ICAEW
REPRESENTATION 61/21

FIRST REVIEW OF THE INSOLVENCY (ENGLAND AND WALES) RULES 2016: CALL FOR EVIDENCE

Issued 30 June 2021

ICAEW welcomes the opportunity to comment on the First Review of the Insolvency (England and Wales) Rules 2016: Call for evidence published by Insolvency Service on 11 March 2021, a copy of which is available from this link.

We believe that some recent changes to the Rules have been counterproductive and that improvements could be made. The Rules form only part of the overall regime which has been subject to extensive change in recent years; we believe that a more holistic review of the regime and the place of the Rules within it could be beneficial.

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This response of 30 June 2021 is made by ICAEW's Business Law Department and reflects consultation with its Insolvency Committee and other expert groups.

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KEY POINTS

1. Some of the recent changes to the Rules have not, in our view, turned out to be helpful. In particular, we believe that the prescriptive requirements for decision taking and constraints on holding meetings are burdensome and have diminished, rather than enhanced, creditor engagement, this being the opposite of government policy intent.
2. It may be possible to address these issues relatively simply eg, by giving more discretion to Insolvency Practitioners ('IPs') in appropriate cases and we hope that government will do this.
3. If this review results in further changes to the Rules, we hope that change will be implemented through a consolidated updated version rather than through separate instruments from which users then need to produce their own consolidated version (as was the case before). We would also suggest that proposed changes be made at the same time in a coordinated way. Frequent changes/tweaks to the Rules and related Statements of Insolvency Practice (SIPs) can be as disruptive to deal with as difficulties caused by the Rules themselves.
4. The Rules constitute only part of the UK's insolvency regime and various changes to law have been made over the past few years that cumulatively amount to significant change. These include, most recently: changes to rights and powers of HMRC including the reintroduction of Crown Preference (through the Finance Act 2020); increased powers of the Pensions Regulator (under the Pensions Act 2021); the Corporate Governance and Insolvency Act 2020 (CIGA), with its focus on survival of the company; and regulations on connected party-pre-packs.
5. Such changes have impacted prospects of creditor returns on insolvency and may have diminished their appetite to engage in the relevant processes. We believe that there is scope for the Rules to better align with creditor needs, particularly around creditor reporting (on which we comment further under Question 4) and suggest that a broader review might be helpful in that context. This could consider ways in which creditors and other stakeholders would feel more engaged in the process and which achieves the best balance between accountability, monitoring for practitioners and the profession, and costs of compliance.
6. We note that the Rules do not appear to have reduced the current reliance on SIPs. While we believe SIPs play a useful role, it is not always clear what criteria government applies in deciding what should be covered by the Rules or by SIPs. For instance, the new regulations on connected party pre-packs left many unanswered questions that we think ought to have been addressed by Parliament at the time and not left for the profession and Insolvency Service to seek to address through SIPs or guidance.
7. We have focused on aspects of the regime which are closely related to the Rules. However, there are other aspects that could be improved eg, conflict between employment law and insolvency law. Given this and the extent of changes in related laws outlined above it could be useful for government to hold a wider review of the regime, including whether there are alternatives to such a rules-based approach; the Insolvency Service's planned Insolvency Research and Technical Conference might be a useful forum to consider this further.

ANSWERS TO SPECIFIC QUESTIONS

Question 1. Do the Rules provide an appropriate framework for the UK's insolvency regime?

Question 2. Is the framework provided by the Rules clear?

8. We suggest that the Insolvency Act 1986 (the Act), rather than the Rules, provides the framework for the UK's insolvency regime; the Rules put flesh on the bones of the Act (and run to over 400 pages). In addition to the Act and the Rules, case law plays an important role (as do SIPs). The Rules cannot therefore meaningfully be read in isolation.
9. Given the complexity of the regime (on which we comment further below), we agree that clarity of the Rules should be judged from the perspective of the primary users, including IPs and well-informed creditors. IPs are required to pass exams which include elements of insolvency and related laws. Our licensees are required to have practical experience, continual learning and are bound by a code of ethics. They are expected to be familiar with related matters such as the Insolvency Act and relevant case law (and to seek advice where necessary). Even where the Rules are sufficiently clear to IPs, it does not mean that they would be clear to the public generally. Indeed, insolvency law is extremely complex and we do not believe that it is widely understood.
10. The consultation invites comment on various policies underlying the Rules and we agree that government should consider not only whether the Rules are coherent in themselves, but also whether the wider framework is serving the UK as well as it could (see Key Points above).

Question 3. Does the updated language used in the new Rules improve upon that used in the Insolvency Rules 1986?

11. In general terms the updated language is an improvement on the previous Rules. However, many of the changes could be regarded as cosmetic, eg, gender neutral language. It is the substance and to some extent ease of use that concerns those bound by, or whose rights derive from, the Rules (and on which we comment below).
12. Notwithstanding the changes, the drafting of the Act and the Rules results in maze-like complexity at times. This is illustrated in our analysis of the decision-making process for Creditors' Voluntary Liquidations ('CVLs') outlined below. Even use of relevant defined terms is challenging, eg, the Rules provide a definition of 'physical meetings' which is dependent upon reading the relevant provisions of the Act (which does not itself use the term) and does not bear the ordinary meaning of the words (ie, of people being physically present at a meeting).

Question 4. What changes, if any, could be made to ensure that the Rules provide an appropriate framework for the insolvency regime or to improve their clarity?

13. We comment here on the Rules that we think problematic, regardless of when the Rule was introduced or the legislative initiative from which it derives. If something is not working well in practice, then we would urge government to put it right, whether that requires a change in policy or a change in drafting of primary or secondary legislation.
14. We appreciate that amending the Act or Rules is potentially administratively challenging, but if the regime is not flexible enough to address practical concerns that arise, consideration should be given to moving away from such a prescriptive rules-based regime (see Key Points above).

Meetings

15. The reforms have been unhelpful where they constrain the ability of IPs to hold certain meetings.
16. We highlight specific concerns under relevant topic headings below (eg, CVLs). To put this in context, we note that, as the experience of the pandemic has made clear, physical business meetings can be effective and productive and virtual meetings can be an acceptable

substitute when necessary. In future, hybrid working is likely to become commonplace. Hybrid meetings, simultaneously physical and virtual, would offer a good mechanism for encouraging engagement and we believe that the legislation should facilitate them. It is difficult to see that the current requirement to ask creditors to request a meeting is efficient or necessary.

17. Where the reforms have facilitated use of virtual meetings, we think they have been useful. For some processes, eg, in Individual Voluntary Arrangements ('IVAs'), virtual meetings are regularly used as they allow modifications easily to be proposed and agreed. However, meetings where attendees are physically present can have advantages in some circumstances and we believe that conveners of meetings should have the option to require them if appropriate.

CVLs

18. CVL is one of the most effective procedures for winding up affairs of many companies. We believe that the procedure is fit for purpose by objective and design and that demand for it is likely to increase as government COVID-19 support measures are wound-down. We believe therefore that government should make it as simple as possible for creditors (the key stakeholders in a CVL) to have their say and that the process is as efficient as possible. One of creditors' most significant powers is the ability to choose the liquidator.

19. The new Rules on appointment of a CVL liquidator replaced the procedure for meetings under what was Section 98 of the Act. We and others (eg, R3) expressed our concerns about this reform at the time and believe that it has proved detrimental. The current process is burdensome (see under Question 12 for more detail on this) and can be difficult to implement; we believe that creditor engagement has diminished here.

20. Under the old procedure, the creditors voted for the liquidator's appointment at a physical meeting convened under Section 98. The meeting was held within 14 days of the shareholders' resolution putting the company into liquidation and often on the same day. A director of the company chaired the meeting and creditors could ask about the reasons for the company's failure. If a creditor did not want to personally attend, they could submit a proxy form to nominate and vote for their preferred liquidator. The S.98 meeting was an excellent tool for creditor engagement because it was easy for them to understand and participate. Remote attendance was not a feature of S.98 meetings (but was not expressly forbidden).

21. We believe that an equivalent procedure should be re-introduced (eg, by amendment of Section 246ZE of the Act), but in a modernised way, so that individual creditors can choose whether to attend the meeting remotely or physically. This would engage creditors from all walks of life including, for example, people with childcare responsibilities that might have prevented them from attending a physical S.98 meeting. As with other similar remote meetings, it would be necessary to ensure that participation and voting is fairly managed, but we believe that could be dealt with relatively easily (eg, by regulatory guidance).

Decision procedures

22. We have outlined how deemed consent provisions operate for CVLs and some of our related concerns under Question 12 below. Similar concerns arise in other contexts too. In our view, deemed consent is burdensome, its implementation is difficult for creditors to understand, its objection procedure is clumsy and complicated and, most significantly, it diminishes, rather than enhances, creditor engagement with the proceedings.

23. At a meeting, whether physical, virtual or hybrid, creditors also have a meaningful opportunity to engage with each other. We suggest that deemed consent should be scrapped and

powers to hold meetings extended. We believe that IPs should have discretion regarding the form of meeting to suit relevant circumstances.

24. Other decision procedures can be useful and efficient (eg, written resolutions for approval of fees) and the discretion to use these should be retained.
25. The deemed time for decisions made either by a decision procedure other than a meeting or by deemed consent is 23.59. We cannot see the need or attractiveness of this and suggest that it be replaced with a time during business hours, such as 11.59 or 16.00 for example.

Creditors' committees

26. As physical meetings are no longer the default forum for decisions by creditors, the opportunity for creditors to establish a committee on their own initiative and on a relatively informal basis has, in effect, been lost in relation to relevant procedures. The IP is now obliged to send creditors a notice inviting them to decide whether to establish a creditors' committee for every decision (Rule 3.39 for administrations, R. 6.19 for CVLs and R.10.76 for bankruptcies) and creditors must 'decide' under the creditor decision-making processes referred to in section 246ZE (and section 246ZF) of the Act.
27. The result is that it is harder for creditor committees to be formed and we doubt that this is either efficient or helping with creditor engagement.
28. Conversely, in a compulsory liquidation, the ability to seek a committee is only available where a decision is sought from the creditors upon appointment; there is no ability to form a committee later. This makes creditor engagement challenging where further input is required, for example in relation to fee approval.
29. We believe that committee invitations should be issued at first meetings and at the next meeting after sufficient creditors to form a committee request one. This should also apply to compulsory liquidations.

Annual progress reports

30. We do not believe that annual progress reports required by the Rules are always useful for creditors and are concerned that the cost of providing the information can be disproportionate. We give this as an example of a topic that might usefully be considered as part of a wider review of the regime (see Key Points above).
31. There are various issues that could be considered in such a review. Obtaining direct evidence of the creditor perspective will be important. Viewed from the perspective of IPs, it seems that creditor interest is limited and falls away very quickly from the first notification.
32. The length of the reports and level of detail required for fees may not be useful for creditors when, for instance, the case is straightforward and there is little prospect of any dividend being paid. If creditors were to be interested in progress, they might be better served by having annual meetings reinstated now that it is possible for them to be held on-line; they would then be able to raise questions and have the report address issues that are of concern to them (rather than having a generic report).
33. Where consumers are involved, they are typically engaged early in the process and IPs provide detailed information on an ongoing basis in whatever way they find most efficient and helpful. This is not prescribed, which perhaps suggests that more discretion could be allowed as regards annual progress reports.
34. Similarly, insolvency can lead to creditors becoming interested in the initial stages (eg, when prospects of recovery are uncertain), and again IPs will typically engage with them as required, even outside any formal reporting requirements.

35. If annual progress reports are required because of the needs of creditors and others, then it is unclear why the Official Receiver should not subject to the same reporting (where applicable) and a review could usefully also encompass the role of the OR.

36. Creditor needs vary and the reports may also serve a compliance related function, so we believe that consultation with interested parties would be needed to establish whether this is a sufficiently material concern to call for a change in the Rules and what better alternatives there may be. Should government wish to pursue this further (whether as a self-contained issue or part of a wider review suggested in Key Points above), we would be happy to provide further input.

Draft final accounts in Members' Voluntary Liquidations

37. We believe that the requirement for liquidators to prepare and send to members both draft final accounts and final accounts in Members' Voluntary Liquidations ('MVLs') is unnecessary, adds to costs and can cause confusion (because members assume the drafts are final and do not understand why they receive another set of accounts later). We suggest that the requirement for draft final accounts in MVLs should be removed. If circumstances are such that office-holders would find it useful to provide draft final accounts, they should have discretion to do so, but the liquidator's release should be deferred if the final accounts are not positively approved.

Meetings for Pre-packs

38. Transparency would be enhanced by disapplying Para 52, Sch B1 of the Act where there has been a pre-pack so that (in combination with our suggestions on meetings generally), there is a meeting to consider the administrator's proposals in all pre-pack cases.

Manolete Partners Plc v Hayward and Barrett Holdings Ltd.

39. Government will no doubt be aware of the judgment in the above case where the judge held (with regret) that any party wishing to bring a company claim (whether that party is the office holder or an assignee) will have to issue a part 7 claim even in circumstances where there are related office holder claims in the same insolvency; in which case two sets of proceedings are required.

40. We believe that amendments to the Rules required to remedy this undesirable outcome should be made.

Small Debts

41. The cost involved of making distributions of small dividends to creditors can be disproportionate. As an example, we are aware of a recent liquidation of a company which has over 15,000 customer accounts with unclaimed balances totalling around £50,000. Over 12,000 customers have potential claims of between £0.01 and £1.00 (totalling under £3,000). Under the relevant Rules (eg, 14.1) the office-holder is required to give notice to all creditors to submit claims, or deal with them as Small Debts no matter the value. In the example above it would inevitably cost more than £3,000 to correspond with the potential creditors and deal with queries/claims. It would be more cost effective for the liquidation estate if the office-holder could pay de-minimis amounts (eg, amounts under £1.00) to charity and not proactively correspond with those potential creditors. This issue can be exacerbated where creditors require to be paid by cheque.

Deadline for making distributions/declaring dividends

42. Rule 14.30 requires the office-holder to declare the dividend within two months of the last date for proving. If the two-month deadline is missed, the office-holder is required to issue a

new notice, to creditors who have not proven their claims, of the office-holder's intention to declare a dividend.

43. Two months may well not be enough time for the office-holder to properly deal with creditor claims before the deadline. As an example, if the office-holder receives a number of claims shortly before the deadline for claims and more information is needed for the office-holder to adjudicate the claim, the office-holder would give the creditor (say) 21 days in which to provide additional information/documentation. If after the creditor has provided the additional information (or failed to do so), the office-holder adjudicates the claim and either (1) rejects it in full, (2) rejects it in part, or (3) values the claim, the creditor would have 28 days, from receipt of the office-holder's decision on the claim, to appeal to Court to have the office-holder's decision to be reversed or varied. Allowing extra days for postage and for the office-holder to properly consider complex claims (and maybe seek advice from solicitors or agents), it would not always be possible to meet the two month deadline. We suggest that government should consider extending the period, eg, from two months to four months (as it was under the Insolvency Rules 1986).

Fees - the 18-month rule

44. Rule 18.22 provides that a liquidator or trustee is entitled to fees on the realisation and distribution scale rate in schedule 11 where in a winding up by the court or bankruptcy they have asked creditors to fix the basis of their fees and creditors have not done so, or in any event if the basis of their remuneration has not been fixed by creditors within 18 months of the officeholder's appointment. But Rule 18.22(1)(a) does not specify a time period, so it is unclear whether the officeholder can ask creditors to approve the fee basis at any time during the insolvency (even though after 18 months they have an 'entitlement' to scale rate). We understand that the Insolvency Service believe that an IP can ask for creditor approval under rules 18.18 – 18.20 at any time and we believe that the same principle should apply to a liquidator in a compulsory liquidation. It would be helpful if (in all cases) this could be made clear in the Rules themselves (or formal public guidance were to be issued on the subject).

45. The second limb of 18.22 seems to allow IPs to apply scale rate after 18 months whether the IP has requested approval or not, as the rule starts by saying 'in any event…' There was a similar provision under the 1986 rules, but a subsequent Dear IP required IPs to actively seek to get creditors to approve a fee basis first. That Dear IP specifically applied to the 1986 rules 4.127 A and 6.138A, so is no longer directly applicable. Also, in rule 18.23 (where the IP can apply to court to fix the basis of their remuneration), the IP is specifically obliged to have first attempted to fix the basis of remuneration. If the intention is that IPs are to be so obliged in compulsory liquidations and bankruptcies, the Rules, as written, are not sufficiently clear. We would also support a position where trustees and liquidators in a compulsory liquidation are not permitted to draw fees on scale rate without having first sought approval to a fee basis from creditors.

Fees - Changes in rates or amounts

46. Rule 18.24 provides that an officeholder who considers the rate or amount of remuneration fixed to be insufficient can ask creditors to increase the rate or amount or change the basis in accordance with Rules 18.25 to 18.27, or can apply to court. Rule 18.25(2) provides that where the fees have been fixed by a committee, the officeholder can apply to creditors. That specific Rule is silent on the position where the general body of creditors first approved the basis. We understand that some consider that the only option in that case is to go to court. Conversely, some believe Rule 18.24(a) allows an IP to ask the general body of creditors, provided one of the subsequently mentioned exceptions does not apply (although as indicated above, 18.25 only covers the position where fees have been agreed by the committee and makes no mention of the position where creditors have approved the fee

basis). While Rule 18.29 allows an IP to seek a change in fee basis where there has been a material and substantial change in the circumstances which were taken into account in fixing it, this Rule does not also say that it applies where a mere increase in amount or rate (as opposed to basis change) is required. Where an IP has sought fees on a time cost basis, the IP can seek a revised fee estimate, if the fees may exceed the original quantum for any reason (and not just for a material and substantial change in circumstance). We believe the Rules should be clarified for those cases where an increase is needed for fees agreed on a fixed and percentage basis.

Administrator's proposals

47. Rule 3.35 sets out the required contents of an administrator's proposals. Where the proposals envisage that the administration will end by the company moving to CVL, subsection (j) requires the proposals to include 'details of the proposed liquidator'. It is unclear whether this requirement is satisfied by stating that the administrators and any successors in office will be the proposed liquidators. There can be an issue if one or both of the administrators is / are replaced by a block transfer order - without such a provision the proposals would need to be revised (at cost to the estate) to provide for successor IP to be appointed liquidator.

48. Rule 3.39 requires a notice inviting a committee etc. to be sent 'to the creditors at any other time when the administrator seeks a decision from creditors'. It is unclear whether this applies where a decision is being sought only from the preferential creditors and, if so, whether the notice should be sent only to the preferential creditors or to all creditors.

Notices to creditors of decision procedures

49. Rule 15.8(3)(g) requires the convenor to tell creditors that those that have opted out may nevertheless vote if they provide a proof. We believe that the drafting of this should be reviewed for consistency with other parts of the Rule to take account of those circumstances where creditors cannot already have opted out (for example when seeking approval of the liquidator's appointment under section 100).

Question 5. Have the policies in the Deregulation Act 2015 and the Small Business, Enterprise and Employment Act 2015 been fully implemented in the Rules?

50. See our response to Question 4 above.

Question 6. Is the Rules' implementation of Deregulation Act and Small Business Act policies clear?

51. See our response to Question 4 above.

Question 7. Does the Rules' implementation of Deregulation Act and Small Business Act policies operate effectively and efficiently?

52. See our response to Question 4 above.

Question 8. What changes, if any, could be made to improve the clarity, effectiveness or efficiency of the Rules that implement the Deregulation Act and Small Business Act policies?

53. See our response to Question 4 above.

Question 9. Are the new policies introduced by the Rules the right ones for a modern, efficient insolvency regime?

54. We have identified in response to Question 4 where we think the Rules (including those reflecting the policies) lead to inefficiency, eg, because they are insufficiently flexible in application as regards modern technologies. While we support use of modern technologies, it is important that the regime also accommodates those without access to those technologies, so that alternatives (eg, paper-based processes) should continue to be made available as long as necessary.
55. The UK regime remains well respected internationally, but the legislation seems overly complex and it, or related legislation, has undergone significant change in recent years. Some changes, eg, the restoration of Crown Preference, seem regressive and at odds with others (eg, the introduction of a moratorium) aimed at helping the enterprise culture.
56. There are other unresolved challenges (eg, conflict between employment law and insolvency law). We are not therefore convinced that the regime as a whole or the role of the Rules within it is as efficient and 'modern' as might be desirable and we think that a more holistic review might be useful (see Key Points above).
57. Another example relates to the costs of carrying out pre-appointment ethical and AML checks. The recent SIP 9 FAQs issued by the RPBs make clear that IPs cannot generally recover these costs, there being no statutory provision for the costs to be recovered. But it is not clear that the outcome results from deliberate government policy or why such a policy should apply to pre-appointment checks but not ongoing customer due diligence (which is recoverable), given that the work is required in both cases.

Question 10. If the new policies introduced by the Rules are not fit for purpose, what alternative policy should be adopted?

58. See our response to Question 4.

Question 11. Is the Rules' implementation of new policies clear?

59. See response to Question 4.

Question 12. Does the Rules' implementation of new policies operate effectively and efficiently?

60. See response to Question 4 generally.
61. We outline below the current procedures for appointment of a CVL liquidator and some of the difficulties arising by way of further evidence to support our proposal for reform outlined under Question 4.
62. Creditors' choice of liquidator is made under Rule 6.14, in the first instance using either the deemed consent procedure or a virtual meeting. In practice, the option of a virtual meeting has not proved popular. From a director's point of view, why convene and chair a meeting of creditors who may hold you responsible for losing their money if you do not have to?
63. From an IP's point of view, the requirement in the definition of a virtual meeting (Rule15.2) that 'persons may participate in the meeting including communicating directly with all the other participants in the meeting' can be problematic, eg who is responsible if technology limitations affect the ability of participants to communicate directly such that the meeting does not qualify as a virtual meeting? We also note that this is not consistent with the approach when creditors attend physical meetings remotely under R15.6(6) where there is no specific requirement for them to be able to communicate directly with all other participants in the meeting.

64. The deemed consent procedure is therefore generally used in practice. It is governed by S.246ZF, which provides that if less than an 'appropriate number' (defined in Section 246ZF(6) of the Act) of relevant creditors object to a proposed decision then creditors are to be treated as having made that decision. Alternatively, creditors can force a physical meeting if a 'minimum number' (defined in S.246ZE(7)) request. Either way, unless creditors can round up enough support and notify the directors in the prescribed manner, they are stuck with the company's choice of liquidator.

65. If a threshold is met for a physical meeting, Rule 6.14(4) applies as follows:

> 'Where the directors have sought a decision from the creditors through the deemed consent procedure under paragraph (2)(a) but, pursuant to section 246ZF(5)(a) (deemed consent procedure), more than the specified number of creditors object so that the decision cannot be treated as having been made, the directors must then seek a decision from the creditors on the nomination of a liquidator by holding a physical meeting under rule 15.6 (physical meetings) as if a physical meeting had been required under section 246ZE(4) (decisions by creditors and contributories: general).'

66. R15.6 explains the convener's responsibilities in connection with the physical meeting. It also sets out time limits for creditors to request a physical meeting although those provisions are qualified by R6.14(6) for a creditors' meeting to nominate a liquidator. If R15.6(6) is complied with, a creditor can attend a physical meeting remotely.

67. The R6.14 deemed consent procedure is instigated by the company's directors and they are the conveners if a physical meeting is subsequently held. These are complicated procedures imposing significant responsibilities on directors at a time when they are dealing with the stress of their company's failure.

68. We believe that the end result of the above is that creditor engagement on appointment of a Liquidator has, in practice, been reduced as a result of the reforms and we believe that further reform should be made to make creditor meetings (with workable options for remote participation) mandatory.

Question 13. What changes, if any, could be made to improve the clarity, effectiveness or efficiency of the Rules that implement new policies?

69. See response to Question 4.

Question 14. (Rule 1.38) In your estimation, what percentage of creditors choose to opt out of receiving information?

70. No comment

Question 15. (Rule 1.38) Could the creditor opt-out process be improved, and if so how?

71. No comment.

Question 16. (Part 15 Chapter 2) What changes could be made to assist office holders with the decision-making processes?

72. See response to Question 4.

Question 17. In your estimation, which changes to the Rules have made it easier or more difficult for creditors in an insolvency to engage with the process?

73. The changes abolishing initial meetings and reducing flexibility for IPs to call meetings have made it more difficult for creditors to engage. See our response to Question 4 above for more detail.

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