THE
INSTITUTE OF
CHARTERED
ACCOUNTANTS
OF SCOTLAND

Response from
The Institute of Chartered Accountants of Scotland to
The Insolvency Service on

A market study by the Office of Fair Trading into The Market for Corporate Insolvency Practitioners

ICAS COMMENT ON OFT REPORT

1. The Institute of Chartered Accountants of Scotland (ICAS) currently authorises 100 insolvency practitioners in Scotland and 15 who operate in England, Wales and Northern Ireland. This represents the vast majority of insolvency practitioners operating in Scotland (approximately 74%).

2. ICAS welcomes the call made by the Office of Fair Trading (OFT), in its report into the market for corporate insolvency practitioners, for a strong independent and competitive profession which works well for those directly affected by insolvency and for the economy as a whole. ICAS agrees with this aim. ICAS suggests that a number of the points raised in the OFT Report are out-with the control of insolvency practitioners and require to be addressed by government.

3. The OFT report concluded that most corporate insolvency cases in its sample do not present cause for concern and that a comprehensive review of insolvency procedures is not warranted. ICAS welcomes the premise that regulations should be proportionate and focused.

4. ICAS is concerned that the report, though based almost entirely on base data relating to companies registered in England and Wales, may be read as indicating that the report's findings apply equally to Scotland. ICAS questions whether this is in fact the case.

Application to Scotland

5. Due to its concerns regarding the relevance to Scotland of the Report ICAS sought clarification from OFT on the incidence of Scottish Data within the samples on which the Report is based. OFT confirmed the following:

	Per report	In Scotland
Company Administration data from Companies House	500	0
In depth creditor interviews	33	1
Online survey of creditors (*head office in Scotland)	1,232	*294
IP responses to the survey	312	32

The data relating to the 500 companies is said to have been used to "analyse how much was owed to creditors, how much they received, the fees charged by IPs and the competitiveness of the IP market". Given that only one creditor interview was held in Scotland and not a single Scottish Administration case was included in the survey, ICAS considers that the Report is unbalanced and cannot be relied upon in relation to the Scottish market.

6. There are a number of comments within the report which do not apply in Scotland. ICAS considers that it would have been helpful had such differences been highlighted alongside the comments to enable readers of the report to gain a better understanding that there are separate jurisdictions.

7. In many aspects legislation and practice in Scotland are different from that applicable in England & Wales particularly in relation to the fixing of fees. Approximately 60% of all corporate cases in Scotland are court liquidations where the requirements are that fees must be fixed by a Court Reporter, who is an officer of the Court and answerable to it. The Courts in Scotland operate a panel of Reporters appointed by the Court who are drawn from experienced insolvency practitioners. The OFT representatives conducted interviews with Court officials in Scotland. The Director in charge of the OFT study confirmed to ICAS that he

considers that this process works well. In a presentation that he made to an ICAS conference in Dunkeld in April 2010 he indicated that he was considering recommending that the process should be adopted in England & Wales however we note that such a recommendation did not find its way into the Report, perhaps due to the impact that it could have on the Courts.

8. Whilst ICAS does not have any data on the incidence of fees being reduced as a result of Court Reports it is aware that there have been a number of such cases and it considers that the interests of creditors are well served by the process that operates in Scotland. ICAS believes that a survey of the experience of the Scottish Courts should be carried out to identify the actual court time involved with the process and whether there are significant reductions in the fees. ICAS urges the Insolvency Service to give this matter careful consideration.

Relationships with Banks and secured creditors

9. ICAS notes the Report's finding that the Bank's use of panels to select IPs for appointment does not cause significant competition issues. Many IPs working in Scotland are either sole practitioners or partners in small to medium sized practices. The reality is that where a Bank wishes to appoint an IP it tends to be in the larger insolvency cases which could not realistically be serviced by sole practitioners. ICAS has on occasion been made aware of discontent by IPs in medium sized practices who had been nominated for appointment by a major creditor only to find that the Bank used its mandate to appoint a panel IP. Perhaps further research is needed into this aspect of the market in Scotland.

10. It is not surprising that there are fewer conflicts where the secured creditor is not repaid in full since the IP effectively has much closer dialogue with the secured creditor, and the IP requires secured creditor sanction of major decisions. They work closely together. Where the secured creditor is repaid in full the IP must communicate with unsecured creditors; their numbers may run into large figures. If there is no creditors' committee in place this presents challenges for the IP.

Relationship between unsecured creditors and insolvency practitioners

11. In relation to Scotland ICAS does not accept the Report's finding that unsecured creditors are provided with poor information (5th bullet point in the Market assessment summary) as this is not borne out by our monitoring visits to our licensed practitioners. IPs are required to provide creditors with regular reports on progress including receipts and payments accounts. In addition the RPBs have developed creditor guides for each type of insolvency process which in terms of SIP9(Scot) are required to be sent to every creditor, together with a receipts and payments account on each occasion when a fee has been fixed or is being sought.

12. Our monitoring visits reveal that our licensed IPs often conduct lengthy correspondence with individual creditors who seek clarification on the particular insolvency process. However a line has to be drawn by the IP between adequate reporting to creditors, and cases in which the creditor's requests are unreasonable and incur unnecessary cost to the case.

13. As the Report points out legislation provides creditors with the opportunity of overseeing the actions of insolvency practitioners through the mechanisms of creditor meetings, which the insolvency practitioner is required to hold, and through creditor committees. There is a satisfactory framework in place and, where unsecured creditors choose not to use their oversight powers; it is unreasonable to suggest that this gives rise to a perceived systemic failure which should be remedied by the insolvency practitioner. It is not for the practitioner to persuade greater engagement by unsecured creditors. That is a role for government. The

Report notes that HM Revenue and Customs is frequently the largest unsecured creditor thus were the Revenue to habitually act on creditors' committees oversight on behalf of unsecured creditors could be assured.

14. Comment is made in the Report that where there are unlikely to be funds available to facilitate payment of a dividend to unsecured creditors in an Administration the practitioner can dispense with holding a creditors' meeting and as a result the unsecured creditors cannot influence the Administration. This is what the legislation provides for and ICAS would argue that it should be so since in reality in such cases the unsecured creditors do not have an actual interest in the case. They do have the option of having a meeting if within prescribed time limits 10% in value of all creditors request one but creditors seldom request such meetings.

Fees

15. Paragraph 3.33 of the Report states that remuneration in a CVL may be fixed in accordance with a statutory scale. There is no statutory scale applicable in Scotland, fees are habitually claimed on a time and line basis.

16. Setting up and running creditors meetings costs money and IPs have strict reporting duties. It follows, where the secured creditor has been repaid in full, that there will be less of an asset pool to fund the insolvency. This fact taken alongside the reality that it is more time consuming, and therefore more costly to deal with several creditors rather than one secured creditor results in the IPs fees appearing as a higher proportion when compared to the fee charged to the secured creditor. ICAS believes that the Report displays a flawed understanding of the insolvency process.

17. All IPs can identify with the fact that it is extremely difficult to achieve adequate attendance at creditors meetings which results in few creditor committees being formed. Insolvency practitioners are acutely aware of their responsibilities to all creditors and they find it frustrating that many unsecured creditors do not engage with the insolvency processes. SIP9 (Scot) sets out requirements that all insolvency practitioners who work in Scotland must comply with and it is the case that creditors are advised of how fees are fixed and what they can do if they are dissatisfied. It is difficult to see what more IPs can do to improve the situation. ICAS believes that the government and the insolvency industry need to work together to find a way of achieving greater creditor engagement. One possible consideration is that since HM Revenue and Customs is a creditor in many insolvency cases the government could consider requiring HMRC to act on creditor committees where the case meets specified criteria.

18. As stated previously the OFT had indicated that it found favour with the Scottish system of fixing fees. ICAS accepts that there are some cases in which fees appear on the face of it to be high but comment should not be made without the particular circumstances of the individual case being reviewed. The level of expertise required on complex cases cannot be compared with consumer debt cases.

19. ICAS believes that professionals are entitled to be paid for work that they have carried out to the best of their ability and in accordance with the legislative requirements. Competition between practitioners is healthy for the industry and ICAS does not support any form of fee capping. An important aspect relating to fees in insolvency cases was not addressed in the OFT Report and it is the incidence of time costs that IPs have to write off. Whilst ICAS does not collate any data that can be put forward in support of this comment it is aware from its monitoring activities that IPs frequently have to write off time costs as there are insufficient

funds in the insolvency to meet their costs in full. IPs take a commercial decision when they accept appointment and therefore they accept write offs but hope that overall they will be adequately recompensed for the work that they have done.

20. ICAS considers that it would not be acceptable for complainers to be able to refer fee complaints to a separate Body. As outlined, there is an existing structure in Scotland for the proper consideration of fees in insolvency cases. The independent adjudication process envisaged by the OFT would need to compliment that structure. We consider that there would be little added benefit. Another reason for our objection is that a reviewer of fees would require to possess a technical understanding of insolvency law and process in order to be able to effectively adjudicate on fees and given the separate law operating in Scotland such a Body would require to have in-house technical expertise which may not be cost effective for the small number of Scottish complaints on fees. A further objection is that as a Regulatory Body it is within our remit to ensure that our members are complying with all aspects of their responsibilities as IPs.

21. ICAS has reviewed complaints lodged against its IPs by subject matter. This reveals that there are very few fee complaints. Further comment is offered under the complaints heading in this commentary.

The Regulatory Regime

22. The OFT recommendation that clear objectives require to be set is welcomed. We live in a changing world and the regulatory system needs to be able to respond to such changes but only after careful discussion between the relevant Bodies, and changes need to be based on concrete evidence rather than a perception.

23. There have been a number of recent examples in which the RPBs have been required to implement changes which are of questionable benefit and may in fact be detrimental to creditors. We agree with the OFT that where the Insolvency Service considers that a suggested change in standards or regulations may have a negative impact on achieving the regulatory objectives then the Insolvency Service should use its detailed knowledge and expertise to ensure that the change is not progressed. In particular where a proposed course of action would be contrary to the government's aim of encouraging the rescue of businesses the Insolvency Service and the profession should be prepared to speak out. ICAS will work with the other RPBs through JIC towards agreeing with the Insolvency Service on a regular basis what the regulatory objectives are and how to implement them.

24. The Report infers that a certain level of switching between RPB for reasons of cost or leniency occurs and it goes on to comment that this together with potential challenge of a disciplinary decision could be potentially crippling for the RPB. We suggest that the costs of an independent complaints Body would in fact afford greater risk to those RPBs that are situated outside London, if for no other reason than the fact that London chargeout rates far exceed rates in the regions.

25. ICAS believes that there is a clear conflict of interest in The Insolvency Service's dual role as oversight body and licensor of IPs. We therefore accept the OFT recommendation that the Insolvency Service should be refocused as the regulator of the RPBs and that it should cease licensing insolvency practitioners.

26. Whilst we accept that the Insolvency Service should be able to recover its direct oversight costs from the authorising Bodies we strongly oppose the concept of fixed charging. All the RPB's set fee income based on IP numbers and charge a fee based on either the size of firm

or the level of insolvency income per IP, as this most fairly represents the level of regulatory activity. The Insolvency Service supervisory activities should take into account the size and nature of the bodies and their licensees and should not take a "one size fits all" approach to charging fees and supervision, as this would not reflect the risk in the market place and would mean that the smaller bodies would be more heavily charged than the larger bodies.

27. ICAS has specialist knowledge and experience of the Scottish insolvency market. The fact that it is a small body means that ICAS has a detailed knowledge of the individual IPs it licenses which greatly improves the effectiveness of monitoring and oversight. ICAS cautions against a regulatory approach that may ultimately lead to a reduction in the number of smaller RPBs from the insolvency sector.

28. ICAS proposes, as the main regulatory Body in Scotland, that it should have periodic meetings with the Insolvency Service to address any issues arising in the Scottish market. These meetings could perhaps be aligned with JIC meeting dates.

Complaints handling

29. ICAS does not accept the negative comments on complaints handling contained in the OFT Report. All RPBs advertise on their web sites how the public can go about making complaints. This is the medium that government is encouraging us to use. In addition ICAS provides hard copies of a complaints leaflet to anyone upon request. We do not accept that the public does not know how to make a complaint against an insolvency practitioner.

30. We do not consider that it is correct to base some comments on public perception alone, and consider that research should be carried out with a view to obtaining accurate evidence.

31. In recommending a radical and costly new structure, the OFT has not adequately set out the basis upon which it considers that the present system fails to ensure IPs act in the best interests of the general body of creditors. Based on its monitoring activity of IPs ICAS refutes the view that IPs do not act in the interests of creditors.

32. The OFT has suggested an independent complaints body (first or second tier) in order to "increase the efficacy and consistency of complaints and restore creditor trust in the regulatory regime" ICAS considers that the OFT has reached this conclusion without due regard to all the relevant issues, including jurisdiction, personal insolvency processes, and the need to ensure consistency of approach by the professional bodies in relation to members irrespective of whether or not they are licensed to carry out insolvency work in the UK.

33. The establishment of an independent complaints body (first or second tier) would create a divergence of our enforcement processes. Namely ICAS would continue to investigate and discipline Members who do not hold an insolvency licence but, under the first tier proposal, all insolvency related complaints would require to be remitted to an external body. There would also be clear differences between these complaints procedures if it is decided that the independent body would have the power to consider "professional service" complaints as well as award "compensation". ICAS does not possess these powers, and a number of other RPBs are in the same position, and so it could not delegate these functions to an independent body, leading therefore to the need for Parliament to legislate on the matter.

34. The operational costs of an independent body would be substantial thus the OFT's recommendation for the funding by the RPBs of any independent insolvency related body would place a disproportionate financial burden on the smaller RPBs. ICAS cannot accept that such an arrangement would be in the best interests of the members or the public.

35. ICAS, in keeping with other RPBs, is already required to contribute to the funding of public interest complaints under the auspices of the AADB. The purpose of that body is well accepted, being the maintenance of confidence in the accountancy profession in the UK. Insolvency practitioners are part of the accountancy profession and there is no proven justification for treating them any differently from others within the profession. Were a complaint against an insolvency practitioner to be received that threatened the public interest it would in the normal course of events be referred to AADB.

36. In our view a radical restructure based upon a review of the corporate insolvency market cannot fairly reflect the general market. The Institute has reviewed its caseload to establish whether unsecured creditor complaints can be said to centre upon an issue over fees (with reference to Section 7.11 of the report). Statistically, ICAS complaints do not relate to IP fees, but rather the conduct of the IP stemming from ethical self review or self interest threats. Most ICAS complaints relate to personal insolvency matters and in the majority of cases, the complaint is initiated by the debtor (often related to the exercise of the trustee's rights over heritable assets).

37. Personal insolvency law in Scotland is radically different from the law applicable in England & Wales and anyone dealing with these insolvency complaints requires specialist knowledge. In handling these complaints ICAS appoints investigating panels drawn from the Investigation and Professional Conduct Enforcement Committee of three individuals comprising at least one Public Interest member and at least one insolvency practitioner.

38. In an effort to increase trust in the market and to counter the public perception regarding the effectiveness of the complaints systems there may be merit in allowing complainers who are dissatisfied with the outcome of the complaint to have the case referred to an Independent Examiner. The criteria for referral would need careful consideration and criteria would need to be specified to avoid raising expectations that cannot be met. Most of the RPBs already have provisions for recourse to an Independent Examiner (or someone similar) in prescribed circumstances. It is not unreasonable to suggest that this is a remedy that may be cost effective and deliverable.

Effectiveness of JIC

39. ICAS offers no comment within this document as it is party to the response that is to be submitted by JIC.

Conclusion

ICAS will continue to work with the Insolvency Service and with the authorising Bodies in an effort to improve performance of IPs and the public's perception of the insolvency regime.

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