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Insolvency Law Committee response to the Insolvency Service consultation entitled Red Tape Challenge - changes to insolvency law to reduce unnecessary regulation and simplify procedures

INTRODUCTION

1. The City of London Law Society ("CLLS") represents approximately 15,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues.

2. The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees. This response in respect of the Insolvency Service consultation paper entitled "Red Tape Challenge – changes to insolvency law to reduce unnecessary regulation and simplify procedures" which was published in July 2013 (the "Consultation") has been prepared by the CLLS Insolvency Law Committee. Members of the working party listed in the Schedule attached will be glad to amplify any comments if requested.

3. Our response focusses mainly on Part 2 of the Consultation, which relates to changes to the law governing insolvency processes, as we consider that many of the questions raised in Part 1 (Technical changes to regulations affecting insolvency practitioners) and Part 3 (Proposals to change how IPs report director misconduct) of the Consultation are best answered by appointment-taking insolvency practitioners ("IPs").

4. The Consultation asks 68 questions, many of which are of a technical nature. The main body of our response therefore highlights the key points which we consider may require further consideration, while the Appendix (which should be read in conjunction with the main body of our response) contains specific replies to the Consultation questions.

GENERAL COMMENTS

5. Initiatives aimed at eradicating unnecessary costs from the administration of insolvency proceedings, thereby potentially increasing returns to stakeholders, are clearly to be welcomed. Potential cost savings must, however, be considered in the context of what a particular provision is intended to achieve. While, in most cases, we consider that the correct balance has been struck between cost-saving and policy considerations, a number of proposals may require further consideration. These are

discussed below.

REMOVAL OF REQUIREMENT TO OBTAIN PRIOR SANCTION IN A LIQUIDATION

6. It is proposed[1] that all of the powers set out in Schedule 4 to the Insolvency Act 1986 ("**IA**") could be exercised without the need for a liquidator first to obtain sanction from either the court or a liquidation committee.

7. We agree that the distinction between the powers exercisable by a liquidator in a compulsory liquidation and those exercisable by a liquidator in a voluntary liquidation is artificial and that it therefore makes sense for the powers contained in Part II of Schedule 4 to be exercisable by any liquidator without prior sanction.

8. We consider, however, that, in relation to Part I of Schedule 4, a distinction should be drawn between applications relating to the commencement of legal proceedings (paragraph 3A of Part 1) and applications in relation to the remaining paragraphs of Part 1.

9. Specifically, it is not clear why a liquidator should, without any prior sanction, be able to pay any class of unsecured, non-preferential, creditors in full or enter into a compromise or arrangement with creditors. While taking such actions may be appropriate, any deviation from the liquidator's fundamental duty to treat equal ranking claims on a *pari passu* basis should remain subject to some element of prior scrutiny[2].

10. As noted in the Evidence Base "*sanction applications … are generally made in respect of the commencement of legal proceedings*"[3]. Our experience suggests that only a small proportion of the identified costs savings of approximately £0.8m per annum would relate to applications under paragraphs 1, 2 and 3 of Part I of Schedule 4 and that any (limited) cost saving resulting from amending these paragraphs would be outweighed by the potential legal uncertainty (and consequent damage to the UK insolvency regime) which may arise from apparently making its easier for liquidators to deviate from the fundamental principle that claims of non-preferred unsecured creditors should be treated equally.[4]

CREDITOR MEETINGS

11. Subject to the two exceptions set out in paragraph 13 below, and to our comments on CVAs and IVAs in paragraph 16, we agree that the default position should be that there would be **no** creditor meeting, unless either (i) the office-holder believed that it would have value, or (ii) the company's creditors wanted a meeting to be held.

12. **Initial Meetings**: We think that it is important that creditors should generally be given at least one opportunity to meet those running the case face-to-face, and to express their concerns to fellow creditors. The reassurance that the insolvency process is being taken seriously, combined with an ability to "let off steam", cannot be valued in monetary terms, but we consider that it is an essential element in a credible insolvency process. We would therefore suggest that:-

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1 In Section 3 of Part 1 of the Consultation

2 While a disadvantaged creditor could subsequently challenge the liquidator's actions, this may not be a practical or cost-effective option for that creditor.

3 Para 12 on Page 26

4 It is also proposed that the powers contained in Schedule 5 IA could be exercised without the need for a trustee in bankruptcy to obtain prior sanction from either the court or a creditors committee. We would, applying the same logic as above, suggest that exercising the power contained in Paragraph 7 of Schedule 5 should still require prior sanction.

(i) The requirement to hold a Section 98 meeting in a CVL should be retained, if only to give creditors the opportunity to meet the liquidator, and to express their views and concerns. Given that the liquidators would be expecting their fees to be paid out of the insolvent estate, retaining an obligation to meet those who are ultimately funding their fees, at an assumed cost of £339,[5] does not seem unreasonable.[6, 7]

(ii) The requirement to hold an initial meeting in an administration should also be retained, particularly where the administration involves a "pre-pack" sale. It would be unfortunate if the pre-pack process were to be made less transparent, by denying creditors the automatic opportunity to have a physical meeting with the administrators to discuss the reasons for the sale, particularly as the Insolvency Service has recently launched a further review into the use of pre-pack administrations, in reaction to concerns surrounding their transparency.

13. **Deemed Consent**: While understanding the potential benefits of having a deemed consent mechanism in certain circumstances, we question how useful this would be in practice, given that there would presumably have to be a relatively significant period before the consent was deemed to have been provided, particularly where the creditor group included foreign creditors.[8] This period might then have to be further extended if, as suggested, a written objection was received from a minority of creditors, requiring that a meeting was held to approve the relevant proposal or document. A quicker and more practical solution, which would encourage active creditor involvement, might be to make it easier for IPs to seek written consents from creditors in suitable circumstances.

14. If a deemed consent mechanism were adopted, further detailed consideration should be given to whether there should be any further exceptions to this rule, other than the three highlighted in the Consultation (resolutions relating to the insolvency practitioners' remuneration, CVAs and IVAs).

CVAs AND IVAs

15. There is a possible inconsistency in the Consultation, as Question 18 appears to assume that the approval of a CVA or an IVA would require a meeting of creditors, but the Evidence Base suggests that this may not be the case.[9] We firmly believe that the current provisions relating to the approval of IVAs and CVAs should be retained. Creditor engagement and trust in the current insolvency regime will not be increased by promoting a procedure which could result in creditors being told that a statutory cram-down of their claims had been implemented without them giving them an opportunity to discuss the merits of the proposal at a meeting with the Nominee and other creditors.

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5 Table following Para 14 on Page 55

6 The position in a CVL is distinguishable from that a compulsory liquidation (where the official receiver may decide not to hold a creditors' meeting unless one is requisitioned), as the liquidator in a CVL will normally only take office where there are sufficient funds to cover their fees (and, presumably, the costs of any creditors' meeting).

7 The argument for retaining such meetings would seem to be strengthened by the proposal in Annex 4 Part 2 of the Consultation that the liquidator may not be required to attend this meeting in person, if they consider that it would be appropriate to have a suitably qualified member of their firm attend instead.

8 If the proposed figure for the filing of claims contained in the draft amendments to the EC Insolvency Regulation were to be used as a rough yardstick, consent may only be deemed to have been provided 30 or 45 days after the document containing the consent request was sent out.

9 At Para 8 on Page 54

16. The merits of the projected saving of £464 where no meeting is held would therefore be significantly outweighed by the detrimental consequences of a potential reduction in transparency and creditor engagement in the CVA and IVA process.

WRONGFUL AND FRAUDULENT TRADING

17. We agree that it makes sense for the existing fraudulent trading powers to be extended to administrators. We also agree that delaying the commencement of wrongful trading proceedings against a director until the company goes into liquidation could be disadvantageous in certain circumstances.

18. We do not, however, believe that it would be appropriate in every case for an administrator to be able to pursue a wrongful trading action, given that a potential wrongful trading liability will only arise, under the current legislation, where the relevant person "*knew or ought to have concluded that there was no reasonable prospect that the company would avoid going into insolvent liquidation*"

19. In order to achieve the intended objective underpinning the Red Tape Challenge, without fundamentally altering the existing concept of wrongful trading as set out in Section 214(2) IA, the administrator's ability to pursue a wrongful trading action should only arise once the administrator is satisfied that the statutory objective set out in Paragraph 3(1)(a) of Schedule B1, namely rescuing the company as a going concern, can no longer be achieved (with the result that the administration is expected to be followed by the liquidation or dissolution of the company).

20. We believe that this approach is consistent with paragraph 126 of the Consultation (which assumes that the administrator is unable to rescue the company), but consider that this point should be made absolutely clear, particularly given the possibility that such wrongful trading claims could be sold to third parties, if the proposals contained in the "*Transparency and Trust*" discussion paper were to be adopted.[10]

PAYMENT OF DIVIDENDS/THE PRESCRIBED PART

21. The Consultation refers to the administrative difficulties inherent in dealing with small claims and paying small dividends, but does not refer specifically to a mechanism contained in the Insolvency Act which increases the chances of these issues becoming relevant, namely the "Prescribed Part" provisions contained in Section 176A IA.

22. Where the company's net assets exceed £10,000, Section 176(A)(2) IA requires a liquidator, administrator or receiver to make a prescribed part of the company's net property available for the satisfaction of unsecured debts unless they obtain a Court order disapplying this requirement, on the basis that the cost of making such a distribution to unsecured creditors would be disproportionate to the benefits.

23. While there is clearly a balance to be struck between policy considerations and cost savings, it would appear that an additional cost saving could be made by removing the requirement for administrators to apply to court to disapply Section 176A(2) in those cases where they are satisfied that the cost of establishing the claims of a

[10] It would be unfortunate for the rescue culture if, for example, directors remained at risk of being pursued by a third party following a successful exit from administration where such exit required a compromise of creditor claims, with the result that the relevant creditors could arguably point to a loss caused by the directors' pre-administration actions.

company's unsecured creditors and then making a distribution would be disproportionate to the benefits derived from doing so.

STREAMLINING THE LIQUIDATION PROCEDURE

24. It is proposed that where a company which is served with a winding-up petition does not contest the debt, it may simply file a notice at court stating that it does not contest the claim, and that this would "*negate the need to have a hearing in that case*". The company in question would therefore, presumably, go into liquidation on filing of that notice.

25. While characterised as a cost saving measure, this new mechanism could have a significant impact on the UK liquidation regime, as it effectively allows a company's directors to put the company into liquidation without either the consent of the company's shareholders or the approval of the court. It also removes the audience rights of the company's other stakeholders, who may have reasonable grounds for arguing that liquidation is not the most appropriate option.

26. It is appreciated that there is a cost associated with retaining rights of audience, but we would suggest that the identified savings across both winding-up and bankruptcies of up to £220,000 per annum may be outweighed by a combination of the detrimental impact of these changes on stakeholder involvement and the risk of the new system being abused by a small minority of directors (who may have a vested interest, as potential purchasers of the company's business or assets, in the company being put into liquidation).

Appendix – Specific questions asked in the Consultation

Removal of requirement to maintain separate case record

Questions 1 to 4

We do not intend to respond specifically on these points, as they are more appropriately addressed by IPs who regularly take appointments and therefore address these issues on a day-to day basis. We do, however, agree with the recommendation set out in Paragraph 32 of the Consultation that there should be a legislative requirement (codifying existing best practice) requiring IPs to maintain whatever records are necessary to justify the actions and decisions that they have taken on cases.

Allowing earlier destruction of books and papers

Questions 5 to 7

As before, we do not intend to respond specifically on these points, as they are more appropriately addressed by IPs. We do, however, agree that it would be entirely logical, as proposed, to bring the provisions regarding the destruction of books and papers in administration and voluntary liquidation into line with those for compulsory liquidation and bankruptcy.

Removal of requirement to seek permission for certain actions in liquidation and bankruptcy

Question 8: Do you agree that the requirement to obtain sanction to exercise certain powers within Schedules 4 and 5 of the Insolvency Act 1986 should be removed?

and

Question 9: Do you agree that the requirement for liquidators and trustees in compulsory winding up and bankruptcy to obtain authorisation from the Secretary of State to operate a local bank account in place of banking with the Insolvency Services Account should be removed?

and

Question 10: Can you provide an estimate of the approximate cost of obtaining sanction in liquidation and bankruptcy?

Please see the discussion in the main response to the Consultation, which explains why, in our opinion, the powers contained in Paragraphs 1, 2 and 3 of Schedule 4 IA and Paragraph 7 of Schedule 5 IA should remain exercisable by a liquidator/trustee in bankruptcy only with prior sanction. We do, however, agree that the requirement to obtain prior sanction should be removed in respect of the powers contained in the remainder of Schedules 4 and 5.

Removal of requirement to keep time records where remuneration is not on a time cost basis

Questions 11 to 14

We do not intend to respond specifically on these points, as they are more appropriately addressed by IPs. We do, however, agree that it would be sensible, as proposed, to restrict the requirement for IPs to maintain time records to those cases where they are being remunerated on a time cost basis. We would, however, suggest[11] that IPs should be subject, where remuneration is being paid on a percentage realisation basis, to a statutory requirement to provide creditors on request with sufficient information to allow them to understand how the remuneration was calculated.

Meetings of Creditors

Question 15: Do you think that meetings always serve a purpose where held?

We agree that there are a number of meetings during the insolvency process which have little value, particularly (i) meetings of unsecured creditors which an administrative receiver is required to convene under Section 48(2) IA and (ii) final meetings of creditors in a liquidation or bankruptcy where it is clear that there will be no significant dividend payable to unsecured creditors. Where the primary function of a meeting is to present a report to unsecured creditors, the insolvency officeholder should be able to exercise their judgment as to whether or not it would be appropriate to hold that meeting.

Question 16: Do you agree that meetings of creditors should no longer be the default position of gauging creditor opinion?

and

Question 17: Do you think some groups' interests will be unfairly harmed by such an approach with meetings of creditors? If so, do you think such harm could be avoided by incorporating statutory protections?

Subject to the exceptions set out in the main body of our response, we agree that the default position should be that there will be **no** meeting, unless either the office-holder believes that it would have value, or creditors want a meeting to be held.

Question 18: Are there decisions (other than those relating to the approval of voluntary arrangements or an office-holder's remuneration) that you think should only be considered at a meeting of creditors?

As discussed in the main body of our response, we believe that the requirement to hold a Section 98 meeting in a creditors' voluntary liquidation and an initial creditors' meeting in an administration should be retained.

Question 19: Do you think that 10% is a reasonable threshold for objecting creditors? If not, what do you think it should be?

Para 56(1)(a) of Schedule B1 IA contains a 10% threshold (by reference to the total debts of the company) for requisitioning a meeting. This figure appears to have been generally accepted and we can see no good reason for moving from it.

Abolition of all final meetings of creditors in liquidation and bankruptcy

[11] Giving effect to the expectation contained in Paragraph 49 of the Consultation.

Question 20: Do you find final meetings to be poorly attended?

and

Question 21: Do you agree that all final meetings should be abolished?

Our experience is this area is relatively limited, as it is often not necessary or cost effective to have lawyers attend such meetings. That said, our experience is that final creditor meetings are generally quite poorly attended. We therefore agree that, provided that the relevant information is provided to each creditor, final meetings should only be held where either the insolvency practitioner considers that it would be appropriate or creditors requisition a final meeting.

Minor Changes to Meetings of Creditors

Question 22: Do you have any comments on any of the minor proposals on meetings of creditors included in Annex 4?

We generally agree that the proposed modifications are appropriate. We would, however, suggest that a distinction should be drawn between the rules for purely administrative meetings and those applicable to meetings where a significant vote may be taken, such as (i) the creditors' meeting in a CVA or IVA, (ii) a meeting to consider the insolvency officeholder's remuneration and (iii) a meeting requisitioned by creditors. In the latter case, there should be a greater requirement to ensure that the meeting is drawn to the creditors' attention and, to engage creditors. Specifically:-

- **Notifying creditors**: Paragraph (a) proposes scrapping the requirement for the office-holder to seek the court's permission to give notice of a meeting by advertisement only. This proposal may be appropriate for meetings whose main purpose is to update creditors, but it is potentially subject to abuse where (for example) the meeting has been requisitioned by unhappy creditors or the purpose of the meeting is to give creditors the opportunity to consider a significant resolution.

- **Proxies**: It is stated in paragraph (d) that where there is more than one proxy holder, there should be no need to state the order in which they are allowed to exercise their proxy. This may be correct where each proxy comes from the same firm, but this will not always be the case. Creating uncertainty as to who is entitled to vote, particularly where the proxy is given a discretion and the relevant individuals have different voting intentions, is unlikely to prove cost effective, as any (minimal) theoretical saving from not specifying who exactly should vote in such circumstances could swiftly be outweighed by the costs of just one contested case.

- **Timing of the delivery of proxies and proofs**: There seems to be an inconsistency inherent in the proposals in that:-

    - it is proposed in paragraph (f) that proxies only need to be delivered at the meeting itself; while

    - paragraph (m) proposes that proofs and proxies for use at adjourned meetings should be delivered the day before the adjourned meeting unless the chair accepts that later receipt is practical; while

    - paragraph (o) proposes that proofs should be submitted by a specified

deadline before the meeting, unless the chair exercises his/her discretion to accept late proofs.

It may avoid confusion, and save both time and costs, if the same rules and deadlines applied, whether the meeting was an initial or adjourned meeting. Any deadline should also take account of both Rule 8.5(4), which currently gives stakeholders the right to inspect proxies and proofs of debt, and the need for the insolvency officeholder and his/her advisers to have sufficient time to check the validity of proofs and proxies where the meeting will involve a significant vote based on those proxies and proofs of debt.

- **Suspension of Meetings:** We agree that provisions preventing a meeting from being suspended for more than an hour should be amended, in order to allow the chair greater discretion, but would suggest that an upper limit (of perhaps 4 hours) should be retained, as an ability to suspend a meeting indefinitely could potentially be subject to abuse where (for example) the meeting in question has been requisitioned by unhappy creditors**.**

- **Connected creditors:** Paragraph (q) contains a proposal to "*simplify the rules on how a chair scrutinises the value of a connected creditor's vote when considering resolutions at a meeting*". It is not clear whether the proposed simplification is just an amendment to the liquidation and bankruptcy rules to mirror connected creditor provisions in a CVA, administration and IVA, or whether something wider is proposed. We would strongly recommend not attempting to "simplify" the existing connected creditor voting rules in a CVA or IVA context. If any such changes were proposed, they should be the subject of a separate consultation.

- **Paragraph (i)**; We were not entirely sure what was intended by the proposal that "*the requirement to call a meeting [should be scrapped] where no valid vote has been received where meeting had been initially held by correspondence*".

Opting-Out of further correspondence

Question 23: Do you agree that creditors should be able to opt out of receiving correspondence sent by the insolvency office-holder?

and

Question 24: Do you think that creditors should stop receiving documents automatically at the point they cease to have an economic interest in an insolvency? If so, should individual creditors be able to request that the insolvency office-holder continue to send them documents after this point?

We can see no value in sending correspondence and documents to a person who has stated that they do not want to receive these (and will probably put the relevant correspondence or documents straight into the shredder on receipt). Such correspondence is simply "insolvency junk mail" and any creditor should be entitled to opt out of receiving it. We do, however, agree that any notices relating to distributions should be an exception to this rule.

The suggestion that a creditor should stop receiving documents automatically at the point when they cease to have an economic interest in the insolvency is more problematic, simply as (for example) this could theoretically result in a creditor not receiving any documents in a "pre-pack administration". This approach appears inconsistent with the general desire to increase transparency. It may also give the unfortunate impression that an insolvency

officeholder, who owes duties to all creditors, has no further interest in a particular class of those creditors.

It may be that the most appropriate solution would be for the insolvency officeholder to write to all creditors giving them the express choice of opting in or opting out of receiving further documents and correspondence (thereby highlighting the possibility of opting-out) but with non-responding creditors being deemed to have opted in to receiving further correspondence and documents.

Increased use of websites in insolvency proceedings

Question 25 - Do you know how often the existing (post-2010) provisions regarding use of websites in insolvency proceedings are used? Do you think that this measure will increase their usage, and if so by how much?

and

Question 26: Do you agree with the proposal to remove the role of the court where the office-holder intends to place all documents on a website, with only one initial notice to creditors of this fact?

The use of websites can be a helpful communication tool, particularly in larger cases where there are a significant number of creditors, provided that an automatic email notification system is in place, notifying creditors when new documents are uploaded to a website. The system proposed in the Consultation would, however, potentially be subject to abuse if there was no requirement for such a notification system, particularly if the proposed deemed consent mechanism (discussed above) were implemented and a document requesting a consent was uploaded onto the website without any general creditor notification.

We therefore believe that removing the requirement to obtain court approval before posting all future documents on a website may be appropriate, but only where (i) an automatic email notification system is in place, notifying creditors when new documents are uploaded to a website and (ii) the officeholder is required to send hard copies of the relevant documents to any creditors whose e-mail address is unknown to the officeholder (or if the website is temporarily unavailable).

The key challenge which we envisage, for the officeholder, will be obtaining each creditor's e-mail address; we wonder whether it may be appropriate, as part of the current modernisation process, to amend statutory proof of debt forms to include the option of providing the claimant's e-mail address (if they have one).

Reduction in "Unnecessary Contact"

Question 27: Do you agree that facilitating greater use of websites as described could reduce unnecessary contact between the office-holder and the creditors? Or do you think that individual notice is always required?

Where a website has been set up, we agree it makes sense for a notice of a meeting to state that the outcome of that meeting will be available on a website, indicating when it will become available. We would, however, characterise this as improving efficient communication rather than as "*reducing unnecessary contact between the office-holder and the creditors*"

Liquidation and Creditors' Committees

Question 28: Do creditors'/liquidation committees continue to play a worthwhile role where they are formed? Could more be done, through the committee structure or otherwise, to increase creditor engagement in insolvency procedures?

We agree with the view expressed in the Consultation that, where such committees are formed, they can prove a useful tool to progress the insolvency, particularly as a number of provisions contained in the Insolvency Act allow the insolvency practitioner to obtain a sanction or approval of an action either from a liquidation/creditors committee or from the court. One key benefit of having a liquidation/creditors committee is that it offers the insolvency practitioner a more cost effective option than going to court, but the potential value of this option may be eroded by the proposals set out in the Consultation, the effect of which may be to reduce the number of occasions on which such sanction or approval is required.

Minor Changes to Communication and Creditor Engagement

Question 29 Do you have any comments on any of the minor proposals on communication and creditor engagement included in Annex 5?

We agree that the proposed modifications are generally appropriate, but question the logic of the proposal contained in paragraph (e), as it is unclear why a liquidator appointed by the Secretary of State should only give notice of this fact in the Gazette, while a liquidator appointed by the court would, under Rule 4.102(5), still be required to give notice of their appointment to all known creditors within 28 days. It would seem consistent for a liquidator appointed by the Secretary of State to be subject to the same notification requirement as a liquidator appointed by the court.

Administration extensions

Question 30: Do you agree that creditors should be able to extend administrations for 6 or 12 months, rather than only 6?

and

Question 31: Do you think that creditors should be able to extend administrations beyond 12 months? If so, what should the maximum period of an extension be?

We agree that there should be greater flexibility, particularly in relation to large administrations, as the existing requirement to obtain court approval where an administration is expected to last more than 18 months is both time consuming and costly. There is, however, a need for a balance to be struck between administrative convenience and encouraging a swift resolution to the procedure, and we believe that the proposal contained in the Consultation that creditors should be able to extend administrations for either 6 or 12 months is a sensible compromise.

Fraudulent and Wrongful Trading

Question 32. Do you agree with the extension of wrongful and fraudulent trading provisions to administration?

and

Question 33 Could you estimate the financial benefit of this proposal?

Are there cases you are aware of in the past, where the current law has hampered recovery action?

These questions are considered in detail in the main body of our response. In summary, we consider that the wrongful and fraudulent trading provisions contained in the Insolvency Act should be extended to administration, but that the administrator's ability to pursue a wrongful trading action should only arise where the administrator is satisfied that the statutory objective set out in Paragraph 3(1)(a) of Schedule B1 IA can no longer be achieved.

We are, however, not able to estimate the financial benefits of this proposal as (i) the pursuit of wrongful trading and fraudulent trading claims is relatively unusual in our experience (the main role of sections 213 and 214 IA arguably being to act as a deterrent, influencing the behaviour of directors pre-insolvency) and (ii) many of the larger administrations that our members are involved in are followed by a creditors voluntary liquidation, with the result that this proposal would simply accelerate the timing of any action.

Payment of Dividends

Question 34: Do you agree that low value dividends should not be distributed? If you do, is £5 or £10 an appropriate minimum dividend level? If not, what level would you suggest?

and

Question 35: Do you think that there are any circumstances where a payment of less than the minimum dividend level should be paid?

We agree that it generally makes little sense to pay a dividend where the administrative cost of making that payment is greater than the amount paid, and that making such payments is unlikely to increase creditor confidence in the insolvency process. Given the combined cost of issuing, posting and processing a cheque (or making a bank transfer), the removal of a requirement to pay a dividend of under £5 seems appropriate, as a general rule. The removal of the administrative requirement to pay a dividend should not, however, in any way limit the relevant creditor's set-off rights.

We would suggest that the two exceptions to this general rule should be (i) the payment of dividends in a Members Voluntary Liquidation and (ii) the payment of dividends to creditors pursuant to a CVA or an IVA (as those preparing the CVA or IVA proposal should decide whether it was appropriate to include a minimum payment provision in its terms).

Question 36: Do you think that the minimum dividend level should reflect the total of all dividends that a creditor might receive in a case in respect of its debt (i.e. any interim dividends together with the final dividend)? Or should the minimum level be applied to each dividend payment for each distribution?

It may not be possible to state accurately when making an interim distribution what the total distribution is likely to be (as the eventual return to creditors may depend, for example, on the outcome of on-going litigation). It is therefore difficult to see how a minimum payment threshold could work in practice other than by reference to each distribution.

If this approach were adopted, it may be worth considering including a mechanism whereby a creditor whose entitlement was below the minimum payment threshold in one distribution was entitled to catch-up, should there be subsequent distributions which result in the creditor's

aggregate entitlement exceeding £5 (or whatever other minimum threshold is adopted).

Question 37: What savings do you think would be achieved in the costs of administering insolvencies were the insolvency office-holder not to make the payments of dividends less than £5 or £10 ?

We do not have sufficient data to suggest a figure.

Question 38: Do you think that funds not distributed should be used for insolvency investigation and enforcement purposes, or should they be paid to HM Treasury?

It would be unfortunate if this provision were to be characterised as a concealed tax. It would therefore be cosmetically preferable for the funds be used for insolvency investigation and enforcement purposes, so that any unpaid creditors could see that any savings were applied in overall creditor protection.

Question 39: Do you agree that a creditor's right to unclaimed dividends should lapse over time? If you do, do you think that 6 years after the payment is initially made is a suitable length of time to allow for a creditor to claim dividends owed to them? If not, what length of time do you suggest?

We agree that a creditor's right to unclaimed dividends should lapse after 6 years, where a cheque has been paid to that creditor, but that cheque has not been presented for payment. It is, however, not clear whether this would still be a significant issue if, as proposed, the Insolvency Rules were amended to create a presumption that dividends would be paid by bank transfer rather than cheque.[12]

There should, however, be a statutory requirement that the relevant officeholder should, before leaving office, write to the last known address of any creditor who has failed to cash a cheque, warning them that their rights may lapse and explaining the procedure for obtaining payment where this has become the responsibility of the Secretary of State.

Crystallisation of floating charges in a Scottish administration

Questions 40 to 42

The questions relate to matters of Scottish Law, and are therefore beyond the ambit of the CLLS.

Streamlining procedure where uncontested creditor's winding-up or bankruptcy petition served

Question 43: Do you agree with the proposal to enable debtors to consent to a winding-up order / bankruptcy order where a petition has been served by a creditor?

and

Question 44: Do you think there will be any circumstances where, despite consent being received by the court from the debtor that they do

[12] Annex 6, Part 2, Para (c)

not object to an insolvency order being made, that a hearing will still be necessary?

and

Question 45: Do you agree that a winding-up petition presented by the company itself need not follow the same procedure as a petition filed by another party?

and

Question 46 Can you think of any drawbacks with having a streamlined process in these cases? Are there any parts of the winding-up petition procedure that you would like to see retained in this streamlined process?

and

Question 47: Do you agree with there being a role for an Adjudicator in this process?

As noted in the main body of our response, this question is not entirely straight-forward, in a corporate context, as there may be differences of opinion between a company's shareholders and its directors, or between various creditor constituencies, as to whether or not liquidation is an appropriate option.

We also question the underlying assumption that "*where the company is petitioning itself, there will be no dispute for the court to rule upon,*"[13] as, for example, (i) the company's shareholders may not agree with the directors' decision, (ii) creditors and other stakeholders may not agree with the directors' decision, (iii) there may be jurisdictional issues and (iv) the winding-up petition may be based on S123(1)(e) or S123(2) IA, both of which require the exercise of judicial discretion. Indeed, the fact that the company is using the compulsory liquidation procedure rather than the CVL procedure may, in some cases, be indicative of the fact that there is an underlying dispute which the court may need to rule on.

Overall, our view is that removing the requirement for a hearing may result in incorrect legal outcomes and may also effectively disenfranchise shareholders and other stakeholders, making the potential downside of this proposal disproportionate to any identified cost savings.

Official Receiver

Question 48: Do you agree that the official receiver's duty to investigate the cause of failure of a company in liquidation should be discretionary, as it is in bankruptcy?

We agree that there is little value in duplication, and that the official receiver's duty to investigate the cause of failure of a company in liquidation should be discretionary in those cases where the official receiver is not acting as the liquidator.

We think that the proposal becomes more difficult (at least cosmetically) in those cases where the official receiver is acting as liquidator, as it is difficult to understand how the official receiver could reach an informed view in relation to his/her reporting duties under section 7(3) of the Company Directors Disqualification Act 1986 without having investigated, to some extent, the causes of the company's failure. The best solution in this scenario may therefore be to make it clearer, if necessary, that the official receiver can exercise discretion as to what level of investigation is appropriate.

[13] Para 157

Question 49: Do you agree that the position of receiver and manager in a bankruptcy should be scrapped and instead the official receiver will become trustee upon the making of the order?

We agree with the view reached in previous consultations that the receiver and manager role has become unnecessary and that the official receiver should be appointed trustee upon the making of a bankruptcy order, in the same way as he/she is appointed liquidator on the making of a winding-up order in a compulsory liquidation

Fast-track voluntary arrangements

Question 50. Do you agree that FTVAs should be abolished?

If, in current economic conditions, on average only one FTVA is being approved every year, it would clearly appear that they do not serve any useful purpose and should therefore be abolished.

Minor changes

Question 51: Do you have any comments on any of the minor proposals that seek to improve insolvency processes included in Annex 6?

We generally agree that the proposed modifications are appropriate. We would, however, make the following recommendations:-

- **Definition of "creditor":** It will be necessary to ensure that no unintended consequences arise from this proposed definitional change. To take one example, a creditor should not able to avoid the provisions of Rule 4.90 by exercising a right of set-off which falls outside the scope of that Rule and then arguing that, as the effect of the set-off was to repay its debt in full, it was no longer a "creditor" and this rule therefore had no application to it.
- **Conversion of debts in a foreign currency:** We agree with the proposed approach but would strongly recommend that there should be a legislative requirement, in order to maintain creditor confidence, that the insolvency officeholder should adopt a consistent approach, to the extent possible, when agreeing the conversion rates for each relevant currency and that the conversion rate should be a published rate of exchange (for example, the rate published by Reuters or the FT). It would follow that from the requirement for consistency that the same published source should be used (where possible) for all currencies that need to be converted.
- **Exits from Administration**: The Consultation refers to a need to "*consider the efficiency of the process by which administration can exit into dissolution or creditors' voluntary liquidation and clarify them, if necessary*." We agree that this is an area which could potentially be simplified, as could the mechanism for the exit of a company from administration once its creditors have been repaid in full, but cannot respond in detail at this stage, in the absence of any firm proposals. We would suggest that this is an area which might benefit from a separate, specific, consultation exercise.

Proposals to change how IPs report director misconduct

Question 52: Do you agree with the proposal that a return be required in respect of all cases? If not, please explain why.

There is a good argument for requiring a return to be submitted in all cases, whether or not misconduct is indicated, in order to provide a mechanism for checking that all cases have been considered by the IP. An alternative, perhaps simpler, option might be to require the IP to confirm, where no return was submitted, that they had considered the position and concluded that there was no relevant misconduct.

The reference to using reports on individuals who have acted properly to "*enhance our intelligence base*" causes some concern because it is not clear how this enhanced database, which would presumably involve incurring additional costs, would be used, or why it is necessary. The underlying implication seems to be that a director who has always acted properly, but who has been unlucky enough to be involved in a number of failed companies, may be subject to additional scrutiny. This seems inconsistent with a desire to encourage an entrepreneurial approach.

Question 53: Do you agree with the proposal that where liquidation follows administration office holders should not be required to submit a further report? If yes, please estimate the average time saved per case based on the current form(s).

We agree with the logic of this proposal, particularly where the same IP holds both offices, but we are not in a position to estimate the time that would be saved by removing this duplicative requirement. It is, however, important that the subsequent liquidator should always retain the right to submit a further report, and that such report should be given an appropriate level of consideration.

Questions 54-68

These questions are specifically directed at, and best answered by, IPs who are taking appointments on a regular basis.

9 October, 2013

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