, we wish to set out in full how the current regulatory framework for insolvency operates, so as to provide a basis from which to consider and evaluate what possible future reforms might be needed.

The UK's insolvency regulatory framework is well established and the insolvency and restructuring profession is subject to close scrutiny by its regulators. The profession is also expected to abide by strict ethical guidelines at all times.

An effective regulatory framework is as important to the insolvency and restructuring profession as it is to debtors, creditors, and other stakeholders. Like others, the profession values regulatory consistency, speed, and transparency. It is crucial that standards are upheld across the profession and that those who fall short face the consequences of doing so.

The role of an insolvency practitioner

The insolvency profession works with thousands of financially distressed and insolvent companies and individuals every year. This can be in a statutory or non-statutory capacity. Statutory insolvency procedures under the Insolvency Act 1986 can be started by an insolvent company's shareholders, directors or creditors when it can be shown that the company cannot pay its debts as they fall due, or if its liabilities outweigh its assets. Typically the purpose of an insolvency procedure is to return as much money as possible to *all* creditors in a regulated and planned manner after a company has become insolvent. This objective can be achieved by winding up or rescuing the company. Insolvency practitioners are the only individuals licensed to take insolvency appointments as an 'office holder' under the Insolvency Act 1986 (except for the government's Official Receiver in a compulsory winding up or bankruptcy).

Licensed insolvency practitioners are bound by strict legal obligations and duties, and at all times – whether appointed as an insolvency 'office holder' or not – are subject to scrutiny from their regulator (a 'Recognised Professional Body' as referred to at page 5), which is in turn answerable to the government.

When appointed to act as an 'office holder' of a company in an administration, liquidation or voluntary arrangement, insolvency practitioners have a duty to maximise returns to the company's whole body of creditors. Insolvency practitioners are aware of the stresses of the insolvency process and will seek to work with company directors and other stakeholders to manage the process sensitively and effectively. As an 'office holder', the insolvency practitioner is not answerable to the company's directors or specifically to the creditor which appointed them. They are answerable to the company's body of creditors as a whole. As an 'office holder' in an administration or liquidation, insolvency practitioners also have the duty to review and report to the Director Conduct Reporting Service (within the Insolvency Service) on the conduct of the company's directors in the three-year period prior to the commencement of the insolvency, on which the Insolvency Service decide whether disqualification proceedings should be taken in respect of any bad conduct identified.

Once appointed as an 'office holder', an insolvency practitioner will seek to establish how they can maximise creditor returns. They will look into all aspects of the company, including whether or not the company has a claim for wrongdoing against its directors or any other parties. These claims will be pursued if they are financially viable and will help achieve the office holder's objective of maximising returns to the company's body of creditors. An insolvency practitioner is required to be independent and objective, and bring transparency to proceedings when reporting to creditors.

An insolvency practitioner's primary duty is to the creditors of the insolvent company, and every decision taken about a distressed company is made with the ultimate benefit of creditors in mind. If a creditor or any stakeholder believes that an insolvency practitioner has acted improperly, they can complain to the insolvency practitioner's regulator via the Insolvency Service's Complaints Gateway. The Gateway was set up in 2013 to act as a single entry point for complaints about insolvency practitioners and it covers complaints across the full range of insolvency procedures.
In addition, insolvency practitioners must – and do – register a complaint when they encounter misconduct by another insolvency practitioner.

The insolvency regulation framework

The role of Recognised Professional Bodies (RPBs)

Under the provisions of the Insolvency Act 1986, the Secretary of State (BEIS) recognises certain independent professional bodies (called 'Recognised Professional Bodies' - RPBs) for the purposes of authorising their members to act as insolvency practitioners.

The Insolvency Service regulates the RPBs to ensure that the members they authorise are fit to act as insolvency practitioners, as well as to ensure that the RPBs themselves are fit for purpose. The RPBs are required to have rules in place to ensure their insolvency practitioners meet acceptable education, practical training and experience requirements.

Each year, the Insolvency Service publishes an annual review of insolvency practitioner regulation which: summarises the regulatory activities of both the Insolvency Service and the RPBs over the year; collates statistical information provided by the RPBs on authorisations, monitoring visits, complaints and disciplinary sanctions; provides statistical information on the performance of the Complaints Gateway; and summarises monitoring activities and findings. The latest review was published in May 2018[1].

There are currently five RPBs, each authorising, at 1 January 2018, a number of non-appointment and appointment taking insolvency practitioners respectively:

Organisation	Total IP authorisations	Appointment takers
Institute of Chartered Accountants in England and Wales (ICAEW)	783	599
Insolvency Practitioners Association (IPA)	557	460
Association of Chartered Certified Accountants (ACCA)	94	89
Institute of Chartered Accountants of Scotland (ICAS)	93	75
Chartered Accountants Ireland (CAI)	43	41

Since 1 January 2017, ACCA has delivered the majority of its insolvency regulatory functions through a collaboration agreement with the IPA, which consolidated the complaints-handling and monitoring arrangements of the two bodies.

[1]https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/706354/Annual_Review_of_IP_Regulation_2017.pdf

There are practical and historical reasons why the current system of regulation has developed in the way it has – not least because there are three different jurisdictions (England and Wales, Scotland, and Northern Ireland) with devolved responsibility for insolvency and different insolvency frameworks. Additionally, some firms comprise a variety of professionals (such as those working on tax and audit, as well as insolvency practitioners) so they may want to ensure all their members are regulated by one body capable of covering the variety of disciplines (rather than an insolvency-specific body). Further, some insolvency practitioners have a legal rather than an accounting background and so are not members of the ICAEW or ACCA.

Any reform to the number or role of RPBs – as per the Government's power to introduce a single insolvency regulator, as referred to on page 10 – would need to take these factors into account.

Insolvency practitioner and RPB monitoring

All insolvency practitioners are subject to regular monitoring visits from their RPB. Monitors seek to establish that insolvency practitioners are adhering to the legislation, and to accepted standards such as Statements of Insolvency Practice (SIPs), the Insolvency Code of Ethics and the relevant rules and regulations of the authorising bodies.

These visits are intensive, with the first taking place within twelve months of an insolvency practitioner obtaining their licence. Visits subsequently take place between every three and five years, depending on the risk profile of the insolvency practitioner (the higher the perceived risk profile of the IP; based on previous monitoring outcomes and the type of appointments taken by the IP, the more frequent the visits that an RPB will undertake). When undertaking a visit, the RPB will look through a sample of open and closed cases to check that all of an insolvency practitioner's work has been carried out as required under the Insolvency Act 1986, the Code of Ethics, and the various SIPs, as set out below.

Monitors from the Insolvency Service visit each RPB on a regular basis (usually at least once in three years) to ensure that the RPB is complying with its commitments. If any RPB fails to meet the requirements set by the IS, the matter may be referred to the Secretary of State, which could result in its status as a recognised professional body being revoked.

The role of the Joint Insolvency Committee (JIC)

Sitting alongside the Insolvency Service and the RPBs, although distinct in its role, the Joint Insolvency Committee (JIC) develops, improves and maintains insolvency standards from a regulatory, ethical and best practice perspective.

The JIC promotes consistency across the profession. It acts as a forum for the discussion of insolvency issues and standard setting. It has responsibility for the development and revision of the Code of Ethics applicable to insolvency practitioners, Statements of Insolvency Practice and Insolvency Guidance Papers.

As shown below, the committee comprises representatives from each of the five RPBs, five lay members (most of whom represent creditors) and representatives from the Insolvency Service and the Insolvency Service Northern Ireland. R3 and the Law Society of Scotland attend JIC as observers. Other observers may attend by arrangement.

JIC member organisations	Category
Association of British Insurers	Lay member
British Property Federation	Lay member
Chartered Accountants Ireland	RPB
Chartered Institute of Credit Management	Lay member
HM Revenue and Customs	Lay member
Insolvency Practitioners Association	RPB
StepChange Debt Charity	Lay member
The Association of Chartered Certified Accountants	RPB
The Insolvency Service	Oversight body
The Insolvency Service, Northern Ireland	Oversight body
The Institute of Chartered Accountants in England & Wales	RPB
The Institute of Chartered Accountants of Scotland	RPB

The membership of creditor bodies and other stakeholders on the JIC ensures that the views and input of external bodies are heard and taken into account in the drafting and revision of the key documents setting out the ethical and practical requirements for insolvency practitioners to comply with at all times.

The Insolvency Code of Ethics

As noted above, insolvency practitioners are required to abide by the profession's Code of Ethics at all times, whether or not they have been appointed as an 'office holder'. Breaches of this code should be reported to or picked up by RPBs.

The code covers the issues which insolvency practitioners must consider carefully in their work, and sets out steps which need to be taken to mitigate risks. The fundamental principles of the code include: integrity; objectivity; professional competence and due care; confidentiality; and professional behaviour. Specific issues covered by the code include (but are not limited to): taking insolvency appointments; conflicts of interest; transparency; and professional and personal relationships.

In 2017, the JIC consulted on changes to the Insolvency Code of Ethics. The consultation received over 400 responses which, the JIC felt, having reviewed them initially, indicated that the code was not fundamentally flawed but was in need of only relatively minor amendment.

We understand that the JIC was due to publish a response earlier this year, but this was delayed due to the fact that the accounting bodies are currently updating their own guidance which is in turn linked to the global update to the ethics code. A JIC working group is currently giving further consideration to the responses to the consultation, and a revised version is expected to be issued later this year following publication of the revised accountancy code.

Statements of Insolvency Practice (SIPs)

SIPs are a series of guidance notes issued to licensed insolvency practitioners with a view to maintaining standards by setting out required principals and best practice and harmonising practitioners' approach to particular aspects of insolvency. Insolvency practitioners are required to adhere to SIPs at all times. All 17 SIPs re listed below, to illustrate the range of areas that the SIPs cover:

SIP	Subject
SIP 1	Introduction to Statements of Insolvency Practice
SIP 2	Investigations by Office Holders in Administrations and Insolvent Liquidations and the submission of conduct reports by office holders
SIPs 3.1, 3.2 and 3.3	Individual Voluntary Arrangements 3.1; Company Voluntary Arrangements 3.2; Trust Deeds (Scotland) 3.3
SIP 4	Disqualification of Directors
SIP 5	Non-Preferential Claims by Employees Dismissed Without Proper Notice by Insolvent Employers (withdrawn)
SIP 6	Deemed Consent and Decision Procedures in Insolvency Proceedings
SIP 7	Presentation of Financial Information in Insolvency Proceedings
SIP 8	Summoning and Holding Meetings of Creditors Convened Pursuant to Section 98 of the Insolvency Act 1986 (withdrawn)
SIP 9	Payments to Insolvency Office Holders and their Associates
SIP 10	Proxy Forms (withdrawn)
SIP 11	Handling of Funds in Formal Insolvency Appointments
SIP 12	Records of Meetings in Formal Insolvency Proceedings (withdrawn)
SIP 13	Disposal of Assets to Connected Parties in an Insolvency Process
SIP 14	A Receiver's Responsibility to Preferential Creditors
SIP 15	Reporting and Providing Information on their Committees and Commissioners
SIP 16	Pre-packaged Sales in Administrations
SIP 17	An Administrative Receiver's Responsibility for the Company's Records

SIPs are issued under procedures agreed between the insolvency regulatory authorities acting through the Joint Insolvency Committee (JIC). They are approved by the JIC and adopted by each of the regulatory bodies listed in the introduction to each SIP.

Complaints procedure and sanctions for wrongdoing

If creditors or stakeholders have concerns about an insolvency practitioner's conduct they can make a complaint through the Insolvency Service's Single Complaints Gateway. Insolvency practitioners face sanctions, including fines or the loss of their licence, for wrongdoing.

Complaints about insolvency practitioner conduct occur in only a very small minority of cases. In 2017, there were **99,196** personal and **17,243** corporate insolvencies (some of which were handled by the Official Receiver as well as insolvency practitioners); in that year, there were a total of 757 complaints about insolvency practitioners to the Complaints Gateway, of which **308** were deemed appropriate to be referred to the RPBs (the Insolvency Service gives a number of reasons why complaints are rejected: no response received from complainant to follow up request for further information; the complaint was about the effect of the insolvency procedure; the complaint was not about an insolvency practitioner; the complaint had already been through the complaints process). A further 86 are on hold while the Gateway seeks further information from the complainant.

In its 2017 review of insolvency practitioner regulation, the Insolvency Service notes that the latest figures "demonstrate a downward trend in the total annual complaints received...in 2017 we received a total of 757 complaints, compared to 847 in 2016." While the profession should not be complacent about this trend, it is positive to see that the number of complaints fell during this period.

Sanctions

As set out in the Insolvency Service's Common Sanctions Guidance[2], which aims to ensure consistency between the RPBs regarding sanctions, once an RPB has investigated the conduct of any insolvency practitioner it licenses, it can (under its own disciplinary processes) impose sanctions on that licence holder. Such sanctions can follow an investigation of a complaint, or can be a result of a finding on a monitoring visit carried out by the RPB or following the receipt of any other intelligence.

The circumstances that lead to a complaint and the issues that arise as part of the complaint will vary, possibly significantly, on a case-by-case basis. Not all complaints about an insolvency practitioner lead to them being disciplined. For example, errors of judgement and innocent mistakes are not generally considered to be misconduct. If, however, an insolvency practitioner has made a serious error or a repeated number of less serious errors, this may mean they have performed their work inefficiently or incompetently to such an extent or on such a number of occasions as to have brought discredit to themselves, their RPB, or the insolvency profession.

Although the aim of the Common Sanctions Guidance is to ensure consistency of approach, it is not prescriptive and does not bind each RPB's processes to a fixed sanctions regime. Although it gives an indication of the level of sanction to be imposed, each RPB's disciplinary committee or tribunal will use its own judgement to set a sanction appropriate to the circumstances of the individual case.

When a disciplinary committee or tribunal considers what would be an appropriate sanction, it will refer to the guidance and may, within its discretion, vary the sanction depending on aggravating and mitigating factors.

When a disciplinary committee or tribunal decides that a complaint has been proved or where it is admitted, the committee or tribunal will decide the appropriate sanction. If the committee or tribunal decides a penalty (for example, exclusion, reprimand or a fine) is necessary, it will identify the relevant category of complaint and the relevant behaviour.

There are two types of sanction available to the disciplinary committee or tribunal: non-financial sanctions and financial sanctions. Non-financial sanctions range from a reprimand, severe reprimand, and suspension of a licence or membership, to withdrawal of a licence (which is career ending), and exclusion from membership, as set out in the RPB's bye-laws. For each type of complaint there is a suggested starting point for a financial sanction, ranging from £1,500 to over £20,000.

Further, since 2014, all published disciplinary sanctions are included on the Insolvency Service's website. The publication includes details of the IP, the nature of the complaint, the finding and any sanction together with reasons for the decision including aggravating and mitigating factors considered as part of that decision.

For example, in March and April this year, five insolvency practitioners incurred financial sanctions of £6,500, £5,000, £1,500, £1,500, and £14,500 respectively. Another insolvency practitioner had their licence restricted.

---

[2] https://www.gov.uk/government/publications/disciplinary-sanctions-against-insolvency-practitioners/common-sanctions-guidance

Given that this information is publicly available and publicised by the Insolvency Service, these sanctions can have substantial reputational, as well as financial, implications.

The Small Business, Enterprise and Employment Act 2015 and the Government's power to introduce a single regulator for insolvency

The last major set of reforms to insolvency law were introduced through the Small Business, Enterprise and Employment Act 2015 (SBEE), with the aim of increasing creditor engagement and to remove administrative burdens in insolvency processes. Among a number of other changes, SBEE:

- Introduced a set of statutory objectives for the regulation of insolvency;
- Strengthened the regulation of insolvency practitioners and the Insolvency Service's role as oversight regulator;
- Reformed the authorisation of insolvency practitioners, allowing them to be authorised solely in relation to personal insolvency, corporate insolvency or both;
- Extended the powers of administrators to raise bring fraudulent or wrongful trading actions;
- Introduced a requirement in England and Wales for insolvency practitioners to obtain an up-front estimate of fees agreed by creditors when wishing to operate on a time and rate basis, with any subsequent variation to this estimate requiring agreement by creditors;
- Brought up to date the qualifying monetary amounts for Debt Relief Orders (DROs) and creditors petitions for bankruptcy in England and Wales, allowing greater access to debt relief for financially distressed individuals.

Single regulator

Of most relevance to this review, however, was the power granted to the Government through the SBEE, to establish a single regulator for the insolvency profession, by 2022. Practically, a decision to use this power will be made by 2020; we understand that the Insolvency Service has already begun work on its review to recommend to the Government whether or not to exercise this power.

R3 does not have a position on whether there should be a single regulator, but we are currently consulting with members, who have a variety of views about the future shape of insolvency regulation. Whatever form this takes, R3 would like to see a regulatory framework which, as set out above, is: fair and proportionate; transparent; effective; efficient; flexible; and consistent.

Current Government proposals for reform of the UK's corporate insolvency framework

Since SBEE being passed into law, the Government has issued two consultations proposing major reform of the insolvency framework: the first, a consultation on reform of the corporate insolvency framework[3], was published in May 2016; more recently, the Government published its insolvency

[3] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/525523/A_Review_of_the_Corporate_Insolvency_Framework.pdf

and corporate governance consultation[4] in March this year. The Government published a joint response to both consultations on Sunday 26th August 2018[5].

In making suggestions for reform of the corporate audit and accounting framework, and indeed the framework for insolvency regulation, your review may wish to refer to the proposals contained in these consultations that the Government has now confirmed it will take forward.

Corporate insolvency framework reform

The Government's 2016 consultation on reforming the UK's corporate insolvency and restructuring framework contained proposals which were designed to boost business rescue and ensure the UK's framework remains internationally competitive and attractive. The UK's insolvency and restructuring profession supported the reforms and believed that, with modifications, they would ensure the UK maintains its position as a leading global insolvency and restructuring hub. In its recent consultation response, the Government confirmed that it would introduce:

- A 28 day moratorium from creditor action for struggling businesses to allow them time to put in place an appropriate rescue plan;

- New 'essential supplies' rules to help businesses to continue trading in a rescue process; and,

- A new court-based restructuring procedure, similar to the US's Bankruptcy Code Chapter 11 under which a US company or partnership usually prepares a plan of reorganisation to keep its business alive and pay creditors over time (http://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-11-bankruptcy-basics).

The moratorium in particular could be helpful in supporting business rescue (by allowing smaller suppliers or contractors affected by the insolvency of a major customer the time to consider their options and develop a rescue plan) while also helping to address concerns around creditor and stakeholder engagement in corporate insolvency procedures such as Company Voluntary Arrangements (CVAs), for example, by enabling directors to engage more fully with creditors without the fear of a hostile creditor action (such as the issuing of a winding-up petition) which could curtail attempts to rescue or restructure a business.

In light of growing competition from other countries and the risks of barriers to resolving cross-border insolvencies in light of Brexit, R3 is calling on the Government to introduce these reforms before the UK leaves the EU. Doing so would be of substantial benefit to the UK economy, given the role that an economy's restructuring and insolvency framework has in influencing where international companies choose to base themselves, where in the world capital is invested, and where companies choose to trade.

Insolvency and corporate governance

Published earlier this year, the Government's insolvency and corporate governance consultation appears to be in reaction to a number of recent high-profile insolvencies and corporate governance failings. To address these, the Government proposed, in short, to:

---

[4] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/691857/Condoc_-_Insolvency_and_Corporate_Governance_FINAL_.pdf

[5] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/736163/ICG_-_Government_response_doc_-_24_Aug_clean_version__with_Minister_s_photo_and_signature__AC.pdf

- Require directors of parent companies, which have sold a subsidiary, to make a contribution to the subsidiary's creditors in the event that the subsidiary becomes formally insolvent within two years of the sale, where the subsidiary was insolvent at the time of the sale, and where the formal insolvency was reasonably foreseeable at the time of the sale;

- Create new powers for office holders to reverse examples of 'value extraction' where, following fresh investment, investors or others have arranged restructurings or transactions to protect themselves against losses in the event that the company subsequently becomes insolvent, and where these have not added value to the company in receipt of the investment; and to

- Expand the director disqualification regime to include directors of dissolved companies (being companies struck-off the Companies House Register) in addition to directors of insolvent companies.

The consultation also included questions about directors' awareness of their responsibilities, the 'prescribed part' (see page 13), and the position of SMEs as creditors in large insolvencies.

R3 raised a number of concerns[6] around these proposals, which looked to create significant new liabilities and risks for directors that could harm business rescue and returns to creditors.

However, R3 welcomes confirmation from the Government that it will look to improve the director disqualification regime, which will help to ensure that directors are less likely to walk away from their responsibilities. R3 would also urge the Government to consider how it can work with the insolvency and restructuring profession to investigate the conduct of directors of dissolved companies and to hold them accountable for their actions.

There already exist a number of tools available to the Government, and to the insolvency profession, to tackle reckless behaviour and wrongdoing by directors, and R3 would like to see the government reconsidering how these powers could be exercised more fully. For example, for the past few years, the annual number of directors who are disqualified has hovered around 1,200, while R3's members have reported frustration at making conduct reports to the Insolvency Service of misbehaviour on the part of directors that are then not followed up. Likewise, greater coordination between different parts of the government, such as HMRC and the Insolvency Service, would help to identify patterns of director misconduct in a more timely fashion, which would prevent further losses to creditors, suppliers, employees, and the public purse.

Looking more generally, R3 welcomes measures that will improve transparency and trust in corporate governance and tackle rogue directors. However a balance must be struck between ensuring that directors are held to account, and allowing distressed businesses to have the chance to be restructured and given the prospect of a sustainable long-term future. Measures that focus solely on holding directors to account, without consideration of business rescue and restructuring, will only discourage enterprise and entrepreneurship and damage the UK's reputation as one of the most attractive places to do business.

We are looking forward to working with the government to progress these proposals, to help strengthen the framework that underpins corporate insolvency and restructuring in the UK.

---

[6] https://www.r3.org.uk/media/documents/policy/consultation_subs/R3_Insolvency_and_Corporate_Governance_Consultation_Response_June_2018_FINAL.pdf

Prescribed part

One specific policy that the insolvency and corporate governance consultation looked at, which we do agree should be reformed, is that of the prescribed part. We note your recent article[7] that also proposed reform of the prescribed part and so we hope it would be helpful to set out our own proposals in this regard.

As you will be aware, the Government's response to this consultation committed to apply an inflationary increase to 31 March 2018 which will result in the cap increasing from £600,000 to approximately £800,000. While R3 welcomes this increase, a simple inflationary increase does not address the arbitrary nature of the prescribed part: there would still be a sudden cut-off in those cases where the cap is easily reached. Any other substantive reform to the prescribed part must also avoid making changes that would be seriously detrimental to floating change holders with the potential to discourage future lending.

Rather than maintaining a fixed cap, R3 suggests the introduction of a tapered one. Under such a system, the value of the prescribed part would remain low in proportion to the total money available to floating charge holders, but proportionately higher compared to what could otherwise be repaid to unsecured creditors. While increasing the prescribed part would mean less money back to floating charge holders, the relative loss would be low.

For example, the prescribed part could be amended so that, subject to the total assets available for the prescribed part exceeding £25,000, the prescribed part would be worth 50% of the first £25,000 of net floating charge realisations; then a further 25% on realisations between £25,000 and £3,000,000; then 10% on realisations between £3,000,000 and £6,000,000; then 5% on any remainder. Under this scenario, a taper would mean, in very large cases, a prescribed part that is several times higher than it is now, but that is still a relatively low proportion of the money available to floating charge holders.

'Inside Insolvency' – Left Foot Forward blog

In your recent blog for Left Foot Forward[8], you make a number of points about the UK's insolvency framework and the professionals who operate within it, particularly with respect to fees, transparency, the make-up of the profession, and the ability of individuals to make complaints about the work of insolvency practitioners. We hope it is helpful to address these points directly.

Fees

As noted above, the insolvency and restructuring profession plays a very valuable role in the economy. It helps rescue businesses and jobs, investigates fraud, and maximises what can be repaid to an insolvent company's creditors, including the taxpayer and other businesses. Without the profession's work, the knock-on effect on the wider economy of each insolvency would be significantly worse.

Fees paid to insolvency practitioners understandably attract attention, but there are strict controls on how they are set and paid. Insolvency practitioners' fees must be approved by creditors, and, when insolvency practitioners are working on a 'time-cost' basis, creditors have to be provided with an up-front estimate of fees. Further creditor approval is required for costs above this estimate.

[7] https://leftfootforward.org/2018/06/to-help-small-businesses-we-must-curb-the-banks-greedy-appetites/
[8] https://leftfootforward.org/2018/08/inside-insolvency-why-its-time-to-investigate-the-undertakers-of-the-corporate-world-carillion/

The profession's fees are monitored by regulators, and insolvency practitioners have to demonstrate that their fees in any case are reasonable. A 2014 review of the profession's fees, commissioned by the Government, found that fees-setting worked well in the majority of cases, particularly when creditors engaged with the process.

Insolvency practitioners are paid alongside other creditors in an insolvency, and, given the nature of insolvency cases, it is unlikely they will be paid in full for their work.

While large cases are rare, the costs involved can be noticeably higher: an insolvency practitioner and their team may have to secure and run a multitude of different sites, deal with hundreds or thousands of employees, work with a number of stakeholders, to keep all or part of a business trading. The insolvency practitioner essentially has to take on the running of a company almost overnight.

Your blog post refers specifically to the fees charged by PwC, which has acted as special manager in the Carillion liquidation. It is important to note how the role of a special manager differs to that of the office holder – in this case, it is the Official Receiver who is the office holder and as such approves PwC's work and fees in this case. As noted in correspondence[9] to the Joint Business, Energy and Industrial Strategy and Work and Pensions Select Committee into Carillion, the Official Receiver referred to its extensive monitoring of performance and fees charged by PwC in carrying out their work.

It should also be noted that PwC is one of the few firms with the scope and expertise to handle a case as large and complex as that of Carillion. Through this work as special manager, essential services have been maintained and contracts have transferred successfully to new organisations; redundancies also have been minimised, with 12,345 jobs (68% of the pre-liquidation workforce) having been saved as at 9 July 2018.

Without this difficult and complex work, the outcome for workers, suppliers and essential public services could have been far worse.

Transparency

Reference is made in your blog to the fact that creditors "can't see the insolvency practitioner's files". Notwithstanding private commercial documentation, insolvency practitioners are required to file a number of documents; including regular progress reports, relating to a business' administration or liquidation at Companies House, which are then available to view online by the public.

The make-up of the profession

Your blog also refers to the make-up of the insolvency profession, stating that "nearly half of all insolvency practitioners operate from the big four accounting firms", further implying therefore, that the majority of all insolvency practitioners charge high levels of fees. This is not correct – of R3's 1,127 licensed insolvency practitioner members, only 89 are from the 'big four'. Even extrapolating for the total number of licensed IPs who are not R3 members (there are 1,570 licensed insolvency practitioners in total), it would not be the case that the majority of insolvency practitioners come from the 'big four'.

---

[9] https://www.parliament.uk/documents/commons-committees/work-and-pensions/Carillion/180329-Letter-from-David-Chapman-Official-Receiver-The-Insolvency-Service-re-PwC-role-Carillion-special-managers.pdf

Complaints about insolvency practitioners

You set out that "individuals and entrepreneurs do not have the resources to mount a legal challenge to IPs. There is no independent ombudsman to adjudicate on disputes. So predatory practices are not rooted out."

As noted above, there is a complaints process in place for individuals to make complaints about the conduct or actions of insolvency practitioners who they believe have acted inappropriately (the Insolvency Service's Single Complaints Gateway). It is not correct to say that there is no avenue through which complaints about insolvency practitioners can be raised.