



R3's manifesto for the 2019 general election

INSOLVENCY

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A roadmap for the future of the UK's insolvency and restructuring framework

R3 - The home of the UK's restructuring and insolvency community

INTRODUCTION

While much has been made of the political uncertainty surrounding the 2019 general election, less attention appears to have been paid to the longer-term economic uncertainty facing the UK and the tools available to assist businesses and individuals when things get difficult financially.

As we approach the start of a new decade, it's worth considering just what a journey the UK economy has been on over the last ten or so years. A decade ago, businesses were navigating the aftermath of the global financial crisis. After something of an economic rebound, the second half of the decade has seen businesses grappling with the implications of Brexit.

There are wider, more long-lasting trends to deal with, too. For years, UK economic growth has been sluggish – and uneven – while the UK 'productivity' puzzle remains unsolved. 'Growth' is not being experienced by everyone. Household debt, and demand for personal debt solutions, is climbing, with many individuals struggling to make ends meet on a monthly basis. These trends will be exacerbated by significant structural changes to the economy, too, with things like automation and artificial intelligence likely to fundamentally transform the economy.

Against that backdrop, the insolvency, restructuring and turnaround profession has been playing a vital role in the UK economy: promoting economic regeneration, resolving financial distress for businesses and individuals, saving jobs, and creating the confidence and public trust which underpin trading, lending and investment. But with uncertain prospects for the economy over the next ten years, it is vital that the profession has the tools it needs to continue this work effectively.

This manifesto sets out a roadmap for policy makers to ensure the framework within which the insolvency and restructuring profession operates is able to provide businesses and individuals with the tools they need to navigate an uncertain economic environment.



Emma Lovell
R3 Chief Executive
Officer



Duncan Swift
R3 President 2019-20

THE INSOLVENCY AND RESTRUCTURING PROFESSION

Insolvency practitioners, and other insolvency and restructuring professionals, play a vital role in ensuring the UK maintains its reputation as one of the best places in the world to do business. The insolvency and restructuring profession:

- Rescues businesses and jobs, and promotes economic regeneration;
- Creates the confidence to trade, lend and invest by returning money to creditors after insolvencies;
- Investigates and disrupts fraud;
- Helps keep businesses fit for the future; and
- Resolves financial distress for businesses and individuals.

There are approximately 1,600 licensed insolvency practitioners in the UK, supported by thousands of colleagues. Thousands of other professionals specialise in insolvency law, restructuring, or providing turnaround advice. The profession is a key part of the UK's insolvency and restructuring framework, which is ranked among the best in the world by the World Bank. The UK framework scores highly for its rapid outcomes for creditors, its cost effectiveness, and its ability to rescue businesses.

What is insolvency and restructuring?

The insolvency and restructuring profession works with financially struggling businesses and individuals, both inside and outside of statutory insolvency procedures. These processes help financially distressed and insolvent companies and individuals to repay what they owe – and to turn their fortunes around where possible.

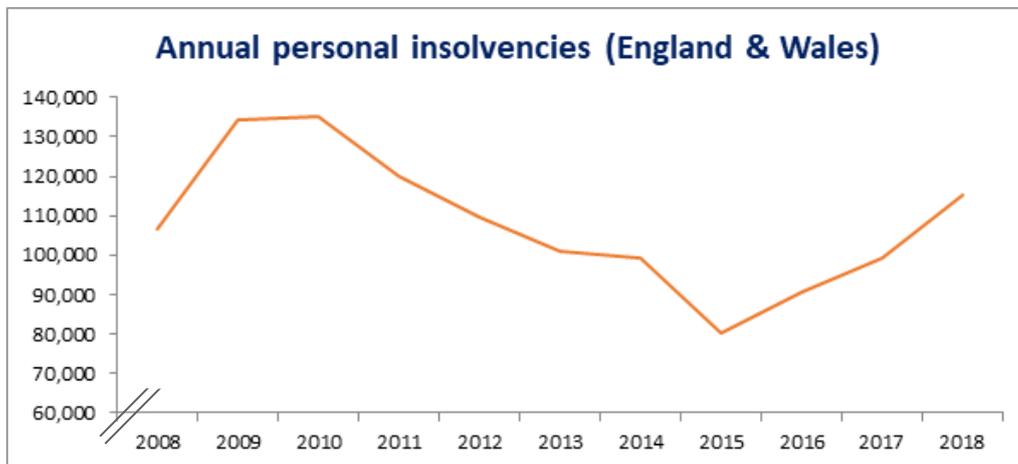
Insolvency

A business or an individual is considered insolvent when their liabilities outweigh their assets, or they are unable to pay their debts when they fall due. There are a number of different insolvency procedures to deal with different insolvency situations. For companies, these include: liquidation (compulsory or voluntary), administration, or a Company Voluntary Arrangement (CVA). For individuals, these include bankruptcy, an Individual Voluntary Arrangement (IVA), or a Debt Relief Order. All insolvency procedures are overseen by either the government 'Official Receiver' or by a licensed insolvency practitioner.

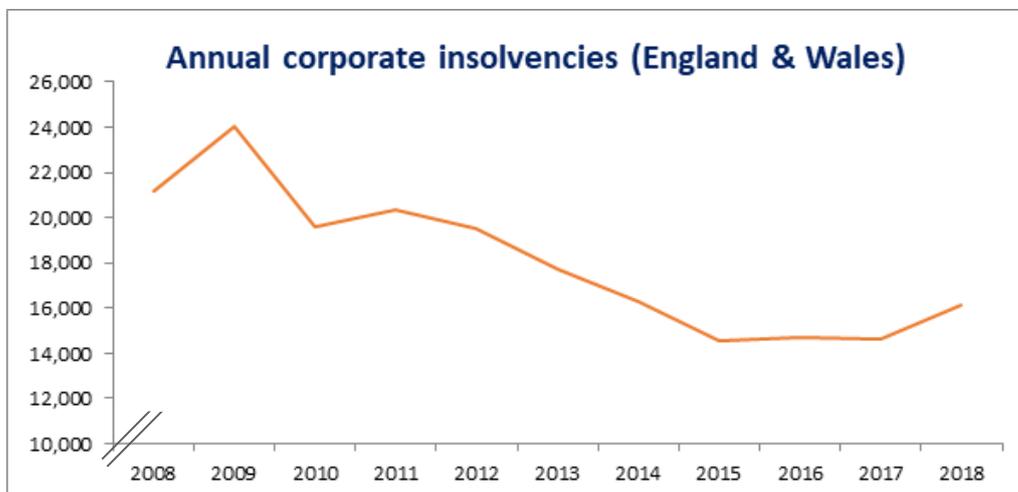
Restructuring

Restructuring is a process that aims to ensure that companies and groups are profitable and have a healthy cash flow. Very broadly, it can take two forms: financial restructuring (where a company looks to restructure the debts it owes to its creditors) and operational restructuring (where the company looks to change how its underlying business works).

THE LATEST INSOLVENCY NUMBERS



Source: Insolvency Service & R3



Source: Insolvency Service & R3

The number of personal insolvencies in the UK started to turn sharply upwards from 2015, after a steady fall following the end of the financial crisis. While corporate insolvency numbers followed broadly the same downward trend as personal insolvencies up until 2015, the situation was remarkably flat between 2015 and mid-2017. However, since then, the number of corporate insolvencies has started to increase steadily.

Looking at the most recent corporate insolvency statistics (Q3 2019), we can see that the number of administrations, a procedure designed to support business restructure and rescue, has increased by 20% since the previous quarter, and is at its highest since the first quarter of 2014. Meanwhile, an increase in Creditors' Voluntary Liquidations suggests business rescue is more difficult to achieve in the current economic environment, perhaps reflecting greater uncertainty that purchasers can deliver sustainable business turnarounds.

Since 2015, the rise in personal insolvency numbers has largely been driven by an increase in the number of Individual Voluntary Arrangements (IVAs), a flexible personal insolvency procedure often used to deal with consumer debts; indeed, comparing Q3 2018 with Q3 2019, IVAs increased by 42.7%, suggesting that for many individuals, maintaining spending levels through debt or by using savings is proving an increasingly unsustainable option, as banks and other lenders have tightened their credit standards in response to the Bank of England's concerns around consumer over-indebtedness.

Against a backdrop of uncertainty regarding the future of the UK's relationship with the EU, and considerable structural changes to the economy taking effect at the same time, there is little sign that these trends – across both personal and corporate insolvencies – will reverse any time soon.

SUPPORT BUSINESS RESCUE

PRESS AHEAD WITH REFORMS TO THE CORPORATE INSOLVENCY FRAMEWORK

The next Government should prioritise the introduction of long-awaited improvements to the UK's corporate insolvency framework, in order to ensure that it remains internationally competitive – and that the profession has the tools available to support business rescue in the years ahead.

In August 2018, the then-Government announced plans for the most significant changes to the UK's corporate insolvency and restructuring framework since the 2002 Enterprise Act. The bulk of these proposals were based on ideas first put forward in 2016.

With a number of countries, including places like Singapore or other EU member states, making significant changes to their own insolvency and restructuring frameworks, the proposed reforms are a vital step towards ensuring that the UK maintains the competitiveness of its internationally renowned insolvency and restructuring framework. A world-class framework is needed if the UK is to remain one of the most attractive places in the world to do business after it leaves the EU.

While R3 believes that the proposals still require some improvement, we support the principles behind most of these measures and feel that they would make a positive difference to the UK's reputation as a place to do business – as well as provide the insolvency and restructuring profession with more tools to support business rescue.

Key proposals in the reform package include: a business rescue moratorium, a new court-based restructuring tool, and measures to make it more difficult for suppliers to disrupt business rescue efforts without a good reason for doing so.

SUPPORT BUSINESS RESCUE

PROTECT THE VALUE OF CVAS AND PRE-PACKS TO THE UK ECONOMY

Any changes to the way in which CVAs and pre-packs – insolvency tools that attract significant public attention – operate, should be evidence-based and recognise their value in supporting business rescue.

Insolvency is an unavoidable – and important – part of the economic and business cycle. No company or economic sector is immune to a decline in fortunes, and the corporate insolvency and restructuring framework is a means of restoring companies to good health and protecting creditors from the consequences of a company's inability to pay its debts.

Insolvency procedures often attract significant public attention: the nature of insolvency means that creditors face losses, and jobs may be at risk. The insolvency and restructuring profession takes steps to minimise creditor losses, and to rescue jobs and businesses. Often, rescuing a business is the best means of protecting both jobs and creditors.

Two procedures used to rescue businesses often attract attention: Company Voluntary Arrangements (CVAs) and 'pre-pack' administrations.

The next Government should tread carefully when responding to stakeholder criticism of these procedures: CVAs are a very flexible tool and can be used in all sorts of situations. Combined with fresh finance, CVAs can help turn around a company and maximise repayments to creditors. Even where they don't meet all their objectives, CVAs can still see more money returned to creditors than alternatives, and they can give a supply chain time to adapt to a struggling company's closure.

Pre-packs are an equally important business rescue tool, and are an effective means of preserving jobs and maximising returns to an insolvent company's creditors. Without pre-packs, creditor returns would be worse.

SUPPORT BUSINESS RESCUE

RETHINK PLANS TO TACKLE 'TAX ABUSE AND COMPANY INSOLVENCY'

Existing plans to give HMRC greater powers to pursue tax debts in company insolvencies need recalibrating to ensure that genuine entrepreneurs and those professionals who support business turnaround aren't unfairly targeted – which could in turn damage business rescue.

The last Government put forward plans to make directors personally liable for corporate tax debts in situations where they are suspected of abusing the insolvency framework in order to avoid paying taxes. While R3 understands the issue which HMRC is seeking to address, we are concerned that, without amendments and strict guidance to accompany the legislation, there is a risk that the policy may be applied much more widely than originally intended.

The implications of the policy are significant: it breaches the principle of 'limited liability' which lies at the heart of the UK's corporate framework; it could make business rescue less likely; and it undermines the principle of creditor equality, by granting HMRC powers to retrieve funds unavailable to other creditors.

The legislation will also allow HMRC to make individuals liable for corporate tax debts if they have links to a number of corporate insolvencies in the past. Those members of the insolvency and restructuring profession who have spent years working to turn around financially distressed business could be placed at risk as a result. This could damage business rescue by making professionals working in this space less likely to seek to engage with struggling businesses. Although ministers have said that HMRC will not apply this power in this way, this needs to be confirmed in legislation.

TACKLE LATE PAYMENT CULTURE

The next Government should build on the efforts of the Small Business Commissioner, the Chartered Institute of Credit Management (overseeing the Prompt Payment Code) and other organisations to discourage late payment, which is a root cause of much financial distress.

The insolvency and restructuring profession works with struggling businesses on a daily basis. Businesses can struggle for a variety of reasons, but a substantial number have otherwise avoidable problems stemming from late payment or the generally poor payment practices of customers. The customers who cause the biggest problems are often larger companies that have the ability and skill to manage their payments in a way which maximises their own position at the expense of smaller suppliers.

R3's statistics show that nearly one in five UK businesses are owed payment on invoices that are more than 30 days overdue. Late payment is endemic in parts of the economy such as construction and food supply. Late payment makes it harder to rescue businesses, to preserve jobs, and to return money to creditors.

ENSURE A FAIRER DEAL FOR CREDITORS

PROTECT ACCESS TO FINANCE AND THE FOUNDATIONS FOR A GROWING ECONOMY, BY DROPPING PLANS TO MAKE HMRC A PREFERENTIAL CREDITOR IN INSOLVENCIES

The next Government should drop existing plans to establish HMRC as a 'preferential creditor' in insolvencies, or otherwise take steps to mitigate the threat this policy poses to returns to creditors, business rescue, and the ability of businesses to access finance.

In insolvency procedures, creditors are repaid according to a strict, statutory hierarchy. Because an insolvent company is very unlikely to be able to repay all its debts, the lower a creditor is down the hierarchy, the less of their money – if anything – they are likely to see back. The last Government announced plans to move HMRC debts 'up' the hierarchy, leapfrogging debts owed to 'floating charge' lenders and debts owed to 'unsecured' creditors, including other businesses and pension funds. From April 2020, these creditors will only see money back from corporate insolvencies once HMRC has been paid what it is owed.

The policy will make it harder to rescue and fund businesses, and will increase the risk of trading and investing.

Floating charge lending is a very common form of business finance, and with these lenders now facing the possibility of not seeing any of their money back if a company becomes insolvent, they will be less willing to lend, particularly to those companies in financial distress that may be in a position to turn themselves around with fresh funding.

At the same time, unsecured creditors will increasingly face seeing nothing back from corporate insolvencies. This will increase the knock-on effect of one company's insolvency on others, and could potentially put other companies at risk. Employees and pension schemes will also lose out.

This means more business failures, leading to more missing taxes and higher redundancy payments for the government to fund. It means fewer growing and thriving businesses, leading to lower than expected tax receipts. The long-term detriment caused by this policy will significantly outweigh any short-term gain. Future governments would likely see better returns from insolvencies by encouraging HMRC to engage in insolvency procedures more actively than it does now.

The Government's policy might lead to a small up-front revenue boost for HMRC – but this will come at a disproportionate cost to the economy, and to the UK's business rescue culture.

SUPPORT THE PROFESSION'S FIGHT AGAINST FRAUD

REFORM AND STRENGTHEN THE POWERS OF COMPANIES HOUSE

The next Government should continue with plans to reform and strengthen the powers of Companies House, including the introduction of director and ultimate owner ID verification. These reforms will improve the integrity of the companies register and support the profession's fight against fraud.

The UK's insolvency and restructuring profession plays a key role in tackling and disrupting fraud. Insolvency practitioners investigate the conduct of directors and others linked to insolvent companies, and can use the insolvency framework to return money to fraud victims. The information held at Companies House often forms a crucial part of the profession's investigations, and R3 welcomed the last Government's moves to improve the quality and reliability of information held on the companies register.

In particular, R3 supports the Government's proposal that individuals acting as company officers and/or having significant control must have their identification verified by Companies House. Our members report that it is all too common to find fraudsters disguising their tracks by registering companies using different versions of their name or date of birth. This makes it hard for insolvency practitioners to trace an individual's activity and to identify other parts of a potentially fraudulent business network. Identity verification at Companies House, as well as a general strengthening of the powers Companies House has, are small but positive steps towards making it easier to tackle fraud.

We would also urge the Government to ensure that insolvency practitioners appointed as office holders in insolvent companies are included in the proposed category of individuals and organisations able to access the non-public information that Companies House does and will hold in future. Doing so will mean that a wider body of professionals will be able to carry out investigations into corporate affairs and director conduct more effectively, thereby identifying and disrupting more frauds.

SUPPORT THE PROFESSION'S FIGHT AGAINST FRAUD

MAKE GREATER USE OF THE INSOLVENCY FRAMEWORK TO TACKLE FRAUD

Making greater use of the powers available to insolvency practitioners under insolvency legislation, and encouraging more effective public-private sector engagement, could significantly increase the amount of fraud that could be tackled.

Insolvency practitioners' extensive powers to investigate and under insolvency legislation provisions, pursue those involved in fraudulent financial activities, puts them in a unique position to disrupt fraud and return money to victims.

An insolvency practitioner's powers include the ability to: interview under compulsion; search and seize property associated with fraud; obtain freezing orders against assets of those involved; overturn transfers to third parties; passport orders (where the individual is ordered to surrender their passport to prevent them leaving the country); order for the delivery up of records; hold private and public examinations before the court; and recover assets for the benefit of victims. Insolvency practitioners also benefit from extensive international recognition which enables them to pursue fraudsters and their assets overseas.

Any investigations by insolvency practitioners are carried out under civil law, which requires a lower burden of proof than criminal law. In appropriate cases, insolvency practitioners' investigations can contribute to the work of law enforcement and other government agencies or departments, by improving the evidence available to obtain criminal prosecutions or a disqualification order against a fraudster.

By encouraging government departments and other public bodies to make greater use of the powers available to insolvency practitioners, the amount and types of fraud that can be tackled, at little or no cost to those public bodies, could be significantly increased.

BETTER SUPPORT INDIVIDUALS IN FINANCIAL DISTRESS

ENSURE THE NEW 'BREATHING SPACE' FOR INDEBTED INDIVIDUALS IS FIT FOR PURPOSE

Plans for a Breathing Space should be amended so that sole traders with business debts above the VAT threshold are able to benefit from the policy.

Since early 2015, R3 has called for the introduction of a Breathing Space for indebted individuals. We believe this could give individuals an opportunity to seek advice about their finances, free from creditor pressure. Our members work with thousands of indebted individuals every year and, in their experience, failure to seek debt advice, or pressure from creditors, can see individuals end up in a debt solution which is not the most appropriate for their situation. We welcomed the last Government's commitment to this policy.

However, we have one key concern: under the current plan, a sole trader's business debts will not be covered by the policy if their business has an annual turnover in excess of the VAT threshold (£85,000).

We feel that this is an arbitrary and unhelpful threshold: sole traders may be personally liable for business debts, but unable to access the Breathing Space because their business turnover is higher than the VAT threshold; at the same time, those who aren't sole traders, but who may have a higher level of debt than a VAT-registered small trader, will be able to access the Breathing Space. For sole traders, business debts are personal debts and there is no meaningful way to distinguish between the two. We believe the next Government should reconsider this aspect of the policy.

MAINTAIN AND IMPROVE THE WIDER INSOLVENCY AND RESTRUCTURING FRAMEWORK

KEEP THE FRAMEWORK OF INSOLVENCY REGULATION FIT FOR PURPOSE

The next Government should ensure that any changes to the framework of insolvency regulation are evidenced-based and focused on outcomes rather than how regulation is delivered.

The insolvency and restructuring profession occupies a position of significant importance and responsibility within the UK's economy. Great trust is placed in the profession to uphold the law, act ethically, and protect and restore economic value. The profession needs to repay this trust. A lack of trust and confidence in the profession will lead to a lack of trust and confidence in the insolvency and restructuring framework, which will ultimately weaken the UK's economy.

At the same time, the profession is able to carry out its duties effectively *because* it has the public's trust and confidence, partly thanks to an effective and trusted regulatory framework which polices and promotes high standards. From the profession's perspective, it is vital for an effective regulatory regime to underpin, and be seen to underpin, the profession's work. Good regulation is essential.

In July 2019, the Government published a call for evidence on insolvency practitioner regulation, which sought views on the current regulatory framework.

R3 believes that while insolvency regulation can be improved, it is by no means in need of an overhaul. Service standards could help speed up disciplinary processes; further transparency around sanctions outcomes is possible; and closer regulatory collaboration on monitoring and sanctions would aid consistency. A broader remit for regulators would be welcomed, too.

While there are improvements to be made, it is vitally important that whatever approach the next Government takes to this issue, any proposed changes are evidenced-based and do not have unintended consequences.

MAINTAIN AND IMPROVE THE WIDER INSOLVENCY AND RESTRUCTURING FRAMEWORK

ENSURE A JOINED-UP APPROACH ACROSS GOVERNMENT ON INSOLVENCY ISSUES

Insolvency touches every sector of the economy and a wide range of policy areas. Creditors, stakeholders, individuals and the profession would benefit from a cross-government approach to insolvency issues.

The main government body leading on insolvency policy and regulation is the Insolvency Service, an executive agency of the Department for Business, Energy and Industrial Strategy.

While it makes sense for one body to have overall responsibility for this important policy area, following a number of high-profile insolvency cases, as well as a series of policy announcements from across government over recent years, it has come in to sharp focus just how many different policy areas and sectors of the economy that insolvency touches. Whether it be tax policy proposals from HMRC that could have a huge impact on business rescue and returns to creditors, Department for Transport proposals for the reform of airline insolvencies which could damage investment in the sector, or the way in which large-scale insolvency cases like Carillion are handled, it's clear that insolvency is a critically important area for government to get right.

A more joined-up approach across government to dealing with these issues would lead to a more coherent policy framework and provide greater confidence for creditors, stakeholders, individuals and the profession.



ABOUT R3

We are the thriving, inclusive organisation at the heart of the UK's insolvency and restructuring profession.

We are the association which embraces the entire community of professionals within the restructuring and insolvency world, whatever the size of their practice, their experience or their specialism.

We play a leading role in ensuring the UK remains a global centre for resolving financial distress, promoting economic regeneration, and maintaining integrity in our framework. R3 protects and promotes the environment and strong restructuring and insolvency framework required to enable our members to fulfil their vital role in the economy and in society.

The insolvency and restructuring profession

Members of the insolvency and restructuring profession protect and restore value at all levels of the UK's economy. Their expertise promotes economic regeneration, resolves financial distress for businesses and individuals, saves jobs, and creates the confidence and public trust which underpin trading, lending and investment.

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