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Rescue
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Renewal

Rt Hon Greg Clark MP
Secretary of State
Department for Business, Energy and Industrial Strategy
1 Victoria Street
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12th April 2017

Dear Secretary of State,

**The role of the UK's world class insolvency framework in building the government's Industrial Strategy**

I write as President of R3, the insolvency and restructuring trade body, in response to the government's 'Building our Industrial Strategy' green paper. While we are unable to comment on the specific consultation questions, the UK's insolvency and restructuring framework underpins the attractiveness of the UK as a place to do business and so plays a key role in supporting the government's industrial strategy.

In its green paper, the government identifies ten pillars to build a UK-wide industrial strategy. A strong and world class insolvency and restructuring framework is a vital part of delivering those ten pillars, particularly supporting businesses to grow and succeed (by accessing finance and management skills) and encouraging trade and investment.

The UK's insolvency and restructuring framework is one of the best in the world according to the World Bank. It has one of the highest rates of returns to creditors, returning money quicker and at a lower cost than in the US, Germany and France. In 2013-14 the insolvency and restructuring profession rescued more than 41% of insolvent businesses with which it worked and saved more than 235,000 jobs[1].

The insolvency and restructuring profession has a key role to play in the UK economy. It:

- Encourages both domestic and cross border investment by increasing the overall efficiency and attractiveness of the UK as a place 'to do business';
- Encourages the timely restructuring of viable companies in financial difficulties, saving jobs and helping companies survive;
- Encourages entrepreneurship and discourages bad behaviour;
- Improves access to credit.

Given the government's policy to introduce an industrial strategy which will make the UK 'one of the most competitive places in the world to start or grow a business', R3 would like the government to ensure that the UK's insolvency and restructuring framework continues to make a substantial contribution to the efficient running of the wider economy in the years ahead.

To this end, we would encourage the government to progress its review of the corporate insolvency framework, and ensure that once the UK has left the EU, the insolvency and restructuring profession is able to continue to work effectively across EU borders, and so encourage UK trade and investment. We would also urge the government to work closely with the profession to promote the importance of financially distressed businesses seeking advice early enough so that businesses can survive and succeed in the long term.

[1] R3 Value of the Profession to the UK economy report (statistic from R3/Com Res member survey) (May 2015)

**Seeking debt advice from appropriately qualified professionals early enough**

R3 welcomes the government's commitment to helping businesses to start up, and scale up. As part of the government's aims to ensure that these businesses can access the finance and management skills they need to grow and succeed, R3 encourages the government to work closely with the insolvency and restructuring profession to ensure that businesses in financial trouble seek advice as early as possible, to give them the best possible chance of long term survival.

In a 2014 survey of R3 members, over a fifth (22%) of those who work on corporate insolvency said that it typically took businesses more than a year to contact them after the point at which they first showed signs of financial distress. Just 1% said that they are typically approached in less than a month after signs of trouble were first spotted. More needs to be done to encourage businesses to seek advice early.

As part of that work, more should also be done to encourage financially distressed businesses to seek advice from properly qualified advisers. Unfortunately, not all of the organisations which offer advice to troubled companies are reputable, licensed or regulated. As the trade body for insolvency and restructuring professionals – whose members are regulated by professional bodies, bound by legal duties and professional rules, and are required to pass a series of exams before being licensed – we are keen to do what we can to promote the importance of professional and regulated debt advice to businesses in financial trouble.

**Brexit and mutual recognition**

We are very keen to ensure that our insolvency and restructuring framework remains one of the best in the world. With the Brexit negotiations underway, we would encourage the government to protect the UK's reputation as an attractive place to do business by preserving the benefits of two EU regulations relevant to insolvency: the European Insolvency Regulation and the Recast Brussels Regulation – the importance of which were underlined recently in the Justice Select Committee's report on the implications of Brexit for the justice system.

These regulations allow automatic recognition of UK insolvency procedures and judgments across the EU and form a vital part of the UK's strong, world class insolvency and restructuring environment. If the benefits of these regulations are not preserved, jobs, growth, inward investment and productivity will be harmed and the cost of borrowing is likely to increase. The UK's position as a centre for international restructuring and insolvency work would also be undermined.

R3 has called on the government to ensure that the benefits of the EU Regulation on Insolvency and the Recast Brussels Regulation are preserved in negotiations via an equivalent treaty between the UK and the EU. Securing such an arrangement would help the government to support its trade and investment pillar.

Please find attached a copy of our policy paper which sets out further details on the potential implications of Brexit on the insolvency and restructuring regime.

**Corporate insolvency framework reforms**

In May 2016 the government launched a consultation that outlined four proposals for reform of the UK's corporate insolvency framework, with the objective of ensuring 'that the insolvency framework supports business rescue where possible, maximising returns to creditors where possible.'

As well as a world class insolvency regime, the UK also has a well-established restructuring and turnaround culture. There are, however, improvements that can be made and R3 welcomes the government's focus on restructuring tools and business rescue, given the rise in restructuring/advisory activity over the last decade.

However, R3 is concerned that, as currently drafted, the proposals lack safeguards to prevent abuse, may not work for smaller businesses, would make too many demands on an over-burdened court system, could harm normal business lending, and are unfair for creditors, particularly small businesses. R3's views are shared by the business community.

While the government has since published a summary of responses to the initial consultation, it has not indicated the extent to which the concerns expressed about the proposals will be taken into account. R3 has welcomed engagement with the Insolvency Service over the last 12 months to discuss the reforms and its concerns, and hopes the government will take on board the wide range of concerns expressed and consider better safeguards than currently proposed – which will help to ensure that the UK remains an attractive destination for domestic and foreign investment, supporting two of the key pillars of the government's Industrial Strategy.

We very much look forward to working with your Department, including the Insolvency Service, to ensure that the UK's insolvency and restructuring framework continues to underpin the attractiveness of the UK as a place to do business over the years ahead.

Should you or your officials require any further information, please contact R3's Public Affairs and Policy Officer, James Jeffreys, on 020 7566 4220 or james.jeffreys@r3.org.uk.

Yours sincerely,

Andrew Tate
R3 President

## Appendix: UK insolvency and debt trends (April 2017)

### About R3

R3 is the trade body for the UK insolvency and restructuring profession. From senior partners at global accountancy and legal firms to practitioners who run their own small and micro-businesses, our members have extensive experience of helping businesses and individuals in financial distress.

**Key facts about the UK's insolvency regime**

- The UK's insolvency regime is one of the best in the world according to the World Bank. It has one of the highest rates of returns to creditors, returning money more quickly and more cheaply than regimes in the US, Germany and France. UK Insolvency Practitioners (IPs) return more than £4bn a year to creditors (including HMRC and businesses).
- There are approximately 1,750 IPs in the UK and around 12,000 professionals who work in insolvency.
- Most insolvency practitioners are accountants or lawyers. They are all qualified and regulated (by one of six regulatory bodies).
- In 2013-14 UK IPs:
    - Rescued approximately 6,700 (41%) of insolvent businesses, saving around 230,000 jobs.
    - Advised 135,000 people about their finances and helped individuals repay £5bn of personal debt within five years.

### Insolvency trends

Business Distress Index – October 2016

The Business Distress Index is R3's tracker of the financial position of UK businesses. The latest survey also looked at the impact of the EU referendum result. It is conducted by BDRC Continental on behalf of R3. The latest report can be found on the R3 website here.

*Brexit:*

- Three-in-four UK businesses (74%) say they have yet to feel any financial impact – positive or negative – from the vote to leave the EU.
- However, 16% of all businesses, equivalent to 283,000 businesses, say the vote has already had a negative financial impact on them, compared to just 5% of businesses (85,000) who say the outcome of the referendum has had a positive financial impact.
- The businesses most likely to say they have seen a negative financial impact from the referendum result are large companies employing 251 or more people.
- 23% of large companies (2,000) say they have seen a negative financial impact from the referendum result, while just 2% say they have experienced a positive impact.
- In comparison, 16% of businesses employing between 2 and 5 people say they have seen a negative impact from the referendum, while 6% say they have experienced a positive impact.

*General:*

- 62% of UK businesses reported at least one sign of business growth, only slightly down from 69% in June. Of the individual indicators, there was a noticeable rise in the numbers experiencing increasing sales volume since June (38% v. 31%) and profits (32% v 22%).
- The proportion of businesses that expect their business activity to increase in the next year fell from 51% in June to 36% in September. The majority (56%) expect it to stay the same, while only 4% expect it to decrease.
- Signs of business distress are down, with only 21% of businesses experiencing indicators of distress, compared to 30% in June.
- Each indicator of distress showed a decrease since the previous survey, with those experiencing decreasing market share (5%), regularly using maximum overdraft (4%) and making redundancies (2%) all at record lows.
- 47% of UK businesses are more optimistic about the economy generally than three months ago, 20% are more pessimistic and 32% are neither.

Sector survey (March 2017)

R3 tracks the level of 'insolvency risk' in major UK sectors. Businesses are assigned a score which indicates a lower or higher than normal risk of entering insolvency in the next twelve months. March indicators showed:

- The hotels sector recorded the lowest risk out of all of the industry sectors tracked by R3, with 18.9% of companies with a higher than normal risk of insolvency. This is followed by: agriculture (19%), manufacturing (20.7%), pubs (21.1%), restaurants (22.5%), retail (23.5%), construction (25.3%), professional services (30.5%), transport/haulage (32.7%) and technology & IT (32.8%).

Zombie businesses (October 2016)

R3 tracks the number of 'zombie businesses' (those only able to pay the interest on their debts). More information on the latest statistics can be provided on request.

- 139,000 businesses in the UK are only paying the interest on their debt and not repaying the debt itself, often a sign of a 'zombie business' – a business only surviving because of low interest rates.
- The number of businesses in this position – equivalent to 8% of all UK businesses – has returned to levels more in line with previous years after falling to 69,000 last year (4%).

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If you would like further information, please do not hesitate to contact: James Jeffreys (R3 Public Affairs & Policy Officer) james.jeffreys@r3.org.uk 020 7566 4220.