
Corporate insolvency framework

Department for Business, Innovation & Skills

(Insolvency Service)

RPC rating: fit for purpose

Description of proposal

The proposal would amend the corporate insolvency rules to encourage more business rescues, by allowing businesses more time to restructure or identify new sources of finance. The proposal will also reduce the scope for creditors with limited financial interest to behave in a way which is not in the interests of creditors as a whole - for example, by delaying processes in the hope of achieving a better individual outcome.

The IA states that consultation will seek views on four proposals, including:

1. Enabling a wider range of viable businesses to take advantage of a time-limited moratorium on debt collection;
2. Introducing new provisions for restructuring, which, subject to safeguards, would enable schemes to be imposed without the agreement of all creditors;
3. Extending the scope of essential suppliers that may be prevented from altering contracts or terminating supplies to insolvent businesses; and
4. Altering the rules in relation to the interaction between existing security arrangements and security for rescue finance arrangements - to enable company property to be used to secure rescue finance where it is in the best interests of creditors as a whole.

Impacts of proposal

The IA sets out the range of potential impacts likely to result from the different elements of the proposals. The estimated effects of the moratorium changes are set out in greater detail than the other elements.

The IA uses information gathered through a 2010 consultation to estimate that the moratorium (proposal one) is likely to be used in only 10 to 20 cases a year, as consultation respondents felt that the potential costs involved would, in most cases, make applying for a moratorium less attractive than other business rescue routes. A moratorium is expected to enable restructuring to be undertaken in a more planned and efficient manner, improving business rescue outcomes. The Department

assumes that 90% of creditors are businesses. This is expected to benefit businesses by approximately £28 million per year. Against this, the cost to business of producing the relevant reports, monitoring compliance and gaining legal agreement to the details of the moratorium is expected to be approximately £23.7 million per year.

The impacts of proposals two, three and four are subject to greater uncertainty because the evidence collected through consultation in 2010 is less relevant. These proposals are expected to result in greater success rates for company voluntary arrangements (one type of insolvency case); they are also expected to result in 10 to 20 more cases each year pursuing routes, such as voluntary arrangements, that are more likely to result in successful resource recovery or increase the level of return to creditors. These changes are expected to result in up to £3.5 million benefit for business each year.

The changes to essential supplier requirements (proposal three) are expected to result in additional costs for five to 10 suppliers - in each of the 30 to 80 cases expected each year. The suppliers will face costs, as a result of insuring against non-payment and legal costs, of around £3.4 million each year.

Familiarisation with the whole package of changes is expected to cost between £0.6 million and £1.2 million, based on around 1,400 insolvency practitioners undertaking a half- to whole-day training course.

Quality of submission

The IA sets out a clear rationale for intervention, highlighting that some creditors may have incentives to behave in a way that has an overall net cost for other creditors and that the inefficiencies in the existing system potentially impose unnecessary transaction costs that reduce the likelihood of business rescue. The IA also sets out a range of options and explains why it would not be possible to pursue non-regulatory options.

The level of analysis is sufficient for this stage. The IA sets out that further information is needed to inform decisions on which elements to implement and to provide further detail on what the potential costs and benefits of the changes will be. Consultation will also be used to develop a clearer understanding of the current market failures - for example, why company voluntary arrangements are currently under-utilised. The Department should also use the consultation to rigorously test its estimates of the familiarisation costs, in light of the multiple ongoing changes to corporate insolvency regulations.

There are, however, some areas that could be improved to support the consultation, and which will need to be included in the final stage IA. In particular, the IA should include consideration of the extent to which the moratorium changes could result in transfers between creditors - for example, from those creditors that have debts frozen during the moratorium to other creditors. The Department should also test whether the changes to security arrangements for existing creditors in relation to security for rescue finance would impose costs on secured creditors beyond familiarisation costs. Consultation should also consider whether the extension of debt collection controls, under the moratorium proposal, could also result in additional costs as a result of increased creditor risk.

Prior to publication, the clarity of the IA should be improved in a number of areas - for example, the section on direct costs and benefits would benefit from identifying more clearly how the impacts are related to each other. This should include discussing whether some of the costs and benefits of moratoria are correlated to each other – for example, discussing whether the higher benefit estimates could happen only if the costs were also at the high end of the estimated range. At final stage, the IA will also need to provide sufficient evidence that there is no double counting of benefits - for example, the benefits discussed in the moratorium section of the IA and the benefits discussed in relation to the increased uptake of more successful insolvency processes (such as moving to company voluntary arrangements, instead of administration) would appear to have some overlap.

Small and micro business assessment

While the proposal is expected to benefit business, as the measure is not eligible for the fast track, a small and micro business assessment is required. The IA explains that the proposal is expected to benefit businesses going into insolvency and their creditors. The beneficiaries will include small and micro businesses. The Department should consider including a specific section discussing the effects on small and micro businesses. This should include a discussion of the evidence presented in relation to previous changes to essential suppliers' rules and the effects on small and micro suppliers. A previous IA on changes to the continuity of essential supplies provisions set out that essential suppliers were, proportionally, more likely to be larger businesses than those benefitting from the changes (insolvent businesses and their creditors). The Department should clarify whether, following the extension of the scope of the essential supplier rules, this is still expected to be the case.

Departmental assessment

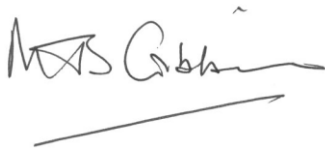
Classification	Qualifying regulatory provision (OUT)
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Opinion: consultation stage IA
Origin: domestic
RPC reference number: RPC-3285-BIS
Date of implementation: not provided

Equivalent annual net cost to business (EANCB)	- £4.1 million
Business net present value	£36.1 million
Societal net present value	£66.4 million

RPC assessment

Classification	Qualifying regulatory provision (OUT)
Small and micro business assessment	Sufficient



Michael Gibbons CBE, Chairman