These notes refer to the Enterprise Act 2002 (c.40)
which received Royal Assent on 7 November 2002

ENTERPRISE ACT 2002

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Part 10: Insolvency

638. The provisions in the Act form part of the Government's ongoing strategy for dealing with the consequences of indebtedness and modernising the court's role in dealing with insolvency. In July 2001, the Government published its White Paper, 'Productivity and Enterprise: Insolvency – A Second Chance'. This built on an ongoing trend established by the Cork Report[1] to promote a culture of company rescue, and continued through the introduction of Insolvency Acts of 1986 and 2000. The White paper also built on The Insolvency Service consultation paper, 'Bankruptcy – A Fresh Start', published in April 2000.

639. The insolvency sections fall into four main sections: corporate insolvency; the abolition of Crown preference; individual insolvency (bankruptcy and individual voluntary arrangements) and the financial arrangements relating to the functions performed by the Secretary of State in relation to insolvency. These notes provide a general commentary on what the legislation seeks to achieve.

Companies etc.

640. Changes to the existing corporate insolvency regime focus on restricting the use of administrative receivership and streamlining administration. The White Paper *'Productivity and Enterprise: Insolvency – A Second Chance'* recognised that the administration procedure introduced by the Insolvency Act 1986 was seen as an important tool in providing companies in financial difficulties with a breathing space in which to put a rescue plan to creditors. However, it also recognised that the procedure could be improved.

641. The existing provisions contained in Part II of the Insolvency Act 1986 allow the court to make an administration order in respect of a company that is in financial difficulties. Broadly speaking, the effect of such an order is to afford the company protection from its creditors whilst attempts are made to save the company or achieve a better result for creditors than would be achieved in a winding-up. However, in practice, in many cases where a company gets into financial difficulties, this will lead to the appointment of an administrative receiver by those providing financial support for the company (typically the company's bank), since they usually will have taken a floating charge over all the company's assets. The holder of a floating charge has an effective veto over the appointment of an administrator. Such a person must be given notice of any application for an administration order, and if he or she appoints an administrative receiver, the court must dismiss the application unless the appointor of the administrative receiver consents to the making of an administration order (see section 9(2)(a) and section 9(3) Insolvency Act 1986).

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1 Insolvency Law & Practice: Report of the Review Committee (Cork Report) (1982) CMND 8558

642. An administrative receiver primarily owes duties to his or her appointor rather than the company's creditors as a whole (as to the duties owed by an administrative receiver see *Medforth v Blake* [1999] 2 BCLC 221). His or her primary function is to seek repayment of the debt owed to his or her appointor. An administrative receiver has no powers or duty to seek to put together a company rescue in the same way that an administrator has (an administrator, both under the old procedure and as amended by this Act, may put proposals to creditors for a Company Voluntary Arrangement (CVA) pursuant to Part I of the Insolvency Act 1986 or a scheme of arrangement pursuant to section 425 Companies Act 1985) (see sections 8(3) and 23 of the Insolvency Act 1986).

643. The sections will alter the above provisions in the following way. First, the appointment of administrative receivers will be restricted to certain exceptions (existing arrangements and capital markets) and the Act seeks to provide that administrators will in future be appointed in situations that would have been dealt with through administrative receivership. Second, the procedure has been amended to streamline the process both in the provisions of the Act and the Rules made under section 411 Insolvency Act 1986 that seek to give effect to the provisions of the Act. Perhaps the most obvious of the measures is the introduction of the non-court routes into administration. The procedure has been amended to provide a single purpose made up of a hierarchy of three objectives and expressly to provide that the administrator must carry out his or her functions in the interests of all the creditors. It was recognised that the administration procedure as it stood prior to commencement of the relevant parts of this Act was to a degree cumbersome.

644. Administration will continue to have many of the features of the current system. At Annex E there is a table of correspondence that will assist readers in identifying to what extent the provisions of the Insolvency Act 1986 are reflected in new Schedule B1.

Section 248 & Schedule 16: Replacement of Part II of Insolvency Act 1986

645. In order to provide for the streamlining of administration, section 248 replaces Part II of the Insolvency Act 1986 with a new Schedule B1 - as set out in Schedule 16 of this Act. This will be inserted after Schedule A1 to the Insolvency Act 1986. The paragraphs referred to below are paragraphs in Schedule B1.

General effect of Section 248 and Schedule 16: Nature of administration

646. In general terms, the effect of section 248 and Schedule 16 is as follows. Whether or not appointed by the court, an administrator is an officer of the court (as well as an agent of the company) and can only be appointed if qualified to act as an insolvency practitioner. An administrator may not be appointed if the company is already in administration. Generally, a company cannot go into administration if:

- a resolution for voluntary winding-up has been passed (see paragraph 8(1)(a)); or
- a winding-up order has been made (subject to an application by the liquidator or a floating charge holder) (see paragraph 8(1)(b)).

The purpose of administration

647. In order to clarify the purpose of administration and to place greater emphasis on company rescue, paragraph 3 replaces the existing four statutory purposes under section 8(3) Insolvency Act 1986. Under a single overarching purpose, which will apply to all cases of administration, the administrator will be required, where he or she thinks it is reasonably practicable, to carry out his or her functions with the objective of rescuing the company as a going concern (rescuing the company in this context is intended to mean the company and as much of its business as possible). Where that is not reasonably practicable or that objective would not provide the best result for the company's creditors as a whole, the administrator may pursue the second objective referred to below. A hypothetical example of a reasonably practicable rescue might be:

Company A is operating at a profit and has excellent products, a loyal customer base and a healthy order book. However, major investment in a new IT system, which is late and over-budget, has knocked the company off its business plan, its cash flow has suffered and it is unable to pay its debts. The company has been placed in administration and the administrator has had an offer for its business that would provide sufficient funds to pay the secured creditors and give 35p in the pound for unsecured creditors. However, the administrator has determined that the problems are short-term and they can be resolved and will not have any ongoing effect. The company's bankers have given their support to the administrator's plans to continue trading, the company's business is profitable and the administrator is confident that the company can be rescued by trading its way out of its current financial difficulties, and provide 65p in the pound return for unsecured creditors within 12 months. The administrator puts his or her proposal to the creditors.

648. An example of a case where a rescue would not be reasonably practicable is one where it is clear that the only viable options depend on the continuing support of the company's bankers. The administrator knows that this support will not be forthcoming and that there is no alternative means of financing the company. Whether a company rescue is a reasonably practicable option is a matter of commercial judgment and, on the basis of the case law in relation to similar decisions under the administration procedure prior to commencement of the relevant parts of this Act, it is envisaged that the courts will not seek to criticise the exercise of the administrator's commercial judgement, except in cases where bad faith can be established or the decision taken was one that no reasonable administrator would have taken. (As to the courts' attitude in relation to commercial matters, see for example, re: T&D Industries plc (in administration) [2000] 1 BCLC 471.)

649. Company rescue is most likely to involve the creditors agreeing to the company entering a CVA or a scheme of arrangement under section 425 of the Companies Act 1985. For the purpose of these sections, a proposal that would result in a 'shell' company remaining would not be considered a rescue.

650. If the administrator thinks that a company rescue is not reasonably practicable, or would not achieve the best result for the creditors as a whole, he or she will seek a better result for the creditors than on a winding-up. This might encompass situations where the company's individual businesses are broken up and sold to one or more buyers as going concerns in order to achieve this better result for creditors. Assets of the company may also be sold other than on a going concern basis. A hypothetical example might be:

Company B has good products, and a sound customer base. The company is making losses, its plant and machinery are outdated, and its overheads and debts have been rising for some time. The company has been placed in administration and the administrator has determined that there are no funds available to maintain its entire trading operation or invest in new machinery and it is therefore not reasonably practicable to rescue the company. The administrator has reviewed the company and determined that a sale of its businesses on a going concern basis would provide a better return than a break-up sale of its assets. The administrator markets the businesses and the best offer he or she receives would provide sufficient funds to pay the secured creditors and give 40p in the pound for unsecured creditors. The administrator reports to the creditors at a meeting and explains why it was not reasonably practicable to rescue the company.

651. The purpose specified in paragraph 3(1)(c) deals mainly with those cases where the company is not viable and has no business that can be sold as a going concern. All that can be done is to sell the company's remaining assets in order to make a distribution to one or more secured or preferential creditors. A hypothetical example might be:

Company C is a service company whose business and reputation were built around its excellent standards of customer service. But a number of key personnel have

recently left, the quality of the company's service and its reputation have suffered badly, customers have become dissatisfied and the company is no longer able to attract and retain business. It has been making losses for a number of months and is unable to pay its debts. The company is then placed in administration. The administrator reviews the company and concludes that its business is not viable and a sale is not possible. The administrator markets the company's assets and realises funds that are sufficient to make a part-payment to the secured creditors, and there are no funds available to pay unsecured creditors, except for those resulting from the operation of the ring-fence (see section 252). The administrator reports to the creditors and explains why it was not reasonably practicable to achieve either a company rescue or a better return for unsecured creditors.

652. An administrator must have regard to the interests of all creditors. In situations under paragraph 3(1)(c) where there are insufficient funds to pay the unsecured creditors, the administrator may only act if he or she does not unnecessarily harm their interests.

Appointment of administrator

653. Currently, administrators can only be appointed by court order (see section 8 Insolvency Act 1986, as originally enacted), and this route into administration has been retained. However, in order to speed up the process, paragraphs 14-34 set out provisions for the holders of floating charges and companies or their directors to appoint administrators without a court hearing. A diagram showing the out-of-court routes into administration is at Annex F.

General Restrictions

654. Paragraphs 6-9 set out instances where the appointment of an administrator is not allowed. These restrictions are included for practical reasons, e.g. the administrator must be qualified to act as an insolvency practitioner; the company must not already be in administration; and the company must not be in liquidation, although the latter restriction can be overruled in certain cases. Paragraph 9 refers to certain types of companies in relation to which the administration procedure applies in a somewhat modified form (see section 422 of the Insolvency Act 1986 and section 360 of the Financial Services and Markets Act 2000), hence the unmodified provisions of Schedule B1 do not apply.

Appointment by court

655. Paragraphs 10-13 set out the court route into administration. A company or its directors, or one or more creditors of a company (which could include a floating charge holder) can apply to court for an administration order (see paragraph 12). The court may only make an order if it is satisfied that the company is, or is likely to become, unable to pay its debts and that the order is reasonably likely to achieve an objective/the purpose of administration (see paragraph 11).

656. Paragraph 12(2) provides that, once an administration application has been made, the applicant must notify, amongst others, anyone who has appointed, or is entitled to appoint, either an administrative receiver or an administrator. The application for administration cannot be withdrawn without the permission of the court (see paragraph 12(3)).

657. On hearing an application for administration, the court may either make the order, dismiss the application or make any other order deemed appropriate, including treating the application as a winding-up petition or making an interim order (paragraph 13).

Appointment by the holder of a floating charge

658. Paragraphs 14-21 set out the out-of-court route into administration for the holders of floating charges. Floating charge holders will be able to appoint an administrator of their choosing, provided that:

- the floating charge on which the appointment relies is enforceable (see paragraph 16). In this context, enforceable means that the floating charge holder is entitled to call in their security;
- he or she has given notice to the holder of any floating charge which has priority over his or her own floating charge (see paragraph 15);
- the company is not in liquidation (see paragraph 8(1)(a) and (b)) nor has a provisional liquidator been appointed (see paragraph 17(a)); and
- neither an administrative receiver (see paragraph 17(b)) nor administrator is already in office (see paragraph 7).

659. Before the administrator takes office, the floating charge holder must file a notice of appointment with the court (see paragraph 18(1)) identifying the administrator and including a statement from the administrator consenting to the appointment (paragraph 18(3)). Attached to this will be a statutory declaration (paragraph 18(2)) by the floating charge holder stating that they have a qualifying floating charge - which may be one or more floating charges (together with other security) - over the whole or substantially the whole of the company's property and that this is or was enforceable on the date of the appointment (as to when the holder of a floating charge can appoint an administrator, see paragraph 14).

Appointment by company or directors

660. Paragraphs 22-34 set out the out-of-court entry route into administration for companies or the directors of companies. A company or its directors will only be able to appoint an administrator if:

- the company has not been in administration (instigated by the company or directors) (see paragraph 23(2)) nor subject to a moratorium in respect of a failed CVA under Schedule A1 to the Insolvency Act 1986 in the previous 12 months (see paragraph 24(3));
- the company is or is likely to become unable to pay its debts (see paragraph 27(2)(a));
- there is no outstanding winding-up petition or application for administration in respect of the company (see paragraph 25(a));
- the company is not in liquidation (see paragraph 8(1)(a) and (b)); and
- there is no administrator or administrative receiver in office (see paragraphs 6 and 25(c)).

661. The 'notice of intention to appoint' will also identify the proposed administrator (paragraph 26(3)). Once the 'notice of intention to appoint' is sent to the floating charge holder and filed at court, an interim moratorium commences (paragraph 44(2)).

662. During the notice period, a floating charge holder entitled to appoint an administrator may either agree to the proposed appointment or appoint their choice of administrator (paragraph 14). The company or directors must give floating charge holders at least five business days' notice in writing of their intention to appoint an administrator in this way (paragraph 26). The 'notice of intention to appoint' must also be filed with the court and accompanied by a statutory declaration, stating that the application meets the criteria set out in paragraph 27(2).

663. If the floating charge holder consents to the company's or directors' nominee or does not respond to the notice within five business days, the company/directors must make the appointment no more than ten business days after filing their 'notice of intention to appoint' (paragraph 28(2)). If the 'notice of appointment' is not filed within this period, the interim moratorium will cease to have effect and an administrator cannot be appointed. If there is no floating charge holder, the company/directors file the 'notice of appointment' at court together with a statutory declaration stating that the application meets the criteria set out in paragraph 27.

664. In both cases, this must be accompanied by a statement from the administrator consenting to act and stating that, in their opinion, the purpose of administration is reasonably likely to be achieved. Following this, the administrator is automatically appointed and takes office once the 'notice of appointment' and accompanying documents are filed at court. The company or directors must then notify the administrator of their appointment.

665. If, for whatever reason, the administrator's appointment is discovered to be invalid, the court may order the person who made the appointment to indemnify the administrator against liability (paragraph 34).

Administration application – special cases

666. Paragraph 35 provides for a floating charge holder to apply to court for an administration order without the need to demonstrate that a company is or is likely to become unable to pay its debts. However, the court must be satisfied that the applicant would be entitled to appoint under paragraph 14 (out-of-court appointment by the holder of the floating charge).

667. If there is a winding-up order in relation to the company that would prevent an out-of-court appointment, the floating charge holder can still apply for administration through the court. If an administration order is made, the court will then discharge the winding-up order (paragraph 37). The liquidator may present an application for administration (paragraph 38).

668. Paragraph 39 sets out that, if an administrative receiver (AR) is in office, the court must dismiss an application for administration unless:

- the appointee of the AR consents to the administration order; or
- the court thinks that the appointee's security may be set aside if an administration order were made.

Effect of administration

669. Paragraph 40 provides that, if the court makes an administration order, it shall dismiss any outstanding winding-up petitions that have not already been dealt with. However, if a company goes into administration as a result of a floating charge holder's appointment of an administrator, then any winding-up petition that has not been dealt with shall be suspended.

670. As already mentioned, paragraph 39 sets out that, if an AR is in office, the court must dismiss an application for administration unless the appointee of the AR consents to the administration order or the court thinks that the appointee's security may be set aside if an administration order were made. Paragraph 41 provides that, on the making of an administration order, an AR will vacate office, and a receiver will do so if requested by the administrator. The paragraph also secures the AR's and receiver's right to remuneration and any entitlement to an indemnity that they may have had, ahead of the claims of the security-holder who appointed them. However, the right to payment is subject to the moratorium under paragraph 43.

671. Paragraphs 42 and 43 provide that, once a company is in administration (i.e. an administration order has been made or the administrator has been appointed following the relevant filings by the directors, the company or the qualifying floating charge holder), the moratorium, which is a feature of administration, takes effect. Under paragraph 42 this means that a resolution cannot be passed, or an order made, to wind up the company except in certain circumstances (i.e. compulsory winding-up orders made on public interest petitions).

672. Paragraph 43 provides that no steps to enforce their rights can be taken by creditors without the consent of the administrator or the permission of the court.

673. Paragraph 44 provides that the moratorium referred to in paragraphs 42-43 will apply from the date that the application for the administration, or the notice of intention to appoint, is filed at court. The interim moratorium does not stop certain specified actions.

674. Paragraph 45 sets out that, while a company is in administration, every business document (e.g. invoices, orders for goods and services or business letters) issued by, or on behalf of, the company or the administrator must identify the administrator and state that the affairs, business and property of the company are being managed by him or her.

Process of Administration

675. A diagram showing the process of administration is at Annex G.

676. Paragraphs 46-48 provide that, in all cases, once the administrator has been appointed, he or she will send notice of the appointment to the company and its creditors as soon as is reasonably practicable and send notice to the Registrar of Companies within seven days of the appointment. He or she will also require, by notice, a representative of the company (e.g. officer of the company, employee) to provide a statement of the company's affairs within eleven days of the notice being received. This statement must be verified by a statement of truth and give particulars of the company's property, debts and liabilities, and the details of each creditor and their security.

Administrator's proposals and meeting of creditors

677. A diagram showing the conclusion of administration is at Annex H.

678. Paragraph 49 provides that, as soon as reasonably practicable, or, in any event, within 8 weeks of the administration commencing, the administrator is required to make a statement setting out proposals for achieving the purpose of administration, although this period can be extended with the permission of the court or with the consent of the creditors (see paragraphs 107 and 108). The administrator will send a copy of the proposals to the Registrar of Companies, the company's creditors and every member of the company (the last obligation may be fulfilled by publishing a notice). In cases where the business of the company had to be sold under a short timescale to maximise the economic value, the administrator will report these facts to the creditors in his or her proposal.

679. Each copy of the administrator's proposals sent to creditors must be accompanied by an invitation to an initial creditors' meeting, which must be held as soon as reasonably practicable, or, and in any event, within ten weeks of the administration commencing, and on a prescribed period of notice (paragraphs 50 and 51). The time periods may be extended with the permission of the court or the consent of creditors (see paragraphs 107 and 108). If the administrator does not consider that it is reasonably practicable to rescue the company and/or achieve a better result for the creditors than on a winding-up, his or her statement must state why (paragraph 49).

680. The administrator's proposals will take into account the purpose of administration, i.e.:

a) to rescue the company as a going concern (paragraph 3(1)(a));

b) if that is not reasonably practicable, or would not yield the best outcome for creditors, to achieve a better result for the company's creditors as a whole than

would have been achieved if the company were wound up (without first being in administration) (paragraph 3(1)(b));

c) if it is not reasonably practicable to achieve 3(1)(a) or 3(1)(b), to realise the company's property and make payments to preferential and secured creditors (paragraph 3(1)(c)).

681. The administrator will present a copy of his or her proposals at the initial creditors' meeting. If the administrator concludes that the company can be rescued as a going concern, he or she will put the proposal to the creditors and they will decide whether to accept an arrangement under which they will agree to accept less than full payment of their debts. This will usually be through a CVA or a scheme of arrangement under section 425 Companies Act 1985. The creditors could decide to reject the proposals or, with the consent of the administrator, amend them.

682. If company rescue is not deemed reasonably practicable, or would not yield the best outcome for creditors, the administrator will explain why this is so, and put the proposal to the creditors setting out how he or she plans to achieve a better result for the company's creditors as a whole (e.g. as a result of selling the company's businesses as going concerns to one or more buyers). The creditors will vote on whether to accept, modify or reject the proposal.

683. Where it is anticipated that there will be no funds available from the insolvent estate for unsecured creditors, outside those flowing from the abolition of Crown preference, the administrator will not be required to call a meeting of the creditors. This will also be the case where the administrator thinks there are funds to pay all creditors in full or that the first two objectives cannot be achieved. However, within the prescribed period, such a meeting may be requisitioned by creditors whose debts amount to at least 10% of the total debts of the company (paragraph 52).

684. An administrator's statement of proposals may not include any proposal that affects the right of a secured creditor to enforce his or her security without his or her consent. In addition, the statement of proposals may not include any action that would result in a preferential debt being paid otherwise than in a priority to a non-preferential debt (paragraph 73).

685. A creditors' meeting may only modify the administrator's proposals with his or her consent (paragraph 53). The administrator cannot subsequently make any substantial revisions to the proposals without first obtaining the agreement of the creditors (paragraph 54).

686. After the conclusion of the initial creditors' meeting (and any subsequent meeting), the administrator will report any decision taken to the court and the registrar of companies. If the creditors fail to approve the proposals, the court may provide that the administrator's appointment shall cease to have effect, adjourn the hearing conditionally or unconditionally, make an interim order, make an order on a suspended petition for winding up, or any other order deemed appropriate (paragraph 55). Paragraph 57 makes provision for the establishment of a creditors' committee.

687. Anything that is required to be done at or by a creditors' meeting may be done by correspondence, including communicating electronically and by telephone or fax (paragraphs 58 and 111).

Functions of the administrator

688. Paragraph 59 provides that the administrator may do anything necessary or expedient for the management of the affairs, business and property of the company. Schedule 1 to the Insolvency Act 1986 sets out the powers of the administrator.

689. Paragraph 61 provides that the administrator may remove or appoint a company director.

690. An administrator may make a distribution to secured creditors and preferential creditors without permission of the court (paragraph 65). He or she may make distributions to unsecured creditors with the permission of the court. The administrator can make a payment if he or she thinks that the payment is likely to assist in achieving the purpose of administration or in accordance with paragraph 13 of Schedule 1 to the Insolvency Act 1986 (paragraph 66). On appointment, an administrator is required to take on custody or control of all the property to which he or she thinks the company is entitled (paragraph 67).

691. Paragraph 70 provides that the administrator may dispose of property, subject to a floating charge (as created), as if the property were unencumbered, without the consent of the floating charge holder. However, the floating charge holder has first call on the proceeds of sale.

692. Paragraph 71 provides that the court may give the administrator the power to override the rights of the holder of a fixed security over the company's property and the power to dispose of the property in question as if it were owned by the company. However, the holder of the fixed security has first call on the proceeds of sale.

693. Paragraph 72 provides that the court may give the administrator the power to sell property subject to a hire-purchase agreement as if the property in question were owned by the company. However, the hire-purchase creditor has first call on the proceeds of sale.

Challenge to the administrator's conduct of the company

694. Paragraph 74 provides that any creditor or member of a company in administration may apply to the court, firstly, if he or she believes that the administrator has acted, or proposes to act, in a way that could unfairly harm his or her interests. Secondly, if he or she believes that the administrator is not performing his or her functions as quickly and efficiently as is reasonably practicable. The use of the expression "reasonably practicable" conveys the idea that one administration may be very different from another, where it may be practicable to act within a short time in the administration of a simple, small company, that may be entirely impracticable in the case of a large complicated case. Furthermore the courts would be unlikely to entertain claims under this provision relating to trivial delays or that are frivolous or unavoidable or cause no harm.

695. The court may grant relief, adjourn the hearing conditionally or unconditionally or make an interim or other order deemed appropriate. However, an order may not be made if it would impede or prevent the implementation of an approved voluntary arrangement or an arrangement sanctioned under section 425 Companies Act 1985, or proposals under paragraphs 53-54, where the challenge is made more than 28 days after the approval of those proposals.

Misfeasance

696. An interested party may apply to the court if he or she considers that the administrator has misapplied or retained the company's property, has become accountable for property, has committed a breach of a fiduciary, or other duty in relation to the company, or has been guilty of misfeasance. The court may order the administrator to repay, restore or account for the property, pay interest, or contribute by way of compensation to the company's property for breach of duty or misfeasance (paragraph 75).

Ending administration

697. The administrator will complete the administration as soon as reasonably practicable, or, in any event, within twelve months of the date the administration commenced. However, this term may be extended for an additional period of up to six months with the consent of creditors. Alternatively, the administrator can apply to court for an

extension for as long as deemed necessary by the courts (paragraph 76 and 78). An extension may not be made not be made once the administrators term of office has ended (paragraph 77).

698. The administrator is required to apply to the court to end the appointment if he or she thinks that the purpose of administration cannot be achieved, that the company should not have entered into administration or if required to do so by a creditors' meeting (paragraph 79).

699. If the administrator thinks that the purpose of administration has been sufficiently achieved he or she will file notice with the court and the Registrar of Companies and send copies to all the company's creditors. The administrator's appointment will end when the notice is filed (paragraph 80). Paragraph 81 makes provision for a creditor to apply to the court to have an administration stopped if he or she considers that the appointment was made under an improper motive.

700. Paragraph 83 allows the administrator to end the administration and convert the proceedings into a voluntary winding-up. This will occur if the preferential and secured creditors have been paid all they are likely to receive (or such has been set aside for them), and there is money available for the unsecured creditors. The administrator will send a notice to the Registrar of Companies and, as soon as is reasonably practicable, file a copy with the court and send a copy to each of the company's creditors. Once the Registrar of Companies has registered the notice, the administrator's appointment ends, the company proceeds to undergo a creditors' voluntary winding-up and the administrator becomes the liquidator of the company, unless the creditors have nominated an alternative liquidator.

Dissolution

701. Paragraph 84 provides that the administrator may take steps to dissolve the company where he or she finds that the company has no further assets to make a distribution to creditors. In which case he or she may send a notice to the Registrar of Companies and send a copy to the court and to each of the creditors. The company is considered dissolved after three months of the registration of the notice. However, it will be open to the court, on the application of the administrator or any other interested person, to defer the dissolution of the company; any such order should be filed with the Registrar of Companies.

Replacing administrator

702. Paragraphs 87-99 provide for the removal or replacement of the administrator under the different routes into administration and provide for release and priority of the administrator's debts and liabilities.

General provisions

703. Paragraphs 100 to 111 make general provisions relating to the appointment of joint and concurrent administrators (paragraph 100 to 103), matters of penalties (paragraph 106), time-limits (paragraph 107 to 110) and interpretation (paragraph (111).

704. Paragraphs 115 to 119 make provision for various issues of relevance to administration in Scotland, in particular, the interpretation of the expressions "filing in court" and "charge", the application of the provisions concerning the disposal of property subject to security and hire purchase agreements, and they provide an express order of priority.

705. Schedule 17 contains minor and consequential amendments arising out of the changes to administration.

Section 249: Special administration regimes

706. This section applies to companies for which special arrangements for the administration procedure have been made by applying Part II of the Insolvency Act 1986, with modifications. These special administration schemes are:

- water companies under the Water Industry Act 1991;
- companies to which railway administration orders apply (railway companies under the Railways Act 1993 and companies involved in the Channel Tunnel Rail Link);
- air traffic control companies under the Transport Act 2000;
- London Underground PPP companies under the Greater London Authority Act 1999; and
- building societies as defined by the Building Societies Act 1986.

707. The section provides an automatic saving provision for Part II as it is presently applied and modified by the various enactments listed above to continue to apply to companies subject to these regimes.

708. It also allows the Secretary of State (or HM Treasury in the case of building societies), by order, to amend the existing provisions in Part II (and to make consequential amendments of other enactments) as they are applied to the special regimes.

Section 250 & Schedule 18: Prohibition of appointment of administrative receiver & Schedule 2A to Insolvency Act 1986

709. This section inserts a new Chapter IV after Chapter III of Part III of the Insolvency Act 1986. Schedule 18 introduces new Schedule 2A to the Insolvency Act 1986 (inserted after Schedule 2).

710. Currently, a floating charge holder, whose security covers the whole or substantially the whole of the company's property, may enforce their contractual right to realise their security by appointing an AR (often simply referred to as a receiver in Scotland). In order to restrict the use of administrative receivership, new section 72A of Chapter IV prohibits, subject to certain exceptions, the holder of a qualifying floating charge (as defined under paragraph 14 of Schedule B1) from appointing an AR. The section applies to any floating charge created on or after the date that it comes into force.

711. However, there are cases where administrative receivership plays a crucial role. These exceptions to section 72A are set out in sections 72B-72G.

712. Section 72B provides that an AR can be appointed in pursuance of an arrangement which is, or forms part of, a capital market arrangement (as defined by paragraph 1 of Schedule 2A of Insolvency Act 1986 – see section 250 and Schedule 18), i.e.:

- it involves security that has been granted to a person holding a capital market investment issued by a party to the arrangement; or
- at least one party to the arrangement guarantees the performance of the obligations of another party; or
- at least one party provides security in respect of the performance of the obligations of another party; or
- the arrangement involves the issue of options, futures or contracts for differences.

713. This only applies if the debt, or expected debt, is at least £50 million and involves the issue of capital market investments as defined by paragraphs 2 and 3 of new Schedule 2A to the Insolvency Act 1986 (paragraph 1(1) of Schedule 18).

714. Section 72C provides that an AR can be appointed in respect of the property of a project company of a public-private partnership (PPP) project with step-in rights:

- a PPP project is one whose resources are provided partly by one or more public bodies and partly by one or more private bodies; or which is designed wholly or mainly to assist a public body in discharging a function.
- a project has 'step-in rights' if the person who provides finance (including an indemnity) for the project has a conditional right that enables them to assume sole or principal contractual responsibility for carrying out all or part of the project or to make payments so to do.

715. Section 72D provides that an AR can be appointed if the floating charge is granted over the property of a project company of a utility project with step-in rights.

716. A utility project is a project designed wholly or mainly for the purpose of a regulated business (e.g. a project that is concerned with a business carried out requiring a licence granted under section 8 Railways Act 1993, or a licence granted under section 7A Gas Act 1986). A full list of such regulated businesses is given in paragraph 10 of Schedule 18.

717. Section 72E provides that an AR can be appointed in respect of an arrangement in relation to a project company of a financed project with step-in rights. This only applies if the project company incurs a debt of at least £50 million for the purposes of carrying out the project.

718. Section 72F provides that an AR can be appointed by someone entitled to do so in connection with a market charge within the meaning of the Companies Act 1989; a system-charge within the meaning of the Financial Markets and Insolvency Regulations 1996; and a collateral security charge within the meaning of the Financial Markets and Insolvency (Settlement Finality) Regulations 1999.

719. Section 72G provides that an AR can be appointed if the floating charge is granted over a company which is registered as a social landlord under Part I of the Housing Act 1996 or Part 3 of the Housing (Scotland) Act 2001.

720. Section 72H inserts what will be new Schedule 2A into the Insolvency Act 1986, after the existing Schedule 2. It also gives the Secretary of State the power to amend the new provisions in Chapter IV to Part III of the Act. Specifically, the Secretary of State may, by order:

- insert additional exceptions to new section 72A;
- provide that an exception already provided for shall cease to have effect;
- amend section 72A in consequence of any new exception (or removal thereof);
- amend any of the exceptions 72B-72G;
- amend Schedule 2A.

Sections 251 and 252: Abolition of Crown Preference & Unsecured creditors

721. The White Paper *'Productivity and Enterprise: Insolvency – A Second Chance'* made a commitment to abolish the Crown's preferential status in insolvency, and to ensure that the benefit went to unsecured creditors for companies that have given floating-charges after the provision has come into force.

722. As a preferential creditor, the Crown can currently claim its debts from an insolvent company or bankrupt estate ahead of secured creditors, who hold a floating charge, and unsecured creditors. The Crown's preferential debts are described in sections 386 and 387 of, and Schedule 6 to, the Insolvency Act 1986, and include arrears of PAYE, NIC, and VAT for the following periods:

- debts due to the Inland Revenue for 12 months prior to the relevant date (category 1 of Schedule 6);
- debts due to Customs and Excise for the 6 to 12 months prior to the relevant date (category 2 of Schedule 6);
- social security contributions for the 12 months prior to the relevant date (category 3 of Schedule 6)..

723. The Act will abolish the Crown's preferential status.

724. The relevant date is defined by section 387 Insolvency Act 1986.

725. Preferential status will remain for:

- contributions to occupational pension schemes (category 4);
- remuneration of employees for the relevant period (category 5); and
- levies on coal and steel production under the European Coal and Steel Community (ECSC) Treaty.

726. In addition, Schedule 17 removes section 189(4) of the Employment Rights Act 1996. As a result, the Secretary of State will no longer be paid in priority to any remaining preferential claims lodged in the insolvency proceedings by former employees. The Secretary of State will remain a preferential creditor where he has "stepped into an employee's shoes" and made payments from the National Insurance Fund to cover all or part of any employee's preferential claims.

Section 251: Abolition of Crown Preference

727. Section 251*subsection (1)* removes paragraphs 1 and 2 (debts due to Inland Revenue), paragraphs 3-5C (debts due to Customs and Excise), and paragraphs 6 and 7 (social security contributions) from Schedule 6 to the Insolvency Act 1986, putting into effect the abolition of Crown preference. Subsection (2) makes similar changes for Scotland.

Section 252: Unsecured creditors

728. This section inserts a new section 176A (Share of assets for unsecured creditors) after section 176 of the Insolvency Act 1986. Section 176A provides for a prescribed part (a percentage share of the company's net property (as defined)) to go to unsecured creditors, although the percentage itself will be prescribed by Statutory Instrument (*subsections (7)-(8)*), the setting of which percentage will be subject to consultation.

729. Where a company has gone into liquidation, administration, provisional liquidation or receivership, the office-holder will make part of the company's net property available to unsecured creditors (i.e. after taking into account any preferential debts, any liability subject to a fixed charge and the costs of realising the company's property). However, it will not be necessary for the office-holder to distribute funds to unsecured creditors if they are less than the prescribed minimum, and he or she thinks that the cost of making a distribution would be disproportionate to the benefits. Where the prescribed part is greater than or equal to the minimum, but the costs of distribution are disproportionate to the benefits, the office holder will be able to apply to the court to waive the requirement.

Sanction of actions in relation to antecedent recoveries

Sections 253 and 262: Liquidator's powers & Powers of trustee in bankruptcy

730. The Insolvency Act 1986 contains measures to enable liquidators and trustees in bankruptcy to take legal action to seek financial restitution for losses caused to the insolvent estate. The provisions providing for the actions in question are: sections 213 (fraudulent trading); 214 (wrongful trading); 238 (transactions at an undervalue –

corporate); 239 (preferences – corporate); 242 (gratuitous alienations – Scotland); 243 (unfair preferences – Scotland); 339 (transactions at an undervalue – bankruptcy); 340 (preferences – bankruptcy) and 423 (transactions defrauding creditors).

731. These sections provide that the liquidator (section 253), or trustee in bankruptcy (section 262) must have sanction (i.e. approval), usually of the creditors or the court, before taking such antecedent recovery action.

Section 254: Application of insolvency law to foreign company

732. This section will allow, for example, the Secretary of State to apply the rescue provisions of the Insolvency Act 1986 to foreign incorporated companies through detailed secondary legislation. Part V of the Insolvency Act 1986 allows unregistered companies to be wound up by the court, such companies include foreign registered companies. Once this secondary legislation has been approved then such companies (particularly those with assets, creditors and employees in this country) will be able to make use of the rescue provisions, whereas currently the only option available is to be wound up by the court as an unregistered company.

Section 255: Application of law about company arrangement or administration to non-company

733. This section allows HM Treasury, with the concurrence of the Secretary of State, to make an order to provide for company arrangement and administration provisions to apply to certain non-companies, namely industrial and provident societies and friendly societies. This will enable the Government to apply those insolvency procedures, with any modifications that are necessary, to some or all of these societies through secondary legislation. The power will not be exercised without full consultation with all interested parties. The order may not apply in relation to a society which is registered as a social landlord under Part I of the Housing Act 1996 or Part 3 of the Housing (Scotland) Act 2001.

Individuals

Sections 256 and 269 & Schedules 19 and 23: Duration of bankruptcy & Minor and consequential amendments

734. Currently, bankrupts are discharged from bankruptcy three years after the making of the bankruptcy order, although there are exceptions to this rule; for example: in cases where the court has made an order for summary administration; where the bankrupt does not comply with his or her obligations and the court suspends automatic discharge; and where the debtor has been an undischarged bankrupt within the previous fifteen years or remains subject to an existing criminal bankruptcy order. However, in general, the duration of the bankruptcy is the same for bankrupts regardless of culpability or the level of their assets or liabilities.

735. Section 256 replaces the existing section 279 Insolvency Act 1986 on duration of bankruptcy. It provides for bankrupts to be automatically discharged one year after the bankruptcy order was made, but the period may be reduced if the Official Receiver files a notice stating that further investigation into the bankrupt's conduct and affairs is unnecessary, or has been concluded. The ability to suspend discharge where the bankrupt fails to comply with an obligation remains (see new subsections (3) and (4)). At present, where a bankruptcy order is made upon a debtor's own petition and, at that time, the debt is less than the small bankruptcies level (currently £20,000), and in the preceding five years the debtor has not been made bankrupt or entered into an individual voluntary arrangement, the court may issue a certificate of summary administration. One of the effects of this certificate is to reduce the discharge period from three to two years.

736. In order to reduce the discharge period to one year, it will be necessary to make amendments to current bankruptcy legislation, for example repealing those provisions in the Insolvency Act 1986 dealing with summary administration. These amendments are made in Schedule 23 to the Act, which is given effect by section 269.

737. As the discharge period is being altered, transitional provision needs to be made to deal with individuals who have already been made bankrupt on commencement but have not yet been discharged. This is done in Schedule 19. In this case, neither the existing nor the new section 279 Insolvency Act 1986 will apply. Instead, Schedule 19 provides that the date of discharge will be one year from the date of commencement of section 256 or earlier if the three-year discharge period is due to end before that date.

738. The position is different for those individuals who have been undischarged bankrupts more than once in the previous fifteen years and who are still undischarged at the time section 256 commences. In this case, the bankrupt is discharged five years from the date of commencement or earlier if an order under section 280(2) Insolvency Act 1986 is made or comes into effect. Section 280(2) allows the court to refuse discharge, conditionally discharge or absolutely discharge a bankrupt on his or her application. An application can be made any time after five years from the date of bankruptcy so that, for example, a person made bankrupt for the second time one year before the date of commencement of section 256 would be eligible to apply for discharge under section 280 four years after. If the court grants discharge on such an application, it will have effect from that date. If he or she makes no such application, or an application is refused, discharge will occur automatically five years after commencement.

739. Those persons made bankrupt under section 264(1)(d) (criminal bankruptcy) can only be discharged by order of the court under section 280 Insolvency Act 1986.

Sections 257 and 263 & Schedules 20 and 21: Post-discharge restrictions & Repeal of certain bankruptcy offences

740. The provisions of the Act remove some of the unnecessary restrictions that automatically apply as a result of bankruptcy (such as disqualification from holding certain offices (see further notes on sections 265, 266, 267 and 268)) and repeal two offences (section 263).

741. They also provide protection to the public and business community against the minority of bankrupts who abuse the system or whose conduct has been dishonest or otherwise culpable, either before or after bankruptcy. The Act introduces bankruptcy restrictions orders (BROs) that will have the effect of imposing restrictions on such bankrupts. BROs will run for a minimum period of two years and a maximum of fifteen years.

742. These restrictions are currently only triggered by the existence of a bankruptcy order (such as the obligation to declare your status as an undischarged bankrupt when obtaining credit of more than £250 (section 360(1) of insolvency legislation and the Insolvency Proceedings (Monetary Limits) Order 1986). By amending the discharge period, these restrictions will fall away for non-culpable bankrupts after a maximum of one year. Schedule 21 amends those provisions of the Insolvency Act 1986 that contain restrictions by adding references to BROs and interim BROs. These include section 31, which makes it an offence for a person to act as receiver or manager of a company's property if he or she is an undischarged bankrupt. In this way, such restrictions will continue to apply to persons whose bankruptcy has been discharged but who are subject to a BRO.

743. Schedule 20 inserts a new Schedule 4A into the Insolvency Act 1986 that sets out the details regarding BROs and bankruptcy restrictions undertakings (BRUs). BROs are made by the court on the application of the Secretary of State or the Official Receiver acting on the direction of the Secretary of State (paragraph 1 of new Schedule 4A).

744. Under paragraphs 7-9 of new Schedule 4A any reference to a person against whom a BRO has been made includes a reference to a person who is the subject of a BRU (paragraph 8). This will allow the bankrupt to agree to be bound by such restrictions without the need for an application to court. The minimum and maximum duration of a BRU will be the same as a BRO.

745. Paragraph 2 of Schedule 4A sets out the kinds of conduct to which the court will have particular regard in making a BRO. Failure to keep proper accounting records, and gambling and rash and hazardous speculation are types of conduct already covered by criminal offences in sections 361 and 362 Insolvency Act 1986. Section 263 repeals those two offences. In future, matters that would have been dealt with under those two offences will, provided the misconduct is material having regard to the circumstances of the case, be dealt with under the new bankruptcy restrictions regime.

746. Paragraph 3 provides that an application for a BRO must be made within one year of the making of the bankruptcy order. It also provides that proceedings may be brought outside this time scale but only with the permission of the court. The order will come into force when it is made and will last until the date specified in the order, which will be a minimum of two years and a maximum of fifteen years (paragraph 4).

747. It is unlikely in many cases that a substantive decision will be made by the court in relation to an application for a BRO before the defendant's discharge. Thus, there is likely to be a gap in time between the discharge of the bankrupt and the making of the BRO in those cases where a BRO is being sought. Paragraphs 5 and 6 make provision for the court to make an interim order that can be made when issuing proceedings. The court may make an interim BRO where the Official Receiver or Secretary of State has made out a *prima facie* case and the court is of the view that the misconduct is so serious that it is in the public interest to make such an order. The restrictions then apply on the making of the interim order, by virtue of paragraph 5(4).

748. Paragraphs 10 and 11 set out the effects of annulment of the bankruptcy on any BRO. Where a bankruptcy order is annulled under section 282(1)(a) Insolvency Act 1986 on the grounds that it ought not have been made, any BRO, either substantive or interim, that is in force will be annulled.

749. A bankruptcy order annulled because an individual voluntary arrangement has been approved by the creditors (sections 261 and 263D of the Insolvency Act 1986), or because the bankruptcy debts and expenses have been paid in full, will not affect whether a BRO or interim order remains in force. Where an application has been made, then those proceedings can be continued notwithstanding the annulment of the bankruptcy. This permits the making of BROs against culpable bankrupts who have managed to have their bankruptcy order annulled solely because they are now able, for whatever reason, to pay off their debts either in full or partially to the satisfaction of their creditors. Where a BRU has been offered, the undertaking can be finalised notwithstanding any annulment under sections 261 and 263D Insolvency Act 1986.

750. Paragraph 12 requires the Secretary of State to maintain a public register of BROs, interim BROs and BRUs. Paragraph 16 of Schedule 23 inserts a new paragraph 29A into Schedule 9 of the Insolvency Act 1986. This allows, amongst other things, Rules to be made about the inspection of the register.

751. Schedule 21 deals with the effect of BROs, interim BROs and BRUs. It amends certain provisions that make particular conduct an offence while an undischarged bankrupt and extends them to cover individuals subject to BROs, interim BROs and BRUs (incorporated by virtue of paragraphs 5(4) and 8 of new Schedule 4A of the Insolvency Act 1986 respectively). The conduct includes:

- acting as receiver or manager of a company's property on behalf of a debenture holder (section 31 Insolvency Act 1986);

- obtaining credit above the prescribed limit without disclosing that you are the subject of a Bankruptcy Restrictions Order (section 360 Insolvency Act 1986);
- trading in a name other than that under which a person was made bankrupt (section 360 Insolvency Act 1986);
- disqualification from acting as an insolvency practitioner (section 390 Insolvency Act 1986); and
- disqualification from acting as a company director (section 11(1) CDDA1986).

752. Section 350(3) of the Insolvency Act 1986 limits the liability of a bankrupt for offences under Part VI of that Act to acts committed prior to his discharge. Paragraph 2 of Schedule 21 qualifies that provision so that a person subject to a BRO who commits an offence extended to BROs after discharge can still be prosecuted.

Section 258: Investigation by official receiver

753. Currently, under section 289 Insolvency Act 1986, there is a duty on the Official Receiver to investigate the conduct and affairs of every bankrupt and to make any report to the court that he or she thinks fit, except in summary cases when the Official Receiver will only investigate if he or she deems it necessary. This distinction is made on the basis that cases with relatively small unsecured liabilities (summary cases with unsecured liabilities of less than £20,000 – often consumer bankruptcies) do not require as extensive a use of the Official Receiver's resources as those involving large debts with greater losses to the creditors. However, there are cases where the bankrupt's debts are large (for example, where the liabilities of a limited company are guaranteed) in which no investigation is required or some small, yet complex, cases that require extensive investigation.

754. Section 258 inserts a new section 289 into the Insolvency Act 1986 that removes this automatic obligation to investigate every case and provides that the Official Receiver is only required to investigate the conduct and affairs of any bankrupt where he or she think it necessary). *Subsections (3) and (4)* of the new provision merely re-enact the old section 289(2) and (3).

Sections 259 and 260: Income payments order & Income payments agreement

755. The current income payments order regime is designed to ensure bankrupts make an affordable contribution towards their debt from their income for up to three years, but in most cases they cease on discharge (see section 310(6)). Against the background of a reduced period of bankruptcy for non-culpable bankrupts, income payments orders will now last for a term of up to three years from the date of the order, irrespective of discharge (see new section 310(6) inserted by section 259).

756. Income payments orders are made by the courts on the application of the trustee in bankruptcy. In practice most are not usually contested. Income payments orders can be varied on the application of the trustee or the bankrupt.

757. In order to remove the need for court involvement in non-contentious cases, section 260 introduces the concept of the income payments agreement by inserting a new Section 310A into the Insolvency Act 1986.

758. Income payments agreements will provide a legally-binding written agreement between the bankrupt and the Official Receiver or trustee that requires the bankrupt (or a third party) to make specified payments to his trustee for a specified period. This will be enforceable as if it were an income payments order made by the court. Whilst in force, an income payments agreement may be varied on an application to the court by the bankrupt, trustee or the Official Receiver or by written agreement between the parties. A court may not vary an income payments agreement to include a provision that could

not be included in an income payments order and must grant a variation if it takes the view that the variation is necessary to enable the bankrupt to retain sufficient funds to meet the reasonable domestic needs of the bankrupt and his or her family.

759. An income payments agreement must specify the period in which it is to have effect and that period can apply after a bankrupt is discharged but cannot extend to a date more than three years after the date of the income payments agreement.

760. Paragraph 7 of Schedule 19 sets out the transitional provisions as they relate to income payments orders in existence at the time of commencement.

Section 261: Bankrupt's Home

761. Section 261 makes provision in relation to the sole or principal residence of the bankrupt, the bankrupt's spouse or the former spouse of a bankrupt, and where the bankrupt has an interest that is comprised in the bankrupt's estate. The section (*subsection (1)*) inserts section 283A into the Insolvency Act 1986. This new section provides that where a bankrupt's estate comprises an interest in such a residence, that interest reverts back to the bankrupt unless within the three year period following the date of the bankruptcy the trustee:

(a) realises the interest;

(b) applies for an order of sale or possession in respect of the premises in which the interest subsists;

(c) applies for a charging order over the premises in respect of the value of the interest; or

(d) enters into an agreement with the bankrupt regarding the interest.

762. The section (*subsection (3)*) also inserts a new section 313A into the Insolvency Act 1986 which provides for the dismissal of applications for orders for sale, possession or a charging order in respect of the bankrupt's residence where the value of the bankrupt's interest is below a level prescribed in secondary legislation.

Section 264 & Schedule 22: Individual voluntary arrangement

763. Individual voluntary arrangements are an alternative to bankruptcy, without the same automatic restrictions, where the debtor comes to an arrangement with his or her creditors about the repayment of his or her debts. They generally provide a better return to creditors. Currently there are around 7,000 individual voluntary arrangements made each year, of which a very small minority are entered into after a bankruptcy order has been made.

764. At present, a debtor can make a proposal for an individual voluntary arrangement (see Part VIII of the Insolvency Act 1986). Those proposals also put forward a person to supervise the implementation of that arrangement, the nominee (on approval of an arrangement the nominee becomes supervisor). To act as the nominee (from 1 January 2003, as a result of the relevant amendments introduced by the Insolvency Act 2000) or supervisor, a person must be a qualified insolvency practitioner. In practice, the debtor sends the nominee a copy of the proposal and a statement of his or her affairs. He or she can then apply for an interim order that has the effect of staying any actions against them or their property (see sections 252–255 of the Insolvency Act 1986). The nominee reports to the court, stating whether a meeting of creditors should be called to consider the proposal. If a meeting is called and the creditors approve the individual voluntary arrangement, the interim order can be discharged and any bankruptcy order may be annulled. Modifications can be made to the proposal if the debtor so consents.

765. In order to encourage greater use of individual voluntary arrangements, this section makes two changes to the current individual voluntary arrangements regime.

766. First, it enables Official Receivers to act as nominees and supervisors for post-bankruptcy individual voluntary arrangements (see paragraph 3 of Schedule 22, which inserts a new Section 389B into the Insolvency Act 1986). This provides debtors and creditors with a choice of who should administer the arrangement: either a private sector insolvency practitioner or an Official Receiver. There is also an order-making power to extend the ability for the Official Receiver to act as nominee and supervisor to all cases.

767. Second, it introduces a new fast-track scheme for post-bankruptcy individual voluntary arrangements where the Official Receiver is the proposed nominee (see paragraph 2 of Schedule 22, which inserts a new section 263A – 263G into the Insolvency Act 1986). Under this regime, the proposal will be agreed with the Official Receiver and filed with the Court. No meeting of the creditors will be called and it will not be possible to modify the proposal. The Official Receiver will send out the proposal to the creditors on a 'take it or leave it' basis and the creditors will either agree to or disagree with the proposal by correspondence. If the individual voluntary arrangement is approved, the Official Receiver will notify the court and the court can then annul the bankruptcy order. It is proposed that the majority required for approval will remain unchanged (the provision on majority is set out in Rule 5.18 of the Insolvency Rules 1986 (SI1986/1925)), which majority is three quarters in value. From 1 January 2003, as a result of changes introduced by SI 2002/2712, that provision will be found at Rule 5.23.

Sections 265, 266, 267 and 268: Disqualification from office: Justice of the Peace, Parliament, Local government & General

768. Currently bankrupts are subject to a wide range of statutory restrictions, prohibitions or disqualifications irrespective of the level of their assets and liabilities, or culpability. These restrictions prevent the bankrupt from being elected to or holding specified positions or offices, or becoming or remaining a member of specified bodies or groups. Generally, these restrictions are in place for the duration of the bankruptcy (currently three years in most cases). While in some cases these restrictions can be justified in the public interest, there is little justification for others (e.g. serving as a Justice of the Peace or member of a Local Authority).

Section 266: Disqualification from office: Parliament

769. Section 427 of the Insolvency Act 1986 imposes a number of restrictions on a member of either House at Westminster if he or she is adjudged bankrupt (or sequestrated in Scotland). In the House of Lords, a member is not allowed to sit or vote in either the House or Committee. In the Commons, a member cannot be elected to, sit or vote in the House (or the devolved equivalent) or on Committee. The restrictions on being elected to and sitting and voting in the devolved assemblies on the ground of bankruptcy feed through from section 427 by virtue of the Government of Wales Act 1998, the Scotland Act 1998 and the Northern Ireland Act 1998.

770. With the exception of a peer in Westminster, in all legislatures a bankrupt is given six months in order to have their bankruptcy order annulled or their bankruptcy discharged. If this has not happened by the end of that period, then their seat is vacated.

771. Section 266 inserts new sections into the Insolvency Act 1986 to deal with disqualification from Parliament, the Scottish Parliament, the Northern Ireland Assembly or the National Assembly for Wales where a BRO is made against a member of any of those Assemblies. It also amends section 427 Insolvency Act 1986 to remove references to England and Wales from that section and to change its title.

England and Wales

772. The new section 426A disqualifies an MP against whom a BRO is made from membership of the House of Commons. On disqualification under this section, an MP must immediately vacate his or her seat. This differs from the current position under

section 427 Insolvency Act 1986, which disqualifies a person on the making of a bankruptcy order but then gives a period of six months for an MP to have the bankruptcy order annulled. Under the new section, an MP is no longer automatically disqualified on the making of a bankruptcy order. Those MPs where some form of culpability can be shown through the making of a BRO will be disqualified automatically and there will be no six months grace period.

773. A member of the House of Lords subject to a BRO will be disqualified from sitting or voting in the House of Lords or from sitting or voting in a committee of the House of Lords or a joint committee of both Houses. No writ of summons can be issued to a lord of Parliament who is subject to a BRO. These are the same restrictions as are currently in place for a bankruptcy order but, again, by replacing bankruptcy with BRO as the trigger to disqualification, only culpable peers will be disqualified.

The Devolved Assemblies

774. The new section 426A will feed through to the devolved Assemblies by virtue of the devolution legislation. A member of the Scottish Parliament against whom a BRO is made will be disqualified from the Scottish Parliament by virtue of section 15(1)(b) Scotland Act 1998 and will have to vacate his or her seat under sections 17(1) and (2) of that Act.

775. The position is the same for a member of the National Assembly for Wales by virtue of sections 12(2) and 14(1) and (2) Government of Wales Act 1998 and for a member of the Northern Ireland Assembly by virtue of sections 36(4) and 37(1) Northern Ireland Act 1998 and Article 370 of the Insolvency (Northern Ireland) Order 1989.

MPs, Peers and Members of the Devolved Assemblies made bankrupt in Northern Ireland or sequestrated in Scotland

776. There is no equivalent regime to BROs in either Scotland or Northern Ireland. Insolvency law in Wales is the same as in England and will be modified by this Act.

777. Therefore, the existing regime for disqualification where an MP, peer or a member of a devolved Assembly is made bankrupt in Northern Ireland or sequestrated in Scotland is being retained. However, section 427 is being amended by section 266(1) and (2) so that it will then only cover those made bankrupt in Northern Ireland or sequestrated in Scotland.

778. For example, an MSP who is sequestrated in Scotland will be disqualified and will have six months to have that order annulled before having to vacate his or her seat.

Two regimes

779. Therefore, two different regimes will be in operation at the same time in Parliament and all the devolved Assemblies, depending on the jurisdiction in which the bankruptcy occurs:

- where a member of Parliament or a member of the devolved Assemblies is made bankrupt in England and Wales, these persons will not be automatically disqualified. Disqualification will be triggered if a BRO is made against him or her and he or she will have to vacate their seat immediately. A peer will be disqualified on the making of a BRO order from sitting and voting in the House of Lords or in Committee;

- where a member of Parliament or a member of the devolved Assemblies is made bankrupt in Northern Ireland or sequestrated in Scotland, they will be automatically disqualified on being made bankrupt or sequestrated and will have six months to have the order annulled. A peer who is a member of a devolved Assembly would be disqualified from the devolved Assembly and have six months to have the

order annulled or his or her bankruptcy discharged and would be disqualified in Westminster from sitting and voting in the House of Lords or in Committee.

The order-making power

780. Section 266 provides for an order-making power to amend sections 426A and 426B, should equivalent regimes be introduced in Northern Ireland and Scotland. The order-making power would be subject to affirmative resolution.

781. Section 265 will remove the automatic disqualification on a bankrupt acting as a justice of the peace. The removal of bankrupt justices of the peace will be left to the Lord Chancellor's general power to appoint and remove justices of the peace where it is thought appropriate.

782. Section 267 will replace the automatic restriction on bankrupts serving as a member of a Local Authority with one disqualifying those subject to a BRO.

783. Section 268 will provide a wide order-making power for any Secretary of State or the National Assembly for Wales, to review legislation under his or her policy control and to maintain, repeal, amend or abolish such restrictions on bankrupts as they deem appropriate. Amendments can include reducing the class of bankrupts to whom a disqualification applies, applying the restrictions to those people who are subject to BROs or undertakings as well as bankrupts or providing that the disqualification is subject to the discretion of a specified person, body or group. Such orders will be subject to affirmative resolution.

Section 269 & Schedule 23: Minor and consequential amendments

784. Section 269 gives effect to Schedule 23, which makes minor and consequential amendments to the Insolvency Act 1986 as a result of the changes being made in the Act. Some of these amendments, such as those made because of the removal of summary bankruptcy, have been mentioned elsewhere. Paragraph 14 reflects the fact that the Official Receiver can act as a nominee and supervisor in an individual voluntary arrangement. Therefore the appointment provisions for Official Receivers in section 399 and the rules-making provisions in Schedule 23 have been amended accordingly.

785. Paragraph 12 extends the offence of concealment of property to section 354 Insolvency Act 1986 to include any failure to account for the loss of any substantial property to the trustee. Currently, the provisions in section 354(3) set out the scope of the offence of a bankrupt failing – without reasonable excuse – either to account to the Official Receiver or the court for substantial losses or give satisfactory explanation for how such a loss came about. However, the realisation of assets is often administered by a trustee other than the Official Receiver.

786. Paragraph 13 adds subsections (4) and (5) to section 355 (concealment and falsification of accounting records) Insolvency Act 1986. The current provisions of section 355(2) and (3) detail offences relating to bankrupts who destroy, conceal, alter or dispose of books, papers or records in the twelve months prior to a bankruptcy petition being presented, or between the petition and order. In the case of ‘trading records’, that period is extended to two years (section 361 of the Insolvency Act 1986). The Act also repeals the current provisions of section 361, which will be dealt with by the new bankruptcy restrictions regime. As the availability of adequate records is crucial to the examination of the bankrupt’s estates and enquiries into the bankrupt’s affairs, subsection (4) extends the period from twelve months to two years. Subsection (5) provides a definition of the term ‘trading record’.

787. County Court Administration Orders (‘CCAOs’) are made in the county courts and fall outside the insolvency regime. They are mechanisms for dealing with individuals with multiple debts and give the debtor respite from enforcement proceedings while they

pay off their debts. Only those who have a county court judgment against them, at least one other debt, and total debts of less than £5,000, can apply for a CCAO. Currently, section 429 Insolvency Act 1986 allows a court to make an order placing restrictions on acquiring credit and the use of a trading name for up to two years where a debtor has failed to pay under a CCAO. Paragraph 15 amends section 429 County Courts Act 1984 to reflect the fact that restrictions flowing from the making of a bankruptcy order will only be for one year following the change to the discharge period. Therefore restrictions flowing from a CCAO will be similarly limited.

Money

788. The current financial regime of The Insolvency Service comprises numerous fees (see the Insolvency Fees Order 1986) covering case administration and a Secretary of State Fee, none of which achieves full cost recovery of activities undertaken by The Service. In addition, because of the low rate of interest set for estate balances invested in the Insolvency Services Investment Account, the amount returned to estates is considerably less than the level of investment income received by the account. The excess income is currently paid into the Consolidated Fund and amounted to some £43 million in 2000-01.

789. The Government has announced its intention to reform the regime to make it simpler and more transparent. It is also proposed to make the regime fairer to creditors, for example by returning to insolvent estates those investment returns that currently flow into the Consolidated Fund. The majority of the changes necessary to achieve reform will be made by using existing powers and changes to secondary legislation and Rules. However, there are two specific areas that require primary legislation, and provisions for these are included in the Act.

Section 270: Fees

790. Section 270*subsection (1)* inserts a new section 415A into the Insolvency Act 1986.

791. The new section will enable the Secretary of State to charge a fee to bodies recognised under section 391 Insolvency Act 1986 as a professional body for the purposes of licensing insolvency practitioners (IPs). It is intended that fees prescribed under this provision not only cover the cost of recognition but also the cost of monitoring the bodies' activities, such as overseeing their procedures and ensuring that licensing is carried out properly. The fee will also cover the cost of more general regulatory functions carried out by The Insolvency Service, such as representation on the Joint Insolvency Council and keeping IPs informed of legislative and other developments through the issuing of newsletters and guidance. The cost of these regulatory functions is currently met by the DTI but the new policy is that they should fall to the profession. The fee, which will be set out in secondary legislation, will be charged to each body based on the number of IPs licensed by them.

792. Subsection (2) of new section 415A provides for a fee to be charged to those IPs licensed by the Secretary of State under section 392, and will be based on the cost of granting and maintaining authorisation. The fee will also include the cost of monitoring the IP and the general regulatory functions undertaken by The Insolvency Service. As with the fee for the recognised bodies, the fee for IPs licensed by the Secretary of State will be set through secondary legislation. The level of the authorisation element of the fee will reflect more closely that charged by the recognised bodies to those IPs they license than the current authorisation fee of £100, which was set in 1986.

793. Subsection (3) provides for payment of fees that relate to the operation of the Insolvency Services Account by The Insolvency Service and money paid into or out of the Account. The Insolvency Service will separate out the costs that relate to its operation of the Insolvency Service Account so that these costs are met by insolvent estates. This will allow for clear identification of those banking services that are carried out in respect of all cases, and that will be charged through an annual service fee, and those that relate

to specific estates and transactions such as investment requests by IPs or the volume of payments out of the account through cheques or bank transfers. These changes will also enable the ending of the current arrangements whereby a number of different fees are used to meet these costs and to cross-subsidise other functions. Subsection (4) applies the conditions that apply to fees under section 414 to those introduced under 415A.

Sections 271 and 272: Insolvency Services Account: interest & Insolvency Services Accounts

794. Section 405 of the Insolvency Act 1986 requires that any excess in investment income from the Insolvency Service Investment Account after payments to insolvent estates and tax should be paid into the Consolidated Fund. Schedule 8 paragraph 16 and Schedule 9 paragraph 21 of the Insolvency Act 1986 enables the interest rate for the return of investment income to insolvent estates to be set through secondary legislation. The current rate of 3.5% has applied to companies since before the implementation of the 1986 Act. The Insolvency Act 2000 provided for payment of interest into bankruptcy estates.

795. Section 271 introduces additions to Schedules 8 and 9 to the Insolvency Act 1986 to allow Rules to be made providing for the interest rate to be set by the Secretary of State by the issuing of a Notice, as opposed to through secondary legislation. This will enable the rate to be reviewed at regular intervals, probably annually, and allow changes in investment returns to the Account to flow through to insolvent estates without having to make regular amendments through statutory instruments.

796. Section 272*subsection (1)* removes the requirement under section 405 Insolvency Act 1986 for excess income from the Insolvency Services Investment Account to be paid into the Consolidated Fund.

797. Section 408 of the Insolvency Act 1986 provides for recourse to the Consolidated Fund where, after payments received from the Investment Account, the Insolvency Services Account has insufficient funds to meet its liabilities. *Subsection (2)* of section 272 substitutes for the current section 408 a new section that incorporates the circumstances covered by the current section 408 and section 405 but provides wider powers that allow for adjustments to be made between the Insolvency Services Account or the Insolvency Services Investment Account and the Consolidated Fund. Adjustments may be necessary due to short-term fluctuations between the expected income, based on the level at which the interest rates are set and the actual investment return. This is because interest rates are set in advance, whereas the Investment Account is made up of investments purchased at different times, for different amounts, with differing returns and over different periods. New section 408 will enable the maintenance of a 'buffer' in the account to deal with such fluctuations and there may be occasions where adjustments need to be made between the account and the Consolidated Fund.