The Insolvency Service

Call for Evidence

Bonding arrangements for insolvency practitioners

15 September 2016

Contents

1. General Information

This call for evidence will principally be of interest to the insolvency industry, including insolvency practitioners and their staff, Recognised Professional Bodies, current and prospective bond providers and brokers, compliance agents, and those involved in insolvency proceedings, in particular creditors. We would welcome responses from any member of these groups or from any other field.

How to Respond

When responding, please state whether you are responding as an individual or representing the views of an organisation. If you are responding on behalf of an organisation, please make it clear who your organisation represents and, where appropriate, how the views of members were assembled.

Please respond in writing via email to IPRegulation.Section@insolvency.gsi.gov.uk or by post to:

Insolvency Practitioner Regulation Section
The Insolvency Service
4 Abbey Orchard Street
London
SW1P 2HT

Confidentiality and Data Protection

Information provided in response to this call for evidence, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

What Happens Next?

This call for evidence will close on 16 December 2016. The Government will analyse the responses received to inform our next steps, such as whether legislative action is required to reform the bonding system. If you have any queries on any of the issues raised please send them to IPRegulation.Section@insolvency.gsi.gov.uk.

2. Introduction

As part of the comments received on insolvency legislation during the Government's Red Tape Challenge initiative, there were a number of calls for changes to the bonding arrangements for insolvency practitioners. As a result, we have had initial discussions with a range of stakeholders, including the Recognised Professional Bodies (RPBs), the current bond providers, successor practitioners, creditor representatives, and industry bodies such as R3, to see whether the current system remains fit for purpose.

This call for evidence seeks your views on the current bonding arrangements and how any problems might be addressed in a future reform of the bonding requirements for insolvency practitioners in England, Wales and Scotland.

The document also explains some voluntary measures that we are currently working on with industry bodies to improve the bonding system, and seeks your views on what other measures could be included.

3. Background

The purpose of bonds was initially set out in the 1984 White Paper "A Revised Framework for Insolvency Law". The White Paper, in addition to proposing the regulation of insolvency practitioners, proposed that an insolvency practitioner should be required to take out insurance cover against losses caused by their dishonesty and negligence in insolvency appointments.

The White Paper led to the introduction of the Insolvency Act 1986, which requires a person to be authorised by an RPB to act as an insolvency practitioner. The Insolvency Practitioner Regulations 1986[1], which supplemented the Act, provided that, subject to certain exceptions, an insolvency practitioner appointed to act must have in place a bond under which, in accordance with the provisions of the Regulations, the surety or cautioner would be liable in the general penalty sum of £250,000. In addition, the 1986 Regulations provided for a specific penalty sum in respect of each appointment, limited to the value of the assets in the estate. Where the assets were deemed to be less than £5,000 the value of the specific penalty sum would be deemed to be £5,000. There was no maximum value set for the specific penalty sum.

The 1986 Regulations were replaced by the Insolvency Practitioner Regulations 1990[2] , which set a maximum of £5,000,000 for the specific penalty sum. Further amendments were made in 1993, requiring insolvency practitioners to submit to their RPB each month a schedule of appointments and extending the bond cover to losses caused by the fraud or dishonesty of the insolvency practitioner "in collusion with one or more persons" and "the fraud or dishonesty of any person committed with the connivance of the insolvency practitioner."

[1] http://www.legislation.gov.uk/uksi/1986/1995/contents/made
[2] http://www.legislation.gov.uk/uksi/1990/439/contents/made

How the current bonding system works

The current requirements for bonding (or caution, as it is referred to in Scotland) are prescribed by the Insolvency Practitioner Regulations 2005[3].

The legislative requirements provide that the bond must be in a form approved by the Secretary of State and should cover losses in the event of either the fraud or dishonesty of the insolvency practitioner (whether acting alone or with another), or the fraud or dishonesty of any person committed with the connivance of the insolvency practitioner.

There are two elements of cover that must be provided by the bond: the General Penalty Sum (GPS) commonly referred to as the enabling bond, and the Specific Penalty Sum (SPS).

The SPS is, as the name implies, case specific. The legislation prescribes that the cover provided per case shall be between £5,000 and £5,000,000 depending on the value of the assets under the insolvency practitioner's control. For each case the practitioner must estimate the value of the assets. If they are collectively worth less than £5,000 then the SPS is £5,000.

The GPS is in force for one year and is provided to the RPB by the practitioner as evidence of his security. The legislation provides a set amount of £250,000 cover across all appointments. The GPS is not specific to any one case. In the event that the cover provided by the SPS is insufficient to meet all claims arising out of any case, claims can be met from the GPS, until that is also exhausted.

Where appointments are taken jointly, each insolvency practitioner must have their own cover for the full value of the insolvent's assets. The premium payable is calculated according to the value of the assets and the assessed risk of the practitioner.

[3] http://www.legislation.gov.uk/uksi/2005/524/contents/made

Every month the insolvency practitioner must submit a cover schedule, also referred to as the bordereau, to the insurer and the authorising body. The schedule details the new appointments in that month, any cases which have been closed for which cover is no longer required and any new estimate of the value of assets in existing cases. The insolvency practitioner must inform the insurer within a month of any increase in estimated value.

In practice, where fraud or dishonesty is suspected, a successor insolvency practitioner will normally be appointed in place of the existing one, usually by the relevant RPB. This generally follows the loss of licence of the existing practitioner but this may not always be the case. The successor insolvency practitioner then assumes the statutory functions of the office holder, investigates any loss from the estates through fraud or dishonesty and, where a loss is found, submits a claim to the insurer. Where a claim is agreed and paid, the fraudulent insolvency practitioner remains jointly and severally liable with the surety for the losses.

Bonds do not provide cover for negligence as there is no statutory requirement for insolvency practitioners to hold such insurance. Each RPB has their own regulations for Professional Indemnity Insurance (PII) which generally require (with some exceptions) a firm to obtain cover for at least £1.5 million for any one claim and in total. RPBs' PII regulations require that there be a period of run-off cover where a practice ceases.

The requirements for bonding apply only to insolvency practitioners – they do not extend to Official Receivers and likewise there are no requirements for PII to be held by Official Receivers (ORs) or the Insolvency Service.

The call for evidence is, however, concerned only with the bonding arrangements for insolvency practitioners, as this is the problem requiring immediate review.

Bonding is an important protection for creditors of insolvencies, as insolvency practitioners deal with thousands of cases each year. During 2015 there were a total of 104,346 insolvencies in Great Britain and of those cases at least 56,443 involved

the appointment of at least one insolvency practitioner (there are no statistics of the number of IP appointments made in bankruptcy and compulsory liquidations).

During 2015 only one insolvency licence was revoked, though such a withdrawal does not automatically mean that there the individual was guilty of fraud. We do not hold any information about the number of successor IP appointments.

In 2015 the bond providers were notified of 3 bond claims, none of which have been resolved or fully quantified. These represent claims against 3 IPs in 92 cases, with a total amount claimed of £805,897.

4. What are the weaknesses with the current bonding arrangements?

A number of weaknesses with the current arrangements have been identified through our discussions with bond providers, RPBs and successor insolvency practitioners. These weaknesses cover both the legal framework and practical issues.

Legal framework

Prescribed bond requirements are unclear and costly

It is suggested that the statutory requirements are not entirely straightforward and could be open to interpretation. They do not allow for any innovation by insurance providers – requiring submission of cover schedules irrespective of the insurer's business model. Cover schedules are burdensome and increase costs for all parties.

Statutory cover limits are inadequate and inconsistent

The monetary limits have not changed since the introduction of bonding requirements some 30 years ago. The GPS amount of £250,000 over all appointments is prescribed as an absolute and may no longer be adequate. Several recent insolvencies would exceed the maximum level set for the SPS.

Bonds rely on the honesty of a potentially dishonest insolvency practitioner to obtain adequate cover

The applicability and amount of the SPS depends on the honesty of the insolvency practitioner to make a correct declaration. If the insolvency practitioner either under declares the value of the assets, or does not declare at all, then the only available cover would be a pro-rata portion of the GPS, assuming that the insolvency practitioner has that in place.

Proceeds of a bond claim are not ring fenced

Once a claim is made, it is paid into the estate and treated in the same manner as any other asset, and is subject to the usual order or priority of costs and fees of the proceedings. We are told it is often the case that creditors who may have been adversely affected by the fraud will receive no direct financial benefit from a successful bond claim.

Lack of provision/control over successor insolvency practitioner fees

The costs of investigating fraud are provided for by the bond, but the liability of the surety is capped at the value of the SPS. The only control over such costs is that they are at the discretion of the surety which can lead to uncertainty. Successor insolvency practitioner fees are determined in the usual manner of any insolvency, though different rates may be charged for bond claim work. Given the age of cases, it can be difficult to engage creditors on these issues. As a result, successor insolvency practitioner fees may exceed the amount available under the bond claim leaving no money left for distribution to creditors.

No statutory requirement for professional indemnity insurance

There is no statutory requirement for specialised PII, which is instead governed by the rules of the individual RPBs, whose requirements differ.

The bond only covers fraud and dishonesty by or with the collusion of the insolvency practitioner

There is no regulatory or statutory requirement for insolvency practitioners or firms to hold fidelity guarantee insurance which would cover fraud or dishonesty of a director or employee without the knowledge or collusion of the insolvency practitioner.

Practical issues

Variation in particulars of bond wording causes confusion

There are wide variations in cover between bond wordings, particularly in terms of reporting deadlines, limits on liability and maximum indemnity periods. These depend not only on the bond provider but on the date of issue. There are reported issues with successor practitioners obtaining copies of the relevant bonds, and having to submit protective claims in order to ensure that cover will be available.

Increasing costs of premiums

In response to increased perceived risk, we are informed that some bond providers have increased SPS premiums for smaller firms (two or less insolvency practitioners) by up to 200% for 2016. While pricing of risk is a commercial matter for the insurers, concerns have been raised that smaller insolvency practices could be priced out of the market, which would reduce competitiveness.

Adversarial nature of claims

We understand there is little interaction between successor practitioners and sureties, with the insolvency practitioner carrying out their usual statutory duties and any investigation according to their own judgement. There is often no discussion or sanction of investigatory work by the surety, who are presented with costs only at the claim stage. There is no agreement to determine the amount of work to be undertaken, which insurers claim can on occasions be disproportionate to the loss suffered by the estate. This lack of co-operation can lead to delays in settling claims and increases costs to the detriment of creditors.

Cessation of cover on non-payment

Some bonds provide that cover is only available when the premiums are paid. While the enabling bond is paid at the outset of cover, the SPS is collected throughout the year as appointments are taken. Where an insolvency practitioner fails to maintain

payments, it is reported that in some instances insurers are terminating cover retrospectively which leaves estates without protection.

Limited number of insolvency practitioners willing to take on successor appointments

Currently there are only a small number of insolvency practitioners willing to take on successor appointments, which means that there is little competition and to some extent those undertaking successor appointments can set their price for undertaking this type of work.

Question 1: These are the issues that have been identified as weaknesses of the current bonding system. Do you agree with this assessment? If you have any evidence, which demonstrates the impact of these weaknesses, it would be helpful if you could provide this.

Question 2: Are you aware of any other weaknesses with the current system that have not been identified? Again, it would be helpful if you could provide any supporting evidence.

5. What similar systems operate in other industries?

In the legal profession, solicitors must hold professional indemnity insurance with minimum terms and conditions which are set by the Solicitors Regulation Authority (SRA) Indemnity Insurance Rules. These are approved by the Legal Services Board and the latest rules in effect are those from 2013.

The SRA also administers the Solicitors Compensation Fund (the Fund), which is designed to replace money that has been misappropriated either by a solicitor or their employees. The Fund can also provide compensation where a solicitor did not have the proper professional indemnity insurance in place.

The Fund is established by the Law Society and funded by contributions from solicitors (including registered foreign or European lawyers), recognised and licensed bodies. During the 2013/14 financial year, any individual holding a practising certificate were required to pay a flat rate of £56. Any legal practice which has held client money in the previous 12 months also had to pay a contribution of £836. These contributions are calculated according to the minimum reserve of the fund and forecasting for the year ahead: the contributions are the balancing figure required to maintain the minimum reserve at the end of the current financial year.

The Fund is a fund of last resort, and payments from the Fund are entirely at the discretion of the SRA. There is no legal entitlement to compensation from the Fund.

Most other professions, including accountants, rely on requirements for individuals to have taken out PII.

Question 3: Do you think that similar arrangements to those covering fraud and dishonesty in the legal profession would work in the insolvency profession?

6. Potential measures for reform

There are a number of ways that the bonding system could be reformed through non-legislative and regulatory change, as well as legislative changes.

Non-legislative and regulatory changes

The Insolvency Service is exploring options with industry to take forward some non-legislative and regulatory changes. These include:

- A claims management protocol agreed by the insurers and RPBs
- An approved panel of successor insolvency practitioners.
- A duty that investigative costs must be proportionate to loss
- Greater transparency over rates for investigation work

Claims management protocol

At present when a successor insolvency practitioner is appointed there is very little engagement between the insurers, RPBs and the insolvency practitioner. It is often only when the practitioner presents his/her claim for costs to the insurers that dialogue takes place and then it tends to be confrontational and adversarial. A claims management protocol will help to improve relationships by setting out the duties and responsibilities of each party. For example, it could set out the information that parties need to provide to each other and timescales for doing so. It could provide for regular reviews between the successor practitioner and the surety during the course of the investigative work.

The aim of the protocol would be to provide clarity of where responsibilities lie, so that parties know where they stand in relation to each other. This should help to reduce costs and avoid lengthy disputes, all of which will benefit the insolvent's estate and ensure that the proceeds of any bond claim reach the creditors, which is the driving objective of bonding.

Approved panel of successor insolvency practitioners

The main aim of the panel would be to encourage a wider circle of insolvency practitioners wishing to taken on successor appointments in potential fraud cases, a function which is currently undertaken by a very small minority of insolvency practitioners. A panel comprised of insolvency practitioners who have expressed an interest in this type of work and have the necessary experience and resources to deal with a portfolio of cases, could encourage more insolvency practitioners to take such appointments.

Only insolvency practitioners on the approved panel would be eligible to be appointed as successor practitioners to investigate potential cases of fraud and dishonesty, and any practitioner on the panel would be agreeing to the terms and conditions set out in the claims management protocol, providing a method of enforcement. These terms and conditions could include provisions regarding the rate charged for investigation and proving a bond claim, for example.

Appointments from such a panel would generally be made by the RPBs.

A requirement that investigation costs must be proportionate to loss

In some cases we have seen evidence where the costs claimed by an insolvency practitioner in proving a bond claim are disproportionate to the loss suffered by the insolvent estate. While insolvency practitioners are expected to use their professional experience and commercial judgement in carrying out their work, it has been suggested that a requirement as part of the protocol for investigation costs to be proportionate could reduce costs to estates which have already suffered a loss.

Greater transparency over rates for investigation of fraud and dishonesty

The Government has never sought to impose statutory limits on the hourly rates or remuneration of insolvency practitioners, the question of remuneration being left to creditors who have an economic interest in the outcome.

Investigation into fraud and dishonesty is not reserved to insolvency practitioners and may be carried out by any suitable person – the Secretary of State may consent to a bond being assigned to any legal person. It is also typical that fraud and dishonesty occurs several years into an insolvency, where creditor engagement will be very low and it is right to protect the interest of those creditors.

Question 4: Are there any other issues that you would like to see addressed through a claims management protocol?

While a claims management protocol would be a non-statutory solution, we would expect it to have regulatory force. Therefore RPBs would be responsible for monitoring successor insolvency practitioners for compliance with the protocol, in a similar way to compliance with Statements of Insolvency Practice and the Insolvency Code of Ethics.

As well as a claims management protocol, we are also working with RPBs to improve early detection of the warning signs of fraud. The RPBs have quarterly meetings to share best practice and discuss common issues they encounter on inspections. One large bond provider has already attended meetings to relay their claims experience so that RPB monitors can consider this information in planning and carrying out visits.

Legislative changes - options

Option 1 – Do nothing

This option would maintain the current legislative status quo. The Secretary of State would continue (through the Insolvency Service) to approve bond wordings and would have limited scope to seek amendments to a proposed bond beyond the prescribed requirements.

The remuneration of the successor insolvency practitioner would, where based upon time spent on the case, be subject to the requirement to estimate their fees in accordance with the Insolvency (Amendment) Rules 2015. As this will only apply to cases where the basis of remuneration is amended after 1 October 2015, it will be several years before any effect is seen in bond claims.

The claims management protocol and regulatory measures outlined on pages 11 and 12 would be introduced alongside the existing legislative framework.

Question 5: Do you think the introduction of a claims management protocol and regulatory action, alongside the existing legislative framework, would be sufficient to resolve the weaknesses identified with the bonding system?

Option 2 – Repeal legislative requirements

This option would remove the legal requirement for an insolvency practitioner to take out a bond or caution. Therefore, there would be no statutory protection for creditors in the event of a loss to the insolvent estate through the fraud or dishonesty of the practitioner or anyone acting with the connivance of the practitioner. This would be similar to arrangements in insolvency jurisdictions in other parts of the world, e.g. Australia, which no longer has statutory bonding requirements.

In the absence of a legislative framework, the insolvency practitioner would retain a liability for any loss caused by their dishonesty or fraud, a right of action, which could be assigned by a successor practitioner if there is a prospect of recovery. RPBs could decide to make it a requirement for granting an insolvency licence that practitioners have adequate insurance in place to cover losses through dishonesty or fraud, in a similar way to the current regulatory requirements for professional indemnity insurance.

The repeal of the relevant legislation would remove the cost of obtaining bonds for insolvency practitioners themselves (in respect of the GPS), which would reduce costs for creditors. It would also remove administrative burdens from practitioners and RPBs in longer having to submit and process monthly bordereau returns.

This option recognises that under the current arrangements the proceeds of claims are often largely consumed by the remuneration and expenses of the successor insolvency practitioner. Hence the legislation is no longer meeting its purpose of protecting creditors' interests; instead creditors are effectively paying for the bond with no benefit to themselves.

Question 6: What do you consider would be the likely impact of removal of the statutory bonding requirements for a) insolvency practitioners and b) the protection of creditors?

Option 3 – Amend the current legislation

There are a number of possible ways in which the legislation could be amended:

a) Amend the current prescribed terms of a bond

Certain terms of a bond are prescribed by Part 2 of Schedule 2 to the Insolvency Practitioners Regulations 2005. The Regulations also set out other terms which may be included in the bond.

Currently the Regulations prescribe terms covering the extent of liability, the manner in which the insolvency practitioner should inform the surety of the cases and asset values, the amount of cover and the limitations on the amount of cover. Other terms are set by the bond providers and different bond providers have different terms governing, for example, the time limit in which claims must be made and the maximum period in which the surety is liable under the policy.

The wording of each bond must be approved by the Secretary of State. In practice this means that when amending wording the surety must submit the proposed wording and any endorsements to existing wordings to the Insolvency Service to review. We then ensure that the minimum terms in the Regulations are covered by the bond but we do not express an opinion on other terms that may be included.

We are told that variations in bond wording can, in some cases, lead to uncertainty where the successor practitioner does not know which bond wording was in force at the relevant time. Also some of the existing requirements (for example, the use of cover schedules to calculate the amount of cover required) may be overly prescriptive and, we are told, have hampered the ability of at least one insurer to use an alternative model which would dispense with the cost to the insolvency practitioner of preparing and reviewing cover schedules in every case.

One option for amendment would be to prescribe terms for a single, universal bond, which would remove any uncertainty from the claims process and mean that the protection for all insolvent estates would be identical irrespective of the provider or the relevant period in which the fraud or dishonesty occurred. This option, however, could stifle competitive pricing of bonds, as all insurers would be bound by the same terms. Some insurers may also be unhappy with the prescribed terms and decide to withdraw from the market, which again would reduce competitiveness. Alternatively it may be possible to remove some of the more administratively burdensome requirements of the current prescribed terms.

A further solution would be to prescribe minimum terms and conditions that all providers must include, with the remainder at their discretion. This could help to reduce variations on claim time limits and limits on liability, but allow insurers flexibility over other areas of the policy wording.

b) Provide that the proceeds of a claim for the benefit of creditors are ring-fenced from the investigation costs

Once a claim under a bond has been agreed, it is paid to the successor practitioner and into the estate account. As with any other funds received into the estate, the bond pay-out is then subject to the usual order of priority in an insolvency, and so is liable for the costs and fees of the proceedings, including the remuneration of the successor practitioner and the costs of the investigation.

In a typical bond claim, the surety will agree the amount of the claim for the loss suffered by the estate through fraud or dishonesty, then any unavoidable costs, such as where the successor has to repeat work that had already been charged to the estate by the initial office holder, and finally the costs of incurred in proving the claim.

Even where the successor practitioner agrees with the surety a settlement of their costs in proving the claim, once paid into the estate account all of the proceeds of the bond claim may legitimately be used to meet outstanding remuneration. This can mean that little or no benefit passes to the creditors, who are supposed to be the beneficiaries of bond claims. Hence one could argue that the investigation has served no purpose as the only beneficiary has been the successor practitioner.

To counter this and ensure the creditors benefit from the investigation, an option would be to amend the insolvency legislation to ring-fence the amount paid by the surety in respect of the actual loss to the estate, such as where money was taken from the estate through fraud or dishonesty. The amount would not be available to meet any other costs of the proceedings, for example the costs of the successor practitioner, but would only be used for distribution to creditors in the usual manner.

c) Provide for investigative costs as a prescribed requirement of a bond

The current system provides for “additional costs” and “unavoidable parallel costs” occasioned by fraud to be met from the bond. However, all of the bonds currently available limit the liability of the surety to the value of the SPS in every case. In practice this means that where the majority of the assets are removed from an insolvent estate there can be no cover for investigation costs.

There is also no provision for a review of other cases in the portfolio and the costs are only covered in those estates where fraud is proven. This has lead to the use of ‘central costs’ incurred across a portfolio of cases which is then met by payments from the cases where fraud is proven, effectively cross subsidising the costs of cases where no fraud was proven.

By setting a limited amount of investigative costs as a prescribed part of the bond, it would allow for a proper review of all cases where a successor practitioner is appointed, but would ensure that the enquiries would be proportionate as the amount available in each case would be limited. However, there could be a disadvantage in that the limit set could become the de facto amount for every case, which could increase costs overall and it could discourage investigation into complex cases.

d) Agree or legislate for a ‘de minimis’ maximum indemnity period

A recent case arose where the maximum indemnity period had expired three years before the successor practitioner had been appointed, which meant the estate was left without cover. By providing for minimum duration for the maximum indemnity period it would ensure adequate cover was in place to protect the estate and creditors in the event that fraud is discovered. However, such a measure is likely to increase the cost of premiums as there will be a longer period of risk.

e) Remove requirements for monthly cover schedules and provide for an annual or global bond cover

Currently an insolvency practitioner is required to declare the value of estate assets and submit cover schedules to their respective insurer and RPB on a monthly basis. This is an administrative burden on all parties. The asset estimates and cover schedules determine the amount of SPS that applies in each case and the premium to be paid. This limits the cover available to the value of the assets lost, and does not provide for additional or duplicate costs of investigation.

By providing for a single annual or global bond, it would reduce administrative burdens and allow insurers to determine the mechanics of operating the bond, rather than prescribing this in legislation. An annual global bond could hold more risk for the insurer, which could increase prices for smaller practices and may make it difficult for them to obtain insurance, but on the other hand, removing the legislative constraints would allow insurers the opportunity to innovate.

f) Amend the existing monetary limits of the GPS/SPS

The monetary limits for the GPS and SPS are currently prescribed by the Insolvency Practitioner Regulations 2005, as amended. They are:

GPS – absolute value of £250,000 across all cases
SPS – minimum of £5,000, maximum of £5,000,000
Global aggregate limit of at least £25,000,000

The amounts set have not been altered since 1993 and are now out of date. The GPS is intended to be available to make up any shortfall in the SPS, but is rarely, if ever, sufficient to do so. The amount could be increased and stated as a minimum, so that bonds could be tailored to practice size.

The SPS is the actual asset value per case. There should be no need to have a maximum – though an insurer may wish to apply an automatic limit that requires consent before a higher amount attaches. The advantages of this would be to allow

the bond to meet the actual amount of cover required. The disadvantage is that an increase in the amount of cover will increase the risk and therefore the premiums.

g) Introduce a duty that investigative costs must be proportionate to loss/cover

There is currently no legislative provision that covers the work of the insolvency practitioner as a successor practitioner and bond investigations. Insurers tell us that investigations are frequently disproportionate to the SPS available or amount of any loss. One way to counteract this would be to introduce a duty or requirement that the successor practitioner acts in a proportionate and commercial manner. This would reduce the costs claimed on those cases where fraud is proven and thereby increase returns to creditors and reduce the costs of premiums. However, there is a risk that it might make successor appointments less attractive, lead to less investigation of cases and leave some dishonesty undetected.

h) Protect estate from non-payment

Where an insolvency practitioner fails to pay the bond premium, the bond will be terminated and the estate will be without cover. It is quite likely that a dishonest insolvency practitioner will not pay the bond premium. Therefore to protect the estate from losses and ensure that the bond cover remains in place, it could be a prescribed term in the bond that payment has to be made upfront. Non-payment of the bond should be reported to the RPB, which could then carry out an early monitoring visit with a view to assessing whether licence removal for the insolvency practitioner is appropriate.

i) Include professional indemnity as a requirement for security, including run-off cover

It is currently not a statutory requirement for insolvency practitioners to have professional indemnity insurance, although it is a requirement of the RPBs in granting an insolvency licence. However, we understand that where negligence claims arise after an insolvency practitioner loses their licence, the professional

indemnity insurance is no longer available and there is no run-off cover in place. It is the responsibility of each IP to ensure that run-off cover is in place, but where a license has been revoked it may not be possible to arrange that cover.

The legislation could therefore be amended to make professional indemnity insurance a statutory requirement as well as insurance to cover fraud and dishonesty, and also to provide for run-off cover for the same period as the bond. This would give increased protection to creditors, but is likely to increase the costs of insurance.

j) Agree or legislate for insolvency practitioner firms to hold fidelity guarantee or similar insurance to protect creditors from fraud by persons other that the insolvency practitioner

A bond is obtained personally by each insolvency practitioner, and applies to the insolvencies over which they are appointed. Cover does not extend to the firm in which the insolvency practitioner works and does not apply to employees or other officers of that firm.

This could be addressed either by regulatory action or legislation, to ensure that creditors are protected. Such cover might only be required where the firm employs a given number of staff, the ratio of staff per insolvency practitioner, or if the firm specialises in insolvencies where there is a greater risk of fraud.

There are insurance products available, such as fidelity guarantees which could provide wider protection for creditors.

Question 7: Do you consider we have correctly assessed the advantages and disadvantages of these options as set out above, and the potential impacts? If not, please give your reasons.

Conclusion

The purpose of this paper is to assess whether the current arrangements for bonding of insolvency practitioners remain fit for purpose and to gather evidence on the likely impact of possible legislative change.

Question 8: Do you agree the paper sets out the full range of issues, or is there anything further which should be considered.

Question 9: Of the proposed options for legislative change, which would be your preferred approach and why?

Question 10: Do you have any further comments you would like us to consider in relation to bonding?