Guidance consultation

Guidance for insolvency practitioners on how to approach regulated firms

GC20/5

December 2020

1 Introduction

1.1 Minimising the impact of a regulated firm failure is a key priority for the FCA. While we cannot stop firms failing, we aim to help minimise disorderly failures that cause serious harm to both consumers and markets. This involves working with insolvency practitioners (IPs) appointed over regulated firms[1] to reduce such harm where possible.

1.2 If an IP is appointed over a regulated firm, the IP takes control of the firm which continues to have regulatory requirements and responsibilities. We are therefore consulting on guidance to help IPs comply with our rules and guidance as well as relevant legislation which aim to achieve better outcomes for consumers and market participants following a failure of a regulated firm.

1.3 The proposed guidance is our view of how an IP should ensure regulated firms meet their ongoing financial services regulatory obligations following appointment. We supervise regulated firms, including those in insolvency proceedings, while they continue to be authorised or registered by us. We are not the regulatory authority for IPs and IPs generally act as officers of the court. We have therefore engaged with the recognised professional bodies, who licence and regulate IPs, on the proposed guidance.

1.4 The proposed guidance is aimed at IPs appointed over firms solely authorised or registered by the FCA. It may also be relevant for IPs appointed over firms that are dual regulated by the FCA and PRA[2].

[1] References to regulated firms refers to firms authorised under the Financial Services and Markets Act 2000, the Payment Services Regulations 2017 and Electronic Money Regulations 2011 unless otherwise stated.

[2] The FCA is the competent authority for solo-regulated firms. The PRA is the competent authority for dual-regulated firms. The Bank of England is designated as the resolution authority for dual regulated firms and certain investment firms (i.e. IFPRU 730k investment firms or solo-regulated firms that are part of a group subject to the Bank of England's resolution power under the Banking Act 2009).

2 The consultation

What we are consulting on

2.1 We set out the proposed guidance we are consulting on in Annex 1 and 2.

2.2 Here, we summarise our consultation, together with the specific questions we would like consultees' views on:

- **Chapter 1 (Introduction)** explains the scope of the guidance and the FCA's role in regulated firm failures.
- **Chapter 2 (Pre-insolvency)** outlines considerations for IPs before a regulated firm's entry into an insolvency procedure, such as obtaining consent for out-of-court administration appointments and sharing court documentation with the FCA.
- **Chapter 3 (Entering insolvency)** explains our expectations on IPs at the point of a regulated firm's entry into an insolvency procedure and shortly thereafter, such as communications with clients and creditors.
- **Chapter 4 (Post insolvency)** explains our expectations on IPs during an insolvency procedure, such as treatment of client assets and treating customers fairly.
- **Chapter 5 (Restructuring procedures)** explains our expectations when a regulated firm enters into a company voluntary arrangement, scheme of arrangement or restructuring plan.
- **Chapter 6 (Checklist)** summarises the key steps from the guidance that an IP will need to consider when appointed over a regulated firm.

2.3 We would welcome consultees' views on the following questions:

Q1: Do you agree with the considerations for IPs before a regulated firm's entry into an insolvency procedure in Chapter 2? If not, why not? Are there any other considerations that would be useful to consider?

Q2: Do you agree with our expectations on IPs at the point of a regulated firm's entry into an insolvency procedure in Chapter 3? If not, why not? Are there any other considerations that would be useful to consider?

Q3: Do you agree with our expectations on IPs during an insolvency procedure in Chapter 4? If not, why not? Are there any other considerations that would be useful to consider?

Q4: Do you agree with our expectations when a regulated firm enters a restructuring procedure in Chapter 5? If not, why not? Are there any other considerations that would be useful to consider?

Who does this consultation affect?

2.4 The proposed guidance is primarily aimed at IPs appointed (or looking to be appointed) over regulated firms. It may also be of interest to professional advisers, trade associations, firms and consumers.

Cost benefit analysis

2.5 The Financial Services and Markets Act 2000 (FSMA) does not require us to publish a cost benefit analysis (CBA) when proposing guidance. However, we produce a CBA for general guidance if a high-level assessment identifies an element of novelty which may be prescriptive or prohibitive such that some costs may be incurred.

2.6 In this CBA, we have assessed the potential impacts of the proposed guidance. Where it is reasonably practicable to do so, we have provided monetary values for the impacts. Where we have been unable to quantify the impact, we have provided a qualitative assessment of these elements.

Rationale for intervention

2.7 The proposed guidance provides our view of how an IP should ensure regulated firms meet their ongoing regulatory obligations following appointment. We do not regulate IPs. However, given the regulatory principles of proportionality and transparency, we have assessed the impact of the proposed guidance on IPs in this CBA.

Firms affected

2.8 As at 1 January 2020, there were 1,553 licensed IPs in the UK, of which 1,236 were appointment takers (The Insolvency Service, Annual Review of Insolvency Practitioner Regulation 2019). Based on our supervision intelligence, over the last two years approximately 20% of IPs and their staff have been appointed over a regulated firm, of which approximately 1% have been appointed on more than 10 occasions.

2.9 For this CBA, we have assumed the affected population of IP firms to be 225 firms, consisting of 11 large and 214 smaller firms. We cannot predict the exact number of IPs that will be appointed over regulated firms for any given period in the future.

Costs to firms

2.10 The proposed guidance is not introducing new obligations on regulated firms but provides our view on how IPs should ensure firms meet their ongoing regulatory obligations during an insolvency process. There will be costs to IPs to familiarise themselves with the guidance and conduct a gap analysis on what, if anything, they need to do.

2.11 We assume that IPs will need to familiarise themselves with and undertake a legal gap analysis of approximately 45 pages of this guidance consultation document. We use standard assumptions to estimate firm costs based on the standardised costs model, of which further details can be found in Annex 1 'How we analyse the costs and benefits of our policies'. We estimate total industry-wide one-off costs at

£670,000 or approximately £6,700 and £2,700 per large and smaller IP firms respectively.

2.12 We do not envisage any ongoing costs for IPs.

Benefits

2.13 The guidance is likely to improve outcomes on a firm failure and achieve the following:

- Reduce insolvency costs by raising awareness and provide easily accessible information to IPs on how to deal with regulated firm failures.
- Help IPs who have limited experience of regulated firm failures and who take appointments to progress such failures more effectively.
- Improve IPs' awareness and knowledge of dealing with regulated firm failures, our requirements and ensure effective engagement with the FCA.
- Encourage best practice in dealing consistently with regulated firms in insolvency scenarios with a view to promoting fair and consistent outcomes aimed at maximising returns to clients and creditors and promoting the public interest.

2.14 We consider it is not reasonably practicable to give an estimate of the resulting benefits from the above examples.

2.15 We expect the proposed guidance to be net beneficial as IPs, regulated firms in insolvency proceedings, their clients and creditors will benefit from reduced insolvency costs and improved outcomes on a firm failure.

Compatibility statement

2.16 Section 1B(1) of FSMA requires the FCA, when discharging its general functions, as far as is reasonably possible, to act in a way which is compatible with its strategic objective, and advances one or more of its operational objectives, and its general duty under section 1B(5)(a) of FSMA to have regard to the regulatory principles in section 3B of FSMA. The FCA also needs, so far as is compatible with acting in a way that advances the consumer protection objective or the integrity objective, to carry out its general functions in a way that promotes effective competition in the interests of consumers.

2.17 We are satisfied that the draft guidance is compatible with our general duties under section 1B of FSMA, having regard to the matters set out in section 1C(2) of FSMA and the regulatory principles in section 3B of FSMA.

2.18 The draft guidance will help us advance our operational objective of providing an appropriate degree of protection for consumers by setting out some applicable regulatory requirements which IPs should be aware of and good practice on how IPs should handle insolvencies of regulated firms including, for example, treating customers fairly, returning client assets and customers' funds, and consumer redress.

2.19 In producing the draft guidance, we have had due regard to the principles in the Legislative and Regulatory Reform Act 2006 (LRRA) and the provisions in the Regulators' Compliance Code for the parts of the proposals that consist of general policies, principles or giving guidance. We are satisfied that we have had regard to

the principles in the LRRA and to the Regulators' Compliance Code to the extent that our proposals consist of guidance and we consider that our proposals are proportionate and will produce an appropriate level of consumer protection when balanced with their impact on firms.

2.20 We have also had due regard to the recommendations made by Her Majesty's Treasury under section 1JA of FSMA about aspects of the economic policy of Her Majesty's Government. The draft guidance takes into consideration the recommendations relating to better outcomes for consumers. The purpose of the guidance is to set out the FCA's views on how to approach regulated firms in insolvency. When the guidance is final, IPs should have due regard to it when undertaking insolvency procedures which will promote best outcomes for clients and creditors.

Equality and diversity

2.21 We are required under the Equality Act 2010 to have due regard to the need to eliminate discrimination, harassment, victimisation and any other conduct prohibited by or under the Equality Act 2010, advance equality of opportunity between persons who share a relevant protected characteristic and those who do not, and to foster good relations between people who share a protected characteristic and those who do not.

2.22 As part of this, we consider the equality and diversity implications of any new policy proposals. We do not consider the proposed guidance will adversely affect any of the groups with protected characteristics.

How to respond

2.23 We welcome comments on the proposed guidance by **18 January 2021**. Please send your comments using the online response form on our website or you can email your responses to gc20-05@fca.org.uk.

2.24 We will consider your feedback and publish our final guidance in due course.

Annex 1 – Draft guidance for insolvency practitioners on how to approach firms authorised under FSMA

Chapter 1: Introduction

1. This document provides guidance to insolvency practitioners (IPs) on how to approach firms authorised under the Financial Services and Markets Act 2000 (FSMA).

2. If an IP is appointed over a regulated firm, the IP takes control of the firm which continues to have regulatory requirements and responsibilities. We are therefore providing this guidance to help IPs comply with our rules and guidance as well as relevant legislation which aim to achieve better outcomes for consumers and market participants following a failure of a regulated firm.

3. This guidance is aimed at IPs appointed over firms solely authorised by the FCA under FSMA. The guidance may also be relevant to IPs appointed for firms that are dual regulated by the FCA and Prudential Regulation Authority (PRA)[3].

4. This guidance is not exhaustive, neither is it a substitute for reading and complying with the FCA's Handbook and other applicable legislative requirements and guidance.

The FCA's role in firm failures

5. The FCA has a role in every regulated firm failure and the role will vary depending on the individual circumstances of the firm. The role may be consenting to an out of court appointment of an administrator or part of our ongoing supervision of the firm.

6. While we are not able to stop firms failing, we aim to minimise harm to consumers and markets that may arise from a disorderly firm failure. This involves working with IPs to reduce such harm where possible.

7. The FCA has a range of powers provided by FSMA which enables us to intervene and take action in insolvency proceedings in relation to a firm to protect consumers and markets. We may also act prior to a firm entering into an insolvency process; this can include, for example, imposing requirements on the firm to take specific actions including the preservation of the firm's books and records, varying the firm's regulatory permissions or taking steps to make an application to the court to place the firm into an insolvency procedure.

[3] The FCA is the competent authority for solo-regulated firms. The PRA is the competent authority for dual-regulated firms. The Bank of England is designated as the resolution authority for dual regulated firms and certain investment firms (i.e. IFPRU 730k investment firms or solo-regulated firms that are part of a group subject to the Bank of England's resolution power under the Banking Act 2009).

Chapter 2: Pre-insolvency

Sufficient experience for an appointment over a regulated firm

8. The Insolvency Code of Ethics requires that an IP should only accept an insolvency appointment where the IP has or can acquire sufficient expertise. If a firm is conducting regulated business, we expect the appointed IP to understand the business model and its regulated activities, or have a detailed plan to gain a full understanding of these shortly after their appointment. This could, for example, involve engaging relevant specialists.

9. We also expect the IP to know what regulatory requirements apply to the firm and identify any issues with compliance. The regulatory requirements may include:

    - **Principles for Businesses (PRIN)**: these apply, in whole or in part, to all FSMA authorised firms and set out high-level but fundamental obligations with which firms must comply under the regulatory systems regarding various aspects, such as treating customers fairly, conflicts of interest and how a firm should communicate with the regulator.

    - **Client Assets Sourcebook (CASS)**: these requirements apply to firms that hold or control client assets[4]. This includes distribution and transfer provisions in the event of a firm failure.

    - **Compensation Sourcebook (COMP) and Disputes Resolution Complaints Sourcebook (DISP)**: COMP contains the rules and guidance that set out the circumstances in which the Financial Services Compensation Scheme (FSCS) may pay claims for compensation where relevant and to whom. DISP sets out how complaints are to be dealt with by firms, the reporting of complaints to the FCA and the operation of the Financial Ombudsman Service.

    - **Supervision Manual (SUP):** this sets out the relationship between the FCA and firms, key individuals within them, their appointed representatives and tied agents, and those who own or control the firm.

    - **Individual requirements, variation of permissions and limitations**: the FCA applies these to an individual firm to vary its regulatory permissions and/or restrict the firm's activities[5]. We may ask a firm to apply for a variation of permission (VVOP) or the imposition of a requirement (VREQ) or impose it via our own-initiative powers (OIVOP/OIREQ). A firm must continue to comply with these variations, requirements and limitations after it enters into an insolvency procedure.

10. We expect an IP to consider whether they have the capacity to take on an appointment, bearing in mind their existing appointments, and the size and complexity of the proposed appointment. If the IP does not have in-house resources to cover this, they should consider how appropriate resources will be engaged.

[4] References in this guidance to client assets refers to both client money and custody assets unless otherwise stated.

[5] Sections 55J and 55L of FSMA

Pre-insolvency checks

11. An IP may often be involved with a firm before it becomes insolvent and advise on whether the firm has the necessary arrangements in place. This includes:

    - A wind-down plan: this details the steps that a firm will take in the event of insolvency, any risks associated with the wind-down and mitigating actions for these. An IP may wish to consult the FCA's Wind-down Planning Guide when advising on the robustness of a wind-down plan to help ensure an orderly wind-down of the firm.

    - A CASS resolution pack for certain firms that hold client assets[6]: this contains specific documents and records relating to a firm's holding of client assets, which will help the IP to return client assets more quickly following a firm failure.

Early engagement with the FCA

12. We expect an IP to engage with us at an early stage, both prior to and after appointment to a regulated firm. The FCA's rules in the Handbook will continue to apply to a firm in an insolvency procedure while it remains authorised. The FCA also has statutory powers to get involved and this differs depending on the insolvency procedure and the type of regulated firm (that is, authorised or formerly authorised, appointed representative or a firm which is or has been carrying out regulated activities without permissions)[7].

Administration

FCA consent to out of court administrator appointments

13. Should a firm or its directors seek to appoint an administrator through an out of court process[8], the administrator cannot be appointed without the FCA's consent which must be filed with the notice of appointment[9]. This should be requested by completing a template letter (see Appendix) and sending it to firm.queries@fca.org.uk or the firm's supervisory contact at the FCA.

14. Consent requests should be submitted by the IP or their legal representatives in a timely manner to ensure that the FCA has sufficient time to consider the request and, where applicable, grant consent before the appointment takes place.

15. When assessing the consent request, the FCA will consider the IP's ability to take on the appointment. This assessment is likely to include (but not limited to) the following factors:

    - the IP's expertise in taking appointments as administrators

    - whether the IP is satisfied that administration will achieve a better result for the firm's creditors than another insolvency procedure

    - the IP's independence from the firm when taking on the appointment[10], and

[6] Investment firms (CASS 10) and debt management firms (CASS 11.12)

[7] Part 24 of FSMA

[8] Paragraph 22, Schedule B1 of the Insolvency Act 1986

[9] Section 362A FSMA

[10] The IP will need to conduct their own conflicts and independence checks before accepting an appointment.

- the IP's past conduct if they have taken previous appointments over regulated firms.

16. Depending on the circumstances of the prospective appointment, the FCA may ask additional questions, which must be answered to a satisfactory standard before consent can be issued.

17. Upon appointment, we expect the administrator to send their notice of appointment to us at firm.queries@fca.org.uk[11]. This will enable us to update our internal and external records on the firm (e.g. the Financial Services Register of regulated firms and individuals).

18. Where an administrator has been appointed and the FCA's consent has not been obtained, the administrator must contact us to request retrospective consent with an explanation of why consent was not sought earlier. This should be done as soon as the administrator becomes aware that consent should have been sought. If retrospective consent is provided, the FCA is not opining on the validity of the appointment, or ratifying, agreeing to or with, and/or endorsing any of the actions taken between the administrator's appointment and the date on which the consent is provided. The administrator should seek legal advice on the validity of their appointment in these circumstances.

Sharing of court documentation with the FCA

19. The FCA is entitled to participate in court proceedings in relation to the regulated firm, such as the hearing of an administration application[12]. An administrator must therefore share any court documentation, administration applications and other documents required to be sent to creditors of the firm with us. The administrator should do so at the earliest opportunity, so that we have sufficient time to decide if our participation in the administration is appropriate.

FCA ability to apply for an administration order

20. If appropriate, the FCA can apply to the court for an administration order in respect of a regulated firm.

Special administration

21. The Investment Bank Special Administration Regime (SAR) is a bespoke insolvency regime for investment firms that hold client assets[13]. The SAR establishes three objectives for the special administrator: return client assets as soon as is reasonably practicable; timely engagement with market infrastructure bodies; and rescue the investment firm as a going concern or wind it up in the best interests of the creditors[14].

22. The SAR interacts closely with the CASS rules of the Handbook to provide a mechanism under which client assets can be returned to clients more efficiently in the event of an investment firm failure. The SAR is currently available for firms which meet the definition of 'investment banks', which includes a range of firms conducting investment business while holding client assets.

[11] Section 361 of FSMA

[12] Sections 362 of FSMA

[13] Section 232 of the Banking Act 2009

[14] SAR Regulation 10(1)

23. The FCA is entitled to be heard at a hearing of a special administration order and any other court hearing in relation to the firm[15]. The special administrator should therefore share court documentation with us at the earliest opportunity, so that we have sufficient time to decide if our attendance is appropriate. The FCA is also able to direct the special administrator to prioritise one of the special administration objectives over the other objectives[16].

24. If a firm is eligible to enter special administration but is considering entering a different insolvency procedure, an IP cannot be appointed over the firm unless the FCA is notified of preliminary steps taken in respect of that procedure. Following receipt of the notice, the FCA has a period of two weeks to inform the person who gave notice whether it consents to the insolvency procedure, whether it intends to apply for that (or an alternative) insolvency procedure or whether it intends to apply for a special administration order[17].

Statutory demands

25. The service of a statutory demand on a regulated firm should be notified to the FCA. We therefore expect an IP engaged by a firm in this situation to ensure that the firm has notified the FCA if they have received a statutory demand[18].

Winding up petitions

26. The FCA has the right to present a winding-up petition to the court in respect of a regulated firm[19].

27. In addition, where a party (other than the FCA) presents a petition to wind up a regulated firm, including where there is an application to have a provisional liquidator appointed, the firm must notify the FCA about this[20]. If an IP is subsequently appointed to the firm, we would expect the IP to engage with the FCA and ensure that a copy of the winding up petition has been provided to the FCA.

Liquidation

28. The appointment of a liquidator must be notified to the FCA[21]. We therefore expect a liquidator to ensure that the firm has notified the FCA of the liquidator's appointment as soon as possible. The appointment of liquidator documents, including copies of the resolution to wind up and the certificate of appointment, must also be sent to firm.queries@fca.org.uk[22].

29. The FCA has the right to participate in any court proceedings in relation to a liquidation, attend creditors meetings and participate in the decision procedure[23]. We therefore expect a liquidator to ensure that court and creditor documentation is shared with us at the earliest opportunity, so that we have sufficient time to decide if our participation is appropriate.

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[15] SAR Regulation 5(2)

[16] SAR Regulation 16.

[17] SAR Regulation 8

[18] Statutory demands and winding-up petitions are currently restricted until 31 December 2020 following the Corporate Insolvency and Governance Act 2020.

[19] Section 367 of FSMA

[20] SUP 15.3.21R

[21] SUP 15.3.21R

[22] Section 370 of FSMA

[23] Sections 374 of FSMA

Notice if a firm is in the same group as a bank

30. An IP should be aware that, where a firm is in the same group as a bank (whether established in the UK or another EU member state), the firm is required to notify the FCA, PRA and the Bank of England seven days before entering an insolvency procedure[24]. An insolvency application cannot be determined until the Bank of England has informed the firm that they do not intend to exercise a stabilisation power over the firm under the Banking Act 2009 or the PRA and Bank of England have confirmed that they do not intend to apply for bank insolvency under the Banking Act 2009.

Members' voluntary liquidation and creditors' voluntary liquidation

31. If a members' voluntary liquidation (MVL) is being considered for a firm, the prospective IP must consider all contingent liabilities, including complaints and other redress claims, including whether they are appropriately reflected in the directors' declaration of solvency. This should involve thoroughly assessing the solvency of the firm, including querying with the firm's management details of any prospective contingent liabilities and complaints made to the Financial Ombudsman Service. If the IP is uncertain on this, they should discuss the matter with us and, if applicable, the FSCS prior to accepting the appointment.

32. Should it transpire that the firm is not solvent, an IP may need to consider the conversion of an MVL to a creditors' voluntary liquidation. We expect the IP to give appropriate consideration on whether there is a conflict for the same IP to act in both processes.

Creditors' committees[25]

33. After a firm has been placed into administration (or special administration), the administrator must, when seeking approval from the creditors on the administrator's proposals, invite the creditors to decide whether a 'creditors' committee' should be established. A similar type of committee can be set up in the context of liquidation, which is known as a 'liquidation committee'.

34. The purpose of the creditors' committee is to assist the IP in the discharge of their functions and to approve the IP's remuneration. Creditors will include all stakeholders of the failed firm, including customers, and their interests are significant to the IP in fulfilling their duties. IPs must therefore invite creditors of a regulated firm to form a committee to enable them to provide a 'voice' in the insolvency process. Clients for whom the firm holds client assets should be considered when forming a creditors' committee and there should be appropriate representation from across all types of clients for whom the firm is holding client assets and, where relevant, the FSCS on the committee.

Insolvency costs

35. We expect an IP to properly record insolvency fees and expenses throughout the insolvency process, and any fees and expenses charged to the client estate should be directly attributable to the distribution of client assets. We also expect that the IP is efficient in their work and take steps with the aim of reducing costs that would be borne by clients and creditors wherever possible.

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[24] Sections 120A of the Banking Act 2009

[25] References in this guidance to creditors' committee refers to any creditors' committee or liquidation committee established by an IP under Part 17 of the Insolvency (England and Wales) Rules 2016 unless otherwise stated.

36. Fees estimates and details of expenses that the IP considers will, or are likely to be, incurred should be realistic and communicated to clients and creditors in a timely and clear manner. An IP should carefully consider when they are in a position, having fully assessed the firm's business and understood the complexities of the insolvency, to seek approval for the basis of their remuneration and, where relevant, to provide a fees estimate and details of expenses to creditors and clients.

37. We expect an IP to properly consider expenses that may be incurred (i.e. legal expenses). It is important to note that if lawyers or other parties are working in conjunction with an IP, they will also need to be able to accurately account for their time, particularly in relation to work directly attributable to the distribution of client assets.

38. We expect an IP to properly allocate costs to relevant estates and, where relevant, consult with, and seek approval from, the creditors' committees and/or seek directions from the court. We expect the IP to update us on the costs that they are charging to the relevant estates, and report this clearly to clients and creditors. An IP should discuss this fully with the creditors' committee, if one is established, when gaining their approval to draw costs as set out in insolvency legislation. In some cases, the creditors' committee may wish to consider the appointment of an independent cost assessor.

39. Given the role of the creditors' committee in this process, it is important that it appropriately represents the client base of the firm. IPs should consider how they ensure appropriate representation across all types of stakeholders of the failed firm on the committee throughout the insolvency process.

Disclosures to the market in relation to firms that have listed or traded securities

40. Any firm with financial instruments that are traded on a UK or EU trading venue, such as the London Stock Exchange, needs to consider its disclosure (including inside information disclosure) obligations to the market on an ongoing basis. This would include any deterioration of its financial position and any decisions to appoint an IP. Any required announcements should be made without delay, although we would expect the firm or the IP to discuss the situation with the FCA's Primary Market Monitoring team at an early stage to ensure steps are taken to prevent a disorderly market.

Chapter 3: Entering insolvency

Interaction with the FCA

41. If a firm is considering entering or has entered into an insolvency process, we would expect an IP to provide regular updates to the FCA for a period agreed with us. We would expect updates on items including the following:

    - client communications
    - client contacts and questions
    - progress in reconciling, distributing or transferring client money and custody assets in line with the CASS rules and relevant insolvency legislation

- client complaints and compensation claims (including interface with the Financial Ombudsman Service and FSCS)
- quality of books and records
- possible sale of the client book or business (if contemplated) including the marketing process, the ability of any proposed purchaser to take on the book, and the implications of any requirements over the firm
- staffing and supplier issues
- adverse press or other commentary
- any intelligence or information arising from the insolvency or investigations into directors' conduct that could give rise to harm
- insolvency costs, especially those relating to the client estate, and
- interaction with foreign regulators and/or other UK authorities involved in the firm's insolvency process.

Communicating with clients

42. If a firm is considering entering or has entered into an insolvency process, we expect an IP to have a communication strategy in place. This strategy should consider the key messages for clients, what their immediate concerns may be and the information they are going to need, the format of that information and how quickly it can be disseminated. Information about the practical effects of the appointment will be the most important initially and must be clear for clients.

43. In addition, the following practical issues should be considered:

- **Use language that is clearly understood by the audience of the communication**[26], particularly if they are retail or vulnerable consumers. This includes adapting template communications to help ensure they are clear, fair and not misleading to the recipient and are easy to understand. An IP should also consider using headings and highlighting key actions that need to be taken by the recipient. Given the rise in scams, any client communications should have a standard 'scam smart' messaging and make clear that a consumer is not required to use the services of a claims management company to pursue a claim. Key messages should not be hidden (i.e. they should be at the top of the communication).
- **Ensure sufficient resource is available for communications with the firm's clients**, particularly where there is a significant number of retail clients. This may require additional phone lines or a call centre, producing scripts for staff including frequently asked questions and, in some cases, providing communications in different languages.
- **Share draft versions of key client communications with the FCA (and other relevant authorities) for comment before finalising**, particularly communications regarding high profile or complex regulated firm failures (e.g. firms that have significant client assets holdings or vulnerable clients). Sharing client communications with the FCA would also help to ensure these are consistent with FCA press releases, where relevant, upon an IP's appointment.

[26] This is in accordance with the firm's obligations under Principle 7 (communication with clients).

44. We are aware that there are statutory communications, including notices, letters and reports, that an IP must issue before and during their appointment. If any communication contains references to the FCA, we expect these to be factual, necessary and, in the case of high profile and complex failures, communicated to the FCA for comment in advance of publication and in good time so that the IP is able to meet any statutory deadlines for such communications. These communications should be sent to firm.queries@fca.org.uk.

Interaction with FSCS

45. The FSCS is the UK's compensation scheme when a protected regulated firm is unable, or unlikely to be able, to pay claims against it. Broadly speaking, the FSCS covers deposits, investments, insurance, home finance advice and arranging advice.

46. The PRA makes the rules governing the compensation scheme relating to claims for a deposit, under a contract or insurance or in respect of Lloyd's managing agents. The PRA's rules are in the Depositor Protection and Policyholder Protection parts of its Rulebook. The FCA makes the rules so far as other claims are concerned. The FCA's rules are in COMP.

47. If the conditions for FSCS payment are met, the FSCS can pay this amount – generally up to the amount of £85,000 per eligible person per firm[27] - to investors that meet the FSCS's eligibility criteria and who have a valid claim. For general insurance firms and intermediaries, there is a limit of 90% of the value of the insurance claim and in some cases 100% of the claim.

48. Once the FSCS has paid compensation, the claimant's legal rights are usually assigned to the FSCS. This enables the FSCS to make a claim in the firm's insolvency. Usually, the FSCS ranks as an unsecured, ordinary creditor for FCA-related FSCS claims.

49. If FSCS compensation is available for clients, an IP should engage with the FSCS at the start of an insolvency process and, if possible prior to appointment, to issue initial communications and to work with the FSCS so that they may declare the firm to be in 'default'. An IP should also engage with the FSCS to agree what information the FSCS will need regarding the firms' records and operations, and to agree how to provide this. A suitable approach to enable the FSCS to validate eligibility and process claims for compensation should be agreed.

50. Following appointment, the IP should liaise with the FSCS to issue a communication to clients and creditors explaining FSCS eligibility rules and the levels of compensation that may be payable by the FSCS. This may be, for example, within the IP's communications or a separate letter from the FSCS.

Interaction with the Financial Ombudsman Service

51. The Financial Ombudsman Service is an independent service for resolving disputes between consumers and businesses, and with a minimum of formality on a fair and reasonable basis. The rules and guidance relating to the operation of the Financial Ombudsman Service is set out in the DISP rules of the Handbook.

52. We would expect an IP to engage with the Financial Ombudsman Service at the beginning of an insolvency process to establish the number of complaints against

[27] See COMP 9.2.1BR. The limit is per eligible person in respect of investments, home finance and client money held by debt management places with firms declared in default from 1 April 2019.

the failed firm and to agree how those complaints will be dealt with going forward. An IP may also need to engage with the FSCS (if applicable) to enable them to deal with any of the complaints.

Notifying customers that they may have a claim for redress

53. If a firm's conduct has been such that customers may have a claim for redress against the firm, we expect an IP to invite claims from the entire population of customers who may be eligible for redress. The IP should send all documents regarding the insolvency to all relevant customers.

Appointed representatives

54. An appointed representative (AR) is a firm or person who undertakes regulated activities on behalf of a firm that is directly authorised by the FCA. The authorised firm is known as the AR's 'principal'. There must be a written contract between the principal and the AR documenting the arrangement. The principal takes full responsibility for ensuring that the AR complies with our rules.

55. Where an IP is appointed over a firm that is an AR, the IP should notify the principal of the AR and consider the terms of the contact between the AR and its principal firm. The principal should be allowed access to the AR's staff, premises and records where required to enable it to meet its regulatory obligations in respect of the AR. The AR may not be able to continue to undertake regulated activities following the insolvency and the IP should request that the principal take the required steps to remove the AR from the Financial Services Register. The IP should also consider our expectations when considering the sale of a client data (see paragraph 121).

56. Where an IP is appointed over an FCA authorised firm that is the principal firm in respect of one or more ARs, the IP should be aware that the ARs undertake regulated activities on behalf of the authorised firm and the authorised firm is fully responsible for ensuring that the ARs comply with FCA rules. Where an AR is removed and/or its customers are transferred to another AR or authorised firm, the IP should ensure the AR continues to treat customers fairly until all regulatory obligations have been met and should act to remove the AR from the Financial Services Register in a timely manner.

Chapter 4: Post insolvency

Claims process

57. We expect an IP to have a suitable claims process in place for clients and creditors. An IP should consider how this claims process is structured to ensure that it is easy to handle from both a client and the IP's perspective. For example, an IP may want to explore the idea of handling the claims process via a web portal.

58. We expect an IP to consider the following when designing their claims process:

- how statements to clients are issued
- how clients and creditors validate their claims

- how an application to the FSCS can be built into this
- validation of KYC details
- how non-responders are treated
- the process should client address details be incorrect
- the need for clients and creditors to add bank account details
- communication to clients on access to the claim portal
- any translations required for non-English speakers
- the process if clients choose to abandon small claims, and
- information/data to be collected regarding engagement with the claims process.

59. An IP may need to consider demonstrating the claims process with the creditors' committee before making it available. They should also consider using the technology systems of the failed firm if suitable (avoiding unnecessary costs). In any case, an IP should consider the need to maintain IT contracts, the resilience and usability of the systems and data security considerations for migration.

FCA participation in court cases and creditors' committees

60. The FCA has statutory powers to participate in court proceedings in relation insolvency proceedings for a regulated entity[28]. The IP should give us due notice of any intended court applications and, if requested, share draft documents with us within an appropriate timeframe. We may request prior copies of any court papers or submissions made by the IP or the firm, to ensure references to the FCA are correct and appropriate, and consider whether the FCA wishes to make its own representations (e.g. if a precedent is being set).

61. The FCA has rights to make representations at meetings of the creditors' committee and are required to receive any documents sent to creditors[29]. We may do this depending on the case and so should be informed of the creation of creditors' committee (or liquidation committee as appropriate), and sent invitations to meetings.

Confidentiality

62. We will not discuss any aspect of the firm's regulatory history at creditors' committee meetings and if questions such as these are raised, they can be raised with the FCA through firm.queries@fca.org.uk. The FCA may also request copies of presentations and minutes taken at the meetings of the creditors' committee. An IP should also ensure that the creditors' committee members are aware of the confidentiality of the meetings.

Client assets

63. CASS provides detailed rules for a firm to follow when it holds or controls client money and/or custody assets (collectively 'client assets') as part of their business. This is to allow client assets to be returned as quickly and as whole as possible to clients if a firm enters an insolvency process. CASS applies to the

[28] Sections 362 and 371 of FSMA

[29] Sections 362 and 371 of FSMA

following types of firms: investment firms, general insurance intermediaries, debt management firms and claims management companies.

64. If a firm holding client assets enters an insolvency process, an IP will need to make sure that such assets continue to be treated in line with CASS and, in particular, follow the post-failure rules for returning client assets[30]. If the firm enters special administration, the IP will also need to comply with the SAR regulations and rules (see paragraph 21).

Steps to take immediately after appointment

Take control of client assets

65. Following appointment, an IP will need to take control of client assets (physical and electronic) and the books and records of the firm. The IP should also identify key individuals and systems required to manage client assets of the firm, including third party administrators, system suppliers and employees of the firms. This information should be available in the firm's CASS resolution pack if applicable[31].

66. CASS sets out requirements on how and where a firm can hold client assets, including appropriate selection of third parties, diversification of client money holdings and when set-off arrangements with third parties over custody assets (e.g. under a lien) are permitted. An IP will therefore need to consider where client assets are held, who has access to them, diversification risks, the operation of any set-off arrangements, and any other requirements over the client accounts.

67. Where a firm is holding client money, the appointment of an IP constitutes a 'primary pooling event' (PPE)[32]. Broadly speaking, this means that all client money held by the firm in client bank accounts and client transaction accounts (if applicable) is notionally pooled, forming a client money pool (CMP). Any client money received after a PPE does not form part of the CMP and is required to be returned promptly to relevant clients (see paragraph 82 below).

Operate different estates

68. We expect an IP to operate at least two separate estates: the client estate comprising client assets (against which only clients can claim) and the general estate comprising the firm's assets (against which all creditors can prove). The client estate is split in various ways – custody assets should be treated separately from client money, and client money should be split between pre-and post-PPE client money as described above.

69. As stated earlier, an IP should accurately allocate costs between the estates. An IP should also accurately record time spent on the different estates and, in respect of the client estate, distinguish time and expenses spent on client money and custody assets as well as pre-and post-PPE client money.

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[30] CASS 5.6 (for general insurance intermediaries), CASS 6.7 and CASS 7A (for investment firms), CASS 11.13 (for debt management firms), CASS 13.11 (for claims management companies)

[31] This is required by CASS 10 (for investment firms) and CASS 11.12 (for debt management firms). It contains documents and records relating to the firm's holding of client money and custody assets, which will help the IP to return client assets more quickly following an investment firm failure.

[32] CASS 5.6.5R, CASS 7A.2.2R, CASS 11.13.4R and CASS 13.11.3R

Immediate reconciliation and final top-up/withdrawal (for firms in the SAR)

70. If a firm has entered special administration and is holding client money, the IP is required to conduct a post-administration client money reconciliation immediately after being appointed and to make a transfer to or from the firm's client bank accounts following that reconciliation[33]. We expect IPs to conduct this reconciliation as soon as they can post appointment. This enables the IP to correct any shortfalls (or excesses) in the firm's client bank accounts using the firm's previous reconciliation method.

71. Where the reconciliation identifies a shortfall in client money, the IP must top-up the client bank account with monies from the firm's own bank account (where there are funds available). Where the reconciliation identifies an excess in client money, an IP must withdraw this from the client bank account and transfer it to the firm's own bank account.

Determine client entitlements

Calculate client entitlements

72. After taking control of client assets, the IP must identify and calculate each client's entitlement in accordance with the CASS rules. This will involve:

    - carrying out client money and custody asset reconciliations (as relevant)[34] to determine the client assets positions as at the time of the firm's failure, and
    - determining each client's entitlement to client money and custody assets as at the point of failure with reference to the reconciliations above.

73. In respect of client money, each entitlement must be established at the point of failure, except in relation to cleared open margin transactions by investment firms[35]. In respect of custody assets, if an IP uses the book value for establishing entitlements, the IP should manage clients' expectations that they may be less value when it comes to the actual return of the asset.

Manage currency risks

74. An IP will need to consider:

    - what currency they should calculate each client's entitlement
    - what currency they should continue to hold client money in, and
    - what currency the IP should return client money in.

75. As part of the above considerations, we expect an IP to look at any relevant contractual terms and the currency of the client's claim.

Treatment of shortfalls

76. A shortfall is the amount by which client assets held by the firm are not sufficient to meet all client entitlements. A shortfall may arise because the costs of

[33] SAR Regulation 10H

[34] CASS 6.6.46R, CASS 7.15.15R and CASS 7.15.26AR

[35] CASS 7A.2.R(-2). CASS requires investment firms to apply the value achieved on close out of all cleared open margin transactions. That is, hindsight should be applied (the 'Hindsight Principle'). For all other open transactions at PPE, the rules require these to be valued using the notional closing or settlement prices prevailing at the PPE.

distributing client assets may be deducted from client assets held by the firm and/or poor controls and record keeping by the firm before it failed.

77. A distribution cost is a cost directly attributable to the distribution of client assets. An IP should endeavour to minimise costs incurred in the distribution process and return client assets to the client as soon as reasonably practicable. As explained above, distribution costs should be recorded and recovered in accordance with insolvency legislation.

78. For shortfalls in client money, including distribution costs, an IP is required to allocate these to all clients of the firm on a pro rata basis[36]. For shortfalls in custody assets due to distribution costs, an IP should consider and agree with the creditors' committee the appropriate method for allocating these. The IP can explore various options in this consideration, such as applying a percentage of the asset value, applying a fixed fee per client or allocating such costs on a pro rata basis.

79. For other shortfalls in custody assets, if the firm has entered into special administration, the SAR requires shortfalls in custody assets of a particular description in an omnibus account to be borne pro rata by all clients for whom the investment firm holds assets of that particular description in that account in proportion to their beneficial interest in those assets[37].

80. Clients should be considered contingent creditors in respect of any shortfall. Clients may also have a claim against the general estate for any client assets that are not returned as part of the distribution.

FSCS compensation for shortfalls

81. A client may be eligible to claim for compensation from the FSCS for any loss incurred because of a shortfall in client assets, if the criteria in COMP are met. An IP should therefore liaise with the FSCS to notify clients if they are able to claim from the FSCS in respect of client assets shortfalls. Where there is eligibility, we expect the IP to liaise with the FSCS to set up the most efficient way in which the FSCS claims can be managed. The IP should also consider and work with the FSCS in relation to claims where the FSCS is able to "look-through" to compensate underlying beneficiaries who may not have a direct contractual relationship with the failed firm[38].

Client money received by the firm after failure

82. A firm is likely to have unsettled or incomplete transactions at the point of entering an insolvency procedure, which may result in the firm receiving client money after it has failed. The IP is required to keep post-PPE client money separate from the CMP (e.g. in a separate bank account that does not contain money in the CMP) and promptly return these to relevant clients directly.

83. An IP should consider the costs of this process. CASS permits the IP to retain costs properly attributable to the distribution of post-PPE client money to each client from these monies. This is different to the costs of distribution of the pre-PPE client money pool, where costs are deducted from the pool before distribution to clients.

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[36] CASS 7.17.2R(4), CASS 11.6.1R(3), CASS 13.1.3R(3))

[37] SAR Regulation 12

[38] COMP 12

84. An IP should also set up procedures to monitor and allocate receipts post failure. For example, the firm may continue to receive dividends for clients in respect of shares and these will need to be allocated promptly to the appropriate shareholders.

Distributions to clients and transfers to a solvent firm

Distributions of client money

85. After determining entitlements to the CMP, an IP must, as soon as reasonably practicable, distribute the client money to each client who is a beneficiary of the CMP rateable to their entitlement. In this process, an IP will need to consider the following issues:

    - how money is returned to the relevant client (e.g. whether it should go directly to the client, should the client be able to nominate a receiving broker, or should it be part of a transfer of client money/custody assets to another firm)
    - if being returned directly to the client, verifying a client's bank details, and completing any required KYC, before returning client money
    - costs of returning client money to each client, and
    - if the client cannot be contacted or disclaims their entitlement.

86. We recognise that an IP needs to close the client estate and cannot retain unclaimed client money indefinitely, but are equally mindful that clients must be given sufficient opportunity to claim their assets. For investment firms, CASS permits[39] an IP to use allocated but unclaimed (or declined) client money entitlements and unallocated client money towards a shortfall in the CMP[40], providing certain reasonable steps have been taken to trace clients concerned. See paragraph 97 for further details on closing the client estate.

Transfer of client assets

87. An IP should consider whether a transfer of client assets to a solvent firm is possible. A transfer is likely to incur lower costs of distribution than a direct return to clients. There are various ways that a transfer can be facilitated: for example, as a pre-pack administration or as part of distribution of client assets in accordance with the CASS rules post insolvency.

Pre-pack administration

88. A pre-pack administration is a sale of all or part of a firm's business and assets, which is negotiated prior to administration on the basis that the sale will be concluded immediately on or shortly after the firm enters administration. Once the plan is ready, the firm (or its directors or creditors) can appoint an administrator, who can then conclude the sale. Assets would be transferred to the purchaser, but generally not any liabilities, so the failed firm will be left with unpaid liabilities and fewer, if any, assets.

89. This type of sale may be better for clients and markets generally if the business of a failed firm, together with relevant client assets, is transferred to a different firm to ensure continuity of service. Clients may then continue to receive services

[39] CASS 7A.2.6AR and CASS 7A.2.6CE for our expectations on "reasonable steps".

[40] After payment of costs in accordance with the statutory waterfall provision (CASS 7.17.2R).

uninterrupted, avoid opportunity costs from having their assets stuck in the failed firm's insolvency and avoid loss of value arising from premature closure of positions or loss of tax wrappers.

Transfer of client assets as part of the distribution of client assets

90. The CASS rules permit an IP to transfer client assets to another entity providing certain conditions in CASS are met[41].

91. An IP would need consider the following practical issues when conducting a transfer of client assets:

- whether the transfer will be a whole or a partial transfer
- whether client consent is provided or needed
- what client communications, including notifications, are necessary
- whether there any requirements on the firm that may affect the transfer (in particular, an asset requirement preventing a transfer without conditions being met[42])
- the type of firm which can take on the business and whether a firm has appropriate regulatory permissions
- the consideration for the transfer and how it will be structured
- warranties and indemnities (if applicable)
- whether the transferee's systems are compatible and if any other arrangements need to be put in place (e.g. where the firm has outsourced functions to a third-party administrator)
- the timetable of the transfer
- the need for any applications for waivers (see paragraph 101)
- arrangements for clients to transfer out of the transferee
- arrangements for assets which cannot be transferred
- transfer of staff in accordance with the Transfer of Undertakings (Protection of Employment) Regulations (TUPE) and whether there is a need for a transitional services agreement
- whether staff are needed to continue with the insolvency, and
- whether there are any phoenixing concerns (see paragraph 118).

92. Where an IP is transferring client assets as part of the distribution of client assets, the IP should use the creditors' committee to discuss the proposed transfer and keep the FCA updated with their plans.

Bar dates

93. The bar date mechanism established in the SAR gives a special administrator the power to set deadlines for clients to submit claims for the return of their assets.

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[41] CASS 5.5.80R(2), CASS 6.7.8R, CASS 7A.2.4R(4), CASS 11.13.7R – CASS 11.3.9R, CASS 13.11.6R – CASS 13.11.10R

[42] Section 55P of FSMA

94. A bar date gives certainty over the group of claimants for an upcoming distribution, ensuring that a distribution of client assets by the special administrator can progress smoothly without disruption from late claimants. In general, a late claimant may not challenge a distribution that was made after a bar date, provided the special administrator carried it out in good faith.

95. In setting a bar date, the special administrator would have to allow a reasonable time after the bar date notice has been published for clients to be able to calculate and submit their claims. The special administrator would then make a distribution of client assets in accordance with a distribution plan (if applicable) or according to clients' entitlements established under the claims received.

96. The special administrator can set two types of bar dates:

- A 'soft' bar date whereby the special administrator can set a deadline for clients to submit claims without having to seek court approval and make interim distributions[43]. Late claimants would lose the right to challenge a distribution made prior to the receipt of their claims to meet claims made before the bar date. This allows the special administrator to make any necessary distributions and proceed with the special administration process, as they would not be required to give regard to the entitlements of clients who had failed to submit claims in good time. However, the special administrator would have to make a distribution to late claimants if there are still client assets available to do so.

- A 'hard' bar date whereby the special administrator can set a final cut-off date for clients to submit claims, with court approval, after which any further client claims can be disregarded in their entirety, any remaining assets can be moved to the general estate and the client estate can be closed completely[44]. Given proprietary rights are extinguished after a hard bar date, the CASS rules require the special administrator to take reasonable steps to notify all clients of the fact they may have a valid claim for client assets prior to the hard bar date taking effect (see below).

Closure of client estate

97. At the appropriate point, the IP will need to close the client estate. If the firm is in special administration, the SAR's hard bar date mechanism may be applied before this occurs.

98. For investment firms, the CASS rules require the IP to take reasonable steps to notify all clients of the fact that they may have a valid claim for client assets, prior to the closure of the client estate or a hard bar date under the SAR regulations taking effect. The CASS rules provide an evidential provision outlining the minimum client contact required[45]. Specifically, we believe it is reasonable for an IP to make at least two attempts to contact the client using different methods (e.g. an email and a phone call) for a professional client and three contact attempts for a retail client. The client must be notified that if no claim is made by the cut-off date, proprietary rights to the claim will be lost and any claims made will be as a general creditor.

99. Where client money is not claimed, we would expect this go to towards the shortfall as outlined in paragraph 86 above.

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[43] SAR Regulations 11 and 12A

[44] SAR Regulations 12B to 12C

[45] CASS 6.7.4E and CASS 7A.2.6C

100. We would expect an IP to share any court documents with us in good time prior to closing the client estate.

Waivers process

101. Should an IP be unable to ensure a firm's compliance with certain rules in the FCA Handbook, the IP may need to consider applying for a waiver or modification of the rule[46]. For example, a waiver may be needed where there is a requirement to obtain client consent to a transfer to a new party (e.g. if clients have not previously consented to a transfer through the terms of business). Note that contract law will also need to be considered by the IP in addition to obtaining a waiver of a requirement in CASS. The IP should discuss any waiver or rule modification application with the firm's supervisor at the FCA in the first instance.

102. All waiver applications must be submitted through the FCA's Connect portal. The FCA will grant the waiver if satisfied the following statutory conditions are met:

- compliance with the rule would be unduly burdensome, or would not achieve the purpose for which the rules were made, and
- the waiver would not adversely affect the advancement of any of the FCA's operational objectives.

103. Further information about applying for a waiver is available on the FCA's website.

Hardship policies

104. Until the IP is in a position to distribute client assets, these will not be returned or available to clients. In such situations, the IP should consider hardship cases to help ensure that they are identified and responded to in an appropriate and consistent manner, including liaising with the FSCS if applicable. It may be that the IP is able to provide earlier distributions of client assets to clients who can demonstrate hardship (although this may not always be possible). We therefore expect an IP to identify potential hardship policies and assess whether there is anything that can be done to support these cases. However, we recognise the ability of the IP to support will depend on the circumstances of the case.

Corporate action policies

105. Where a firm holds client assets, clients will not be able to exercise their rights over the assets where there are corporate actions. This may include being unable to participate in a rights issue, exercise warrants or vote at a general meeting. In such situations, an IP should assess whether it is possible to offer clients the opportunity to participate in corporate actions prior to distribution, which assets and actions would be eligible and the relevant charge for doing this. If the IP considered it appropriate, we would expect the IP to establish a corporate actions policy to ensure, so far as possible, that all clients with holdings of assets within the policy are aware of services offered in accordance with the policy.

[46] The FCA would not be able to grant a waiver of rules deriving from EU requirements.

Continuity of supply

106. We expect an IP to consider how they will make sure that the failed firm continues to comply with our regulatory requirements whilst it remains authorised. If the firm loses a supplier, it is still required to comply with our rules. The continuity of service provisions in the Insolvency Act[47] assist an IP by enabling them to limit the terms that essential suppliers can impose as a condition for the continued supply of their service and compel continued supply by restricting the effect of existing insolvency-related terms in an essential supply contract. If the firm has entered special administration, the SAR further restricts suppliers of the failed firm from terminating supply after commencement of the administration[48]. Continuity of supply also helps to facilitate distribution of client assets (e.g. where third party suppliers have been used to maintain client records and IT systems).

107. The continuity of supply provisions is not available for liquidations. An IP must therefore consider on an ongoing basis how they ensure the insolvency is conducted in compliance with our rules.

Equitable set-off

108. Equitable set-off occurs where a customer of the failed firm owes money to the firm and is owed money by the firm, and the mutual debts are related. It is up to each customer to exercise their right to equitable set-off if they wish, although an IP must honour legitimate requests for equitable set-off.

109. An IP may set off redress amounts owed against amounts owed to the firm. Equitable set-off should be considered quickly by an IP as customers to whom it might apply could continue paying debts that would otherwise be set off.

Trading while in an insolvency process

110. An IP may decide that it is the best outcome for creditors if the failed firm continues to trade. We expect an IP to be aware that continuing to trade may mean using FCA permissions and, if this is the case, that the firm must remain authorised until the firm ceases to be carrying out regulated activities. When FCA permissions are no longer required, the IP should cancel the firm's permissions by liaising with the FCA (see below).

111. We would expect firms to tell us if they were continuing to trade while in an insolvency process and consider the impact on any client assets held (e.g. ensure that the CASS rules are complied with and pre- and post- PPE client monies held separately). IPs should be aware of the FCA requirements applicable to the firm (including any imposed on the firm's permissions through a VREQ or OIREQ) and make sure that they maintain the firm's organisational arrangements to comply with them (this may include, for example, the application of the senior management regime and relevant conduct of business rules).

Cancellation of permissions

112. When a firm goes into an insolvency process, the appointed IP should consider when it is appropriate to cancel the firm's permissions. We expect an IP to consider at an early stage in the insolvency what information the FCA would need to cancel the firm's permissions as this can then be prepared at a relevant

[47] Sections 233 and 233A of the Insolvency Act 1986

[48] SAR Regulation 14

time (e.g. when the client estate is closed) rather than at the end of the process. It is only appropriate to apply to cancel the permissions of the firm if it has stopped carrying out all regulated activities and no longer holds any client money or custody assets.

113. An application to cancel the authorisation of a FCA regulated firm can be made using our online system Connect. For further information, see the FCA's guide for completing an application to cancel.

Suspension or cancellation of listing

114. Where a firm with securities admitted to the Official List has made a decision to appoint an IP, it gives rise to grounds for a suspension of listing in order to protect investors. To ensure an orderly market, consideration should be made at an early stage and a conditional suspension can be requested from the FCA's Primary Market Monitoring team in advance of any such decision being made, which can then smoothly be implemented should the event crystallise. Once control has passed from the firm to the IP, the FCA can only deal with requests for suspension or cancellation of listing from the IP and would expect due co-operation on such matters.

115. For urgent live market situations, the Primary Market Monitoring team can be contacted via the Emergency Line on 020 7066 8354 and suspension requests should be sent to PMOsuspensions@fca.org.uk.

Reporting of unauthorised businesses

116. An IP should report to us if they come across any unauthorised firms or individuals that they believe are carrying out FCA regulated activities without the appropriate permissions to do so and any scams relating to financial services. Please note, however, that we are only able to look into scams and unauthorised conduct involving financial services regulated by the FCA.

117. An IP may also find that the firm over which they are appointed is being scammed or cloned. An IP should be vigilant to this and other scams and ensure to communicate to clients appropriately and report it to us at firm.queries@fca.org.uk.

Phoenixing

118. Phoenixing is a common term used to describe the practice of closing a firm and that firm re-appearing under a new guise to avoid liabilities arising from the old firm. Each time this happens, the insolvent company's assets, but not its liabilities, are transferred to a new, similar 'phoenix' company. The insolvent company then ceases to trade and might enter into formal insolvency proceedings (liquidation, administration or administrative receivership) or be dissolved.

119. The FCA will stop any practices that cause harm to consumers. There is a risk that directors, shareholders and senior staff wind up companies owing significant sums, often in the form of consumer redress awarded by the Financial Ombudsman Service, or who have engaged in financial misconduct, only to reappear connected with a new firm of strikingly similar business. The FCA considers this to be unacceptable practice.

120. If an IP becomes suspicious of phoenixing in respect of a failed firm, they should report these suspicions to firm.queries@fca.org.uk immediately. We are asking IPs to carefully consider the parties buying the business, and if there has been a sale prior to the entry into an insolvency to investigate the propriety of the transaction.

Sale of client data

121. An IP may consider selling a client book or part of a client book (i.e. clients' personal data) as part of a transfer or sale of the business of the failed firm. We expect the IP to consider the following matters in this scenario:

- **Notice to the FCA:** An IP should notify the FCA in good time, including sufficient details, if they are planning to sell a client book.
- **Fair treatment of clients**: Before transferring clients' personal data, an IP must consider whether this is in the interests of the clients and treats them fairly[49].
- **Selling to a claims management company (CMC):** if an IP proposes to sell the client book to a CMC, the IP should consider the FCA and Information Commissioner's Office (ICO) joint statement on dealing with personal data.
- **Obtain legal advice on the application of data protection legislation**: Data protection legislation applies to data controllers including IPs. Relevant legislation includes the Data Protection Act 2018, General Data Protection Regulation (EU) 2016/679 (GDPR) and Privacy and Electronic Communications Regulations (EC Directive) 2003. An IP should obtain legal advice on their obligations under such legislation to ensure that they handle client data appropriately.
- **Communication to clients:** As outlined in paragraph 42 above, an IP must pay due regard to the information needs of their clients and communicate with them in a way which is clear, fair and not misleading. This includes clearly articulating the transaction with a suitable helpline/contact(s) being provided to support and respond to client queries. The IP should also encourage the buyer to inform clients on the sale and their rights, so that they can manage their rights appropriately.
- **The sale is not facilitating phoenixing of the failed firm (see paragraph 118).**

122. For further details on the FCA's expectations of handling client data more generally, please see our communication on this.

Liaising with overseas regulators

123. Where an IP receives or issues correspondence to an overseas regulator in relation to the insolvency process, this information should be shared with the FCA at firm.queries@fca.org.uk. This would help us to keep abreast of the situation and inform any discussions that the FCA may have or be required to have with the overseas regulator.

[49] Principle 6 (Customers' interests)

Chapter 5: Restructuring procedures

124. Firms may consider using other procedures to enable them to restructure and continue trading. These can include:

- Scheme of arrangement
- Company voluntary arrangement (CVA)
- Restructuring plan

125. If an IP is advising a firm on their options or take forward a scheme of arrangement, CVA or restructuring plan in respect of a regulated firm, or which impacts on a regulated firm, the firm should notify us of their plans in good time.

126. The FCA has rights to make representations at court and creditor meetings for all restructuring procedures. We therefore expect appropriate notice so we can attend if we choose to do so. We also expect the firm or an IP (in their capacity as supervisor of a scheme of arrangement, restructuring plan or CVA) to send reports on a regular basis regarding the progress of these procedures to us so that we can review as appropriate. Reports should be sent to firm.queries@fca.org.uk.

127. If a firm is likely to be placed into administration or liquidation while subject to one of these procedures, the firm is required to promptly notify the FCA[50] .

Chapter 6: Checklist

128. The checklist overleaf summarises the key steps from this guidance that an IP will need to consider when appointed over a regulated firm.

[50] SUP 15 (General notification requirements) and Principle 11 (Relations with regulators)

	Key step	Tick
1.	Understand the firm's business model and how FCA requirements apply to the firm before appointment.	
2.	Engage with the FCA and FSCS (if applicable) as early as possible, including sharing court documentation and consent requests, and throughout the insolvency process as appropriate.	
3.	Communicate appropriately with clients.	
4.	Treat client money and custody assets in accordance with the CASS rules.	
5.	Ensure costs are properly recorded and communicated to clients and creditors in an appropriate manner.	
6.	Do not facilitate phoenixing and notify the FCA promptly of any concerns.	
7.	Cancel the firm's permissions when the firm is no longer conducting regulated activities and all client assets have been returned or transferred.	

Appendix: Template letter for section 362A FSMA consent requests

Financial Conduct Authority
12 Endeavour Square
London
E20 1JN

For the attention of [ ]

[date]

STRICTLY PRIVATE & CONFIDENTIAL

Dear Sirs,

[ ] ('the Company')

[I/ We] refer to the proposal that the directors of the Company are currently considering to place the Company into administration under paragraph [ ] of Schedule B1 of the Insolvency Act 1986.

[I/ We] have been advising the directors of the possible administration and understand that if they seek to place the Company into administration, they will ask me [and [ ]] to accept the appointment as [joint] administrators.

In connection with such a proposed appointment, [I confirm on behalf of myself and [ ]] [We confirm] that -

1. [I am a/ We are] licensed under the Insolvency Act 1986 as insolvency practitioner[s];

2. [I am / We are] satisfied that [I/ we] have the required professional qualification and experience to accept the appointment. [I/We] have experience and expertise of taking appointments as administrators, and indeed provisional liquidators, of companies, [including companies regulated by the Financial Conduct Authority]. [Given that the Company is authorised by the Financial Conduct Authority for the carrying on of regulated activities, [I/ we] confirm that persons with the relevant financial services experience will provide the necessary assistance]; and

3. [I am/ We are] [satisfied that it is reasonably likely that administration will achieve a better result for the Company's creditors as a whole than would be likely if the Company were wound-up.] (if the purpose of the administration is the realisation of the company's assets) [[I/ We] believe that the distribution of the Company's assets to those entitled is not likely to be slower than would be the case if the Company were to be placed into liquidation.]

If you have any questions on the above, please do not hesitate to contact [me/ us].

Annex 2 – Draft guidance for insolvency practitioners on how to approach payments and e-money institutions

Chapter 1: Introduction

1. This document provides guidance to insolvency practitioners (IPs) on how to approach payments institutions (PIs) and electronic money institutions (EMIs) authorised or registered under the Payments Services Regulations 2017 (PSRs) or Electronic Money Regulations 2011 (EMRs).

2. If an IP is appointed over a regulated firm, the IP takes control of the firm which continues to have regulatory requirements and responsibilities. We are therefore providing this guidance to help IPs comply with our rules and guidance as well as relevant legislation which aim to achieve better outcomes for consumers and market participants following a failure of a regulated firm.

3. This guidance is not exhaustive, neither is it a substitute for reading and complying with the FCA Handbook and other applicable legislative requirements and guidance.

The FCA's role in firm failures

4. The FCA has a role in every regulated firm failure and the role will vary depending on the individual circumstances of the firm.

5. While we are not able to stop firms failing, we aim to minimise harm to consumers and markets that may arise from a disorderly firm failure. This involves working with IPs to reduce such harm where possible.

6. PIs and EMIs are regulated by the PSRs and the EMRs respectively. The FCA has certain powers provided under the PSRs and EMRs, which enable us to take certain actions prior to a firm entering an insolvency process. This can include, for example, imposing requirements on the firm to take specific actions including the preservation of the firm's books and records, varying the firm's regulatory permissions, or taking steps to make an application to the court to place the firm into an insolvency procedure.

Safeguarding customers' funds

7. PIs and EMIs are required to safeguard funds belonging to customers[51] on receipt ('relevant funds'). The PSRs and EMRs set out how these funds must be safeguarded and distributed on the occurrence of an insolvency event[52]. See paragraph 35 for further details on how relevant funds are defined and our expectations on how these funds should be treated following an insolvency event.

[51] References in this guidance to customers are to payment service users and e-money holders (as relevant) unless otherwise stated.

[52] Insolvency event is defined in regulation 23(18) of the PSRs and regulation 24 of the EMRs

Chapter 2: Pre-insolvency

Sufficient experience for an appointment over a regulated firm

8. The Insolvency Code of Ethics requires that an IP should only accept an insolvency appointment where the IP has or can acquire sufficient expertise. If a firm is conducting regulated business, we expect the appointed IP to understand the business model and its regulated activities, or have a detailed plan to gain a full understanding of these shortly after their appointment. This could, for example, involve engaging relevant specialists. We also expect the IP to know what regulatory requirements and guidance that applies to the firm and identify any issues with compliance. The regulatory requirements and guidance may include:

    - **Principles for Businesses (PRIN):** these apply, in whole or in part, to all firms and set out high-level but fundamental obligations with which firms must comply under the regulatory system itself regarding various aspects, such as treating customers fairly, conflicts of interest and how a firm should communicate with the regulator.

    - **The Payment Services Regulations 2017 (PSRs):** these apply to all payment service providers (PSPs), including PIs and EMIs. They set out the authorisation, prudential and safeguarding requirements for PIs, as well as conduct requirements for all PSPs.

    - **The Electronic Money Regulations 2011 (EMRs):** these apply to all electronic money issuers. They set out the authorisation, prudential and safeguarding requirements for EMIs and conduct requirements for all electronic money issuers.

    - **FCA guidance on payment services and electronic money:** the FCA's Approach Document sets out our approach to implementing the PSRs and EMRs. This provides guidance on the requirements of the PSRs and EMRs and the regulatory approach the FCA takes. In respect of safeguarding and prudential risk management, the FCA also recently published additional guidance on safeguarding customers' funds.

    - **Disputes Resolution Complaints Sourcebook (DISP)**: DISP sets out how complaints are to be dealt with by firms, the reporting of complaints to the FCA and the operation of the Financial Ombudsman Service.

    - **Supervision Manual (SUP):** this sets out the relationship between the FCA and firms, key individuals within them and those who own or control the firm.

    - **Individual requirements and variation of permission**: the FCA applies these to an individual firm to vary its authorisation or registration and/or restrict the firm's activities[53]. We may ask a firm to voluntarily accept a variation of permission (VVOP) or the imposition of a requirement (VREQ) on is permission or impose it using our own-initiative powers (OIVOP/OIREQ). A firm must continue to comply with these variations and requirements after it enters into an insolvency procedure.

9. We expect an IP to consider whether they have the capacity to take on an appointment, bearing in mind their existing appointments, and the size and

[53] Regulation 12 of PSRs and Regulations 7 and 8 of the EMRs

complexity of the proposed appointment. If the IP does not have in-house resources to cover this, they should consider how appropriate resources will be engaged.

Pre-insolvency checks

10. An IP may often be involved with a firm before it becomes insolvent and advise on whether the firm has the necessary arrangements in place. This includes the firm having a wind-down plan. A wind-down plan details the steps that the firm will take in the event of insolvency, any risks associated with the wind-down and mitigating actions for these. An IP may wish to consult the FCA's Wind-down Planning Guide when advising on the robustness of a wind-down plan to help ensure an orderly wind-down of the firm.

Early engagement with the FCA

11. We expect an IP to engage with us at an early stage, both prior to and after appointment of an IP in relation to a regulated firm. The PSRs and EMRs will continue to apply to a firm in an insolvency procedure. Our rules and guidance will also continue to apply to a firm while it remains authorised or registered.

12. We expect an IP to ensure that the firm has notified us of the IP's appointment as soon as possible. We also expect any documents on the IP's appointment and other court documents relating to the firm in insolvency are sent to firm.queries@fca.org.uk.

13. If appropriate, the FCA also has the power to apply to the court to place a PI or an EMI into administration or present a winding-up petition of such firms to the court[54].

Notice if a firm is in the same group as a bank

14. An IP should be aware that, where a firm is in the same group as a bank (whether established in the UK or another EU member state), the firm is required to notify the FCA, PRA and the Bank of England seven days before entering an insolvency procedure[55]. An insolvency application cannot be determined until the Bank of England has informed the firm that they do not intend to exercise a stabilisation power under the Banking Act 2009 or the PRA and Bank of England have confirmed that they do not intend to apply for bank insolvency under the Banking Act 2009.

Future insolvency changes

15. On 3 December 2020, Her Majesty's Treasury consulted on the following changes to the insolvency framework for PIs and EMIs:

    - a bespoke special administration regime which provides tools to facilitate a speedy return of relevant funds, and
    - applying all insolvency powers under Part 24 of the Financial Services and Markets Act 2000 (FSMA) so that the FCA has rights to participate and protect consumers of such firms in an insolvency process, as it does for other FCA supervised firms.

16. We will keep this guidance under review as these developments progress.

[54] Section 359 and 367 of FSMA

[55] Sections 120A of the Banking Act 2009

Creditors' committees[56]

17. After a firm has been placed into administration, the administrator must, when seeking approval from the creditors for the administrator's proposals, invite the creditors to decide whether a 'creditors' committee' should be established. A similar type of committee can be set up in the context of liquidation, which is known as a 'liquidation committee'.

18. The purpose of the creditors' committee is to assist the IP in the discharge of their functions and to approve the IP's remuneration. Creditors will include all stakeholders of the failed firm, including customers, and their interests are significant to the IP in fulfilling their duties. IPs must therefore invite creditors of a regulated firm to form a committee to enable them to provide a 'voice' in the insolvency process. Customers for whom the firm holds relevant funds should be considered when forming a creditors' committee and there should be appropriate representation from across all types of customers for whom the firm is holding relevant funds.

Insolvency costs

19. We expect an IP to properly record insolvency fees and expenses throughout the insolvency process, and any fees and expenses charged to the client estate should be directly attributable to the distribution of relevant funds. We also expect that the IP is efficient in their work and take steps with the aim of reducing costs that would be borne by customers and creditors wherever possible.

20. Fees estimates and details of expenses that the IP considers will, or are likely to be, incurred should be realistic and communicated to customers and creditors in a timely and clear manner. An IP should carefully consider when they are in a position, having fully assessed the firm's business and understood the complexities of the insolvency, to seek approval for the basis of their remuneration and, where relevant, to provide a fees estimate and details of expenses to creditors and customers.

21. We expect an IP to properly consider expenses that may be incurred (i.e. legal expenses). It is important to note that if lawyers or other parties are working in conjunction with an IP, they will also need to be able to accurately account for their time, particularly in relation to work directly attributable to the distribution of relevant funds.

22. We expect an IP to properly allocate costs to relevant estates and, where relevant, consult with, and seek approval from, the creditors' committees and/or seek directions from the court, as relevant. We expect the IP to update us on the costs that they are charging to the relevant estates, and report this clearly to customers and creditors. An IP should discuss this fully with the creditors' committee, if one is established, when gaining their approval to draw costs as set out in insolvency legislation. In some cases, the creditors' committee may wish to consider the appointment of an independent cost assessor.

23. Given the role of the creditors' committee in this process, it is important that it appropriately represents the customer base of the firm. IPs should consider how

[56] References in this guidance to creditors' committee refers to any creditors' committee or liquidation committee established by an IP under Part 17 of the Insolvency (England and Wales) Rules 2016 unless otherwise stated.

they ensure appropriate representation across all types of stakeholders of the failed firm on the committee throughout the insolvency process.

Chapter 3: Entering insolvency

Interaction with the FCA

24. If a firm is considering entering or has entered into an insolvency procedure, we would expect an IP to provide regular updates to the FCA for a period agreed with us. Items that an IP should update us on include:

- communications to customers
- customer contacts and questions
- progress in collecting in, reconciling or distributing relevant funds in line with the PSRs/EMRs and relevant insolvency legislation
- customer complaints including interface with the Financial Ombudsman Service[57]
- quality of books and records
- possible sale of the customer book (if contemplated) including the marketing process, the ability of any proposed purchaser to take on the book, and the implications of any requirements over the firm
- staffing and supplier issues
- adverse press or other commentary
- any intelligence or information arising from the insolvency or investigations into directors' conduct that could give rise to harm
- insolvency costs, especially those relating to the client estate, and
- interaction with foreign regulators and/or other UK authorities involved in the firm's insolvency process.

Communicating with customers

25. If a firm is considering entering or has entered into an insolvency process, we expect an IP to have a communication strategy in place. This strategy should consider the key messages for customers, what their immediate concerns may be and the information they are going to need, the format of that information and how quickly it can be disseminated.

26. Information about the practical effects of the IP's appointment will be the most important initially and must be clear for customers. This should include implications for in flight payments and whether e-money cards will continue to work.

27. In addition, the following practical issues should be considered factors:

[57] FSCS is not currently available for customers of PIs and EMIs.

- **Use language that is clearly understood by the audience of the communication**[58], particularly if they are retail or vulnerable consumers. This includes adapting template communications to help ensure they are clear, fair and not misleading to the recipient and are easy to understand. An IP should also consider using headings and highlighting key actions that need to be taken by the recipient. Given the rise in scams, any customer communications should have a standard 'scam smart' messaging and make clear that a consumer is not required to use the services of a claims management company to pursue a claim. Key messages should not be hidden (i.e. they should be at the top of the communication).

- **Ensure sufficient resource is available for communications with the firm's customers**, particularly where there is a significant number of retail customers. This may require additional phone lines or a call centre, producing scripts for staff including frequently asked questions and, in some cases, providing communications in different languages.

- **Information on treatment of relevant funds**. An IP should avoid giving customers misleading impressions on the protection they receive from safeguarding requirements. An IP should also avoid suggesting to customers that any of the relevant funds held by the insolvent firm are protected by the Financial Services Compensation Scheme (FSCS)[59] given FSCS is not currently available for customers of PIs and EMIs.

- **Share draft versions of key customer communications with the FCA (and other relevant authorities) for comment before finalising**, particularly communications regarding high profile or complex firm failures (e.g. firms that hold significant sums of safeguarded funds or vulnerable customers). This would also help to ensure that customer communications are consistent with any FCA press releases upon an IP's appointment.

28. We are aware that there are statutory communications, including notices, letters and reports, that an IP must issue before and during their appointment. If any communication contains references to the FCA, we expect these to be factual, necessary and, in the case of high profile and complex failures, communicated to the FCA for comment in advance of publication and in good time so that the IP is able to meet any statutory deadlines for such communications. These communications should be sent to firm.queries@fca.org.uk.

Interaction with the Financial Ombudsman Service

29. The Financial Ombudsman Service is an independent service for resolving disputes between consumers and businesses, and with a minimum of formality on a fair and reasonable basis. The rules and guidance relating to the operation of the Financial Ombudsman Service is set out in DISP rules of the Handbook.

30. We would expect an IP to engage with the Financial Ombudsman Service at the beginning of an insolvency process to establish the number of complaints against the failed firm and to agree how those complaints will be dealt with going forward.

[58] This is in accordance with the firm's obligations under Principle 7 (communication with clients).

[59] Paragraph 1.26 of Coronavirus and safeguarding customers' funds: additional guidance for payment and e-money firms.

Agents and distributors

31. Many PIs and EMIs provide payment services through agents. An agent is any person who acts on behalf of a PI or an EMI (i.e. a principal) in the provision of payment services[60]. These entities are required to be registered with the FCA. An EMI may also engage distributors to distribute and redeem e-money. An EMI cannot provide payment systems through a distributor and distributors do not have to be registered by the FCA. We expect an IP to be mindful of any agent and distributor arrangements as part of the insolvency process.

Chapter 4: Post insolvency

Claims process

32. We expect an IP to have a suitable claims process in place for customers and creditors. An IP should consider how this claims process is structured to ensure that it is easy to handle from both a customer and the IP's perspective. For example, an IP may want to explore the idea of handling the claims process via web portal.

33. We expect an IP to consider the following when designing their claims process:

- how statements to customers are issued
- how customers and creditors validate their claims
- validation of KYC details
- how non-responders are treated
- the process should customer address details be incorrect
- the need for customers and creditors to add bank account details, including where relevant funds are held in joint names and the bank account details are in only one name
- communication to customers on access to the claim portal if available
- any translations required for non-English speakers
- the process if customers choose to abandon small claims, and
- information/data to be collected regarding engagement with the claims process.

34. An IP may need to consider demonstrating the claims process with the creditors' committee before making it available. They should also consider using the technology systems of the failed firm if suitable (avoiding unnecessary costs). In any case, an IP should consider the need to maintain IT contracts, the resilience and usability of the systems and data security considerations for migration.

[60] See regulation 2 of the PSRs and regulation 2 of the EMRs

Treatment of customers' funds

35. PIs and EMIs are required to safeguard 'relevant funds'. Under the EMRs, these are funds that have been received in exchange for issued e-money[61]. Under the PSRs, relevant funds are:

    - sums received from, or for the benefit of, a payment service user for the execution of a payment transaction, and
    - sums received from a payment transaction on behalf of a payment service user.

36. The safeguarding requirements[62] apply to all authorised PIs, authorised EMIs and small EMIs. Small PIs and small EMIs undertaking payment services unrelated to the issuance of e-money must comply with the safeguarding requirements if they choose to safeguard funds.

37. If a PI or an EMI that is holding relevant funds enters an insolvency procedure, an IP will need to ensure that such funds continue to be treated in line with the PSRs and EMRs (as applicable).

How are relevant funds safeguarded?

38. An IP should note that there are two ways in which a firm may have safeguarded relevant funds prior to entering into an insolvency process:

    - **Segregation method:** this requires the firm to keep relevant funds separate from all other funds it holds and, if the funds are still held at the end of the business day following the day on which they were received, deposit the funds in a separate account with an authorised credit institution or the Bank of England or to invest the relevant funds in secure, liquid assets and place those assets in a separate account with an authorised custodian[63].
    - **Insurance or guarantee method:** this requires the firm to arrange for the relevant funds to be covered by an insurance policy with an authorised insurer, or a comparable guarantee[64].

39. As set out in a recent court judgment[65], PIs that safeguard using the segregation method hold safeguarded funds on trust. We also consider that this is true for EMIs.

Steps to take immediately after appointment

Take control of relevant funds

40. Following appointment, an IP will need to take control of relevant funds and assets, and the books and records of the firm. The IP should also identify key individuals and systems required to manage relevant funds of the firm, including third party administrators, system suppliers and employees of the firms.

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[61] Regulation 20(1) of EMRs

[62] The safeguarding requirements are set out in regulations 23 of the PSRs and regulations 20 to 27 of the EMRs. Our expectations on how firms should comply with these requirements are explained in Chapter 10 of the FCA's Payment Services and Electronic Money – Our Approach and the FCA's Coronavirus and safeguarding customers' funds: additional guidance for payment and e-money firms.

[63] Regulation 21 of the EMRs 2011 and paragraph 10.31 of the FCA's Payment Services and Electronic Money – Our Approach

[64] As defined in Regulation 24 of the EMRs 2011 and Regulation 23 of the PSRs 2017.

[65] Supercapital (in administration) [2020] EWHC 1685 (Ch)

Furthermore, the IP should cooperate with any payment systems to facilitate settlement or completion of inflight payments.

41. On the occurrence of an insolvency event[66], an 'asset pool' is formed of the relevant funds that have been segregated, funds or assets held in a safeguarding account[67] and the proceeds of any insurance policy/comparable guarantee. To constitute the asset pool, the IP will need to collect all relevant funds safeguarded by the firm. This includes checking the terms of any safeguarding insurance or guarantee policy and, if a claim should be triggered, exercising the relevant provisions that enable the pay-out of proceeds for the asset pool. The IP should also take reasonable measures to include all identifiable relevant funds in any other account held by the firm (e.g. unsegregated funds).

42. For relevant funds which have been segregated by investing in liquid assets, the IP may consider there being benefit in holding the relevant funds in those liquid assets until is necessary to distribute the funds to customers.

43. EMIs may undertake both e-money issuance and unrelated payment services – in this scenario, there would be two types of customers (e-money holders and payment service users) and two asset pools (one for e-money issuance and one for unrelated payment services).

Operate different estates

44. We expect an IP to operate at least two separate estates: the client estate comprising the asset pool (against which claims of customers are paid in priority to all other creditors) and the general estate comprising the firm's assets (against which all creditors can prove). The estates may be further split if the firm is operating two asset pools (as described above).

45. As stated earlier, an IP should accurately allocate costs between the two estates. An IP should also accurately record time spent on the different estates and, in respect of the client estate, distinguish time and expenses spent on each asset pool.

46. It is possible that a firm holds both client money under the FCA's Client Assets Sourcebook (CASS) and relevant funds under the PSRs/EMRs. CASS client money must be segregated from relevant funds and accordingly separate pools following insolvency.

Determine entitlements

47. After forming the asset pool, the IP should identify customers with an entitlement to relevant funds owed by the firm at the time of failure. This could involve looking at records of the firm's previous reconciliation, customer database and transaction history.

Manage currency risks

48. An IP will need to consider:

- what currency they should calculate each entitlement
- what currency they should continue to hold the relevant funds in the asset pool in, and

[66] As defined in the PSRs and EMRs

[67] Where the PI or EMI is a participant in a designated payment system, this may include funds received into a settlement account in the circumstances described in regulation 23(9) of the PSRs.

- what currency the IP should return relevant funds in the asset pool in.

49. As part of the above considerations, we expect an IP to have regard to any relevant insolvency rules, contractual terms and the currency of the customer's claim.

Treatment of shortfalls

50. A shortfall is the amount by which relevant funds and assets held by the firm are not sufficient to meet all customer entitlements. A shortfall may arise for various reasons including deductions from the asset pool because of distribution costs and/or poor controls and record keeping by the firm before it failed.

51. It is our view that a distribution cost is a cost directly attributable to the distribution of the asset pool. For example, this may include gathering in, reconciling, calculating entitlements, transaction costs of sending the money. An IP should endeavour to minimise costs incurred in the distribution process and return relevant funds and assets to the customer as soon as reasonably practicable. As explained above, distribution costs should be recorded and charged appropriately following authority from the creditors' committee or court as appropriate.

52. For shortfalls in the asset pool, an IP should consider and agree with the creditors' committee on the appropriate method for allocating these or obtain directions from the court. The IP should explore various options, such as applying a fixed fee per customer or allocating such costs on a pro rata basis.

53. Customers should be considered contingent creditors in respect of any shortfall. Customers may also have a claim against the general estate for any relevant funds that are not returned as part of the distribution of the asset pool.

Relevant funds received by the firm after insolvency

54. A firm is likely to have unsettled or incomplete transactions at the point of entering an insolvency procedure, which may result in the firm receiving relevant funds after it has failed. This may include transfers of funds from payment systems. These amounts do not form part of the asset pool. An IP should consider setting up procedures to monitor and allocate receipts post insolvency and return these promptly to customers. An IP should also cooperate with the relevant payment systems to facilitate appropriate treatment of inflight transactions.

Distributions of the asset pool

55. The IP is required to pay claims of customers from the asset pool in priority to all other creditors[68]. In this process, an IP may need to consider the following issues:

    - how relevant funds are returned to the relevant customer (e.g. whether it should go directly to the customer or as per the customers' instructions)
    - verifying a customer's bank details before returning relevant funds
    - costs of returning relevant funds to each customer, and
    - if the customer cannot be contacted or disclaims their entitlement.

[68] The exception is expenses of the insolvency proceedings which take priority so far as they are in respect of the costs of distributing the asset pool.

Closure of client estate

56. At the appropriate point, the IP will need to close the client estate. An IP is required to take reasonable steps under general trust law and their obligations as an IP to notify all customers of the fact that they may have a valid claim for relevant funds, prior to the closure of the client estate. An IP should consider making at least three attempts to contact the customer using two different methods (e.g. an email and a phone call) regarding their opportunity to claim their relevant funds. The IP will also need to determine what to do with any unclaimed relevant funds.

57. We would expect an IP to share any court documents with us in good time prior to closing the client estate.

Hardship policies

58. Until the IP is in a position to distribute the asset pool, funds will not be returned or available to customers. In such situations, the IP should consider hardship cases to help ensure that they are identified and responded to in an appropriate and consistent manner. It may be that the IP is able to provide earlier distributions of their funds to customers who can demonstrate hardship (although this may not always be possible). We therefore expect an IP to identify potential hardship policies and assess whether there is anything that can be done to support these cases. However, we recognise the ability of the IP to support will depend on the circumstances of the case.

Continuity of supply

59. We expect an IP to consider how they will make sure that the failed firm continues to comply with our regulatory requirements whilst it remains authorised. If the firm loses a supplier, it is still required to comply with our rules. The continuity of service provisions in the Insolvency Act[69] assist an IP by enabling them to limit the terms that essential suppliers can impose as a condition for the continued supply of their service and compel continued supply by restricting the effect of existing insolvency-related terms in an essential supply contract. Continuity of supply also helps to facilitate distribution of relevant funds (e.g. where third party suppliers have been used to maintain customer records and IT systems).

60. The continuity of supply provisions is not available for liquidations. An IP must therefore consider on an ongoing basis how they ensure the insolvency is conducted in compliance with our rules.

Trading while in an insolvency process

61. An IP may decide that it is the best outcome for creditors if the failed firm continues to trade. We expect an IP to be aware that continuing to trade may mean using FCA authorisation and registration, and, if this is the case, that the firm must remain authorised or registered until the firm ceases to be carrying out regulated activities. When FCA authorisation or registration is no longer required, the IP should cancel the firm's authorisation or registration by liaising with the FCA (see below).

62. We would expect firms to tell us if they were continuing to trade while in an insolvency process and consider the impact on relevant funds. They should

[69] Sections 233 and 233A of the Insolvency Act 1986

consider how any continued trading impacts on the asset pool, and ensure that any relevant funds received post insolvency are held separately. IPs should be aware of any requirements and make sure that they maintain the firm's organisational arrangements to comply with them.

Cancellation of authorisation or registration

63. When a firm goes into an insolvency process, the appointed IP should consider whether and when it is appropriate to cancel the firm's authorisation or registration. We expect an IP to consider at an early stage in the insolvency what information the FCA would need to cancel the firm's permissions as this can then be prepared at a relevant time (e.g. when the client estate is closed) rather than at the end of the process. It is only appropriate to apply to cancel the authorisation of the firm if it has stopped carrying out all regulated activities in the future and no longer holding any relevant funds.

64. An IP can request to cancel a firm's authorisation or registration[70] by using our online system Connect.

Reporting of unauthorised businesses

65. An IP should report to us if they come across any unauthorised firms or individuals that they believe are carrying out FCA regulated activities without the appropriate permissions to do so and any scams relating to financial services. Please note, however, that we are only able to look into scams and unauthorised conduct involving financial services regulated by the FCA.

66. An IP may also find that the firm over which they are appointed is being scammed or cloned. An IP should be vigilant to this and other scams and ensure to communicate to customers. appropriately and report it to us at firm.queries@fca.org.uk.

Phoenixing

67. Phoenixing is a common term used to describe the practice of closing a firm and that firm re-appearing under a new guise to avoid liabilities arising from the old firm. Each time this happens, the insolvent company's assets, but not its liabilities, are transferred to a new, similar 'phoenix' company. The insolvent company then ceases to trade and might enter into formal insolvency proceedings (liquidation, administration or administrative receivership) or be dissolved.

68. The FCA will stop any practices that cause harm to consumers. There is a risk that directors, shareholders and senior staff wind up companies owing significant sums, often in the form of consumer redress awarded by the Financial Ombudsman Service, or who have engaged in financial misconduct, only to reappear connected with a new firm of strikingly similar business. The FCA considers this to be unacceptable practice.

69. If an IP becomes suspicious of phoenixing in respect of a failed firm, they should report these suspicions to firm.queries@fca.org.uk immediately. We are asking IPs to carefully consider the parties buying the business, and if there has been a sale prior to the entry into an insolvency to investigate the propriety of the transaction.

[70] Regulations 10 and 14 of the PSRs and regulations 10 and 15 of the EMRs

Sale of customer data

70. An IP may consider selling customers' data as part of a transfer or sale of the business of the failed firm. We expect the IP to consider the following matters in this scenario:

    - **Notice to the FCA:** An IP should notify the FCA if they are planning to sell customer data in good time, including sufficient details.
    - **Fair treatment of customers**: Before transferring customers' personal data, an IP must consider whether this is in the interests of the firm's customers and treat them fairly[71].
    - **Selling to a claims management company (CMC):** if an IP proposes to sell the customer data to a CMC, the IP should consider the FCA and Information Commissioner's Office (ICO) joint statement on dealing with personal data.
    - **Obtain legal advice on the application of data protection legislation**: Data protection legislation applies to data controllers including IPs. Relevant legislation includes the Data Protection Act 2018, General Data Protection Regulation (EU) 2016/679 (GDPR) and Privacy and Electronic Communications Regulations (EC Directive) 2003. An IP should obtain legal advice on their obligations under such legislation to ensure that they handle customer data appropriately.
    - **Communication to customers:** As outlined in paragraph 25 above, an IP must pay due regard to the information needs of their customers and communicate with them in a way which is clear, fair and not misleading. This includes clearly articulate the transaction with a suitable helpline/contact(s) being provided to support and respond to customer queries. The IP should also encourage the buyer to inform customers on the sale and their rights, so that they can manage their rights appropriately.
    - **The sale is not facilitating phoenixing of the failed firm (see paragraph 67).**

71. For further details on the FCA's expectations of handling customer data more generally, please see our communication on this.

Liaising with overseas regulators

72. Where an IP receives or issues correspondence to an overseas regulator in relation to the insolvency process, this information should be shared with the FCA at firm.queries@fca.org.uk. This would help us to keep us abreast of the situation and to inform any discussions that the FCA may have or be required to have with the overseas regulator.

Chapter 5: Restructuring procedures

73. Firms may consider using other procedures to enable them to restructure and continue trading. These can include:

    - Scheme of arrangement

[71] Principle 6 (Customers' interests)

- Company voluntary arrangement (CVA)
- Restructuring plan

74. If an IP is advising a firm on their options or take forward a scheme of arrangement, CVA or restructuring plan in respect of a regulated firm, or which impacts on a regulated firm, the firm should notify us of their plans in good time.

75. The FCA have rights to make representations at court and creditor meetings for all restructuring procedures. We therefore expect appropriate notice so we can attend if we choose to do so. We also expect the firm or an IP (in their capacity as supervisor of a scheme of arrangement, restructuring plan or CVA) to send reports on a regular basis regarding the progress of these procedures to us so that we can review as appropriate. Reports should be sent to firm.queries@fca.org.uk.

76. If a firm is likely to be placed into administration or liquidation while subject to one of these procedures, the firm is required to promptly notify the FCA[72] .

Chapter 6: Checklist

77. The checklist below summarises the key steps from the guidance that an IP will need to consider when appointed over a regulated firm.

	Key step	**Tick**
1.	Understand the firm's business model and how FCA requirements apply to the firm before appointment.	
2.	Engage with the FCA as early as possible and throughout the insolvency process as appropriate.	
3.	Communicate appropriately with customers.	
4.	Treat relevant funds in accordance with the PSRs, EMRs and FCA guidance.	
5.	Ensure costs are properly recorded and communicated to customers and creditors in an appropriate manner.	
6.	Do not facilitate phoenixing and notify the FCA promptly of any phoenixing concerns.	
7.	Cancel the firm's authorisation or registration when the firm is no longer conducting regulated activities and relevant funds have been returned.	

[72] SUP 15 (General notification requirements) and Principle 11 (Relations with regulators)

Annex 3 – Abbreviations used in this paper

CASS	Client Assets Sourcebook
CBA	Cost benefit analysis
CMC	Claims management company
CMP	Client money pool
CVA	Company voluntary arrangement
COMP	Compensation Sourcebook
DISP	Disputes Resolution Complaints Sourcebook
EMI	Electronic money institutions
EMR	Electronic Money Regulations 2011
FCA	Financial Conduct Authority
FSCS	Financial Services Compensation Scheme
FSMA	Financial Services and Markets Act 2000
GDPR	General Data Protection Regulation
IP	Insolvency practitioner
LRRA	Legislative and Regulatory Reform Act 2006
MVL	Members' voluntary liquidation
OIREQ	Own-initiative imposition of requirement
OIVOP	Own-initiative variation of permission
PI	Payments institutions
PPE	Primary pooling event

PRA	Prudential Regulation Authority
PRIN	Principles for Businesses
PSP	Payment service provider
PSR	Payments Services Regulations 2017
SAR	Special Administration Regime
SUP	Supervision Manual
VREQ	Voluntarily accept the imposition of a requirement
VVOP	Voluntary variation of permission