Consultation on an effective insolvency framework within the EU

Fields marked with * are mandatory.

Introduction

An appropriate insolvency framework is important for society at large and in particular for investors, creditors and debtors. It is an essential element of a good business environment and is therefore important for jobs and growth.

A good insolvency framework maximises the efficiency, predictability and effectiveness of insolvency proceedings. This makes it easier to trade, supports an effective credit system and ensures a favourable investment climate, in turn benefiting the wider economy.

Insolvency frameworks should provide a transparent, predictable and cost-effective set of rules that can be used to preserve and maximise the value of debtors' assets. The rules should make it possible, either to:

- save businesses (by restructuring the existing company or by selling it as a "going concern"); or
- make it easier to liquidate a company and its assets if that company has not prospect of survival.

Efficient insolvency rules could also help increase the recovery rate of debts and avoid the build-up of non-performing loans in the financial system.

The Commission's Annual Growth Survey 2016 explicitly recognises the importance of *'well-functioning insolvency frameworks'*. These are *'crucial for investment decisions since they define rights of creditors and borrowers in the event of financial difficulties'*.

Conversely, inefficient and ineffective frameworks result in the discontinuation of viable businesses, lengthy procedures and a low rate of recovery. This often translates into significant problems for the Member States concerned and for the wider European economy. These problems may take the following forms:

- Unnecessary liquidation of viable businesses, resulting in a loss of productive capacity;
- *De facto* or *de jure* disqualification of failed entrepreneurs or the exclusion from economic life of indebted members of the public;
- Barriers to corporate lending and investment, including cross-border investment. Uncertainty or difficulties over realising value from distressed debt may be particularly pronounced in the case of cross-border lending and investments. This may increase the cost at which investors and creditors are willing to invest in or lend to cross-border borrowers.
- Difficulties for creditors in recovering value from distressed debt. This may contribute to persistently high levels of non-performing loans, which weigh on bank balance sheets and may constrain bank lending.

In the public consultation on a Capital Markets Union, insolvency laws were singled out as one of the key barriers preventing the integration of capital markets in the EU. Consultation respondents broadly agreed that both the inefficiency and divergence of insolvency laws make it harder for investors to assess credit risk, particularly in cross-border investments. Convergence of insolvency and restructuring proceedings would facilitate greater legal certainty for cross-border investors and encourage the timely restructuring of viable companies in financial distress [1].

Focus on restructuring and a second chance:

A clear and effective approach to debt restructuring can benefit both the borrowing and lending sides of the market. Businesses that are in temporary distress should be able to restructure and be saved if their business is viable. Member States' legal frameworks have a crucial role in creating the conditions for successful restructuring, whether within or outside formal insolvency proceedings.

To encourage entrepreneurial activity, entrepreneurs and managers of companies should not be stigmatised when honest business endeavours fail. Individuals should not be deterred from entrepreneurial activity or denied the opportunity for a 'second chance'. Similarly, managers of companies may benefit from clear rules on their disqualification over insolvency-related misconduct.

For consumers (i.e. individuals with debts of a non-professional nature), a possible second chance might give them the incentive to start consuming again and take up gainful employment without the stigma of insolvency burdening them for years on end.

This means that for individual debtors, whether entrepreneurs or consumers, the rules on how to discharge the remaining debt following bankruptcy are important. Any rules providing for debt discharge need to be carefully designed to prevent abuse and incentivise careful management of business debt from the outset.

As a result, in the Capital Markets Union Action Plan, the Commission announced its intention to propose a legislative initiative on business insolvency, including early restructuring and second chance. The legislative initiative seeks to address the most important barriers to the free flow of capital, building on national sets of rules that work well.

The Commission Communication '*Upgrading the Single Market: more opportunities for people and business*' states that the effects of a potential bankruptcy deter individuals from entrepreneurial activity. The prospect of a fresh start for bankrupt entrepreneurs encourages would-be entrepreneurs to start and scale-up new business activities. This creates a more beneficial environment for innovation.

Helping creditors (banks) to recover value in the event of insolvency

The Five Presidents' Report on 'Completing Europe's Economic and Monetary Union' identified insolvency laws as a key component of Financial Union. An effective insolvency framework should also contribute to the efficient management of defaulting loans and reduce the accumulation of non-performing loans on banks' balance sheets.

This position on insolvency reform was set out in the Commission Communication 'Towards the Completion of the Banking Union' of 24 November 2015. Efficient insolvency frameworks would increase recovery rates and improve pricing of non-performing loans in the interest of developing a secondary market. Such loans would not then remain on banks' balance sheets for protracted periods of time, debts could be at least partially recovered and debtors could have a fresh start.

The Commission has examined national insolvency regimes as part of the European Semester, the EU's economic governance framework. Lengthy, inefficient and costly insolvency proceedings in some Member States were found to be a contributing factor to insufficient post-crisis debt deleveraging in the private sector and exacerbating debt overhang.

Objectives of this consultation

This consultation asks about the key insolvency barriers. It focuses in particular on gathering views on:

- the efficient organisation of debt restructuring procedures;
- the rationale and the process for debt discharge for entrepreneurs (and its possible extension to consumers).

Beyond these two policy areas, the consultation also invites views on selected aspects of efficient and effective insolvency frameworks which may have particular importance for the Internal Market or the integration of capital markets. Such frameworks should help to maximise the value received by creditors, shareholders and other stakeholders.

The responses will be used to identify which aspects should form part of a legislative initiative [2] and other possible complementary action in this field. The responses will be taken into account alongside the results of an external economic study carried out on behalf of the Commission as well as other evidence and analysis. The results of the consultation are without prejudice to any potential future Commission proposal.

This consultation is run via the 'EU-Survey' online tool, which makes it easier to collect answers from the widest possible range of respondents. In addition to choosing from the pre-defined answers, respondents are encouraged to explain their views or add additional information or explanations in the free text boxes provided. Respondents can add additional information at the end of the consultation and/or can do so by clicking on the 'other' options and the boxes that follow. Alternatively, separate contributions can be sent to the dedicated mailbox.

[1] An Inception Impact Assessment which contains a detailed description of the problems found in this area, as well as the policy objectives and options for action is available on http://ec.europa.eu/smart-regulation/roadmaps/docs/2016_just_025_insolvency_en.pdf.
[2] The Commission Work Programme for 2016 announced a legislative initiative framing a new approach to business failure and insolvency.

I. Information about you

This consultation is addressed to the broadest public possible, as it is important to get views and input from all interested parties and stakeholders.

*** 1. Please indicate your role for the purpose of this consultation**

☐ Private individual
☐ Self-employed person
☐ Company
☐ Bank, credit institution, investment fund, financial institution

☐ Judge
☐ Insolvency practitioner
☐ Other legal practitioner
☐ Business adviser or business support organisation
☐ Public authority
☐ Academic
☐ Think tank
☒ Other

***Please indicate the size of your company:**

☐ large (more than 250 employees)
☐ medium (51-250 employees)
☒ small (11-50 employees)
☐ micro (0-10 employees)

***Please specify (bailiff, lawyer, notary or other)**

R3 is the leading professional association for insolvency practitioners (IPs) in the UK, promoting best practice for professionals working with financially troubled individuals and businesses, promoting the work and value of the insolvency professions' work to government and key policy makers, producing guides for insolvency practitioners and members of the public, running courses and conferences to promote learning and best practice within the insolvency profession.

Our core employees total 22 however they are supported by R3 Council (27 members) and 11 further committees made up of practising insolvency practitioners, solicitors and lawyers. We have approximately 3,000 members who handle the whole spectrum of work with financially distressed businesses and individuals including advice, rescue and turnaround and formal Insolvency Act 1986 appointments.

We have provided illustrations from the UK regime by way of example, where appropriate.

***Please specify**

Name of your organisation (if applicable)

R3 (Association of Business Recovery Professionals) – the insolvency trade body

2. Is your organisation included in the Transparency Register?

(If your organisation is not registered, you can register here.
You do not have to be registered to reply to this consultation.)

☒ Yes
☐ No

If you are registered, please indicate your register ID Number:

Assoc0014513770

***3. Have you had practical experience with insolvency proceedings?**

☒ Yes

☐ No

***In what capacity?**

☐ As a creditor

☐ As an employee in the context of an insolvency proceeding of my employer

☐ As an owner or director of an insolvent business

☐ As an over-indebted private individual or consumer

☐ As a judge

☐ As an insolvency practitioner

☐ As another kind of legal practitioner

☐ As a business adviser or business support organisation

☒ Other

***Please specify**

Our membership is made up of practising insolvency practitioners, lawyers and solicitors who work in the field of insolvency and other professionals working within or having an interest in the insolvency profession. The responses given are based on direct feedback from practising insolvency practitioners who make up our committees.

***4. Please indicate the country where you are located:**

☐ Austria

☐ Belgium

☐ Bulgaria

☐ Cyprus

☐ Czech Republic

☐ Germany

☐ Denmark

☐ Estonia

☐ Greece

☐ Spain

☐ Finland

☐ France

☐ Hungary

☐ Croatia

☐ Ireland

☐ Italy

☐ Lithuania

☐ Luxembourg

☐ Latvia

☐ Malta

☐ Netherlands

☐ Poland

☐ Portugal
☐ Romania
☐ Sweden
☐ Slovenia
☐ Slovak Republic
☒ United Kingdom
☐ Non-EU country

*Please specify

5. Please provide your contact information:

*First name

Victoria

*Last name

Jonson

*Postal address (if you are replying on behalf of an organisation, please provide your professional postal address)

120 Aldersgate Street, London, EC1A 4JQ

*E-mail address (if you are replying on behalf of an organisation, please provide your professional e-mail address)

Victoria.Jonson@r3.org.uk

*6. Please indicate your preference over the publication of your response on the Commission's website:

☒ Under the name given: I consent to publication of all information in my contribution and I declare that none of it is subject to copyright restrictions that prevent publication.

☐ Anonymously: I consent to the publication of all information in my contribution, except my name/the name of my organisation and I declare that none of it is under copyright restrictions that prevent publication.

☐ Please keep my contribution confidential (it will not be published, but will be used internally within the Commission)

Please note that regardless of the option chosen, your contribution may be subject to a request for access to documents under Regulation 1049/2001 on public access to European Parliament, Council and Commission documents. In this case, the request will be assessed against the conditions set out in the Regulation and in accordance with applicable data protection rules.

II. Questions

In general, an insolvency framework should ensure that viable businesses can be restructured and continue operating, while non-viable ones can be quickly liquidated. Over indebted individuals should also have access to insolvency proceedings and discharge provisions subject to certain conditions. Member States have in place different systems, some of which comply at least partially with these requirements and some of which do not. These differences may have an impact on the functioning of the internal market.

1. Scope

1.1. Which measures should be taken to achieve an appropriate insolvency framework within the EU? (choose all that apply)

☐ a) Preventive measures to enable the restructuring of viable businesses
☐ b) Measures to increase the recovery rates of debts in insolvency
☐ c) Measures to ensure the discharge of debts for entrepreneurs (individuals)
☐ d) Measures to ensure the discharge of debts for consumers
☐ e) Measures governing employees' rights in insolvency
☐ f) Measures ensuring the enforcement of debts
☒ g) Other measures
☐ h) No opinion

Please explain

The options listed above are all 'good' measures to take into account when considering an appropriate insolvency framework in the EU. However, R3 does not believe that it is appropriate that all or indeed, any of these measures should be dealt with at the EU level, and should instead be considered by Member States. For example, 'Measures to ensure the discharge of debts for entrepreneurs (individuals)' and 'Measures to ensure the discharge of debts for consumers' are not differentiated in the UK regime, whereas we appreciate that these measures are differentiated in other Member States. A number of the measures, such as 'Measures governing employees' rights in insolvency' are matters of policy which will be influenced by political and social considerations, which Member States will have polarized views on. Therefore, whilst a 'framework' could be set at EU level, Member States should be allowed to agree the specifics of these measures.

R3's view mirrors that stated by the UK Government in its response to the Capital Markets Union Green Paper with regard to "What specific aspects of insolvency laws would need to be harmonised in order to support the emergence of a pan-European capital market?". The response stated that the UK Government does not see a need to harmonise insolvency law in order to support the emergence of a pan-European capital market. The response went on to state that the objective of stronger insolvency regimes across the EU which promote recovery for business and improve predictability and legal certainty for investors would instead be better achieved by the introduction of common principles that all Member States should adhere to in the creation of their insolvency regimes. This would best address current barriers whilst working within the legal and cultural differences of Member States. The response stated that the UK welcomes the Commission's proposals around improving the effectiveness of insolvency frameworks, with the intention of promoting business recovery and returning capital to creditors for it to be re-invested back into the European market.

1.2. To what extent do the existing differences between the laws of the Member States in the areas mentioned below affect the functioning of the Internal Market?

(For example, differences affect the Internal Market when creditors or investors and debtors are located in different Member States and this has an impact on the recovery of debts, the legal certainty of transactions, the quantification of risks etc.)

	To a large extent	To a considerable extent	To some extent	Not at all	No opinion
a) Preventive measures to enable the restructuring of viable businesses	☐	☐	☐	☐	☒
b) Measures to increase the recovery rates of debts in insolvency	☐	☐	☐	☐	☒
c) Measures aimed to ensure the discharge of debts for entrepreneurs (individuals)	☐	☐	☐	☐	☒
d) Measures to ensure the discharge of debts for consumers	☐	☐	☐	☐	☒
e) Measures governing employees' rights in insolvency	☐	☐	☐	☐	☒
f) Measures ensuring the enforcement of debts	☐	☐	☐	☐	☒
g) Other measures	☐	☐	☐	☐	☒

Please explain

Detailed and extensive data would be required to assess the impact of differences in the laws of Member States on the functioning of the internal market. We are unaware of any such research having been undertaken in this regard. However the suggested answers appear to anticipate that respondents will provide an opinion. We question the value of opinions provided except where there is evidential support. As a trade body representing a large number of insolvency practitioners, it would be inappropriate for us to provide such an opinion.

R3 believes however, that the effect on the functioning of the internal market is likely to be negligible because a small percentage of businesses (as a percentage of the total number of businesses) become insolvent.

1.3. To what extent do the measures mentioned below have an impact on the creation and operations of newly established companies?

	To a large extent	To a considerable extent	To some extent	Not at all	No opinion
a) Preventive measures to enable the restructuring of viable businesses	☐	☐	☐	☐	☒
b) Measures to increase the recovery rates of debts in insolvency	☐	☐	☐	☐	☒
c) Measures to ensure the discharge of debts for entrepreneurs (individuals)	☐	☐	☐	☐	☒
d) Measures governing employees' rights in insolvency	☐	☐	☐	☐	☒
e) Measures ensuring the enforcement of debts	☐	☐	☐	☐	☒
f) Other measures	☐	☐	☐	☐	☒

Please explain

For the reasons explained above, R3 does not have any statistical data but anecdotal evidence from our members suggests that such measures do not feature as a significant or determining factor when new businesses are created. Operations tend to focus on the likely upside of the business and other considerations such as the tax treatment of the business or employees' rights generally, together with other commercial factors which may dictate the location of the operations.

2. Saving viable businesses in difficulty

In general, an insolvency framework should ensure that viable businesses can be restructured and continue operating. However, the conditions under which a company is deemed viable and should be restructured or liquidated differ from Member State to Member State. In this consultation, the term ‘restructuring’ covers both restructuring as an existing company and the sale of a company as a going concern to another company. There is also a difference between the viability of a legal entity and that of a business contained within it or even spread across several legal entities.

The rules regulating restructuring procedures (including the contents of the restructuring plan and related procedural issues) have a crucial role in creating the conditions for successful restructuring, whether within or outside insolvency proceedings. There are major differences across Member

States in the rules on the procedure for adopting a restructuring plan, including required majorities for its adoption and the rights of dissenting creditors.

Laws of Member States also differ on the standards applied by the courts when asking for a stay of individual enforcement actions (i.e. a suspension of the right to enforce a claim by a creditor against a debtor, also known as a 'moratorium') to be granted, when approving the plan and the possibility to challenge such approval. Moreover, under certain national insolvency frameworks, courts may have wide discretionary powers over the approval of the plan and possible changes to it, while under other laws these powers are rather more limited.

Rigid and impracticable rules may hinder the chances of adopting a restructuring plan. Restructuring viable businesses avoids unnecessary liquidation and thus helps safeguard the debtor's assets as a going concern, maximising value for owners and shareholders as well as for creditors. An efficient business restructuring procedure may also give equity investors a chance to recover the value of their investment. At the same time, restructuring procedures must be safeguarded against misuse and depletion of the assets in the process.

There are also significant differences between the criteria for opening insolvency proceedings. In certain Member States, insolvency proceedings may be opened only for debtors that are already affected by financial difficulties or are already considered insolvent. In others, proceedings can be opened for solvent debtors that anticipate facing insolvency in the imminent future. Such proceedings do not have the character of informal pre-insolvency proceedings. Further differences may also be found in insolvency tests (liquidity test, balance sheet test, over-indebtedness test) and in the obligation for a debtor to file for the opening of insolvency proceedings when insolvency occurs.

In a company, directors exercise corporate powers which are generally balanced with duties of care prohibiting wrongful trading. Some Member States have certain obligations in place for directors in the period before insolvency occurs and impose liability for any harm caused by continuing to operate when it was either clear or should have been foreseen that insolvency could not be avoided. The rationale for such provisions is to create appropriate incentives for early action through the use of voluntary restructuring negotiations. It may also encourage directors to obtain competent professional advice when financial difficulties occur and thus avoid insolvency.

GENERAL QUESTIONS

2.1 To what extent do existing differences between the laws of the Member States in the areas mentioned below affect the functioning of the Internal Market?

(For example, differences affect the Internal Market when creditors or investors and debtors are located in different Member States and this has an impact on the recovery of debts, the legal certainty of transactions, the quantification of risks etc.)

	To a large extent	To a considerable extent	To some extent	Not at all	No opinion

a) Measures to give access to a toolkit enabling fast restructuring	☐	☐	☐	☐	☒
b) Measures to ensure the assessment of a debtor's viability	☐	☐	☐	☐	☒
c) Measures to provide minimum standards in relation to the definition of insolvency	☐	☐	☐	☐	☒
d) Measures to lay down the duties of directors in companies in financial distress	☐	☐	☐	☐	☒
e) Measures to protect new financing given to companies that are being restructured	☐	☐	☐	☐	☒
f) Measures to clarify the position of shareholders of companies in insolvency or close to insolvency	☐	☐	☐	☐	☒
g) Measures to promote assistance to financially distressed debtors	☐	☐	☐	☐	☒
h) Other measures	☐	☐	☐	☐	☒

Please specify which other measures in national laws affect the functioning of the Internal Market.

As explained above, R3 is not aware of any statistical evidence available in this regard.

However, a number of our members undertake pan-European insolvencies and deal with debtors and creditors in different countries and they have indicated that in cases of a substantial size and complexity, the difference of laws in the various locations of the debtor and its creditors, whilst something that is taken into account, is not necessarily an obstacle to rescue or recovery. More importantly, they have recognised that having a wide choice of options and a system that can be regarded as well tested and predictable is more important than a common

standard.

For smaller cases with cross border aspects, it is recognised that additional costs may be incurred in restructurings although most creditors will approach their participation from a commercial perspective (in both domestic and pan-European cases) and ultimately what they anticipate they will recover. These may be influenced by some of the measures identified but will very much be dealt with on a case by case basis. Minimum standards will not necessarily change this, as each situation will need to be considered on its own merit - some situations, even entirely domestic situations, will be more complex than others.

There are a number of other measures, which are not outlined above, which often in combination with those set out above have a significant effect on the functioning of the Internal Market. Of particular relevance are the capacity of the courts to deal with fluctuating volumes of work (thus providing ready access to the courts) and the experience, knowledge and specialism of the judiciary and the insolvency practitioners entrusted to implement the measures in each Member State.

Therefore, it would be worthwhile to consider measures to encourage Member States to ensure that their court systems are efficient and effective and that insolvency practitioners in all Member States are highly qualified and regulated.

2.2 What impact do the different types of measures mentioned below have on saving viable businesses?

	Very strong impact	Considerable impact	Little impact	No impact at all	No opinion
a) Measures to give access to a toolkit enabling fast restructuring	☒	☐	☐	☐	☐
b) Measures to ensure the assessment of the viability of a debtor	☐	☐	☐	☒	☐
c) Measures to provide minimum standards in relation to the definition of insolvency	☐	☐	☐	☒	☐
d) Measures to lay down the duties of directors in companies in financial distress	☒	☐	☐	☐	☐
e) Measures to protect new financing given to companies that are being restructured	☒	☐	☐	☐	☐

f) Measures to clarify the position of shareholders of companies in insolvency or close to insolvency	☒	☐	☐	☐	☐
g) Measures to promote assistance to financially distressed debtors	☒	☐	☐	☐	☐
h) Other measures	☒	☐	☐	☐	☐

Please specify which other measures have an impact on saving viable businesses.

There are a significant number of measures which have an impact on saving a business, ranging from legislative measures to access to timely professional advice.

b) Measures to ensure the assessment of the viability of a debtor. There is no formal framework in the UK to ensure that there is an assessment of the debtor's viability, but inevitably in a restructuring context, the debtor will need to persuade its creditors to engage and support any restructuring proposals. In the UK, a distressed business is usually required by its key creditor stakeholders to allow independent financial advisers to carry out a business review. This often assists the debtor in formulating its proposals for rescue, and has the advantage of already having the creditors on board. At other key stages in a restructuring in the UK, creditors will usually want to satisfy themselves as to the company's prospects to restructure so, for example, a valuation of the business and likely alternatives to a restructuring are often used in the promotion of any scheme or company voluntary arrangement. The informal assessments that take place are in contrast to other jurisdictions. In other jurisdictions, for example Germany in the context of Protective Shield Proceedings, a "restructuring certificate" is required confirming that the business is viable before it can make use of that process. Likewise in Italy, debt restructuring agreements require feasibility reports from independent experts to be provided. The experience of our members suggests that these procedures in Germany are little used, likewise in Italy, but this may be due to the fact that they are still in their infancy.

c) Measures to provide minimum standards in relation to the definition of insolvency. The definition of insolvency is important in the UK for determining the point in time at which directors should have taken steps to protect the interests of creditors, and for most insolvency procedures, for determining the court's jurisdiction. We assume this question is directed towards determining whether minimum standards for the definition of insolvency should require, for example, both a balance sheet and cash flow test. If this is the case, we refer to our answer to 2.7.1 where we recommend a combination of an illiquidity and balance sheet test. However absent statistical comparative information we are unable to assess the impact which such measures have on saving viable businesses and in fact the rescue procedures for the most part are designed to prevent formal insolvency. If a minimum standard is advocated we suggest that the UK definition of insolvency set out below would be a good model:

A company is insolvent (unable to pay its debts) if either the value of its assets is less than the amount of its liabilities, taking into account its contingent and prospective liabilities (the balance sheet test) or if it is unable to pay its debts as they fall due (the cash flow test), which can be evidenced by an unpaid statutory demand or unpaid judgment or it is otherwise proved in court to be the case.

h) Other measures. There are a significant number of issues that have an impact on saving viable businesses which includes:

- The cost of restructuring
- The availability/ range of recognised informal measures
- The court system in terms of speed, cost and ‘commerciality’
- The ability of qualified and regulated insolvency processionals to lead the restructure/ business rescue

- The broader business environment and regulatory regime.

SPECIFIC QUESTIONS

2.3 If creditors are situated in a different Member State(s) than their debtors, what impact does this have on the restructuring of the business of debtors as opposed to a purely national situation?

☐ a) Very significant impact
☐ b) Significant impact
☒ c) Little impact
☐ d) No impact at all
☐ e) No opinion

Please explain your choice, including which aspects are particularly affected.

The impact of creditors being in a different Member State will vary depending on which Member State the insolvent debtor is in and what insolvency process is entered into. If creditor engagement is required to approve the restructuring the following factors may negatively affect the process: changes in language may frustrate understanding, currency differences may affect outcomes for creditors in different Member States, differences in local rules for submitting creditor claims, differences in local technologies may make timely communication with creditors more difficult, there may be alternative recovery options available in a creditor's domestic country which they choose to pursue over the interests of the creditors as a whole. These issues may be alleviated by the changes introduced by the Recast Regulation on Insolvency Proceedings which includes information on national insolvency laws, the establishment of standard claim forms, standard notices to creditors and publicly available insolvency registers.

Where creditor engagement is not required there will be minimal impact.

There can be problems in relation to proceedings which are outside of the scope of European Regulation.

2.4 When should debtors have access to a framework of restructuring measures enabling them to restructure their business/liabilities?

☐ a) Only once the debtor is already insolvent
☒ b) Before the debtor is insolvent, but where there is a likelihood of imminent insolvency (for example because the debtor has lost a major client)
☐ c) At any time
☐ d) At another moment in time
☐ e) No opinion

Please explain

R3 believes that there should be another option provided for the timing of when debtors are able to have access to a framework of restructuring measures. We believe that businesses should be able to access restructuring measures somewhere between b) "Before the debtor is insolvent but where there is a likelihood of imminent insolvency" and c) "At any time". This response is based on the fact that that there are and should continue to be solvent restructures, but that there should be controls in place to ensure that businesses cannot simply use restructuring measures to 'dump debts'. Therefore, this option takes into account that there should be some controls in place and some 'factors' that a business must have to be able to use such a tool.

As outlined in Section 1, R3 aims to provide illustrations from the UK regime by way of example:

Within the UK, solvent companies may be wound up using the members' voluntary liquidation process. This is beneficial to the restructuring of groups where the business model has changed or directors wish to split the business undertaken by a company, or a company intends to cease trading. In such a situation the debtor company is required to repay all debts in full.

The UK definition of insolvency provides for a company to take into account the likelihood of imminent insolvency and therefore directors can access forms of formal insolvency and restructuring processes, such as administration or a company voluntary arrangement without the need to wait for creditor action to be taken following the insolvency and failure of the company. This may or may not result in creditors being paid in full. Creditor approval to such processes is required.

2.4.1 Should such restructuring measures always require, at some stage, the opening of some sort of a formal procedure in which a court (or other competent authority or body) is involved?

☐ a) Yes, as of the beginning of the negotiations on a restructuring plan
☒ b) Yes, from the moment it becomes necessary to stay enforcement actions (moratorium) or obtain confirmation for the restructuring plan
☐ c) No, the involvement of a court should not be an absolute requirement
☐ d) Other options
☐ e) No opinion

Please explain

Any moratorium or restructuring plan should be subject to monitoring, supervision, or be controlled by a 'competent authority', who should be an independent and regulated experienced insolvency practitioner or the court, as appropriate.

2.4.2 Should such restructuring procedures always require publicity (e.g. through an Insolvency Register)?

☐ a) Yes, as of the beginning of the negotiations on a restructuring plan
☐ b) Yes, from the moment it becomes necessary to stay enforcement actions (moratorium) or obtain confirmation for the restructuring plan
☒ c) No, publicity should not be an absolute requirement
☐ d) Other options
☐ e) No opinion

Please explain

R3 would warn against any type of publicity. Business rescue is only able to happen at all in a significant number of cases because of confidentiality. Therefore, there is a significant risk to business rescue in suggesting that restructuring procedures should require publicity. However, it depends what is meant by 'publicity' and greater detail should be provided to stakeholders. It is accepted that greater transparency aids greater understanding and transparency is a fundamental principle underlying the insolvency profession within the UK.

2.5 Restructuring measures in which the courts are involved to a lesser degree (e.g. only for the confirmation of a restructuring plan) or not at all (e.g. an out-of-court process) should be available to: (choose all that apply)

☒ a) Microenterprises (up to 10 employees)
☒ b) Small and medium-sized enterprises, excluding microenterprises
☒ c) Large enterprises
☐ d) Other
☐ e) No opinion

Please explain

R3 believes that restructuring measures should be available to businesses of any size.

2.5 Who should do the assessment of whether a debtor is viable and fit for restructuring?

☐ a) The courts or external experts appointed by the courts
☒ b) The debtor or external experts chosen by the debtor
☐ c) The creditors or external experts chosen by the creditors
☐ d) Other persons or bodies than those listed in points a), b) or c)
☐ e) No one
☐ f) No opinion

Please specify who

There are various stages of restructuring dependent on where the business is on the 'decline curve'. Debtors (the business in financial difficulty) are often those who initiate the process and speak to their financial advisers to see if restructuring is a viable option for that business. However, creditors (often banks) may ask a business to speak to external experts to consider restructuring options, the experts being formally instructed by the debtor but usually their identity being agreed with the key creditors. There are also other stakeholders, such as a potential purchaser who is interested in taking on the business, who would wish to assess the potential for restructuring.

The debtor company prepares proposals for restructuring with the assistance of a professional adviser or insolvency practitioner and often with the support of its creditors. In relation to cases which involve a formal insolvency process such as administration or company voluntary arrangement, the creditors will have the opportunity to vote and approve the proposals and will assess whether the debtor is viable and fit for restructuring.

In all instances, expert professional advice should be sought from qualified and regulated advisers.

There should be appropriate sanctions against directors or expert advisers to discourage abuse of this process.

2.7 Is there a need for a common definition of insolvency at EU level?

☒ a) Yes
☐ b) No
☐ c) Other
☐ d) No opinion

Please explain

R3 believes that a common definition at EU level, which outlines common characteristics and is principles based (rather than a strict definition), would be beneficial but we do not consider that it is necessary to have a common definition. Having a variety of procedures, which include the ability of a debtor to resolve its issues at an early stage, whether or not it precisely fits a definition, is more important.

2.7.1 What should be included in such a definition (insolvency test)?

☐ a) Inability to pay debts as soon as they fall due (illiquidity/cash flow test)
☐ b) Value of a company's assets compared with its liabilities, including prospective and contingent liabilities (balance sheet test)
☒ c) The combination of an illiquidity and a balance sheet test
☐ d) Other
☐ e) No opinion

Please specify

No further detail required.

2.8 Should debtors in the context of restructuring measures be able to keep control over the day-to-day operations of their business (so-called 'debtor-in-possession arrangements')?

☐ a) Yes, without any supervision or control
☒ b) Yes, but subject to supervision from a suitably qualified mediator/ supervisor/ court
☐ c) Yes, but subject to conditions other than supervision from a suitably qualified mediator/ supervisor/ court
☐ d) No, debtors should not be able to keep control over the day-to-day operations at all
☐ e) Other
☐ f) No opinion

Please explain

In all cases, R3 recommends that a professionally qualified and regulated insolvency practitioner should have an oversight role. In an administration the directors lose control of the company and their powers to run the company cease. In the UK, the administrator is an agent of the company and an officer of the court and has wide powers to do anything necessary or expedient for the management of the affairs, business and property of the company.

In April 2016, R3 published "A Moratorium for Businesses: Improving Business and Job Rescue in the UK" (https://www.r3.org.uk/media/documents/policy/research_reports/bus_distress_index/R3_Moratorium_Proposal_April_2016.pdf). This proposal recommends the introduction of a moratorium for struggling businesses, with the directors remaining in control of the business during the moratorium and an insolvency practitioner acting as a Moratorium Supervisor over the length of the moratorium.

2.9 When should debtors be able to ask for a stay of individual enforcement actions?

☐ a) Only in formal insolvency proceedings
☒ b) In formal insolvency proceedings and in preventive/pre-insolvency restructuring procedures
☐ c) Other
☐ d) No opinion

Please explain

There are circumstances where a breathing space from creditor action would enable a company to put together proposals to enable it to restructure or enter into some form of formal insolvency process which would ensure the ongoing viability of the company.

In the UK filing notice of intention to appoint an administrator creates a moratorium over the company's property preventing any creditor from commencing legal action or continuing with existing legal action against the company, without express permission of the court. This moratorium continues for the duration of the subsequent administration, giving the administrator the opportunity to formulate and implement proposals.

With a company voluntary arrangement, once 75% of creditors (in value) who vote agree to the proposals all unsecured creditors are bound for the duration of the arrangement and are unable to take enforcement action against the debtor for any debts included within the arrangement. There are additional measures available to companies that qualify as a 'small company' in that a prior moratorium is available for a period of 28 days leading up to the approval of the arrangement.

As per the response to question 2.8, R3's recently published proposals for a Moratorium in the UK suggest that suppliers may not withdraw supply or change the terms of supply during the moratorium – although suppliers may request to be paid pro-forma or require a guarantee from directors.

There is value in a general stay but if the question is directed only towards targeted stays focusing on specific creditors then R3 could anticipate circumstances where it would be helpful but only under strict court supervision and in very rare circumstances, for example where one creditor's (or group of creditors') self-interest is acting directly in conflict with other creditors.

2.9.1 For how long should the enforcement of actions of individual creditors be stayed once the restructuring attempts are ongoing?

☐ a) 2-3 months, without the possibility of renewal
☐ b) 4-6 months, without the possibility of renewal
☐ c) 2-3 months, with the possibility of renewal in certain circumstances
☐ d) 4-6 months, with the possibility of renewal in certain circumstances
☐ e) Any time limit set by the court subject to the fulfilment of certain conditions
☒ f) Other
☐ g) No opinion

Please explain

Again, in order to respond appropriately to this question, it would be helpful to know what is meant by enforcement of actions of **individual** creditors and we refer to our answer above regarding the very limited role, if any, that might be served by incorporating scope for stays targeted at specific creditors or groups of creditors, as opposed to a general stay of all creditor action.

In relation to the concept of a general stay, as noted in our response to question 2.8, R3's recently published proposals for a Moratorium in the UK recommend the introduction of a 21-day moratorium for struggling businesses. It could be extended either with the issue of a CVA proposal or by applying to court for a 21 day extension. During the moratorium, creditors will be prevented from taking any action to recover their debts.

2.9.2 Should an individual creditor be allowed to ask the court to lift the stay granted to the debtor?

☐ a) Yes, in all cases
☒ b) Yes, subject to certain conditions
☐ c) No
☐ d) Other
☐ e) No opinion

Please explain

There is already provision in UK insolvency law where third parties may apply to court in an administration to enable them to recover assets or enforce security. In such cases the court must balance the potential prejudice caused to the individual/third parties against the risk that lifting the stay will upset the purpose of the administration and have a negative effect on the creditors as a whole. Assessment is done on a case by case basis as required. Insolvency practitioners may also consent to the lifting of the stay – they will take into account similar considerations.

2.10 Should a restructuring plan adopted by the majority of creditors be binding on all creditors provided that it is confirmed by a court?

☐ a) Yes, including on secured creditors
☐ b) Yes, but secured creditors should be exempted
☐ c) No
☒ d) Other
☐ e) No opinion

Please explain

It is recognised that not all restructurings can take place on a consensual basis. Therefore having the ability to bind a minority, where the majority has agreed is a useful tool. It is however recognised that in binding a dissenting minority certain safeguards need to be in place. For example, the UK regime facilitates secured creditors to be compromised under a Scheme of Arrangement but the secured creditors still have the benefit of a classification and so are not rolled into the same class as unsecured creditors. Under a Scheme of Arrangement creditors and members who possess similar interests are grouped together in classes. Of each class at least 75% in value and more than 50% in number of those who vote must approve the Scheme. The court must also approve the scheme, and confirm that it is fair and reasonable.

Under a company voluntary arrangement 75% in value of unsecured creditors who vote are required to approve the arrangement which is then binding on all unsecured creditors.

In an administration the proposals are approved if a majority (in value) of those voting vote in favour. The proposals are then binding on all creditors.

2.10.1 Should a 'cross-class cram down' (i.e. the confirmation of the restructuring plan supported by some classes of creditors in spite of the objections of some other classes of creditors), be possible?

☐ a) Yes, in all cases
☒ b) Yes, but subject to certain conditions
☐ c) No
☐ d) Other
☐ e) No opinion

Please specify

In appropriate cases, this can prove to be a valuable tool.

Please explain

There is a need to have an ability to avoid 'hold-out' creditors blocking restructurings that the vast majority of creditors support and which would be beneficial to creditors as a whole. So, with the appropriate court supervision, and creditors being no worse off than in a liquidation/ or other likely alternative, cram down tools can be very important.

2.11 Should financing necessary for the implementation of a restructuring plan/ensuring current operations be protected if the restructuring subsequently fails and insolvency proceedings are opened?

☐ a) Yes, always
☐ b) Yes, but only if agreed in the restructuring plan and confirmed by the court
☐ c) No, never
☒ d) Other
☐ e) No opinion

Please specify

There should be appropriate incentives and safeguards to encourage the provision of financing to enable restructuring to take place. It is considered, however, that new funding should not be protected at the expense of existing creditors of a failed business.

2.12 Should directors of companies be incentivised to take appropriate preventive measures if companies are in distress but not yet insolvent, for example by being able to avoid related liability?

☐ a) Yes
☐ b) No
☒ c) Other
☐ d) No opinion

Please explain

R3 believes that directors should be encouraged to act responsibly. Most incentives are provided by means of the threat of civil or criminal sanctions against directors who fail to take preventive measures in a timely fashion. The threat of criminal proceedings, in particular, whilst compelling, can have a negative and harmful effect on restructurings. Directors, faced with the threat of criminal proceedings, are more likely to take precipitate action - such as early filing for insolvency - which can and often does jeopardise the chances of successfully restructuring a business outside of formal insolvency proceedings (e.g. our members have seen examples of this in Germany where there is a mandatory 21 day filing period with criminal sanctions attached to failure). Similarly, even in jurisdictions where directors are permitted to formulate restructuring proposals rather than filing for insolvency, the threat of criminal proceedings can result in the hasty promulgation of restructuring plans that prove to be unrealistically optimistic and which then have to be revisited several times. Consequently, as with so many areas, a fine balance must be struck between imposing sanctions that are sufficiently compelling to encourage responsible behaviour, but not so onerous as to incline directors to focus on protecting themselves from the sanctions, rather than taking the best steps to rescue the financially distressed business. In this regard, we consider that the wrongful trading regime in the UK strikes a good balance.

2.13 Should Member States be encouraged to take specific action to help debtors in financial distress, such as setting up special funds or insurance systems covering the provision of cheap and accessible restructuring advice, possibly subject to certain conditions?

☐ a) Yes, for all debtors
☐ b) Yes, but only for SMEs
☐ c) Yes, but only for SMEs and individuals
☐ d) Yes, but only for individuals
☐ e) No
☒ f) Other actions
☐ g) No opinion

Please explain

Member States could be encouraged to consider measures to help debtors in financial distress. However, the extent to which funds and insurance schemes are established should be at the discretion of each Member States.

For example, R3 does not believe that a contribution scheme should be introduced as a minimum. Any insurance scheme typically subsidies the weak at the expense of the majority of well-run businesses.

There is also a real value of directors having ready access to training.

3. Second chance

The Competitiveness Council in May 2011[3] invited Member States to promote a second chance for entrepreneurs by limiting, where possible, the discharge period and enabling debt settlement for honest entrepreneurs once they are insolvent. An 'honest' failure is a case in which the business failure occurred through no obvious intentional fault of its owner or director, i.e. it was honest and above-board. This would be contrary to cases in which the bankruptcy was fraudulent, for example where the debtor transferred its assets outside the jurisdiction, made an advance payment to a single creditor, accumulated excessive private expenses, etc.

An important element to support an effective second chance regime is the 'time to discharge'. This is the time from when an entrepreneur enters into insolvency proceedings to when he/she can effectively restart an entrepreneurial activity. Currently, the discharge time varies significantly from country to country. In some countries, honest entrepreneurs in bankruptcy are automatically granted a discharge immediately once liquidation of the assets is finished. In others, bankrupted entrepreneurs have to apply for a discharge, while in some countries they cannot obtain discharge at all.

Furthermore, the procedures to release consumers from a 'debt trap' vary significantly between Member States. In some countries, there is no bankruptcy or debt settlement procedure for consumers. In others, a general insolvency regime with some changes applies to consumers.

[3] Council of the European Union, Competitiveness (Internal Market, Industry, Research and Space), Brussels, 30 and 31 May 2011. Press release available at: https://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/intm/122359.pdf.

3.1 Should honest debtors (entrepreneurs and consumers) who are over-indebted be offered the chance to restructuring their debt?

☒ a) Yes, entrepreneurs (individuals) as well as consumers
☐ b) Only entrepreneurs (individuals) for debts related to their professional activity
☐ c) Only consumers
☐ d) Neither entrepreneurs (individuals) nor consumers
☐ e) Other options
☐ f) No opinion

Please explain

R3 believes that an appropriate 'second chance' regime promotes entrepreneurial risk-taking and intervention that are key components of a healthy capital-based economy. Similarly, extending such a regime to consumers can be an important social measure, allowing 'honest' mistakes and poor behaviour to be overcome and the individual to be financially rehabilitated and able once again to participate fully in the economy.

In the UK, the opportunity to restructure debt is available to individuals (both entrepreneurs and consumers) by way of a number of statutory procedures – the Individual Voluntary Arrangement (IVA) procedure in England, Wales and Northern Ireland, and the Protected Trust Deed and Debt Arrangement Scheme procedures in Scotland.

3.1.1 To what extent do existing differences between the laws of Member States in the area of second chance affect the functioning of the Internal Market?

(For example, differences affect the Internal Market when creditors or investors and debtors are

located in different Member States and this has an impact on the recovery of debts, the legal certainty of transactions, the quantification of risks etc.)

☐ a) To a large extent
☐ b) To a considerable extent
☐ c) To some extent
☐ d) Not at all
☒ e) No opinion

3.2 Should over-indebted individuals have access to free or low cost debt advice?

☐ a) Yes, entrepreneurs (individuals) and consumers, possibly subject to certain conditions
☐ b) Only entrepreneurs (individuals) for debts related to their professional activity, possibly subject to certain conditions
☐ c) Only consumers, possibly subject to certain conditions
☐ d) Neither entrepreneurs (individuals) nor consumers
☒ e) Other options
☐ f) No opinion

Please explain what particular conditions, if any, should be attached to such access.

R3 believes that all over-indebted individuals should be able to access comprehensive debt advice to ensure that they are able to enter the most appropriate debt relief solution for their circumstances and so that their creditors can receive repayment of debts as far as possible.

Please explain

Access to comprehensive, high quality debt advice can become a necessity for any individual at any stage in their life. Seeking professional debt advice is often the best way for indebted individuals to begin to deal with their debt problems. In the UK, free and expert advice is widely available – the vast majority of insolvency practitioners will offer an hour's worth of professional advice for free, while many debt advice agencies and charities employ trained advisers to provide debt advice. Complex cases may, however, require more work and greater expertise. It would therefore be unreasonable to expect such advice to be low cost or free beyond an initial exploratory meeting.

3.3 Should a full discharge of debts, possibly subject to certain conditions, be offered to all over-indebted individuals provided they are 'honest' debtors?

☐ a) Yes, to entrepreneurs (individuals) and consumers
☐ b) Only to entrepreneurs (individuals) for debts related to their professional activity
☐ c) Only to consumers
☐ d) Neither to entrepreneurs (individuals) nor to consumers
☒ e) Other options
☐ f) No opinion

Please explain

In the UK, a full discharge of debts in a bankruptcy or Scottish sequestration occurs, whether or not the bankrupt individual (consumer or entrepreneur) is adjudged to be 'honest'. Subject to any suspension of discharge provisions which are imposed on the individual, discharge from bankruptcy in England and Wales takes place automatically after 12 months, while in Scotland it takes place after a minimum of 12 months following an application for discharge, at which point all debts included within the process are no longer the responsibility of the individual (see answer to question 3.3.3 for debts which are excluded from bankruptcy) and the restrictions of bankruptcy are lifted.

3.3.1 Should the test of 'honesty' be made the same across all EU Member States?

☒ a) Yes
☐ b) No
☐ c) No opinion

What should be the substance of such test?
(please explain)

R3 agrees that there should be a distinction between honest and dishonest insolvents. The question is how to establish a mechanism for making this distinction in a cost-effective and objective manner.

We believe that any system which requires positive demonstration of honesty in every case is likely to be impracticable to implement. This is because of the difficulty of establishing a definition of 'honest', which by its nature is a subjective test, as well as the probable time, complexity and expense that such a system would involve.

The UK legislation does already make the distinction between honesty and dishonesty, but approaches the question by means of a negative test. Where it can be shown that an individual debtor or company director has been culpable, dishonest, or, in some cases, downright incompetent, the court may impose penalties on them and restrict their activities for a specified period of time. They may be made subject to a Bankruptcy Restrictions Order in England and Wales or Undertaking (for individuals who have been declared bankrupt/ sequestrated), which extends the restrictions of bankruptcy/ sequestration that the individual is subject to for between two and 15 years, or disqualified from acting as a director of a company for between two and 15 years. However, in the absence of such sanctions being imposed, people are free to continue to pursue business activities in the normal way. We believe that the UK's negative test for honesty is the preferable and most practical approach.

In the UK, there are statutory provisions setting out the behaviour(s) that constitute culpable conduct for both bankrupt/ sequestrated individuals and company directors, and there is a body of established case law resulting from court decisions.

3.3.2 What should be the maximum discharge period for honest debtors who cannot repay their debts (in other words, what should be the period after which such debtors would be completely discharged from debt, as long as they meet the obligations imposed by national laws)?

☐ a) 1 year or less
☐ b) 3 years
☐ c) 5 years
☐ d) More than 5 years
☒ e) Other
☐ f) No opinion

Please explain

We assume that this question relates only to personal insolvency. The concept of 'discharge' has no meaning in the context of corporate insolvency in the UK. As far as the period of disqualification for delinquent directors is concerned, in the UK, it is limited to a maximum of 15 years.

In the case of individual debtors, at present the discharge period from bankruptcy in the UK is 12 months, unless the discharge has been suspended in England and Wales due to the bankrupt individual's conduct during the term of their bankruptcy. In England and Wales, prior to 2004, the standard term of bankruptcy was three years, but it was reduced to one year with the aim of promoting entrepreneurship by allowing those who had accrued debts through

their business ventures to be swiftly rehabilitated and re-entered into the economic cycle.

In Scotland, the discharge period from sequestration was also reduced from three years to one year by the Bankruptcy and Diligence etc. (Scotland) Act 2007. There have since been further changes to the discharge period in Scotland as a result of the Bankruptcy and Debt Advice (Scotland) Act 2014, which changed the rules for discharge to require an application for discharge (which will usually be granted routinely) after a minimum of 12 months have passed from the date of sequestration . However, in minimum asset cases, where there is a generally simplified procedure, discharge can take place earlier, after six months.

However, given that the vast majority of bankruptcies in the past 10 years have been domestic consumers rather than entrepreneurs in need of swift rehabilitation, it is difficult to see how a 12 month term of bankruptcy can still be justified, and R3 has suggested elsewhere that the standard discharge period should revert to three years, to help redress the balance between bankrupt individuals and their creditors. This should be capable of extension to a maximum of 15 years for the most culpable.

We would support a maximum discharge period of three years, but it would need to be possible to extend the period where the debtor's conduct, either before or during the period of the bankruptcy, warrants it (as outlined in R3's Personal Insolvency Landscape paper: https://www.r3.org.uk/media/documents/policy/policy_papers/personal_insolvency/R3_Personal_Insolvency_Landscape_Jan_2014.pdf).

We believe that it is also important to distinguish between the period of discharge (i.e. the period of time after which the debtor is released from his/her bankruptcy debts and ceases to be subject to the restrictions of bankruptcy) and the period of time which it takes for the trustee in bankruptcy to deal with the assets within the bankrupt individual's estate. The latter period of time is unrelated to the period of discharge and may be a longer or shorter period of time. It is not appropriate or desirable to place a statutory time limit on the administration of insolvent estates; the circumstances of each case may make it impossible to comply with a specified time limit without applying for an extension of time and this would act against the interests of creditors by impeding asset realisations or the pursuit of litigation, or incurring the cost of seeking an extension.

It is also worth noting that, in Scotland, following the changes implemented by the 2014 Act referred to above, an individual who is able to contribute towards their debts will be required to contribute from their income for four years, notwithstanding their discharge, and any assets acquired after they have been discharged can still form part of their estate for four years. Similarly, in England and Wales, a bankrupt individual can be made subject to an Income Payments Agreement or Order before their discharge from bankruptcy, which will require them to make payments from their income for a period of three years, even after their discharge has taken place.

3.3.3. In the case of debtors that are insolvent, should a full discharge be conditional on the repayment of a certain amount of debt?

☐ a) Yes
☒ b) No
☐ c) Other options
☐ d) No opinion

Please specify what that amount should be

R3 believes that it is undesirable to make a full discharge conditional upon the repayment of a certain amount of debt. In our view, it is more important to ensure that the personal insolvency framework provides a range of insolvency procedures to suit the diverse circumstances of individual debtors. In some instances, debtors will have disposable income and/or assets which would enable them to repay their creditors in full or in part, given the most appropriate formal process to do so. In other cases, the debtor will simply not have any available income or assets to repay any of their debts. As such, it would be unrealistic, and potentially detrimental to individuals, to impose a blanket requirement for all debtors to only receive a full discharge once they have repaid a specified amount of debt.

Please explain

3.3.3 Which special types of debt should be excluded from discharge?

(choose all that apply)

☒ a) Tort claims
☒ b) Fines
☒ c) Child support
☐ d) Tax and other public liabilities
☒ e) Other types of debt
☐ f) No opinion

Please specify

In the UK, the main types of debt which are excluded from discharge in a bankruptcy or Debt Relief Order are as follows:

- post-bankruptcy debts where the debt or liability did not arise from an obligation incurred prior to the bankruptcy;
- secured loans and other secured debts, such as mortgages and charging orders on properties;
- court fines, compensation orders and victim surcharges from a magistrates' court or the Crown Court;
- any payments that the debtor has been ordered to make under a confiscation order, for example, for criminal offences;
- any debts incurred due to fraud;
- maintenance payments and child support payments ordered as part of family proceedings;
- student loans;
- damages that the debtor owes in respect of the death or personal injury of another person;
- social fund loans;
- some benefits and tax credit overpayments; and
- foreign taxes, except where the EC Regulation on Insolvency Proceedings applies.

The types of debt which are excluded from discharge in a Scottish sequestration or protected trust deed are similar although not identical.

3.4 If it is decided that the discharge of debts should be offered to all individuals, whether entrepreneurs or consumers, should the conditions for the discharge be the same?

☒ a) Yes

☐ b) No, the conditions applicable to entrepreneurs should be stricter than those applicable to consumers

☐ c) No, the conditions applicable to consumers should be stricter than those applicable to entrepreneurs

☐ d) Other options

☐ e) No opinion

3.4.1. Please explain

We see no reason to make a distinction.

4. Increasing the efficiency and effectiveness of the recovery of debts

The efficient and effective recovery of debts depends on many factors. The recovery rates of debts may depend on:

- the effectiveness of insolvency proceedings;
- their length;
- the specialisation of the people dealing with them;
- the qualification of the directors of distressed companies.

The recovery rate of debts also has an impact on high levels of non-performing loans in the EU.

The laws of Member States differ significantly on the priority of claims in insolvency. This has an impact on how insolvency proceedings are run and how debts are recovered. Laws also differ on possibilities for avoiding contracts detrimental to companies and creditors. Differences concern conditions under which a detrimental act can be avoided (avoidance actions) and the period within which such acts can be challenged.

Also, the laws of Member States have different rules on insolvency practitioners themselves, namely the qualifications and eligibility for their appointment and also their licensing, regulation, supervision, professional ethics and conduct. The questions related to insolvency practitioners concern any mediators or supervisors engaged in the insolvency process. Moreover, in most Member States, insolvency proceedings are administered by a judicial authority, often through commercial courts, courts of general jurisdiction or through specialised insolvency courts. Sometimes judges have specialised knowledge and responsibility for insolvency matters, while in other cases insolvency matters are just one of a number of wider judicial responsibilities of the courts.

There is currently no rule at EU level which ensures that directors who have been disqualified in one Member State, e.g. because of fraudulent behaviour, are prevented from setting up a new company or from being appointed as director of a company in another Member State. This means that disqualified directors can easily move from one Member State to another and manage companies in the EU even if they were not allowed to, at least for a certain period of time, in the Member State that disqualified them. The European Commission supports cross-country access to information about whether directors have been disqualified. The Commission will establish a decentralised system to interconnect insolvency registers. Under this system, Member States are invited, in accordance with Article 24(3) of Regulation (EU) 848/2015, to include in their national insolvency registers documents or additional information such as insolvency-related disqualifications of directors.

GENERAL QUESTIONS

4.1 To what extent do existing differences between the laws of the Member States in the areas mentioned below affect the functioning of the Internal Market?

(For example, differences affect the Internal Market when creditors or investors and debtors are located in different Member States and this has an impact on the recovery of debts, the legal certainty of transactions, the quantification of risks etc.)

	To a large extent	To a considerable extent	To some extent	Not at all	No opinion
a) Minimum standards on the ranking of claims in formal insolvency proceedings	☐	☐	☐	☐	☒
b) Minimum standards on avoidance actions	☐	☐	☐	☐	☒
c) Minimum standards applicable to insolvency practitioners/mediators/supervisors	☐	☐	☐	☐	☒
d) Measures providing for a specialisation of courts or judges	☐	☐	☐	☐	☒
e) Measures to shorten the length of insolvency proceedings	☐	☐	☐	☐	☒
f) Measures to prevent disqualified directors from starting new companies in another Member State	☐	☐	☐	☐	☒
g) Other measures	☐	☐	☐	☐	☒

Please explain

Detailed and extensive data would be required to assess the impact of differences in the laws of Member States on the functioning of the internal market. However the suggested answers appear to anticipate that respondents will provide an opinion. We question the value of opinions provided without evidential support, but in any event, as a trade body representing a large number of insolvency practitioners, it would be inappropriate for us to provide such an opinion.

4.2 Which measures would contribute to increasing the recovery rates of debts?
(choose all that apply)

☐ a) Minimum standards on the ranking of claims in formal insolvency proceedings
☐ b) Minimum standards on avoidance actions
☒ c) Minimum standards applicable to insolvency practitioners/mediators/supervisors
☒ d) Measures providing for a specialisation of courts or judges
☐ e) Measures to shorten the length of insolvency proceedings
☐ f) Measures to prevent disqualified directors from starting new companies in another Member State
☒ g) Other measures

☐ h) No opinion

Please explain

The UK's insolvency regime is recognised across the world for its efficiency, emphasis on business rescue and high levels of returns to creditors. In the European Commission's September 2015 report 'The Economic Impact of Rescue and Recovery Frameworks in the EU', the UK was ranked top of the Commission's rankings for overall efficiency of the EU pre-insolvency frameworks.

The UK is ranked 13th at 'resolving insolvency' (according to the World Bank) behind six EU Member States (Finland, Germany, Denmark, Portugal, Belgium and the Netherlands. It is also behind the US). However, the World Bank data also shows that the UK returns more money faster and cheaper than Germany, the US and Portugal. The UK also returns more money to creditors than Denmark and is quicker than the Netherlands. The different insolvency indicators show that there are different ways in which an insolvency regime can be judged – the cost of recovery, speed and amount returned to creditors are three important factors when considering 'recovery rates'.

R3 believes that there are multiple factors which contribute to an effective insolvency regime which are also mentioned in our response to question 2.2. This includes:

- The cost of restructuring
- The availability/ range of recognised informal measures
- The court system in terms speed, cost and 'commerciality'
- The ability of experienced, qualified and regulated insolvency processionals to lead the restructure/ business rescue
- The broader business environment and regulatory regime.

SPECIFIC QUESTIONS

4.3 Which claims should have priority in insolvency proceedings (i.e. be satisfied first from the proceeds of the insolvent estate)? (choose all that apply)

☒ a) Secured creditors should be satisfied in principle before all other creditors
☐ b) Secured creditors should be satisfied before unsecured creditors but not before privileged creditors such as employees and/or tax and social security authorities
☐ c) Tort claims should have a higher priority than other unsecured claims
☐ d) Other ranking of priorities
☐ e) No opinion

Please explain

The entire purpose of security is to provide a higher ranking in the event of the debtor's insolvency. Other than that R3 does not generally believe that the special pleading of specific interest groups (including tax authorities) and with the possible exception of employment claims, should be rewarded with priority ranking.

It is also important to ensure that insolvency office holders' costs and expenses are provided for in a manner which provides certainty for them to accept an appointment.

4.4 What minimum standards should be harmonised for 'avoidance actions'? (choose all that apply)

☒ a) Rules on the types of transactions which could be avoided
☒ b) Rules on 'suspect periods' (periods of time before insolvency when a transaction

is presumed to be detrimental to creditors)

☒ c) Other rules

☐ d) No opinion

Please explain

Minimum standards for avoidance actions could usefully be harmonised so long as the standards are set at a satisfactory level. This would restrict the ability of parties determined to undertake dubious transactions from forum shopping. In addition to harmonisation of the types of transactions which could be avoided and the look back provisions, it is considered that the burden of proof and outcomes of such action could also be standardised.

4.5 In what areas would minimum standards for insolvency practitioners help to increase the efficiency and effectiveness of insolvency proceedings? (choose all that apply)

☒ a) Licensing and registration requirements
☐ b) Personal liability
☒ c) Subscribing to a professional liability insurance scheme
☒ d) Qualifications and training
☒ e) Code of ethics
☐ f) Other
☐ g) No standards should be harmonised
☐ h) No opinion

Please specify

4.6 Which additional minimum standards, if any, should be imposed on insolvency practitioners specifically dealing with cross-border cases? (choose all that apply)

☐ a) Relevant foreign language knowledge
☐ b) Sufficient human and financial resources in the insolvency practitioner's office
☐ c) Pre-defined period of experience
☐ d) Others
☒ e) No additional standards are needed compared with those relevant for domestic insolvency cases
☐ f) No opinion

Please specify

R3 does not think it necessary to introduce additional minimum standards for insolvency practitioners dealing with cross-border cases in the areas outlined above. The key to ensuring that minimum standards are fulfilled is to ensure that insolvency practitioners are appropriately trained and regulated. It is through regulation, whether by the courts or an independent external body, that insolvency practitioners will be 'tested' to ensure that they meet minimum standards. For example, regulators can examine if an insolvency practitioner working on a cross-border case has 'sufficient human and financial resource' to get the job done. This can be examined on a case by cases basis rather than imposing a minimum standard.

4.7 What are the causes for the excessive length of insolvency proceedings? (choose all that apply)

☐ a) Judicial activities concerning the supervision or administration of insolvency proceedings
☐ b) Delays in the liquidation of the debtor's asset
☐ c) The time taken to obtain final decisions on cases concerning the rights and duties of the debtor (e.g. claims, debts, disputed property in goods)
☐ d) A lack of promptness in exercising creditors' rights
☐ e) Lack of electronic means of communication between the creditors and relevant national authorities, such as for the purposes of filing of claims, distance voting etc.

☒ f) Other

☐ g) No opinion

Please explain

R3 would like to challenge an assumption implicit in the question that insolvency proceedings are excessive in length. This is not the experience of insolvency cases in the UK, which according to the World Bank, are on average one year in duration. Indeed, there may be instances where a complex case could last a number of years but this is not inherently wrong as it will depend on the specifics of the case – a case may take many years but provide a significant return to creditors. A robust insolvency practitioner regulatory regime should be able to adequately deal with any instances of cases that take too long to be finalised, with action being taken against the insolvency practitioner where expected standards have not been met.

It is considered that additionally the following can have a negative effect on the duration of insolvency proceedings;

- Non-cooperation of directors and members
- Delays caused by court processes where court action has been taken to recover assets/further investigations
- Completion of proper investigations into a company's affairs and dealings
- The existence of subsidiaries or holding of assets in other jurisdictions where lack of treaties or language barriers may hinder the process
- Not having the power to take action to recover assets in other jurisdictions
- Inter-company disputes in groups, which can be exacerbated where there are cross-border dealings. This is often because the office-holders in the respective entities are duty-bound to maximise the recoveries for their own estate, which can lead to dispute rather than concession on contentious matters.

4.8 Would a target maximum duration of insolvency proceedings — either at first instance or including appeals — be appropriate?

☐ a) Yes

☐ b) Yes, but only for SMEs

☒ c) No

☐ d) Other possibilities

☐ e) No opinion

Please explain

There should not be a target maximum duration of insolvency proceedings as every case is different. As discussed in our response to question 4.7, a case which might take a number of years to reach its conclusion is not inherently wrong. A significant amount of damage may be caused by the imposition of a time limit.

Currently there are some restrictions in place with regard to UK insolvencies. However there is flexibility to extend the duration of certain procedures in set circumstances. For example, administrations will automatically come to an end after 12 months, however creditors and the court have the power to extend the duration by set periods if required. Therefore, R3 believes that whilst absolute time limits are unhelpful, Member States should, when formulating regimes, strive to find the correct balance between imposing deadlines to focus attention with the flexibility for the time limit to be extended to ensure that matters are given proper attention and that matters are brought to an efficient and tidy conclusion.

4.9 What incentives could be put in place to reduce the length of insolvency proceedings? (please explain)

No incentives should be introduced to reduce the length of insolvency proceedings as outlined in our response to questions 4.7 and 4.8. However it is important to ensure that the courts are adequately resourced to support the relevant regime so that they can deal with cases in an efficient manner.

4.10 When disqualification orders for directors are issued in one Member State (i.e. the 'home State'), they should:

☒ a) be made available for information purposes via the interconnected insolvency registers so that other Member States are informed
☐ b) automatically prevent disqualified directors from managing companies in other Member States
☐ c) not automatically prevent disqualified directors from managing companies in other Member States, but make them subject to intermediary steps (e.g. a court order)
☐ d) Other options
☐ e) No opinion

Please explain

Legislation has been recently introduced in the UK on this matter through the Small Business Enterprise and Employment Act (SBEEA) 2015. Those convicted of relevant offences in foreign jurisdictions can now face a parallel UK disqualification by court order on the application of the Secretary of State.

The sharing of information via interconnected insolvency registers would help ensure either cross border enforcement of a disqualification if that is provided for, or flag up a warning to enquirers in the absence a disqualification itself being effective across borders.

4.11 Directors disqualified in one Member State (home State) should be prevented from managing companies in other Member States (host States): (choose all that apply)

☐ a) Always
☐ b) Only for the duration applicable to equivalent disqualification orders in the host State
☐ c) Only in the same or similar sector of activity
☐ d) Never
☒ e) Other options
☐ f) No opinion

Please explain

The specific circumstances of each case should be taken into account before preventing a director from managing a company in another Member State.

4.12 Which measures would contribute to reducing the problem of non-performing loans? (choose all that apply)

☒ a) Measures to improve the effectiveness of insolvency proceedings
☒ b) Measures enabling the rescue of viable businesses
☒ c) Measures to provide user-friendly information about national insolvency frameworks
☒ d) Measures to ensure a discharge of debts of entrepreneurs (individuals)
☒ e) Measures to ensure a discharge of debts of consumers
☒ f) Other measures related to insolvency

☒ g) Measures unrelated to insolvency (e.g. enforcement of contracts)

☐ h) No opinion

Please explain

There are many more factors that would contribute to reducing the problem of non-performing loans, not just those related to insolvency e.g. lending practices.

5. Additional comments

Are there any additional comments you wish to make on the subject covered by this consultation?

The Commission's consultation deals primarily with rules and procedural matters. However, the success of any formal regime for insolvency and restructuring depends on a number of other factors. There are therefore many areas where harmonisation of insolvency law would not be possible without harmonising some of these underlying areas of law.

First, insolvency law does not exist in isolation, but rests on a body of other laws which govern fundamental issues such as security rights, contract law, company law, the law of trusts, tax and employment law, and a whole host of other relationships. These other areas of law also affect the ability to restructure outside of a formal insolvency process.

Secondly, the effectiveness of a legislative regime depends not only on the rules themselves, but also on the quality of the courts which enforce them, the ability of the practitioners who implement them, and the general prevailing commercial and business culture. These vary considerably across the various EU member states.

Thirdly, the emphasis on rescue should not obscure the need to recognise that in an open market economy, enterprises that destroy value should be allowed to fail and their resources redeployed for more productive use elsewhere (rather than risk distorting free market competition). Rescue cannot be viewed in isolation from insolvency.

You can also send a separate written contribution by uploading your document here: