EXPLANATORY MEMORANDUM TO

THE INSOLVENCY (ENGLAND AND WALES) RULES 2016

2016 No. 1024

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Business, Energy & Industrial Strategy in conjunction with the Insolvency Service and is laid before Parliament by Command of Her Majesty.

1.2 This memorandum contains information for the Joint Committee on Statutory Instruments.

2. Purpose of the instrument

2.1 The Insolvency (England and Wales) Rules 2016 ("the 2016 Rules") provide the procedural framework for the Insolvency Act 1986 ("the Act"). They prescribe matters required by the Act and set out the procedural rules to be followed in the conduct of insolvency proceedings.

2.2 The 2016 Rules do three things. They consolidate the Insolvency Rules 1986 ("the 1986 Rules") with the 28 amending instruments made since the 1986 Rules came into force. They restructure the Rules and update the language including gender neutral drafting. Finally they modernise those Rules to take account of the changes made to the Act by the Deregulation Act 2015 ("DA") and the Small Business, Enterprise and Employment Act 2015 ("SBEE"); in particular amendments enabling modern methods of communication and decision making to be used in place of paper communications and physical meetings.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 The Act is a complex piece of legislation which brought together personal and corporate insolvency procedures and has been heavily amended since it was made. In relation to different insolvency proceedings there is a lack of consistency in what is contained in the Act and what needs to be contained in Rules to supplement the Act. Users of the Rules need to relate the individual rules to the sections which the rule completes or complements. In order to assist the users there are a number of non-legislative notes in the Rules. These are contained in square brackets and are labelled as notes. These have a number of purposes. For example they draw the user's attention to those provisions in the Act which a particular rule complements. In rule 1.2 (definitions) there are pointers to definitions that are found in different places in the Act and which in some cases are applied by the Rules for other purposes. There are also notes which refer the reader to things which are *not* in the Rules. For example where a rule in the common parts applies to some but not all insolvency procedures, there are notes to indicate where equivalent previous are found in the Act for the procedures that are not covered. Finally there are notes which point the user to other parts of the Rules that are relevant to an individual rule or a Part of the Rules such as the pointers to information required in documents by Part 1.

3.2 We recognise that the use of notes to such an extent is unusual however members of the Insolvency Rules Committee ("the IRC") (with whom the Lord Chancellor must consult before making these Rules) and other interested parties have informed the Department that they find these useful. Indeed the IRC specifically requested the insertion of the notes referring to the requirements for documents to contain the standard contents at the start of each Part or Chapter where it is relevant.

3.3 The Committee may also wish to note that rule 12.3 provides elucidation on the application of section 117 of the Act to proceedings other than winding-up proceedings. The Department for Business Innovation and Skills had promised the JCSI to provide elucidation on this point in its memorandum to the Committee (See the 3rd Report of the 2014-15 Session regarding the Insolvency (Commencement of Proceedings) and Insolvency Rules 1986 (Amendment) Rules 2014 (S.I. 2014/817).

Other matters of interest to the House of Commons

3.4 As this instrument is subject to the negative procedure and has not been prayed against, consideration as to whether there are other matters of interest to the House of Commons does not arise at this stage.

4. Legislative Context

4.1 The 2016 Rules has three purposes: to consolidate the 1986 Rules and the 28 amending instruments; to restructure and update the language; and to modernise and to give effect to policy changes made to the Act by the DA and the SBEEA.

5. Extent and Territorial Application

5.1 The extent of this instrument is England and Wales.

5.2 The territorial application of the instrument is England and Wales.

6. European Convention on Human Rights

6.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy background

What is being done and why

7.1 The first purpose of the 2016 Rules is to consolidate the existing instruments which together comprise the 1986 Rules. This will result in a single instrument which will better meet the needs of users, including the judiciary, insolvency office-holders, creditors and public officials.

7.2 The second purpose is to update the 1986 Rules both in terms of their structure, language and style of the drafting. Modernised language and gender neutral drafting has been used in the 2016 Rules, accompanied by re-drafting the Rules in a simpler fashion to make them easier for users to understand. The Rules have been restructured for example by separating out the winding-up provisions into three separate Parts for members' voluntary liquidation, creditors' voluntary liquidation and compulsory liquidation. Undue repetition has been avoided through the greater use of common parts that apply to multiple insolvency procedures. An example is the decision-making provisions of Part 15 that will apply in all insolvency proceedings in the

future. Repetition has also been avoided by the wider use of standard content provisions for notices and documents.

7.3 One further significant change is the approach taken of prescribing content for notices and documents in the rules themselves rather than in statutory forms. This builds in a significant degree of future-proofing as there will be less need for amendment to accommodate advancements in technology, business practice and to enable e-delivery.

7.4 The third purpose is to modernise and give effect to policy changes, some of which result from amendments made to the Act by the DA and the SBEEA. These changes result from deregulatory initiatives. Those relating to the SBEEA stem from the Red Tape Challenge and many of these were put forward by a range of stakeholders. The policy impetus for all these measures was to remove unnecessary regulatory burdens to reduce the cost of administering insolvency proceedings. Reducing costs will benefit creditors in the form of improved dividend returns.

7.5 As business practice has developed, particularly as a consequence of technological advances, amendments to the law have, at times, been slow to follow. This has meant users have not always been able to take advantage of the quickest, most cost effective or most convenient methods of achieving certain tasks. In the context of insolvency proceedings this is particularly prevalent in the ways insolvency office-holders communicate with creditors and other parties. A number of policy changes have therefore been made and the main changes are summarised below.

Electronic communication

7.6 Where a debtor and a creditor have been customarily corresponding electronically prior to insolvency, under the 1986 Rules an insolvency office-holder could not continue to correspond in that way without first obtaining the creditor's written consent. Stakeholders stated that this is a big barrier to e-communications and did not reflect the way the business world operated (even more so than in 2010 when e-communications were first permitted by the Insolvency (Amendment) Rules 2010[1]). The 2016 Rules change this so that where electronic communication was customarily used pre-insolvency, then that method of communication can continue post-insolvency. This will encourage e-communication, which is generally cheaper and speedier than traditional post.

Use of websites

7.7 Under the 1986 Rules an office-holder who wants to put all future documents on a case on a website after only an initial notice to creditors, must obtain an order of the court. This requirement has been removed and the 2016 Rules permit an office-holder to send a notice to creditors stating that all future documents will be made available on a website, subject to certain exceptions.

Progress reports

7.8 The 2016 Rules introduce a fixed reporting requirement for administration, company voluntary liquidation and compulsory liquidation and bankruptcy where the office-holder is not the official receiver, which will remain the same regardless of whether or not the proceedings have been extended or transferred to another insolvency practitioner. The 6 or 12-month (depending on procedure) cycle of reporting will remain unchanged throughout the life of the case.

7.9 In addition, the 2016 Rules revert to a position in effect prior to commencement of the Insolvency (Amendment) Rules 2010 by reintroducing the requirement for an administrator to file a final progress report together with the notice sent to the registrar of companies required under paragraph 83 of Schedule B1 to the Act. This notice, once registered, converts the administration into liquidation proceedings. Information on any relevant activity which takes place in the period between the sending of the notice and registration will be provided to creditors in the liquidator's first progress report. This will reduce the number of filings necessary.

Statements of Affairs

7.10 Statements of affairs contain full details of all creditors, including their names and addresses, and the amounts of their claims. These details will include any employees or ex-employees owed money by the insolvent company or debtor for wages or similar payments, and also any customers who may have made advance payment for goods or services. In some corporate proceedings the statement of affairs must be filed with the registrar of companies, which leads to those details being placed in the public domain. This has led to concerns over protection of privacy and identity theft.

7.11 New provisions now require that where a statement of affairs is to be filed with the registrar of companies, details of employees, ex-employees, and customers who are consumers must be contained within a separate schedule, and only a summary will appear in the body of the document. That schedule will be removed before the statement of affairs is filed with the registrar.

Removing meetings of creditors

7.12 Amendments made to the Act by SBEE remove meetings as the default mechanism for seeking decisions from creditors in insolvency proceedings. In many cases the office-holder will be able to use a process of deemed consent, where they write to creditors with a proposal. Provided they do not receive objections from 10% or more of creditors by value then the proposal will be deemed to be approved. In the event that 10% or more of creditors object to the proposal then the office-holder will use an alternative decision-making process, such as a virtual meeting, correspondence or electronic voting.

7.13 The Rules specify what types of alternative decision-making processes may be used. The form the alternative decision-making process takes in respect of a particular decision will be at the discretion of the office-holder, with two exceptions. An office-holder may only call a physical meeting of creditors if this has been requested by 10% or more by value of the creditors, or 10% of the total number of creditors, or 10 individual creditors. It is open to creditors to make this request at any time they are asked to make a decision. This means that the expenses of calling a physical meeting will be incurred and charged to the insolvency estate only where creditors have asked for this to happen, so unnecessary charges will be prevented. The thresholds for requiring a physical meeting of creditors are contained within the primary legislation.

7.14 The second exception relates to the appointment of a liquidator in a creditors' voluntary liquidation. In that process the only methods of seeking a decision from creditors that the company may use are a virtual meeting or deemed consent. If creditors object to the use of deemed consent then the company must immediately call a physical meeting. Creditors may still require that a physical meeting is held in any case.

7.15 These new provisions will apply equally to decisions made by contributories.

Abolition of final meetings

7.16 Final meetings of creditors in liquidation and bankruptcy proceedings are held to allow the office-holder (other than where the official receiver) to give a concluding report on the administration of the insolvency proceedings. The office-holder would normally obtain their release from office upon reporting the outcome of the meeting to the registrar of companies (liquidation) or the court (bankruptcy). However, creditors may resolve against the office-holder's release at the final meeting, in which case he or she would need to seek release by application to the Secretary of State (the effect of the release is that the office-holder's liability for the administration of the proceedings ends). Stakeholders have said that these meetings are of little value and are rarely, if ever, attended by creditors.

7.17 The amendments to the Act made by SBEE remove all final meetings of creditors where they were required – creditors' voluntary liquidation, and compulsory liquidation, and bankruptcy where someone other than an official receiver is trustee. Final meetings of members (shareholders) in members' voluntary liquidations will also be scrapped. It will still be necessary for the office-holder to engage with members by sending them a copy of the final account, and members will continue to be able to object to the release of the office-holder upon receipt of that document by notifying the office-holder of their objection.

Opting out of further correspondence

7.18 Currently the Act (and hence the 1986 Rules) require the office-holder to send all notices, reports etc., to all known creditors. Even where a creditor has no further interest in a case and wants no further information on it – for example if there is little or no likelihood of a financial return – they cannot ask the office-holder to omit them from future mailings. The amendments to the Act to which the Rules give effect allow a creditor to opt out of receiving further correspondence, therefore relieving the office-holder of the expense of sending notices and the creditor of the expense of dealing with them. Notices of intended dividends will not be subject to the opt-out and creditors will retain the ability to opt back in to receiving notices.

Allowing an office-holder to pay a dividend in respect of a debt of less than £1,000 without the need for the creditor to submit a formal claim

7.19 To receive a dividend in an insolvency, a creditor must first submit a claim to the office-holder, which must contain prescribed information. The office-holder may ask for further evidence from the creditor if thought necessary. Such claims must be scrutinised by the office-holder prior to distribution of any dividend. New provisions in the Rules allow an office-holder to rely on information contained in a company or bankrupt's statement of affairs or accounting records, and to pay a dividend without the need for the creditor to submit a claim but only where the debt in question is below the prescribed limit of £1,000.

Official receiver to be appointed trustee on the making of a bankruptcy order

7.20 The Rules reflect the amendments to the Act removing the status of receiver and manager of the bankruptcy estate, which an official receiver currently becomes between the date of the bankruptcy order and the appointment of a trustee. Instead, an official receiver will be appointed as trustee on the making of an order. The initial appointment as receiver and manager had not been shown to have any practical

benefit in the administration of bankruptcy cases and could serve to delay the realisation of assets.

Appointment of insolvency practitioner as interim receiver

7.21 Whilst previously an insolvency practitioner could only be appointed as an interim receiver ahead of a bankruptcy petition hearing in very limited circumstances, amendments to the Act now permit the court to appoint an insolvency practitioner as interim receiver in all circumstances (an official receiver may also be appointed as interim receiver, as previously). The Rules reflect this change.

8. Consultation outcome

8.1 The 2016 Rules have been informed by an extensive programme of consultation and engagement with a range of parties affected by insolvency. Such parties include: the insolvency profession, creditor representatives, insolvency regulators and public bodies.

8.2 Informal consultation has been ongoing for several years as the process of consolidation has been undertaken. In more recent years, a public consultation was held between 26 September 2013 and 24 January 2014. Over 1,000 individual comments were received from a broad cross-section of interested parties.

8.3 During the course of 2014 and 2015 revisions were made to the draft rules published as part of the 2013 consultation. A programme of regular engagement was undertaken with individuals representing many of those who had responded to the public consultation. This group included: insolvency practitioners, technical managers and lawyers from major professional services firms, representatives from insolvency regulators and creditor organisations. This engagement took the form of rule by rule scrutiny of the major parts of the draft rules.

8.4 In July 2015 draft rules were submitted to the IRC for the purpose of the Lord Chancellor's statutory consultation pursuant to section 413 of the Act. The draft submitted to the IRC was also published online. The IRC undertook its examination of the draft rules between July 2015 and August 2016, engaging with officials of the Insolvency Service and the Department on a regular basis including through meetings and written correspondence. The IRC confirmed on 5 October 2016 that it had considered the draft instrument and was satisfied with its content.

9. Guidance

9.1 Throughout the extensive programme of engagement outlined above, the Insolvency Service has met with and corresponded with interested parties to discuss and provide information relating to the 2016 Rules including highlighting the differences between the 2016 Rules and the 1986 Rules and what they would mean in practice. Further information has been provided by way of bulletins to targeted parties affected by the introduction of the 2016 Rules. The Insolvency Service will continue to engage with stakeholders as they prepare themselves for commencement of the 2016 Rules.

10. Impact

10.1 The impact on business, charities or voluntary bodies relates to their capacity as creditors in insolvency proceedings and is deregulatory. The efficiency savings delivered by the 2016 Rules will result in lower costs in dealing with the administration of an insolvency. This in turn should lead to better returns to creditors.

10.2 The impact on the public sector is divided into two main areas. The Insolvency Service provides a range of services in fulfilment of statutory duties. These include cases in which an official receiver acts as the office-holder in compulsory liquidation and bankruptcy. The efficiency savings delivered by the 2016 Rules should also allow the Insolvency Service, particularly in respect of its official receiver operations, to undertake its duties at a lower cost. The second main impact relates to the public sector as a creditor in insolvency proceedings. In such cases, the public body should also benefit from the same better returns as other creditors.

10.3 Two Impact Assessments are submitted with this memorandum and are published alongside the Explanatory Memorandum on the legislation.gov.uk website.

11. Regulating small business

11.1 The legislation is deregulatory and applies to activities that are undertaken by small businesses.

12. Monitoring & review

12.1 The effectiveness of the 2016 Rules will be borne out by their ability to facilitate and achieve more effective, efficient and transparent insolvency processes and, in doing so, deliver the savings to business as set out in the accompanying Impact Assessment. The 2016 Rules will be reviewed within 5 years after they come into force on 6 April 2017. Should it be decided that the legislation is no longer fit for purpose following this review, the legislation will be amended accordingly.

13. Contact

13.1 Sam Roberts at the Insolvency Service Telephone: 020 7291 6822 or email: sam.roberts@insolvency.gsi.gov.uk can answer any queries regarding the instrument.