

# FINANCIAL CONTROLS FOR INSOLVENCY CASES AND WHAT TO DO IF YOU DISCOVER FINANCIAL IRREGULARITIES



## 1. About this helpsheet

This helpsheet is for insolvency practitioners (IPs).

IPs should be familiar and comply with the requirements of [Statement of Insolvency Practice \(SIP\) 11](#). Also, since 1 May 2018, there has been a new Insolvency Licensing Regulation 3.5A which imposes an explicit obligation on ICAEW's IPs to protect the estate funds held on their appointments.

It is essential that an insolvency practice has robust controls over estate accounts and cashiering procedures, both to ensure that estate monies are safe, and also to enable you to prepare accurate statutory returns, and receipts and payments accounts.

The first part of this helpsheet focuses on the financial controls that will typically be appropriate for insolvency estate accounts. It is not an exhaustive list and the level of controls needed will vary depending on the size of the practice.

The second part of the helpsheet focuses on the [steps you need to take if you discover any financial irregularities](#), and the responsibility of any joint officeholder.

The controls and procedures detailed in this helpsheet are not prescriptive but if they are not adopted, we would expect firms to have at least equivalent procedures and policies in place.

## 2. Controls

SIP 11 requires the financial controls and safeguards, including levels of insurance cover, to be fully documented and reviewed by the office holder for their adequacy, as and when appropriate (and at a minimum annually). This should include professional indemnity insurance and such other insurances as are in place, such as fidelity insurance.

### 2.1 Receipts

The following basic steps should ensure that receipts are completely and accurately recorded.

- All receipts should be recorded when received, including cheque and electronic receipts.
- Where possible, someone independent of the cashiering function should open the post and log any cheques and BACS remittances. It's important that there's a regular, independent, review of the cheque and remittance log to make sure all receipts have been banked and cleared to the correct account.
- Cheques should be banked on the day of receipt if possible. Where an office holder receives estate money in a manner such that it cannot be paid directly into an estate account, such money may be cleared through an account maintained in the name of the office holder or an entity in which they are working. Such accounts should be operated in accordance with the client money rules and regulations as may from time to time be in force by virtue of that office holder's authorisation. Funds paid into such accounts should be paid out to the estate to which they relate as soon as is reasonably practicable.

- We recommend using sequentially numbered receipt vouchers and attaching a copy of the cheque and any supporting remittance or other document to the voucher.
- Where receipts may require a bond increase, there should be a system in place to make sure this is done promptly, preferably before the bond limit is exceeded.

## 2.2 Payments

The following basic steps should ensure that payments are only made in relation to properly incurred, valid liabilities.

- Cheque books should be kept secure, in a locked cupboard.
- We recommend using payment vouchers summarising the details of the payment, the posting code and showing who requested and authorised the payment.
- The cashier, the case administrator, case manager and the cheque signatory should check that the liability relates to the estate in question.
- Third party documentation justifying the payment should be attached to the payment request so that the signatory can be satisfied that the payment relates to an appropriate and valid expense. If the payment relates to a trading case, it may also be appropriate to attach a copy of the purchase order and the delivery note. Where possible, purchase orders should be posted to the daybook, so that any not matched to an invoice can be investigated.
- There should be adequate supporting documentation for any payments made by online banking, and the identity of the person who made the online payment should be clear.
- Where possible, the person requesting the payment should not be the same person that prepares the cheque or online payment. Similarly, the person or persons signing a cheque or authorising an online payment shouldn't be able to prepare the payment.
- Where possible, you should limit the size of the transactions that can be processed by different grades of staff.
- You should review any exception reports and investigate any anomalies including any unapproved payments; missing cheques or unpaid invoices.

### Petty cash

- Where you use petty cash, there should be clear policies for its use and approval. These policies should be followed by all staff and office-holders.
- An imprest system should be used.
- Any cash advances should be recorded and signed for by the recipient.
- Receipts and any change should be promptly provided and reconciled to the amount of the advance.
- Any requests to breach the petty cash policies in place should be reported to the whistle-blowing officer or an IP.

## 2.3 Bank statements and reconciliations

The following basic steps should ensure that bank reconciliations are an additional, effective check on the financial records.

- Bank statements should be reviewed alongside other incoming post and should not be removed from the post before it has been reviewed.
- All bank statements should be reconciled within a reasonable period of receipt. Although there is no guidance on how frequently an estate account should be reconciled, ICAEW's clients' money regulations require members to reconcile their client accounts at least once every five weeks. This timescale could also be applied to estate accounts, although it may not be appropriate for all cases; eg, it is unlikely to be cost-effective to reconcile ISA accounts this frequently if they relate to court-work cases with low balances and few transactions.

- Bank reconciliations should be subject to independent review. When reviewing them, the reviewer should check the relevant bank statement and the reconciliation.
- All reconciling items should be investigated promptly.
- If funds have been transferred from one estate account to another (eg, placed on deposit), the reviewer should confirm that the transfer has been made by checking both the statement for the account from which the funds were transferred, and the receiving account.
- The closure of bank accounts should be confirmed in writing and closing statements obtained and retained.
- Where an insolvency proceeding is followed by another, the closing balances on the cashbook of the first insolvency, should be reflected as opening balances in the subsequent proceedings. Where there are outstanding VAT reclaims or payments, the relevant entries should be posted to the cashbook of the subsequent insolvency proceedings, to prompt the relevant returns to be submitted and / or refunds to be pursued if not received.

#### **2.4 IT systems and security**

The following basic steps should ensure that IT systems do not allow inappropriate behaviour.

- Journals should be documented and authorised by someone other than a cashier, wherever possible.
- Documentation should be retained to provide an audit trail supporting the reason for the journal.
- Authority levels for the cashiering and diary management system should be reviewed periodically to make sure they remain appropriate.
- Cashiers should not have unfettered access to the entire system, or the highest security or authority level.
- Passwords for online banking should be kept secure and not widely known.

#### **2.5 Staff**

When you recruit new staff, you should always seek references from the individual's previous employer. Although references may not always be helpful, it can be very telling if the referee declines to provide a reference.

You should also ask all staff to complete an annual declaration of competency and integrity.

Segregation of duties is an integral part of any financial control system. Except in the smallest practices, as a minimum, one person alone should not have sole responsibility for a specific area; for example income (receiving, recording, processing, depositing and reconciling).

Depending on the extent of estate funds held and procedures in place to safeguard estate funds, you may consider that the overhead cost to your business of fidelity insurance, (to insure against loss or theft caused by the actions of your staff), is merited.

#### **2.6 Reviewing the operation of the cashiering system**

You should regularly review cashiering work to ensure that staff comply with the firm's procedures.

These reviews can be incorporated into your insolvency compliance review (ICR) process. For example, we would expect any cold case reviews of an insolvency case to

include a review of the cashiering files, and to look at whether the firm's procedures have been complied with.

These reviews can easily look at whether:

- there is adequate supporting documentation for payments;
- receipts on the case have been banked promptly;
- journals have been documented and authorised;
- bank reconciliations have been carried out regularly, and reviewed at an appropriate level.

The person signing a bank reconciliation should check that there aren't any suspense entries that aren't being investigated and that the reconciled difference between the cashbook and bank account balances is nil.

Reconciliations between bank and cashbook balances should be done at a particular date. You shouldn't reconcile the bank account balance at one date with a cashbook balance at a different date.

Alternatively, in a particular year you may consider it appropriate to focus your ICR on cashiering procedures. This review could look at the operation of the cashiering systems across a range of cases, and could also look at those areas that can't be tested on individual insolvency cases, such as system security and access levels.

## **2.7 Additional simple steps that can help avoid problems**

In our experience the following steps could reduce the chance of financial irregularities or make it more difficult for any perpetrator to continue undetected.

- Do not allow staff to use signature stamps to authenticate documents.
- Make sure the requirement for payments to be supported by third party documentation is enforced.
- As a signatory, refuse to sign cheques if there is not adequate supporting documentation.
- If you are the joint appointee, consider whether you have adequate knowledge of a case to be satisfied that the payment is appropriate and justified.
- Don't allow an apparent urgent need for a payment to over-ride the firm's systems and procedures.
- If urgent payments are likely to be required, ensure your procedures cover such circumstances and that there is adequate provision for the validity of the payment to be checked.
- Ensure that the cashiering team is not isolated and has adequate access to, and contact with, senior members of the team.
- Ensure that exception reports are produced regularly to show when estate accounts were last reconciled. These should be reviewed by someone independent of the cashiering team.
- Ensure that the firm has a whistle-blowing policy in place, that staff are aware of it, and know who to contact with any concerns or policy breaches.
- Investigate subsequent downward revisions to individual case outcomes and question the validity of the adjustments.
- Ensure that dominant personalities are not able to by-pass systems or operate in isolation.

### 3. Responsibility of joint officeholders

It is common for corporate insolvency appointments in particular to be taken by two or more IPs as joint officeholders, with one IP usually assuming a lead role.

The Insolvency Guidance Paper on the Control of Cases confirms that if there is delegation (which includes taking a reduced role on a joint appointment), the IP must be satisfied at all times that work is being carried out in a proper and efficient manner, appropriate to the case.

Although the involvement of any joint, non-lead IP will vary from case to case and firm to firm, the joint officeholder cannot deny responsibility for a case. If any issues about financial irregularities arise, ICAEW's Insolvency Licensing Committee will automatically consider referring the joint officeholder for investigation, to determine whether they have acted appropriately and whether any irregularities should have come to their attention.

As joint, non-lead officeholder you should therefore be satisfied that there are adequate controls in place to enable you to be satisfied that such cases are being handled properly. The extent of appropriate controls is likely to vary from firm to firm.

### 4 What to do if you discover any financial irregularities

Even when there is a good system of financial controls in place, it is only a safeguard against deliberate misstatement of accounts and deliberate misappropriation or misuse of funds.

If you discover any financial irregularities we expect you to:

- consider whether you need to submit a Suspicious Activity Report to your MLCO and / or NCA;
- contact the secretary to ICAEW's Insolvency Licensing Committee immediately;
- report the matter to the police immediately;
- contact your PII and other insurers (including those in relation to any fidelity insurance or the bond provider, depending whether the perpetrator was a member of staff or an IP); and
- arrange for an independent review to be carried out, to examine the extent of the issue and how it arose.

You need to consider the tipping off provisions in the Money Laundering Regulations when reporting.

Under paragraph 2.14 of ICAEW's Insolvency Licensing Regulations, all IPs are required to notify the Insolvency Licensing Committee in writing, as soon as possible, and no later than 10 business days after becoming aware of any matter that may affect their status as a fit and proper person. Regulation 3.11 also requires a licence holder to establish and maintain procedures designed to ensure that anyone, at any time, employed by or associated with them in connection with their insolvency work is a fit and proper person.

Regulation 3.12 requires a licence holder to make sure that there are adequate procedures and supervision in place to comply with the licensing regulations.

These regulations as a whole mean we expect you to tell us as a matter of urgency if you discover any financial irregularities in your practice, whether that is by a fellow IP or a member of staff.

In addition, if the person responsible for the financial irregularities is an ICAEW Chartered Accountant, the duty to self-report misconduct also applies.

Further, Statement of Insolvency Practice 1 requires an IP who becomes aware of any IP who they consider is not complying or who has not complied with relevant laws and regulations and whose actions discredit the profession, to report that IP to the complaints gateway operated by the Insolvency Service or to that IP's recognised professional body.

Under UK criminal law there is no general requirement to report criminal acts to the police. Nevertheless, if a person is aware that a criminal act is being carried out and actively tries to cover it up, they could be prosecuted for conspiracy to pervert the course of justice. ICAEW's Insolvency Licensing Committee expects IPs to report any financial irregularities to the police promptly; failure to do so could be seen as a breach of the Code of Ethics.

#### **4.1 What happens next?**

If we receive information suggesting there has been some financial irregularity affecting insolvency estates, we will report this to the Insolvency Licensing Committee, who will consider the information and the circumstances. Depending on the circumstances, the committee may remove the IP's licence and refer them to the Investigation Committee for disciplinary action.

The committee will be particularly concerned about the creditors on the cases affected, and who is representing their interests. The committee will be concerned to see that there is an independent assessment of the loss.

If the firm does not volunteer to arrange for an independent review to be carried out, the committee may require the IPs in the firm to do so, as a condition of retaining their licences. In most cases the Insolvency Licensing Committee will want to be kept up to date about the steps being taken to reimburse estates and creditors for any loss.

As well as considering licensing issues, we will also consider the need for disciplinary action against any members. The committee will also automatically consider whether any joint officeholder should be referred for investigation, to satisfy itself that the conduct of the joint officeholder was appropriate.

## **5. Summary**

Although a good system of financial controls will provide some protection, it cannot guarantee full protection from deliberate misappropriation. You can reduce the risks by taking some simple steps and carrying out regular reviews of your systems to make sure they are operating as expected. It's important you take appropriate steps promptly if you discover any irregularities.

## **6. Contact us**

If you have any queries about this helpsheet please contact us.

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## **7. Disclaimer**

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