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By email: gc20-05@fca.org.uk

25 January 2021

Dear Sir or Madam

FCA Guidance Consultation – Guidance for insolvency practitioners on how to approach regulated firms ("GC20/5")

The City of London Law Society ("**CLLS**") represents approximately 17,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues. The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees.

This letter has been prepared by the CLLS Regulatory Law Committee (the "**Committee**"). The Committee not only responds to consultations but also proactively raises concerns where it becomes aware of issues which it considers to be of importance in a regulatory context.

We welcome the opportunity to respond to GC20/5. It is, in our view, a helpful and welcome contribution to the existing understanding of the important role of an insolvency practitioner at an FCA-regulated firm.

1. Overview

In the experience of the members of the Committee, dialogue between Insolvency Practitioners and the FCA is an important aspect of the proper management of an administration of an FCA-regulated firm. We believe that that dialogue should be begin early, continue frequently, be open, and focus on the proper treatment of clients and their assets (for example, client money and assets held under the CASS regime).

We also think it is important to recognise, and we would encourage the FCA explicitly to acknowledge, that the duties of an insolvency practitioner under the Insolvency Act 1986 involve the handling of the insolvency process in the interests of the creditors. There is, therefore, a balance to be found between the statutory objectives of the insolvency regime, and the consumer protection objectives set out in the financial services regime.

2. Pre-insolvency

We agree that it is important that any IP has sufficient relevant expertise to be appointed to a firm conducting regulated business (paragraph 8). We also agree that it is important that an IP knows the key regulatory requirements that apply to the firm (paragraph 9). We think it is important that the IP focuses on identifying key issues with compliance, such as those listed in paragraph 9 (such as CASS). However, we would not expect an IP to expend the time and expense in attempting to "identify *any* issues with compliance" irrespective of importance to the insolvency process. Contrast for example, key issues such as CASS for a firm that holds client money or assets on the one hand against issues such as historic late filings of RMAR returns. We think clarity on this point would be helpful.

We consider that when referring to the need to obtain prior FCA consent to an out-of-court appointment (paragraph 13), the guidance should carefully reflect s362A FSMA. The FCA consent needs to be filed along with any relevant notice of intention to appoint or, where there is none, it must accompany the notice of appointment. While we appreciate the guidance is not intended as a technical resource for administrators, the appointment procedure for administrators is highly complex and we are aware of several cases where the FCA consent was obtained/filed at the wrong time risking the entire appointment and requiring court determinations on the law. As such, it would be preferable for the guidance in paragraph 13 to mirror the wording used in s362A to avoid somebody reading it and taking the wrong approach.

We note (paragraph 15) the FCA will take into account a number of factors when considering an IP's ability to take on an appointment as administrator. One of these is the IP's expertise, with which we agree (see above). Another is the IP's past conduct. We are concerned that this factor may be seen as giving the FCA the ability to try to direct IPs to act, on a particular administration, in a particular way (notwithstanding the interests of creditors generally), for fear that otherwise this would be held against them by the FCA subsequently in respect of their "past conduct". We assume that this is not what the FCA intends to convey. Administrators carry out their responsibilities, in general, in a serious and diligent way, and have to make a number of balanced judgements which, it is inevitable, will not always be the preferred approach for some of the various stakeholders (be they client money or asset beneficiaries, other creditors, employees, directors, or the FCA). We assume that the FCA intends to convey only that serious issues, such as a wilful disregard for the regulatory regime, or past good relationships (irrespective of individual decisions that may not accord with the FCA's preferences) would be taken into account. We consider that the FCA should make clearer that this is the case.

We also consider that the guidance should reflect the fact that *before* their appointment, a prospective IP – whether administrator, liquidator or special administrator – is not able to cause the firm to act. It is only after they have been appointed that the IP becomes the agent of the firm and so can cause it to act. The guidance, in places, appears to assume that a prospective IP is able to determine how the firm acts. For example:

- paragraph 14 seems to assume that the (as yet not appointed) administrator would make the consent request/put the FCA on notice. The notification obligation in s362A is on the applicant (i.e. in most cases the appointing firm/its directors) and so the consent request should be made by them rather than the prospective administrators. The template letter appended to the guidance would require consequential adjustment;

- paragraph 19 should reflect the position that it is not the responsibility of the prospective administrator to share with the FCA any court documentation, administration applications or other documents required to be sent to creditors of the firm (prior to their appointment) but for the appointing firm/its directors to do so. It may also be helpful more generally for the guidance here to note the FCA's ability to participate in court proceedings, creditor meetings etc (as per s362 FSMA and as noted in paragraph 29 in the context of liquidation); and

- similarly, the guidance in paragraph 23 suggests that it is the role of the prospective special administrator to give notice or serve court documents. Until their appointment, these requirements are for the firm/its directors to undertake and the prospective appointee has no power to do so. We also note that paragraph 23 refers to the prioritisation of objectives once the special administrator has been appointed under SAR Regulation 16 and in our view it would be better to set this out later in the guidance when dealing with what happens following appointment.

3. Entering insolvency

We agree that an IP should provide regular updates to the FCA (paragraph 41), and that typically those updates would cover matters such as those set out in GC20/5 (paragraph 41). We agree that prompt two way interaction in relation to matters such as communication with clients (paragraphs 42 and 43) is important. In our view, the guidance in paragraphs 45 – 52 inclusive (relating to interaction with the FSCS and the FOS) would be better placed in chapter 4, covering post-insolvency.

The guidance in paragraph 39 suggests that IPs should consider how they ensure appropriate representation on the committee. However, this should not be over-stated as the ability of the IP to determine the membership of a committee is often limited, and it is ordinarily a matter for the creditors to vote upon (albeit there are for some processes provisions to assist in getting a cross-section of those with relevant interests). In our view, paragraph 39 should reflect this limitation.

4. Post-insolvency

We agree that an IP will need to focus, at an early stage, on control over client assets (paragraph 65).

We note that there are aspects of the guidance that do not reflect the insolvency law changes made by the Corporate Governance and Insolvency Act 2020. For example, paragraphs 106 and 107 (together with footnote 47) should incorporate the new *ipso facto* provisions set out in s233B of the Insolvency Act 1986 noting that that section is not restricted to "essential" suppliers (unlike s233) and does apply in liquidation. Additionally, footnote 18 should highlight that the restrictions on the use of statutory demands and winding up petitions have been extended to 31 March 2021 (rather than ending on 31 December as currently noted).

Finally, it is not clear to us why paragraphs 108 and 109 of the guidance focus on equitable set-off. The position on set-off is that in a liquidation, or an administration after notice of distribution has been given, there will be mandatory, self-executing insolvency set off. This position may differ in some regimes (such as the SAR) and mandatory set off may be disapplied in certain cases (e.g. the protections afforded to close-out netting provisions). However, we consider that the emphasis in paragraphs 108 and 109 of the guidance to a customer's possible right to equitable set-off does not reflect what happens in most insolvency situations. Where mandatory set-off does not (yet) apply, contractual set off is likely to be more relevant than equitable set-off. In our view, therefore, paragraphs 108 and 109 should be clarified to this effect as they otherwise seem rather anomalous.

5. Restructuring procedures

We agree that detailed discussions on the use of the various restructuring arrangements between the IP and FCA is important to ensure that restructurings operate to balance the interest of the various parties involved in any administration.

If you would find it helpful to discuss any of these comments then we would be happy to do so. Please contact Karen Anderson by telephone on +44 (0) 20 7466 2404 or by email at Karen.Anderson@hsf.com in the first instance.

Yours faithfully

Karen Anderson
Chair, CLLS Regulatory Law Committee

THE CITY OF LONDON LAW SOCIETY
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