Association of Business Recovery Professionals

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31 October 2014

Dear Lord Smith

"Have your say"

A recent meeting of the R3, Association of Business Recovery Professionals' Scottish Technical Committee (STC) agreed to write to you and the Smith Commission to express concerns and make some suggestions in respect of Scottish Corporate Insolvency.

Below is background information on the STC and a brief summary of our views further details of which are contained in the attached submission.

1. The Association's Scottish Technical Committee (STC) has provided technical support and advice on insolvency matters of particular Scottish interest to the UK and Scottish Governments. The STC is comprised of IPs, solicitors, advocates and leading academics. In accordance with the published guidelines for submissions, the STC welcomes the opportunity to have its say on the proposed devolution of further powers to the Scottish Parliament.

2. STC believes that an appropriate insolvency framework should underpin the principles of a stronger Scottish economy through efficient processes, job preservation and better regulation. We recognise that the terms of reference for the Smith Commission is to produce recommendations for further devolution of powers to the Scottish Parliament, however, in order to deliver legislation which is 'fit for purpose' as part of a devolved administration, there are two key points we would like to make:

    a. To better serve the public interest and to ensure creditors and the Scottish economy are no longer placed at a disadvantage, we suggest that the Scottish Parliament reconsider the current devolved powers in respect of corporate insolvency and review the recommendations made by the Calman Commission. Different primary legislation between Scotland and England & Wales infers that the rules will differ in the two jurisdictions. What we have been calling for over a number of years is for the Scottish Corporate insolvency rules to be modernised and that they should not continually lag behind those of England & Wales.

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b. We suggest that there is no further devolution of insolvency powers to the Scottish Parliament for the reasons given below and in the attached submission. Unified approach to corporate insolvency under the auspices of Westminster makes legal and practical sense.

3. Of increasing importance in the modern world is the achievement of clarity and consistency of approach by the European Community in particular and across the globe in general. Scotland can facilitate the process by ensuring a level playing field exists in the UK.

Please find attached the submission from STC. We would be happy to provide any further information should it be required.

Yours sincerely

Eileen Blackburn CA
Chair
R3 Scottish Technical Committee

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THE ASSOCIATION OF BUSINESS RECOVERY PROFESSIONALS' (R3) SCOTTISH TECHNICAL COMMITTEE (STC)

"HAVE YOUR SAY"

SUBMISSION BY R3 SCOTTISH TECHNICAL COMMITTEE

TO THE SMITH COMMISSION

31 October 2014

"Have your say"

Introduction

1. R3, the Association of Business Recovery Professionals, is the leading professional association for insolvency, business recovery and turnaround specialists in the UK. It promotes best practice for professionals working with financially troubled individuals and businesses. R3 has UK-wide representation and debates key issues facing the profession. A significant number of insolvency practitioners (IPs) and legal professionals who are insolvency specialists and operating in Scotland are members.

Background to Corporate Insolvency in Scotland

2. Under the Scotland Act 1998 whereas Personal Insolvency is almost wholly devolved to the Scottish Parliament powers relating to Corporate Insolvency is split between Westminster and Holyrood. Corporate insolvency is in the main a reserved power, although the process of winding up and matters relating to floating charges and receivers are excepted from that general reservation. The result of this distinction is that although there is consistency North and South of the border in Administrations and Company Voluntary Arrangements there is no such consistency in Liquidations and Receiverships. This lack of a level playing field has led to difficulty and uncertainty in practice and additional cost to creditors and the Scottish economy.

3. Representation was made to the Calman Commission and to the Scottish Parliament by R3 STC, the Institute of Chartered Accountants of Scotland ("ICAS") and the Law Society of Scotland ("LSS") for corporate insolvency to be re-reserved to Westminster. Although the Calman Commission recommended the re-reservation, the provisions were rejected by the Scottish Parliament and removed from the draft Scotland Bill 2012.

4. Undertakings were made at the time that the issues raised would be addressed and steps taken to resolve matters. Attached is correspondence from Fergus Ewing, MSP, Minister for Energy, Enterprise and Tourism and John Swinney, MSP then Cabinet Secretary for Finance, Employment and Sustainable Growth.

5. The Scottish Government's view is that as a devolved Government it is best placed in partnership with its UK counterparts to serve the interests of Scottish businesses. We contend that in the area of corporate insolvency this can be better achieved by the re-reservation of corporate insolvency to Westminster. This would allow the UK Insolvency Service to be wholly responsible for drafting insolvency legislation ensuring consistency and timely responses to be made, drawing upon Scottish legal expertise to deal with the interaction of reserved regulation with Scots Law. Adopting this approach will yield a cost benefit to the Scottish Government through sharing existing experience and expertise in the complex area of insolvency law which the Insolvency Service possesses.

6. Changes introduced to Corporate Insolvency legislation in E&W have not been reflected timeously in Scottish legislation which has led to further divergence in the processes. It has been demonstrated over the years that the Accountant in Bankruptcy (AiB) who has responsibility for corporate insolvency policy in Scotland lacks the necessary resource and qualified personnel to perform the role. IPs in Scotland have been at the disadvantage of having to seek direction from the Courts on a number of issues, or having to undergo procedure which is not necessary in England & Wales thereby incurring additional cost with the resultant reduction in return to creditors to the detriment of the Scottish economy.

Current situation

7. Responding to a letter dated 3 May 2012 from ICAS, R3 STC and the LSS, Fergus Ewing MSP in his response dated 29 May 2012 stated that *"the Scottish Government have committed to set up a new team with specific responsibility for developing new corporate insolvency rules."* A working group which included stakeholders was appointed in November 2012 to consider the draft rules. However meetings were cancelled and insufficient time was given to the working group to review the draft rules in any depth before they were laid before the Scottish Parliament. Further, questions raised on key issues were not addressed.

8. Insolvency (Scotland) Amendment Rules 2014 which came into force on 30 May 2014 have addressed some recent issues. These Rules have introduced in Scotland similar provisions to those introduced in England and Wales four years earlier and which have allowed efficiencies to be made in insolvency processes through the use of technology. However, the amendments fail to provide for 'remote attendance' at meetings as is permitted in Administrations and Company Voluntary Arrangements. The Small Business, Enterprise and Employment Bill 2014 currently making its way through the UK Parliament contains more than 30 clauses related to the UK's insolvency framework. The Bill is expected to be passed and receive Royal Assent in spring 2015. Based upon past experience, due to the constraints of resource and expertise within the AiB we have reservations that the Scottish Government will deliver its commitment. There will be further divergence between legislation in the two jurisdictions at a cost to creditors in particular and the Scottish economy in general.

9. There is much inter-relation between insolvency law and other areas of law - Employment law, Health & Safety law, Environment law – to name a few. This has been apparent in recent high profile cases notable among them is the liquidation of Scottish Coal Company Limited . This case demonstrated a conflict between Scottish property law, which does not recognise the power of a Scottish liquidator of a Scottish registered company to abandon heritable property. This is a power which the liquidator of an English company can use by virtue of the statutory power of disclaimer of onerous property (including land) under ss.178-182 of the Insolvency Act 1986. The inability to disclaim onerous property can have a significant impact on creditors. The same issue arises for liquidators of English registered companies which own heritable property in Scotland.

10. Precisely what the effect of this is, is left uncertain. This inconsistency doesn't support an effective and economically beneficial UK regime of corporate insolvency particularly where corporates have interests in both England and Scotland. The Courts made it clear that it was not their role to resolve such conflicts, which leaves it to the legislature to do so.

11. Cross border issues arise in group administrations with multiple locations where some of the companies are incorporated in England & Wales and some are incorporated in Scotland. Where there are issues surrounding security and ranking/distribution, additional costs are incurred by IPs having to deal with two separate sets of rules which are not always compatible. Examples include the administration/liquidation of USC Limited and Gadget Shop Limited.

12. A further example of the additional costs in Scotland relates to the interest payable when creditors are paid in full. Interest is payable at 15% per annum. This historic rate has not been updated by the Scottish Government despite interest rates generally having reduced. In the group administration of Aberdeen manufacturing company R B Farquhar, after the sale of parts of the business all creditors were paid in full with interest and control passed back to the directors and shareholders. Interest of £133,975 was paid reducing the return to the shareholders as a result of this historic anomaly.

Financial advantages to re-reserving Corporate Insolvency to Westminster

13. As demonstrated above significant savings to creditors and the Scottish economy can be made by the re-reservation of corporate insolvency to Westminster. R3 STC considers that in the public interest UK corporate insolvency procedures ought to be the responsibility of one authority as this would provide for greater consistency. Corporate insolvency procedures should apply UK wide but take into account relevant differences in Scots Law.

14. Scotland requires the opportunity of being in a position whereby insolvency practitioners can rely upon legislation applicable in Scotland being on a par with and being updated in tandem with that applying in England & Wales. This will avoid the associated costs of divergent legislation.

Conclusion

15. A number of practices have become more harmonised across the UK as a result of decisions made by the highest courts in the land. A recent example relates to dealing with rent in administrations.

16. 'Forum shopping' issues within the UK may arise as they do across the European Community, if one regime is perceived to be more sympathetic than the other. A single unified process would make cross UK-border insolvency proceedings more efficient.

17. We submit there are areas where a single legislative body serves the best interests of all parties. Corporate insolvency legislation is one. Responsibility for this important and complex area of law should apply UK-wide.

18. The STC is firmly of the view that corporate insolvency should be re-unified. For the reasons laid out in this submission, in the absence of the introduction of a robust and adequately resourced system in Scotland to deliver a fully devolved corporate insolvency regime, the Committee's preference is that the responsibility falls to Westminster rather than the Scottish Parliament.

19. R3 STC shall continue to support and assist the Scottish Government where possible to ensure Scotland's insolvency regime serves the interest of the Scottish people and the Scottish economy.

Eileen Blackburn
Chair R3 Association of Business Recovery Professionals
Scottish Technical Committee