



CALL FOR EVIDENCE: REVIEW OF THE PERSONAL INSOLVENCY FRAMEWORK

Issued 21 October 2022

ICAEW welcomes the opportunity to comment on the Call for Evidence: *Review of the personal insolvency framework* published by the Insolvency Service on 5th July 2022, a copy of which is available from this [link](#).

For questions on this response please contact our Business Law team at representations@icaew.com quoting REP 88/22.

We believe that government should consider radical reform of the personal insolvency regime. It may need to extend the scope of the current call for evidence to do this to cover elements of the regime covered by FCA in addition to insolvency processes covered by the Insolvency Service.

It could then consider scope for simplifying the regime by making FCA responsible for all 'consumer debt' relief and insolvency processes, leaving the Insolvency Service regime to focus on non-consumer insolvencies.

We believe that Government should also consider how reduce the volume of avoidable personal insolvencies, for instance through education of the public and introducing measures to restrict access to easy credit where appropriate.

This ICAEW response of 21 October 2022 is made by ICAEW's [Business Law Department](#) and reflects consultation with ICAEW's Insolvency Committee.

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KEY POINTS

NEED FOR A MORE HOLISTIC REVIEW

1. We believe that the personal insolvency regulatory regime is flawed; its complexity means it is difficult for many individuals in financial difficulty to choose the most appropriate solution for their circumstances.
2. We therefore welcome this call for evidence. However, we believe that the scope of the review is too narrow and that Government should consider all of the debt relief processes available to individuals, not just the insolvency processes within the remit of the Insolvency Service. It should also consider how it might reduce the number of individuals getting into financial difficulty in the first place, eg through education, the welfare system, or regulation to restrict availability of unaffordable credit.
3. While the review is open in nature, it focuses on potential changes to the current procedures. However, we believe government should consider more radical change, for instance whether the current procedures should be replaced in their entirety.
4. We are concerned that government has approached insolvency reform on a piecemeal basis over the last couple of decades and it is becoming difficult to know what its underlying objectives are.
5. We suggested in our response to the consultation on the Future of the Insolvency Profession ([Rep 30/22](#)) that an extensive review along the lines of the Cork Review 40 years ago is needed. This would consider both personal and corporate insolvency processes (which have areas of overlap). However, if government prefers to consider personal insolvency as a distinct matter, we urge it to consider it in broad terms so that the regulatory regime (and any other measures) can be tailored to meet those objectives in a holistic way, ideally resulting in a simpler regime that will help individuals make good choices, improve efficiency, and reduce tensions faced by regulators.

REGULATORY RESPONSIBILITY FOR CONSUMER INSOLVENCY

6. A fundamental question that the Insolvency Service has not raised, is whether regulatory responsibility for personal insolvency processes (or a subset of them) should be moved from it to FCA. We have suggested that this should be considered in the past (including in [Rep 30/22](#) referred to above) and continue to believe government should consider this carefully.
7. There would be obvious advantages in terms of potential simplification of the regime and related efficiencies and regulatory coherence (given the FCA already has a consumer focus and regulates the main providers of credit to consumers). Government should be considering the whole lifecycle of debt, the problems that arise and all the potential solutions, of which formal insolvency procedures are only part.
8. We believe that the FCA would, in principle, be the most appropriate regulator for what we term 'consumer debt' and related processes for debt relief. The Insolvency Service would continue to be responsible for non-consumer personal insolvencies (as well as corporate insolvencies).
9. It would, however, be necessary to ensure that FCA is appropriately resourced to carry out such responsibilities and it would be necessary to ensure that there continue to be enough suitably skilled practitioners to provide the relevant services to the debtors. It may be that this would call for continued involvement of one or more professional bodies.
10. It would also be necessary to define what is meant by 'consumer debt' in this context. The priority should be to streamline and simplify the process for the relatively large number of individuals in distress of modest means who are not suspected of dishonesty. It may be that

individuals who have some business interests should still be treated as consumers for this purpose.

11. Setting relevant perimeters may not be straightforward, but we believe government should at least consider (through further consultation) if, and how, it might be done. Factors to be considered might include:
 - Aggregate amount of debt/liabilities
 - Amount of assets (consumer processes being largely designed for those with modest assets)
 - Proportion of debts owed to banks and other mainstream providers of credit to consumers (and regulated by FCA)
 - Whether registered for VAT or PAYE
 - Whether homeowner (and perhaps amount of equity in the home)
 - Whether there is reason to suppose the debtor is 'dishonest'
 - Whether a shareholder or director in a company
 - Complex arrangements, eg a partner in a partnership with significant assets or a sole trader with ongoing trading arrangements.
12. A mechanism may be required to enable a case to be moved from the consumer regime to the non-consumer regime if appropriate, eg if new facts emerge after the initial characterisation (such as complexities arising from interests in partnerships) where involvement of Insolvency Practitioners (under the insolvency regime) would be appropriate.

EDUCATING THE PUBLIC

13. As noted in the consultation, a person may become insolvent for a variety of reasons, ranging from extreme poverty where such an outcome seems inevitable (which raises questions for government that go beyond the insolvency regime) to reckless extravagance and irresponsibility. Between the two extremes are those who become insolvent because they failed to manage their finances appropriately and could have remained solvent had they done so (without undue hardship associated with extreme poverty).
14. Government should therefore ensure that our education system provides children and young adults with the basic tools to manage their finances, including basic maths skills and ability to plan for income and expenditure and the cost of borrowing.
15. The insolvency regime is not a substitute for financial education. While some individuals do learn relevant skills as a result of experiencing insolvency, others do not (and are likely to find themselves in financial difficulty again). We are not sure that changing the balance to be more, or less, debtor friendly will have much impact on this.

RESTRICTING EASY CREDIT

16. The consultation paper notes that the current regime developed on the assumption that expansion of household credit would lead to economic growth, but that policy institutions such as the International Monetary Fund now believe that, on the contrary, high levels of household debt can reduce or stifle economic growth, as households carrying heavy debt loads must reduce expenditure.
17. While this finding may support the 'fresh start' objective for an insolvency regime, the opposite might also be true. If increased consumer credit is bad for the economy, then perhaps Government should seek to deter unaffordable consumer indebtedness.
18. ICAEW has often commented on the UK's productivity puzzle, e.g [Solving the UK's productivity puzzle](#). The post financial crisis period of (until recently) extraordinarily low

interest rates has been accompanied by anaemic productivity growth [Why is UK Productivity Low and How Can It Improve? - NIESR](#) .

19. At an individual level, the easy availability of debt to fund lifestyle purchases must surely diminish the incentive to work hard (i.e. increase productivity) and as interest rates increase, the potential adverse impact on households of historic debt becomes ever more burdensome. The increasing use of 'buy now, pay later' offerings where consumers are given easy access to credit at the point of purchase is particularly concerning in this respect.
20. We therefore believe that government should consider this issue much more fully and design policies best intended to create economic growth, so reducing levels of personal insolvency.

COMMENTS ON THE CONSULTATION QUESTIONS

22. In light of our general comments above, we have commented only selectively on the specific consultation questions below.

Chapter 5.1 - The underlying purpose of the framework

Question 1: What should be the fundamental purpose of the personal insolvency framework? Does the current framework meet that purpose?

23. We think that the paper identifies the key objectives of an insolvency regime and how the balance between them may change from time to time:
- to maximise returns to creditors (can pay, should pay); and
 - to rehabilitate debtors, ie release them from obligations to pay historic debts (fresh start)
 - identify (and sanction) fraud etc
24. We believe that the paper also identifies the key considerations to be considered in setting the balance, including:
- Impact on creditors/lending prospects if likely returns are reduced;
 - The concept of moral hazard ie the risk that the availability of debt relief may lead to excessive or reckless borrowing by individuals;
 - Differentiating between honest/unfortunate insolvents and dishonest/reckless insolvents through a range of criminal and civil sanctions; and
 - Differing circumstances (eg where there are, or may be, high value assets at stake).
25. We think it doubtful that the regime encourages responsible borrowing and management of personal finances and believe that this would best be addressed through education or other regulatory initiatives (see Key Points above).
26. Feedback from our licensees operating in this field suggests that cases of clear intent to defraud or deliberate abuse of the regime are rare, so that efforts to prevent this should be targeted so that it does not use resource that might more usefully be used elsewhere.
27. It is difficult to say whether the regime meets its 'purpose', because, as noted in the paper, there are more than one purposes, sometimes pulling in opposite directions. We think it is right for government to consider whether the balance has shifted too far in the direction of debt forgiveness or should tilt further in that direction, but we express no view on that here. Our concerns are primarily:
- whether the regime is clear and comprehensible both to the public (eg potential insolvency individuals) and those who need to administer it (eg Insolvency Practitioners)
 - whether it operates efficiently (eg quick and cost-effective outcomes)
 - whether there are aspects of the regulatory regime that have unintended consequences.
 - entry costs and the funding model. Entry costs can deter people from a particular solution (as can waiting to see a voluntary sector debt adviser).

Question 2: If 'fresh start' and 'can pay, will pay' are the right objectives for the personal insolvency regime, does the current framework get the balance right?

28. The current regime is so complex and there are so many variables (eg different fee regimes), that it is difficult to know exactly what balance it is intended to achieve.

Question 4: Please explain whether there should be different objectives for different personal insolvency procedures.

29. Objectives should not be built around procedures. Rather, the procedures should be built to meet the objectives. We are concerned that there are too many procedures and that it should be possible to design a simpler regime.

Question 5: Please consider whether there should be different options for trading and consumer debtors. If so, how would the features differ?

30. We think that there is a distinction to be drawn between consumer and business debt, albeit that there are areas of overlap (eg sole proprietors). We believe that the regime could be significantly simplified were 'consumer debt' to be regulated by FCA and other insolvencies by Insolvency Service (see Key Points above).

Question 7: To what extent does the current enforcement regime (BROs/DRROs and criminal sanctions) adequately achieve the aims of deterring future misconduct (both individual and general) and protecting the public?

31. We believe that incidence of abuse is relatively low. Whether this is because of deterrent effect of sanctions is hard to say, but we think it doubtful.

Question 9: Are there any features of other regimes that would be beneficial to consider for England and Wales and how effective are these features? For example, debt counselling and rehabilitation programmes.

32. We believe that education of the population at an early age is key – by the time debtors seek help it may be too late for them to learn new disciplines and break old habits. However, counselling at any time could be beneficial, for instance at the end of an IVA. See also Key points above.
33. We also believe that individuals should obtain some advice before choosing any insolvency option, but this is not currently required where individuals choose the bankruptcy option.

Chapter 5.2 - Fees, funding and costs

Question 12: What options are available to debtors and creditors who are unable to afford the cost of bankruptcy, IVA or a DRO?

34. There is an upfront fee to be paid for both DRO and bankruptcy. Some DMP providers ask for a month or two in advance, but a person can enter an IVA as a consumer without having to pay an upfront fee - there is an argument that this is one of the reasons for the attractiveness of the IVA. Another factor is that many consumer IVAs can be set up almost immediately, taking away the (immediate) worry and stress being faced by the debtor.

Question 14: How can we reduce the stigma of insolvency to both encourage early action by those in financial difficulty and to support a 'fresh start' from debt relief?

35. Some words (most obviously 'bankruptcy') have associations for some that may have nothing to do with the qualities of the procedure itself (or alternatives to it) but result from historic usage. This can mean that debtors are deterred from choosing what would otherwise be the most suitable procedure (eg bankruptcy). This could (in theory) be addressed by a change in name.
36. Some procedures result in public disclosure (see also Q24 below). This is in part to help potential creditors assess risks of lending (rather than 'naming and shaming'). If the public

understand the rationale for debt forgiveness and the relevant procedures, then it should not of itself result in stigma (although it may make it harder for the debtor to obtain credit).

37. If the concern around stigma can be addressed it could make a debtor consider the option more fully where it is appropriate, which would be a good outcome.

Chapter 5.3 - The current insolvency procedures and how they are working

Question 16: Do you believe the current insolvency procedures are working as intended? Please provide any evidence you have.

38. Due to the number of procedures and their piecemeal development (along with FCA processes), it is difficult to know how they are intended to operate collectively.
39. We have little doubt that some debtors have used ‘wrong’ procedures (in the sense that they would have had better financial results using a different one – it is difficult to say that a decision is ‘wrong’ where subjective considerations arise, as they often do). The Insolvency Service already has evidence on this issue (eg in the context of volume IVAs) and it would not be appropriate for us to comment on individual cases here.

Question 17: How well do those in financial distress navigate the current regime and could this be improved? Please provide evidence to support your answer.

40. The regime is extremely difficult to navigate. Debtors need to consider not only the procedures covered by the Insolvency Service, but also those covered by FCA. We believe that government should consider radical reform to simplify, including potentially bringing all ‘consumer debt’ solutions under auspices of the FCA.

Question 18: Are the current personal insolvency procedures the right products to service the needs of both debtors and creditors today or are new procedure(s) needed to serve debtors and creditors better?

41. We do not believe that government should be considering ‘new’ (ie yet more) procedures but rather should consider whether the current procedures are meeting society’s needs and whether they could be simplified. It may be a question of starting afresh. See Key Points above.

Question 23: How could an individual’s decision to enter a particular procedure could be better informed?

42. We believe that individuals should be faced with fewer and simpler choices. Presently debtors face a multitude of options and face making decisions, often under pressure from creditors, without the ability for financial reasons to take independent advice from qualified persons.
43. As relevant debtors may be unable to pay for advice, the role of the not-for-profit sector is important here. Government should consider how best to signpost debtors to relevant organisations (eg the charity StepChange) so that they can be better informed.

Question 24: What evidence do you have of the impact that a public register has on an individual’s decision to choose a particular insolvency route?

44. Both IVA and bankruptcy are recorded in the same register. The number of consumer IVAs continue to grow. It is, therefore, apparent that the register has little impact on the debtor. The perception that bankruptcy involves a white van clearing out all their personal possessions is much stronger.
45. We believe that the cost is a material deterrent to use of the bankruptcy procedure. To many potential bankrupts £680 is a huge sum. The commercial impacts may be even more

important. For example, debtors may be concerned that car HP agreements will be terminated, insurance policies will require an annual up front premium, mobile phone contracts will be difficult to get and are probably restricted to pay as you go, landlords may terminate tenancies, employers may terminate employment etc.

Question 25: What impact does professional debt advice have on debtors when choosing a personal insolvency solution? Please provide evidence to support your answer.

46. The review paper suggests that FCA authorised debt advisors are in some way better qualified to provide debt advice than Insolvency Service/RPB regulated Insolvency Practitioners. We do not understand why the Insolvency Service might think this. However, we note that the FCA regulation applies at a firm level whereas IP advice regulation applies at an individual level (currently, reforms are anticipated). Firm regulation is crucial in a high-volume environment where the requirement for adequate processes and controls become all the more important.
47. We agree that professional debt advice is an essential requirement under the current regime where there are a variety of choices and large number of variables (eg fees). However, debtors may choose not to follow advice they are given. They are often in a vulnerable state and may make economically unsound choices to escape the threat of the bailiff or the calls of a collection agent. Therefore, any solution that takes those potential outcomes away quickly and with the minimum intervention by the debtor themselves is attractive.

Chapters 5.1 – 5.3 – the international perspective

Question 28: Which elements of other national regimes could improve the personal insolvency framework in England and Wales?

48. We believe that the UK could learn from experience elsewhere. However, simply looking at how existing procedures could be tweaked as a result seems like a wasted opportunity. Rather, it would be interesting to know if other countries have found simpler solutions, perhaps with less reliance on the need for professional advice. The Australian income focused regime would offer scope for simplification but has wider implications that would need to be considered.