



Baroness Vere of Norbiton  
Parliamentary Under Secretary of State  
Department for Transport  
Great Minster House  
33 Horseferry Road  
London  
SW1P 4DR

Thursday 20<sup>th</sup> June 2019

Dear Lady Vere,

**Insolvency and restructuring trade body R3 response to the Airline Insolvency Review final report: submission to the Government's 'Aviation 2050' consultation**

I write, as President of the insolvency and restructuring trade body R3, to provide feedback on the Airline Insolvency Review's ('the review') final recommendations, and to highlight areas where further consideration by the Government is required as it seeks to introduce reforms to ensure passengers and the taxpayer are better protected in the event of an airline becoming insolvent. I understand that the Government is seeking views on the review's recommendations as part of its 'Aviation 2050' consultation.

By the way of background, R3 represents the UK's insolvency, restructuring, advisory, and turnaround professionals. From senior partners at global accountancy and legal firms to practitioners who run their own small and microbusinesses, our members have extensive experience of helping businesses and individuals in financial distress.

We have engaged with the review since its inception and were pleased to be able to meet with the Chair Peter Buck and his officials in August 2018; we were also pleased that one of our members was then invited to join the review's panel of experts. We very much welcomed this positive engagement.

However, as we noted in our submission to the review's call for evidence, airline insolvencies are very complex operations, with serious financial and operational challenges which prevent their continued operation. At first glance, it does not appear that the review's recommendations will be able to resolve these challenges.

Rather than repeat in full the comments in our original submission (a copy of which is enclosed for reference), we hope to set out our thoughts on the most relevant of the review's recommendations and to highlight those areas where further consideration by the Government is required before any measures are taken forward. We would be very happy to meet with you or your officials to discuss these points in more detail.

## **A Flight Protection Scheme**

The review recommends the Government introduce a 'Flight Protection Scheme' (FPS) to fund passenger repatriation in the event of an airline becoming insolvent. This scheme would be paid for by the airlines themselves, and the review estimates that this would cost up to 50p per passenger. This proposal will have financial implications for airlines, and additional costs may be passed onto passengers.

In response to the review's original call for evidence, R3 recommended that passenger repatriation could be funded by an expansion of the existing ATOL protection scheme, which currently operates as an insurance mechanism for 'package' travel arrangements, so that it can cover 'flights-only' arrangements. The proposed FPS would fulfil a similar function to an expanded ATOL scheme and, as such, we do not have particular concerns with this suggested reform.

## **Passenger Repatriation**

The review recommends three means of repatriating passengers, funded by the FPS: self- and assisted-repatriation, where stranded passengers arrange their own flights home; chartered repatriation, where a new, chartered fleet would be deployed; and a 'keep the fleet flying' approach where the insolvent airline would continue to operate for a short time.

The 'keep the fleet flying' approach would be supported by two further changes: changes to the Civil Aviation Authority (CAA) regime to allow insolvent airlines to retain their operating licence (this is currently suspended upon insolvency); and the introduction of a Special Administration Regime for airline insolvencies, which would prioritise passenger repatriation over maximising creditor returns.

R3 has a number of concerns with the proposal that the Government should consider a 'keep the fleet flying' option. This approach does not address the practicalities of airline insolvencies (as set out below and in further detail in our response to the review's call for evidence) which prevent an insolvent airline from flying, and it will have a serious impact on the risks of trading with and lending to UK airlines.

### *Practical Challenges*

Even assuming insolvent airlines keep their operating licence, there will be a number of reasons why an insolvency office holder will not be comfortable with letting the airline's planes continue to fly. For example, the airline's planes can be vulnerable to action by overseas creditors, potentially putting aircraft and crew safety at risk: suppliers and other stakeholders may impound planes at non-UK airports, demanding repayment of debts in return for releasing the aircraft. Among many other factors, office holders will also consider crew wellbeing, and insurance costs.

Moreover, the daily costs of running large airlines (such that would be subject to this new regime) are likely to be very substantial in a Special Administration – without the mitigation of cash coming into the business in the form of fresh ticket sales. Whether the FPS will be large enough to fund the full scope of an airline's operations, rather than simply funding charters or emergency ticket purchases, remains to be seen.



## *Consequences of a Special Administration Regime*

The review's proposal that a Special Administration Regime (SAR) prioritise passenger repatriation over maximising creditor returns could well have serious implications for the financial health of the airline sector, and the taxpayer – unless the Government can ensure that the operation would be sufficiently funded via the FPS or some alternative method.

As above, running an airline is expensive and continuing operations will deplete the value of what the insolvent airline can repay to creditors. By increasing creditor losses in the event of an insolvency, a SAR for UK airlines may well deter lenders, investors, and other companies from lending to, investing in, or trading with a UK airline in the first place. Similarly, the costs of repatriation may mean funds are not left over to cover office holders' costs, disincentivising insolvency practitioners from taking airline appointments. This would leave airline insolvencies to be handled by the government's Official Receiver – and therefore funded by the taxpayer – again, unless these costs can be absorbed by the FPS.

In addition, the Government would need to address the significant financial risks faced by an administrator continuing to operate an insolvent airline. The review suggests (6.58) that “professional indemnity insurance, if an appropriate policy were available” would help to mitigate these risks. As we set out in our response, even if such a policy was available, the likely highly significant premiums, cover limits and excesses could still leave the office holder exposed – and would be an uneconomic prospect from the offset.

As an alternative, the review points out (6.59) that “in other SARs there are also powers for a Secretary of State to provide a grant, loan, or indemnity to administrators appointed under these regimes, in order to provide comfort that they will not be held personally liable for continuing a particular service.” This may be the only feasible option for the Government to consider, but would risk a loss to the taxpayer.

If the Government wishes to pursue a SAR, it should carefully consider the potential impact on the funding available to the airline sector, as well as the need for some form of insurance or indemnity to provide an insolvency practitioner with sufficient reassurance about the scope of their liability before they will contemplate taking an appointment as an office holder of an insolvent airline under a SAR framework.

Elsewhere, a recent Government proposal illustrates the potential issues that could arise from prioritising passenger repatriation over maximising creditor returns. HMRC has proposed that, in all corporate insolvencies, the repayment of some HMRC debts be prioritised over repayment of most other categories of debt. This proposal has been met with strong criticism from UK lenders and business representatives, who have warned that the move will lead to a restriction on UK access to finance, trading and investment, driven by lenders and creditors reacting to the increased risks associated with insolvency. The airline SAR, and the risk it may pose to creditor returns, may cause similar problems for the airline sector (which will also be dealing with the impact of HMRC's proposal).

## **Existing Proposals for Reforms to the UK's Corporate Insolvency Framework**

In 2016, the Government proposed a series of reforms to the UK's corporate insolvency framework. Included in these proposals are a number of new procedures or potential changes which could have a significant impact on airline insolvencies and could address some of the current difficulties.

Among the proposed reforms are:

- A short moratorium against creditor enforcement which would leave a company's directors in charge and would give the company time to develop a rescue or turnaround plan. This moratorium may be followed by an insolvency process or a non-statutory agreement with creditors.
- New rules to protect an insolvent company's access to supplies essential to its business (which would stop creditors or suppliers holding a business rescue to 'ransom').
- A new court-based restructuring tool, similar to the US Chapter 11 and the England and Wales Scheme of Arrangement, which would provide companies with alternative ways to bind creditors into a restructuring agreement. One of the key factors of the US Chapter 11 in its use in airline rescues is that it is not seen as a terminal 'insolvency' procedure but as a 'restructuring' tool. This allows funding sources and other creditors and stakeholders to have more confidence in trading and dealing with the insolvent company.

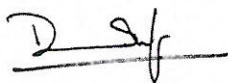
As we stated in our original response to the review, it may be more helpful if the Government were to concentrate on introducing a wider package of restructuring reforms than on introducing a series of SARs across different sectors of the economy. Introducing the 2016 reform proposals would provide airlines – and other companies – with means of avoiding insolvency in the first place. A series of SARs, however, would create administrative burdens and would make the UK's insolvency and restructuring framework harder to navigate.

To that end, we would strongly encourage the Department for Transport to work closely with the Insolvency Service, which is developing these wider reforms, to ensure a 'joined up' approach to policy making in this area.

Should your officials require any further information, or if it would be helpful to meet to discuss this issue in more detail, please do not hesitate to contact R3's Public Affairs Manager, James Jeffreys, on 020 7566 4220 or at [james.jeffreys@r3.org.uk](mailto:james.jeffreys@r3.org.uk).

We look forward to hearing from you.

Yours sincerely,



Duncan Swift  
R3 President