

Insolvency Practitioner's Investigatory Powers

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An insolvency practitioner (IP) can expect to get access to the company's books and records (both hard copy and electronic) upon their appointment. In practice, the quality of the company's books and records received on appointment will vary significantly. While some companies maintain comprehensive accounting and operational records, office holders are frequently appointed over businesses where records are incomplete, unavailable or have not been properly maintained for a considerable period.

Common issues encountered on appointment include:

- Missing accounting records
- The absence of bank statements
- Directors using personal email accounts rather than company systems
- Cloud-based accounting records to which access has been lost
- Records held by third parties'
- Incomplete board minutes and statutory records
- Former employees who have left taking key knowledge of the business with them

As a result, investigations frequently begin with an incomplete picture of what happened prior to insolvency. The powers contained in Sections 234, 235 and 236 of the Insolvency Act 1986 (IA) are therefore often used not simply to recover specific documents, but to help an IP build a fuller picture supporting their investigations into potential claims. Given that an IP will have no personal knowledge about the company or its dealings, the powers set out in Sections 234–236 of the IA are a valuable tool.

This quick guide aims to give an overview of those powers, how they might be used and highlight points that an IP will need to consider ahead of exercising those powers.

Using S234 of the Insolvency Act 1986

Recovering company information/documents

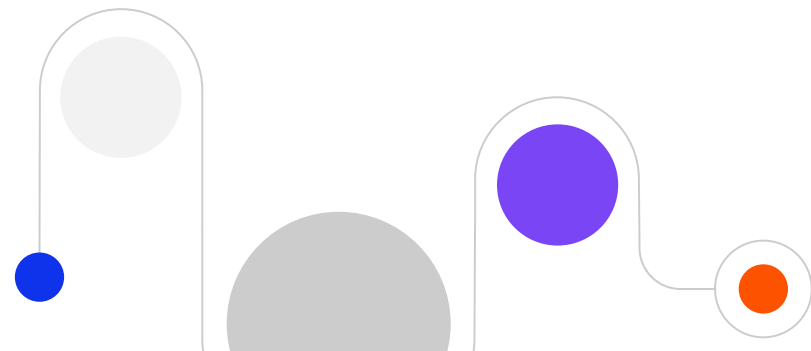
Section 234 of the IA gives an IP power to "get in" company property. This gives an IP power to recover books, papers or records to which the company appears to be entitled, from any person who holds them.

This power is extremely useful given it is wide reaching; enabling an IP to obtain information and records to support their investigations into the company's affairs.

In practice, Section 234 is more commonly used where key records are held by third parties. It allows an IP to request documents/records from the company's accountants, former solicitors, lenders, IT providers and cloud-based storage providers, as well as the former directors who may have documents stored on company or personal laptops and group companies.

The meaning of records (see the definition in Section 436 IA) encompasses non-documented records enabling an IP to request, not just physical hard copy documents, but any records that might be stored in a different format. Anything recovered, can be used by the IP as evidence to support a future insolvency claim.

Usually, a simple written request to the party holding the information is sufficient (subject to the reasonableness requirements discussed below), but if the third-party resists that request, an IP can make an application to court requiring them to deliver up the relevant books, papers and/or records.



How does an IP exercise this power?

As noted above, usually a written request to the person holding the relevant records will suffice, but when doing so an IP will need to explain why they want the information, and will need to justify that the books, papers and/or records are required for the purposes of them being able to fulfil their statutory duties.

Blanket requests for “all documents to aid in the IP’s investigations” without clearly explaining what is required and specifically why, could be refused. Furthermore, there needs to be a balance struck between what the IP is asking for, against the time and cost that the third-party will expend in complying with that request. An IP cannot simply ask for everything the third-party has, even if on appointment the company has limited or even no records. There must be a valid reason for the request.

If the person in receipt of the books, papers and/or records refuses to deliver those up, an IP can apply to court for an order requiring them to do so. The court has discretion whether to make such an order, therefore it is important that an IP is able to demonstrate that they have made a valid request; given a clear explanation as to why the information is required and addressed any concerns raised in reply.

Documents obtained by an IP under Section 234 may also be passed on to litigation funders if the IP later assigns a litigation claim. If the IP is entitled to use the documents, so is an assignee of the claim. It is likely that an IP can also do the same in respect of information obtained under Section 235, discussed below.

Practical barriers

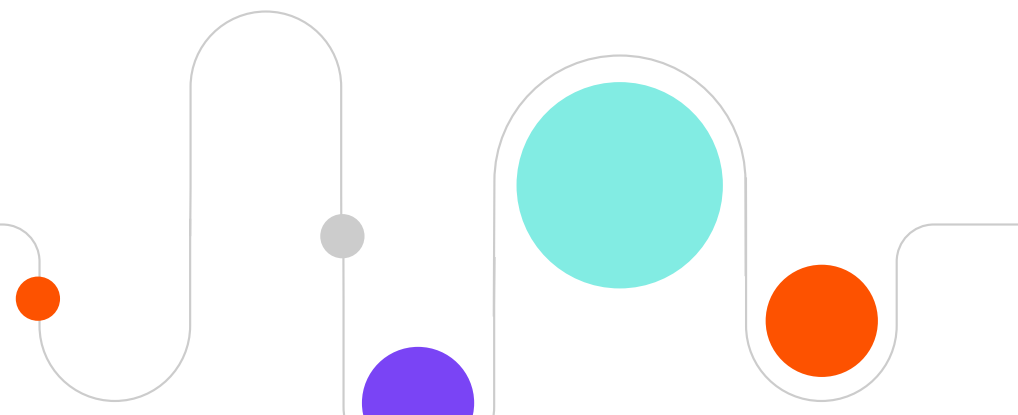
An IP is only entitled to recover books, papers or records to which the company appears to be entitled. It follows therefore, that if the company would not be entitled to the information, neither is the IP. An IP can face arguments that they are not entitled to the information, if for example, it is privileged. This is often an argument raised by the company’s former solicitors or accountants. Not all of the information on a solicitor’s or auditor’s file is available to their client, and the power given to an IP under Section 234 does not override this. An IP may need further assistance in understanding whether privilege applies if a request is denied on this basis, as arguments on privilege can be quite technical.

Requests for information can also be denied if a third-party claims ownership of the documents. In such cases, it would be appropriate to determine who is entitled to the documents before proceeding further with the request, or an application to court because the court will not deal with complicated disputes over title as part of a Section 234 application.

An IP will only be able to recover books, papers or records that the third-party actually has in their possession. If they no longer have the records, they cannot be compelled to deliver them up. However, a third-party may simply deny they have the requested documents/information (even if they do have them), which in itself creates a hurdle because the IP will need to be sure that the documents are held by that person before pursuing a court order.

It is not uncommon for those receiving a request to argue that it is too costly (in time or money) to comply. This is not on its own an excuse for noncompliance but will require the IP to explain why their request is a reasonable one – see further commentary on reasonableness below.

It is also possible that records may have been destroyed and, in that case, there is little the IP can do, other than perhaps to look to Section 235 to seek an explanation.



Using S235 of the Insolvency Act 1986

Obtaining an explanation: Duty to cooperate

Section 235 is of equal importance to an IP who is trying to establish a full picture ahead of deciding whether there are grounds for litigation. It will not necessarily be obvious, from the paperwork alone what the reasons for a particular transaction were. Section 235 gives an IP the ability to gain a wider understanding of the company's actions and operations where documents or records may lack detail or require further explanation.

For example, the records may show that an asset was transferred shortly before insolvency but give no explanation for the transfer. Bank statements may show significant withdrawals of cash, but again the reasons for those are not explained in the paperwork. In such cases, questioning individuals involved will help an IP understand the reasons and wider context for the specific transaction. Not every transaction can be challenged, there may be a good commercial explanation for it.

An IP can use Section 235 to obtain explanations, understand decision making and/or obtain more information about the whereabouts of books and records, or other parties who might know more about a specific matter.

Section 235 sets out the categories of people who are obliged to cooperate with the IP. For the purposes of investigating the company's affairs, an IP is most likely to find the ability to ask the current and former officers and employees of the company for information or documents regarding the company, its business and affairs most useful. Those persons are obliged to cooperate, and if they do not, an IP can apply to court requiring them to do so.

The breadth of this provision is wide and can capture the providers of professional services to the company, including solicitors, accountants and banks.

How does an IP exercise their power?

Although not as broad as Section 234, which applies to "any person", the powers given to an IP by Section 235 are invaluable because they enable an IP to compel those individuals falling within s235, to attend meetings or answer questions which the IP may have.

It is usual for an IP to request a meeting, but it is also a usual response for those receiving such a request to ask the IP to set out a list of questions for them to answer, so that they can deal with a reply in writing.

From an IPs perspective, a meeting is preferable as it enables the IP to ask to follow up questions and open up the discussion. For those responding to a request for information, they are likely to resist a meeting initially and insist on dealing with responses in writing because this enables the recipient to limit their responses to the written questions. Either way, the onus is on the IP to make sure their requests for information are reasonable, because, as with Section 234, there needs to be a balance between what the IP is asking and what the third-party is being asked to provide.

It is unlikely to be reasonable for an IP to request a full and detailed explanation of every transaction the company has ever entered, and more likely to be reasonable to ask specific questions about a particular transaction or to seek an explanation of specific documents. However, much will depend on the facts, and an IP needs to think carefully about what they are asking and why.

If a recipient of a Section 235 IA request fails to cooperate, then the office holder can seek a court order under Section 236 IA to force their cooperation.



Practical barriers

The value of Section 235 depends on the willingness of individuals to cooperate. Directors may say they can't remember or give poor explanations and there may be conflicting accounts or concerns about self-incrimination. Trying to "unpick" the true position can therefore be difficult, but Section 235 does have some teeth because if a person fails to reasonably comply, they can be liable for a fine and risk facing a court application particularly if they are deliberately uncooperative.

Using S236 of the Insolvency Act 1986

Examination before the court

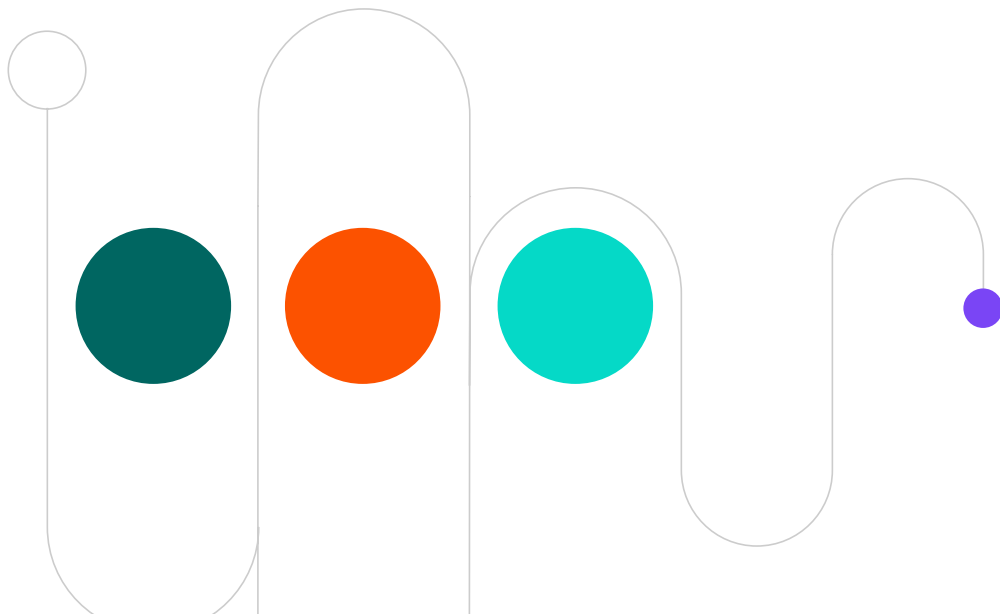
An IP can make an application to court under Section 236 IA requiring certain persons to appear and answer questions under oath. This is more commonly referred to as a private examination, although tends to be used as a last resort. Section 236 is extremely wide ranging and captures any officer of the company including directors, company secretary or auditors, as well as any person who appears to be able to give information concerning the company, its business or affairs.

Before applying to court, an IP will have to consider carefully, things such as the costs of litigation verses the likely benefit – can the cost be justified; can the information be obtained elsewhere; is there a risk of adverse costs. The court has a discretion whether to make an order under Section 236, so an order cannot be guaranteed.

Furthermore, the court will have to balance the necessity of the information requested by an office holder against the respondent's rights in any subsequent litigation. The office holder cannot use the private examination of a respondent to improve their position in future litigation. If a claim is already being brought against the respondent, then Section 236 cannot be used to discover in advance, the respondent's defence/ evidence and provide a special advantage in support of the claim. If the court thinks the IP already has enough information to take a decision on whether to bring a claim or not, then a Section 236 application is likely to fail.

Reasonableness

The court has recently reaffirmed that these powers are limited to information the office holder reasonably requires, even in scenarios where there were no records of the company and no employees at all. Although reconstituting corporate knowledge is a fair and legitimate purpose, the scope of the request needs to be justified. An IP cannot use these powers as a "fishing expedition" i.e. in the hope or wish that something might turn up. The powers cannot be used on speculative basis without sufficient justification.



Key takeaways

The powers that an office holder has under Sections 234–236 can be used against a wide scope of different people. The powers are useful in securing a variety of different sources of information, to allow an office holder to gain a detailed picture of the company's dealings, and are generally used in conjunction with one another as part of a wider investigation strategy.

In general terms an IP should:

- Identify where there are gaps in documents/knowledge ahead of using the Sections 234–236 powers
- Provide a clear explanation of why the information/explanation is needed
- Explain why the material sought will help fulfil their statutory duties
- Consider proportionality, broad requests are possible, but must be justified
- Avoid requests for information or documents that place an overly burdensome requirement on the recipient
- Avoid generic requests

The most effective use of these powers is usually targeted rather than expansive. Office holders who can clearly identify what information they need, why they need it and how it advances their statutory functions are more likely to obtain cooperation voluntarily and, where necessary, secure the court's support for compulsory disclosure.

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