

EXPLANATORY MEMORANDUM TO THE TRIBUNAL REPORT

THE EXECUTIVE COUNSEL TO THE FINANCIAL REPORTING COUNCIL

-and-

(1) DAVID COSTLEY-WOOD (2) KPMG LLP

The FRC has published the report of the Disciplinary Tribunal (the Tribunal) appointed under paragraph 9(2) of the Accountancy Scheme to hear the Formal Complaint brought by the FRC's Executive Counsel against David Costley-Wood and KPMG LLP relating to conduct in the run up to the administration of various companies in the Silentnight group of companies.

The sole purpose of the Tribunal was to hear and determine the Formal Complaint made against Mr Costley-Wood and KPMG LLP and brought by the FRC's Executive Counsel, and to do so on the basis of the evidence and arguments relied on by those parties. The Tribunal Report follows a public hearing.

The Tribunal has not made, and should not be taken to have made, any finding against any individual or entity other than Mr Costley-Wood and KPMG LLP. It would not be fair to treat any part of the Tribunal's findings, including any part(s) of the Tribunal Report, as constituting or evidencing findings against anyone other than Mr Costley-Wood and/or KPMG LLP.

The published Tribunal Report anonymises several third parties, who are instead identified by various descriptors and ciphers.

IN THE MATTER OF:

THE EXECUTIVE COUNSEL TO THE FINANCIAL REPORTING COUNCIL

And

(1) DAVID COSTLEY-WOOD

(2) KPMG LLP

Counsel for the Executive Counsel: Richard Coleman QC, Nicholas Medcroft QC and Samuel Ritchie.

Counsel for the Respondents: Mark Phillips QC, Anna Boase QC and Matthew Abraham, instructed by Linklaters.

REPORT OF THE DISCIPLINARY TRIBUNAL

Introduction

1. This is the report of the Disciplinary Tribunal comprised of Terence Mowschenson QC, chairman, Michael Brooks (CIMA) and Colin Wilby (Lay Member), appointed pursuant to paragraph 9 (2) of the Accountancy Scheme effective from 8 December 2014 (“the Scheme”)¹ of the Financial Reporting Council (“the FRC”) by the Convenor of the FRC to hear the Formal Complaint of the Executive Counsel of the FRC against the above named Respondents David Costley-Wood and KPMG LLP (“KPMG”).
2. The Tribunal reached unanimous agreement on the findings and conclusions made [and the orders proposed in this Report]

The Respondents

3. Mr Costley-Wood is a partner of KPMG and a member of the Institute of Chartered Accountants in England and Wales (“ICAEW”). At all material times he was (i) an experienced accountant (admitted as an ACA in 1992) and insolvency practitioner and (ii) worked from KPMG’s Manchester office.
 - 3.1. KPMG is a member firm of the ICAEW.
4. References to “the Respondents” are to Mr Costley-Wood and KPMG. It is common ground that KPMG is liable for any Misconduct by Mr Costley-Wood pursuant to the provisions of paragraph 5 (11) of the Scheme. Mr Costley-Wood is only liable for his own Misconduct, but since he was a party to almost all the conduct of which complaint is made it is in general unnecessary to distinguish between them, but where it is necessary we do so.

The Allegations (in summary)

5. The Executive Counsel alleges that from about mid-2010, HIG pursued a strategy of driving Silentnight into an insolvency process (or to the brink of such a process) with a view to passing the Pension Scheme to the Pension Protection Fund (“PPF”) in accordance with the arrangements established by the Pensions Act 2004 (“the 2004

¹ The Scheme was replaced by a new Scheme from 1 January 2021 (“the 2021 Scheme”) which was in turn reissued on 30 March 2021.

Act”), so that HIG could acquire an otherwise profitable business without the burden of the Pension Scheme liabilities. HIG took control of Silentnight after purchasing its debt in February 2011 and creating a liquidity crisis. The strategy was supported by at least some of Silentnight's management to whom HIG had promised equity in the restructured business.

6. The Executive Counsel contends that there ought to have been an obvious objection to such a strategy from the point of view of Silentnight and any member of the ICAEW considering and protecting his or her client's interests. The Executive Counsel’s case is that Silentnight was not already on the brink of entering into a formal insolvency process. A strategy that deliberately put at risk Silentnight’s ability to survive and pre-empted a proper consideration of the alternative restructuring options available to it (if restructuring of any kind was necessary), would not be in the interests of Silentnight, its members and creditors (whose interests would represent the interests of the company to the extent that its solvency was in issue).
7. The Allegations under consideration relate to the Respondents’ conduct in the run up to the administration of the various companies in the Silentnight group of companies. The Allegations relate to the period 16 August 2010 to about 5 April 2011. The First Allegation (“Allegation 1”) is broken down into two periods, the period 16 August 2010 to 13 January 2011 (prior to a formal retainer of KPMG by Silentnight) and thereafter (after KPMG had been retained by Silentnight) to 31 March 2011. Broadly, the allegation is that the Respondents advised and/or assisted both Silentnight and HIG in relation to a proposed acquisition of Silentnight by HIG free of Pension Scheme liabilities at a time when there was a conflict of interest between the interests of Silentnight and HIG, and further the Respondents were seeking to develop a business relationship with HIG, and as a result the Respondents’ judgement was compromised and judgment impaired.
8. In the period prior to 14 January 2011 the Executive Counsel contends that had the Respondents considered their professional obligations they would have been driven to conclude that, in circumstances where they had not conducted an assessment of the financial condition of the company or of the options that might reasonably be available to it, they could not lend their assistance to a transaction whose very purpose was to divest the company of the Pension Scheme liabilities, to the prejudice of the Pension Scheme’s members, and which also threatened the ability of the company to continue trading, to the prejudice of all unsecured creditors and, to the extent they had an economic interest in the company, the shareholders as well.
9. Thereafter, until about 31 March 2011, after the Respondents had been retained by Silentnight to review and advise on the options available to it following from the withdrawal of its overdraft and to assist with the management of its key stakeholders including the shareholders of Silentnight, [Bank 1], HIG, the trustees of the Silentnight Pension Scheme (“the Trustees”) , the PPF and the Pension Regulator

(“tPR”) it is alleged that the Respondents advised and assisted both Silentnight and HIG in circumstances where Silentnight and HIG continued to have conflicting interests, and they had already been involved since 16 August 2010 in assisting HIG. Further the continuing professional involvement of KPMG with Silentnight depended on HIG continuing to pursue its strategy to acquire Silentnight. The Respondents’ professional judgment and objectivity was therefore compromised and impaired by bias in favour of HIG (or was likely to be compromised).

10. As a result of the matters set out in Allegation 1, the Executive Counsel contends that the Respondents’ objectivity was impaired (or was likely to be impaired) and they thereby failed to act in accordance with Fundamental Principle (b), Objectivity, and sections 120, 210 and 220 of the Code.
11. The Executive Counsel’s primary case is that there was an actual impairment of objectivity however in the alternative she relies upon the Respondents’ alleged failure to recognise and address obvious threats to their objectivity.
12. The Respondents deny the allegation. First, they contend that they did not advise HIG, and that to the extent that any assistance was provided to HIG it was with Silentnight's approval and in accordance with market practice. Secondly, they say that Silentnight was on its last legs and bound to fail and that HIG was the only viable option. On the Respondents’ case, Silentnight's and HIG’s interests were aligned at all material times such that there was no conflict and therefore no threat to their objectivity.
13. The Second Allegation (“Allegation 2”) is that the Respondents knowingly or recklessly assisted with the provision of untrue and/or misleading and/or materially incomplete explanations to the PPF, tPR, Silentnight and the trustees of the Pension Scheme regarding the causes of Silentnight’s financial difficulties and HIG’s involvement as a “white knight” in relation to Silentnight in breach of the Fundamental Principle (a), Integrity, and section 110 of the Code.
14. The Third Allegation (“Allegation 3”) is that the Respondents knowingly or recklessly provided and assisted in the provision of untrue and/or misleading and/or materially incomplete explanations to the PPF regarding whether or not HIG was connected with Silentnight in breach of Fundamental Principle (a), Integrity and section 110 of the Code.
15. As a result of the alleged conduct the Executive Counsel contends that the Respondents conduct fell significantly short of the standards reasonably to be expected of a Member (in the case of Mr Costley-Wood) and of a Member Firm (in the case of KPMG) and has brought, or is likely to bring, discredit to Mr Costley-Wood, to KPMG and to the accountancy profession.

16. We incorporate in our Report, as Annex 1, the terms of the Allegations as set out in the Executive Counsel's Amended Formal Complaint.

17. Paragraph 9(7) of the Scheme requires us to determine whether to make an Adverse Finding in respect of the Misconduct alleged by the Executive Counsel in the Formal Complaint or to dismiss the Complaint. An "Adverse Finding" is defined in paragraph 2(1) of the Scheme, so far as is relevant, as:

"a finding by a Disciplinary Tribunal that a Member or Member Firm has committed Misconduct."

18. "Misconduct" is defined in the same paragraph as:

"an act or omission or series of acts or omissions, by a Member or Member Firm in the course of his or its professional activities (including as a partner, member, director, consultant, agent, or employee in or of any organisation or as an individual) or otherwise, which falls significantly short of the standards reasonably to be expected of a Member or Member Firm or has brought, or is likely to bring, discredit to the Member or the Member Firm or to the accountancy profession."

19. The Executive Counsel relies on both limbs of the definition of Misconduct, i.e., conduct falling significantly short of the standards reasonably to be expected and conduct that has brought, or is likely to bring, discredit to the profession.

20. In the MG Rover case (FRC Executive Counsel v Deloitte and Einollahi (Tribunal 2 September 2013, Appeal 2014/15)) the Tribunal gave the following summary of the test:

[18] Before we can make a finding that the Respondents or either of them are guilty of misconduct and make a finding adverse to them we have to be satisfied not only that there has been a departure from the conduct reasonably to be expected of a member or member firm but that that departure has been significant. Whether that departure is significant is a matter for our judgment. A trivial departure will not suffice. We have to be satisfied before we reach a conclusion that there has been such a departure, that the Executive Counsel has proved that no reasonable accountant would have acted in the way that the Respondents have acted.

[24] We accept the Respondents' contention that for the Respondents to be guilty of misconduct and to have acted in a way that no reasonable professional would have acted the conduct has to amount to more than mere carelessness or negligence and has to cross the threshold of real seriousness. It is not sufficient for the Executive Counsel to prove that the Respondents failed to act in accordance with good or best practice or that most or many members of the profession would have acted differently. The conduct has to be more serious than that.

21. We have applied this test which has been applied in a number of cases.
22. The Executive Counsel bears the burden of proof in proving to the satisfaction of the Tribunal that the facts and matters relied upon amount to Misconduct. The standard of proof is the civil standard, i.e., the balance of probabilities: paragraph 12 of the Scheme. In the light of the seriousness of the Allegations we cannot conclude that there has been Misconduct unless it is supported by clear and cogent evidence.
23. On 5 March 2021 the Executive Counsel made an application to adduce 14 documents which had been disclosed by the Respondents after the Tribunal hearing had ended on 11 December 2020 and in addition tPR 's Regulatory Intervention Report ("the RIR") which was published on 2 March 2021. The Respondents did not oppose the production of 12 of the 14 documents which had not been disclosed earlier due to technical difficulties with the computer searches run by KPMG to find relevant documents. 2 of the documents had been disclosed. As the Respondents do not oppose production we do not propose to describe the technical difficulties which caused delay in production. The Tribunal has jurisdiction to take into account any relevant evidence, whether or not such evidence would be admissible in court (paragraph 9 (6) of the Scheme. Insofar as the Tribunal find the additional documents of assistance they are referred to in our Report where they are relevant. The Respondents also did not object to the RIR being adduced but did not agree that the RIR should be treated as prima facie evidence of the facts found for the purposes of paragraph 16 (4) (vi) of the 2021 Scheme. We deal with the manner in which we propose to deal with the material in the RIR in the context of other regulatory proceedings referred to below.

The standards of conduct

24. In determining what were the relevant reasonable standards applicable to the Respondents, the Tribunal is bound to be guided by the Principles and Statements of Guidance set out in the ICAEW's Code of Ethics ("the Code").
25. The standards reasonably to be expected of a Member or Member Firm include the Fundamental Principles and guidance in Parts A and B of the Code.
26. There are two relevant versions of the Code:
 - 26.1. the version which applied from 1 September 2006 to 31 December 2010;
 - and
 - 26.2. the version which applied from 1 January 2011 to 31 December 2019.
27. Both versions apply to Allegation 1, which covers the period from 16 August 2010 to 31 March 2011. The 2011-2019 version of the Code applies to Allegations 2 and 3 (the integrity allegations).

28. Section 1 of the Code contains the introduction and explains the approach, scope and authority of the Code including the approach taken by the ICAEW to secure the maintenance of high professional standards among its members in the interests of the public:

1.1: One of the principal objects of the Royal Charter is to maintain high standards of efficiency and professional conduct of members of the ICAEW. The Code of Ethics applies to all members and member firms.

1.2: Professional accountants have a responsibility to take into account the public interest (considered in more detail in paragraph 100.1) and to maintain the reputation of the accountancy profession. Personal self-interest must not prevail over those duties. The Code helps professional accountants meet these obligations by providing ethical guidance.

1.3: . . .

1.4: Professional accountants are expected to follow the guidance contained in the fundamental principles in all their professional and business activities whether carried out with or without reward and in other circumstances where to failure to do so would bring discredit on the profession. . .

1.6: Professional accountants shall be guided not merely by the terms but also by the spirit of the Code and the fact that particular conduct does not appear among a list of examples does not prevent it from being misconduct.

1.11: ... significance will be relevant in determining whether there has been a breach of the guidance. Where the intent behind and consequences of the action in question are trivial and inconsequential, the requirements of this Code will not have been breached. In the event of a complaint, the Investigation and Disciplinary Committees will consider the matter, including perceptions of a reasonable and informed third party, having knowledge of all relevant information and will be the arbiter.

1.16: Members who are in doubt as to their ethical position are encouraged to seek advice.

29. Part A of the Code establishes the Fundamental Principles and provides a conceptual framework that requires a professional accountant to identify, evaluate and address threats to compliance with the fundamental principles.² The Fundamental Principles relevant to the Formal Complaint in this matter are integrity and objectivity. Subsection 100.5 of the 2006-2010 version of the Code³ explains the rationale for having a conceptual framework:

The circumstances in which professional accountants operate may give rise to specific threats to compliance with the fundamental principles. It is impossible to define every situation that creates such threats and specify the appropriate mitigating action. In addition, the nature of engagements and work assignments may differ and

² See ss. 100.2 of both Codes.

³ The equivalent passage in the 2011-2019 Code is 100.6.

consequently different threats may exist, requiring the application of different safeguards. A conceptual framework that requires a professional accountant to identify, evaluate and address threats to compliance with the fundamental principles, rather than merely comply with a set of specific rules which may be arbitrary, is, therefore, in the public interest. This Code provides a framework to assist a professional accountant to identify, evaluate and respond to threats to compliance with the fundamental principles. If identified threats are other than clearly insignificant, a professional accountant should, where appropriate, apply safeguards to eliminate the threats or reduce them to an acceptable level, such that compliance with the fundamental principles is not compromised.

30. The following subsections of Part A explain that the responsibility of members is to act in the public interest, the importance of taking account of reasonable and informed public perception when deciding whether or not to accept or continue an engagement, and members' obligation to evaluate threats to their compliance with the Fundamental Principles. (The extracts are from the 2006-2010 version of the Code. References to the equivalent passages in the 2011-2019 version of the Code are footnoted.):

100.1⁴: A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. Acting in the public interest involves having regard to the legitimate interests of clients, government, financial institutions, employers, employees, investors, the business and financial community and others who rely upon the objectivity and integrity of the accounting profession to support the propriety and orderly functioning of commerce. This reliance imposes a public interest responsibility on the profession. Professional accountants should take into consideration the public interest and reasonable and informed public perception in deciding whether to accept or continue with an engagement or appointment, bearing in mind that the level of the public interest will be greater in larger entities and entities which are in the public eye. Therefore, a professional accountant's responsibility is not exclusively to satisfy the needs of an individual client or employer. In acting in the public interest a professional accountant should observe and comply with the ethical requirements of this Code.

100.6⁵ A professional accountant has an obligation to evaluate any threats to compliance with the fundamental principles when the professional accountant knows, or could reasonably be expected to know, of circumstances or relationships that may compromise compliance with the fundamental principles.

110.7⁶: ...If a professional accountant cannot implement appropriate safeguards, the professional accountant should decline or discontinue the specific professional service involved.

100.10 and 100.11⁷, which provide a non-exhaustive list of threats and safeguards.

⁴ The equivalent passage in the 2011-2019 version of the Code can be found at ss. 100.1.

⁵ The equivalent passage in the 2011-2019 version of the Code can be found at ss. 100.8.

⁶ The equivalent passage in the 2011-2019 version of the Code can be found at ss. 100.9.

⁷ The equivalent passage in the 2011-2019 version of the Code can be found at ss. 100.12 – 100.14.

100.15⁸: The nature of the safeguards to be applied will vary depending on the circumstances. In exercising professional judgement, a professional accountant should consider what a reasonable and informed third party, having knowledge of all relevant information, including the significance of the threat and the safeguards applied, would conclude to be unacceptable.

31. Part B of the Code applies specifically to professional accountants in public practice. It provides guidance on how the conceptual framework is to be applied in specific situations and provides examples of safeguards that may be appropriate. Subsection 100.9 of Part A of the 2006-2010 version of the Code⁹ explains that the guidance and examples in Code B are not exhaustive:

Parts B and C of this Code include examples that are intended to illustrate how the conceptual framework is to be applied. The examples are not intended to be, nor should they be interpreted as, an exhaustive list of all circumstances experienced by a professional accountant that may create threats to compliance with the fundamental principles. Consequently, it is not sufficient for a professional accountant merely to comply with the examples presented; rather, the framework should be applied to the particular circumstances encountered by the professional accountant.

32. Section 200.2 of Part B of the 2006-2010 version provides:¹⁰

A professional accountant in public practice should not engage in any business, occupation or activity that impairs or might impair integrity, objectivity or the good reputation of the profession and as a result would be incompatible with the rendering of professional services.

33. The Executive Counsel relies on the following sections of Part B of the Code: s. 200 (introduction), s. 210.0– 210.8 (regarding Professional Appointments including evaluation of any threats to compliance with the fundamental principles, the evaluation of such threats and the application of safeguards) and 220 (regarding conflicts of interest).

Integrity

34. References are to the 2011-2019 version of the Code which is the relevant Code for the purposes of the two integrity allegations, i.e., Allegations 2 and 3.

⁸ The equivalent passage in the 2011-2019 version of the Code can be found at ss. 100.7.

⁹ The equivalent passage in the 2011-2019 version of the Code can be found at ss. 100.3.

¹⁰ The wording of ss. 200.2 in the 2011-2019 version of the Code differs slightly: “A professional accountant in public practice shall not knowingly engage in any business, occupation, or activity that impairs, or might impair integrity, objectivity or the good reputation of the profession and as a result would be incompatible with the fundamental principle.”

35. The Principle of Integrity imposes an obligation on all professional accountants “to be straightforward and honest in all professional and business relationships” (see ss. 100.5(a) and 110 of the Code).
36. The Executive Counsel’s case in relation to Allegations 2 and 3 is that the Respondents failed to act with integrity. Although it is alleged that the Respondents’ conduct was dishonest, Allegations 2 and 3 do not depend on dishonesty being established. Integrity under the Code is a broader and more exacting standard than honesty (the concept of dishonesty is considered separately below). In professional codes of conduct, “integrity” is a useful shorthand to express the higher standards society expects from professional persons and which the professions expect from their own members. Integrity connotes adherence to the ethical standards of one’s own profession - and that this involves more than mere honesty (see Wingate and Evans v The Solicitors Regulation Authority [2018] 1 WLR 3969 (at [97] & [100])). The courts have eschewed a comprehensive definition. As Rupert Jackson LJ observed in Wingate, at [99], the observations of the Financial Services and Markets Tribunal in Hoodless v FSA [2003] UKFIT [7] have met with general approbation. In Hoodless, the FSMA Tribunal said (in an extract quoted at [66] of Wingate) that “integrity” connotes moral soundness, rectitude and steady adherence to an ethical code”. As Rupert Jackson LJ observed at [102] “[i]n every instance, professional integrity is linked to the manner that particular profession professes to serve the public”.
37. Under the Code, integrity includes being “straightforward and honest”, “fair dealing and truthfulness” and performing work which is “uncorrupted by self-interest and not influenced by the interests of other parties” (s. 110.1 of the later Code). Integrity also requires that an accountant must not be knowingly associated with false or misleading information. Section 110.2 of the Code provides:
- A professional accountant shall not knowingly be associated with reports, returns, communications or other information where they believe that the information:
- contains a materially false or misleading statement;
 - contains statements or information furnished recklessly; or
 - omits or obscures information required to be included where such omission or obscurity would be misleading.

When a professional accountant becomes aware that the accountant has been associated with such information, the accountant shall take steps to be disassociated from that information.

Dishonesty

38. The two stage test for dishonesty is that established by the Supreme Court in Ivey v Genting Casinos [2018] AC 391: (a) what was the defendant’s actual state of knowledge or belief as to the facts and (b) was his conduct dishonest by the standards of ordinary decent people (R v Barton Booth [2020] 2 Cr. App.R. 7 at [85], [105],

[107] – 108]). Following Ivey, there is no longer any divergence between the test for dishonesty in criminal cases and the test in civil actions.

Recklessness

39. The Executive Counsel and the Respondents were in agreement as to the criteria for recklessness. A person acts recklessly with a respect to:

- (i) A circumstance when he is aware of the risk that it exists or will exist;
- (ii) A result when he is aware of a risk that it will occur; and

it is in the circumstances known to him, unreasonable for him to take the risk. This definition of recklessness has been adopted in disciplinary proceedings before the Solicitors Disciplinary Tribunal (Brett v SRA) [2014] EWHC 2974] and the Financial Conduct Authority (Carrimjee v FCA) [2015] UKUT 0079).

Objectivity

40. Unless otherwise stated, the references are to both versions of the Code.

41. The Principle of Objectivity imposes an obligation on all professional accountants “not to compromise their professional or business judgement because of bias, conflict of interest or the undue influence of others.” (ss. 120 of Part A of the Code). Objectivity is defined as “the state of mind which has regard to all considerations relevant to the task in hand but no other” (s. 120.1 of the Code).

42. Subsection 120.2 of the Code states: “A professional accountant may be exposed to situations that may impair objectivity. . . . The final sentence of the equivalent subsection of the 2011-2019 version of the Code states: “A professional accountant shall not perform a professional service if a circumstance or relationship biases or unduly influences the accountant’s professional judgment with respect for that service.”.

43. Compliance with the Fundamental Principles, including the Principle of Objectivity, may be threatened by a broad range of circumstances. The main categories of threat are identified in s. 100.10 of the 2006-2010 version of the Code.¹¹ They include threats arising from self-interest, advocacy and familiarity.

44. In addition to those threats to objectivity, section 220 of the Code deals with threats to objectivity arising from conflicts of interest. Section 220.1 gives an apt example: “a threat to objectivity or confidentiality may also be created when a professional accountant in public practice performs services for clients whose interests are in conflict or the clients are in dispute with each other in relation to the matter or

¹¹ Ss. 100.12 of the 2011-2019 version of the Code.

transaction in question.” Section 220.1 goes on to provide that “Subject to the specific provisions, there is, however, nothing improper in a professional accountant in public practice having two clients whose interests are in conflict.” However it is clear from section 220.1, and indeed from the Code as a whole, that this sentence does not sanction a professional accountant acting where the conflicting interests of two clients pose a threat to his objectivity and safeguards are not in place that eliminate or reduce that threat to an acceptable level.

45. The Executive Counsel contends that the Respondents’ objectivity was in fact impaired; however the Executive Counsel’s case does not depend on existence of actual impairment of objectivity. The Code provides that a professional accountant in public practice shall not knowingly engage in any activity that impairs or might impair integrity or objectivity (s.200.2); actual as well as the risk of impairment is covered.
46. The policy of the disciplinary scheme is to guard against the risk that integrity and objectivity might be compromised. Accordingly section 220.2 of Part B of the Code indicates that the objectivity principle is contravened if a reasonable and informed observer would perceive that the objectivity of the professional accountant is likely to be impaired.

Identifying threats to objectivity

47. The Code provides detailed guidance in relation to (a) identifying threats to compliance with fundamental principles and (b) safeguards to eliminate such threats or reduce them to an acceptable level. In addition to the subsections of Code A referred to above:
 - 47.1. section 200 of Part B also deals with threats and safeguards.
 - 47.2. ss 210.1 and 210.7 of Part B¹² require that the professional accountant consider threats to compliance with the fundamental principles “before accepting a new client relationship” and “before accepting a specific client engagement”.
48. Section 220.1 of Part B of the Code (Conflict of Interest) provides that “A professional accountant in public practice shall take reasonable steps to identify circumstances that could pose a conflict of interest. Such circumstances may create threats to compliance with the fundamental principles” and s.220.2:

“A professional accountant in public practice shall evaluate the significance of any threats and apply safeguards when necessary to eliminate the threats or reduce them to an acceptable level. Before accepting or continuing a client relationship or specific engagement, the professional accountant in public practice shall evaluate the significance of any threats created by business interests or relationships with the client or a third party.

¹² ss. 210.1 and 210.6 of the 2011-2019 version of the Code.

A test is whether a reasonable and informed observer would perceive that the objectivity of professional accountants or their firms is likely to be impaired. The professional accountants or their firms shall be able to satisfy themselves and the client that any conflict can be managed with available safeguards. “.

49. Possible safeguards in relation to a conflict or possible conflict of interest are identified in sections 220.3 and 220.4. If the threat to the fundamental principles cannot be eliminated or reduced to an acceptable level through the application of safeguards, the accountant should conclude that it is not appropriate to accept a specific engagement or shall resign from one or more conflicting engagements: section 220.5.
50. As regards the importance of client identification, the Executive Counsel relies on MG Rover (Executive Counsel to the FRC v Deloitte and Einollahi), per Sir Stanley Burnton at [139]:
- [B]etween January and the end of June 2011, it was unclear for whom Deloitte and Mr Einollahi were acting. As we pointed out above, such a lack of clarity does not necessarily involve misconduct. The importance for the accountant of clear identification of the client at as early a stage as is possible is that it enables the accountant not only to determine what work is required of him but also to address the question whether there is any relevant conflict of interests, and if there is to take appropriate remedial or preventative action so far as possible. Its importance for the client for whom he does not act on the engagement in question is that it should enable him to decide whether he wishes to obtain independent advice. If there were no question of conflicts or lack of objectivity on the part of the Appellants, we would be reluctant to consider that delay in identifying the client or in providing an engagement letter of itself amounted to misconduct.
51. Section 200.3 of the 2006-2010 version of the Code provides that safeguards which should normally be implemented in the case of a conflict of interest include notifying the client that the firm’s activities might represent a conflict of interest and obtaining the client’s consent to the accountants acting or informing all the parties that the accountant for the parties is acting in circumstances where their respective interests are in conflict.
52. The Respondents contend that there are three “gateways” into the objectivity principle namely (i) bias, (ii) conflict of interest and (iii) undue influence of others. We do not consider that the references to the three matters are gateways. Objectivity is defined as “the state of mind which has regard to all considerations relevant to the task in hand but no other” (s. 120.1 of the Code). The references to bias, conflict of interest and undue influence are to three ways in which the principle of objectivity might be infringed. Further the Respondents contend that the expressions should be interpreted in the manner in which they have been interpreted in the context of legal cases. Thus, for example, they contend that the expression “bias” should be interpreted as one

would construe it in the case of a person exercising a judicial role and conflict of interest and undue influence should be construed by reference to the manner in which the expression is construed as applying to fiduciaries, or in the case of undue influence, in accordance with equitable principles. We reject that submission. The Respondents' contention would prevent the objectivity principle from being applicable in cases where the practitioner was not acting as an officer of the court or limit it to cases where the practitioner was exercising a quasi-judicial role, or acting as a fiduciary. The expressions are intended to apply to accountants whether or not acting as officers of the court or whether they are in a fiduciary relationship with their clients. They may often not be in a fiduciary relationship with their clients. The words are to be given their ordinary English meaning as can be seen from the definition of objectivity set out above.

Witness evidence

53. The Tribunal heard the following witnesses of fact:

for the Executive Counsel:

53.1. [Bank 1 Senior Management 1], a former director (who was appointed in 2009) in the Strategic Business Services ("SBS") division within [Bank 1] ("the Bank"). The Silentnight file was passed to him in about April 2010. He gave evidence to the effect that the Bank was keen to exit the relationship with Silentnight but had confidence in Silentnight's management. The Bank was concerned with its reputation in the community and was aware that the insolvency of Silentnight could damage its reputation. He gave evidence to the effect that the Bank insisted on terminating the overdraft as part of the sale of the Silentnight debt to HIG. In relation to renewal of banking facilities in November 2011 (including the exit fee of £5 million) he declined to speculate as to whether the Bank would have placed Silentnight into administration but insisted that all options would have been considered by the Bank.

53.2. [Private Equity Firm 3 Partner] gave evidence to the effect that [Private Equity Firm 3]'s withdrawal from its attempt to acquire Silentnight was connected to the merits of the take over and did not have anything to do with the conduct of Mr Costley-Wood or KPMG.

53.3. [External Financial Advisor 4 Partner 1], a former partner of [External Financial Advisor 4] who was involved with Silentnight who produced the Project Jane report in March 2009 and understood that the Bank was supportive of Silentnight in 2009 and that Silentnight was paying its debts as they fell due. [External Financial Advisor 4] acted for the shareholders in January and February 2011 in relation to [Private Equity Firm 3]'s attempts to refinance Silentnight after the Debt Sale Agreement.

for the Respondents:

53.4. Mr Costley-Wood: One of the difficulties with Mr Costley-Wood's evidence was that he did not keep contemporaneous notes of telephone conversations or meetings. In response to a number of questions relating to telephone conversations with personnel from HIG and [Silentnight Board Member 1] he said that he could not remember what the subject matter of the conversation was. Our impression of him was that he was a person who worked quickly and under pressure and spent little time reviewing documents to assess their accuracy before he agreed to them and could act (including answering questions in cross examination) somewhat impetuously. At times his oral evidence differed from that contained in his witness statement. For example he described the purpose of a meeting held on 16 August 2010 as being to consider restructuring options (consistently with [HIG Senior Management 2]'s email of 10 August 2010 in which he indicated that he wanted a recommendation at the meeting on "administration – post pack vs. CVA vs. other") and that he became aware of HIG's strategy during the course of the meeting but in evidence he said that he attended the meeting in order to convince HIG not to place Silentnight into administration. In other words that he was aware of HIG's intentions prior to the meeting. We have taken into account that it is likely that his witness statement was drafted for him by his solicitors and some of the discrepancies may be due to the characteristics set out above. Furthermore

53.4.1. When tPR requested documents from KPMG in 2011 so that tPR could investigate the circumstances of Silentnight's insolvency in order to ascertain whether to use tPR's moral hazard powers, Mr Costley-Wood, appreciating that his colleague, [KPMG Employee 6], had not created a contemporaneous note emailed his secretary, [KPMG Employee 7], to draw up a note of the meeting and provided her with text to insert in the note. He did not ask his secretary to place a rubric on the note to the effect that it had been produced on 21 September 2011 and was not contemporaneous. Instead the date at the top of the note erroneously refers to a meeting held on 16 August 2011 (the meeting was held on 16 August 2010) and at the bottom of the note it states in small letters DCW/js/2011 (which might be a typing or filing reference). The note was then sent to tPR on 23 September 2011 without attention being drawn to the date when it was produced – as shown by the recently adduced covering email of [KPMG Employee 5] to tPR. Mr Costley-Wood accepted that the meeting on 16 August 2010 was important and that the note was created for the purpose of providing information to tPR. In Mr Costley-Wood's witness statement he refers to the note as 'incorrectly dated'. When asked whether he had considered the note carefully in the course of the preparation of his witness statement he replied in the affirmative and added "although from memory, the note was prepared a while after the meeting" and confirmed that he appreciated the note was an important note of a material meeting and was prepared in the context of a request by tPR using his statutory powers to investigate. However he refused to accept the proposition from counsel that he should have made it clear to tPR that the note had been

prepared more than one year after the meeting or that he should have produced his email to his secretary asking for the note to be typed up. His evidence was that tPR could see the date the note was prepared from the date on the bottom of the note. The Tribunal was concerned at Mr Costley-Wood's attitude to revealing the date on which the note was prepared; if tPR had been aware it was prepared 13 months after the meeting tPR might have wished to explore its accuracy. Although Mr Costley-Wood said he read the note before it was sent to tPR, he himself missed the erroneous date on which the meeting was recorded before he arranged for it to be sent, as it appears did tPR when tPR received it, and Executive Counsel (or her staff) when she first saw the note. The matter came to light when leading counsel for the Executive Counsel saw Mr Costley-Wood's email to his secretary which was referred to in the exhibit to the expert evidence of Mr Shaw, the Respondents' expert witness shortly before the hearing. Mr Costley-Wood's refusal to accept that he should have brought the date on which the note was prepared to tPR's attention illustrates a somewhat casual approach to procedure and regulation. The contents of the note were not accepted as accurate by Executive Counsel.

53.4.2. In addition Mr Costley-Wood tended to bolster his case during the course of his evidence which was not supported by the contemporaneous evidence.

53.4.2.1. In the course of his evidence he suggested that Silentnight faced a burning platform for a number of reasons including the liability to the Pension Scheme and for the Exit Fee due on 30 November 2011. The contemporaneous evidence shows that he and everyone else concerned considered that the burning platform was caused by the withdrawal by the Bank of the overdraft facility in the context of the Debt Sale Agreement.

53.4.2.2. In his witness statement and in evidence he stated that KPMG had not undertaken any independent financial analysis of Silentnight before 17 January 2011 or carried out an options analysis before 14 January 2011 (the end of the first period in Allegation 1). There was no documentary evidence which suggested that he had done so, no such evidence was shown to Mr. Shaw, and if he had undertaken such an analysis, one would have expected such documentation to exist, and to be produced particularly in the light of the manner in which Executive Counsel put her case. Subsequently in the course of his cross examination he asserted that he had performed a financial analysis and done so in his head. He had not produced a written options report because [Silentnight Board Member 1] had not asked him to as [Silentnight Board Member 1] did not wish to incur the cost and he, Mr Costley-Wood, did not have the time. The absence of any reference in the documentation in the first period to any option other than a CVA or administration indicates that there was no consideration of the options available to Silentnight in the light of its financial position.

53.4.3. KPMG sent Silentnight and HIG documents on 6 and 7 September 2010 which stated that KPMG “can provide advice to HIG and the Company throughout the CVA process – both pre and post” in circumstances in which it should have been clear that it could not advise both. Mr Costley-Wood could not recall whether he noticed the statements in the document, but he stated that at that time it was still possible for KPMG to have advised both as a retainer with Silentnight had not been signed.

53.4.4. In the KPMG Restructuring Risk Management Panel form dated 30 March 2011, a compliance form which was submitted to the KPMG’s Restructuring Risk Management Panel), the form stated that KPMG had “been engaged to assist . . . following the withdrawal of [Bank 1 Trading brand] as the Group’s main funder” and noted that the work could lead to an appointment as nominee or supervisor in a CVA or to an appointment as administrator. Under the heading scope of work and under Engagement Partner (i.e., Mr Costley-Wood) view it stated that “we have been working for Silentnight company side since January firstly with an options review and then to try and agree a PPF compromise with the Pensions Regulator and PPF.” The question for the KRRMP to review was whether given that the KRRMP referral was mandatory “are we able to accept this engagement given the consideration given to managing the material professional relationship that may exist between us and the Group.” [sic]. The form was incomplete as it did not describe the ad hoc retainer that existed between KPMG and Silentnight from about 16 August 2010 and pursuant to which Mr Costley-Wood and [KPMG Employee 10], on the Respondents’ case spent about 104 hours of chargeable time at a cost of about £45,000 prior to 14 January 2011.

53.5. [KPMG Employee 9], a partner and UK Head of Debt Advisory at KPMG who was involved in the introduction of HIG to KPMG in 2009. He had no evidence to give as to the exchanges between Mr Costley-Wood or [KPMG Employee 10] and HIG but could give evidence as to the events leading to the introduction of HIG to KPMG and subsequently how HIG mentioned its interest in Silentnight in mid-2010.

53.6. [KPMG Partner 2], a Risk Director in the Restructuring Team at KPMG who explained the firm’s compliance procedures in his statement. He had no first-hand knowledge of matters relating to Silentnight and gave his evidence fairly and in order to assist the Tribunal.

53.7. [Partner at Silentnight Law firm 1], whose firm was instructed by Silentnight on about 25 January 2011 to advise on the proposed restructuring of Silentnight. She could not give any substantive assistance on the issues before the tribunal.

53.8. [A restructuring adviser at the PPF] [redacted], who was one of the recipients of allegedly misleading statements which form the subject matter of Allegations 2 and 3. Albeit in his witness statement he stated that (i) the chronology of how the Silentnight Debt was acquired was not relevant to his considerations as to whether the PPF should be a party to the restructuring but that he was concerned with the situation before him and the PPF Guidance to the situation; and (ii) the precise circumstances in which “HIG/Bayside” acquired the Silentnight Debt were not relevant to his decision making process, he went on to say in his witness statement that if an otherwise healthy company were deliberately “busted” that would be a risky strategy because tPR might decide to use its moral hazard powers. The apparent inconsistency in his witness statement was partly resolved once one understood that he considered that tPR was responsible for considering the exercise of tPR’s moral hazard powers and would not sanction a compromise by the Trustees and the PPF, if it considered it might wish to use its powers. Further the PPF would always consider whether a contribution notice or a financial support direction by tPR might generate more money for pension scheme than the transaction proposed to the PPF. In cross examination he shifted his position slightly as it was an unrealistic suggestion that the PPF would negotiate a compromise ignoring matters that were likely to be of interest to tPR and which might lead it to withhold consent to a compromise. We do not consider he set out to mislead the Tribunal but had a particularly binary approach to the different responsibilities of the PPF and tPR in certain sections of his witness statement.

54.

54.1. In addition the Executive Counsel relied on various witness statements (as hearsay) served in contribution proceedings brought by tPR against a number of HIG entities and individuals to recoup losses allegedly sustained by the Pension Scheme as a result of the transactions involving Silentnight some of which provide background to the Formal Complaint:

54.1.1. [Silentnight Board Member 6] [redaction];

54.1.2. [Trustee 1], a professional trustee of the Silentnight Pension Scheme;

54.1.3. [Trustee 2], a trustee of the Silentnight Pension Scheme;

54.1.4. [Senior Advisor at tPR], [redaction] at tPR; and

54.2. the Respondents relied (as hearsay) on the following witness statements also provided in the contribution proceedings brought by tPR;

54.2.1. [Silentnight Board Member 1], [redaction] Silentnight;

54.2.2. [Silentnight Board Member 2], [redaction] Silentnight;

54.2.3. [Silentnight Board Member 4], [redaction] of Silentnight;

54.2.4. [HIG Senior Management 2], [redaction] HIG;

54.2.5. [HIG Senior Management 3], [redaction] within the HIG group;

54.2.6. [HIG Board Member 2], [redaction], and

54.2.7. [Senior Advisor at tPR].

55. The Tribunal also heard expert evidence from Mr Kevin Murphy for the Executive Counsel and Mr Mark Shaw for the Respondents. Further an expert report produced for HIG by Mr Alastair Beveridge dated 16 December 2015 and filed in tPR proceedings was contained in the Tribunal bundle; it was included at the request of the Respondents in case it was required for cross examination and was used by counsel for the Respondents for that purpose.

Approach to the evidence

56. In addition in assessing the evidence we have to take into account that some of the matters under scrutiny took place about 10 years before the hearing. Accordingly, the recollection of those witnesses who gave evidence relating to the events under considerations such as Mr Costley-Wood and [A restructuring adviser at the PPF] , might have faded over time and been replaced or supplemented by reconstruction or hindsight, or they might simply have been unable to recollect events.

57. In this connection, contemporaneous evidence assumes considerable importance for obvious reasons. We were referred to the observations of Leggatt J (as he then was in Gestmin SGPS SA v Credit Suisse (UK) Limited [2013] EWHC 3560 (Comm) at [16] – [22]. We also take into account that Mr Costley-Wood’s practice was not to make contemporary notes of telephone calls or meeting and so we do not draw any adverse inference from his inability to produce a contemporary note where that might have been useful and others in his position might have made such a note. There is no allegation that the failure to keep accurate records amounted to Misconduct but his evidence would have been assisted had he kept a contemporaneous record as there were a number of occasions when he could not recall what occurred during the course of a conversation or meeting.

58. Insofar as evidence in witness statements prepared for tPR proceedings is concerned we approach it with additional care. It was not tested by cross examination and certain of the witnesses may have been motivated in providing their evidence by self-interest or dissatisfaction with what occurred in relation to Silentnight.

The Key Protagonists

Silentnight

59. The Silentnight group of companies, referred to as “Silentnight”, was at all material times based in the North West of England. In early 2011, at the time HIG acquired the Silentnight Debt from the Bank it was the largest bed and mattress manufacturer in the UK. It also had valuable exclusive rights to make and sell [Supplier A] mattresses (the world’s leading brand) in the UK. It employed approximately 1,250 employees across sites in Lancashire, Cumbria, West Yorkshire. It also had a site in Ireland.

60. Silentnight was owned by the [Shareholder A family], having been founded by [Shareholder A] in 1946. The company had been publicly listed but in 2003, in a

transaction financed by [Bank 1], the [Shareholder A family] took the company private again and it was delisted.

61. The structure of Silentnight was as follows:

61.1. ABF Limited was the main trading entity and was owned by Silentnight Group Limited.

61.2. Silentnight Group Limited was owned by Silentnight Holdings Limited, which was in turn 75 percent owned by Famco Holdings Limited (“Famco”) and 25 percent by [Silentnight Board Member 5].

62. Famco was the entity which held the family’s interest. [redaction]..

63. As a result of a combination of unsuccessful acquisitions in the late 1990s and early 2000s, the [Shareholder A family]’s reacquisition of the entire interest in the business in 2003, and (from 2008) the global financial crisis, Silentnight was burdened with substantial debt and a rising pension deficit which presented its management with the challenge of securing the long-term viability of the company. In 2004 the Bank transferred responsibility for Silentnight to its SBS division within Bank 1] where it remained until the Bank sold the Silentnight Debt in early 2011. Normally a company in the SBS division within Bank 1] would have been expected to remain there for 1 to 2 years. The Bank had had significant concerns as to the future viability of the Silentnight Group over a number of years and as to the level of security held by the Bank albeit these concerns appear to have been alleviated during the course of 2010.

64. In 2006, [Silentnight Board Member 3] and [Silentnight Board Member 1] were appointed to address the challenges facing the company. In 2006, [Bank 1] refinanced the business in the absence of any other willing funder. These facilities which are described in more detail below, including a Term Loan (“the Term Loan”) repayable by 30 November 2011 and an overdraft facility (the indebtedness on the Term Loan and the overdraft balance are referred together as “the Silentnight Debt”). The Term Loan included an escalating Exit Fee which is described more fully below.

65. Silentnight also had a Defined Benefit Pension Scheme (“the Pension Scheme”) with about 1300 members. By the time of the events material to these proceedings there was a substantial deficit in the Pension Scheme’s assets as compared with the actuarial assessment of its liabilities. The deficit was a long-term unliquidated liability which was based on fluctuations in the valuation of the Pension Scheme’s assets and on actuarial predictions about the assets required to meet the Pension Scheme’s accrued obligations to members stretching over many years. Pension Scheme deficits are influenced by developments in the economy and expand and contract with movements in stock markets, interest rates, mortality rates and so on. However, as described below, the deficit was not threatening the day-to-day viability of the company in the relevant period. The trustees of the Pension Scheme (“the Trustees”) remained supportive of the company throughout. There was no question of the Trustees seeking

to liquidate the company, as they believed that the ongoing viability of the company was in the interests of the Pension Scheme members. The Trustees' approach was entirely in accordance with tPR guidance, which recognises that, where there is a substantial deficit, the best means of delivering members' benefits is usually for the scheme to have the continued support of a viable employer.

66. There are various approaches to valuing pension deficits depending on the purposes of the valuation:

66.1. Section 179 of the 2004 Act requires an actuarial valuation of a pension scheme's assets and liabilities at least every three years in order to determine whether the scheme is sufficiently funded. This must be reported to the PPF and is used to establish the PPF levy. This funding shortfall was estimated at £39.5million in June 2010 based on the 2008 accounts. In the Project Bale Report on 31 January 2011, the Respondents estimated it (as at 1 December 2009) at £53.6 million.

66.2. A [redacted] deficit gives rise to an obligation on the part of the trustees and company to agree a deficit repair plan in a process that is regulated by tPR.

66.3. If an employer suffers an insolvency event it becomes liable to the pension scheme in an amount determined by section 75 of the [redacted] Act. The section 75 liability is based on the cost of purchasing insurance to secure members' benefits (referred to as "the buyout cost"). If the PPF assumes responsibility for the pension scheme it succeeds to the trustees' rights in respect of the section 75 debt. The section 75 debt is usually much higher than an actuarial assessment of a scheme's deficit. In the case of Silentnight, the section 75 debt was estimated at c.£100,000,000 in 2011. The relevance of the section 75 debt in the present case is that if the PPF assumed responsibility for the pension scheme in the context of a CVA, the section 75 debt would be triggered. That would both substantially increase the amount of Silentnight's liabilities to the trustees of the Pension Scheme and also impact on the amount that other unsecured creditors whose claims ranked *pari passu* with the trustees (or the PPF as their successors) would recover from the insolvent estate.

66.4. When producing the annual financial statements, the [Silentnight Board] would report a value according to Financial Reporting Standard 17 on (Retirement Benefits). The net pension liability shown on the consolidated balance sheet for the financial year ended 30 January 2010 was £18,288,000.

66.5. [Trustee 1], a professional trustee of the Pension Scheme explained in his witness statement prepared in connection with tPR investigations that actuarial valuations are prudently calculated. His judgement based on expert advice was that the true long-term cost for the company was materially lower than the actuarial deficit. In February 2011 he obtained advice from the scheme actuary, [redaction]

for the purpose of seeking to agree a solvent compromise with HIG of the company's liability to the Pension Scheme. They advised that whilst the section 75 buy out deficit was between £80 million and £100 million, the "best estimate" deficit, based on full benefits, was actually around £12 million.

67. A Deficit Repair Plan ("the 2010 Deficit Repair Plan") had been agreed with the Trustees 25 June 2010, which provided for contributions to be made by Silentnight as follows:

- (a). £340,000 p.a. from 1 July 2010 to 31 January 2014;
- (b). £1million p.a. from 1 February 2014, increasing by £100,000 p.a. until 1 February 2017;
- (c). £2.3million p.a. from 1 February 2017, increasing by £234,000 p.a. until 1 February 2039.

68. Silentnight had made a profit in the years 2006 to 2010. The UK was emerging from a recession. On HIG's own analysis in its document "Silentnight – Opportunity Update dated December 2010" Silentnight had a market share of 23 percent of the UK bedding market worth £586 million and had made sales over the 12 months ending December 2010 of £115.2 million and an EBITDA of £6.7million. A reasonable estimate of Silentnight's maintainable EBITDA going forward was £7.4 million per annum. However, in mid 2010 Silentnight remained indebted to the Bank and would not be able to generate sufficient trading profits to pay the balance of the Term Loan of about £3 million and the Exit Fee of £5 million that would become due to the Bank on 30 November 2011. As a result of these obligations, it was common ground that, absent refinancing or restructuring, Silentnight would not have been able to trade beyond 30 November 2011 when its facilities with the Bank were repayable.

69. Refinancing or restructuring could, in theory, take a number of different forms, with differing consequences for those who had a legally recognisable interest in the company (the shareholders, the creditors the largest of which was the Pension Scheme, the PPF and tPR):

69.1. A refinancing could involve raising additional funds from a funder, whether it be from the Bank, another funder, the shareholder, and/or the Pension Scheme itself. [Silentnight Board Member 1] had approached [Bank 2], [Bank 3] and [Bank 4] to seek a refinancing of the Silentnight Debt although none had come to fruition. In November 2010, he apparently considered that refinancing with the Bank was likely to be Silentnight's best option as he wrote in an email sent on 22 November 2010 to [Trustee 2], albeit he was at the same time encouraging HIG to acquire the Silentnight Debt.

69.2. A restructuring could take a number of forms including as follows:

69.2.1. It could involve an agreement with the Trustees whereby the liabilities to the Scheme were reorganised so that they were manageable over the long term. The Trustees might agree such a restructure where they considered that the reduced benefits members would receive would still exceed what would be paid if Silentnight failed and the Scheme passed to the PPF (as a consequence of which certain members would receive reduced benefits).

69.2.2. Alternatively, if the PPF and tPR were persuaded that an insolvency process was inevitable if the pension liabilities were not restructured, then a restructuring might involve an agreement with the PPF, approved by tPR, that the Pension Scheme be passed to the PPF in exchange for a payment to the PPF and an equity share in the business. A restructure of this kind is referred to as a Regulated Apportionment Arrangement (“RAA”) or “solvent compromise”, as it would not involve Silentnight itself entering an insolvency procedure.

70. So far as the liability to the Pension Scheme was concerned, it was undoubtedly an inconvenient liability, as it made Silentnight unattractive to third party lenders and unattractive to purchasers. However that did not, in itself, justify making arrangements under which the Pension Scheme transferred to the PPF and relieved Silentnight of its liability. If the circumstances did not justify a transfer to the PPF or a compromise funded by a third party could not be properly achieved, Silentnight had to live with and deal with the liability over a course of time even if it could not do as well as it might without the liability.

71. Furthermore, and there is no evidence that Mr Costley-Wood was aware of all of these matters, there appear to have been tensions between the shareholders and the executive directors (in particular [Silentnight Board Member 1] and [Silentnight Board Member 3]) as the executive directors appear to have viewed the need to raise funds as necessary to ensure an improved future for Silentnight and the shareholders were reluctant to see a dilution of their shareholding, which they did not accept was worthless, whether through a fund raising exercise or as part of an incentive scheme for the executive directors, and were reluctant or unable to subscribe further capital to Silentnight themselves. In addition, there is some evidence that there were tensions between certain of the Trustees and the executive directors with one Trustee suggesting that a proposal put forward by the Trustees to invest in Silentnight in early 2010 had been rejected in part because the executive directors request for a shareholding in Silentnight had been refused.

72. Throughout 2010 and 2011 insofar as Mr Costley-Wood acted on behalf of Silentnight he received instructions from [Silentnight Board Member 1], [Silentnight Board Member 3] and the chairman of the [Silentnight Board], [Silentnight Board Member 2]. These persons had ostensible authority to give Mr Costley-Wood (and KPMG) instructions except between 31 January 2011 and 4 February 2011 when Mr Costley-

Wood attended a board meeting when the [Silentnight Board] resolved that KPMG be stood down for a period.

HIG

73. HIG is a private equity group owned and controlled by [HIG Board Member 1] and [HIG Board Member 2]. It consisted of the following companies and corporations collectively referred to as HIG save where a differentiation is required:
- 73.1. HIG Capital LLC (“HIG Capital”), incorporated in Delaware, by [HIG Board Member 1] and [HIG Board Member 2] in 50 percent shares.
 - 73.2. HIG Partners, an English LLP;
 - 73.3. Grace Bay II Holdings SARL (“Grace Bay”), a company incorporated in Luxembourg. This was wholly owned by HIG GP II, which was also incorporated in Delaware and owned in 50 percent shares by [HIG Board Member 1] and [HIG Board Member 2];
 - 73.4. HIG Luxembourg Holdings Fifteen SARL (“HIG Luxembourg”). This was a company incorporated in Luxembourg and wholly owned by HIG GP II;
 - 73.5. HIG Bayside Debt & LBO Fund II (“Bayside”), a Delaware Limited Partnership;
 - 73.6. HIG Snooze Newco Limited, (“HIG Snooze”) an English company incorporated on 10 February 2011. HIG Snooze was wholly owned by HIG Luxembourg.
74. The two people from the HIG Group who had the most day-to-day involvement in the events from which these proceedings arose were [HIG Senior Management 2], who was a director of HIG Capital, and [HIG Senior Management 3], who was a director of Bayside. [HIG Board Member 2] was the ultimate decision maker as to whether the investment in Silentnight went ahead. They had little or no experience of English insolvency law and in particular of CVAs or administrations.

[Bank 1]

75. [Bank 1] (“the Bank”) were the bankers to Silentnight prior to the debt being sold to HIG in January 2011. [Bank 1 Trading brand] is a trading brand of [Bank 1]. It was, at the time, owned by [Bank 1’s parent].
76. Silentnight had been under the responsibility of the SBS division within [Bank 1] since 2004. The relationship with Silentnight at the Bank was managed by [Bank 1 Senior Management 1] and [Bank 1 Senior Management 2].

The Pension Protection Fund (“the PPF”)

77. The PPF is a statutory body under the 2004 Act, which in certain circumstances assumes responsibility for pension schemes in order to protect the interests of members. It is funded by a levy on all companies operating defined benefit pensions schemes, recoveries from employers of insolvent schemes that the PPF takes over and

investment income. One of the circumstances in which the PPF will assume responsibility for a scheme is if the company to which a defined benefit pension scheme is attached suffers an insolvency event (e.g. enters into administration). If a scheme enters the PPF, certain of the members receive less than their full pension entitlement.

78. Aside from entry into a formal insolvency procedure, the PPF might agree to take on a pension scheme as part of a rescue or restructuring transaction. The circumstances in which the PPF would agree to such an approach were set out in guidance issued by the PPF. The PPF Guidance stated in 2010:

“In certain circumstances, it is possible for the Pension Protection Fund to participate in the restructuring or rescue of an insolvent business. This can mean the defined benefit pension scheme is much better off than it would have been if the business was simply left to fail. This always involves removing or compromising the pension debt from the company. A simple example of this would be a company which would have a positive cash flow and make a profit if the pension scheme was removed. In such instances, someone may be prepared to pay the scheme money to make sure that party keeps or acquires that earning capacity.”.

79. On the face of it, engaging in such discussions is contrary to one of the purposes of the 2004 Act, namely to stop employers ‘dumping’ their pension scheme. Therefore, the PPF would only participate in pension compromises where certain conditions were satisfied, three of which are particularly relevant to these proceedings.

80. First, insolvency must be inevitable (i.e the PPF would get the pension scheme debt whatever happened):

80.1. Insolvency in this context means “entry into a formal insolvency procedure”. It is not a question of whether a company is technically balance sheet or cash flow insolvent under the Insolvency Act 1986, which are obviously not insolvency events. [A restructuring adviser at the PPF] [redacted], explained in his evidence that inevitable insolvency, in the sense of the guidance, meant that the employer would suffer an insolvency event but for the PPF taking on the pension scheme as part of a pension compromise.

80.2. The PPF guidance did not define what “inevitable” meant. The Executive Counsel relied upon its ordinary meaning (as does Mr Murphy), i.e. something which is certain to happen and cannot be prevented. Mr Costley-Wood’s understanding at the time was that the insolvency had to be “real and imminent” albeit both he and Mr Murphy had experience of the PPF accepting an insolvency as being inevitable when it was more than one year away. This essentially accords with Mr Murphy’s view of what was required. Mr Murphy’s opinion is that “it is likely to be much easier to persuade the PPF that insolvency is inevitable if it is also imminent”. Mr Murphy used the term “burning platform” “as shorthand to describe the position where insolvency is demonstrably inevitable, and that a

formal insolvency procedure is also imminent”. That terminology was also used by Mr. Costley-Wood in substantially the same sense. Any relaxation of the approach to “inevitability” would open up opportunities for dumping pension schemes on the PPF, at the expense of pension scheme members and the levy payers, when alternatives had not been properly explored. It could also clash with tPR’s duty to seek contributions from qualifying people who have caused material detriment to a pension scheme if tPR cleared the transaction.

- 80.3. Secondly, the PPF would be given 10 percent of the equity where the future shareholders are not “currently involved” in the company and 33 percent if the parties are currently involved. The concept of “currently involved” in the PPF guidance is relevant to Allegation 3, and is addressed in more detail below. The PPF does not provide a precise definition of the term. [A restructuring adviser at the PPF] in his evidence used the phrase “in its common parlance sense to allow it to look at all relevant circumstances before agreeing to restructuring transaction”.
- 80.4. Thirdly, tPR was prepared to clear the transaction. If tPR does so, tPR loses the ability to bring contribution proceedings against qualifying persons who may have been responsible for the company’s inability to fulfil its obligations to the scheme members. This is an important consideration when considering Allegations 2 and 3, since tPR cannot make an informed decision as to whether or not to approve the deal if it is misled or if the relevant facts are not disclosed to it. It was in HIG’s interests to agree a deal in order to avoid later being a target of a tPR Warning Notice of intention to seek a contribution.
81. A solvent compromise or Regulated Apportionment Arrangement (“RAA”) would involve a transaction under which a pension scheme is transferred to a specifically created new company (often referred to as “Newco”) that is then placed into insolvency. The scheme thereby passes into the PPF. The original company itself does not undergo any insolvency process or the consequences that attach to such process often called “solvent compromise” or PPF compromise. As mentioned, RAAs are reached via agreement with PPF and tPR. The trustees, whose members will be affected by an RAA and the loss of benefits that result, will also be involved. Compromises which were done as part of a RAA are often referred to as a “PPF compromise.”.
82. Where a solvent compromise is not possible, a company voluntary arrangement (“CVA”) under Part 1 of the Insolvency Act 1986 may allow an insolvent company to agree with its creditors to only pay a proportion of its debts over a period of time in order to avoid entry into administration or liquidation. It must be approved by 75 percent (in value) of creditors. Where pension fund trustees represent more than 75 percent in value of a company’s creditors, as the Trustees did in the case of Silentnight, they, in effect, have a veto over the approval of a CVA. In an insolvency the liability to a scheme is assessed by reference to the section 75 liability, i.e. in the

case of Silentnight, approximately £100 million in 2010/2011. In the event that a CVA fails on the grounds that it is not acceptable to the creditors, a company will generally be placed in administration. The PPF will have no option but to accept the pension scheme and tPR may have to resort to tPR's moral hazard powers if tPR considers that the administration was intended to "dump" the pension scheme.

The Pension Regulator (TPR)

83. [redacted] TPR has "moral hazard" powers by which it can bring proceedings in order to seek a contribution to pension schemes that have entered the PPF. A general understanding of these powers is necessary for an assessment of the statements made to tPR and others, which are the basis of Allegations 2 and 3. One of the main objectives of tPR in exercising its functions is to reduce the risk of situations arising which may lead to a pension scheme being unnecessarily transferred to the PPF.
84. The power to seek a contribution to a pension scheme is vested in tPR under s.38 of the Pension Acts 2004 ("the 2004 Act"). That power may be exercised if tPR considers that a scheme has suffered a "material detriment" under s.38(5) of the 2004 Act. "Material detriment" is defined in s.38A(1) of the 2004 Act as:
- "For the purposes of section 38 the material detriment test is met in relation to an act or failure if the Regulator is of the opinion that the act or failure has detrimentally affected in a material way the likelihood of accrued scheme benefits being received (whether the benefits are to be received as benefits under the scheme or otherwise)."
85. The power may also be exercised if tPR considers that the main purpose or one of the main purposes of the relevant act or failure to act was to prevent recovery of the whole or any part of the debt which was, or might, become due from the employer in relation to the pension scheme under section 75 of the 2004 Act (s.38(5)(a)).
86. In the case of an employer with an underfunded pension scheme, an insolvency process is likely to lead to material detriment, and to prevent recovery of the whole of or part of any debt that might become due under section 75.
87. The exercise of tPR's powers is subject to the following further conditions:
- 87.1. The powers can only be exercised against a "Target". A Target is defined in s.38(3)(a) of the 2004 Act as a natural or legal person who was party to, or knowingly assisted, an act or deliberate failure to act that caused the material detriment.
- 87.2. The act must have taken place in the previous six years: s.38(5)(c).
- 87.3. The Target must also have been the employer or connected to or associated with the employer: s.38(3)(b). Insolvency practitioners are excluded from being potential targets: s.38(11).
- 87.4. It must in all the circumstances be reasonable to require the Target(s) to pay the sum specified in any contribution notice to the pensions scheme: s.38(3)(d).

88. The power is lost if tPR agrees or provides clearance for the solvent compromise or CVA.

Other proceedings related to the events at Silentnight in 2010/2011

TPR Proceedings

89. The EC's investigation was opened on 13 October 2015 following a referral from tPR regarding the Respondents' conduct.

90. TPR had launched its own investigation into the demise of Silentnight and, specifically, whether HIG and three of its officers, [HIG Senior Management 2], [HIG Senior Management 3] and [HIG Board Member 2] (together "the Targets") were liable to make a contribution to the former Silentnight Pension Scheme under s.38 of the 2004 Act. Neither Mr Costley-Wood nor KPMG is a target of tPR Proceedings (and could not be under the relevant statutory framework).

91. TPR issued a warning notice on 11 December 2014 ("the First Warning Notice"), warning the Targets of its intention to seek a contribution notice against them in the amount of about £17.16 million. The basis for that contribution notice was that the group's business and assets had allegedly been sold at an undervalue with a resulting loss to the Pension Scheme of about £17.16m. That sale was conducted by Mr Costley-Wood, as administrator. It relates principally to the pre-pack administration sale of Silentnight, with which these proceedings are not directly concerned.

92. On 22 June 2016, tPR issued a second warning notice ("the Second Warning Notice"). The Second Warning Notice was issued on the basis that Silentnight need not have entered an insolvency process at all: Silentnight could have remained solvent throughout the relevant period and supported the Pension Scheme. In short, tPR alleges that were it not for the "unreasonable conduct" of HIG in relation to the acquisition of the Silentnight debt with a view to forcing an insolvency process and passing the Pension Scheme onto the PPF, Silentnight would not have entered administration, the Pension Scheme would not have entered the PPF and Silentnight would have discharged its obligations to the Pension Scheme over the long term.

93. In tPR's proceedings, tPR also relied upon [a section] of the 2004 Act, which make it an offence to provide misleading information to the regulator in certain circumstances. TPR alleges that HIG provided misleading information as to circumstances surrounding the Bank's withdrawal of the Overdraft. That allegation arises out of the same facts that form the basis of Allegation 2 in these proceedings.

94. On 2 March 2021 tPR published the Regulatory Intervention Report ("RIR"). The RIR described the grounds of the contribution notices issued by tPR and described tPR case. It then recorded that both contribution claims had been settled by HIG

agreeing to pay £25 million which, with the proceeds from the administration of £10 million, resulted in the Pension Scheme receiving £35 million.

95. The RIR was published by tPR pursuant to its powers under section 89 of the 2004 Act which provides that tPR might “if it considers it appropriate to do so in any particular case, publish a report of the consideration given by it to the exercise of its functions in relation to that case and the results of the consideration.”. The report may be published in such form and manner as tPR considers appropriate. TPR’s guidance states that section 89 provided tPR with the power to publish information on cases where tPR had exercised or considered exercising its powers and that the publication might include information which tPR had obtained in the course of its statutory function.
96. The Executive Counsel relies on paragraph 16 (4) (vi) of the 2021 Scheme which provides that any finding of fact in a report or proceedings which in the opinion of the Tribunal corresponds to any report or proceedings referred to in paragraphs 16 (4) (i) to (v) of the 2021 Scheme shall be prima facie evidence of the facts found. In our opinion the description of facts in the RIR are not “findings of fact” which implies that the facts are contained in a report prepared by an independent fact finding body or person (such as the Determinations Panel) which corresponds to the report or proceedings referred to in paragraph 15 (4) (i) to (v) of the 2021 Scheme. TPR’s report does not so correspond. A transitional provision has been inserted into the latest version of the Scheme to ensure it continues to apply to insolvency matters where an investigation has been commenced prior to 1 January 2021.
97. Accordingly the Tribunal does not consider that any matters described in the RIR should be treated as prima facie evidence of the facts described insofar as the facts amount to recital of the facts put forward to support the Allegations.

The ICAEW’s Investigation

98. We note that the ICAEW has also launched an investigation into the Respondents’ conduct. That investigation concerns their conduct in relation to (i) their engagement on 1 April 2011 to advise on and plan for a possible CVA and for the administration of Silentnight and a sale of its business in the event that a CVA failed and (ii) Mr Costley-Wood’s appointment on 7 May 2011 as an administrator. The ICAEW’s investigation has been stayed pending the outcome of these proceedings.

The history of Silentnight’s attempts to deal with its debt and liabilities

Silentnight’s relationship with the Bank

99. Silentnight’s relationship with the Bank began in 2003 when Silentnight was in need of additional finance as a result of two unsuccessful acquisitions in the late 1990’s and went through a “take private” restructuring in which the Bank lent some £39 million. By 2004 Silentnight had been placed under the responsibility of the SBS

division within [Bank 1] which had the responsibility of monitoring underperforming borrowers. It remained under SBS division within [Bank 1] supervision until HIG acquired the Silentnight Debt in January 2011. Normally a company would be expected to remain under the responsibility of the SBS division within [Bank 1] for a period of one to two years. Silentnight remained under supervision until the Bank sold the Silentnight Debt in January 2011.

100. By late 2005 the Bank made it a condition of further support that Silentnight attract additional investment and discussions were held by Silentnight with a number of private equity houses and [Supplier A] which supplied Silentnight with beds. [Supplier A] made a formal offer in 2006 which was accepted but then reduced by [Supplier A] after it had carried out due diligence. The reduced offer was not acceptable to the shareholders.
101. In 2006 Silentnight was still making losses and had to refinance with the Bank (no other funder being available) which imposed stringent terms in an agreement entered into on 24 November 2006 (“the Term Loan”). Under the Term Loan Silentnight borrowed £26 million which it agreed to apply to reduce the Silentnight’s Group overdraft with the Bank. The Term Loan imposed stringent terms on Silentnight; it was subject to a Pre-payment Fee and an Exit Fee. Both were intended by the Bank to induce Silentnight to repay the Silentnight Debt as quickly as possible. The Exit Fee had to be paid in certain events including a flotation, change of control, a sale of all or substantially all the assets of the group, or the sale of all or any shares in the Obligor, which expression included Silentnight Group Limited, save where permission was given for the sale: clause 13.4 of the Term loan. The Exit Fee increased annually and was £2,500,000 if the relevant event occurred prior to 31 January 2010 but after 31 January 2010 was £5,000,000 if it occurred prior to or on including the Final Repayment Date, i.e., 30 November 2011. The Prepayment Fee had to be paid if the Term loan was repaid early in circumstances other than one attracting the Exit Fee and increased over the period from £1m (for the period to 31 January 2008) to £2.5 million if the Term Loan was repaid after 31 January 2009 but prior to 30 November 2011. The structure of the Term loan was intended to reflect the “equity risk” which the Bank considered it was taking in agreeing to the Term Loan which was beyond the Bank’s normal lending parameters.
102. In addition a management fee of £100,000 had to be paid to the Bank on each of the 30 November 2007 to 2010 in addition to an arrangement fee of £150,000 payable on draw down: clause 13.1 and 13.2. Interest was payable on the Term Loan at 2.25 percent above LIBOR: clause 10 of the Term Loan.
103. All the monies due under the Term Loan became immediately payable in the event of a failure to pay monies on the due date under any other Facility Agreement: clause 23 of the Term Loan. The expression Facility Agreement included the agreement providing for the overdraft facility.

104. Any monies prepaid could not be reborrowed: clause 9.5.
105. The bank was free to assign its rights under the Term Loans to any other financial institution or investor in loans: clause 24.
106. The Term Loan included other onerous obligations inserted to protect the Bank's interests by ensuring it could closely monitor the performance of Silentnight and its management. It provided for repayment of the Term Loan in instalments starting at £500,000 in 2007 rising to £750,000 from February 2008 and mandatory prepayment on disposal of any asset, undertaking or business (all of which were subject to the Bank's first charge security). It included standard and enhanced financial covenants. In early 2008 Silentnight asked the Bank to consider altering the Exit Fee (which was not altered). In late 2009 the Bank agreed to accept reduced loan repayments during 2010. [Bank 1 Senior Management 1] said in evidence the Bank had considered it had no option but to continue its support Silentnight with a view to exiting the relationship.
107. On 9 November 2007 [Bank 1 Senior Management 2] an Associate Director of the Bank informed [Silentnight Board Member 1] that the Bank was not anticipating lending any more monies for the foreseeable future and if Silentnight wished to expand or restructure it would be well advised to look to another bank for financing. [Silentnight Board Member 1] informed him that Silentnight had contacted two other banks in order to find alternative financing so that the Bank could be repaid swiftly and the Exit Fee avoided. [Bank 1 Senior Management 2] understood that the alternative financing would be obtained in 2008. In February 2008 the Bank agreed to loosen the financial covenants in the Term Loan as otherwise Silentnight would have been in breach of them. The Bank was prepared to do so as it had a cross default clause in the Term Loan and it was likely that Silentnight would have exceeded the permitted overdraft limit which would have enabled the Bank to rely on the cross default clause in the Term Loan.
108. In December 2009 the Bank rejected an offer from [Private equity firm 1], introduced by [Private equity firm 2], to buy the Silentnight Debt. The offer was rejected because the Bank considered it did not compensate it for the Pre-payment Fee or the Exit Fee under the Term Loan. The concept as explained to the Bank was that [Private equity firm 1] would acquire the Silentnight Debt and place Silentnight into administration and sell its business by way of a pre-pack sale, and restructure the balance sheet which would no longer reflect the Pension Scheme liability; that would be transferred to the PPF. The Bank recorded that Silentnight's management viewed the proposal favourably and would be offered equity in the acquiring company. The Bank had been offered 90 pence in the pound for the Silentnight Debt. The Bank responded by stating that at a minimum it would require the Silentnight Debt to be purchased at par plus compensation for the accrued Exit Fee. By 11 April 2010

[Private equity firm 1]had increased its offer to par but did not cover the Exit Fee. [Bank 1 Senior Management 2]considered that it was unlikely that Silentnight could refinance with another bank. The Bank's internal note recorded that the Bank faced a reputational risk in the proposed transaction but also noted the risk to the Bank if they did not proceed if management, for which they had a high regard, left the business which could result in a deterioration of Silentnight's business and the ability of Silentnight to service the Silentnight Debt. The internal note made no reference to informing Silentnight's shareholders or management of the offer.

109. By late 2010, Silentnight had reduced the amount outstanding under the Term Loan to £3.7m (from £26 million) and the Bank was supportive of Silentnight's management. Silentnight achieved the reduction in the Term Loan to £3.7 million by selling off many of its properties.
110. As noted above it was common ground that, absent refinancing or restructuring, Silentnight would not have been able to trade beyond 30 November 2011 when its facilities with the Bank were repayable.

The issues raised by the liability to the Pension Scheme.

111. Silentnight had a substantial liability to the Pension Scheme and a history of being unable to maintain its employers' obligation to the Pension Scheme. If the liability remained with Silentnight it made it an unattractive subject of take-over and also hindered Silentnight's attempts to refinance the Silentnight Debt so as to reduce the liability of the Exit Fee. On a PPF basis the liability had grown from £39.5 million (as at 1 December 2008) to £53.6 million as at 1 December 2009.
112. A ten-year recovery plan agreed between the Trustees and Silentnight in 2005 was modified in February 2009 because the company could not afford the agreed contributions (of £1.2m per year). In February 2010, the company set about renegotiating the modified payment schedule.
113. The Trustees and Silentnight failed to put a new recovery plan in place by 28 February 2010 (the statutory deadline for submission to tPR) and negotiations between the Trustees and Silentnight lasted many months. On 25 June 2010, the 2010 Deficit Recovery Plan was eventually agreed between the Trustees and the Scheme, and submitted to tPR for its review. There were a number of respects in which the Deficit Recovery Plan might have attracted tPR's interest. For example, it provided for Silentnight to repair the deficit over a 30-year period; this was significantly longer than the usual period of 10 years. It was "back end loaded" and provided for contributions to escalate over time.
114. During the negotiations for the 2010 Deficit Repair Plan, Silentnight acknowledged that it might not be able to afford the proposed contributions, but made its proposals on the basis that the 30-year recovery plan would in any case be reviewed again in a

further three years. [Silentnight Board Member 1] regarded the 2010 Deficit Recovery Plan “as a holding plan pending the expiry of Silentnight’s banking arrangements in November 2011.”.

115. The view of [Silentnight Board], the Trustees, and Mr Costley-Wood (in evidence) was that the 2010 Deficit Recovery Plan was open to challenge by tPR who might have insisted on a shorter schedule with higher contributions. That was not wholly consistent with the evidence of [Senior Advisor at tPR] whose statement was partially relied on by the Executive Counsel and the Respondents. His evidence was that there is considerable flexibility in calculating a pension scheme’s liabilities and if the calculation reveals a deficit as against a scheme’s assets the trustees must agree a deficit repair plan with the employer. Such a plan will usually provide for a series of payments to be made by the employer hence the expression “deficit repair plan”. The 2004 Act requires that a deficit repair plan must be appropriate having regard to the nature and circumstances of the scheme and must be recorded in a schedule of contributions due from the sponsoring employer and members and is only effective after the scheme actuary has issued the appropriate certificates. After the effective date the recovery plan and schedule of contributions must be sent to tPR within a reasonable period. The documents must include a valuation summary which shows the assumptions adopted by the trustees. The recovery plan does not require approval by tPR and there is no provision in the 2004 Act (s. 231 (2)) for tPR to provide approval albeit there are circumstances in which tPR could make changes to a scheme’s funding arrangements including requiring the trustees to review and revise a scheme recovery plan. The circumstances in which trustees could be required to review a payment recovery plan are closely circumscribed and the power can only be issued by the Determinations Panel – albeit tPR can instigate the use of the section 231 power. The power has been used in only three cases.

116. A funding statement published in 2008 provided guidance as to which deficit repair plans tPR might consider further. There were 10,000 defined benefit schemes and tPR expected the majority of them to be in deficit and require a recovery plan. Accordingly tPR had established some “triggers” to identify those plans which merited further scrutiny. Amongst the triggers were those plans which were longer than 10 years and where the plan was significantly back end loaded (i.e., higher contributions towards the end). The 2010 Deficit Repair Plan satisfied both these criteria which explains why the Trustees at a meeting held on 1 July 2010 noted that tPR might request them to revisit the deficit repair plan agreed with Silentnight and why [Silentnight Board Member 1] informed [KPMG Partner 3] on 6 July 2010 that Silentnight had filed a recovery plan “which is back end loaded and over thirty years - we’re expecting a call”. That email was attached to an email sent to Mr Costley-Wood on 7 July 2010 by [KPMG Partner 3].

Other professional advice

[External Financial Advisor 4] Review of options

117. Silentnight had obtained professional advice on its options prior to the involvement of the Respondents, but had been unable to progress due in part to a failure to agree a way forward by the Shareholders and management.
118. On 16 February 2009, Silentnight engaged [External Financial Advisor 4] to “perform a detailed review of the options for the Company, set against the backdrop of the deteriorating trading conditions facing the Company”. [External Financial Advisor 4]’s engagement letter indicated that its work would be led by [External Financial Advisor 4 Partner 2] and [External Financial Advisor 4 Partner 1].
119. On 31 March 2009, [External Financial Advisor 4 Partner 1]’s team produced the Project Jane Report. [External Financial Advisor 4] considered five options for Silentnight and summarised its “key findings” on each as follows:
- 119.1. Option 1 - Continue as is: “We believe there is currently no equity value in the group and little prospect of being any in the foreseeable future. There is a significant risk that if no pro-active action is taken by the company, deteriorating performance will result in the Bank seeking a restructure or insolvent sale of the business.”. Option 1 was not ruled out but the risk referred to could be avoided if Silentnight took pro-active action.
- 119.2. Option 2 - Sell all or part of the Group: “We do not believe a solvent sale of all or part of the group is possible.”
- 119.3. Option 3 - Refinance or recapitalise: “We do not believe a refinance recapitalisation through external funds is a viable option.” However the Project Jane Report noted that the Bank could sell its debt to a specialist turnaround/restructuring funder. However it predicted this would lead to an insolvent restructuring with potentially poor returns for other stakeholders. The Report considered an AMA (accelerated mergers and acquisition process) to be the Bank’s most likely preferred exit route.
- 119.4. Option 4 - Pension restructure (i.e., an RAA or Scheme only CVA): “This is a possibility but is dependent on the position of the Bank, the ability to find new equity for a restructured business and the view of the PPF.” [External Financial Advisor 4] noted that the position of the Bank and ongoing funding requirements would be critical in ascertaining whether insolvency was inevitable.
- 119.5. Option 5 - Insolvent restructure: “This option has no value for shareholders, however may be the only viable option for business survival and be preferred by the Bank if it is unwilling to increase exposure to the Group and felt there was insufficient time to pursue a restructure of the pension position.”.
120. The Project Jane Report presented a somewhat pessimistic picture of the company’s fortunes. The only two options considered viable by [External Financial Advisor 4] both involved the pension scheme entering the PPF, either by agreement with the Trustees and the PPF in option 4 or by force via a pre-pack administration in option 5. These were described as being the most logical options for Silentnight to consider in the presentation of the Project Jane Report to the [Silentnight Board]. Both options

required external funding. [External Financial Advisor 4]’s emphasis at this time was on option 4. However the Report noted that in an administration [External Financial Advisor 4]’s security analysis estimated a small surplus of around £2 million could be realised above the secured bank debt with the majority of any surplus payable to the Pension Scheme/PPF as the largest unsecured creditor of the group. [External Financial Advisor 4 Partner 1] said in evidence the calculation did not take into account the Exit Fee. The Report noted both of the options had advantages and disadvantages and needed to be considered more closely by Silentnight before any detailed plans to pursue either were made. Furthermore it did not suggest that insolvency was inevitable but there was a significant risk of it if no action was taken.

121. On 16 April 2009, the Project Jane Report was presented to the [Silentnight Board]. The Shareholders did not accept the conclusions of the Project Jane Report, choosing the “continue as is” option, even though [External Financial Advisor 4] had advised it was not realistic. In contrast, the management of Silentnight who had commissioned the report were keen to pursue one of the options [External Financial Advisor 4] considered to be viable. [Silentnight Board Member 1] agreed with [External Financial Advisor 4] that option 4 was the most suitable way forward and took active steps to seek the external funding needed to give effect to it.

122. [External Financial Advisor 4]’s conclusion that the equity in Silentnight had no value was one which the Shareholders had difficulty in accepting. They considered that the business was a family enterprise and should remain one. They were unwilling or unable to invest themselves but were uncooperative with management’s efforts to bring about a restructuring needed to enable the business to expand.

[External Financial Advisor 4] – advice on pension restructuring

123. On 27 January 2010 [External Financial Advisor 4] produced a paper entitled “Alternative to Pensions Restructuring: Hive down and “Invest co’ model” which referred anonymously to Silentnight and proposed a restructuring solution. The proposal was presented to [Silentnight Board Member 1] on 10 March 2010. The plan was to transfer the pension fund out of the Group into a newco freeing Silentnight from the pension liabilities (which would be serviced by an intercompany debt).

124. On 1 June 2010 [External Financial Advisor 4 Partner 1] and [External Financial Advisor 4] were engaged by Silentnight “to assist the group in preparing a proposal for the Pensions Regulator and to present that proposal to the Pensions Regulator once agreed.”.

125. [Silentnight Board Member 3] and [Silentnight Board Member 1] requested [External Financial Advisor 4] to produce “an analysis outlining a number of illustrative investment structuring scenarios” for a restructuring that was assumed to complete on 31 July 2010. On 22 June 2010 [External Financial Advisor 4] produced a report headed “Silentnight Pension Restructuring: Illustrative scenario modelling.”.

[External Financial Advisor 4] advised a funding requirement of £38m. [External Financial Advisor 4] advised “it is unlikely that it would be possible to facilitate a restructuring given the combination of insufficient returns for all shareholders and a lack of headroom in the early years” and stated that “from the Pension Regulator’s clearance perspective it is likely to be unacceptable ...”. [External Financial Advisor 4] also advised “Our view is that it is unlikely this scenario would be acceptable to private equity investors given the low level of returns.” .

126. On 4 August 2010, [External Financial Advisor 4] met with Silentnight and produced a further report and continued to be retained by Silentnight to consider the issue of the liability to the Pension scheme. As late as November 2010, [External Financial Advisor 4 Partner 1] was pursuing his “hive down” model which was inconsistent with insolvency being inevitable.

Silentnight’s other efforts to solve its funding issues.

127. As noted above negotiations for a sale of the business to a supplier of beds, [Supplier A], had reached an advanced stage in 2006, but had ultimately failed after [Supplier A] carried out due diligence and discovered the extent of the pension deficit and the Shareholders had refused to renegotiate.
128. Silentnight also considered a proposal made by the Trustees that the Pension Scheme itself might make a loan to or buy shares in the company to assist in repaying the Term Loan and avoid the full Exit Fee. This idea was raised on 20 October 2009 and pursued by the Trustees in late 2009 and early 2010, with advice from [External Advisor A] (whose high-level paper described the Trustees as a "reluctant investor") and [External Law firm 2] (who advised "extreme caution" in relation to the proposed investment). Some of the key restrictions were that the Trustees could not invest more than 5 percent of the value of the Scheme's resources into the Silentnight business (effectively limiting the investment to £5m) and the requirement to adjust the investment depending on the value of all the Pension Scheme’s investments. Furthermore, the Trustees could not lend money to Silentnight, limiting the investment to some form of share purchase such as preference shares, and any investment needed to provide an appropriate investment return (in the region of 6-12 percent). On 25 February 2010, [Silentnight Board Member 1] told the Trustees to suspend any further work on their proposal until the summer of 2011 during which he indicated he proposed to negotiate with the Bank in relation to the Term Loan and Exit Fee and their restructure. [Silentnight Board Member 1] apparently concluded that the Trustees' proposal was "not a realistic option".
129. The management of Silentnight had approached and kept in touch with a number of banks in late 2009 and through to June 2010 to ascertain if they might take over from the Bank as lender. None were willing to fund Silentnight. In an internal memo written on 22 April 2010 the Bank itself noted that Silentnight would find it "difficult to refinance with another bank" given the state of Silentnight’s balance sheet.

130. Towards the end of 2009 Silentnight sought advice from other professionals including Mr Costley-Wood. His first formal introduction to Silentnight occurred when he attended a meeting with [Silentnight Board Member 1] on 18 December 2009 at which [Silentnight Board Member 1] expressed a wish to be advised on Silentnight's options in the light of Silentnight's financial state which Mr Costley-Wood understood was not sound. On 18 January 2010, Mr Costley-Wood sent a short presentation (which was a tender to provide advice) summarising his understanding of Silentnight's financial position, three potential restructuring options and a description of KPMG's credentials. The 18 January presentation noted that KPMG had a detailed understanding of the Pension Scheme, as KPMG had worked with the Silentnight Group for a number of years, and KPMG's multi-disciplinary team had a good understanding of Silentnight's business. The 18 January presentation referred to the Term Loan the Exit Fee and the Pension Scheme deficit described as being in deficit by £45 million. It noted there was little prospect of Silentnight generating sufficient cash to meet its responsibilities in full and that Silentnight needed a solution to avoid a further bank ratchet (i.e., an increased Exit Fee), mitigate the pension issue, satisfy shareholder demands and take the business and brand forward. Mr Costley-Wood noted that the shareholders had already been presented with an appraisal of options and recommended that Silentnight should seek an independent appraisal. The 18 January presentation described three available options: (i) Fund raising which might produce sufficient funds to enable a compromise with all stakeholders (through a CVA) including a sales process to test the market, (ii) a compromise with the Trustees which increased the funding above the PPF level but severed the Pension Scheme ties to Silentnight; Mr Costley-Wood's view was that, in the light of the deficit, that would require additional funding and (iii) a PPF compromise (i.e., a solvent compromise or RAA); that was likely to involve the PPF taking a stake in Silentnight and to assist the compromise there was a need "to demonstrate that an insolvency of the business is inevitable if no action is taken". KPMG noted that it had recent experience of PPF compromises for various companies and believed "this could be a viable option for the Group subject to creating a real "burning platform". In the adjacent column of the presentation under the heading "considerations" the presentation provided that to assist negotiations with the PPF there was a need to demonstrate that an insolvency of Silentnight was inevitable if no action was taken. Mr Costley-Wood in evidence said the reference to the expression "creating" was an error and it should have read with the expression "demonstrating". He was well aware of the pitfall with tPR of artificially creating a burning platform.

131. The management of Silentnight also had meetings with various private equity funders, and with a private equity broker, [Private equity firm 2] which had introduced [Private equity firm 1] (which was, in parallel, in private talks with the Bank to broker an acquisition of the Silentnight Debt). [Silentnight Board Member 1] positively encouraged the interest of such parties, meeting with them and providing financial

information to assist their consideration of a possible investment, understanding that a "loan to own" strategy would be in contemplation.

132. After the Bank rejected the offer from [Private equity firm 1], [Private equity firm 2] continued to remain involved, carrying out its own detailed investment appraisal (in about May 2010) (which noted management unease regarding insolvency and noted that the pension liability was growing and "getting closer"). However it concluded that the business was attractive if sold "free of legacy issues" which referred to the liability to the Pension Scheme. It also noted that the Bank wanted to end the relationship with Silentnight but was concerned with reputational issues. [Private equity firm 2] commissioned legal advice on securities from [External Law firm 3], financial modelling from corporate financial advisers [External Financial Advisor 1] and tax structuring and pensions advice from [External Financial Advisor 2], which advice was shared with HIG in May 2010. [Private equity firm 2] also sought insolvency advice from [External Financial Advisor 3] and proposed on 21 June 2010 that [External Financial Advisor 3] should ultimately be engaged as administrator.
133. On 11 May 2010, [Silentnight Board Member 1] had an update call with Mr Costley-Wood and sent KPMG's Silentnight's latest annual accounts for the 12 months ending 31 January 2010 noting that the statutory accounts showed "Silentnight remaining profitable and generating substantial cash through management actions.". Mr Costley-Wood said in evidence that he understood that [Silentnight Board Member 1] was emphasising the strength of Silentnight's senior management team and Silentnight's ability to generate cash as a factor to pass onto potential purchasers or investors and although [Silentnight Board Member 1] sounded upbeat about Silentnight's financial performance he continued to pursue a solution to what he held out to be Silentnight's financial problems vigorously. Mr Costley-Wood accepted that the accounts were accurate.
134. With [Silentnight Board Member 1]'s consent, on Silentnight's behalf, Mr Costley-Wood approached his contacts at two private equity funds, namely [Private Equity Firm 3] (with whom he had dealt with previously) and [Private Equity Firm 4] which he knew had experience of solvent pension restructuring. In his high level discussions with [Private Equity Firm 3 Employee 1] it became clear that [Private Equity Firm 3] was only interested in a "loan to own" strategy. Subsequently on 20 May 2010 Mr Costley-Wood forwarded Silentnight's account to [Private Equity Firm 3].
135. [Private equity firm 2] (as broker) effected the introduction of [HIG Senior Management 2] to [Silentnight Board Member 1] on 17 May 2010. [Silentnight Board Member 1] was impressed by [HIG Senior Management 2] and provided HIG with a number of documents including three year plan summaries and a PowerPoint presentation setting out Silentnight's financial position.

136. HIG prepared an Early Stage Opportunity Review in May 2010 (which was an internal document) which noted amongst other matters that that (i) [Private equity firm 2] had negotiated a pre-arranged deal with the Bank and Management, (ii) the Bank was willing to sell the Silentnight Debt at par with an additional Exit Fee of £2.5 million, (iii) the existing shareholders were in agreement with the deal terms, (iv) the key issue was the pension liability which had a deficit of £17 million on a FRS17 basis or assumed capital buy out cost of £70 million and (v) the equity was effectively worthless. The document also envisaged the equity structure on an acquisition as HIG 75 percent, [Private equity firm 2], 3 percent and existing management 22 percent. A revised Early Stage Opportunity Review Update prepared in June stated that the acquisition of Silentnight's business would be "out of administration" and that the Pension Scheme would pass to the PPF and HIG envisaged an investment return of £45 million. The terms of the update suggest that HIG was receiving expert advice as to the restructuring – presumably from [External Financial Advisor 3]. [Private equity firm 2] did not share its detailed proposals with [Silentnight Board Member 1] until 18 June 2010 but by 7 June 2010 HIG was confident that it had the support of [Silentnight Board Member 1] and the senior management of Silentnight. [Silentnight Board Member 1] preferred to avoid an administration and wanted Silentnight to proceed by way of a CVA.

Silentnight's financial position at the end of July 2010

Burning platform

137. In his evidence Mr Costley-Wood suggested that in August 2010 Silentnight faced a number of "burning platforms" by which we understand him to say that it faced more than one liability which would cause imminent insolvency in the sense described above. The three causes of a burning platform he described were the liability under the Deficit Repair Plan, the Exit fee of £5 million due on 30 November 2011, and the cancellation of the overdraft or other facilities replacing it in the event that HIG acquired the Silentnight Debt.

138. As noted above a Deficit Repair Plan had been agreed on 25 June 2010. It had been agreed by the Trustees to assist Silentnight, in part, to enable Silentnight to repay the Term Loan and pay the Exit Fee due on 30 November 2011. The 2010 Deficit Repair Plan had just been agreed and one presumes that Silentnight would not have agreed a payment plan which it could not meet in the immediate future. Silentnight was in fact making about £4 million profit per year so the amount was affordable. Secondly, as [Silentnight Board Member 1] noted at the time, Silentnight would have the opportunity to renegotiate the plan in the event it became unaffordable. Thirdly, the plan did not require the approval of tPR who could challenge it under his powers which were rarely used, and fourthly, as tPR recorded in a statement published in September 2008, tPR would have full regard to the employing company's viability, including its ability to fund the scheme and its long term health. "Our position is that the best means of delivering the members' benefits is usually for the scheme to have

the continued support of a viable employer.”. There is no contemporary evidence that the Trustees and Silentnight expected it to be challenged as opposed to tPR raising some questions about it, and it is unlikely that if tPR had considered some terms needed to be changed, tPR would have required terms to be changed such as to render Silentnight insolvent.

139. TPR’s publications on scheme funding emphasised that scheme funding should be determined by what is reasonable to the employer and Mr Shaw agreed in cross examination that tPR and PPF would have been reluctant to cause an insolvency. [TPR Employee 1] considered that the plan was consistent with what was affordable considering the precarious position that Silentnight was in. On 21 February 2011 tPR’s internal actuarial advisor, [tPR Employee 2], considered the 30 year recovery plan and noted that an insolvency/avoidance case had by then been raised, no doubt as a result of the acquisition of the Silentnight Debt. He noted that the 2010 Deficit Repair Plan met many of the warning signs of a weak employer, vulnerable with high likelihood of financial distress but the recovery plan seemed affordable but required monitoring. He noted that the recovery plan was 30 years long and significantly back end loaded, with a weak employer (therefore plenty of warning signs). “This effectively strips most if not all the prudence from the funding strategy and seems inappropriate for a weak employer.”. The note ended with a suggestion of a conference call as there were strong concerns over the Trustees approach and suggested a number of matters which required exploration including the risks associated with a 30 year recovery plan. However, even at that stage, it does not appear that tPR would have taken steps which would have led to the insolvency of Silentnight.

140. In cross examination Mr Costley-Wood admitted that he could not recall seeing the 2010 Deficit Repair Plan or the schedule of contributions set out in it or the Trustees email to tPR explaining the basis of the agreement. There is no contemporary document showing that Mr Costley–Wood considered the 2010 Deficit Repair Plan or the prospects of it being challenged. It was not put to the PPF or tPR in March or April as a reason for Silentnight facing a burning platform. That was always attributed to the Bank cancelling the overdraft.

141. Furthermore, the Trustees were prepared to support Silentnight so that it could continue trading and to that end were prepared to invest in Silentnight so that it could prepay the Term Loan and thus save £2.5 million of the £5 million Exit Fee. They had discussed investing in Silentnight on 20 March 2009 and took advice from [External Advisor A] and [External Law firm 2] on a number of occasions thereafter. On 25 February 2010 they were “stood down” by [Silentnight Board Member 1] who informed them that Silentnight hoped to pay off the Term Loan by accumulating cash. The Trustees held a meeting on 1 July 2010. [Silentnight Board Member 1]attended to deal with certain items – particularly the Silentnight covenant - on the agenda for the meeting. The chairman of the Trustees [Silentnight Pension Scheme] asked

[Silentnight Board Member 1] to ensure that the trustees continued to receive regular updates with regard to the banking position as the Trustees were concerned about the Exit Fee, how it was to be financed, and that steps be taken to minimise the £5 million due on 30 November 2011.

142. On 20 November 2010 [Trustee 2] emailed [Silentnight Board Member 1] to the effect that he remained keen for Silentnight to repay the Term Loan “even if that means you will call on the Pension Scheme funds in the short term”. On 22 November 2010 the chairman of the Trustees [Silentnight Pension Scheme] wrote to [Silentnight Board Member 1] asking to see what progress was being made in relation to the payment of Silentnight debt due on 30 November 2011. He mentioned that the Pension Scheme would be holding cash of nearly £4 million in early 2011 and that the Trustees needed to know what the position was as the 2010 Debt Recovery Plan had been predicated on Silentnight’s requirements to apply monies to service its obligations to the Bank. [Silentnight Board Member 1] replied (when he was well advanced in discussions with HIG) that his strategy was to try to renegotiate financing with the Bank after the 31 January 2011 accounts had been prepared, and asked the Trustees to maintain investment flexibility with the Pension Scheme funds in case they were required in the Spring or Summer of 2011. After HIG acquired the Silentnight debt and it became apparent that HIG would not provide sufficient funds to fund a PPF compromise the Trustees once again considered with advisers the possibility of investing in Silentnight including acquiring the Silentnight brands so that HIG would not be a creditor. The latter proposal was unacceptable to tPR as it involved too high a level of risk. The Trustees’ actions demonstrate that the Trustees would be very reluctant to take any steps to force Silentnight into insolvency and were supportive of Silentnight.

143. The contemporary documentation created in the period before 13 January 2011 contains no indication that there was, or that Silentnight, Mr Costley-Wood or HIG considered that there was a burning platform created by the Term Loan, the Exit Fee or Pension Deficit Plan:

143.1. When the Project Jane Report was shown to the Bank it informed Silentnight’s management that the Bank would not be looking to put Silentnight into insolvency due to the reputational risk to the Bank. Further the Bank told management that it would not instigate insolvency proceedings for the purpose of a pensions restructure. On 26 May 2010 in a briefing note for [External Financial Advisor 4] the understanding of [Silentnight Board Member 3] and [Silentnight Board Member 1] was that the Bank had informed them that it would refinance the Term Loan which they passed onto [External Financial Advisor 4] who were advising on a Pension Scheme Restructure. The Bank was described as “[H]appy to extend arrangements and remain our Bank”;

- 143.2. The Bank’s relationship overview also noted that Silentnight’s management were currently exploring refinancing options with other institutions to limit the prepayment fee. In the event that the Bank needed to refinance Silentnight at maturity of the Term Loan “we would have to refinance the fee ourselves”;
- 143.3. [Silentnight Board Member 1] was issuing optimistic reports as to Silentnight performance. A trading update issued on 25 February 2010 by [Silentnight Board Member 1] noted that both trading profit and cash flow were above budget and he informed Mr Costley-Wood on 11 May 2010 that Silentnight continued to generate a positive outcome and generate cash and that looking forward to 2010/2011 Silentnight was broadly on track to execute budget plans. He also noted that the Bank remained supportive of Silentnight and respected Silentnight’s management;
- 143.4. The meeting of 16 August 2010 proceeded on the premise that Silentnight was insolvent – there appears not to have been an express statement that it was insolvent or that there was a burning platform;
- 143.5. Mr Costley-Wood raised concerns expressed in his email of 16 August 2010 to [KPMG Partner 3] and [KPMG Partner 5] to the effect that tPR would raise questions in relation to the burning platform; that suggests that at that time he did not consider that the Exit Fee or 2010 Deficit Repair Plan created a burning platform;
- 143.6. The diffident approach of [External Financial Advisor 3] in their email of 17 August 2010 to the issue of Silentnight’s insolvency which referred to the presumption “that the company could not avoid some sort of insolvency”;
- 143.7. On 20 August 2010 [Silentnight Board Member 1] sent [External Financial Advisor 5 Partner 1] Silentnight’s statutory auditor, Silentnight’s trading update. The report was upbeat and noted that Silentnight continued to enjoy a strong position in its sector, continued to enjoy a supportive relationship with the Bank, and that Silentnight was performing better than it had budgeted and remained on target to deliver the full year profit and cash targets;
- 143.8. [Silentnight Board Member 1]’s draft process note sent to Mr Costley-Wood on 31 August 2010 for his approval noted, in relation to the need to satisfy tPR that an insolvent solution was inevitable, that this could be a difficult hurdle as Silentnight had the support of the Bank and could pay its debts as they fell due;
- 143.9. HIG’s Silentnight update produced in the latter half of September noted that Silentnight “was not a distressed business facing a burning platform. Silentnight is technically insolvent because of a circa £18.5m pension liability” and also noted that the Bank was unwilling to pull the trigger by making a demand and would not facilitate the restructuring themselves;
- 143.10. [HIG Employee 4]’s email of 18 September 2010 noted that HIG would have to turn off some liquidity and use their unwillingness to renew the overdraft as a means of “creating a burning platform.”;
- 143.11. In an email sent by [Bank 1 Senior Management 2] to [Bank 1 Senior Management 1] on 19 October 2010 he noted that given the asset base the Bank was secured in full and that in the event that there was no sale of Silentnight’s Debt

the Exit Fee would crystallise albeit the Bank would have to fund it. [Bank 1 Senior Management 2] noted that Silentnight was servicing its debt “and there is sufficient cover to ensure repayment in a forced sale situation. It is acknowledged that the offer (i.e., the offer from HIG) does allow full recovery of the outstanding debt but my preference would be to try and achieve some upside on our position by either selling at a premium or crystallising the exit fee next year”. Accordingly the Bank considered it was fully secured, and as Mr Murphy stated in evidence, that made it more likely that the Bank would finance the Exit Fee on 30 November 2011. The improvement in Silentnight’s position in relation to the Bank would also have been a factor which the Bank would take into account in deciding whether to extend the overdraft facility which was due to expire on 31 January 2011 and roll over the Exit Fee on 30 November 2011 and, indeed, renew facilities thereafter;

- 143.12. On 20 October and 22 December 2010 [Silentnight’s Board] resolved that Silentnight could continue to trade as a going concern. That is inconsistent with Silentnight facing imminent insolvency;
- 143.13. On 9 November 2010 Silentnight produced its business plan and budget 2011/2012 headed “Preparing for the Upturn”. The summary noted that the UK beds and furniture market would start to recover from the recession later than forecast in the 3 – year plan but Silentnight would continue to focus on delivering a trading profit of £4 to £5 million. All the main retailers were continuing to survive and all Silentnight’s competitors were still “in play” with their improved sale capability starting to impact on Silentnight. Although Silentnight were still budgeting for sales growth, this would be driven by value rather than volume increases;
- 143.14. On 18 November 2010 [Silentnight Board Member 1] sent the most recent external briefing on the group’s performance up to and including the quarter to [External Financial Advisor 5 Partner 1]. The report noted that Silentnight enjoyed a very strong first quarter of 2010/11 followed by a weaker second quarter caused by a significant dip in order intake in early July; the latest forecast for full year sales was £113.7 million, some £(3.5)million worse than originally budgeted and about £(900)k worse than our last forecast at the half-year; the trading profit forecast remains at £4 million equal to budget. Silentnight had beaten all covenants across the year to date. Silentnight was forecast to meet covenants for the balance of the year and the year as a whole and continued to enjoy a supportive relationship with its Bankers;
- 143.15. The Project Bale report produced on 31 January 2011 linked Silentnight’s liquidity crisis to the Debt Sale Agreement and the cancellation of the overdraft facility;
- 143.16. In a note written by [Silentnight Board Member 1] on 1 February 2011 regarding a meeting with the Trustees in respect of the level of payments due from Silentnight to the Pension Scheme [Silentnight Board Member 1] noted in relation to the Exit Fee of £2.5 million or £5 million that there “is some prospect of refinancing in spring/summer 2011 but this is by no means certain.”;

- 143.17. In an internal email sent on 16 May 2011 discussing the reasons why tPR was considering the sale of Silentnight's business and its ramifications for the Pension Scheme Mr Costley-Wood wrote "I'm sure that they will want to review the prepack but I think it is the January debt purchase that they will be most interested in as that created the burning platform";
- 143.18. Mr Costley-Wood cannot have been influenced by anything in the Project Jane Report before 17 January 2011 as he was supplied with it for the first time on that date and that report did not suggest that there was a burning platform;
- 143.19. The Respondents in their Amended Response at paragraph 120.2 admitted that HIG sought to engineer the insolvency of Silentnight but averred that Silentnight was insolvent for other reasons and already faced a threat of entry into an insolvency procedure. [HIG Senior Management 2]'s evidence in tPR proceedings was that he considered a liquidity crisis as "extremely likely", which was inconsistent with HIG's own internal documents such as the Silentnight update referred to above and [HIG Employee 4]'s email of 18 September 2010, but as [HIG Senior Management 2] stated, it was always HIG's intention to use its role as lender ultimately to restrict liquidity and thus bring about a liquidity crisis which it did within two weeks of acquiring the Silentnight Debt.

Silentnight's Solvency, the Term loan and the Exit Fee.

144. The Respondent's relied heavily on [External Financial Advisor 4]'s Project Jane Report prepared on 31 March 2009 to show that Silentnight was in a perilous financial position. However the Report stated that further investigation had to be carried out before a CVA or administration was implemented. It noted in relation to a pension restructure that in determining the issue whether insolvency was inevitable the position of the Bank and ongoing funding requirements would be critical. The report did not rule out carrying on "as is" but indicated there was a significant risk in that approach.
145. The 2010 Deficit Repair Plan was agreed after the Project Jane Report so that its beneficial impact on Silentnight 's cash flow could not be taken into account in the Report.
146. As noted above by late 2010 Silentnight's term loan had been reduced to £3.7 million (albeit at the cost of selling capital assets) from £26 million in 2006. The CID facility of £15 million was being utilised to an average balance of £5 to £7 million and the Bank was considering reducing it to £10 million By late 2010 Silentnight's total indebtedness to the Bank under all its facilities had reduced to about £13 million as opposed to about £25 million at the time of the Project Jane report The Bank recorded in its relationship overview that it was secured by a debenture and that as the bank would be the trigger for any insolvency proceedings it would be able to manage its on demand facilities downwards to minimise to limit the Bank's exposure

at the time of insolvency and considered that its security was such that it should get out in full.

147. The Bank was conscious of the public relations impact on the Bank's reputation if it triggered an insolvency of Silentnight.
148. Until the Debt Sale Agreement the [Silentnight Board] considered that Silentnight was a going concern and had represented to [External Financial Advisor 5] (the auditors) on 27 April 2010 that the financial statements to 31 January 2010 had properly been prepared on a going concern basis and the financial statements were signed by the [Silentnight Board] on that basis. The fact that the overdraft was repayable on demand did not render Silentnight insolvent. Until the Debt Sale Agreement it had the support of the Bank which had confidence in its management. In December 2010 the [Silentnight Board] considered the issue whether Silentnight could pay its debts as they fell due and considered that they could.
149. The experts, Mr Shaw and Mr Murphy were agreed that, absent a refinancing or restructuring of the Term Loan (including the Exit Fee) it was likely that Silentnight could not pay its debts as they fell due on 30 November 2011. However in order to reach the conclusion prior to 13 January 2011 that insolvency was inevitable one had to reach the conclusion that no such a restructuring or refinancing would occur or that tPR would take some drastic action in respect of the 2010 Pension Deficit Plan. Mr Shaw's opinion on cash flow insolvency prior to 13 January 2011 is based on the assumption that the Term Loan and Exit Fee had to be paid on 30 November 2011 and that the £4.4 million free cash flow which Silentnight might generate in the year to 31 January 2012 would be insufficient to meet the £8.7 million (probably £7.7 million as payments would be made in 2011) obligation due on the repayment of the Term Loan and payment of the Exit Fee. However Mr Murphy did not consider that the Bank would not refinance or restructure the Term Loan and Exit Fee. He considered that the contemporary documentation showed that there was a reasonable possibility of the Term Loan and Exit Fee being refinanced or restructured in November 2011 or that he could not be satisfied that it would not be. The material relating to the Bank's attitude to refinancing referred to above suggests that it was highly likely that the Bank would have restructured and refinanced the Term Loan and Exit Fee and contemplated doing so. Furthermore, even absent a restructuring or a refinancing agreement, he did not agree that a formal insolvency procedure was inevitable when considered prior to 13 January 2011 (even if the insolvency occurred after that date) as he considered that a consensual restructuring in respect of the liabilities to the Pension Scheme was an alternative to a formal insolvency procedure. However as Mr Shaw said the time scale in which Silentnight would enter into an insolvency process changed after 13 January 2011 as a result of the purchase of the Silentnight Debt by HIG and the withdrawal of the overdraft facility as HIG was less likely than the Bank to offer overdraft facilities until November 2011. HIG intended to use the threat of the withdrawal of the overdraft facility or revolving credit facility to create and maintain a burning platform, so as to

force through a consensual restructuring, or if this was not possible, through a formal insolvency procedure as it wished to relieve Silentnight or its business of the obligation to the Pension Scheme.

150. In our opinion it was likely that had it been necessary the Bank would have agreed to refinance all or some of the Term Loan or Exit Fee on 30 November 2011 (possibly with some involvement by the Trustees) and entered into a new facility agreement with Silentnight rather than take steps to place it into insolvency. By 30 November 2011 the Term Loan would have been reduced to about £2.2 million as Mr Shaw agreed in evidence. The conclusion that the Bank would probably have financed the balance of the Exit Fee and Term Loan is supported by the Bank's internal documents referred to above. Albeit the Bank had some time previously indicated it wanted to terminate the relationship, Silentnight's indebtedness to the Bank had reduced substantially over a relatively short time and it was trading profitably. The indications in [Bank 1 Senior Management 2]'s email of 19 October 2010 was that the Bank considered the security was sufficient to ensure it was "repaid in full", which we understand to cover the Exit Fee, but we conclude that even if the Bank had some unsecured exposure it would probably have refinanced the Term Loan and the Exit Fee. What the terms of the refinancing might have been is a matter for speculation but on Mr Shaw's evidence, a refinancing of the balance of the Term Loan and the full Exit Fee could have been achieved over a period of 3 years albeit management in a 10 year plan written by management on 10 August 2010 contemplated a period of 5 years (which would have alleviated the annual cost of paying off the Exit Fee). Accordingly applying the cash flow test, whether Silentnight was able to pay its debts as they fell due in the reasonably near future, we consider that it could do so, because applying a commercial approach as held by Lewison LJ in Bucci v Carman [2014] EWCA Civ 383 at [29 – 30]; the likelihood was that the Bank would restructure the Term Loan and Exit Fee (possibly with the involvement of the Trustees) as it itself envisaged in its internal documents. Silentnight might have faced a liability that was due to mature on 30 November 2011, that liability could possibly be restructured or refinanced, and so did not constitute an immovable "debt wall" as referred to by Lady Wolffe in Re Premier Oil [2020] CSOH 39. The repayment of the Term Loan and Exit Fee bore no relation to the debt looming in Re Premier Oil which was in the sum of about \$2.56 billion (and which itself did not satisfy the test for statutory insolvency under section 123 of the Insolvency Act 1986 due to the date it fell due) and which Lady Wolffe held in all likelihood could not be paid when it fell due.

151. Further we consider it unlikely that tPR would have challenged the 2010 Pension Deficit Plan as opposed to waiting for a further periodic review to review the status of the deficit in the light of Silentnight's trading performance, balance sheet, and the extent to which it remained indebted to the Bank or any replacement funder. As noted above, the tPR and PPF would have been reluctant to cause the insolvency of Silentnight as Mr Shaw agreed in cross examination. There was also the possibility of a solvent compromise of the Pension Scheme based on the burning platform which

might have existed on 30 November 2011. The fact that the Bank had agreed to reduce Silentnight's loan covenants and the repayment of the Term Loan from £3 million to £1.5 million is consistent with the Bank supporting Silentnight and being reasonably confident in its future.

152. Furthermore, a company may continue trading although it is technically insolvent; see e.g. BNY Corporate Trustee Services v Eurosail UK Ltd [2013] 1 WLR 1408. The Insolvency Act 1986 section 123 (2) provides that a company is deemed unable to pay its debts if it proved to the satisfaction of the court that the value of the company's assets is less than the amount of its liabilities, taking into account its contingent and prospective liabilities. Lord Walker at para [42] approved a statement by Toulson LJ to the effect that section 123 (2) requires

“ . . . the court to make a judgment whether it has been established that looking at the company's assets and making proper allowance for its prospective and contingent liabilities, it cannot reasonably be expected to be able to meet those liabilities. If so, it will be deemed insolvent although it is currently able to pay its debts as they fall due. The more distant the liabilities, the harder this will be to establish.”

Lord Neuberger made the point in the Court of Appeal (at para 47 of his judgment) in Eurosail that he could not see any conceivable policy reason why a company should be at risk of being wound up simply because the aggregate value of its liabilities exceeded that of its assets. Mr Shaw's view in cross examination was consistent with that view when he accepted that businesses did not fail, in general, due to balance sheet insolvency alone. As noted above we do not consider that either the 2010 Deficit Recovery Plan or the Term Loan and Exit Fee were likely to crystallise into a liability which Silentnight could not meet in the near future. Accordingly Silentnight did not face any burning platform due to its liabilities exceeding its assets in the period to 13 January 2011.

153. The way the Executive Counsel puts her case does not require her to establish that, if all available options had been properly considered, Silentnight would definitely have refinanced or restructured its banking facilities by November 2011, when the Term Loan and Exit Fee were due to be repaid. Nor, so the Executive Counsel contends does the Executive Counsel need to establish that, but for HIG's actions, Silentnight would have continued to trade profitably, supporting its Pension Scheme in the interests of its members. She contends that it is sufficient for the purposes of Allegation 1 for the Executive Counsel to prove that there were other potentially viable options that ought to have been considered before supporting a transaction that risked harming the company, the Pension Scheme and other unsecured creditors and, to the extent they had an economic interest in the company, the shareholders. Those options, she contends, included but were not limited to refinancing by the Bank itself when the Term Loan expired in November 2011.

The development of the relationship between KPMG and HIG

154. In May 2010 KPMG through its Corporate Finance and Transaction Services Division (“Corporate Finance”), was attempting to develop a relationship with HIG as HIG had recently opened a European Investment Fund and was exploring opportunities in the UK. HIG was potentially an important client for KPMG. At about the same time [Silentnight Board Member 1] had suggested that HIG contact KPMG in order to understand the potential restructuring options available to Silentnight so that HIG could understand whether it was willing to fund and support the arrangements. On 15 June 2010, HIG hosted a drinks reception for KPMG. This was an informal networking event organised by HIG and one of KPMG’s marketing managers to enable HIG to continue building a relationship with KPMG and expand their contracts there. [KPMG Employee 9] attended together with other members of the corporate finance team. Mr Costley-Wood did not attend the reception. On the 16 June 2010 [HIG Senior Management 2] emailed [KPMG Partner 4] (Corporate Finance) and indicated that HIG wanted a telephone call in order to give a “deal update” and for an indication from KPMG’s “restructuring and pension guys” on how KPMG could help HIG. He added that Silentnight’s management had agreed to work with HIG and for the Bank to meet with HIG. HIG proposed to get the shareholders on board. He was optimistic that HIG could get the stakeholders on board. He noted that the “big uncertainty” remained the Pension Scheme. Mr Costley-Wood was subsequently copied into the email when the call was being arranged. The call (held on 17 June 2010) was attended by Mr Costley-Wood, [KPMG Employee 9, KPMG Partner 4, KPMG Partner 3, HIG Senior Management 2 and HIG Employee 4]. That was Mr Costley-Wood’s first contact with HIG. As Mr Costley-Wood understood it the purpose of the call was to learn more about HIG’s proposal for the Silentnight business and to discuss KPMG’s relevant experience. In the course of this call Mr Costley-Wood understood that HIG was pursuing a “loan to own” strategy.

155. After the call he emailed [KPMG Employee 9] (of Corporate Finance) to the effect that it might be worth mentioning to HIG that HIG could consider a pension scheme only CVA to compromise the Pension Scheme. That proposal he considered might be a little aggressive but the “PPF” would be brave to vote against it as that would result in an administration and put jobs at risk. A Pension Scheme only CVA would protect the [Supplier A] licence (under which Silentnight marketed [Supplier A]’s beds) and protect tax losses. He suggested that that suggestion be passed on to HIG before anyone else suggested it. He was aware – from the call with HIG - that they were in discussion with other professionals as was Silentnight which had been discussing restructuring with [External Financial Advisor 4]. He also emailed [KPMG Employee 9] to the effect that a material change to Silentnight’s financial arrangements might be an event which required clearance from tPR. [KPMG Employee 9] passed on both messages to HIG on the evening of the 17 June 2010.

156. Mr Costley-Wood later described the call of 17 June 2010 in an email of 25 June 2010 as being a discussion about the difference between a prepack and a trading administration and the options for compromising a defined benefit scheme. In addition [KPMG Employee 9]'s note of the call recorded that HIG was going to discuss a sale of the Silentnight Debt with the Bank to ascertain its willingness to sell and would discuss the potential sale with Silentnight's shareholders.
157. There was some rivalry between the members of KPMG's Corporate Finance team and the insolvency team and Mr Costley-Wood had to finesse the fact that albeit the Corporate Finance team was keen to act for HIG on transactions, and had had the first contact with HIG, they were unlikely to be involved in the restructuring of Silentnight or matters relating to the Pension Scheme if that went ahead.
158. On the 18 and/or 24 June 2010 HIG sent letters to [Silentnight Board Member 3] and [Silentnight Board Member 1] setting out HIG proposals in relation to HIG's proposed investment in Silentnight. The letter extolled HIG's ability to help Silentnight's management improve Silentnight's business. The letter also noted that there were some significant complexities amongst the stakeholder group not least in relation to the shareholder position and pension fund deficit which would require HIG's involvement in any potential negotiation as part of a transaction. The letter went on to provide that if HIG successfully acquired Silentnight it wished to do so on the basis that it had agreed outline terms for management equity participation of 22.5 percent of the ordinary shares in any future acquisition vehicle. HIG assumed five managers would participate in the equity. The equity share would increase or decrease within limits depending on the performance of the business. HIG also sought a period of exclusivity by seeking an undertaking that the management would not, amongst, other matters seek or encourage any third party to acquire the debt. The latter term was not agreed to by [Silentnight Board Member 3] and [Silentnight Board Member 1].
159. On 25 June 2010 Silentnight and the Trustees agreed the 2010 Deficit Repair Plan based upon a pension deficit of £39.5 million the terms of which are summarised above.
160. HIG spoke to [KPMG Employee 9] on 25 June 2010 and informed him that HIG had spoken to the Bank which had indicated a willingness to sell the debt but were keen that the shareholders were supportive of any deal as the Bank saw reputational risks attached to any "aggressive deal" to which they were a party. HIG had indicated that they proposed to meet the shareholders to discuss their proposals.
161. On 1 July 2010 [HIG Senior Management 2] sent [KPMG Employee 9] a report of a decision by tPR imposing a £5 million contribution notice in relation to the Bonas Group Pension Scheme on the grounds (amongst others) that the company had not engaged openly with the trustees of that scheme. TPR spokesman indicated that tPR

would use the “moral hazard” powers to protect members’ benefits and the PPF. [HIG Senior Management 2] also informed [KPMG Employee 9] that the shareholders had agreed in principle to support HIG and that he proposed to meet with them as they had agreed that the [External Financial Advisor 4] proposal did not work. The email was copied to Mr Costley-Wood.

162. As noted above, [Silentnight Board Member 1] had suggested that HIG contact KPMG. In early July 2010 Mr Costley-Wood appears to have been concerned that Silentnight, so he thought, was unaware that HIG had contacted KPMG and considered it wise to leave them unaware until HIG introduced KPMG to the transaction and that in relation to a proposed meeting, KPMG should remain cordial but non-committal. He was – apparently – anxious not to take any step which might prevent KPMG acting for Silentnight or for HIG in case there was a conflict of interest.
163. On 8 July 2010 [HIG Senior Management 2] informed Mr Costley-Wood that HIG proposed to meet the shareholders and the shareholders’ advisor [Silentnight Board Member 6] in Manchester on 28 July 2010 in order to agree a deal and asked to meet Mr Costley-Wood on that day. In the event a meeting was arranged for mid-July at which the general structure of a CVA was discussed at a high level. On 20 July 2010 Mr Costley-Wood emailed [HIG Employee 4] to the effect that he would get someone to prepare a summary of a CVA proposition and email it to HIG and Silentnight. [KPMG Employee 6] sent Mr Costley-Wood a general slide entitled “what is a CVA” and Mr Costley-Wood indicated he wanted it amended to deal with what he referred to as the Silentnight proposal.
164. On 20 July 2010 the Silentnight Board agreed that Silentnight could continue to trade as a going concern and that that issue would be considered again at a board meeting to be held in October 2010.
165. On 22 July 2010, before going on holiday, Mr Costley-Wood emailed [Silentnight Board Member 1] to arrange a “catch up” on his return, commenting that “we have been helping HIG come up with some solutions for you”. In reply, [Silentnight Board Member 1] welcomed the opportunity for a discussion. Mr Costley-Wood’s email appears to have been intended to keep the relationship with Silentnight open.
166. The meeting between HIG and the shareholders in Silentnight appears to have had a positive outcome with the shareholders reported as stating that a solution had to be found for Silentnight due to the state of its balance sheet. An email sent on 29 July 2010 by [Private equity firm 2] recorded that HIG wanted an all parties meeting to discuss Silentnight’s options in early/mid-August and described KPMG as being advisors to HIG together with [HIG’s External solicitors]. [HIG Senior Management 2]’s email of 29 July 2010 asking for a meeting to be set up recorded the proposed attendees as being [Private equity firm 2], Silentnight management, [External

Financial Advisor 3] and KPMG. [External Financial Advisor 3] had been advising [Private equity firm 2] and HIG for some time. On 30 July 2010 same day [HIG Senior Management 2] emailed Mr Costley-Wood and asked him to give him a call as he could update Mr Costley-Wood on the positive progress HIG had been making.

Allegation 1

167. Allegation 1 is to the effect that from 16 August 2010 at the latest until 14 January 2011 the Respondents advised and/or assisted both Silentnight and HIG in relation to HIG's proposed acquisition of Silentnight. From about 14 January 2011 until about 31 March 2011 the Respondents were engaged by Silentnight to review and advise on the options available to it following the cancellation of the overdraft and to assist with the management of its key stakeholders of Silentnight including the Bank, HIG, the Trustees, the PPF and tPR. The Respondents advised and/or assisted both Silentnight and HIG and accepted and performed the engagement in circumstances where their judgment was compromised (or likely to be compromised) and their objectivity was impaired (or was likely to be impaired) and thereby failed to act in accordance with the Fundamental Principle (b), Objectivity and sections 120, 210 and 220 of the Code.

Mr Costley-Wood's role and duties in the pre engagement period (16 August 2010 to 13 January 2011).

168. There was a large measure of agreement between Mr Murphy and Mr Shaw as to the function generally fulfilled by an insolvency practitioner or restructuring adviser ("IP/RA") prior to appointment as, in the case of a CVA, the nominee or supervisor. There can be a substantial period between an IP/RA being contacted by the prospective client and receiving a formal engagement. One reason is that the ramifications of a restructuring for a distressed company may be serious, both for the company and its stakeholders such as its shareholders and creditors. As Mr Costley-Wood stated in his evidence a decision to compromise a pension scheme is often "slow burning" in that there can be a significant lead time between a prospective client being advised about a potential pension restructuring and a formal engagement to begin work. Amongst the reasons for this is that a decision is often taken by directors after all the other options to reduce the deficit are exhausted. It is a significant decision for directors to take to compromise a pension scheme and as he said in his witness statement that "requires a company to conclude that, absent a compromise, the company would need to enter into a formal insolvency process and it is therefore inevitable that the scheme will enter the PPF." Further the decision to enter the PPF has serious consequences for all stakeholders in the business, including employee members of the pension scheme who will receive reduced benefits on the scheme's entry in to the PPF. Accordingly directors will want to receive clear advice that the company has no other option before embarking on the restructuring.

169. The starting position of the IP/RA is to ascertain the company's financial position and recent trading performance and to understand its assets and liabilities. Prior to engagement, the IP/RA will often work with the company to understand its position, identify the options available to it and potentially negotiate or broker and possibly execute a solution which secures the long term future of the business. He can then produce plans for the preferred option or options. In doing so, if the option is appropriate, the IP/RA might – perfectly properly - engage with various stakeholders if so instructed by management, and if an insolvency practitioner, assume a formal insolvency appointment. In brokering a settlement an IP/RA may have to negotiate with parties whose interests differ from those of the company such as the PPF or tPR or prospective funders. What he should not do (other things being equal) is simply to embark on an option without considering whether that was in the interests of a company or its creditors.

170. KPMG produced a power point presentation entitled “CVA discussion document” dated 6 August 2010 in relation to Silentnight Holdings Limited. The first draft of the document had been produced by [KPMG Employee 6]. The document was in very general terms and did not purport to give any general advice but was limited to comparing the advantages of a CVA over an administration. It noted that Silentnight might wish to consider a CVA to compromise creditor claims and that KPMG could assist with the calculation of the amount of HIG's contribution. It added under the heading “Next Steps” that a feasibility review should be undertaken to confirm whether a CVA might be achievable and that KPMG could provide advice to HIG through the CVA process – “both pre and post”. At this time it was not clear that KPMG would act for Silentnight and the document was generic in terms and contained no specific information peculiar to Silentnight.

171. As noted above HIG asked for an all parties meeting to be held which was eventually fixed for the 16 August 2010. On 10 August 2010 [HIG Senior Management 2] emailed Mr Costley-Wood regarding the meeting. He stated that he wanted to walk away from the meeting to be held on the following Monday with a recommendation in relation to:

1. Administration – post pack vs CVA vs. other
2. Pension Regulator – likely reaction
3. Commercial impact – on business of each approach

172. On the same date [Private equity firm 2 Employee 1] emailed [HIG Senior Management 2] that he would be reminding people at the meeting to be held on the Monday that following the purchase of the Silentnight Debt HIG would conduct a strategic review of its position to include a consensual restructuring and that the option relating to administration which was under discussion was one of the areas that would be given general consideration as part of the wider review process. It was, important, [Private equity firm 2 Employee 1] wrote, that attendees at the meeting did not get the

“wrong” impression that administration was a foregone conclusion when in fact it was one of several options, including consensual restructuring, that would be given consideration after the Silentnight Debt purchase and that that point was a very important point for the directors. [Private equity firm 2 Employee 1]’s email might well have been intended to allay the concerns of [Silentnight Board Member 1] and [Silentnight Board Member 3] because HIG, [Private equity firm 2] and [External Financial Advisor 3] appeared to have been keen on administration as the route forward.

173. A draft of the CVA Discussion Document dated 13 August 2010 was circulated prior to the meeting to be held on 16 August 2010 by [KPMG Employee 6]. It provided that Silentnight might wish to consider a CVA to compromise creditor claims. It noted that a feasibility review should be undertaken to confirm whether a CVA was achievable for Silentnight and that KPMG could advise both Silentnight and HIG “throughout the CVA process – both pre and post.”. Mr Costley-Wood hoped to act for Silentnight in the restructuring as he noted in an email 13 August 2010 to [KPMG Employee 8], KPMG’s Business Development Manager.

174. The 16 August 2010 meeting was attended by (amongst others) representatives of [Private equity firm 2] ([Private equity firm 2 Employee 1]), [Silentnight Board Member 3] and [Silentnight Board Member 1], representatives of HIG ([HIG Senior Management 2]) and Bayside [HIG Employee 4, External Financial Advisor 3, External Financial Advisor 3, Employee 2] and [External Financial Advisor 3 Employee 1, External Law firm 4, External Law Firm 4 Employee 1, HIG’s External solicitors acting for HIG’s External solicitors Employee 1] and Mr Costley-Wood. Mr Costley-Wood attended the meeting at the request of Silentnight albeit HIG had agreed to Mr Costley-Wood attending the meeting. As noted above, Mr Costley-Wood’s note of the meeting was prepared on 21 September 2011 by his secretary using wording supplied by Mr Costley-Wood in an email on September 2011. Mr Costley-Wood said in evidence that he had a vivid recollection of the meeting and that the note was accurate.

175. Mr Costley-Wood said in evidence that he attended the meeting at the request of [Silentnight Board Member 1] in order to persuade HIG not to place Silentnight into administration but to follow the CVA route which would only succeed if the Trustees voted in favour of it due to the size of the liability to the Pension Scheme. The emphasis in his witness statement was rather different where he described the purpose of the meeting as being to discuss potential restructuring options for the business if HIG proceeded with its investment and that he became aware of HIG’s strategy during the course of the meeting. He understood that [Silentnight Board Member 1] and [Silentnight Board Member 3] were supportive of HIG acquiring the Silentnight Debt and he was aware from discussions with Silentnight that it had been trying to find a funder for some considerable time as the executive directors considered that Silentnight required a financial restructuring in order to flourish. His understanding

that the management of Silentnight wanted HIG to acquire the Silentnight Debt was also shared by the Bank following discussions with [Silentnight Board Member 1] .

176. Mr Costley-Wood's evidence was that the premise of the meeting was that Silentnight was in financial distress and needed restructuring to avoid insolvency. [Silentnight Board Member 1] had told him that Silentnight had sufficient cash to pay its debts as they fell due in the short term but would run out of cash and breach its overdraft facility some time in 2010 or early 2011. Mr Costley-Wood's understanding of Silentnight's financial position was based on information supplied by Silentnight in December 2009, what [Silentnight Board Member 1] had told him in the telephone call which took place on 11 May 2010 and the annual accounts which were also sent to him. He understood that Silentnight was looking to refinance its debt to the Bank, that the facilities contained an Exit Fee of £5 million and that Silentnight had a significant Pension Scheme deficit in excess of £45 million that he was led to believe by [Silentnight Board Member 1] was unaffordable. He also understood from [Silentnight Board Member 1] that the management team considered that there was little prospect of Silentnight generating sufficient income to meet those liabilities and that if the business was not able to secure sufficient funding it would "shortly need to enter into a formal insolvency process.". That understanding underlay the proposal or pitch submitted by KPMG to Silentnight on 18 January 2010. Thereafter he had had little contact with Silentnight until about 11 May 2010 when he received Silentnight's financial statements for the year ended 30 January 2010 (which did not suggest that Silentnight's position was precarious) until HIG came on the scene and so his knowledge of Silentnight's financial affairs had not progressed. KPMG did not carry out its own financial analysis of Silentnight until after 17 January 2011.

177. Mr Costley-Wood's note of the meeting records that [External Law firm 4] and [External Financial Advisor 3] were recommending an administration as that would result in a lower price being paid and would keep control of the process away from unsecured creditors such as the Trustees. Mr Costley-Wood proposed that an alternative "solvent" structure should be considered such as a PPF compromise (i.e., an RAA) or CVA. The PPF compromise was briefly considered but apparently not followed up on the grounds that it would take too long and might cost Silentnight too much and the timetable did not suit HIG. The alternative structures would probably deliver a better result for the unsecured creditors including the PPF than a post pack through an administration. The note recorded that the general consensus of the meeting was that a "consensual CVA type" deal would be better for all concerned than a post-pack and there was little or nothing to do unless HIG agreed terms with the Bank which might take until Christmas.

178. As noted above, a requirement of a solvent restructuring such as a PPF compromise is that the PPF have to be satisfied that but for the PPF compromise the employer would become insolvent (i.e., that there was a burning platform and the pension scheme would fall under the control of the PPF in any event) and the PPF would

receive less in the insolvency than under the compromise. Similarly the Trustees/PPF would not vote in favour of a CVA if considered that the offer in the CVA was inadequate or that tPR might wish to use his moral hazard powers.

179. When asked in cross examination what he relied on as a burning platform on 16 August 2010 Mr Costley-Wood responded that there were a number of matters which led to there being a burning platform; the debt wall by which he meant the £5 million Exit Fee due on 30 November 2011 (together with the balance of the Term Loan) and the liability to the Pension Scheme, but the largest cause of the burning platform was that the Bank was willing to sell the Silentnight Debt to HIG which wanted to place Silentnight into administration, i.e., it would not be interested in continuing to finance Silentnight on its then current basis. As noted above we do not consider that either the Exit Fee or the liability under the Pension Deficit Repair plan constituted a burning platform and there is no contemporary evidence that Mr Costley-Wood thought they did. We determine that Mr Costley-Wood was aware that a “burning platform” would be one caused or engineered by HIG once it acquired the Silentnight Debt.

180. Mr Costley-Wood’s understanding at, and following the meeting, was that KPMG was seen by all the parties as the prospective advisors to Silentnight and he informed [HIG Senior Management 2] that he would start the process of engaging with Silentnight unless [HIG Senior Management 2] told him otherwise and set up a meeting with [Silentnight Board Member 1]. Mr Costley-Wood was still conscious that KPMG was trying to obtain HIG as a client and so had no wish to run the risk of offending HIG.

181. Late on 16 August 2010 Mr Costley-Wood emailed (i) [KPMG Partner 3] and [KPMG Partner 5] to call HIG to discuss tPR’s response to a CVA or to recommend some other person to discuss the matter (which cannot have been in response to the [External Financial Advisor 3] email as suggested by Mr Costley-Wood in cross examination as that was sent on 17 August) and (ii) [Silentnight Board Member 1] as he wanted to understand the forecast cash position together with the recent history with the trustees and tPR as he anticipated there would be further questions relating to the “burning platform” and the approach to tPR. He also noted that KPMG would have to bill Silentnight for any time spent on investigating feasibility and that it would be normal for an advisor to contract with Silentnight in these circumstances. He also suggested that Silentnight might wish to check the position with HIG. Mr Costley-Wood said in cross examination that for him that was the date the “informal retainer started” and he accepted that there was a conflict of interest between Silentnight and HIG at that date, albeit he stated that he had managed the conflict by persuading HIG to move towards a consensual restructuring by which he meant a CVA as opposed to a pre-pack in the context of an administration. He should have considered whether Silentnight’s and HIG’s interest might be in conflict even if Silentnight followed the CVA route. That might have led him to insist on being provided with information as

to Silentnight's financial affairs so that he could consider whether Silentnight's only options were a CVA or administration or could involve a solvent compromise or restructuring of the Silentnight Debt or other third party funding.

182. On 17 August 2010 [External Financial Advisor 3] wrote to [HIG Senior Management 2] in an attempt to promote their solution of an administration and noted that the "key question posed to the meeting was, presuming that the company could not avoid some form of insolvency process, what were the advantages and disadvantages of a CVA vs a Post-pack Administration sale particularly with respect" to (i) potential action by the Pension Regulator and (ii) adverse public relations and its impact on the business. The email was forwarded to Mr Costley-Wood who noted there were a number of errors in the email but it was not suggested that the meeting had not proceeded on the assumption that Silentnight could not avoid some sort of insolvency.
183. Also on 17 August 2010 Mr Costley-Wood offered to meet [HIG Senior Management 2] in London to discuss the position of tPR accompanied by a pensions colleague who has been on secondment to tPR. Following the meeting on 16 August 2010 Mr Costley-Wood had some communications with HIG at the behest of [Silentnight Board Member 1] as HIG had little understanding of a CVA. Mr Costley-Wood said in cross examination that he did not have a detailed discussion with HIG about the financial condition of Silentnight but that HIG would have discussed that issue with [Silentnight Board Member 1].
184. On 18 August 2010 Mr Costley-Wood and [KPMG Employee 3] met [Silentnight Board Member 1] at Silentnight's offices as a follow up to the meeting on 16 August 2010. Mr Costley-Wood's evidence was that he could not recall what was discussed at the meeting but thought that [Silentnight Board Member 1] was focussed on learning as much as he could about the CVA process.
185. On 19 August 2010 Mr Costley-Wood emailed [KPMG Employee 6] asking him to kick off compliance, i.e., KPMG's internal compliance process. He says he would like the company signed up asap and that it is "an introduction from HIG Capital [HIG Senior Management 2].".
186. On 20 August 2010 [Silentnight Board Member 1] left a message for Mr Costley-Wood to the effect that Silentnight would engage KPMG. Mr Costley-Wood asked [KPMG Employee 6] and [KPMG Employee 3] to draft a scope of work for KPMG to send to Silentnight and that the scope should be high level to assist Silentnight "in assessing strategic options". Later on 20 August 2010 KPMG sent a draft scope of work to Silentnight:
- KPMG would perform the following:
Obtain an understanding of the Company's operations, group structure, financial position and key stakeholders

An assessment of the options available to the Company including the benefits and risks of each
Identify any additional issues which may impact on strategies being considered

187. In fact the engagement letter was not entered into as [Silentnight Board Member 1] was anxious to save costs and see whether HIG did acquire the Silentnight Debt. Furthermore he had been advised by solicitors not to enter into a retainer until the Silentnight Debt had been sold. Accordingly KPMG did not act in accordance with the unsigned retainer but acted on an ad hoc basis fulfilling whatever instructions it received from Silentnight and charging for its time. KPMG's work prior to the formal engagement was carried out on an ad hoc basis – albeit for reward. In carrying out work after 16 August 2010 KPMG owed Silentnight a duty of care, in contract or at common law, and both versions of the Code provided that professional accountants are expected to follow the guidance in the fundamental principles in all their professional activities with or without reward. The principles apply in the same way to work carried out under an ad hoc engagement as to a formal engagement and once Silentnight was identified as the potential client the Respondents were bound to act in Silentnight's interest as Mr Murphy stated in his expert opinion. Mr Costley-Wood originally asserted in cross examination that under the ad hoc retainer KPMG did not owe Silentnight a duty of care as there was no retainer. Subsequently he backtracked slightly into saying he did not know if KPMG owed a common law duty of care. Mr Shaw who had not been instructed that Mr Costley-Wood had acted for Silentnight on an ad hoc retainer prior to 14 January 2011 was reluctant to accept that Mr Costley-Wood from then on had to act in Silentnight's interest and consider all the options. Whether the ad hoc retainer was on the basis of the draft submitted on 20 August 2010 or an ad hoc retainer to deal with issues relating to a CVA, we consider that Mr Costley-Wood had to act in Silentnight's interest and that involved considering whether a CVA was in Silentnight's interests and its options for avoiding a CVA. As Mr Costley-Wood accepted, Silentnight might not have had a formal "retainer but [Silentnight Board Member 1] recognised that I was helping [Silentnight] deal with HIG and, as you know, those costs were £45,000 and [Silentnight Board Member 1] paid them when we got formally engaged.". Mr Shaw accepted in cross examination that the Code applied to the pre-engagement period and that if the informal retainer was in the terms of the 20 August 2010 draft then the options had to be examined. We consider that the options had to be considered even if the ad hoc retainer was not on the terms of the draft of 20 August but to advise Silentnight on a CVA, and in relation to HIG, then the Respondents could not so advise without considering whether a CVA was in the interests of Silentnight, i.e., they needed to consider the options available to Silentnight.
188. On the 20 August 2010 KPMG assigned the name Project Arran to the potential engagement with Silentnight Holdings Limited and KPMG began its conflicts checking process which involved the completion of the Sentinel Form. That form noted Mr Costley-Wood as the engagement partner, Silentnight Holdings Limited as

the engaging party, and noted (amongst others) the Bank and HIG Capital LLC as influential parties. Under the description of services to be supplied by KPMG it provided “CVA feasibility study and assessment of the options available to the Company. This may lead to an appointment as: Nominee and Supervisor of a CVA; or as administrator of the Company.”. Under the heading “relationship between the parties” the form recorded that the Bank currently funded Silentnight, but that it was probable that HIG would be purchasing the Silentnight Debt.

189. On 24 August 2010 Mr Costley-Wood had a meeting with [Silentnight Board Member 1] to discuss the CVA proposal and other options in more detail and other unspecified matters relevant to Silentnight.
190. On 31 August 2010 KPMG’s Sentinel process issued its conflicts clearance for an engagement with Silentnight.
191. [Silentnight Board Member 1] drafted a process note dated 31 August 2010 which he sent on 1 September 2010 to Mr Costley-Wood for him to review and which, after review, he proposed to send to HIG. The options reviewed were taken from the [External Financial Advisor 4] Project Jane Report and the note recorded in relation to:

Option 4 (pension restructure) referred to in the note as solvent/consensual deal with tPR would be impossible to achieve unless the Regulator is first convinced that the deal must be done and that “this would mean that in the absence of a deal then an insolvent solution is ‘inevitable.’”. The note recorded: “This has previously proven to be a difficult hurdle given that the Company (retaining the support of its incumbent banker) can continue to pay its debts as they fall due”.

Option 5A (CVA): the note recorded its significant advantage over an administration and noted that it required the consent of the creditors and that meant that tPR effectively had a casting vote.

Option 5B (administration). The note referred to the risk of regulatory challenge which could include a contribution notice to NewCo and the risk of loss of control of the process in a post pack.

Under the heading CVA v Admin it noted that the CVA carried with it some key advantages over administration and that Mr Costley-Wood advised that KPMG had never failed to obtain agreement to a CVA at a creditors’ meeting. It also noted that the potential advantages of a CVA over Administration was some £11.2 million taking into account retained tax losses and reduced deal costs.

Under the heading Discussion with the Pension Regulator the note recorded

“The presumption (from discussion with DCW) is that we might “start” negotiations with tPR at c3million with a potential higher limit of £4 to £5million. The requirements of CVAs are that all creditors must be treated equally – assuming that the s75 deficit is c£100 million and that other creditors are £12 million then tPR gets 88% of nett proceeds....”.

The note referred to a request by [HIG Employee 4] that Mr Costley-Wood validate [Silentnight Board Member 1]’s review.

192. Mr Murphy’s evidence (which the Tribunal accepts) was that by this stage Mr Costley-Wood should have been aware that the acquisition of the Silentnight Debt by HIG might not be in Silentnight’s interest. He had not investigated Silentnight’s financial affairs or carried out an option review, and so was not in a position to advise whether either a CVA or administration was in the interests of Silentnight or whether it should pursue another option. [Silentnight Board Member 1] was saying that Silentnight could pay its debts as they fell due, i.e., insolvency was not imminent. He had no reason to believe that Silentnight did not retain the support of the Bank in the event that the Silentnight Debt was not assigned. A CVA was being considered as being a favourable alternative to administration (which would be triggered by HIG using its powers under the newly acquired secured facility) and that after it acquired the Silentnight Debt it could either make or engineer a demand for payment of the overdraft or engineer a shortage of liquidity by declining to renew it. He also understood that the transaction envisaged by HIG was a “loan to own” and that HIG was unlikely to allow Silentnight until 30 November 2011 to arrange a refinancing or restructure of the Term Loan and Exit Fee. This was to Silentnight’s disadvantage and as a result Silentnight’s interest and that of HIG were in conflict. This was an opportunity for Mr Costley-Wood to have appreciated that there was a conflict of interest between Silentnight and HIG.

193. Looking forward, the contemporaneous evidence shows that the HIG transaction had the effect of creating a liquidity crisis for Silentnight in the early months of 2011. Thus KPMG’s Project Bale Options Review produced on 31 January 2011 noted that following the Bank’s decision to sell its debt and associated rights to HIG, the Group’s £5 million overdraft facility would be cancelled on 14 February 2011. This was likely to create a cash crisis for the Group resulting in administration as early as 14 February. As a matter of urgency, management had asked KPMG to assess what options are available to avoid Administration. The only realistic option was to engage immediately with HIG and possibly [Private Equity Firm 3] to understand which if any of the options opposite they would be prepared to fund. If neither was prepared to fund a solvent solution, then KPMG recommended that a CVA was proposed by management as it offered a better outcome for creditors and employees than a sale through Administration. On 1 February 2011 [Silentnight Law firm 2] advised [Silentnight Board Member 2] that Silentnight would be insolvent on 14 February and after the HIG transaction Silentnight had a high level of uncertainty as to its funding

prospects. Mr Costley-Wood himself referred to the changed circumstances of Silentnight after the HIG transaction when he sent [Silentnight Board Member 1] some text to insert in a letter to [Trustee 1] in response to an offer of compromise when he wrote that “six months ago . . . this would have been of interest to the [Silentnight Board] as we have been wrestling with a solvent solution to the scheme for over two years. However we are in different circumstances now. We have a Bank that has withdrawn its facilities and a new lender Bayside/HIG that has no intention of owning a business with a defined pension scheme. That . . . rules out any solvent compromise where the scheme stays on the balance sheet and/or where the scheme owns a significant majority of the shares.”. The acquisition by HIG of the Silentnight Debt had the effect of restricting the options available to Silentnight to restructure and it was foreseeable that the acquisition would do so from late August 2010.

194. However Mr Costley-Wood appears not to have considered the issue of detriment to Silentnight at all but proceeded after the 16 August 2010 meeting on the basis that Silentnight had no option but a CVA or administration, and that if Silentnight adopted the CVA route its interest was aligned to that of HIG. He accepted in cross examination that he had not carried out an options review so as to be able to conclude that Silentnight had no option but a CVA or administration – but subsequently tried to step back from that admission, by saying he had carried one out in his head and that the options could be assessed in less than two hours which could give rise to a professional view. Albeit it appears a solvent compromise was raised briefly at the meeting on 16 August 2010 Mr Costley-Wood’s evidence was that it was not considered further because “to the best of my knowledge, it was dropped because of the time frames, that . . . didn’t suit HIG’s timeframes for acquiring the business . . . what they said at meeting, there wasn’t enough time for it.”. If HIG was not prepared to consider a solvent compromise because the time frame did not suit it, that was a stark example of the conflict of interest between Silentnight and HIG. It might well have been in the interests of Silentnight and its creditors to consider a solvent compromise.

195. The Tribunal conclude that Mr Costley-Wood did not carry out an assessment of the options available to Silentnight and confined his consideration to the merits of a CVA and administration after 16 August 2010 until the end of the first period. He should have warned Silentnight that he could not advise on a CVA without considering whether it was in Silentnight’s interests to enter into a CVA; if the [Silentnight Board] declined to instruct him to consider whether a CVA was in Silentnight’s interest he should have declined to act for Silentnight. As a result he did not warn the [Silentnight Board] that the HIG transaction (and the attendant CVA) might not be in Silentnight’s interest and consider with them what steps Silentnight might take to try and prevent the HIG transaction, or whether it was appropriate to cooperate with HIG and build a relationship with them, and he did not review the options available to Silentnight other than a CVA or administration. Albeit the Bank was entitled to assign the Silentnight Debt, it might well have engaged in discussions

with Silentnight if the [Silentnight Board] had indicated their objections to the HIG transaction in conjunction with the shareholders and Trustees. Silentnight could have entered into discussions relating to the Exit Fee whether alone or in conjunction with the Trustees who were willing to assist by investing up to £5 million in Silentnight. In addition, in the light of the reaction of the Bank, Silentnight could have clarified the attitude of the PPF and tPR as to whether they regarded Silentnight as facing a burning platform and if so, whether a CVA or solvent compromise was a possibility. A CVA might have been preferable to administration but even a CVA could cause harm to Silentnight's business through supplier disruption and a loss of goodwill. If Silentnight faced a burning platform then a solvent compromise with the Trustees, PPF and tPR would have been far less disruptive to Silentnight and was something which should have been considered through the period 16 August 2010 to 13 January 2011. When it was considered, as a result of the [Private Equity Firm 3] offer, it was considered in the context of considerable time constraints (set by HIG) and in a context where the PPF and tPR were concerned that the burning platform relied on had been engineered by HIG and that they did not have sufficient time to agree matters.

196. Further as he did not advise the [Silentnight Board] that a CVA or administration might not be inevitable and that there were options to explore, Silentnight was not in a position to give him fully informed consent to actions which might otherwise give rise to a conflict of interest or breach of duty such as communication and assistance to HIG. Albeit that interchanges between an IP/RA and a potential secured creditor to the procedure and funding of CVA might be acceptable in certain cases, if it was possibly not in Silentnight's interest that HIG acquired the Silentnight Debt and became a secured creditor, then Mr Costley-Wood and KPMG should not have been party to certain of the exchanges with HIG or provided assistance to HIG in relation to a CVA prior to it becoming a secured creditor, and it becoming clear that a CVA was in Silentnight's interests.

197. An internal HIG Opportunity Update written in September 2010 recorded that HIG had held a meeting with KPMG, [External Financial Advisor 3, HIG's External solicitors, External Law firm 4], and Silentnight's management and that the considered advice of financial and legal advisers was that Silentnight should pursue a CVA to compromise creditors' claims. The CVA would require 75 percent of voting creditors (by value) to approve the CVA and if approved would reduce the risk of tPR litigation. HIG would continue to acquire the Silentnight Debt and HIG would provide £3-4 million to Silentnight to pay to creditors. The Pension Scheme would dwarf all the other creditors as the section 75 deficit was in excess of £100 million. In relation to the Pension Scheme, a CVA had some merit as it (i) enabled an initial dialogue with the Trustees and provided them with some value as opposed to none arising from an administration [sic] (ii) if the Pension Scheme accepted the offer that would make the CVA a consensual deal; if "the pension trustee declines to support the proposal it places them in a difficult position if they pursue legal action when they

get nothing from an Administration process.”. In the situation overview the update noted that “this is not a distressed business facing a burning platform. The company is technically insolvent because of an £18.5m pension liability . . . a more fundamental restructuring of the pension scheme will only be achievable where there is a burning platform. The Pension Regulator will only engage with the management and Group’s advisors in light of an impending liquidity crunch”. In relation to key stakeholders it noted that management were in discussion with KPMG regarding the delivery of a CVA should that prove necessary.

198. On 6 and 7 September 2010 respectively Mr Costley-Wood sent [Silentnight Board 1] and HIG a draft document entitled “Silentnight Holdings Limited Proposal 3 September 2010”. This was Mr Costley-Wood’s response to the process note sent by [Silentnight Board Member 1] on 1 September. The document was general in terms and started with a section entitled “what is a CVA?”. It had a draft timeline of a CVA and started by noting that Silentnight might wish to consider a CVA. It compared a CVA with administration and outlined the key differences. Under the heading “suggested proposal, considerations and next steps” the document considered a proposal whereby HIG purchased Silentnight’s share capital and contributed cash towards a CVA. It also stated that a feasibility review should be undertaken to confirm whether a CVA was achievable for Silentnight and noted that KPMG could provide advice to HIG and Silentnight throughout the process. The draft went on to consider the cash flow differences between a CVA and administration. Mr Costley-Wood could not recall whether he reviewed this document in its entirety as certain passages were carried forward from the documents produced by KPMG on 6 and 13 August 2010; in particular he could not recall whether he focused on the passage which stated that KPMG could advise both Silentnight and HIG albeit in his witness statement he suggests that remained technically possible as Silentnight had not at these dates retained KPMG. We do not consider that at this stage, since he understood that KPMG would be retained by Silentnight, he could have properly been retained to act for HIG. More importantly, we do not consider that it was appropriate in these circumstances for KPMG to hold itself out as being able to advise both Silentnight and HIG as it had not been established that their interests were aligned.
199. On 8 September 2010 Mr Costley-Wood emailed [KPMG Employee 4] attaching his CVA proposal “which we have pitched to do” and noted that KPMG was likely to contract with Silentnight as to contract with HIG might spoil negotiations with tPR and HIG were aware of that.
200. On 18 September 2010 [HIG Employee 4] emailed [HIG Board Member 2] attaching some slides describing HIG’s progress with the transaction and included much of the material from the September Opportunity Update noting that in due course HIG “would have to turn off some of the liquidity but as a backstop the overdraft facility expires on 31 January 2011 and we can use our unwillingness to renew as a way of creating a burning platform.”.

201. On 30 September 2010 Mr Costley-Wood sent an email to KPMG [Employee 4] asking him not to discuss Silentnight with [Private Equity Firm 3] or other funders as it appeared that [Private Equity Firm 3] were still interested in acquiring the Silentnight Debt. In cross examination he said that he had sent the email because he was under the impression from [Silentnight Board Member 1] that HIG and Silentnight had an exclusivity agreement and that he was concerned that KPMG's corporate department might still be trying to obtain a contract to carry out due diligence from other funders. In fact Silentnight had not agreed an exclusivity agreement.
202. On 12 October Mr Costley-Wood was informed by [Silentnight Board Member 1] that negotiations between HIG and the Bank were progressing and that [Silentnight Board Member 1] hoped that HIG would acquire the Silentnight Debt before the end of November so as to permit a restructuring in January 2011.
203. On 13 October 2010 [HIG Senior Management 2] invited Mr Costley-Wood to join his table at the Insider Awards dinner to be held on 18 November in Manchester. Mr Costley-Wood accepted the invitation.
204. On 19 October 2010 [Bank 1 Senior Management 2] of the Bank sent an email to [Bank 1 Senior Management 1] about the HIG offer to buy the Silentnight Debt. In favour of a sale of the debt was that the Bank would be selling at par where the debtor had been in the SBS division within [Bank 1] for about 5 years. Senior management were becoming increasingly frustrated and might leave Silentnight if they did not perceive value for them in remaining with Silentnight. The liability to the Pension Scheme was significant and future trading of Silentnight was inevitably uncertain. Against a sale was the fact that Silentnight was trading well through difficult times and he considered that there was sufficient security to ensure that the Bank was paid in full and the Bank derived significant fees from Silentnight. In the event that there was no sale, the Exit Fee of £5 million would crystallise (albeit the Bank would need to fund it). [Bank 1 Senior Management 2]'s preference was to sell at a premium or crystallise the Exit Fee in order to get some "upside".
205. At a Silentnight board meeting held on 20 October 2010 the [Silentnight Board] agreed that Silentnight could continue to trade as a going concern. [Silentnight Board Member 1] informed the board that the 2011/12 budget had been reduced from the 3 year plan as there had been some significant negative impacts in recent months as the market had become more difficult and might remain flat or decline as opposed to increase by 3 per cent as envisaged in the budget. The board noted that an Exit Fee of £2.5 million was budgeted for, which was lower than the £5 million provided in the Term Loan, and would only be achievable if Silentnight refinanced before 30 November 2011 which might not be possible. The minutes do not record any

reference to the Silentnight Debt possibly being acquired by HIG and how that might impact Silentnight.

206. Mr Costley-Wood emailed [HIG Senior Management 2] on 26 October 2010 (presumably in response to a question) that he had had quick chat with his partner, [KPMG Partner 1], to the effect that if there was a conflict between a creditor and a shareholder in approving a CVA there was no need to go to court and KPMG did not consider that a CVA could be used to force a share transfer. HIG would need to review Silentnight's articles to ascertain whether there were any relevant articles. Mr Costley-Wood should have appreciated that the HIG transaction was potentially detrimental to Silentnight. He was rendering advice or assistance to HIG the interests of which might be adverse to those of Silentnight, and he also should have understood that HIG was prepared to consider a non-consensual acquisition of the shares in Silentnight, if that were possible. If Mr Costley-Wood's motive in answering the question was to keep HIG's focus on a CVA as opposed to administration, as he suggested in cross examination, that assumed that Silentnight had no option but to let HIG acquire the Silentnight Debt and then implement a CVA.

207. On 12 November 2010 a telephone call to be held on 15 November 2010 was arranged between Mr Costley-Wood, [HIG Senior Management 2, HIG Employee 5 and HIG Senior Management 3]. No agenda was prepared for the call and Mr Costley-Wood believes that he answered some general queries in relation to the CVA process. After the call Mr Costley-Wood emailed [HIG Senior Management 2] stating that he hoped that [HIG Employee 5] and [HIG Senior Management 3] were reassured after the call. That suggests that the call was about the CVA process. This call is not set out in the particulars of Allegation 1. Despite the references in the particulars set out thereunder as "exemplifying" the complaint (and there being no request for further particulars), we do not make any finding in relation to this exchange.

208. On 18 November 2010 Bayside wrote to the Bank submitting a non-binding offer to acquire the Silentnight Debt. The offer was to acquire the outstanding balance under the CID Facility, Term Loan, and the overdraft facility at par and to share the prepayment fee to the extent that Silentnight actually paid it.

209. On 19 November [External Financial Advisor 4] sent a revised scope of work and fee structure relating to their work on their proposed restructuring of the Pension Scheme. [External Financial Advisor 4] had had a "no names" brain storming workshop with tPR to discuss [External Financial Advisor 4] 's proposal.

210. On 21 November 2010 [HIG Senior Management 2] sent an email to [HIG's External solicitors Employee 1]and informed him that working on the assumption that HIG would have purchased the Silentnight Debt in early December he wanted to prepare a CVA work plan to put into immediate action through to February. His assistant would arrange a meeting at HIG's offices in the next 10 days so that the

attendees could agree a plan and “appropriate roles and responsibilities”. He added, addressed to Mr Costley-Wood, “as the CVA process will be new for all on the HIG side we’ll be relying on your guidance on timing and approach, in particular as it relates to the pension regulator and trustees, SN shareholders and trustees [sic] management and trade creditors”. The meeting was duly convened for 25 November 2010. Mr Costley-Wood should have appreciated that he was being placed in a position where a conflict of interest was likely to arise and should have responded that it was inappropriate for him to attend the meeting as he was advising Silentnight. The procedure and timetable of a CVA might well be under the control of a company through its nominee/supervisor and as Mr Costley-Wood said in his evidence, HIG support for a CVA was crucial as it would be putting up all or some of the additional funds required to enable the CVA to succeed. However, before Silentnight embarked on a CVA, it had to be satisfied, after appropriate advice, that a CVA was the appropriate course for it to take.

211. On 22 November 2010 Mr Costley-Wood thanked [HIG Senior Management 2] for the invitation to the Insider Dinner and added “Let’s hope Silentnight wins turnaround of the year next year.”. Albeit that might have been light-hearted, this was an encouragement to [HIG Senior Management 2] and gave an indication of his support of the HIG transaction. If he had been working to protect Silentnight’s interests it would have been difficult to send an email in those terms.
212. On 24 November 2010 the [Silentnight Board] met. [Silentnight Board Member 1] informed the board about the Trustee’s enquiry regarding the Exit Fee and that he had responded explaining Silentnight’s options and the principal strategy for 2011. [Silentnight Board Member 1] said he would circulate a copy of his response to the Trustees to the board.
213. On 25 November 2010 there was a telephone call attended by [HIG Senior Management 2], [HIG Senior Management 3, Bank 1 Senior Management 2] and Mr Costley-Wood. There is no note relating to the call produced by Mr Costley-Wood. Mr Costley-Wood could not remember what the call was about which illustrates the consequences of not keeping a note in circumstances where the only person on the call representing Silentnight’s interest was Mr Costley-Wood.
214. On the same day [HIG Senior Management 2] sent [HIG’s External solicitors] and Mr Costley-Wood an article about a [Pension Provider] which referred to the issue whether tPR’s claims ranked ahead of creditors in a liquidation. HIG then asked Mr Costley-Wood whether a FSD (a financial support directive) would rank ahead of an administrator’s fees in an administration. KPMG discussed the issue internally and then, presumably, advised HIG. Certain of the documents relating to this issue were produced after the end of the hearing and accordingly were not the subject of cross examination. If the question related to Silentnight, it should have caused some

concern to Mr Costley-Wood as it referred to administration and tPR's moral hazard powers.

215. A meeting was arranged for 25 November 2010 at HIG's offices attended by Mr Costley-Wood, HIG and [HIG's External solicitors Employee 2] (who had also been invited by HIG to bring a pension specialist to the meeting). [HIG's External solicitors] were advising HIG and had insolvency expertise and could provide legal and strategic advice. Mr Costley-Wood does not recall the meeting but said he believed it was to deal with procedural matters affecting a CVA which would be in the control of Silentnight through its nominee and supervisor, and not HIG, which had no previous experience of the procedure. However in an email sent on 26 November 2010, the day after the meeting, [HIG's External solicitors Employee 2] noted that Mr Costley-Wood had "yesterday" expressed concerns that the [Silentnight Board] should not take any action to assist the assignment of the Silentnight Debt which placed Silentnight in a worse position prior to the assignment of the Silentnight Debt. Accordingly the meeting of 25 November 2010 went beyond mere procedural matters. [HIG's External solicitors Employee 2] then went on to discuss – in the email – pressure being placed on Silentnight after the assignment including by making a demand. He then asked Mr Costley-Wood if he had any thoughts "on your side on the risks of using the threat of demand to get the customer to do things after the debt assignment?". Mr Costley-Wood said in his witness statement that he did not advise HIG whether a CVA was in its best interests. Mr Costley-Wood did not respond to questions raised in the chain of emails relating to the overdraft or BACS facility after the debt had been assigned and whether a demand might be used to force Silentnight to "do things" such as change the mandate. What the email does suggest is that [HIG's External solicitors Employee 2] , having attended the meeting on 25 November 2010 viewed Mr Costley-Wood as advising HIG at the meeting. When he declined to attend a telephone call on 26 November 2010 to discuss issues raised in emails dated 26 November 2010 due to his lack of availability, [HIG's External solicitors Employee 2] told him not to be concerned as his attendance was probably not a good use of Mr Costley-Wood's resources. If Mr Costley-Wood had not realised the possibility of a conflict between the interests of Silentnight and HIG before he should have realised the conflict at that time. He was being told that HIG might take steps in relation to Silentnight which were not in its interests. In addition he should have indicated that it was inappropriate for him to be copied in and involved in email exchanges for advice between HIG's solicitors, [HIG's External solicitors] and HIG. He did not, and he should have, made it clear that he advised Silentnight and not HIG and therefore could not assist HIG even in relation to procedural matters unless he and Silentnight were satisfied that a CVA was the appropriate course for Silentnight.

216. [HIG Senior Management 3]arranged a telephone call with Mr Costley-Wood "about the CVA process" on 29 November 2010 but Mr Costley-Wood could not recall whether the call took place.

217. Between 30 November 2010 and 2 December 2010 the Bank considered the issues which might arise for the Bank as a result of the assignment of the Silentnight Debt. The offer from HIG was for the acquisition of the Silentnight Debt and the overdraft at par plus a premium of £1.25 million. The Bank was prepared to accept £1.25 million instead of the pre-payment fee of £2.5 million “in order to get the deal done”. [Bank 1 Senior Management 2] who emailed his colleagues on 30 November 2010 in order to get the approval of the Bank’s internal stakeholders was under the impression that HIG was taking advice from KPMG about a future CVA. There was no evidence as to how he formed that view and he may have done so on the basis that he was told that KPMG was advising on a CVA and he assumed that KPMG was advising HIG. He was also aware that [External Financial Advisor 4] had been advising Silentnight albeit in relation to pension matters. [Bank 1 Senior Management 2] reported that after HIG acquired the Silentnight Debt it would not renew the facilities but would give Silentnight 6 weeks to find alternative funding and if the funding could not be obtained a CVA would follow- “This would be our event of default.”. HIG would provide working capital facilities during the CVA. Ultimately HIG would own the Silentnight Group. Shareholders would be offered a continuation of their dividend payments and the Trustees would be paid a sum equivalent to the 2010 Deficit Repair Plan currently before tPR. [Bank 1 Senior Management 2] had notified [Silentnight Board Member 2] that the Bank was considering an assignment of the Silentnight Debt and he noted that Silentnight had been taking advice on a potential restructuring for the previous 18 months to no avail. [Bank 1 Senior Management 2]’s reasons for seeking approval for the deal was that it gave the Bank the opportunity to make a clean break after the Bank had placed Silentnight under the SBS division within [Bank 1] for a number of years, and a significant concern was the frustrated management team who were held in high regard by the Bank, and who were unlikely to remain for a shareholder solution. [Bank 1 Senior Management 3] (the Bank’s Head of Group, SBS division within [Bank 1] UK and US) forwarded the email to another colleague and commented that “the insolvency process will be used to deal with the current family shareholders who are reluctant to accept reality and also the pension fund liabilities. A proposal will, we understand, be made to the trustee and whilst it may not be ideal, we are told they are likely to accept.”. The Bank was aware that a CVA in this context involved the Pension Scheme transferring to the PPF and that by transferring the Silentnight Debt it was setting off a chain of events that in all likelihood would see Silentnight going into a CVA and the Pension Scheme “taking a hit” as part of a restructure.

218. In early December 2010 a number of staff at KPMG (at Mr Costley-Wood’s direction) had a workshop with [HIG Employee 3] at which various issues relating to a CVA of Silentnight were discussed. Amongst the issues discussed were Silentnight’s capital requirements during a CVA and that of its trading subsidiary A.B.F Limited and creating a detailed planning document setting out the steps to completion for a CVA to take place in mid-February 2011. The workshop should not

have taken place in the light of the possible conflict of interest between Silentnight and HIG. KPMG was assisting HIG.

219. On 2 December 2010 [Bank 1 Senior Management 4] (Executive Director, UK) sought approval from [redaction] [Bank 1 Executive Director/Board 1] to the assignment of the Silentnight Debt. He summarised the position as follows: “Essentially we are facilitating a pre-pack administration that the management want to pursue, so it is their choice not ours. We will be repaid in full but ordinary creditors and the pension fund will lose out unless the management can find an alternative funder which I very much doubt.”. [Bank 1 Executive Director/Board 1] [redaction] responded by email within two hours and agreed with the recommendation.
220. An update of the HIG Silentnight – Opportunity Update document summarised the profit which HIG expected to make on the acquisition as £46 million and a 60.9 percent Internal Rate of Return assuming an exit in January 2014. It noted that in the event of a failure of the CVA Silentnight would be placed in administration which would produce similar returns for HIG as it would obtain in a CVA. Bayside produced a similar analysis which rehearsed the benefits of a CVA in similar terms to those set out above including the fact that the Trustees would be the majority in value of the creditors and the CVA would enable an initial dialogue with the Trustee “and provides them with some value against no value from the Administration process, which we are told is key in the current environment given the stance taken by the Pension Regulator”. Bayside’s analysis also noted that if the CVA failed Silentnight would be placed in administration.
221. On 3 December 2010 [HIG Senior Management 2] sent an email to [HIG’s External solicitors Employee 1], copying in Mr Costley-Wood, asking how much information HIG was legally entitled to once it owned the Silentnight Debt so that he could assess the financial position of Silentnight. He wrote to Mr Costley-Wood “to feel free to jump in.”. Mr Costley-Wood did not reply to this email which was answered by [HIG’s External solicitors Employee 1] and [HIG’s External Solicitors Employee 3]. He should have replied to the effect he should not have been copied in as the questions were matters for HIG’s legal advisors to advise upon and he acted for Silentnight.
222. On 2 December 2010 and 6 December 2010 Mr Costley-Wood, [KPMG Employee 10] and [HIG Senior Management 2] held meetings respectively at HIG’s offices and KPMG’s offices. Mr Costley-Wood said that he did not have notes of the meetings and cannot recall precisely what was discussed but he understood that during this period of time HIG and Silentnight were modelling the cash flow implications of a CVA and wanted to ensure KPMG agreed with their analysis and the likely impact of a CVA on the company’s cash flow and needs as it was likely that HIG would have to provide funding for working capital. That is consistent with [HIG Senior Management 2]’s email of 5 December 2010 when he wrote to [Private equity firm 2 Employee 1] that he was meeting with Mr Costley-Wood on 6 December 2010 to

“walk through the WC needs of the business during a CVA”. A further meeting attended by [KPMG Employee 10] (who had met [Silentnight Board Member 1] to discuss Silentnight’s cash flow models) and [HIG Employee 3] was held on 8 December 2010 to consider the cash flow models. Once again KPMG were assisting HIG in relation to a potential CVA which might not be in Silentnight’s interests and proceeding on the unquestioned assumption that a CVA was in Silentnight’s interests.

223. On 7 December 2010 [Private equity firm 2 Employee 1] wrote to [HIG Senior Management 2] that KPMG needed to be pressed more on project planning and the timescale and needed to provide HIG/ [Private equity firm 2] with more detail. He noted that Mr Costley-Wood had “implied” at the meeting on 6 December that he would “flip” Silentnight into administration if the CVA failed.

224. On 7 December 2010 [HIG Senior Management 2] emailed Mr Costley-Wood asking for an estimate of KPMG’s fees and other fees would be incurred for a CVA. Mr Costley-Wood responded on 8 December 2010 would be £500,000 for KPMG and £200,000 for legal fees.

225. A note prepared by the Bank’s lawyers in early/December 2010 provided that the Bank wanted a clean break in relation to the overdraft facility and did not wish to operate it after assignment. Upon completion of the assignment the obligation to provide an overdraft had to be terminated.

226. Thereafter there was correspondence in relation to the overdraft between [HIG Senior Management 2, HIG’s External solicitors and Bank 1 Senior Management 1]. HIG raised the possibility of Silentnight requiring overdraft facilities after the assignment of the debt to HIG. HIG’s original offer had provided for HIG to acquire all rights of the Bank under the facilities including the overdraft. The Bank was concerned at the possibility of not getting a clean break and the possibility of an ongoing facilities including overdraft facilities involved a significant shift from HIG’s original proposal. On 14 December [External Law firm 1 Employee 1], acting for the Bank confirmed to [HIG’s External solicitors] that the Bank was not prepared to offer an overdraft facility in reply to a request by HIG that HIG wanted overdraft facilities to be provided after the assignment (supported by a collateralised indemnity from HIG) but that the Bank would allow the bank account to be operated if it was in credit and would offer CID facilities if secured and ancillary banking services. On the 16 December 2010 [External Law firm 1 Employee 1] clarified that the Bank would only give notice of non-renewal of the overdraft facility in the event that the sale agreement was signed and that Silentnight/HIG could ask for an extension to the overdraft facility but there would be no commitment on the part of the Bank to grant it. Albeit [Bank 1 Senior Management 1] gave evidence to the effect that the overdraft was cancelled because that was required under the debt sale agreement it is clear that the Bank insisted that the Debt Sale Agreement contained a provision for the cancellation of the overdraft and was not prepared to commit to the provision of

overdraft facilities. It was prepared to give Silentnight 30 days' notice to repay the facility after which it could serve a demand for payment.

227. [HIG Senior Management 2] emailed [HIG's External solicitors] (copying in Mr Costley-Wood) on 14 December 2010 for advice on how to deal with a debit on the overdraft once a CVA proposal was issued. Mr Costley-Wood responded that he thought HIG needed to take on the overdraft but it could be reduced if there was headroom in the discounting facility but if the security permitted the overdraft facility to be paid off after the amount due on the discounting facility then there would not be a problem. [HIG Senior Management 2] asked a further question on working capital and also stated that HIG would only be prepared to provide working capital if a share transfer had taken effect. In relation to the transfer of the shares Mr Costley-Wood wrote that "[I]t is better from a tpr point of view to tfr [transfer] the shares post cva creditor agreement so a call option of a conditional sale agreement may be better than a straight tfr when the proposal is issued.". Mr Costley-Wood was elliptically advising on an issue that touched on the question whether HIG would be treated as "connected" (the test was in fact was whether it was "currently involved") to Silentnight for the purpose of a solvent compromise and the amount of equity which the PPF might require as part of a compromise. The email did contain advice to HIG to assist it carrying out a transaction which might well not be in Silentnight's interest. Mr Costley-Wood should have declined to advise and referred [HIG Senior Management 2]to [HIG's External solicitors].

228. On 15 and 16 December 2010 there were more communications between HIG (through [HIG Employee 3]) and Mr Costley-Wood in relation to Silentnight's working capital requirements and the attitude creditors would take in their dealings with Silentnight once they were informed of the proposed CVA. Mr Costley-Wood and [KPMG Employee 10] also looked at slides prepared by HIG showing the working capital model for Silentnight. When [HIG Senior Management 2] sent the slides to [HIG Board Member 2] he wrote that KPMG supported their assumptions and set out KPMG's observations on the additional headroom which had been included in the model. In the light of the possible conflict of interest Mr Costley-Wood should not have responded to the emails. HIG was not a secured creditor and it might not have been in Silentnight's interest that it should become one.

229. At about this time KPMG undertook various compliance matters. A project name "Project Bale" was allocated and [KPMG Employee 10] stated that the project was a company CVA and under work type provided "CVA planning". A second sentinel request was submitted. HIG was not mentioned under "other parties" and the services to be provided were identified as "options for review for the group and subsequent potential CVA planning". The form was submitted by a junior, [KPMG Employee 11], and Mr Costley-Wood did not review it but did later comment to Sentinel and [KPMG Employee

230. [11] that he thought clearance had been covered by the previous sentinel as “none of it went ahead.”. Mr Costley-Wood stated in his witness statement that he had considered that the original application submitted in August 2010, which did refer to HIG, remained valid. The sentinel request was approved for the period 16 December 2010 to 16 December 2011 pursuant to the request submitted on 16 December 2010.
231. On 17 December 2010, [KPMG Employee 10] sent Mr Costley-Wood a graphical representation of the time frame leading to a CVA/creditors meeting and noted that [Silentnight Law firm 2] had advised Silentnight to refrain from engaging KPMG until they had received notification of the assignment from the Bank. The graphical representation showed that KPMG was to be engaged to carry out an options review on 4 January after the Debt Sale Agreement and also set out a proposed timetable for a CVA which included a CVA proposal being printed and ready to send out 9 days after the option review.
232. Between 18 and 21 December 2010 [HIG Senior Management 2] raised various issues which would arise for Silentnight if the Bank terminated the remaining banking facilities (such as the confidential invoice discounting facility) it was supplying to Silentnight in the event of an administration. [HIG Senior Management 2] wanted to know how important termination would be for Silentnight, would the administrators be able to find alternative facilities, what would the impact be on funding to be expected from HIG, and why would a bank be willing to provide the facilities (backed by a letter of credit) in a CVA but not in an administration. Mr Costley-Wood responded that a termination would not cause serious difficulties for Silentnight as KPMG planned to do a contingent sale and not trade themselves but in any event other providers would be available. On 20 December 2010 [HIG Senior Management 2] wanted to know how easy it would be for Silentnight to obtain ancillary banking facilities and a new invoice discounting facility. He also raised his concerns that if HIG funded the payment of creditors after the issue of the CVA proposal it would not benefit from the creditor “haircut to the same extent were we to [sic] have full agreement pre-payout”. A call with [HIG’s External solicitors , HIG Senior Management 2, HIG Senior Management 3] and Mr Costley-Wood to discuss the issue of the cancellation of banking facilities on both a CVA and administration was fixed for 21 December 2010. The email arranging the call sent on 21 December 2010 attached an email string between HIG, the Bank’s solicitors and [HIG’s External solicitors] including an email dated 16 December 2010 which recorded that the Bank would only give notice of non-renewal of the overdraft in the event that the Debt Sale Agreement was signed. Mr Costley-Wood dialled in on the call but said in evidence that as he was not actively involved in the discussion he left the call as he did not consider it necessary to participate. If Mr Costley-Wood had not realised by this stage that the HIG transaction might not be beneficial to Silentnight he should have appreciated that the intention was to create a liquidity shortage for Silentnight in circumstances where under the existing arrangements it could pay its debts as they fell due and that, but for the assignment of the Silentnight Debt, Silentnight would not

suffer a liquidity crisis. Mr Costley-Wood took no steps to alert the [Silentnight Board] of that and to explore available options with them. The options included an approach to the Bank, possibly in conjunctions with the Trustees and shareholders, and the [Silentnight Board] threatening not to cooperate with HIG. Albeit he was taking instructions from [Silentnight Board Member 1] and [Silentnight Board Member 3] he should have raised the matter with them and if necessary ascertained whether the Silentnight Board was aware of the position. We note that Mr Costley-Wood said in evidence that he kept [Silentnight Board Member 1] fully informed about his communications. We have difficulty in accepting that as there were many communications, and very few references to communications or conversations in the emails which passed between them, and do not consider that Mr Costley-Wood was so organised or had the time to report back on each occasion.

233. On 21 December 2010 Mr Costley – Wood submitted a client acceptance questionnaire for the Silentnight engagement under the code name “Project Bale” for an options review and CVA preparation for Silentnight. It did not reveal any established client relationship. On the same day Mr Costley-Wood submitted a RestructuringEngagement Questionnaire. The questionnaire did not refer to HIG in relation to the question whether there were any third parties involved which were clients with conflicting interests.
234. By the end of 2010 Silentnight’s liabilities to the Bank had been substantially reduced. The Term Loan amounted to about £3.7 million, the average overdraft amounted to £3 to £4 million and the CID facility averaged between £7million and £8 million. The potential Exit Fee provided an additional liability of at least £2.5 million.
235. On 4 January 2011 Mr Costley-Wood was informed by email by [KPMG Employee 10] (somewhat strangely in the light of the circumstances) that Silentnight had been informed by the Bank of the advanced negotiations and that the next step was for Silentnight to request disclosure of the counter party and ascertain their intentions. This was curious as [Silentnight Board Member 1] and [Silentnight Board Member 3] were closely involved with HIG and were well aware of the potential assignment of the Silentnight Debt. [KPMG Employee 10] added that [Silentnight Board Member 1] foresaw further negotiations with the shareholders culminating in the appointment of KPMG to undertake the options review. Mr Costley-Wood forwarded the email to [HIG Senior Management 2].
236. On 7 January 2011 [HIG Senior Management 2] emailed Mr Costley-Wood asking whether customers could withhold their payments or offset receivables including in the case of a liquidation or shut down. [KPMG Employee 10] informed [HIG Senior Management 2] that he and Mr Costley-Wood could take a call that afternoon. Mr Costley-Wood could not recall whether the call took place. Once again it appeared that HIG was under the impression that it could look to KPMG for advice.

237. On 10 January 2011 [HIG's External solicitors] emailed Mr Costley-Wood regarding a number of questions [HIG Senior Management 3] had raised regarding the administration process relating to the funding of Silentnight during an administration and whether any other funders could offer funding and disadvantage HIG and asking Mr Costley-Wood to participate in a telephone call. The call took place later that date. As Mr Costley-Wood was acting for Silentnight and it was clear that the HIG transaction might be to Silentnight's disadvantage he should have declined to attend the call. A rival funder might have been an advantage to Silentnight; it might have assisted it to avoid an administration or increased the monies realised in an administration. As he attended the call he should have alerted the [Silentnight Board] that HIG was still considering administration and that that might not be in Silentnight's interest.

238. On 11 January 2011 Bayside prepared an internal presentation in which it recorded that it was working in partnership with HIG to acquire control of Silentnight by means of a CVA. The envisaged transactions included acquisition of the Silentnight Debt and a permanent capital investment of £5.5 million to fund the Pension Scheme deficit and transaction fees. The presentation noted that the transaction carried a number of risks including the risk of a filing for administration. Bayside's working capital model was in line with KPMG's recommendations and the presentation described the benefit to Bayside if it was unsuccessful in obtaining the business through an administration including the payment of the £5 million Exit Fee. Under the heading Transaction Timeline and Action Steps it noted that Silentnight would retain restructuring advisers (KPMG) to advise on alternatives including a CVA or administration. In the light of the advantages of a CVA it assumed that KPMG would advise that a CVA should be pursued and would approach the Trustees and PPF with a view to gaining support for the CVA. A further step envisaged Bayside/HIG acquiring the equity for Silentnight in exchange for a consulting contract under which the shareholders would earn fees (of approximately £300,000) and Bayside/HIG's undertaking that it would provide working capital to Silentnight through the CVA. The presentation noted that Bayside/HIG might not end up owning the business if Silentnight went into administration as there might be a rival bidder which outbid Bayside/HIG.

239. On 12 January 2011 the Silentnight Debt Sale Agreement was entered into between the Bank and Grace Bay. Under the Debt Sale Agreement the debts owed by A.B.F. Limited and Silentnight Group Limited in respect of the Term Loan and overdraft facility were to be acquired by Grace Bay. No later than 1 business day after the date of the deed, the Bank was required to give notice that the overdraft facility would not be renewed on the expiry of the 30-day period from the date of the notice: clause 5 of the Debt Sale Agreement. The Debt Agreement provided that if the Silentnight Debt was repaid in full (together with all fees) and the overdraft cancelled prior to the Completion Date the sale would not take place and all obligations except certain immaterial obligations would terminate.

Allegation 1 - 14 January 2011 to 31 March 2011

240. On the 13 January 2011 the Bank gave notice to Silentnight of the sale of the Silentnight Debt to HIG and that the overdraft would expire on 31 January 2011 but that the Bank was prepared to give a short extension to 11 February 2011 to enable Silentnight to obtain alternative banking facilities. It followed that the Completion Date was 14 February 2011. The effect of these terms was that Silentnight had until 11 February 2011 to try to raise alternative finance to repay the Silentnight Debt if it wanted to prevent its assignment to HIG. Silentnight did not have the funds to continue trading without alternative finance. Accordingly, unless it could obtain further finance Silentnight faced insolvency, i.e., a burning platform. It was common ground that this was a situation which HIG had sought to engineer.

241. In mid-January 2011 Mr Costley-Wood should have appreciated that the interests of Silentnight and HIG differed. HIG's objective was to implement its loan to own strategy (as cheaply and quickly as possible) which involved creating a liquidity crisis in order to implement a restructuring of the pension scheme liability whether through a consensual restructuring or a formal insolvency procedure. Silentnight's interest (which coincided with the interests of its creditors) was that it had as much time as possible to restructure the Term Loan and the Exit Fee whether through raising funds from the Trustee alone or in conjunction with the Bank or a third party funder which might be prepared to finance a consensual restructuring. In the light of the service of the non-renewal notice Silentnight faced imminent insolvency on or shortly after 14 February 2011 and unless Silentnight obtained additional finance its future lay in HIG's hands. There was a conflict of interest between Silentnight which needed to consider alternatives to its acquisition by HIG and HIG which wanted to take it over.

242. [Silentnight Board Member 1] forwarded the notice of non-renewal to Mr Costley-Wood on 13 January 2011. KPMG's letter draft letter of engagement was sent the same day and after some slight amendment was signed on 14 January 2011. The services to be provided by KPMG were set out in the appendix to the letter:

Phase 1

Options review:

- Obtain an understanding of the group's operations, structure, financial position and key stakeholders
- An assessment of options available to the group including the benefits and risks of each
- Identify any additional issues which may impact on the strategies being considered

Shareholder management

- Assist the group to manage its key stakeholders during this period including the shareholders, the Bank, HIG, the trustee of the Pension Scheme, PPF and tPR.

Phase 2:

Once the appropriate option(s) have been identified, KPMG will assist the group with implementation as required.

Estimated fees for Phase 1: £50,000

On 28 February 2011 the retainer was amended to include dealing with tPR and PPF on Silentnight's behalf.

243. Between 25 November 2010 and 14 January 2011 Mr Costley-Wood and [KPMG Employee 10] had recorded about 104 hours of chargeable time to the KPMG billing system in respect of their work on Silentnight with time costs of about £45,000. These costs were included in KPMG's invoices to Silentnight in January 2011.

244. On 14 January 2011 Mr Costley-Wood signed an additional Restructuring Acceptance Questionnaire. The purpose of this additional questionnaire was to identify if further senior approval was required in the light of the risks attaching to the engagement (the preparation of the options review) before the engagement was accepted. Mr Costley-Wood signed the questionnaire to confirm that all issues had been discussed with another partner and that approval was confirmed. The document was countersigned by [KPMG Partner 1], as Consultation Partner, completing the formal engagement acceptance procedures. KPMG's handbook provided that before the Restructuring Acceptance Questionnaire was completed the engagement partner was required to consider the scope of conflicts of interest that might threaten independence and objectivity such as relationships with third parties connected to the project. KPMG's Client and Acceptance Manual provided that each new engagement should be evaluated and approved using the CEAC (Client and engagement acceptance and continuance) policies and process. The CEAC provided that it was the responsibility of the engagement partner to evaluate a new engagement to ascertain (amongst other matters including the risks to the firm) that the firm could meet the client's expectations, any independence issues that might prevent the service being provided and any potential conflicts of interest. [KPMG Partner 2] said in his evidence that if there were particular risks to be noted they might not be noted on the questionnaire but might be put on a separate sheet of paper as the form had limited space for answers. On the questionnaire, the box for "other involved parties" was left blank. [KPMG Partner 2] accepted that he would have expected the names of connected parties on the Sentinel form to be supplied in response to the question. The form incorrectly and inconsistently stated that there would be no reliance by third parties but then identified tPR might wish to see the options review. The space for third party involvement was also uncompleted and one would have expected to see

HIG referred to in the box as [KPMG Partner 2] accepted. The box for any impairment to independence was marked in the negative as was the box marked further risk factors which included a risk to objectivity of the engagement team. [KPMG Partner 2] said in his evidence that this was an opportunity to note that there were risks which had not been mitigated. The information on the questionnaire and any accompanying document would then be appended to the KRRMP form or noted. No other accompanying form has been produced and we conclude that it was not created. [KPMG Partner 1] counter signed the form and sat in the same room as Mr Costley-Wood. He did not give evidence and we do not know whether he understood the nature of KPMG's involvement with HIG or what the substance of his discussions with Mr Costley-Wood was. In terms of providing information for an evaluation of risk the questionnaire was obviously deficient as KPMG had been advising Silentnight and HIG.

245. On 14 January 2011 [KPMG Employee 6] prepared a workstream schedule which envisaged a CVA after discussions with the Trustees and tPR. It did not refer to a solvent compromise or other compromise with the Trustees.
246. On the same date there was a call between (amongst others) Mr Costley-Wood, [HIG Senior Management 2 and HIG Employee 2, Silentnight Board Member 1 , Silentnight Board Member 3, Silentnight Board Member 2 and Silentnight Law firm 2 Employee 1] who were advising the [Silentnight Board]. The note of the meeting records that (i) It was acknowledged by the management team that a restructuring of the business was required and KPMG were asked to report on the options available to the Group in the light of the cancellation of the overdraft and (ii) KPMG and the [Silentnight Board] acknowledged the requirement to engage with the Trustees during the period of the options review.
247. On 16 January 2011 [HIG Senior Management 3] emailed [HIG Board Member 2] to the effect that the Debt Sale Agreement had been signed and KPMG had been appointed "as planned" and had started to work.
248. On 17 January 2011 [HIG Senior Management 2] sent Mr Costley-Wood a brief summary of certain terms of the Debt Sale Agreement including the fact that notice had been given to Silentnight by the Bank that the overdraft facility would be withdrawn on the first business day after 11 February 2011. Mr Costley-Wood had not seen the Debt Sale Agreement or been involved in the negotiation of its terms. [Silentnight Board Member 1] sent Mr Costley-Wood a copy of [External Financial Advisor 4] 's Project Jane Report produced on 31 March 2009. On the same day KPMG sent an initial request for information to Silentnight for the purpose of the options review. The list was a fairly comprehensive list of documentation including the background to Silentnight's then current financial circumstances. Much of the information should have been sought in August 2010 if KPMG was to advise Silentnight in relation to a CVA.

249. On 18 January 2011 [Silentnight Board Member 1] sent Mr Costley-Wood information about bankers who had either been involved in providing facilities to Silentnight or been asked to provide substantial banking facilities who had received Silentnight's regular quarterly trading update. They had each declined to provide facilities. In addition he supplied Mr Costley-Wood with a copy of a note to the [Chairman of the Trustees Silentnight Pension Scheme] written on 22 November 2010 in which he had emphasised the need to find a third party funder.
250. On the same day Mr Costley-Wood emailed [Silentnight Board Member 2] informing him that he understood that [External Financial Advisor 4] had reignited the shareholders' interest in a PPF compromise/pension scheme hive down (i.e., a procedure in which the Pension Scheme is not compromised but is hived off to a newco in return for newco receiving a shareholding or equivalent investment in the ex-sponsoring employer) , and that he would be covering this in the options review, and would encourage the shareholders to pass on any ideas to KPMG. [Silentnight Board Member 2] replied that his understanding was not correct and further explained that "the shareholders, as is their right, are looking at all options to replace the current [Bank] overdraft and term loan. This is the brief I understand [External Financial Advisor 4] are assisting the shareholders on. If they are successful in raising finance, then the shareholders are aware that they would still need to restructure the business with some form of PPF compromise/pension scheme hivedown ... The likelihood of alternative finance is slim at best.". He added that it would be helpful if HIG would spell out the future options for current shareholders. In the light of [Silentnight Board Member 2]'s comment about HIG, Mr Costley-Wood forwarded the email to [HIG Senior Management 2].
251. Meanwhile the interest of [Private Equity Firm 3] in investing in Silentnight had revived. [Private Equity Firm 3 Employee 1] emailed [Private Equity Firm 3 Partner] on 18 January 2011 that based on the January 2010 balance sheet, conservative break value in an insolvency looked like c £12m "but that's before considerable upside likely from brands/goodwill. FRS17 [pension] deficit is £18m". He attached to the email [Private Equity Firm 3]'s briefing note entitled "Project Gloria" which was a briefing note for discussion purposes. The document noted that Silentnight's business development had been inhibited by the onerous balance sheet (e.g. pension deficit), passive shareholders, and the Bank which "wanted out". It noted that Silentnight needed to do a deal as the Bank wanted an exit and Silentnight had little chance for traditional financing without a new equity sponsor. It also stated that there had to be a solution to the pension deficit. Under the heading "options" the briefing note referred to a consensual restructuring with Trustees and noted that [External Financial Advisor 4] had ideas but their ideas could take some time to achieve.
252. On 18 January 2011 [KPMG Employee 10] emailed Mr Costley-Wood regarding the short term cash forecast to the effect that HIG's working assumption that there

would be an overdraft and continuing working capital need on 14 February was not correct. The short term forecast indicated that Silentnight would be in credit on 14 February by about £1.4 million rising to about £1.8 million the following week. The requirement in March would be an overdraft facility of £1 million in the week ending 4 March but the account was forecasted to be back in credit after one week. The pattern would repeat on a monthly basis peaking at £1.6 million at the beginning of May. [KPMG Employee 10] asked Mr Costley-Wood whether he wanted him to raise the matter with [HIG Senior Management 2] but Mr Costley-Wood stated he would not raise the issue but asked about other solvency triggers such as those in Bank facilities including the Term Loan. Mr Costley-Wood's evidence was that he did not pass this information onto [HIG Senior Management 2] because it was not in Silentnight's interest to do so as it might have reduced Silentnight's dependence on HIG to provide working capital, and might allow it more time to carry out a restructuring. However it appears that HIG was informed about the extent to which Silentnight might require overdraft facilities as described below.

253. On 20 January 2011 [HIG Senior Management 2] described to colleagues at HIG what he said were initial views of KPMG regarding the planning for a CVA. He said KPMG would issue a more detailed plan once Silentnight had approved a CVA. The detail steps included that on 27 January KPMG expected to present its options review to the [Silentnight Board] where "they will recommend a CVA" and 28 January 2011 when KPMG would issue an options review and a copy would be sent to the Bank which in turn would send it to HIG. The [Silentnight Board] would approve a CVA on 31 January (which was not under KPMG's control) and 1 February Silentnight would "officially inform HIG and agree CVA plan based on forecasted cash flows.". The note also added that Mr Costley-Wood was very confident that Silentnight would have a zero overdraft balance in February and would not require an overdraft facility during the period of the CVA. [Silentnight Law firm 2] had been appointed by Silentnight to advise on the restructuring work. HIG were meeting the shareholders the next day and envisaged a conditional sale agreement with the shareholders for the sale of their shares. In the light of the level of communication between Mr Costley-Wood, [KPMG Employee 10] and HIG, the description of the timing of the CVA and the description of the conclusion to be expected in the options review must have emanated from KPMG and probably from Mr Costley-Wood (directly or indirectly). Since 16 August 2010 he had not advocated any other course.

254. At a meeting held on 21 January between HIG and shareholders representatives, according to the shareholders, HIG made it clear that its intention was to ensure that Silentnight went into a formal insolvency process such as a CVA shortly after it acquired the Silentnight Debt. HIG made an offer which included a £300,000 consulting fee on condition that the shareholders supported a CVA and did not deal with any third parties. [Silentnight Board Member 2] who attended the meeting, noted in a letter dated 26 January 2011 to [Silentnight Board Member 6], that HIG had stated

that it would consider all options, both solvent and insolvent, following receipt of the KPMG report.

255. On 24 January 2011 [Private Equity Firm 3] had a meeting with [Silentnight Board Member 6], [Silentnight Board Member 5] and [External Financial Advisor 4 Partner 1], of [External Financial Advisor 4] in order to make a presentation to the ultimate shareholders of Silentnight to promote [Private Equity Firm 3] as an alternate provider of funds to HIG. [Private Equity Firm 3] had prepared a document entitled “An Introduction to [Private Equity Firm 3]& Proposal to Silentnight shareholders” which provided that the existing shareholders would retain a 25 percent interest in Silentnight’s equity (management would obtain 15 percent and [Private Equity Firm 3] 60 percent) and that [Private Equity Firm 3] was highly experienced in dealing with defined benefit scheme deficits and overcoming the challenges they represent. Following the meeting [Private Equity Firm 3] made an offer to fund Silentnight addressed to [Silentnight Board Member 6] and [Silentnight Board Member 5] as directors of Silentnight Holdings Limited. The letter noted that Silentnight faced significant challenges in the short term including the deficit on the Pension Scheme. The offer was to provide a secured facility of £25 million by 11 February to enable repayment of the Term Loan, the overdraft facility and provide working capital. If required [Private Equity Firm 3] would also supply the funds to replace the CID facility out of the £25 million secured facility. [Private Equity Firm 3 Partner] did not accept that [Private Equity Firm 3]’s offer could properly be described as a “loan to own” because it did not involve an insolvency process. [Private Equity Firm 3] also understood that steps had to be taken to remove the Pension Scheme deficit of Silentnight’s balance sheet and considered that that would require an agreement with the Trustees, tPR and PPF and probably require a cash and equity offer, i.e., a solvent compromise.
256. On 25 January [Silentnight Board Member 6] (who was a director of Famco, Silentnight Holdings and Silentnight group Limited) wrote to [Silentnight Board Member 2] about the importance of avoiding an insolvency. He and Silentnight Board Member 5 had met [Private Equity Firm 3 Partner] and [Private Equity Firm 3 Employee 1] and believed that Silentnight’s best interests might be served by pursuing negotiations with [Private Equity Firm 3] which might provide a viable solvent solution in contrast to the proposals emanating from HIG the intention of which he believed was to place Silentnight into a formal insolvency process. He required the [Silentnight Board] to consider the [Private Equity Firm 3] proposal and was concerned to avoid a situation where too much focus was given to the HIG proposal when there was a viable solution on the table with [Private Equity Firm 3]. He also asked the [Silentnight Board] to provide information to [Private Equity Firm 3] to enable it to finalise its offer. The letter was forwarded by [Silentnight Board Member 1] to Mr Costley-Wood on 26 January 2011. [Silentnight Board Member 2] replied to [Silentnight Board Member 6] by letter dated 26 January 2011 stating that the [Silentnight Board] had considered the [Private Equity Firm 3] offer upon receipt of

the letter and was pleased to note that [Private Equity Firm 3] was willing to work with Silentnight with a view to exploring options including the provision of facilities of up to £25 million and wished to explore long term solutions for the business with respect to both market conditions and the Pension Scheme deficit.

257. On 26 January 2011 [Bank 1 Senior Management 1] summarised Silentnight indebtedness to the Bank as follows:

- Term Loan £3.7m
- Overdraft £194,000
- CID facility £8,778,000
- BACS £4.4m
- Bonds/guarantee £50,000
- Derivatives £415,000

He added that in the event of a refinancing the prepayment fee of £2.5 million would be payable as well the Bank's legal fees and security release fees.

258. On 26 January 2011 [HIG Senior Management 3] wrote to Mr Costley-Wood that he estimated that a third party funder would need to invest approximately £40 million and that HIG had already obtained investment approval for an investment of that amount. His calculation assumed new working capital facility of £5-6 million to be provided during a CVA or other procedure and £3 million plus to the Trustees. Mr Costley-Wood replied that the sums in relation to the CVA or restructure and payment to the Trustees would only be required if there was some form of restructure which, whilst this was likely, [Private Equity Firm 3] did not need to demonstrate that they could support that level of facilities. [HIG Senior Management 2] and [HIG Senior Management 3] then exchanged emails in which [HIG Senior Management 3] wrote that HIG needed to beat [Private Equity Firm 3] on the substance and attack the [Private Equity Firm 3] proposal, beat them on timing, and hamper their ability to put in place a facility before 11 February, when the overdraft would expire unless HIG agreed to extend the facility. [HIG Senior Management 2] responded that he had spoken to management and Mr Costley-Wood "on same" about the [Private Equity Firm 3] offer and told Mr Costley-Wood that HIG would follow the [Private Equity Firm 3] solvent solution if necessary.

259. On 26 January 2011 the [Silentnight Board] met. The board noted that [Private Equity Firm 3] had a good reputation and that [Private Equity Firm 3]'s offer was a solvent solution which would require the support of the Trustees. The board agreed to meet with [Private Equity Firm 3] to clarify the terms of their offer and pursue both the HIG and [Private Equity Firm 3] offers in parallel.

260. [HIG Senior Management 2] in an email sent on 26 January 2011 to [HIG Board Member 2] copied to [HIG Senior Management 3] commented on the [Private Equity Firm 3] offer and noted that he had told Mr Costley-Wood that HIG “would follow the same route as [Private Equity Firm 3] “solvent solution” if necessary.”. He added that management “are not happy and nor is [Silentnight Board Member 2] (nonfamily) so we are fighting a tactical battle to ensure their personal preference to go with HIG is aligned to their fiduciary duties as board members.”.

261. On 27 January 2011

261.1. [Private equity firm 2 Employee 1] emailed [HIG Senior Management 2] to tell him that he had tried to warn [Silentnight Board Member 1] off [Private Equity Firm 3] and that their end game would be an insolvent solution. He added that Mr Costley-Wood ought to attend the meeting with [Silentnight Board Member 1] as he might conclude that [Private Equity Firm 3] were “miles away and not credible in their thinking.”.

261.2. HIG wrote to the [Silentnight Board]. The letter explained what HIG had to offer including the provision of substantial funds of up to £75 million to cover the funding requirements of the withdrawal of the overdraft facility, the continuation of other facilities offered by the Bank such as the CID facility, the Group’s working capital requirements and measures to support organic and external growth. The letter added, as a sting in the tail, a reminder to the [Silentnight Board] to act in accordance with their fiduciary duties.

260.3 The board of Famco met. A report of the shareholders’ meeting with HIG was given. The shareholders understood that HIG were committed to calling in the overdraft taking over Silentnight by means of a “creditors’ [sic] voluntary arrangement” and keeping it for up to 6 years. HIG was unwilling to cede any element of ownership to the family albeit they could receive a consultancy fee of £300,000. HIG had also asserted that Silentnight was insolvent as HIG intended to call in the overdraft on 11 February 2011. The board expressed concern as to what they perceived as KPMG’s multiple appointments and hoped that Chinese walls were in place as they understood that KPMG also advised HIG and the Silentnight Pension Scheme. The Famco board considered that the £25 million offered by [Private Equity Firm 3] would be required in full in order to guarantee the CID facility which the Bank was willing to continue to operate. The Board resolved that [Silentnight Board Member 6] and [Silentnight Board Member 5] were authorised to continue their discussions with all parties to achieve the best outcome and that [Silentnight Board Member 6] was granted authority on behalf of Famco to sign “on its behalf any and all documentation that may be necessary to enable [Private Equity Firm 3] to complete its investment in . . . Silentnight Holdings Limited.”.

262. On 27 January 2011 the [Silentnight Board] met. [Silentnight Board Member 2] advised the [Silentnight Board] of the appointment of KPMG to produce a report which [Silentnight Board Member 2] hoped to circulate to all board members on 28 January 2011. [Silentnight Board Member 2] indicated that it was Silentnight's intention to pursue the [Private Equity Firm 3] and HIG proposals in parallel.
263. On 27 January 2011 KPMG produced their first draft of the Project Bale Report which contained their options review. It was not in substance very different to the final report the contents of which are described below.
264. On 28 January 2011 [Silentnight Board Member 6] (a shareholder and director of Famco and Silentnight Holdings Limited) wrote to [Silentnight Board Member 2] expressing the shareholders' support for the [Private Equity Firm 3] proposal and indicated that the HIG proposal was not in the interest of Silentnight. In his view the [Private Equity Firm 3] proposal which was a solvent deal was preferable to that offered by HIG. He added that because there was a credible offer of financing from [Private Equity Firm 3] the [Silentnight Board] could now concentrate on supporting its shareholders as opposed to having an overriding preoccupation with the position of creditors generally. He also wanted a suspension of KPMG involvement until 11 February 2011 and was concerned that KPMG might be passing information on the [Private Equity Firm 3] proposal to HIG.
265. On 31 January 2011 KPMG produced the final Project Bale Report. It dealt with six options. A copy was sent to Silentnight and to HIG, [Private Equity Firm 3] and the Bank at the request of Silentnight. The introduction to the Report summarised KPMG's conclusions. It noted that following the Bank's decision to sell its debt and associated rights to HIG, the Group's £5 million overdraft facility would be cancelled on 14 February 2011. This was likely to create a cash crisis for the Group resulting in administration. As a matter of urgency, management had asked KPMG to assess what options were available to avoid Administration. To avoid administration, the only realistic option was to engage immediately with HIG, and possibly [Private Equity Firm 3], to understand which if any of the options opposite they would be prepared to fund. If neither was prepared to fund a solvent solution, then KPMG recommended that a CVA was proposed by management as it offered a better outcome for creditors and employees than a sale through Administration: In relation to the options it noted:
- Continue as is – not recommended as this would ultimately lead to the failure of the Group. Following cancellation of the overdraft on 11 February the short term forecast indicated that the Group was likely to face additional funding requirements of between £1 million and £4.3 million in the week ending 4 of March 2011 with similar requirements during the first week of April and May 2011. . . .

- Debt refinance - unlikely but worth pursuing. The restricted timescale, termination fee payable on a refinance, the quantum of funding required and lack of assets to provide security were likely to prove barriers to a refinance. The report added that previous attempts to refinance had proved fruitless but that management were exploring obtaining funding from [Private Equity Firm 3] . The Trustees – even if permitted – could not provide sufficient finance even to cover the Term Loan, Exit Fee and overdraft facility. Management should investigate the offer from [Private Equity Firm 3] as based on KPMG’s experience [Private Equity Firm 3] had the ability to refinance a business within a two-week period. Management needed to be clear about the long term funding requirement of the Group. Whilst the most pressing issue was the overdraft the business was ultimately likely to fail due to lack of cash investment and the cash demands of the pension deficit. Any solution which dealt with all these issues offers better longterm prospects to a short term “fix”. The requirement would be significant and KPMG understood that HIG has committed up to £30 million to cover the existing Bank exposure.
- Pension Scheme solvent compromise – not viable as a stand-alone option. The process would be lengthy and the Group did not have sufficient time to negotiate a compromise; any compromise would not address the underlying cash flow issues and in isolation was not practical. KPMG understood that management had sought advice in respect of a solvent compromise with the PPF/tPR albeit no agreement had been reached. Unless the imminent working capital requirement could be met there was little point in pursuing the option and insufficient time to agree a compromise. In addition the PPF/tPR required certain condition to be met before agreeing a compromise notably that insolvency was inevitable and the Pension Scheme was given an equity stake in the business going forward plus a lump sum greater than the likely dividend in an insolvency.
- Accelerated sale – not recommended. An accelerated sale was likely to lead to a sale via administration due to the Pension Scheme deficit and this could have an adverse effect on customer and brand loyalty. Given the tight time scales KPMG did not consider an accelerated time scale to be the best option available unless the only option was to appoint an administrator and sell the business.
- CVA – recommended subject to funding and conditions attached. In the absence of a solvent solution a CVA was the best solution and was a more elegant solution than an administration and would deliver most

value for the Groups' key stakeholders. To implement a CVA the Group needed to secure additional funding to support the CVA dividend, ongoing working capital, ransom payments and associated costs. If the CVA was rejected administration would follow. The Pension Scheme liability in a CVA would be approximately £100 million and thus the Trustees would, in effect, control whether the CVA was approved or not. Approval would only be given if the dividend in a CVA appeared to be larger than the dividend in an insolvency. Compromising the Pension Scheme would not deal with the pressing cash issues. An alternative to an all creditors CVA was a scheme only CVA which would comprise, in effect, the liability to the Pension Scheme which in a CVA would be measured at about £100 million and the PPF/tPR would have the casting vote in relation to that CVA. The attitude of the PPF to a compromise would depend on the dividend being offered and whether the PPF/tPR was satisfied that the return was probably greater than the return to the fund in an insolvency, the shareholding structure in an insolvency, and the implications for other creditors.

- Administration – likely to be the worst outcome for the business. Whilst administration currently appeared inevitable KPMG saw administration of all or part of the Group as the worst option as it would require significant additional funding, result in the [Silentnight Board] losing control of the business and cause considerable damage to the brand, arguably the Group's most significant asset. Based on the cash flow of the Group, the [Silentnight Board] needed to take independent advice as without the continuation of existing facilities beyond 14 February 2011 the business was likely to be forced into administration.

266. Under the heading "next steps" the Report noted that there were two options available to the Group; a debt refinance or a CVA. KPMG recommended that management should explore the offer from [Private Equity Firm 3] to establish the terms and structure and should also engage with HIG to ascertain whether they would be willing to support a solvent restructure or alternatively a CVA. The Report did not recommend a solvent compromise with the Trustees, PPF and tPR and described that process as lengthy and Silentnight as not having the time to carry out the negotiation. That was consistent with the view of HIG expressed at the 16 August 2010 meeting.

267. On 31 January 2011 the Project Bale Report was considered at a board meeting of Silentnight. Mr Costley-Wood and a representative of [Silentnight Law firm 2] solicitors retained by Silentnight attended the meeting. [Silentnight Law firm 2] advised that further information be obtained from HIG and [Private Equity Firm 3] as to their offers. It was noted that given the Pension Scheme deficit both HIG and [Private Equity Firm 3] should be asked whether they intended to place Silentnight into a CVA or some other form of insolvency and that the HIG and [Private Equity

Firm 3] offers should contain a contingency plan in the event that their primary offer and proposal on how to deal with the Pension Scheme could not be achieved. It was agreed that [Silentnight Board Member 6] and [Silentnight Board Member 2] would be the primary contact with [Private Equity Firm 3] and HIG to receive the offers. Mr Costley-Wood took the meeting through the Project Bale Report and noted that KPMG's advice was that a CVA would be their proposed solution with funding obtained to fund the compromise. [Silentnight Board Member 2] considered that the Trustees would consider a proposal in the light of the 2010 Deficit Repair Plan, back ended and spread over thirty years, to fund the arrears in the Pension Scheme and Mr Costley-Wood considered that Silentnight's cash flow problems might provide better leverage with tPR to secure a compromise as the Pension Scheme was likely to enter the PPF at some time.

268. The meeting also resolved that to ease the cost of professional advisers KPMG should be "stood down" until 4 February to allow Silentnight and the shareholders to obtain written offers from HIG and [Private Equity Firm 3]. It was agreed by the [Silentnight Board] that these offers should deal with the ongoing funding requirements of Silentnight, the proposals for the shareholders and the proposal for dealing with the Pension Scheme. Silentnight would then consider the offer and reengage KPMG to prepare a contingency plan, if necessary.

269. On 1 February Mr Costley-Wood had a telephone call with [Silentnight Board Member 1], [Silentnight Board Member 2] and [HIG Senior Management 2] in which [HIG Senior Management 2] said that HIG could make an offer to finance a solvent compromise but would need to liaise with KPMG to ensure that the numbers worked. Mr Costley-Wood is recorded as saying that a compromise could take a long time and tPR would try to call Silentnight's "bluff" whereas in a CVA the [Silentnight Board] would be in control of the process and it did not automatically involve shares or warranties or loan notes which tPR might require in a compromise. Further if creditors increased more than HIG thought they might not want to follow the CVA route but a compromise would not be ruled out if tPR and PPF agreed in principle quickly. The suggestion by HIG to offer to finance a solvent compromise was prompted by the offer from [Private Equity Firm 3] as noted in [HIG Senior Management 2]'s email of 26 January 2011 to [HIG Senior Management 3] and [HIG Senior Management 2]'s email to [HIG Board Member 2] sent later on 2 April 2011 in which he wrote that HIG had been forced into negotiating a solvent compromise by the offer from [Private Equity Firm 3]. At this stage KPMG had been stood down by the [Silentnight Board] but Mr Costley-Wood was offering assistance and advice to HIG and raising the difficulties which might be faced in trying to achieve a solvent compromise.

270. At the beginning of February [Private Equity Firm 3] explained their offer further. In a letter dated 1 February 2011, the purpose of which was to outline the equity arrangements should a long term investment by [Private Equity Firm 3] proceed,

[Private Equity Firm 3 Employee 1] explained that [Private Equity Firm 3] would provide up to £25 million to the Silentnight Group for the purpose of repaying the Silentnight Debt and avoiding the consequences of the proposed debt sale to HIG. [Private Equity Firm 3] intended ultimately to acquire 80 percent of the shares in/or the economic value of Silentnight, 15 percent of which was to be allocated to key members of the senior management team as an appropriate incentive to maximise longer term value for all stakeholders. 20 percent of its equity would remain with the current shareholders (as opposed to 25 percent in the proposal made on 24 January 2011). The funding would be short term because of the risk of being a “connected” or “associated” party to Silentnight and so [Private Equity Firm 3] could not acquire equity immediately and risk the PPF asking for 33 percent of the equity. After the facilities had been advanced to Silentnight [Private Equity Firm 3] wanted to start discussions between [Private Equity Firm 3], management, the Trustees and tPR to develop and review proposals such that [Private Equity Firm 3] funding was converted into longer term support and provide the Group with the funding it required for turn around and growth. [Private Equity Firm 3] was willing to consider the provision of a further £10 million to drive growth in shareholder value.

271. Silentnight wrote to [Private Equity Firm 3] on 2 February 2011 seeking clarification of its offer and in particular whether they regarded some form of pension restructuring a requirement of the business and if so how did [Private Equity Firm 3] envisage the restructuring proceeding. [Private Equity Firm 3] responded by letter dated 5 February 2011. [Private Equity Firm 3] replied setting out the terms of its offer but stated that it did not consider it appropriate to discuss the options the Group had in mind in relation to the Pension Scheme without first interacting with the stakeholders. The offer, also, on the face of it, was a lesser offer of facilities of £20 million (as opposed to £25 million) and the offer to consider an additional £10 million was not repeated. [External Financial Advisor 4 Partner 1] acting for the shareholders had produced a draft of part of the letter dealing with the Pension Scheme for [Private Equity Firm 3] and had been in communication with [Private Equity Firm 3].
272. On 3 February 2011 [Private equity firm 2 Employee 1] wrote to [HIG Senior Management 2] expressing some irritation with both [Silentnight Board Member 1] and KPMG for considering and exploring the offer from [Private Equity Firm 3].
273. On 3 and 4 February 2011 KPMG and HIG corresponded over the timetable for a solvent compromise.
274. On 4 February 2011 [Private Equity Firm 3] discussed refinancing Silentnight with the Bank. It was looking for enforcement rights within the security so that if they failed to address the pension deficit, they would have the ability to enforce. The offer described by [Private Equity Firm 3] to the Bank was insufficient to decrease the level of risk to the Bank. [Bank 1 Senior Management 2] emailed [Bank 1 Senior Management 1] to the effect that had the offer been received in 2010 the Bank would

“have snapped their hand off.”. He was however becoming concerned as to the reputational risk of completing the transaction with HIG. On 4 February [Bank 1 Senior Management 2] emailed [Private Equity Firm 3 Partner] to the effect that [Private Equity Firm 3] would have the right to appoint an administrator subject to giving the Bank 60 days’ notice which was subsequently reduced to 10 days on 5 February 2011.

275. On 4 February 2011 HIG responded to Silentnight’s letter of 1 February 2011 asking, amongst other matters for it to provide details as to how it would deal with the Pension Scheme deficit. It set out its plans as Plan A as being a solvent compromise with cash and equity being given to the PPF with clearance from tPR. Plan A was HIG’s preferred route. The letter also noted that in the run up to the CVA being proposed HIG would enter into arrangements to acquire equity in Silentnight upon the compromise of the Pension Scheme becoming effective. HIG then set out what it perceived to be the challenges to Plan A including obtaining the approval of the Trustees, tPR and the PPF; the drawn out nature of the process, and the need for the Trustees to seek financial advice. The letter then set out a proposed timeline for Plan A. Under Plan A the Pension Scheme would be offered up to £5 million which would be significantly more than it would receive in an insolvency. Plan B was that participating employers in the Group all enter into CVAs and the Pension Scheme would receive the same dividend as other creditors. Formal clearance from tPR would be sought if the [Silentnight Board] were in favour of seeking it. HIG would enter into arrangements to acquire the equity upon the CVAs becoming effective. HIG would fund the CVAs to a similar extent to a solvent compromise including a cash payment of up to £5 million to the PPF and would provide up to £30 million for future expansion. A timeline was provided for the CVAs and HIG considered that the Pension Scheme’s dividend would be about £5 million. In the event of a failure of the CVAs, HIG expected administration to follow and was not the outcome which HIG wished to pursue.

276. On 5 February 2011 the Bank considered that it had reached an agreement with [Private Equity Firm 3] which would take out HIG from the picture by paying off the overdraft. Mr Costley-Wood asked [Trustee 1] what the chances were of getting a “hearing” with tPR the following week to discuss a compromise. [Trustee 1] replied that he thought the chances were high.

277. On 6 February 2011 HIG wrote a strongly worded letter to the [Silentnight Board] emphasising their duty to act in accordance with their fiduciary duties and their duty to creditors and urging them to engage with HIG.

278. On 7 February 2011 at a meeting of the [Silentnight Board], the [Silentnight Board] decided to accept the [Private Equity Firm 3] offer over HIG’s offer. It did so on the basis that the [Private Equity Firm 3] offer was an offer to provide short term finance to pay off the overdraft whereas HIG would become Silentnight’s creditor holding the

amount due on the overdraft. Further the HIG offer would consign the Pension Scheme to the PPF whereas the [Private Equity Firm 3] offer gave Silentnight more time to approach the Trustees to agree a compromise and the prospect of avoiding an insolvency. On the same day [External Financial Advisor 4 Partner 1] had a conversation with [Senior Advisor at tPR] to discuss the position. [External Financial Advisor 4 Partner 1]'s note of the conversation (prepared in advance of the conversation) recorded that HIG had told the shareholders on 21 January 2011 at their meeting that HIG proposed to use a CVA to restructure the Silentnight group provided the shareholders cooperated, and that if they did not, Silentnight would be placed in administration. HIG also had informed the shareholders that Silentnight was being advised by KPMG who did not report to HIG. The note also recorded that [External Financial Advisor 4 Partner 1] proposed to tell [Senior Advisor at tPR] that [External Financial Advisor 4] had previously advised the shareholders that the status quo with the Pension Scheme was an impediment to raising additional funds and that [Private Equity Firm 3] wanted to consider options relating to the Pension Scheme as the [Private Equity Firm 3] facilities were offered on the basis that they were short term. TPR's note of the conversation records [External Financial Advisor 4 Partner 1] as using the expression "insolvency process" and then stating that [Private Equity Firm 3] had stepped in to avoid immediate insolvency and would speak to the shareholders and Trustees to obtain the best outcome for the Pension Scheme and Silentnight as "they want to avoid administration". [Private Equity Firm 3 Partner] said in evidence that his understanding was that HIG was planning to put Silentnight into administration and sell the business through a pre-pack and that was the basis of his conversation with tPR.

279. On 7 February 2011 Mr Costley-Wood emailed his team to the effect that they were stood down as Silentnight was to accept 3 months facilities from [Private Equity Firm 3]. HIG had been informed and he would call [HIG Senior Management 2] for his reaction. He had told [Silentnight Board Member 1] that KPMG was happy to work with [Private Equity Firm 3] and Silentnight on a PPF compromise or act for the Trustees. He also understood that [HIG's External solicitors] were holding an internal review as to "how" the Debt Sale Agreement did not contain a provision to prevent what had occurred.

280. On 8 February 2011 the Trustees had a conference call attended by [Trustee 1] who informed the Trustees that Silentnight had decided to go with [Private Equity Firm 3] and that Silentnight would have a period of grace to allow [Private Equity Firm 3] to evaluate Silentnight. [Trustee 1] noted that [Private Equity Firm 3] might be able to force Silentnight into insolvency by making Silentnight reliant on it for credit facilities and then withdrawing the facilities at short notice. [Trustee 1] had also spoken to tPR who indicated that they had been aware for some time that "this situation" might arise with Silentnight and that they had spoken to [Private Equity Firm 3] on 7 February 2011. TPR had expressed concern about the "loan to own" process and asked to be kept informed as to what action [Private Equity Firm 3] proposed. [Trustee 1]

considered that tPR might consider a PPF+ compromise solution and that a compromise which offered better than PPF benefits would likely be the best option for the Scheme's members. He also reported a conversation – as he had understood it - with Mr Costley-Wood to the effect that KPMG had been acting for HIG and so were unlikely to be involved going forward.

281. In the afternoon of 8 February 2011 [HIG Senior Management 2] wrote to [HIG Senior Management 1] to brief him on the position with Silentnight. He described the offer by [Private Equity Firm 3] as one which provided bridging finance to Silentnight for 6 months and he believed that the [Private Equity Firm 3] plan was ultimately to place Silentnight into administration. [HIG Senior Management 2] thought that the shareholders had somehow pressurised the [Silentnight Board] to accept the [Private Equity Firm 3] offer and in doing so “chose to ignore the advice of [Silentnight's] advisors KPMG to go with the HIG plan.”.

282. However, on 8 February [Private Equity Firm 3] decided not to proceed with the deal with Silentnight as the risk to reward profile was unattractive. [Private Equity Firm 3]'s decision does not appear to have been communicated to Silentnight that day but on 9 February.

283. In the evening of 8 February [Silentnight Board Member 5] heard that [Private Equity Firm 3] had run into difficulties with the Bank on the terms of the CID facility and the cash guarantee and Silentnight might have to revert to HIG for financial backing. Also that evening [HIG Senior Management 2] heard that [Private Equity Firm 3] had offered a mixture of 3 month and on demand money and that they would present themselves to tPR as a “white knight”. [HIG Senior Management 3] suggested that HIG offer to extend the facility by 6 months. Mr Costley-Wood heard that HIG might be improving its offer and emailed [HIG Senior Management 2] of [Silentnight Law Firm 1] that he had his fingers crossed.

284. HIG decided to offer to extend the overdraft facility in order to better the [Private Equity Firm 3] offer. The improved offer made by letter dated 9 February 2011 raised the overdraft limit to £10 million which was based on the £7.5 million referred to in the Project Bale Report to be management's expectation of the future requirement together with additional headroom unforeseen requirements and to give Silentnight time to find a solution to the Pension Scheme Deficit. The facility would be available for an initial period of 6 months and on the same terms as the existing facility. In addition the interim repayments due on the Term Loan would be deferred to the expiry of the Term Loan in November 2011.

285. The letter was forwarded to Mr Costley-Wood by [HIG Senior Management 2] who noted that he “would be interested to see how the new pension Trustee would view this”. Mr Costley-Wood replied that he “would say the [Silentnight Board] seriously risk an action against them personally by the regulator under his moral hazard

provisions if they ignore this offer to the pension scheme when it is clearly superior to the other one. Equally, I don't think signing a 3month facility, particularly when it is silent about how it deals with the largest creditor, removes the risk of insolvency and [Silentnight Law firm 2 Employee 1] needs to be robust that the duty [to] creditors remains.". Subsequently Mr Costley-Wood emailed [HIG Senior Management 2] that "you could say you will match and exceed any genuine offer made to the regulator by [Private Equity Firm 3] suitably caveated. Also if the [Silentnight Board] have had a chat with [tPR] about a compromise then they should not be taking directions from the shareholders anymore.". Later that day he emailed [HIG Senior Management 3] to ask how the project was looking and subsequently to say that if there was anything he could do [HIG Senior Management 3] should let him know and later still, at 22:17 he emailed [HIG Senior Management 2] "I will speak to [Silentnight Board Member 1] in the morning but anything I can do let me know, You can't let a small fund like [Private Equity Firm 3] steal one of your deals.". Shortly afterwards [HIG Senior Management 2] informed him that [Private Equity Firm 3] had backed out.

286. There was further email contact between Mr Costley-Wood and [Partner at Silentnight Law firm 1]. On 10 February 2011 Mr Costley-Wood forwarded [HIG Senior Management 2]'s email (informing him that [Private Equity Firm 3] had withdrawn) to her and she replied that she was holding her breath as well as crossing everything. Mr Costley-Wood joked that he was "going to buy [External Financial Advisor 4 Partner 1] some SN vouchers to help him sleep at night (in lieu of a fee)". Subsequently on 10 January 2011 he emailed [HIG Senior Management 2] congratulating him on a "great result".

287. On 10 February 2011 the [Silentnight Board] met and it was resolved that the revised HIG offer was a better offer for Silentnight. It was noted that the 6 month overdraft facility was repayable on demand. The [Private Equity Firm 3] offer had been withdrawn and the HIG offer was the only offer open to Silentnight and whatever Silentnight decided HIG would own the Silentnight Debt on 14 February 2011. Accordingly, the [Silentnight Board] acknowledged that Silentnight would pursue the HIG offer.

288. Later on 10 February 2011 Mr Costley-Wood emailed [HIG Senior Management 3] noting that if Silentnight has £10 million for 6 months there was a risk the burning platform would be partially extinguished so that any pension deal would take longer. He followed up that email with another stating that he was going to have a think about the "flip" from solvent to CVA. "On reflection even if the regulators demands were unreasonable it was quite an aggressive step to cancel an overdraft just because it was on demand when by their very nature all overdrafts are on demand. Other triggers might help.". [HIG Senior Management 3] responded that that was what he had been thinking as well and that that might increase the risk of a contribution notice.

289. On 10 February 2011 HIG and Silentnight Holdings Limited, Silentnight Group Limited, and ABF Limited entered into an exclusivity agreement in relation to the sale of shares or business of the companies.
290. On 11 February 2011 Mr Costley-Wood emailed colleagues at KPMG to the effect that HIG controlled Silentnight as it had taken an assignment of the Silentnight Debt.
291. On 12 February HIG Snooze Newco Ltd (“HIG Snooze”) and the shareholders signed a Conditional Sale Agreement for the shares in Silentnight Holdings Limited.
292. On 12 February 2011 Grace Bay entered into an agreement with Silentnight providing Silentnight with £10 million working capital facility repayable on demand and in any event at the end of 6 months. HIG allegedly applied pressure on the shareholders and Silentnight to enter into the Conditional Sale Agreement and the facility agreement with the threat of administration if they were not signed.
293. On 12 February 2011 [HIG Senior Management 2] emailed Mr Costley-Wood that HIG had finally completed on the Sale Agreement referring to the assignment of the Silentnight Debt and added “Thanks for your advice. Now onto part 3!”. Mr Costley-Wood emailed [KPMG Employee 9] saying “your referral is safe after all” and [KPMG Employee 9] replied that “your place in the starting line-up is safe”. Mr Costley-Wood replied to [HIG Senior Management 2]’s email “Fantastic. Great result Mark. We will get in front of the trustees next week. Regards, David. PS In the meantime I will try to resist sending [External Financial Advisor 4 Partner 1] some bed vouchers.”.
294. On 14 February 2011 Mr Costley-Wood completed the “Restructuring Engagement Acceptance Questionnaire” noting that the expected fee was likely to exceed £250,000.
295. On 14 February 2011 there was a telephone call between [Silentnight Board Member 1] , Mr Costley-Wood, [KPMG Employee 5] and [Partner at Silentnight Law firm 1]. In relation to a solvent compromise it was mentioned that HIG thought it might take too long. [Silentnight Board Member 1] stated that a solvent compromise was better for Silentnight and asked whether Silentnight could ask HIG for a grace period, i.e., an amount of time to try to seek a compromise during which HIG would not demand repayment. Mr Costley-Wood told him that he thought a 6 week period was appropriate, and Mr Costley-Wood ended the call under the impression that Silentnight would request a 6 week grace period to enable it to try and negotiate a solvent compromise with the Trustees; if a compromise was not agreed Silentnight would consider a CVA. KPMG would need to look at a full CVA compared to a compromise, and a pension scheme CVA was untested. He thought TPR might demand 10 percent of the equity.

296. On 15 February 2011 [Silentnight Board Member 1] emailed Mr Costley-Wood to the effect that Silentnight's annual accounts were due to be released in late April or early May 2011. If a deal was not done with the Trustees by that time Silentnight's options would include additional disclosure to the going concern statement or they would need to be filed later than normal in which case Silentnight risked alerting the wider community including trade insurers as to its financial position which in itself might create a burning platform.
297. On 16 February [Trustee 1] emailed the other Trustees noting that [External Financial Advisor 2] would be acting for HIG and that he had had a number of informal discussions with tPR who were concerned at venture capital companies working with other companies to remove pension schemes. TPR were keeping a close eye on Silentnight.
298. On 16 February 2011 [HIG Senior Management 2] set about arranging a meeting for Mr Costley-Wood to update HIG and [HIG's External solicitors] on progress with a CVA. [HIG Senior Management 2] set out the agenda for the meeting which included the method by which Silentnight and HIG could convince tPR that there was a burning platform now that Silentnight had 6 month money and tPR might not be inclined to respond quickly. HIG had the option "to push him hard and hope he works in step or alternatively, giving [Silentnight] a deadline within the next couple of weeks.". Mr Costley-Wood responded "As stated last week, confirming to [Silentnight] that you will not demand for six months will elongate the pension process and actually risk the company being able to survive without the facility from August onwards due to cash generation in the next six months. Thus in reality the timetable could get pushed out to the end of Nov when the loan fee triggers. That's a long time with no control of the business. Also the regulator will be suspicious with HIG having been in place for an extended period rather than coming in as a white knight allowing a consensual restructure and avoiding administration following [the Bank's] overdraft termination. The alternative is to provide a short fixed period to allow [Silentnight Board] to restructure while they need an overdraft and while there is momentum especially with the [T]rustees. This is what the [Silentnight Board] are expecting but assumes the overdraft has been set up as literally on demand without requiring a formal breach.". As noted above, a 6 week period had been suggested by Mr Costley-Wood in the telephone call held on 14 January 2011 with [Silentnight Board Member 1] .
299. On 16 February 2011:
- 299.1. There was a meeting between Mr Costley-Wood (and others from KPMG) and [Silentnight Board Member 1, Silentnight Board Member 3, and Silentnight Board Member 2]. [Silentnight Board Member 1] explained that the facility (including the £10 million revolving credit facility) was on demand and no default was required. Mr Costley-Wood pointed out that for a "drop-in "there needed to

be an agreement by the end of March and the papers for a CVA needed to be ready by early April. The compromise had the benefit of less adverse public relations for tPR and would help the business. Silentnight operated “just in time” and could not afford disruption to the supply chain.

299.2. [KPMG Employee 10] supplied HIG with the workings which supported the working capital analysis which would be included in KPMG’s up dated Project Bale Report and were based on work that [HIG Employee 3, Silentnight Board Member 1 and KPMG Employee 10] which had previously been carried out. The update had been prepared at a meeting that day attended by Mr Costley-Wood and [Silentnight Board Member 1] at Silentnight and [Silentnight Board Member 1] wanted them shared with HIG who would be funding the additional capital requirements.

300. On 18 February 2011:

300.1. Mr Costley-Wood spoke to [Trustee 1]. Rumours of a restructuring were spreading amongst employees and [Silentnight Board Member 1] was very concerned that suppliers and creditors would get to hear of them. [Silentnight Board Member 1] wanted to act quickly and wanted to know how quickly a compromise deal could be reached. Mr Costley-Wood mentioned that there had been “very limited” discussions with HIG and he proposed to discuss with HIG the comparison between a compromise and a CVA route. Mr Costley-Wood would try to reach an April deadline with HIG but thought they might want a shorter period. Mr Costley-Wood explained that by compromise he was referring to a solvent compromise or potentially a longer term solution. The CVA would be an all creditors CVA. Management preferred the compromise solution. [Trustee 1] told Mr Costley-Wood that calling a CVA without due prior discussion with the Trustees or without allowing adequate time for full assessment would be viewed as an aggressive act and was very unlikely to elicit a positive response – and would also be viewed unfavourably by the regulator. It would probably fail and the [Silentnight Board] would be at risk given tPR’s powers.

300.2. KPMG produced an updated Project Bale Report. It noted that administration remained an option but was not in the best interests of the Group’s stakeholders and the main options were a solvent compromise with the PPF, a CVA which sought to compromise the Pension Scheme only and a CVA which sought to compromise all creditors. The Report commented on the merits of the main options. In relation to a solvent compromise it noted that the procedure could be lengthy as the PPF might request loan notes, warranties and an equity stake, but had the merit of little operational disruption as trade creditors would be unaware of it. A Scheme only CVA incurred the risk of some creditor disruption but that should be manageable as trade creditors would not be affected. KPMG would not recommend an all creditors CVA unless appropriate funds were made available to support supplier ransom payments which together with delayed customer receipts

were estimated at between £4.5 and £7.7 million in the first two months of the CVA. Rejection of the proposal would result in administration. An all creditors CVA incurred the greatest risk of disruption to the supply chain and could damage the brand value. As 75 per cent of the creditors needed to approve the CVA, the PPF would, in effect, have the casting vote. Rejection of the proposal would result in administration.

301. The Project Bale report noted that the Group's cash flow position remained precarious and whilst HIG had indicated its support, for this to continue the Group needed to implement a restructure.
302. On 18 February 2011 [HIG's External solicitors] sent [HIG Senior Management 2] a draft timetable for a compromise or CVA scheduled to complete just before the facilities were due to expire in 6 months. [HIG's External solicitors] noted that as previously discussed the "burning platform still exists albeit the new facility has been granted by HIG to give the group more time to pursue Plan A (i.e., the solvent solution)". [HIG's External solicitors] noted that the draft timetable was consistent with the non-binding offer set out in HIG's letter dated 9 February 2011 and suggested it should be sent to Mr Costley-Wood for his comments. [HIG Senior Management 2] responded that HIG was considering Plan A but Plan B was more likely.
303. On 19 February 2011 [Trustee 1] emailed the other Trustees informing them that he had been told that tPR classified the Pension Scheme as a "as a potential avoidance case and has been allocated a very senior representative . . . The Regulator has said that it is very likely to issue HIG with a warning (essentially a letter saying they are watching and setting out the regulator's powers) in an attempt to ensure they act appropriately in relation to the pension scheme."
304. On 22 February 2011 at a meeting attended by Mr Costley-Wood, [Silentnight Board Member 1, HIG Senior Management 2, Partner at Silentnight Law firm 1 and HIG's External solicitors], HIG informed the meeting that HIG had offered Silentnight 6 weeks to agree a deal with tPR. If a compromise was not agreed in principle by 31 March 2011, the CVA proposal would be sent out. If the compromise was not implemented by the end of May a CVA proposal would be sent out.

Determination on Allegation 1

The period 16 August 2010 to 14 January 2011

305. The principle of objectivity imposed an obligation on the Respondents "not to compromise their professional or business judgment because of bias, conflict of interest or the undue influence of others": Fundamental principle (b). Section 220.1 of the Code identifies as an example of a threat to objectivity the case where the professional accountant performs services for clients whose interests are in conflict.

306. Throughout this period the interests of Silentnight and HIG were in conflict as HIG was considering creating an insolvency event by making a demand under the Silentnight Debt if it acquired it, or acquiring the Silentnight Debt under an agreement which provided for the Bank to terminate the overdraft facility, or making a demand under any substitute facility which it provided so as to create a liquidity crisis, so as to create a burning platform, in circumstances where no such burning platform existed or would exist without the assignment, and then in reliance on the burning platform, seek to persuade the PPF and tPR that the PPF should assume the responsibility for the Pension Scheme as part of a solvent compromise or CVA. Further the Respondents were aware that the PPF might not accept the Pension Scheme or vote in favour of CVA if it was aware that HIG had acquired the Silentnight Debt as part of an arrangement to dump the Pension Scheme on the PPF if the burning platform had been engineered and that tPR would not give its consent to a solvent compromise or CVA but might use its moral hazard powers.

307. At all times during this period Mr Costley-Wood knew that HIG intended to proceed as described above. Mr Costley-Wood did not consider that there was any “burning platform” other than that created in the context of the Debt Sale Agreement by HIG acquiring the Silentnight Debt which it did on 12 January 2011. He had made no independent financial investigation into Silentnight’s financial affairs and had been informed by [Silentnight Board Member 1] that Silentnight had the support of its bankers and could continue to pay its debts as they fell due. Albeit he had referred briefly to a solvent compromise at the meeting held on 16 August 2010 he proceeded throughout this period on the basis that Silentnight’s only options were a CVA or administration. He did not consider whether there were any other options but participated in Silentnight’s and HIG’s preparations for a CVA (failing which, he understood Silentnight would be placed into administration). The draft scope of work KPMG sent to Silentnight on 20 August 2010 had referred to KPMG acquiring an understanding of Silentnight’s financial position and an assessment of its options available to the company including the benefits and risks of each – presumably because KPMG needed to acquire an understanding of Silentnight’s financial position before advising Silentnight on its options.

308. Mr Costley-Wood appears to have gone along with [Silentnight Board Member 1] and [Silentnight Board Member 3]’s (and possibly) [Silentnight Board Member 2]’s desire to see Silentnight free of the Pension Scheme through a CVA or administration (if the CVA failed), and to deal with HIG, without questioning whether the fulfilment of their wish was appropriate. He could have insisted on the retainer being signed (so that he could carry out an option review) or stated that he could not act as he was not in a position to advise whether a CVA was in the interests of Silentnight. Instead Mr Costley-Wood and KPMG appear to have proceeded on the basis that it could advise both Silentnight and HIG as it stated in its document entitled Silentnight Holdings Limited proposal 3 September 2010 which was sent to both [Silentnight Board

Member 1] and HIG. By 6 September 2010 he described KPMG as having pitched to carry out a CVA.

309. The Respondents advised and or assisted HIG:

309.1. On 26 October 2010 he advised [HIG Senior Management 2] to the effect that if there was a conflict between a shareholder and a creditor in approving a CVA he did not consider that a CVA could be used to force a share sale;

309.2. On 25 November 2010 in relation to procedural and other matters;

309.3. KPMG arranged a workshop in early December at which various issues relating to a CVA of Silentnight were discussed including Silentnight's requirements for capital and a procedural timetable;

309.4. On 2 and 6 December he advised on Silentnight's cash flow requirements during a CVA and [KPMG Employee 10] advised further on 8 December;

309.5. On 14 December Mr Costley-wood advised on the manner in which a debit on Silentnight's overdraft should be dealt with and on Silentnight's working capital requirements. He also advised on the manner in which a share purchase and transfer should be effected;

309.6. On 15 December and 16 December Mr Costley-Wood advised HIG on Silentnight's working capital requirements;

309.7. On about 20 December Mr Costley-Wood advised on the impact of the withdrawal of facilities from Silentnight in the event of a CVA or administration;

309.8. On 10 January 2011 he advised HIG on whether other funds could intervene in an administration to HIG's disadvantage.

310. On 21 November 2010 Mr Costley-Wood encouraged HIG in its endeavours to acquire Silentnight.

311. Mr Costley-Wood did not at any time during this period resist HIG's requests for advice or assistance but by providing advice and assistance encouraged HIG in its efforts to acquire Silentnight. He acted in this way because he failed to consider the conflict of interest between Silentnight and HIG, and consider Silentnight's interests alone. It is also noteworthy that HIG considered it could turn to KPMG for advice when it wanted advice.

The period 14 January 2011 to 31 March 2011

312. By 14 January 2011 KPMG had been advising both Silentnight and HIG for some time (since at least the latter half of August 2010) and had become committed to a CVA as being a solution to Silentnight's financial problems and Mr Costley-Wood expected and hoped to be appointed to manage or supervise a CVA or if that failed,

to be appointed administrator. There is no evidence that KPMG considered whether there was any threat to its objectivity arising from its interchanges with HIG prior to 14 January 2011 or that Silentnight's and HIG's interests might conflict as provided in section 220.1 of the Code. As noted above, the Restructuring Engagement Acceptance Questionnaires of 21 December 2010 and 14 January 2011 made no reference to HIG. The Code provides substantial guidance on identifying threats to compliance or with fundamental principles and suggests safeguards to eliminate or mitigate such threats. As there was no consideration of any threat to compliance, there was no consideration of any safeguards to mitigate any threat to objectivity as suggested in the Code.

313. In our opinion Mr Costley-Wood demonstrated a lack of objectivity in favouring the HIG offer over the [Private Equity Firm 3] offer. He was aware that the [Silentnight Board] wished to pursue both the [Private Equity Firm 3] and HIG offers from the board meeting held on 31 January 2011 and yet continued a dialogue with HIG. On 7 February 2011 he had been informed that Silentnight had accepted the offer from [Private Equity Firm 3] and acknowledged that KPMG had been stood down, and appeared to regret that the [Private Equity Firm 3] offer had been accepted, noting that [HIG's External solicitors] were holding an internal review as to the structure of the Debt Sale Agreement which had allowed [Private Equity Firm 3] to intervene.

314. On 9 February 2011 when he heard that HIG might be improving its offer he hoped that it would do and when he received the offer he encouraged HIG by sending an email to [HIG Senior Management 2] that he considered that the [Silentnight Board] would have to consider it as it was clearly superior to the offer of [Private Equity Firm 3]. He also advised HIG to state that HIG would match any offer made by [Private Equity Firm 3] to the regulator and added that the [Silentnight Board] should not be taking any directions from the shareholders any longer. He invited HIG to let him know if there was anything he could do to assist and that HIG should not let a small fund like [Private Equity Firm 3] steal one of HIG's deals. He did not suggest to Silentnight or [Private Equity Firm 3] that [Private Equity Firm 3] might wish to improve its offer at any time. The emails from Mr Costley-Wood sent on 9 February 2011 demonstrated a partiality by Mr Costley-Wood in favour of HIG and its offer. The [Private Equity Firm 3] offer was withdrawn (as [Private Equity Firm 3] considered that the transaction was not in its interests) shortly before Mr Costley - Wood's emails (albeit he was unaware of the withdrawal) but that is not in point. Both Mr Murphy and Mr Shaw were agreed that an IP/RA would have attempted to engineer competing offers from [Private Equity Firm 3] and HIG but Mr Costley-Wood's approach in the emails of 9 February 2011 do not suggest that he was doing so. There was nothing in the [Private Equity Firm 3] offer or about [Private Equity Firm 3]'s financial circumstances which suggested that an [Private Equity Firm 3] offer should have been disregarded and Mr Costley-Wood had no basis for believing, until he was aware that [Private Equity Firm 3] had withdrawn its offer, that [Private

Equity Firm 3] might not improve its offer. He himself had originally approached [Private Equity Firm 3] in 2010 and the Project Bale Report of 31 January 2011 noted that [Private Equity Firm 3] could refinance Silentnight's business prior to 14 February 2011. Mr Costley-Wood's email of 9 February 2011 congratulating [HIG Senior Management 2] on a "great result" was consistent with him favouring HIG over [Private Equity Firm 3] .

315. The Executive Counsel also relies on the Respondent's conduct as set out in respect of allegations 2 and 3 in respect of Allegation 1. Insofar as the Executive Counsel relies on communications set out under Allegation 2 which we hold to be misleading, those communications demonstrate a lack of objectivity, as they demonstrate that Mr Costley-Wood was prepared to associate himself with material or statements that were misleading in order to assist HIG.
316. A further issue arises as to the "grace period" to be given by HIG to Silentnight to negotiate a solvent compromise to restructure the Pension Scheme. The Pension Scheme liability under the Deficit Recovery Plan posed no immediate threat to the solvency of Silentnight and there was no pressing need to restructure the Pension Scheme in 2011. What was required was a restructure of the Term Loan or some external funding to resolve the Term loan and Exit Fee. Accordingly there was no need to preserve a situation where Silentnight would become insolvent in March or April 2011. If financing for repayment of the Term Loan and Exit fee (or a restructuring) could not be procured then the burning platform might have existed on 30 November 2011.
317. As noted above the 6 week period arose as a result of a discussion between [Silentnight Board Member 1] and Mr Costley-Wood in which Mr Costley-Wood advised that it would be appropriate to ask HIG for a 6 week grace period to negotiate a solvent compromise. He had been aware from the meeting held on 16 August 2010 that HIG's reluctance to explore a solvent compromise stemmed from the time it would take. Further the Project Bale Report commented on the time that a solvent compromise would take. On 16 February 2011 Mr Costley-Wood advised HIG that a six month period would "elongate the pension process" leading to a risk that Silentnight might remain solvent after the expiry of the six month facility offered by HIG until 30 November 2011 when repayment of the Term Loan and payment of the Exit Fee was due. The email was in response to one from [HIG Senior Management 2] addressed to [HIG's External solicitors] raising the question how "we convince the regulator that there is a burning platform i.e. [Silentnight] now has 6mth money (albeit "on demand") so he'll be inclined not to respond quite so fast.". A six month period would have been in the interests of Silentnight as it would have been provided additional time to pursue other financing or restructuring options with or without the participation of the Trustees. It had been [Silentnight Board Member 1]'s long standing strategy to examine financing options after the financial results for January 2011 were known and that would have left a substantial amount of time to consider a

refinancing and a restructuring or a consensual compromise with the PPF. What appears to have motivated Mr Costley-Wood in suggesting a period shorter than 6 months was HIG's own interest in having control over the business and the perception of the regulator as to HIG's involvement with Silentnight for an extended period rather than appearing as a white knight to rescue Silentnight as set out in his email to [HIG Senior Management 2] of 16 February 2011. We note that in his May 2011 note attached to his email sent on 8 June 2011 (and produced after the hearing) Mr Costley-Wood wrote that the Trustees voted for the CVA and the PPF against because they could not agree in the timescale whether the Pension Scheme was eligible to enter the PPF.

318. In our opinion the exchange over the Grace Period demonstrated a further lack of objectivity by Mr Costley-Wood. His suggestion favoured HIG's interests over those of Silentnight and resulted in a severely curtailed period for negotiations with the PPF.

Self-interest and familiarity from 16 August 2010 to 31 March 2011.

319. Further the relationship between KPMG and HIG was such that it affected or might reasonably have been perceived to affect the Respondents duty to act in the interests of Silentnight through self-interest and familiarity. KPMG had been trying to build a relationship with HIG since 2009 and HIG was an attractive client with the ability to provide KPMG with additional work. Mr Costley-Wood took care to ensure that he treated HIG with considerable respect. On 18 August 2010 when he asked [KPMG Employee 6] to start compliance he noted that Silentnight was an introduction from HIG Capital. He checked with [HIG Senior Management 2] in August 2010 that it was in order for KPMG to contract with Silentnight in case [HIG Senior Management 2] had an objection and he suggested that Silentnight also check if HIG had any objection to Silentnight retaining KPMG to check on feasibility. When he emailed [KPMG Employee 4] on 8 September 2010 to the effect that KPMG was likely to contract with Silentnight he put forward as a reason that if KPMG contracted with HIG that that "might spoil negotiations with" tPR. He remained conscious of the importance of the potential relationship of HIG to KPMG throughout both periods. On 9 February 2011 [HIG Senior Management 2] emailed Mr Costley-Wood to the effect that it looked like "we're nearly there" as he had discovered that [Private Equity Firm 3] had withdrawn its offer. Mr Costley-Wood forwarded the email to [KPMG Employee 9] and others with the comment that "[Y]our referral is safe after all."

320. Furthermore by 14 January 2011 KPMG had been advising or assisting HIG for a considerable period going back to June 2010, but in particular after 16 August 2010, and had been involved with assisting them in planning a CVA, had given some advice on how to structure the acquisition of the shares in Silentnight and encouraged HIG to acquire Silentnight. It would have been difficult for KPMG to advise Silentnight that a CVA was not the appropriate course to take. It was HIG that suggested a solvent

compromise should be attempted in response to the offer from [Private Equity Firm 3].

321. Consistent with a possible wish to nurture HIG as a client, Mr Costley-Wood then proffered advice as to how HIG might beat [Private Equity Firm 3]’s offer and how it should curtail the grace period to 6 weeks so that it was not out of control of Silentnight’s business for a long period.
322. The Executive Counsel also relies on the Respondents’ desire to earn fees from Mr Costley-Wood’s potential role as a nominee or supervisor of a CVA, estimated at £700,000, or £2,000,000 from acting as an administrator. It is clear that Mr Costley-Wood wished to act for Silentnight and he perceived that there were rival insolvency practitioners available depending on how the arrangements for Silentnight progressed, someone from [External Financial Advisor 3] in the case administration was adopted at the August meeting, and possibly [External Financial Advisor 4 Partner 1] if the [Private Equity Firm 3] offer succeeded, the Tribunal considers that the desire to obtain the appointment was a motivating factor for Mr Costley-Wood (but not improperly so) but the self-interest motivating factor was the desire to keep HIG onside as a potential client. We note that on 10 May 2011 an email was sent by [KPMG Employee 1] to the effect that Mr Costley-Wood had started to explore the opportunity of post-sale work for HIG Snooze and HIG Snooze Newco II Ltd which had acquired the Silentnight business in administration. The emails were supplied after the hearing. We note that they are consistent with a desire to develop an relationship with HIG.

Identification, evaluation and safeguards against threats to objectivity

323. The Respondents were obliged to evaluate any threats to objectivity as provided by paragraph 100.6 of the Code. No threats were identified in the first period as Mr Costley-Wood did not see himself in a situation where his duty to Silentnight might conflict with his duty to HIG even where [HIG Senior Management 2] stated that he would be relying on Mr Costley-Wood for advice in relation to a CVA. There is no evidence that there was any evaluation of threats to objectivity in the second period. Accordingly, it is not surprising that there was no attempt to put in place any safeguards in accordance with paragraph 100 of the Code – even if such safeguards existed in the light of the extent of the conflict of interest between Silentnight and HIG.
324. There was a delay in formalising the engagement of Silentnight from 20 August 2010 to 14 January 2011. That was due to the attitude of Silentnight and the advice it received to delay signing the engagement. Nonetheless that should not have prevented KPMG identifying – formally – Silentnight as a client whilst it gave it ad hoc advice. The danger was foreseeable; if the feasibility study into options was delayed until the

Silentnight Debt was assigned to HIG then some of the options previously available might no longer be available or might be restricted. In fact the procedures within KPMG which were intended to assist in the provision of safeguards were not complied with. Thus the Sentinel Request dated 16 December 2010 was not properly completed as it omitted to refer to HIG in the space for the identities of any other parties connected to the engagement. That might not have mattered as HIG had been entered on the Sentinel Form dated 20 August 2010. The Engagement Acceptance Questionnaire dated 13 January 2011 was incorrectly completed. It made no reference to HIG under the reference for other involved parties, there was no reference to HIG in response to the question relating to third party involvement, no “independence impairs” were recorded and no risks to objectivity were identified. The Restructuring Engagement Acceptance Questionnaires dated 14 January and 14 February 2011 also omitted to refer to HIG as they did not refer to the Respondents’ prior relationship or dealings with HIG over the past 6 months. Similarly the KPMG Restructuring Risk Management Panel had to review an online form and give their approval to the restructuring engagement involving Silentnight. Once again the reference to HIG was omitted. The questionnaires should have referred to the de facto retainer by Silentnight and the fact that fees of £45,000 in respect of 104 chargeable hours had been incurred. Albeit only the Engagement Acceptance Questionnaire dated 14 January 2011 is pleaded they are evidence that what is pleaded, that the Respondents failed to identify and evaluate threats to their objectivity during the period 16 August 2010 to 31 March 2011, is correct.

325. We conclude in relation to Allegation 1 that the Respondents conduct amounted to Misconduct within the definition of Misconduct as expounded in the MG Rover case (FRC Executive Counsel v Deloitte and Einollahi) (set out above). The conduct of the Respondents fell significantly short of the standards to be expected of a Member or Member Firm and further was likely to bring discredit to the Member or Member Firm or to the accountancy profession.

Allegation 2.

326. Allegation 2 is that the Respondents knowingly or recklessly assisted with the provision of untrue and/or misleading and/or materially incomplete explanations to the PPF, tPR, Silentnight and the Trustees regarding the causes of Silentnight’s financial difficulties and HIG’s involvement as an alleged “white knight” in relation to Silentnight, in breach of the Fundamental Principal (a) Integrity, and section 110 of the Code. The allegation concerns eight statements which fall into three categories:

326.1. Written statements made by HIG on 28 February 2011 to Silentnight, on 28 March 2011 to tPR and 4 April 2011 to Silentnight;

326.2. Written statements made by Silentnight (on 10 March 2011 to the PPF, tPR and the trustees, on 9 March 2011 to the Trustees and 31 March 2011 to the PPF; and

326.3. Oral statements allegedly made by HIG, Silentnight and HIG’s solicitors to the PPF, tPR and the Trustees at a meeting held on 30 March 2011.

327. Mr Costley-Wood understood that HIG wanted Silentnight to relieve itself of the pension liability by persuading the PPF to accept the Pension Scheme with the approval of tPR and to do so as cheaply as possible. There was a brief time in February 2011 where there were discussions about a PPF+ compromise with the Trustees but those discussion did not succeed. In order for the PPF, tPR, and the Trustees to be persuaded that the PPF should assume the Pension Scheme it was necessary that they should understand the cause of Silentnight's difficulties and the reason why there was a burning platform.
328. From mid-February to March there were negotiations for a solvent compromise which was Silentnight's and – ostensibly - HIG's preferred option. At the heart of the negotiation was the nature and extent of the consideration which Silentnight would offer to the Pension Scheme in exchange for Silentnight's liability to the Pension Scheme being transferred to the PPF. Albeit Silentnight (advised by the Respondents) and the Trustees were the parties to the negotiations Silentnight depended on HIG as HIG would provide the funds and equity for a compromise and in the case of the Trustees, they required the approval of tPR and the PPF. HIG also wanted the approval of tPR because such approval would rule out contribution proceedings instituted by tPR .
329. As noted above, Mr Costley-Wood had been aware from at least 16 August 2010 that HIG intended to acquire Silentnight or its business in circumstances where it became free of its liability to the Pension Scheme and that in order to deal with the PPF, whether as a negotiated compromise or through a CVA, there needed to be a "burning platform". Further Mr Costley-Wood was aware that at the end of 2010 Silentnight was not facing a burning platform and that a burning platform would be created as a result of the acquisition by HIG of the overdraft and Term Loan which were being acquired at the instigation of HIG. By mid-February he knew that the Bank had cancelled the overdraft facility pursuant to the terms of the Debt Sale Agreement and that that facility had been replaced by Grace Bay offering a six month finance revolving credit facility for 6 months repayable on demand. By late February he was aware that HIG had indicated that it would not make a demand for 6 weeks so as to enable a compromise to be negotiated with the Trustees, PPF and tPR and that he himself had suggested the 6 week period to ensure that there was a burning platform in the first quarter of 2011. He himself considered that it was the Debt Sale Agreement and the cancellation of the overdraft in that context, which created the burning platform as he stated in an internal KPMG email sent on 16 May 2011 and did not suggest otherwise in 2010 or 2011.
330. On 23 February 2011 the Trustees held a meeting attended in part by [Silentnight Board Member 1] and [KPMG Employee 10]. The Trustees were informed that Silentnight's focus was on a solvent compromise. HIG had offered to transfer £3 million to the Pension Scheme in the context of a compromise. The Trustees

indicated that they would not consider such a proposal without considering all the other options available. In the course of the meeting [Trustee 1] warned that he expected tPR/PPF to demand further information, in due course, to ensure that recent events and the proposed solution had not effectively been contrived to prejudice the pension scheme and secure the company cheaply. [Trustee 1] pointed out that any CVA would require approval from the PPF and would be voted down at the sort of level of contribution that was being mentioned, i.e., £3 million.

331. On 25 February 2011 [HIG Senior Management 2] emailed [HIG Employee 1] to the effect that HIG had been forced to look at a solvent compromise as [Private Equity Firm 3] had “pre-wired” tPR and the Trustees to that being a suitable option. However that was not as bad as it might seem as that would only decrease HIG’s return by a small margin, would reduce the risk of damage to Silentnight’s trade caused by a CVA, and [Supplier A] had expressed a strong preference for a solvent compromise. The key was for Silentnight to pursue both options in parallel in an effort to force tPR to come to the table.
332. The Respondents were well aware of the conditions which had to be satisfied before the PPF and tPR would agree to take on a pensions scheme. As noted above the conditions included (i) inevitable insolvency or burning platform (ii) the requirement to offer 10 or 33 percent of the equity (depending on the circumstances) and (iii) tPR had to be prepared to clear the transaction. If it did so it lost its opportunity to bring contribution proceedings against certain parties such as the new owners of the business.
333. On 28 February 2011 [HIG Senior Management 2] sent Mr Costley-Wood a draft of a letter that he intended to send to Silentnight stating that he was going to send the letter to him in an official capacity, however he wanted Mr Costley-Wood’s thoughts. The draft letter provided:

David,

As you are aware HIG did not create the present situation. The Group’s significant pension scheme deficit has been a major issue for some time and the Group’s already weak financial position was exacerbated by [Bank 1 Trading brand]’s decision to withdraw the Group’s overdraft at the beginning of this month. HIG have become involved as a “white knight” trying to rescue the business and also protect creditors where possible.

The draft also provided:

If these milestones [31 March – tPR to have agreed a deal in principle, 6 May documents agreed with tPR and 30 May CVA nominee [of Newco] to have reported

to the court] are not achieved we reserve our rights generally, including but not limited to our right to demand on the overdraft facility. The additional on demand facility we have made available was agreed solely to give the Group time enough to explore a “solvent solution”. However we are not prepared to give the Group an unlimited period. The Group is still facing the “burning platform” that [Bank 1 Trading brand] created, albeit we have delayed what may prove to be inevitable if we reach the conclusion that the “solvent solution” will not happen or will not be effected in time in time we have given the Group commercially it will be reasonable and necessary for us to withdraw the current basis of our support and suggest that the Group implement its best contingency option.

The draft added that HIG wanted to see Silentnight carrying out contingency planning lest the solvent solution was not achieved.

334. The draft was untrue and/or misleading/ and or materially incomplete in its description of what had occurred. HIG created the situation by initiating the discussion for the acquisition of the Silentnight Debt and then entered into the Debt Sale Agreement on terms which provided for the Bank to cancel the overdraft. Had the Debt Sale Agreement not been entered into the overdraft would most probably have been renewed. The fact that HIG might have asked the Bank to continue the provision of overdraft facilities is neither here nor there; the Bank insisted that it wished to cancel the overdraft as a term of the agreement in which it agreed to assign the Silentnight Debt and HIG was content to accept the term. Mr Costley-Wood’s evidence was that he had some comments on the milestones but did not see it as his role to comment on the body of the letter, i.e., the reference to Silentnight’s financial position being exacerbated by the Banks’s decision to call in the overdraft, that HIG had been involved as a “white knight” and that the Group was facing the ‘burning platform” which the Bank had created. So far as he was aware the Bank had decided to call in the overdraft and that had exacerbated the situation and there was nothing surprising in that as most banks would have called in their debt upon assigning the security securing repayment of the debt. The Bank had cancelled the overdraft despite a request by HIG that it be continued.

335. Mr Costley–Wood gave evidence to the effect that he considered the description “white knight” about HIG’s role in providing finance was not inappropriate. HIG was willing to provide substantially more funds to Silentnight than the Bank, or indeed other providers which had been contacted over the years, and far greater funds than [Private Equity Firm 3] had been prepared to provide. The description of what occurred was seriously misleading as it failed to disclose that HIG had been in negotiations to acquire the Silentnight debt some considerable time before entering into the Debt Sale Agreement on 12 January 2011, pursuant to which HIG acquired the Silentnight Debt, and that HIG had intended that HIG should be in a position after acquiring the Silentnight Debt to create a liquidity crisis for Silentnight

regardless of whether the Bank continued to provide an overdraft facility. If the overdraft had not been cancelled, HIG would have ensured that the assignment permitted it to procure the Bank to cancel the overdraft as it was always its intention to create a liquidity crisis. Accordingly HIG was not a white knight appearing on the scene to rescue Silentnight.

336. The final letter was sent to Mr Costley-Wood on 28 February 2011. He contacted [HIG Senior Management 2]'s assistant and informed her that the letter should be sent to [Silentnight Board Member 1] who could then forward it to him and the letter was duly sent to [Silentnight Board Member 1]. The letter included the passages in the body of the letter described above. Albeit [Silentnight Board Member 1] and [Silentnight Board Member 3] might have been aware of the true position, not all the [Silentnight Board] had been involved in the details of the acquisition of the Silentnight Debt by HIG. The Respondents subsequently included the letter as appendix 3 to the PPF compromise proposal presented to the Trustees. Mr Costley-Wood denied in cross examination that he had allowed the letter to be included to mislead the Trustees, the PPF or tPR and would not accept that it was misleading.

337. On 23 March 2011 [HIG Senior Management 2] asked KPMG to assist in drafting a letter to tPR-which would challenge the notion that HIG “will make a killing” out of the acquisition of Silentnight. In an email sent on 25 March 2011 suggesting matters to put before tPR Mr Costley-Wood suggested that [HIG Senior Management 2] put the following under his heading of “key commercial points for the Regulator”:

“Clearly however, when HIG bought the debt, the overdraft had been cancelled and the business was heading towards administration. Whilst HIG were preparing to make a bid for the business out of administration, the [Silentnight Board] requested a short breathing space to agree a solvent compromise with the pension scheme. This was to enable a solvent solution and provide a better return for the scheme. However, in common with general private equity practice at the moment, HIG have confirmed it was never its intention to purchase the business with a pension scheme deficit on its balance sheet . . . if the company cannot agree a solvent compromise with the Pensions Regulator and the PPF during this hiatus period, then the business will revert to its original course and become insolvent.”.

The extract above was untrue or misleading and/or materially incomplete. The Bank's overdraft was cancelled as a term of the Debt Sale Agreement to which HIG was a party. At the time the overdraft was cancelled Silentnight was not immediately heading for administration, but possibly for a CVA. Administration had not been the intended result since 16 August 2010 and Mr Costley-Wood had been working towards a CVA for some 8 months. Administration was the last resort after a failure of a solvent compromise or CVA. Mr Costley-Wood would not accept that the key points were

misleading in the manner they described the cancellation of the overdraft and the reference to administration.

338. Mr Costley-Wood was copied into a draft of the letter to tPR on 28 March 2011 and invited to provide any “feedback”. On the same day HIG sent the letter to tPR. The letter stated that Silentnight was on the brink of insolvency for a number of reasons including the fact that the Bank had cancelled its overdraft facility and added in similar terms to those made by Mr Costley-Wood in his key commercial points set out above:

As you are aware, H.I.G. did not create the present situation; the Group's already weak financial position was exacerbated by [the Bank's] decision to withdraw the company's overdraft and ancillary banking facilities.

When HIG bought the Silentnight debt, the overdraft had been cancelled by [Silentnight's] bank and the business was heading rapidly towards administration (following [Silentnight's] failure to get financial support from any other source).

Whilst HIG was preparing to make a bid for the business out of administration, the [Silentnight Board] requested a short breathing space to agree a solvent compromise with the pension scheme. This was to enable a solvent solution and to provide a better return for the scheme and other creditors.”.

The letter was misleading for the same reasons as Mr Costley-Wood's key commercial points set out above. Mr Costley-Wood accepted that the letter was written in an effort to persuade tPR to agree a compromise but denied that he had any professional obligation to have the letter corrected as he did not act for HIG.

339. On 29 March 2011 [Silentnight Board Member 1] prepared a note for his presentation to tPR at a meeting due to take place on 30 March 2011. He sent a copy of the note to Mr Costley-Wood (amongst others) and indicated that he was happy to take any comments or additions. In relation to 2010 it described Silentnight meeting various institutional investors who declined to involve themselves in the Group due to the Pension Scheme deficit and conversations with the Bank about refinancing the Exit Fee. It did not mention the discussions with HIG in 2010 relating to the acquisition of the Silentnight Debt. Under the heading “recent activity” the draft presentation noted that the Bank had advised Silentnight on 13 January 2011 that they were not renewing the overdraft facility and had sold the term debt to HIG/Bayside and that the Bank “had found an exit”. The Bank gave 30 days' notice of the cancellation and it was clear that without the facilities the Group was immediately insolvent and the Group had appointed KPMG to advise on options. KPMG had advised that without an immediate cash injection Silentnight would probably go into administration on or shortly after 14 February 2011. Mr Costley-Wood responded stating that he would concentrate on the second half of the note rather than the first “especially the current trading which implies you need HIG investment to survive notwithstanding the pension issue.”.

340. On 30 March 2011 Mr Costley –Wood and [KPMG Employee 10] were present at a meeting held on 30 March 2011 attended by representatives of tPR, the PPF, the Trustees, Silentnight, HIG and [HIG’s External solicitors]. Mr Costley- Wood accepted in cross examination that HIG was looking to him to guide them through a PPF compromise and that tPR’s note of the meeting was accurate. Under KPMG’s retainer as amended on 28 February 2011 KPMG was retained to provide advice in relation to communications with the PPF and tPR. During the course of the meeting (as evidenced by the meeting notes of tPR and PPF) [Silentnight Board Member 1] provided tPR and PPF with an explanation regarding the circumstances in which HIG had become involved with Silentnight. He said that in January 2011 the Bank had given 30 days’ notice that it would not continue the overdraft, and that if the overdraft had been withdrawn without alternative financing, Silentnight would have entered into an insolvency procedure, namely administration. KPMG advised, after a review of the options, that administration was imminent. After the Bank had given notice Silentnight spoke to HIG and [Private Equity Firm 3] about taking over the Silentnight Debt. [HIG Senior Management 2] stated that the Bank, by giving notice of withdrawal of the overdraft, was responsible for the imminent risk of insolvency that Silentnight faced and that HIG had simply come in to keep Silentnight out of immediate insolvency. Mr Costley-Wood did not accept that [HIG Senior Management 2] said that the Bank was responsible for the imminent risk of insolvency but [HIG Senior Management 2] is recorded as stating that that was the cases in tPR note and we are satisfied that it was said. [HIG’s External solicitors] stated that the situation which Silentnight found itself in had not been engineered. There was no mention of the Debt Sale Agreement and the term in the Debt Sale Agreement that the Bank give notice of withdrawal of the overdraft.

341. Mr Costley – Wood admitted in cross examination that no disclosure was made at the meeting that HIG had been planning to purchase the Silentnight Debt as a means of acquiring Silentnight since June 2010 and that HIG always intended to dump the Pension Scheme. However he denied that there was any misrepresentation of the position in relation to the Silentnight Debt or that the description given at the meeting was materially incomplete and that he failed to act in a straightforward way.

342. What was said at the meeting on 30 March 2011 was seriously misleading as it failed to disclose that HIG had been in negotiations to acquire the Silentnight debt some considerable time before entering into the Debt Sale Agreement on 12 January 2011 pursuant to which HIG acquired the Silentnight Debt and that HIG had intended that Silentnight should be in a position of imminent insolvency for at least the previous 9 months. Further KPMG had not advised that administration was imminent. The fact that [A restructuring adviser at the PPF] appeared to see through the description by stating that one way of looking at it was that HIG had engineered the insolvency and the PPF would not want to agree a deal which would prevent tPR issuing a contribution notice suggests that the attempt to mislead the PPF and tPR might have

failed. Mr Costley-Wood said nothing at the meeting or subsequently to correct the impression conveyed by [Silentnight Board Member 1, HIG Senior Management 2 or HIG's External solicitors]or in the letter dated 28 March 2011 from HIG to tPR. As a result he associated himself with the description of events presented at the meeting and in the letter. He should have taken steps to correct the misrepresentations.

343. The Executive Counsel relies on a letter dated 4 April 2011 sent by HIG to Silentnight relating to the extension of the revolving credit facility. Mr Costley-Wood was asked to comment on the draft of the letter on 1 April 2011 and did so. When the letter was sent by HIG to Silentnight it contained additional wording to the effect that "As you are aware, HIG didn't create the present situation, but became involved as a "white knight" trying to rescue the business and also protect creditors where possible.". A copy of the final version of the letter was forwarded to Mr Costley - Wood by [Silentnight Board Member 1]. The reference to "white knight" was misleading for the reasons set out above. Albeit Mr Costley-Wood appreciated that [Silentnight Board Member 1] understood the correct state of affairs he ought to have considered that the letter had been drafted in the way it was in case it was shown to the Trustees, PPF or tPR or the [Silentnight Board] who were not aware of the circumstances surrounding the acquisition of the Silentnight Debt. In cross examination he said he did not know that the letter might be produced to them (but he should have considered it might be) as Silentnight was in negotiations with the PPF and tPR, and the letter might well have been drafted the way it was in order to mislead them or anyone else who read it such as the Trustees. Mr Costley-Wood should have taken steps to have the misleading statement corrected.

344. In addition the Executive Counsel relies upon four other communications put forward to the trustees and PPF about the causes of Silentnight's financial difficulties and HIG/Bayside's role as an alleged rescuer of Silentnight.

344.1. In a document dated 9 March 2011 KPMG produced a Project Bale PPF compromise proposal which set out the arguments to support a compromise with the Trustees and the PPF and was intended to be shown to the Trustees and which Mr Costley-Wood, despite his protestations to the contrary in cross examination, must have envisaged might be passed onto the PPF and tPR. Under the heading "overview" the document provided:

"However, in January of this year events overtook the Group when [Bank 1] gave 30 days' notice to cancel the overdraft. At the same time it agreed to a conditional sale of the term loan to a company called Bayside, an affiliate we understand of a US private equity group called HIG. The loss of the overdraft left the group facing imminent insolvency and KPMG was engaged by management immediately to assess the options available to the Group. Our recommendation at the time was to try to persuaded Bayside to provide

a temporary overdraft and fund a CVA to avoid administration, whilst at the same time exploring refinance options before the overdraft expired.”.

344.2. Also on 9 March 2011 Mr Costley-Wood supplied [Silentnight Board Member 1] with draft wording for a covering letter to be sent to the Trustees with the Project Bale PPF compromise proposal.

“Following the overdraft cancellation by [Bank 1] in February, we are facing a cash flow crisis. Our efforts to secure a new funder from the likes of [Private equity firm 1] and [Private Equity Firm 3] have failed. However, we have been granted a “stay of execution” by the funder who bought the [Bank 1] term loan, Bayside. They have granted us funding which allows us to continue trading until the end of March and agree a PPF compromise with the Trustees and [tPR].”.

The draft went on to provide that if a deal could not be done then the funding would be withdrawn and the Group would go into insolvency. However the funders had indicated that they were willing to offer £2 million and 10 percent of the equity in return for PPF taking on the Pension Scheme. The draft then suggested a meeting with HIG/Bayside and tPR/PPF as soon as possible. Mr Costley-Wood would not accept that the description of the termination of the funding was misleading as it did not refer to HIG’s involvement.

344.3. On 25 March 2011 Mr Costley- Wood provided wording to [Silentnight Board Member 1] to send to the Trustees in response to a counter offer they had made. The emails provided that Silentnight had:

.” . . a bank that has withdrawn its facilities and a new lender Bayside/HIG that has no intention of owning a business with a defined benefit pension scheme.”.

Mr Costley-Wood would not accept that the reference to the withdrawal of facilities was misleading in the absence of a reference to HIG’s involvement in the cancellation.

344.4. On 31 March 2011 at Mr Costley-Wood’s suggestion [Silentnight Board Member 1] wrote to the PPF with a “best offer”. Mr Costley-Wood advised on the contents of the letter. The letter provided that the Bank:

“Revoked our overdraft facility from mid-January. Had it not been for the emergency bridge funding provided by Bayside we would already have been forced to file for administration.”.

345. In our opinion the communications set out above were misleading and/or materially incomplete.

- 345.1. First they suggested that the Bank's decision to withdraw the overdraft facility was unconnected to HIG's acquisition of the Silentnight Debt whereas it was a term of the Debt Sale Agreement and an integral part of the arrangements under which HIG would acquire control of Silentnight.
- 345.2. Secondly, the letters suggested that HIG/Bayside had offered facilities to Silentnight after Silentnight had found itself in difficulties following the cancellation of the overdraft to assist Silentnight in circumstances which HIG/Bayside had no responsibility for creating the difficulties. In fact the liquidity crisis suffered by Silentnight was part of the plan by HIG/Bayside to assist in the dumping of the liability to the Trustees in respect of the Pension Scheme.
346. In cross examination Mr Costley-Wood would not accept that the description of the termination of the overdraft by the Bank reflected the documents described above was misleading.
347. Whether or not certain members of the [Silentnight Board], the Trustees, the PPF or tPR were in fact misled by the wording described above is not in point but we do note that [A restructuring adviser at the PPF] appears to have been misled. In cross examination he said in relation to what was said at the meeting on 30 March 2011:
- “You would have gathered from the witness statement that we listened to what they had to say. They had bought debt from the bank that had basically threatened to foreclose, which put them in a very, very strong position from a negotiating point of view.”
- The “foreclosure” i.e., the cancellation of the overdraft, was a term of the Debt Sale Agreement negotiated by HIG. HIG had not come onto the scene as a result of that cancellation.
348. We note that the letter dated 28 March 2011 to tPR was referred to in the Second Warning Notice issued by tPR on 22 June 2016 as materially misrepresenting the sequence of events in which HIG acquired the Silentnight Debt which also recorded that the position had been misrepresented in a similar manner at the meeting held on 30 March 2011.
349. Statements can be untrue and/or misleading and/or materially incomplete even if the recipient is not in fact misled or does not rely on the statement. The test is whether – objectively – the statement is misleading. [A restructuring adviser at the PPF]'s somewhat surprising evidence at one stage of his evidence was to the effect that the PPF would not be concerned as to the cause of Silentnight's difficulties but as he said in his evidence in chief, and in cross examination, tPR would be concerned that the circumstances affecting Silentnight, i.e., the burning platform, had been deliberately engineered and that an attempt might be being made to dump the Pension Scheme. Mr Costley-Wood confirmed in cross examination in relation to the 9 March 2011 PPF Compromise Proposal that tPR “wants to know if there is anything that's gone

on in the run-up to this that could be subject to anti avoidance legislation . . .” by which we understand him to have referred somewhat loosely to the moral hazard powers of tPR . The PPF would not enter into a compromise if more money would be generated by a contribution notice from tPR . If tPR had such concerns it would be most unlikely to agree to the Trustees or PPF entering into a compromise because in doing so it would forgo its moral hazard powers. He then admitted in cross examination that had he been aware that HIG had had the opportunity to purchase the Silentnight Debt at par, restrict the available facilities to put pressure on the [Silentnight Board] to restructure, and facilitate a discussion with the Trustees then that would have been a matter about which he would have been talking to tPR to ascertain what tPR thought about it, and what tPR thought it could do. The PPF looked to tPR to protect it. Further, assuming a burning platform, a loan to own strategy might impact the offer expected from HIG as the PPF would be interested at the nature of the current involvement of HIG/Bayside with Silentnight so as to assess whether to require 10 or 33 percent of the equity in the context of a solvent compromise. In other words the circumstances of the acquisition of the Silentnight Debt were factors which would have been of concern to both the PPF and tPR and we do not accept [A restructuring adviser at the PPF]’s evidence, if that is what he meant to say, that the PPF would not have been interested in the circumstances in which the overdraft had been cancelled.

350. In his May 2011 note (attached to his email of 8 June 2011 and not produced until after the hearing) in relation to Silentnight, Mr Costley-Wood, when referring to tPR’s moral hazard powers and the fact that Silentnight was placed in administration by Bayside, noted that “this is the issue they (tPR) have to be seen to deal with, and if they can get to the bottom of why [the Bank] cancelled the overdraft, then they may issue a [contribution notice].”. The May note suggests that Mr Costley-Wood was aware that tPR had not “got to the bottom” of the reasons for the cancellation of the overdraft – which it had not, and that the full picture was relevant to tPR as Mr Costley-Wood acknowledged in cross examination.

Determination of Allegation 2

351. Fundamental Principal (a) (Integrity) requires a professional accountant to be straightforward and honest in all professional and business relationships and implies fair dealing and truthfulness. Section 110.2 emphasises that a professional accountant shall not knowingly be associated with communications where the professional accountant believes that the information contains a materially false or misleading statement or information furnished recklessly and when a professional accountant becomes aware that the accountant has been associated with such information he should take steps to dissociate himself from that information.

352. Mr Costley-Wood was aware of the status of the PPF (a statutory fund) and tPR (a regulator). He was well aware that the attempt to agree a solvent compromise would be closely examined by the PPF and tPR to ascertain if an attempt was being made to

dump the liability in respect of the Pension Scheme on the PPF and that tPR had moral hazard powers which made the circumstances in which the Silentnight Debt was acquired by HIG very relevant. In cross examination Mr Costley-Wood accepted one had to be open and transparent with the Trustees, PPF and tPR and that tPR had a legitimate interest in information which would be relevant to whether a person was trying to dump a pension scheme on the PPF. He also accepted that the PPF and tPR were dependent on the information being supplied to them by Silentnight and HIG.

353. Mr Costley-Wood knew that HIG had been involved in planning the acquisition of the Silentnight Debt since mid 2010 and he knew that the creation of a liquidity crisis so that a burning platform existed was necessary in order to persuade the PPF to take on the Pension Scheme. He had been aware since about 16 August 2010 that tPR would examine the cause of the burning platform and he never suggested that it was caused by anything other than the cancellation of the overdraft until he gave evidence before the Tribunal. He also knew that (i) HIG had acquired the Silentnight Debt (ii) in that context the overdraft had been cancelled (iii) Silentnight and HIG required a burning platform to persuade the PPF to assume the liabilities of the Pension Scheme and (iv) the PPF would not take on the Pension Scheme (through a solvent compromise) if there had been an attempt to dump the Pension Scheme. He also knew in March and early April that an administration of Silentnight was a last resort after a solvent compromise and CVA had failed.

354. Further the statements which form the subject matter of Allegation were made to further the interests of Silentnight under the control of HIG.

355. Section 110.2 of the Code (under integrity) provides that an accountant must not knowingly be associated with communications or other information which they believe to be false where they believe that the information contains a materially false or misleading statement, statements furnished recklessly or omits or obscures information required to be included where such omission or obscurity would be misleading.

356. In the light of Mr Costley-Wood's knowledge as to the correct facts, he should not have assisted with the provision of untrue and misleading and/or materially incomplete statements to Silentnight, the Trustees, PPF or tPR as to the causes of Silentnight's difficulties. We take on board that Mr Costley-Wood denied in his evidence that any of the statements were misleading but we hold that they were misleading, or omitted information which rendered them misleading, and that he knew enough about the facts to know that a misleading picture was being put forward, and we hold that as such his conduct would be regarded as dishonest by the standards of ordinary decent people.

357. In acting as described above Mr Costley -Wood and the Respondents acted in breach of their duty to act with integrity as provided in Fundamental Principal (a).

We do not consider that in putting forward the version of events in the documents referred to above and in associating himself with the statements made at the 30 March 2011 meeting Mr Costley-Wood acted with integrity as he was prepared to advance and associated himself with a description of events which was not true or were misleading or materially incomplete and did so to assist HIG in its efforts to enable Silentnight to shed its liability under the Pension Scheme as cheaply as possible.

358. We conclude in relation to Allegation 2 that the Respondents conduct amounted to Misconduct within the definition of Misconduct as expounded in MG Rover case (FRC Executive Counsel v Deloitte and Einollahi (set out above). In respect of the matters the subject matter of Allegation 2 the conduct of the Respondents fell significantly short of the standards to be expected of a Member or Member Firm and further was likely to bring discredit to the Member or Member Firm or to the accountancy profession.

Allegation 3

359. Allegation 3 is that the Respondents knowingly or recklessly provided and assisted in the provision of untrue and/or misleading and/or materially incomplete explanations to the PPF regarding whether or not HIG was connected with Silentnight, in breach of Fundamental Principle (a), Integrity and section 110 of the code.

360. At the meeting held on 30 March 2011 with the PPF and tPR [A restructuring adviser at the PPF] had emphasised that the Silentnight/HIG offer then on the table was not acceptable and the PPF would normally expect 33 percent of equity in circumstances such as those which appeared to apply in the case of Silentnight. [A restructuring adviser at the PPF] also emphasised that as everyone at the meeting was clear on the position of the PPF and tPR the parties would need to consider a better deal. He did not elaborate on the reasons why the PPF would require 33 percent as opposed to 10 percent of the equity.

361. The background to this allegation is that under the guidance issued by the PPF, it would require an equity interest when a business was being purchased out of insolvency or restructured via a CVA. The Guidance stated that:

“The scheme is given 10of the equity where the future shareholders are not currently involved in the company and 33% if the parties are currently involved. (this is a form of anti-embarrassment protection to ensure that we not find ourselves with a large pension liability and not much to go with it and whilst the purchaser goes off with a valuable business because there was some golden nugget in it which no one on our side of the deal spotted or was told about it at the time.”.

362. As noted above Mr Costley-Wood advised [HIG Senior Management 2] on 14 December 2010 that the Share Purchase Agreement should provide for a “call option or conditional sale agreement” as opposed to an immediate purchase as that might be

better for a tPR point of view. By that we understand him to have been under the impression that the holder of an option to acquire shares might not be a “connected” party, whereas a shareholder would be, as Mr Costley-Wood was under the assumption that the criteria for the PPF requiring a percentage in excess of 10 percent depended on “connection” (which he assumed meant an existing equity interest) and which in turn would lead to the conclusion that a party was currently involved.

363. On 2 March 2011 Mr Costley-Wood had forwarded to [HIG Senior Management 2] an email from [A restructuring adviser at the PPF] sent to him on 24 March 2009 setting out the principles applicable to a solvent compromise. The principle in relation to the extent of the equity sought by the PPF was set out as:

“The scheme is given 10 percent of the equity where the future shareholders are not connected and 33 percent if the parties are currently connected.”

364. In fact the principle as to 10 or 33 percent of the equity had been changed from the criterion of connection to “current involvement” a much wider and more opaque concept. Mr Costley-Wood was aware of the change. The reason for the change was that the PPF wanted to keep the criteria for 33 percent as broad and flexible as possible and might well have applied it to a lender, or to a lender succeeding to another lender’s loan, or a person replacing facilities.

365. After the meeting held on 30 March 2011 with the PPF and tPR [HIG Senior Management 2] informed Mr Costley-Wood that he thought he could obtain approval to increase the offer to be made by Silentnight/HIG to £2.5 million and 10 percent of the equity. He did not wish to put it forward unless he had had an indication that the PPF would accept it.

366. On 31 March 2011 Mr Costley-Wood spoke to the PPF and put the offer of £2.5 million and 10 percent of the equity as a best and final offer. He reported back to [Silentnight Board Member 1] and [HIG Senior Management 2] that the PPF had an issue with the 10 percent or 33 percent “because of Bayside’s involvement” and the PPF considered that agreeing to 10 percent would justify a higher than normal cash contribution and suggested that [HIG Senior Management 2] considered a further offer of loan notes, cash and more than 10 percent equity Bayside was not the holder of the option to acquire shares in Silentnight – that was held by HIG Snooze.

367. On 31 March 2011 [Silentnight Board Member 1] submitted an offer of £2.5 million and 10 percent of the equity formally. He also sought to contend that Bayside was not a “connected” party and reiterated that Bayside had provided emergency funding after the Bank withdrew the overdraft facility in January 2011, and otherwise Silentnight would have had to go into administration, and Bayside would not sanction an increased offer. He added that Silentnight was preparing the papers for a CVA and also planning for, in the worst case, an administration.

368. [A restructuring adviser at the PPF]replied to the effect that if [Silentnight Board Member 1] looked at the PPF website he would see that the PPF expected 33 percent of the equity “in circumstances such as these”. He was copying in tPR as Silentnight would need its agreement as well and he warned that if the [Silentnight Board] declined the offer it would not entertain a further better offer. [HIG Senior Management 2] confirmed to [Silentnight Board Member 1] that the offer was the best and final offer and sent an email (copied to Mr Costley-Wood) suggesting some arguments to bolster the argument that HIG and Bayside were not “currently involved” with Silentnight or its shareholders.
369. On 31 March 2011 [HIG Senior Management 2] sent some suggested text to [Silentnight Board Member 1] (copied to Mr Costley-Wood) providing reasons why HIG and Bayside should not be seen as parties connected to Silentnight or for that matter “connected” to each other. One point [HIG Senior Management 2] made was that HIG had no equity stake in Silentnight (albeit it had the benefit of the option agreement through HIG Snooze).
370. Mr Costley-Wood was aware that HIG entities involved in the acquisition of the Silentnight Debt and HIG Snooze were acting together. He had noted in December 2010 that on the purchase of the Silentnight Debt HIG would control Silentnight. While HIG Snooze had the benefit of the option agreement to acquire the shares in Silentnight, Grace Bay was the party to the Debt Sale Agreement and the provider of the £10 million facility, whilst Bayside had provided guarantees to the Bank in respect of Grace Bay’s obligation under the Debt Sale Agreement. All the parties in the negotiations appeared to refer to HIG/Bayside acknowledging that the parties were acting together.
371. On 1 April the PPF rejected the Silentnight’s solvent compromise offer. Mr Costley-Wood spoke to [A restructuring adviser at the PPF]to ascertain why the PPF board had rejected the offer of a solvent compromise. [A restructuring adviser at the PPF]explained that Bayside/HIG were “connected” parties and therefore HIG was a 33 percent party. The fact that Bayside bought the debt and at the same time HIG acquired an option over the shares was evidence of this and the renewal facility letter proved this. In addition the £2.5 million offer was far too low. The PPF board had deep reservations about the HIG/Bayside deal and would always treat them as connected parties for the purpose of any compromise. He reminded Mr Costley-Wood that any compromise would have to satisfy the reasonableness test and £2.5 million did not meet that criteria. Mr Costley-Wood’s understanding when he finished the call that the PPF regarded Bayside and HIG as connected to Silentnight and therefore were “currently involved” and the PPF should receive 33 percent of the equity.
372. Also on 1 April [Silentnight Board Member 1] wrote to [A restructuring adviser at the PPF]contending that neither HIG nor Bayside were currently involved with

Silentnight and they were separate funds and that Bayside were being penalised for providing short term funds.

373. On 4 April 2011 Mr Costley-Wood asked [A restructuring adviser at the PPF] for an indication as to what tPR /PPF would accept. [A restructuring adviser at the PPF] replied that the current offer was not fair. The Pension Scheme would get less than on an insolvency (£2.5 million as opposed to £8.5 million in an insolvency), and the offer “only gives the scheme 10% rather than 33% equity (clearly HIG and Bayside are connected on this deal whatever they may say about finance from different funds - see the contract presenting Bayside with the equity for £1 if HIG can achieve a solvent restructuring). The PPF website is very clear - “the scheme is given 10% of the equity where the future shareholders are not currently involved with the company and 33% if the parties are currently involved” Clearly, HIG/Bayside are currently involved and will be future shareholders.” Mr Costley-Wood forwarded [A restructuring adviser at the PPF]’s reply to [Silentnight Board Member 1] noting that “[A restructuring adviser at the PPF] was still hung up about the share percentage but perhaps not surprising give [sic] his comment about the contract I think we need to see a copy of this.”.

374. On the same day Mr Costley-Wood emailed [KPMG Employee 2] and asked her to ascertain who owned, HIG Snooze. [KPMG Employee 2] replied that the company was owned by [HIG Senior Management 2] and HIG Luxembourg Holdings. The company registration documents attached to [KPMG Employee 2]’s email recorded [HIG Senior Management 2] as a director and the single issued share as registered in the name of HIG Luxembourg Holdings Fifteen SARL (“HIG Luxembourg”). Mr Costley-Wood immediately emailed [A restructuring adviser at the PPF] to the effect that KPMG had checked with the current shareholders and the conditional sale agreement was definitely with HIG and made no mention of Bayside so he was struggling to see how HIG was currently “involved in the company”. [A restructuring adviser at the PPF] replied that as lenders and the party conditionally entitled to the shares “they are involved . . . that is certainly the kind of thing that the wording on the website is meant to capture.”.

375. Mr Costley-Wood responded to the effect that he had:
“done some digging. There are two 50% parties behind the conditional buyer. One is definitely not a lender to the company. The other is registered in Luxembourg and it is not clear at this stage whether they are connected to Bayside or are a lender to SN [Silentnight] but I will try to find out . . . This is confidential information obviously.”.

He may have replied without looking at the attached pdf as he said he could not recall looking at the pdf. Mr Costley-Wood assumed that HIG Luxembourg was part of the HIG Group and an affiliate of HIG and he also understood that HIG Snooze was the party to the conditional share purchase agreement and that Bayside

was not. Mr Costley – Wood’s evidence was that he understood that the debate with the PPF was whether the party to the conditional sale agreement was also the lender (or closely connected to the lender) so as to make it “currently involved” for the purpose of the PPF 33 percent requirement. He was not focussing on the expression “currently involved” which the PPF interpreted widely to include a lender, possibly a person who acquired a loan from a previous lender, and a party who was a party to a conditional sale agreement or option to acquire equity.

376. On 5 April 2011 Mr Costley-Wood wrote to [A restructuring adviser at the PPF]:

“We act for the company and therefore are not advocates for HIG, but we cannot trace a direct connection between HIG and the company. Therefore it appears that the 10% rule should be applied not the 33%, particularly as the existing shareholders are giving up 100% of their shares. Bayside, for their part, are debt traders. They have stepped into the shoes of [the Bank] (who cancelled the overdraft with 30 days' notice) and have provided a brief respite for an RAA, but if it does not succeed they will recover their money from a prepack sale and see if they can make a 'turn' on the £5 million termination fee which they bought at a discount.”.

377. Mr Costley-Wood said in his evidence in chief that he was anxious to be as transparent as possible so he rang [A restructuring adviser at the PPF] to tell him that he was working on the assumption that the Luxembourg entity was a HIG group company, and that it was an affiliate of HIG, not Bayside, and that [A restructuring adviser at the PPF] thanked him for the information. [A restructuring adviser at the PPF] had no recollection of the conversation and there is no note of it. Mr Costley-Wood’s understanding was that the PPF was already aware that HIG and Bayside were working together and that the issue between Silentnight/HIG and the PPF was whether or not the party to the conditional share agreement was also the lender (or closely connected to the lender) to Silentnight making it “currently involved” for the purpose of the PPF criterion for requiring 33 percent. He could not understand why the acquisition of a shareholding in the future (thereby establishing a connection) should result in the conclusion that HIG was currently involved (which he did not appreciate was the test or what the implications of the expression were). Part of his confusion may have arisen as [A restructuring adviser at the PPF] used the expression “connected” in relation to HIG and Bayside and “currently involved” when considering the relationship of HIG/Bayside to Silentnight and Mr Costley-Wood appears not to have focussed on [A restructuring adviser at the PPF] referring to the website as using the expression “currently involved”.

378. Executive Counsel contends that Mr Costley-Wood knew that his explanations as to the lack of connection between HIG Snooze and Silentnight were untrue and/or misleading and/or materially incomplete because he knew that the HIG entities were acting in concert to achieve a takeover of Silentnight divested of the Pension Scheme liability and that pursuant to that objective, Grace Bay had acquired the Silentnight

Debt in order to create a burning platform so that the Pension Scheme liability would be assumed by the PPF and that as a result of the Debt Sale Agreement and the Share Purchase Agreement, HIG and its associates) in effect controlled Silentnight and was in a position to exercise significant influence over it.

379. In our opinion the events described above demonstrate some confusion on the part of the PPF as to the identity of the conditional purchaser of the shares but they understood enough about the transaction to understand that HIG and its companies were acting together to acquire control of Silentnight. There was no attempt by Mr Costley-Wood to suggest that HIG and Bayside were not working together but he did not understand the reason why they should be regarded as “connected” – an expression which he interpreted narrowly - to Silentnight which was the issue which he considered was important whereas the real issue was whether they were “currently involved” which provided plenty of scope for different interpretation and which expression he did not focus on. It is noteworthy that he referred to the expression “connected” in his email of 8 June 2011 (but forwarding a note drafted in early May) referring to “pension zombies”, i.e., companies which could never pay off their pension deficit and referred to the PPF expecting “connected” parties to give up 33 percent of the equity. This email was produced after the hearing.

380. Accordingly we do not consider that Mr Costley-Wood knowingly or recklessly provided or assisted in the provision of untrue and/or misleading and/or materially incomplete explanations to the PPF regarding whether or not HIG was connected with Silentnight in breach of Fundamental Principle (a) integrity. He was confused and not focussing on the right issue. Furthermore the expression “currently involved” was an opaque expression adopted by the PPF to give itself scope to argue for a 33 percent equity share.

381. As to the alternative complaint in relation to the statement in the email sent on 4 April 2011 and referred to at paragraph 7 (e) of the particulars of Allegation 3 to the effect that Mr Costley-Wood knew that the statement in the email to the effect that it was not clear to him whether the owners of HIG Snooze were connected to Bayside was untrue or misleading and/or materially incomplete, in the light of the fact that he was taking a narrow view of the meaning of the expression “connect” or “connection” which involved an equity interest, the Tribunal is not satisfied that he made the statement without believing that it was true, not misleading or materially incomplete. Further he wrote in the email that he would try to find out the connection as it was not clear. We do not consider that he was reckless or that he was making a definitive statement.

382. Accordingly we do not consider that Allegation 3 is made out and it is dismissed.

Sanctions.

383. We now turn to deal with sanctions. Our draft conclusions on the Allegations were sent to the parties prior to the Sanctions and Costs hearing which took place on 21 and 22 June 2021. The Executive Counsel submits that the following sanctions are appropriate:

KPMG:

- a. A severe reprimand.
- b. A direction that KPMG (a) conduct a root cause analysis of the reasons for the Misconduct and (b) perform a review of its current engagement and conflicts procedures and implement the recommendations arising. The terms of the proposed review are set out in Appendix B to this Report; and
- c. A fine of not less than £15 million plus a substantial uplift to reflect aggravating features.

Mr Costley-Wood:

- a. An order that he be excluded from membership of the ICAEW for 15 years;
- b. An order that he be ineligible for an insolvency licence for 15 years; and
- c. A fine of not less than £500,000 plus a substantial uplift to reflect aggravating features.

384. There are four sources of guidance and regulations. These are the Scheme, the Accountancy Regulations (“the Regulations”), the Sanctions Guidance (“the Sanctions Guidance”) of March 2021 and the Review Panel Report following Sir Christopher Clarke’s independent review of the FRC’s enforcement procedure (“the Review”)

385. Paragraph 3 (ii) of the Scheme requires the Tribunal to have regard to the Sanctions Guidance. The Sanctions Guidance provides that Tribunals may have regard to sanctions imposed in other cases: paragraph 7. However Tribunals

“... must determine the sanction which they think appropriate on the facts and circumstances of the case before them and should not feel constrained by the sanctions imposed (or not imposed) in earlier cases to impose a sanction which they do not think appropriate.”

The search for consistency with previous decisions involves the difficulty that they are concerned with different facts, and decided at different times, and are therefore not directly comparable. Furthermore sanctions imposed by a disciplinary tribunal are not designed as precedents. Nonetheless, previous cases may contain features by reference to which some measure of consistency and predictability can be achieved by a Tribunal in its approach to sanctions.

386. Paragraph 9 of the Sanctions Guidance provides that the Tribunal should have regard to the reasons for imposing sanctions for Misconduct in the context of professional discipline and that sanctions are imposed to achieve a number of objectives, namely,
- 386.1. to declare and uphold proper standards of conduct amongst Members and Member Firms and to maintain and enhance the quality and reliability of accountancy work;
 - 386.2. to maintain and promote public and market confidence in the accountancy profession and the quality of corporate reporting and in the regulation of the accountancy professions;
 - 386.3. to protect the public from Members and Member Firms whose conduct has fallen significantly short of the standards reasonably to be expected of that Member or Member Firm; and
 - 386.4. to deter members of the accountancy profession from committing Misconduct.
387. Paragraph 9 of the Sanctions Guidance also emphasises that the primary purpose of imposing sanctions for acts of Misconduct is not to punish, but to protect the public and the wider public interest.
388. Paragraph 10 of the Sanctions Guidance provides that the Sanctions Guidance has been developed to assist the Tribunal in achieving the objectives described above by imposing sanctions which:
- 388.1. improve the behaviour of the Member or Member Firm concerned; paragraph 11 of the Sanctions Guidance provides that in considering this aspect the Tribunal should consider whether, and if so, to what extent the sanctions proposed would be likely to led to improvements in respect of the matters which gave rise to the proceedings and in the quality of work of the member or Member Firm concerned;
 - 388.2. are tailored to the facts of the particular case and take into account the nature of the Misconduct and the circumstances of the Member or Member Firm concerned;
 - 388.3. are proportionate to the nature of the Misconduct and the harm or potential harm caused;
 - 388.4. eliminate any financial gain or benefit derived as a result of the Misconduct; and

388.5. deter Misconduct by the Member, Member Firm or others.

389. The Tribunal should also consider whether the sanction or combination of sanctions, financial and/or non-financial, achieve the objectives of the Scheme and there may be circumstances in which the objectives can be achieved without a Fine: paragraph 12 of the Sanctions Guidance.

390. The Tribunal is directed to consider the full circumstance of each case and the seriousness of the Misconduct involved before determining the sanction or combination of sanctions to impose on the Member or Member Firm. The Sanctions Guidance provides a number of factors which might be relevant to the Tribunal's consideration: paragraph 13 of the Sanctions Guidance. Furthermore the Tribunal must have regard to the principle of proportionality, i.e., the Tribunal should consider whether a particular sanction is commensurate with the circumstances of the case, including the seriousness of the Misconduct found and the actual or potential loss or harm caused by the Misconduct: paragraph 14 of the Sanctions Guidance. The seriousness of the Misconduct found should be determined by reference to a number of factors including the nature of the Misconduct, the level of responsibility of the Member or Member Firm in committing the Misconduct and the actual or potential loss or harm caused by the Misconduct: paragraph 15 of the Sanctions Guidance. In Fuglers LLP v Solicitors Regulatory Authority [2014] EWCH 179 (Admin) Poplewell J said at paragraph 29 (on an appeal from the Solicitors Disciplinary Tribunal):

“In assessing seriousness the most important factors will be (1) the culpability of the misconduct in question and (2) the harm caused by the misconduct. Such harm is not measured wholly, or even primarily, by financial loss caused to any individual or entity. A factor of the greatest importance is the impact upon the standing and reputation of the profession as a whole. Moreover the seriousness of the misconduct may lie in the risk of harm to which the misconduct gives rise, whether or not as things turn out the risk eventuates . . .”.

391. Paragraph 17 of the Sanctions Guidance provides for the approach which should be adopted by a Tribunal considering a combination of sanctions. A Severe Reprimand can be ordered in conjunction with any other sanction, and if a Severe Reprimand is merited, it will be appropriate to order it in conjunction with another sanction; a Fine can be ordered in conjunction with another sanction, and an Exclusion (which is only available against a Member), can be imposed together with a Fine and/or a Severe Reprimand.

392. The Tribunal has been informed that Mr. Costley-Wood retired from the KPMG partnership on 4 June 2021 having submitted his resignation in June 2019 and that he does not intend to continue practicing as a licensed chartered accountant or licensed insolvency practitioner. Furthermore he contacted the ICAEW (in April 2021) to

terminate his membership and insolvency licence. The ICAEW have not accepted his resignation pending the completion of disciplinary proceedings against him. However, resignation would not prevent Mr. Costley-Wood undertaking work of a similar nature as a sole practitioner, with another firm as a consultant, without being a Member of the ICAEW or licensed insolvency practitioner. Save in relation to formal insolvency appointments set out in section 388 of the Insolvency Act 1986, restructuring work is largely unregulated.

393. Paragraph 18 of the Sanctions Guidance sets out the normal six-stage approach to determining the sanction which the Tribunal should follow and which cross refers to the relevant paragraphs in the Sanctions Guidance:
- 393.1. Assess the nature and seriousness of the Misconduct found by the Tribunal;
 - 393.2. Identify the sanction or combination of sanctions that the Tribunal consider potentially appropriate having regards to the nature and seriousness of the Misconduct (“Steps 1 and 2”);
 - 393.3. Consider any relevant aggravating or mitigating circumstances and how those circumstances affect the level of sanction under consideration;
 - 393.4. Consider any further adjustment necessary to achieve the appropriate deterrent effect;
 - 393.5. Consider whether a discount for admissions or settlement is appropriate; and
 - 393.6. Decide which sanctions to order and the level and duration of the sanctions where appropriate (“Steps 3 to 6”).

Step 1: The nature and seriousness of the Misconduct.

394. Paragraph 21 of the Sanctions Guidance lists 23 non-exhaustive factors that the Tribunal will normally consider in assessing the nature and seriousness of the Misconduct. We address those factors which appear relevant below. Having identified the factors that it regards as relevant, the Tribunal should decide the relative weight to ascribe to each relevant factor: paragraph 20 of the Sanctions Guidance. We only refer to those factors which are or may be relevant.

Factor (a): Financial benefit derived or intended to be derived from the Misconduct

395. The Sanctions Guidance states that the financial benefit derived or intended to be derived may include any loss avoided or intended to be avoided where it is possible to quantify this. For example this could be quantified in appropriate cases by the fees received by the Member or Member Firm; and that the Tribunal may allocate an amount in respect of interest on the benefit obtained: paragraph 21 (a) of the Sanctions Guidance.

396. KPMG's fees (excluding VAT) for the Silentnight engagements amounted to around £1.6 million, comprising;

396.1. Silentnight engagements in the pre-administration period (January 2011 to May 2011): £484,210;

396.2. Fees billed and paid in respect of the administration (7 May to 15 December 2011): £822,773;

396.3. Liquidation work (16 December 2011 to March 2015, when partners of KPMG ceased holding office as liquidators): £281,565 - a total of £1,588, 548.

397. These fees resulted from the Misconduct. If the Respondents had properly addressed and dealt with threats to their objectivity, including the conflict of interest, they would not have been able to advise and assist both HIG and Silentnight. It is possible that KPMG would have done work for Silentnight for which it would have been paid if it had conducted itself properly (e.g. for carrying out an independent options review and any work arising from it), but the extent of any work cannot be ascertained. What can be said is that, in the absence of the Misconduct, KPMG would not have done the same work that has brought it substantial fees. The Respondents contend that insofar as the fees are attributable to the period after 5 April 2011 (i.e., exceed £260,393) they should not be taken into account as the period after falls within the period that is the subject of the investigation by the ICAEW. The Tribunal has been careful not to trespass into the events falling after 5 April 2011 in considering the events giving rise to issues of Misconduct. However in considering the extent of the financial benefit derived or intended to be derived from the Misconduct it is appropriate to consider the nature of the benefit received whenever the benefit arose. That is what Factor (a) requires and the benefit envisaged by the Respondents included acting as a supervisor or nominee of a CVA or an administrator of Silentnight.

398. The Executive Counsel also contends that the Tribunal should take into account the substantial fees which KPMG derived from the relationship which it developed with HIG from mid 2010. We found that KPMG had been trying to build a relationship with HIG; HIG was an attractive client with the ability to provide KPMG with additional work (paragraph 318). The Respondents wished 'to nurture HIG as a client' (paragraph 320) and 'keep HIG onside as a potential client' (paragraph 321). [KPMG Employee 9] also explained in evidence how attractive HIG was to KPMG.

399. In addition to the fees from the Silentnight engagements, KPMG derived significant financial benefit from its profitable commercial relationship with HIG. Silentnight was the first time KPMG had worked for HIG. It was because of the Misconduct (including the advice and assistance described at paragraphs 308 – 317) that the Respondents were able to forge this relationship with HIG. On 10 May 2011 an email was sent by [KPMG Employee 1] to his colleagues evidencing the opportunities to work for HIG Snooze and HIG Snooze Newco II Ltd, following

HIG's acquisition of the Silentnight business in administration. The opportunities identified include: "follow-up acquisition work; and ongoing tax compliance" and "ongoing audit".

400. In the 11-year period from January 2010, KPMG generated £8,509,207 in gross fee income from HIG, Bayside, HIG persons and HIG related entities. However of that £8,509,207, the sum of £1,356,386 were fees billed to and paid by specific HIG partnership or corporate entities; the balance of £7,152,821 was earned from HIG portfolio companies which are independent companies with separate boards and management to HIG and as KPMG submits "whose choice of advisers were not exclusively determined by HIG.". Of the £7 million, £4.8 million was attributable to clients which were clients before mid 2010 and so were not influenced in engaging KPMG by HIG as a result of any goodwill generated as a result of the Respondents' Misconduct. The Respondents accepted that £2.3 million of fees earned was attributable to companies which engaged KPMG after the Respondents' involvement with Silentnight. The Tribunal does not conclude that these fees were all earned as a result of Misconduct. HIG is a large private equity business with \$44 billion of equity and it is to be expected that some of the entities in the portfolio would have engaged the services of KPMG in the succeeding years after 2010 even if the Misconduct had not occurred. The corporate finance and transaction services teams at KPMG (in particular, [KPMG Employee 4], [KPMG Partner 4] and [KPMG Employee 9]) had been trying to develop a relationship with HIG since 2009 (paragraphs 154 and 318). Whether those efforts would have been successful without the Silentnight transaction cannot be ascertained. Whilst it may not be possible to quantify the full extent of the benefit, it is likely that the Misconduct contributed to the development of a profitable commercial relationship with HIG.

401. So far as Mr Costley-Wood is concerned, he has stated in correspondence through Linklaters that he personally derived no specific benefit from the Silentnight transaction, although the revenue generated from the engagements, together with other engagements for which Mr Costley-Wood was responsible in that period, would have been considered as part of his partner appraisal process (which we understand would have determined the level of his remuneration).

402. In assessing the weight of Factor (a) we take into account the uncertainties inherent in the exercise of ascertaining the financial benefit derived or intended to be derived from the Misconduct and the fact that some of the fees might have been earned in any event.

Factor (b): The gravity and duration of the Misconduct

403. The Tribunal's Report contains serious findings of Misconduct.

403.1. The Respondents knew throughout the first period (16 August 2010 to 14 January 2011) that HIG's strategy was to create a burning platform and then seek to persuade the PPF and tPR that the PPF should assume the responsibility for the

Pension Scheme (paragraphs 179, 305 - 306 and 328). Mr Costley-Wood acknowledged in evidence that it would have been entirely improper for him to have assisted in a strategy of creating a burning platform in order to achieve a PPF compromise. His evidence was that a real, genuine burning platform had to exist: it could not be engineered.

403.2. There was an obvious conflict of interest between HIG and Silentnight (paragraph 194), where we described HIG's reluctance to consider a solvent compromise at the 16 August 2010 meeting because it did not suit it as a "stark" example of the conflict of interest between Silentnight and HIG (paragraph 194), a consideration of pressure being applied to Silentnight by making a demand for payment (paragraph 240), Silentnight requiring time to restructure the Term Loan and Exit Fee and paragraphs 305 – 307, the creation of a burning platform. We note the Respondents' submission that the conflicts of interest were not obvious but reject the submission. To a professional accountant the conflict of interests should have been obvious.

403.3. The Respondents failed to consider the conflict of interests between Silentnight and HIG (paragraphs 311 & 318-324). The Respondents should have been aware of the conflict, or potential conflict, by 1 September 2010 at the latest (paragraph 192). There were many other occasions in Autumn 2010, when the conflict of interest manifested itself, but which went unheeded (for example paragraphs 194, 210, 211, 214, 215, and 231).

403.4. The Respondents failed, in addition, to consider the self-interest and familiarity threats which arose from their relationship with HIG and from their desire to nurture HIG as a client and keep HIG 'onside' (paragraphs 311 and 320-324). Mr Costley-Wood was conscious of the importance of the potential relationship of HIG to KPMG throughout both periods (paragraph 318).

403.5. The Respondents advised and assisted HIG in its plan to dump the Pension Scheme on the PPF, despite the obvious conflict between HIG's and Silentnight's interest. They acted in this way because they failed to consider the conflict of interest and failed to consider Silentnight's (i.e. their client's) interest alone (paragraph 305-310).

404. The Respondents lost their objectivity. The loss of objectivity underlay or drove much of what they did in relation to Silentnight throughout the relevant period, including assisting and advising HIG in its plan to acquire Silentnight free of the Pension Scheme liability from the summer of 2010. Amongst other things, Mr Costley-Wood (and through him, KPMG) demonstrated a lack of objectivity in:

404.1. favouring the HIG offer over the [Private Equity Firm 3] offer (paragraphs 312-313).

- 404.2. suggesting a ‘Grace Period’ shorter than six months. His advice favoured HIG’s interests over those of Silentnight. His advice stemmed from his desire to nurture HIG as a client and resulted in a severely curtailed period for negotiations with the PPF (paragraphs 317, 320 and 321); and
- 404.3. associating himself with material or statements that were misleading, in order to assist HIG (paragraph 314).
405. The Respondents dishonestly advanced or associated themselves with untrue and misleading and/or materially incomplete statements to the PPF, tPR, Silentnight and the Trustees as to the causes of Silentnight’s difficulties (paragraphs 353 – 355). There were eight separate and distinct such statements. The Misconduct is especially egregious given that, as we found:
- 405.1. The Respondents knew that (i) they had to be open and transparent with the Trustees, the PPF and tPR, (ii) tPR had a legitimate interest in being aware of information that was relevant to whether a person was trying to dump a pension scheme on the PPF 30 and (iii) the PPF and tPR were dependent on the information supplied to them by Silentnight and HIG (paragraph 351);
- 405.2. Mr Costley-Wood (and through him KPMG) acted dishonestly. Mr Costley-Wood knew enough of the facts to know that a misleading picture was being put forward (paragraph 355); and
- 405.3. The Respondents’ intended the PPF, tPR and the Trustees to be misled. Their motivation was to assist HIG in its efforts to enable Silentnight to shed its liability to the PPF under the Pension Scheme as cheaply as possible (paragraphs 35 and 356).
406. The effect of transferring the Scheme to the PPF (as the Respondents knew) would have serious and adverse consequences for those members of the Scheme not in pension at the time of the transfer (as their benefits were limited to 90 per cent of what they would otherwise have received) and the burden of funding of any shortfall in the Scheme assets required to fund the pensions would fall on other eligible defined benefit schemes and levy payers. HIG on the other hand would acquire Silentnight or its business free of the liability to fund the Scheme. We note that it was envisaged that HIG might fund a payment to the PPF as an inducement to take on the Scheme but the amounts put forward by HIG were low and not intended to make the Scheme “whole”; indeed it was less than 20 per cent of the amount which HIG eventually agreed to pay tPR to settle its claim under his moral hazard powers. HIG eventually succeeded in its aim albeit via an administration of Silentnight which occurred on 7 May 2011.

407. The ramifications of the Misconduct were serious. Due to its concerns over the acquisition of Silentnight and the reasons for its insolvency tPR issued a contribution notice in the sum of £96.4 million because it considered that the insolvency of Silentnight had been engineered by HIG which was the amount of the deficit in the Scheme on a buy-out basis at the time of the administration. TPR contribution notice proceeding was settled by the payment of £25 million by HIG to the Scheme which was insufficient to eradicate the deficit on a PPF basis. The consequences which followed demonstrated why the Misconduct was serious as it may have deprived Silentnight of the opportunity to avoid an insolvency engineered by HIG had it been receiving objective advice given solely in its interest: paragraph 194. It is no answer to say that the executive directors of Silentnight appeared to support HIG's aim. If it was improper to assist HIG in its aim of dumping the Scheme by creating a burning platform, it did not become proper because the executive directors apparently approved of that course. As we recorded, Mr. Costley-Wood did not consider that there was any other burning platform other than that to be created by HIG.

408. We consider that the gravity of the Misconduct was very serious. Due to their loss of objectivity the Respondents failed to act in the interest of Silentnight, which was their client, and as a result Silentnight did not receive objective advice as to the most appropriate manner in which to deal with the implications of HIG's interest in acquiring the Silentnight Debt in circumstances where it was HIG's intention to dump the Pension Scheme of which Silentnight's employees and former employees were members. As we noted at paragraph 70 the fact that the liability to the Pension Scheme was inconvenient and had unattractive aspects did not in itself justify making arrangements to dump the pension Scheme on the PPF. Mr Costley-Wood acknowledged in evidence that it would have been entirely improper for him to have assisted in a strategy of creating a burning platform in order to achieve a PPF compromise which is precisely what he did. The duration of the matters in Allegation 1 ran for some 8 months and in relation to Allegation 2 the series of misleading statements were made over a period of about 5 weeks.

409. There was nothing spontaneous in the representations the subject matter of Allegation 2 which followed a consistent and deliberate course of conduct intended to assist HIG and were, in effect, the culmination of the loss of objectivity. Objectivity from professional advisors is something which is expected of them and which the Respondents did not provide to Silentnight. Mr Costley-Wood should not have made those statements he made and should not have associated himself with the statements he did not make by not correcting them. We refer to paragraph 37 above and section 110.2 of the Code.

Factor (c): Whether the Misconduct caused or risked the loss of significant sums of money

410. The Sanction Guidance states, in relation to this factor, that this could be quantified in appropriate cases by reference to loss to creditors.
411. The Respondents' Misconduct, especially the Misconduct the subject matter of Allegation 1, risked the loss of significant sums of money. The Respondents assisted HIG in its strategy of driving Silentnight into an insolvency process, or to the brink of such a process, with a view to passing the Pension Scheme to the PPF at the expense of Pension Scheme members and levy payers. This strategy deliberately put at risk Silentnight's ability to survive and tens of millions of creditors' claims, potentially exceeding £100 million (including the Pension Scheme). That risk was both inherent in the Misconduct and an obvious consequence of it. As a result of the Misconduct, Silentnight lost the opportunity to explore whether there were alternatives to the acquisition of the Silentnight Debt by HIG: see for example paragraphs 142, 144, 149, 150, 151 and 196. We do not accept the Respondents' submission that, even if the Respondents had not been involved, the insolvency of Silentnight was a likely outcome, and have determined that there was no burning platform other than that engineered by HIG with the assistance of the Respondents.
412. It was not necessary for the Executive Counsel to prove that loss was actually suffered. It is sufficient that the Misconduct "risked" the loss of significant sums of money. There was a real risk:
- 412.1. There was no burning platform prior to HIG's involvement (paragraphs 143, 152 and 179). The Trustees were prepared to support Silentnight (paragraph 141). It is likely that [Bank 1] would have agreed to refinance all or some of the Term Loan or Exit Fee on 30 November 2011 and enter into a new facility agreement with Silentnight rather than take steps to place it into insolvency (paragraph [150]). It is unlikely that tPR would have challenged the 2010 Pension Deficit Plan (paragraph 151).
- 412.2. HIG engineered the burning platform. HIG's strategy was to create an insolvency event, or a liquidity crisis, and thus a burning platform. (paragraphs 179, 305, 306 and 328).
- 412.3. The Respondents were aware that the 'burning platform' would be caused or engineered by HIG once it acquired the Silentnight debt (paragraphs 179 and 306). The Respondents advised and assisted HIG in its plan, and encouraged HIG in its endeavours to acquire Silentnight, despite the obvious conflict between HIG's and Silentnight's interest (paragraphs 305-310). They did so because they failed to consider the conflict of interest between Silentnight and HIG and failed to consider Silentnight's interests alone (paragraph 310) and because they sought to nurture HIG as a client (paragraphs 318 – 321).

413. As noted above, the Misconduct put at risk Silentnight's ability to survive and tens of millions of pounds of creditors' claims, potentially exceeding £100 million as the liability to the Pension Scheme would crystallise:

413.1. The contemporaneous documents show that, as the Respondents appreciated, at the time that the pension liability was £100 million on a buy-out basis and that other company creditors amounted to around £12 million. There was therefore an obvious risk at the time of the Misconduct that third parties would suffer harm running into several tens of millions, and potentially exceeding £100m, as a result of the Misconduct.

413.2. Silentnight went into administration on 7 May 2011 as a result of Grace Bay calling in the working capital facility. This culminated in the sale of the business out of administration to HIG, with the PPF assessing whether to assume the Pension Scheme. This was at the expense of Pension Scheme members and levy payers. At the time of the administration, unsecured creditors included the Pension Scheme (at c.£100million), trade creditors (at c.£10.7million) and HMRC (c.£2.7million in VAT and PAYE). The estimated dividend as at 2012 was between c.7 and 10p in the pound.

413.3. [External Law firm 5], on behalf of the Trustees, have recently provided further information. In a letter dated 14 May 2021, they state, "Without additional funds, c. 1200 people and their dependents will lose, on average, around 30% of their promised pension entitlement from the Scheme. For some members the impact is materially larger. This 30% equates to some £50 million of pension, over members' future lifetime." [External Law firm 5] explain that the majority of the membership comprises factory workers, many of whom had worked for Silentnight for much of their working life. Many are pensioners with relatively modest incomes in retirement and no opportunity to improve their positions now. We have had no explanation as to how the figure of 30 per cent was reached and had understood the members who might suffer the 10 per cent reduction amounted to about half the members of the Pension Scheme. As we understand the matter, many of those who are not in pension at the date of the insolvency will lose up to 10 per cent of their pensions. In the case of modest pensions, a loss of 10 per cent is significant.

414. It is clear that the Misconduct might have risked causing substantial loss to the Pension Scheme and other creditors. We do not assume that Silentnight would have inevitably survived in the long term but, as we have held, we do not consider that it faced inevitable insolvency in 2010 or 2011, but for the insolvency engineered by HIG, but we are satisfied that Misconduct risked the Pension Scheme and other creditors facing a substantial loss even if one takes into account the possibility that Silentnight might eventually have faced insolvency at some date in the future. As we

noted at paragraph 195 the Misconduct may have deprived Silentnight of considering, and taking, steps to avoid the arrangements proposed by HIG.

415. We also note that the subject matter of the representations in Allegation 2 were intended to persuade the PPF to accept the Pension Scheme. Had the PPF and tPR accepted the proposal to take on the Pension Scheme in return of the contributions offered by Silentnight and HIG, tPR would have lost the opportunity to recover £25 million from HIG.

416. We note that HIG settled tPR's claim for £25 million in circumstances where he sought to recover £96 million. That does not provide an answer to the question whether the Misconduct risked causing a loss. The fact that a loss is the subject of compensation by a third party is no answer to the issue whether the Misconduct risked causing a loss.

Factor (d): where the Misconduct involved a failure to comply with professional standards, whether such a failure was intentional or unintentional.

417. The Misconduct which is the subject of Allegation 2 was intentional. We have held that the Respondents dishonestly advanced and associated themselves with misleading statements to tPR and the PPF and they did so to assist HIG in its efforts to enable Silentnight to shed its liability under the Pension Scheme as cheaply as possible (paragraphs 355 - 356). Mr Costley-Wood knew enough of the facts to know that a misleading picture was being put forward (paragraph 355).

418. The Executive Counsel submits that the loss of objectivity which arises under Allegation 1 should be treated as intentional within the meaning of sub-paragraph 21(d) of the Sanctions Guidance:

418.1. The dishonest (intentional) misrepresentations which are the subject of Allegation 2 demonstrate a lack of objectivity for the purpose of Allegation 1 (paragraph 314).

418.2. Loss of objectivity is encompassed within conscious wrongdoing: see the approach the Tribunal adopted in FRC v Deloitte and others ("Autonomy") at paragraphs 817 and 852.

418.3. The Respondents knew that the 'burning platform' was to be engineered by HIG (paragraphs 179 and 306). The Respondents advised and assisted HIG in its plan (paragraphs 305-310).

418.4. We have found that the Respondents favoured HIG's interests over Silentnight; that what appears to have motivated Mr Costley-Wood in suggesting a grace period a shorter than 6 month "was HIG's own interest in having control over the business" (paragraph 316); that Mr Costley-Wood "remained conscious

of the importance of the potential relationship of HIG to KPMG throughout both periods” (paragraph 318); he wished to “nurture HIG as a client” (320) and the “self-interest motivating factor was the desire to keep HIG onside as a potential client” (paragraph 321).

419. We consider that the conduct giving rise to the loss of objectivity was intentional within the terms of Factor (d).

Factor (e): the nature, extent and importance of the standards breached

420. The Respondents accept that the standards found to have been breached are important.

421. The standards of integrity and objectivity are of fundamental importance. They express the most basic requirements that society expects of professional accountants. Members of the profession have a privileged and trusted role in society. In return, they are required to live up to their own professional standards. Society expects high standards from professional persons; and the professions expect high standards from their own members. This is reinforced by section 1 of the ICAEW's Code of Ethics, and also paragraph 100.1 of Section A of the Code. Breaches of the principles of integrity and objectivity risk seriously undermining public confidence in the standard of conduct of Members and Member Firms and in the profession generally, all the more so where, as here, the professional has acted dishonestly. Dishonesty is inimical to everything that a profession stands for and especially destructive of public confidence.

422. As to the extent of the standards breached see paragraphs 401 and following above.

Factors (f) and (g): whether the Misconduct involved a failure to act or conduct business with integrity; whether the conduct was dishonest, deliberate or reckless.

423. The Misconduct involved a failure to act with integrity; it was dishonest and deliberate. See paragraphs 416 and following above.

Factors (j) and (k): whether the Misconduct was isolated, or repeated or ongoing and, if the latter, the length of time over which the Misconduct occurred

424. The Misconduct was not isolated:

424.1. The Respondents repeatedly failed to identify and consider threats to their objectivity over a period of eight months.

424.2. The loss of objectivity was on going from about 16 August 2010.

424.3. The misrepresentations (which were the subject of Allegation 2) were repeated, on eight separate and distinct occasions, over a period of about 5 weeks.

Factor (n): whether the Misconduct adversely affected, or potentially adversely affected a significant number of people in the United Kingdom (such as the public, investors or other market users, consumers, clients, employees, pensioners or creditors).

425. For the reasons set out in paragraphs 412 and following above, the Misconduct potentially adversely affected, a significant number of people. The Misconduct put at risk Silentnight's ability to survive (which was, of course, HIG's plan, as the Respondents knew). As noted above, Silentnight but for the acquisition by HIG of the Silentnight Debt did not face a burning platform. Those members of the Pension Scheme not in pension are likely to be adversely affected as have creditors other than members of the Pension Scheme: As noted earlier in these submissions, the majority of the membership comprised factory workers, many of whom had worked for Silentnight and contributed to the pension scheme for much of their working life. This was a foreseeable consequence of HIG's plan to 'dump' the pension scheme into the PPF.

Factor (p): whether it is likely that the same type of Misconduct will recur

426. Mr Costley-Wood retired from the KPMG partnership on 4 June 2021, having resigned in June 2019; he does not intend to continue practising as a licenced chartered accountant or licenced insolvency practitioner. As noted above, he contacted the ICAEW on 22 April 2021 to terminate his membership and insolvency albeit his resignation has not yet been accepted. On one view, therefore, the Misconduct would seem unlikely to recur. However, Mr Costley-Wood will be able to undertake work of a similar nature, whether as a sole-practitioner, with another firm or as a consultant, without being a Member of the ICAEW or a licenced Insolvency Practitioner. Save in respect of formal insolvency appointments set out in Section 388 Insolvency Act 1986, restructuring work is largely unregulated. In the circumstances, and given the lack of insight and regret shown by Mr Costley-Wood in relation to his Misconduct contending in his evidence that "This whole case here is just a witch hunt" "The fact that I am sat here being accused of dishonesty...and misconduct is frankly outrageous") and his "somewhat casual approach to procedure and regulation" (paragraph 53.4.1), there is some risk that the same type of Misconduct will reoccur.

427. As regards KPMG, the events giving rise to these proceedings relate to events over a decade ago and the firm's processes have undergone changes since then. Furthermore KPMG has disposed of its restructuring business and will no longer be involved in insolvency appointments. We are satisfied that KPMG will not commit the same type of Misconduct again in the context of restructuring but what remains unclear is whether there was a deficiency in KPMG's internal systems and procedures

which allowed Mr Costley-Wood to act as he did without his actions coming to the attention of those in charge of compliance at KPMG, and whether a similar gap exists in KPMG's systems which would allow similar conduct in respect of the business which KPMG continues to carry on.

Factor (r): Whether the Misconduct could undermine confidence in the standards of conduct in general of Members and Member Firms / in financial reporting / corporate governance in the United Kingdom.

428. For reasons which are self-evident, the Misconduct could seriously undermine confidence in the standards of conduct of Members and Member Firms in general, and in the profession. The Respondents do not dispute this. The history of KPMG's involvement with Silentnight after 16 August 2010 is a deeply troubling one as KPMG failed to act solely in its client's interest, acted in fundamental respects contrary to its interests, and in the interest of a party the interests of which were diametrically opposed to those of Silentnight.

429. As Lord Bingham MR stated in Bolton v Law Society [1994] 1 WLR 512, 518-9, a profession's most valuable asset is its collective reputation and the confidence which that inspires. The Misconduct could seriously damage the reputation and public confidence in the integrity of the accountancy profession.

430. KPMG rightly acknowledge that they are expected to act to the highest professional standards and that stakeholders, and indeed the general public, are entitled to rely on them doing so. Thus, KPMG's Global Code of Conduct states that, "We are here for our clients and stakeholders who need us, the capital markets we protect, and the general public we are entrusted to serve with integrity". KPMG's Global Code of Conduct goes on to explain "our commitments extend beyond compliance to our broader obligations to clients, our colleagues and society as a whole". These "commitments" include "maintaining our objectivity and independence" and "Building public trust".

Factor (s): the effectiveness of KPMG's procedures, systems or internal controls.

431. The history of what occurred shows that KPMG's relevant procedures, systems and internal controls were ineffective to prevent the Misconduct. In particular:

431.1. KPMG's procedures, systems and internal controls failed to identify or reveal:

431.1.1. The relationship between the Respondents and HIG;

431.1.2. the informal retainer between the Respondents and Silentnight;

431.1.3. that KPMG had been advising and assisting Silentnight and HIG;

- 431.1.4. the obvious conflict of interests;
 - 431.1.5. the existence of familiarity and self-interest threats to the Respondents' objectivity; and
 - 431.1.6. Mr Costley-Wood's loss of objectivity
- 431.2. The compliance forms were not properly completed and contained inaccuracies. In terms of providing information for an evaluation of risk they were obviously deficient: paragraph 243.
- 431.3. Although there was a Consultation Partner, [KPMG Partner 1], who counter-signed some of the compliance forms and sat in the same room as Mr Costley-Wood, did not identify the facts and matters set out above. As the Tribunal noted, [KPMG Partner 1] did not give evidence (paragraph 243). It is apparent that involving a Consultation Partner was insufficient to ensure that KPMG effectively considered the nature of the Respondents' involvement with HIG or that Mr Costley-Wood was appropriately questioned and challenged.
- 431.4. The Complaint made no specific allegation in relation to KPMG's procedures, systems and internal controls. We note that the events took place over 10 years ago and that KPMG's procedures and controls have been the subject of substantial revision since that time. We expect that the revised procedures will be re-examined in the light of this Report and the review we have directed.

Factor (t): in the case of a Member Firm, when the Member Firm's senior management became aware of the Misconduct and what action was taken at that point

432. KPMG's senior management have been aware of the Misconduct since at least 15 October 2015 when they were notified of the opening of Executive Counsel's investigation. The Formal Complaint was served in October 2018.
433. Prior to that, KPMG and Mr Costley-Wood received tPR's First Warning Notice dated 11 December 2014 which contained explicit criticism that, "Mr Costley-Wood provided advice to HIG in relation to its acquisition of the Silentnight Business... Despite the obvious conflict of interest which would have been plain to an experienced businessman such as [HIG Senior Management 2] (and others at HIG), so far as the Regulator is aware none of Mr Costley-Wood, anyone else at KPMG, [HIG Senior Management 2] or anyone else at HIG, ever decided that KPMG could not and/or should not provide advice to HIG and the Silentnight Group at the same time. HIG used this situation to its advantage...". Such strong criticism from a public regulator should have prompted a thorough investigation of Mr Costley-Wood's conduct and

of KPMG's systems, process and controls. There is no suggestion that KPMG took such steps.

434. Factor (t) is directed to investigation into or steps taken to remedy the matters which form the subject of the alleged Misconduct as opposed to steps directed to defending the Misconduct. There has been no acceptance by senior management of any Misconduct at any stage and the Respondents do not suggest that they have taken any specific substantive action in response to it. However, as noted above, KPMG's procedures and controls have been the subject of substantial revision since that time.

Factor (v) and (w): whether the Member held a senior position and/or supervisory responsibilities; was he solely responsible for the Misconduct?

435. Mr Costley-Wood held a senior position. He was a Partner in the Restructuring team and had been since 2008. He sat on the KPMG Manchester Board from 2014 to 2017. In 2017 he was promoted to be Head of the KPMG Manchester Restructuring team (a position which he retained until recently) and from 2018 to 2020 he was Head of Inclusion and Diversity for Restructuring. The Respondents accept that Mr Costley-Wood held a senior position within KPMG with supervisory responsibilities during the relevant time. Albeit on occasion he was accompanied at meetings or assisted by a more junior person we consider that he was primarily responsible for the Misconduct subject to the effect of paragraph 5 (11) of the Scheme.

436. KPMG also accepts that it is liable for the Misconduct by virtue of paragraph 5 (11) of the Scheme but denies that it is responsible for the Misconduct. Paragraph 5 (11) of the Scheme provides that anything done or omitted by an employee of a Member Firm within the scope of their employment or as an agent of a Member Firm, shall be taken as having been said, done or omitted by that Member Firm. The effect of paragraph 5 (11) of the Scheme is to make KPMG responsible for the acts of Mr Costley-Wood

The Appropriate Sanctions

Step 2: In the light of the Misconduct identified in Step 1, identification of the sanction or combination of sanctions which are potentially appropriate

A description of the sanctions available to the Tribunal is set out at paragraphs 25 to 55 of the Sanctions Guidance.

KPMG

437. Reprimands serve three main purposes: (i) signalling to a Member or Member Firm a Tribunal's disapproval of its conduct; (ii) communicating that disapproval to the wider profession and public through publication; and (iii) marking a Member's or Member Firm's disciplinary record, serving to alert the FRC, a Tribunal or Participant when deciding on appropriate action or sanctions in respect of any future Misconduct.

438. This is a case where a Severe Reprimand is justified. KPMG accepts that a Severe Reprimand is justified. Paragraph 17 (a) of the Sanctions Guidance provides that if the Misconduct is such as to merit a Severe Reprimand it will be appropriate for it to be ordered in conjunction with another sanction.

Other sanctions

439. It is also common ground that the imposition of a fine is appropriate. That is a recognition that a Severe Reprimand alone is not sufficient to fulfil the objectives described in paragraph 9 of the Sanctions Guidance

440. The Tribunal should aim to impose a fine that (a) is proportionate to the Misconduct and all the circumstances of the case; (b) will act as an effective deterrent to future Misconduct; and (c) will promote public confidence in the regulation of the accountancy profession and in the way in which Misconduct is addressed: paragraph (34) of the Sanctions Guidance.

441. In assessing the amount of the Fine a Tribunal should normally aim to impose a fine that takes into account the seriousness of the Misconduct, the size/financial resources of the Member Firm and the effect of a fine on its business and the factors set out in paragraph 21 (which have been set out above): paragraph 35 of the Sanctions Guidance.

KPMG: Fine starting level

442. As noted above the Tribunal considers that the Misconduct was very serious and the reasons why it was serious are set out above. A factor to be taken into account in imposing a Fine is the revenue of the Member or Member Firm: Sanctions Guidance paragraphs 36 to 40.

443. KPMG have provided the following financial information:

	2020 £m	2019 £m	2018 £m
Revenue of KPMG LLP	2,303	2,398	2,338
Operating profit of KPMG LLP	421	308	466
Average partner distribution (£ thousands)	572	640	690
Revenue of KPMG LLP Restructuring business	135	119	119

444. We consider that Tribunal should have regard to the entire revenue of the KPMG, not the revenue of the restructuring business (which has since been sold) for a substantial sum; KPMG and not the former restructuring business will bear the loss.

KPMG has – correctly - not sought to contend that the Fine should be levied by reference to the revenue previously generated by the restructuring unit.

445. We note that paragraph 5.31 of the Review (by Sir Christopher Clarke) states that:

“if one of the Big 4 firms was guilty of seriously bad incompetence, in respect of the audit of a major public company, where the errors were measured in nine figures or more and there had in consequence been either widespread actual loss or the risk thereof, a financial penalty of £10 million or more (before any discount) could be appropriate as being (a) commensurate with the seriousness of the wrongdoing; (b) a meaningful deterrent; and (c) sufficient to meet the primary objectives of sanctions. That assumes that the failings did not involve dishonesty or conscious wrongdoing. If they did, the figure could be well above that.”

446. This paragraph is directed at serious incompetence in relation to statutory audits but may also serve as some guidance insofar as comparisons can be made with the instant case. The Misconduct is significantly more serious than the type of case contemplated. It is much more serious than an incompetence case. It involves dishonesty and loss of objectivity (i.e. conscious wrongdoing) which led to the Respondents failing to provide advice and act in the interests of their client Silentnight which is to be distinguished from doing what the Respondents were retained to do, but not doing it competently. It put at risk Silentnight’s ability to survive with possibly serious ramifications for the Pension Scheme, general creditors, and those who had to fund the levy to the PPF.

447. We were referred to FRC v PwC and Stephen Denison (“BHS”). PwC was fined £10 million (reduced to £6.5 for early settlement); the audit partner, Mr Denison, was fined £500,000 (reduced to £325,000 for early settlement). Mr Denison was made subject to a condition not to perform audit work for 15 years and undertook to remove his name from the register of statutory auditors and not to reapply for 15 years.

448. In BHS,

448.1. the threat to objectivity was the failure to guard against the self-interest threat. It was not suggested that Mr Denison’s objectivity was in fact impaired (in contrast to our finding in the present case that the Respondents lost their objectivity).

448.2. there was no dishonesty. Mr Denison’s lack of integrity consisted in backdating his audit opinion by three days. As the Tribunal noted in Autonomy, at paragraph 856 of the Report, “This was plainly a breach of the principle of integrity, but it was not a very serious breach”.

448.3. the ‘Particulars of Facts and Acts of Misconduct’ do not state or imply that settlement was on the basis that Mr Denison was responsible for the losses suffered by creditors and employees.

449. BHS may be contrasted with KPMG, Mark Taylor and Anthony Hulse re ESML (Tribunal Decision, 1 February 2019, where the Tribunal imposed a fine of £6 million on KPMG, and with PwC, Jaskamal Sarai and Arif Ahmad re Redcentric (Audit Enforcement Notice, 22 May 2019) where PwC agreed to a fine based on a starting point of £6.5 million before a discount for early settlement. The misconduct in these audit cases consisted of a serious failure to exercise professional scepticism and to obtain adequate audit evidence. Lack of integrity and loss of objectivity were not in issue, which in the opinion of this Tribunal are more serious.

450. We were also referred to the decision in Autonomy where a Fine of £15m was levied on Deloitte. Autonomy was a much larger company and the potential losses suffered by third parties could have well exceeded the loss suffered by Silentnight or its creditors. In addition the acts the subject matter of complaint occurred in relation to the financial statements for more than 2 years; the tribunal in that case did find a single instance of a lack of integrity in failing to correct a misleading statement made at a meeting with the Financial Reporting Review Panel and a loss of objectivity (amongst other allegations which the tribunal accepted). Autonomy did not involve finding of dishonesty. However the risk of harm in the case of Silentnight was comparably greater as it included a risk to the future of Silentnight and the loss of its business with the attendant consequences for its creditors including the Pension Scheme. Mr Costley-Wood said in his witness statement:

“ . . . it is a significant decision to be taken by the directors of a company that a pension scheme must be compromised. This requires the company to conclude that absent a compromise, the company will need to enter a formal insolvency process and it is therefore inevitable that the scheme will enter the PPF. This decision has serious ramifications for all stakeholders in the business, including employee members of the pension scheme who will receive reduced benefits on the scheme’s entry into the PPF. Given the ramifications, directors will often want to receive clear advice (and often from more than one adviser) that the company has no other options before embarking on this type of restructuring.”.

The lack of objectivity in this matter went to the core of the relationship between Silentnight and KPMG. Silentnight required advice about how to deal with the liability to the Pension Scheme and the issues arising from HIG’s intention to acquire the Silentnight Debt. The lack of objectivity resulted in Silentnight not receiving advice at the right time, KPMG not informing Silentnight early in the relationship that it could not give the advice absent a feasibility study, and thus could not act. When KPMG was engaged by Silentnight in mid-January 2011 it did not act solely in the interests of Silentnight but still acted in HIG’s interests and acted on occasion

against Silentnight's interests. In addition to the lack of objectivity in relation to the Respondents' dealings with Silentnight we have held that Mr Costley-Wood acted dishonestly and therefore he and KPMG acted with a lack of integrity in their dealings with the PPF and tPR despite Mr Costley-Wood acknowledging that there was an obligation to act transparently in relation to a regulator.

451. We have found the decisions to which we were referred of limited assistance, as the facts and issues of this matter are very different to those the subject matters of the decisions. We also bear in mind that the primary purpose of sanctions is not to punish but to protect the public and wider interest and bear in mind the aims and objectives of the Disciplinary Scheme.

452. This matter was referred to the FRC under paragraph 6 (2) of the Scheme with the intention that if appropriate it should be dealt with under the Scheme and not by the ICAEW. We consider that we should apply the principles set out in the Sanctions Guidance which apply to matters before the Tribunal under the Scheme. The ICAEW may be looking at events occurring after the period with which we are concerned but under their own Guidance on Sanctions any sanction we impose should be taken into account to the extent that it is relevant to do so. We understand that an investigation or disciplinary proceeding by the ICAEW is currently stayed pending the outcome of these proceedings and whether or not that stay is lifted is a matter for the ICAEW.

453. We note that the passage from the Review quoted above referred to a starting point of £10,000,000 where one of the Big 4 firms was guilty of serious bad incompetence in respect of the audit of a major public company, the errors were measured in nine figures or more and there was a risk of widespread loss and noted that the figures could increase if there was conscious wrongdoing or dishonesty. We have summarised above the reasons why we consider that the failures by KPMG were particularly serious. We take on board that Silentnight was not a major public company, but it was a substantial company nonetheless, and the actions risked causing serious harm to a substantial group of people and risked damaging the public confidence in the accountancy profession.

454. Taking into account the objectives of the Scheme as set out in paragraph 9 of the Sanctions Guidance we consider that the starting point for a Fine to be paid by KPMG is £13 million. A fine in that amount would be about 3.6% of KPMG's operating profits for the year ended 2020 and less than 0.65% of its revenues for the year ended 2020. We do not consider that a fine of a lesser amount (the Respondents suggest £5 million) would reflect the gravity of the Misconduct.

Condition/Direction.

455. The Executive Counsel has submitted that we should exercise our discretion to impose a direction requiring KPMG to (a) conduct a root cause analysis of the reasons

for the Misconduct and (b) perform a review of its current engagement and conflict procedures and implement any recommendations arising. KPMG oppose this on the grounds that the events occurred more than 10 years ago, KPMG has sold its restricting business and so the particular Misconduct could not reoccur, there was no criticism of KPMG's procedures in these proceedings, and since the ICAEW has made specific allegations in the ICAEW proceedings it is appropriate that the ICAEW should have the responsibility for ordering any review. In addition KPMG's policies and procedures have evolved substantially since 2010. The Executive Counsel's concern, as we understand it, is not so much that the substantive procedures were defective, but that they were not implemented and that there appeared to be no effective check on ensure that they were implemented and adhered to.

456. After some debate between Executive Counsel and KPMG as to the terms of a review (which was not agreed) Executive Counsel submitted terms providing for a review in response to terms put forward by KPMG, to be considered by the Tribunal if the Tribunal was minded to make an order for a review. That review requires KPMG to provide to the FRC copies of its current policies, procedures and training programmes applicable to its Relevant Advisory Services (corporate finance, transaction services and debt advisory) connected with the identification and safeguarding of threats to compliance with the fundamental principles of objectivity. In addition the suggested direction would include a root cause review of the Silentnight engagement and a representative sample of prior insolvency engagements by KPMG concluded in the period 1 January 2018 to January 2021 in respect of entities which entered into an insolvency procedure with a defined pension scheme deficit and where the pension scheme deficit was transferred to the PPF or in a PPF Assessment period, the sample size to be the greater of 10 or 33 per cent of these cases. The aim of the review being to focus on whether the fundamental principle of objectivity was appropriately identified and safeguarded in the period prior to the appointment of office holders, and the reasons for such failures. A review would then be made of the policies, procedures and training programmes of KPMG in the light of the results of the route cause review.

457. Albeit that we have evidence that KPMG has new policies we have had no evidence that the root cause of the failures which we have held occurred have been investigated and the cause of the failure to adhere to the procedures have been dealt with.

458. We consider that a review in the terms supplied to us by Executive Counsel should be carried out. A copy of that review is attached to this Report as Appendix B.

Mr Costley-Wood

459. We refer to the matters set out above in this Report as to the gravity of the breaches of the obligation to act objectively and with integrity.

Severe Reprimand

460. The Executive Counsel has not sought a severe reprimand against Mr Costley-Wood who does not oppose the issuing of a Severe Reprimand. We consider that it is appropriate that such a Severe Reprimand should be issued.

Exclusion and preclusion

460. We consider that in the light of his responsibility for the Misconduct he should be excluded from membership of the ICAEW for the period of 13 years and be ineligible to hold an insolvency licence for a similar period.

Fine starting level

461. Mr Costley-Wood's remuneration was as follows:

2018 -	£613k
2019 -	£850k
2020 -	£833k
Half year 2021 -	£406k

462. KPMG have confirmed that they will indemnify Mr Costley-Wood in respect of any financial penalty and costs, to the extent those sums are not insured. That is not a ground for increasing any fine beyond the level that would otherwise be considered appropriate for Mr Costley-Wood: Sanctions Guidance paragraph 42(a). As KPMG will indemnify Mr Costley-Wood in respect of the Fine the Tribunal does not need to consider reducing an otherwise appropriate fine on the grounds that it might have serious financial implications for him or otherwise be unaffordable.

463. As we have stated above the Misconduct in this matter was very serious. Mr Costley-Wood was the person primarily and directly responsible for the matters giving rise to the Misconduct. We consider that the starting point for a Fine is £500,000. That is not out of line with his earnings and were he to have to pay the Fine himself, other things being equal, we would have fixed the starting level of the Fine at that level. We do not consider that a lesser Fine (those acting for Mr Costley-Wood suggest £250,000) would reflect the gravity of the Misconduct.

Step 3: Aggravating and Mitigating Factors.

464. The Executive Counsel relies on three matters as comprising aggravating features which should lead to sanctions over and above those which might otherwise have been given. The matters are that:

- a. The Respondents failed to cooperate with, or hindered the investigation of the Misconduct by the Executive Counsel, ICAEW and tPR: factor 61 (b).
- b. The Respondents (through Mr Costley-Wood) advanced a fundamentally untruthful narrative in their defence which falls within factor 61 (b) (lack of cooperation/hindering the investigation, and paragraphs 63 to 65)) and factor 61 (d) (concealing the Misconduct);
- c. The Respondents sought to conceal the Misconduct or reduce the risk that the Misconduct would be discovered :factor 61 (d);

Lack of cooperation/hindering the investigation

465.Paragraph 61(b) of the Sanctions Guidance states that non-cooperation may be an aggravating feature. Paragraph 64 of the Sanctions Guidance gives some helpful examples. It provides:

64. A failure to provide the level of cooperation required will be considered as an aggravating factor at the point of determining appropriate sanction. Non-exhaustive examples of such failures would include:
 - a. incomplete provision of documents and information in response to Notices and requests;
 - b. failure to provide adequate explanation of information provided;
 - c. failure to comply with deadlines specified in Notices under the Scheme and other written requests;
 - d. failure to properly prepare for interviews conducted under the Scheme (including failure to review material provided by the Executive Counsel in advance of such interviews);
 - e. failure to conduct an adequate search for documents and information.

466. Paragraph 65 of the Sanctions Guidance makes it clear that the examples are merely illustrative and that the Tribunal should consider the overall level of cooperation provided during the course of the investigation and enforcement process.

467. In understanding what counts as a failure to provide cooperation in this context it is helpful to consider what is meant by cooperation. In the Review, Sir Christopher Clarke stated:

“Cooperation may take several forms. The prime example is where an individual or firm reports him/itself to the FRC. Cooperation will also be shown by dealing timeously, properly and fully with requests by investigators, not placing inappropriate obstacles in the way of progress; or seeking without good reason to delay either the investigation or the disciplinary proceedings. We rather doubt that it is necessary to spell out to professional accountants what cooperation means in this context. Cooperation is, in any event, what the FRC is entitled to expect – so that any reduction on account of the fact that the individual or firm was not uncooperative may not be much.”

The untruthful narrative or unsuccessful defence

468. As to the nature of the defence advanced by Mr Costley-Wood it was untruthful in that he did not believe that there was a burning platform throughout the material period and

was aware that the burning platform was created by the withdrawal of the overdraft facility in the context of the Debt Sale Agreement. Had he admitted that the only burning platform was that created as a result of HIG acquiring the Silentnight Debt the course of the hearing might have been very different.

469. So far as advice to HIG, and the statements the subject of Allegation 2, were concerned, Mr Costley-Wood denied that he had advised HIG or that the statements were misleading.

470. In relation to these matters care has to be taken to ensure that the Respondents are not penalised at stage 3 for a matter taken in to account at stage 2 or penalised in relation to defending an issue. We do consider that the defence put forward by Mr Costley-Wood in relation to the burning platform was a construct invented by him to assist in his defence. So far as the advice to HIG and the misrepresentations were concerned it was not out of order to defend them.

Concealing the Misconduct (Factor 61 (d))

471. In addition to the points made above, so far as failing to disclose the prior relationship in the compliance documents dated 12 and 14 January 2011, 30 March 2011 and the two documents submitted to the court which fall outside the period with which the Tribunal is concerned we made no finding that the omissions were deliberate. Before March 2011 there was no question of any investigation and no evidence that Mr Costley-Wood had any insight into his actions which he might have wished to conceal; the errors in the forms are consistent with his casual approach to regulation and our impression that he did not review documents carefully before he signed them. Mr Costley-Wood was not cross examined in relation to the first three documents to the effect that he deliberately sought to conceal the advice given to HIG and that the failure to note in the KPMG's Restructuring Risk Management Panel form dated 30 March 2011 that KPMG had rendered advice to Silentnight from about 16 August 2010 to 14 January 2011 was also deliberate. Accordingly we do not find that these errors were designed to hinder the investigation of Misconduct or conceal the Misconduct.

472. The Executive Counsel contends that incomplete information was given to her and the ICAEW in the 7 June 2016 presentation at which Mr Costley-Wood took the lead. It omitted to refer to a number of matters including (i) the informal retainer of KPMG by Silentnight during which some £45,000 of time costs were incurred prior to 12 January 2011, (ii) the nature of the advice given to HIG in this period which went beyond a general presentation designed to attract Silentnight or HIG as clients but involved the giving of substantive advice to both. Whilst the presentation included an extract from the CVA Discussion document, it did not refer to the version of the CVA Discussion document stating that KPMG could give advice to both Silentnight and HIG throughout a CVA process "both pre and post". The Respondents' legal advisers, Linklaters LLP, had informed the FRC by letter dated 13 January 2017 that the initial presentation was "intended as an initial overview and orientation of the issues to assist

the FRC at an early stage of the investigation rather than a comprehensive presentation of each and every relevant fact”. By letter dated 21 March 2017 the FRC raised the failure to refer to the work done prior to 14 January 2011 and requested the Respondents to review the presentation material and confirm whether the Respondents wished to clarify or amend it. By letter dated 28 April 2017 Linklaters responded to the letter dated 21 March 2017 stating that there were no matters which the Respondents wished to clarify as the June presentation was intended as a “high level summary of KPMG’s involvement in the Silentnight engagements. It was not, and could never have been at that stage nor in the time allotted, a comprehensive account of each and every relevant fact relating to KPMG’s engagements.”. By letter dated 5 April 2019 Linklaters once again defended the June presentation by reference to the fact that the presentation did not seek to address each individual documents or communication with any of the Silentnight stakeholders within the Relevant Period. KPMG has not reviewed “every relevant document in advance of the presentation nor spoken to all team members”. One assumes that KPMG had spoken to Mr Costley-Wood who led the 7 June 2016 presentation.

473.The failure to refer to the £45,000 of work billed prior to 14 January 2011 is difficult to explain. It should have been reflected in KPMG’s systems and been fairly easy to discover albeit a forensic review of time records was not undertaken prior to the presentation. It was a matter which one would have expected to feature in a high level presentation as it went to the commencement of the relationship between Silentnight and KPMG. We have some difficulty in believing that in preparing for the 7 June presentation Mr Costley-Wood overlooked it inadvertently; it may have been intended to downplay the level of contact between Silentnight and KPMG in the period up to 14 January 2011 as the nature of the communication with HIG was also downplayed, as it went beyond general advice about a CVA but involved advice to HIG and the Silentnight transaction. The failure to reveal the ad hoc retainer with Silentnight may have delayed Executive Counsel’s investigations as to how KPMG discharged its obligations to Silentnight. In any event that failure manifested a lack of cooperation.

474.The Executive Counsel relies upon the circumstances in which the note of the 16 August 2010 meeting was produced. We have referred to that at paragraph 53.4.1. The Executive Counsel did not accept the accuracy of the note and the full picture emerged as to how it was created emerged in the cross examination of Mr Costley-Wood. Mr Costley-Wood’s witness statements did not refer to the fact that it was not produced contemporaneously. That emerged in the course of cross examination although by then his email to his secretary to produce the note had been exhibited to Mr Shaw’s expert report. The failure to reveal that the note was produced over a year after the meeting amounted to a lack of cooperation even if the note bore a date a year later than the meeting date and might have led a reader to question when it was created.

475.In addition to:

- a. the incomplete provision of information in the course of the 7 June 2016 presentation;
- b. Incomplete provision of documents and information in relation to the Respondents' relationship with HIG and Silentnight;
- c. Incomplete information concerning the 16 August [2010/2011] meeting note and the email in September 2011 asking for the note to be written up,

The Executive Counsel relies upon the Respondents' failure:

- a. to conduct an adequate search for documents by reference to the name "Costly" instead of "Costley"; the person responsible for carrying out searches misspelled Mr Costley-Wood's name and as a result a further 118 documents were produced including one which had some materiality. When Linklaters discovered the error it was brought to the attention of the Executive Counsel. The error is regrettable but is the type of mistake which can happen in a large organisation when matters have to be delegated to more junior employees.
- b. to conduct adequate searches into Mr Costley-Wood's personal emails. By letter dated 18 May 2016 the Executive Counsel raised the question whether Mr Costley-Wood had used his personal email in relation to Silentnight matters. KPMG responded by letter dated 27 May 2016 to the effect that Mr Costley – Wood had informed them that he had not used his personal email for such a purpose. The Executive Counsel raised the matter again with KPMG on 20 March 2019 as they had discovered that [Silentnight Board Member 1] and [Silentnight Board Member 3] had used their personal emails. Linklaters referred back to their reply in their letter dated 27 May 2016 but apparently no further searches for personal emails were made and the Respondents' relied upon Mr Costley-Wood's recollection of events occurring some 9 years earlier. Following further prompting by Executive Counsel on 15 February 2021 (as she had noted that Linklaters had produced some emails sent from Mr Costley-Wood's personal email address), Linklaters confirmed by letter dated 22 February 2021 that Mr Costley-Wood had used his personal email address on limited occasions and for administrative purposes such as to enable him to print documents at home and that they had found some 60 documents. Linklaters further confirmed that searches had not previously been carried out for documents bearing Mr Costley-Wood's email address. Following a letter dated 23 February 2021 from Executive Counsel asking Linklaters to ensure that further searches were carried out on another platform which carried KPMG electronic documents, a further search was carried out and another 623 documents were discovered. Linklaters also confirmed that those of Mr Costley-Wood's emails from 2010 to 2011 which had not been copied to Mr Costley-Wood's KPMG email address would have been deleted. As a result

the Executive Counsel may have lost the opportunity to follow up lines of enquiry arising from the deleted emails. The failure to carry out comprehensive searches in response to the specific requests by the Executive Counsel is a serious matter as it does exhibit a failure to cooperate.

- c. to conduct adequate searches which resulted in documents being produced after the hearing of the Formal Complaint. By letter dated 5 February 2021 Linklaters revealed that the Respondents had discovered an error in the searches which had led to an additional 2,367 documents being discovered of which 1,834 were relevant to Silentnight. Following further enquiries further documents were produced as late as 4 March 2021. The substantive hearing had been completed in Mid-December 2020. The late production may have deprived the Executive Counsel of additional lines of enquiry and her team had to review an additional 2000 documents. The failure appears in the main to be attributable to errors in the manner in which the searches were carried out in that certain documents were recorded as being reviewed for disclosure which had not been. In the light of the substantial number of documents produced we do not consider that it would be correct to conclude that the documents were withheld due to any intention not to cooperate.

476. In the light of the sanctions proposed in Stage 2 the Tribunal does not consider that the aggravating circumstances described above require an adjustment to the sanctions.

Mitigating Factors

477. The subject matter of the Allegations occurred more than 10 years ago. Mr Costley-Wood has indicated that he wishes to resign from the ICAEW and cease to hold a licence to hold office as an insolvency practitioner. KPMG has sold its restructuring business so that the specific type of Misconduct is unlikely to be repeated.

478. Mr Costley-Wood has no prior findings of Misconduct against him.

Step 4: Adjustment for deterrence.

479. The sanctions described in Step 2 adequately deal with deterrence and no adjustment is required.

Step 5: Adjustment for admissions or settlement

480. This does not arise.

Step 6: the appropriate level of sanctions.

481. In the light of the matters described above we consider that the following sanctions should apply:

Mr Costley-Wood:

- a. A Severe Reprimand should be issued to Mr Costley-Wood;
- b. Mr Costley-Wood should pay a Fine of £500,000; and
- c. Mr Costley-Wood should be excluded from membership of the ICAEW and be ineligible to hold an insolvency licence for a period of 13 years.

KPMG:

- a. A Severe Reprimand should be issued to KPMG;
- b. KPMG should pay a Fine of £13,000,000; and
- c. A direction should be issued that KPMG implement the matters set out in Appendix B

Mr Costley-Wood and KPMG

Costs

482. We direct that Mr Costley-Wood and KPMG pay costs (as agreed) of £2,450,000 in respect of the investigation and proceedings and in addition pay the costs of the Tribunal in the sum of £305,814 amounting in aggregate to £2,755, 814 such amount to be paid within 28 days of the date of this Report.

483. We express our appreciation to the considerable work on the part of Executive Counsel and the Respondents (and to those in their respective teams who worked behind the scenes to manage the considerable documentation) and to the very able and helpful representation by counsel. We would also thank those who managed the technology to allow these proceedings to be heard virtually and Ms Rosemary Rollason, the Secretary to the Tribunal for her unfailing efficient support.

484. This is the unanimous decision of the members of the Tribunal.

Terence Mowschenson QC

Chairman of the Disciplinary Tribunal

12 July 2021

Appendix A – The Complaint

APPENDIX B

- (1) Within four weeks of the date on which the FRC Disciplinary Tribunal sends its Report (made under paragraphs 9(7) and 9(8) of the Accountancy Scheme) to the FRC Conduct Committee (the “**Report**”), KPMG shall provide to the FRC copies of all current policies, procedures and training programmes applicable to its Relevant Advisory Services¹³ business connected with the identification and safeguarding of threats to compliance with the fundamental principle of Objectivity.

- (2) Within two months of the date on which the FRC Disciplinary Tribunal sends its Report to the FRC Conduct Committee, KPMG shall, at its own cost, instruct appropriate consultants, agreed with the FRC and independent of KPMG, (the “**Independent Reviewer**”) to conduct the following reviews, the terms of which shall be agreed with Executive Counsel within the said two-month period:
 - (i) A review (the “**Root Cause Review**”) of the Silentnight engagement and an agreed representative sample of prior insolvency engagements by KPMG concluded in the period 1 January 2018 to 1 January 2021, in respect of entities that entered into an insolvency process, with a defined benefit pension scheme deficit (and where such pension scheme deficit was transferred to the PPF or is in a PPF assessment period) (“Qualifying Cases”). The sample size shall be the greater of 10 or 33% of such Qualifying Cases. The Root Cause review shall focus on (1) (in relation to non-Silentnight engagements) whether identification of threats to compliance with the fundamental principle of objectivity were appropriately identified and safeguarded in the period prior to the appointment of office holders; (2) (in relation to Silentnight and other engagements in the sample) the reasons for any such failures; and (3) any additional matters as may be agreed between KPMG and the FRC. The Root Cause Review shall be completed within 12 months of being commenced. The Independent Reviewer shall provide an interim report to the FRC after 6 months of commencement. A copy of the final report or reports prepared by the Independent Reviewer on completion shall be provided in full to the FRC.

 - (ii) A review (the “**Policies Review**”) of the policies, procedures and training programmes referred to at paragraph 1 above. The Policies Review shall be

¹³ Being, the following service lines: Corporate Finance, Transaction Services, and Debt Advisory.

completed within three months after the Root Cause Review is completed and the Independent Reviewer shall provide their recommendations for improving the said policies, procedures and training programmes. The report or reports by the Independent Reviewer arising from the Policies Review shall be provided in full to the FRC. KPMG shall, as soon as practicable but in any event within three months of receipt of the Policies Review Report, implement the recommendations of the Policies Review. Further, if deemed appropriate by the Independent Reviewer, KPMG shall instruct (at its own cost) an independent provider approved by the FRC to deliver additional training to all Relevant Advisory Services partners within 12 months of the conclusion of the Policies Review.

