

EXPLANATORY MEMORANDUM TO
THE INSOLVENCY (SCOTLAND) (COMPANY VOLUNTARY ARRANGEMENTS
AND ADMINISTRATION) RULES 2018

2018 No. 1082 (S. 4)

1. Introduction

- 1.1 This explanatory memorandum has been prepared by the Department for Business, Energy & Industrial Strategy in conjunction with the Insolvency Service and is laid before Parliament by Command of Her Majesty.
- 1.2 This memorandum contains information for the Joint Committee on Statutory Instruments.

2. Purpose of the instrument

- 2.1 The Insolvency (Scotland) (Company Voluntary Arrangements and Administration) Rules 2018 (“I(S)CVAAR”) will consolidate the procedural rules for CVAs and administration which are currently contained in the Insolvency (Scotland) Rules 1986 (“the 1986 Rules”), together with the various amending instruments made since the 1986 Rules came into force.
- 2.2 The I(S)CVAAR will restructure the rules in relation to company voluntary arrangements (“CVAs”) and administration procedures, and update the language including gender-neutral drafting.
- 2.3 Finally they modernise the 1986 Rules to take account of the changes made to the Act by the Small Business, Enterprise and Employment Act 2015 (“SBEEA”); in particular amendments enabling modern methods of communication and decision making to be used in place of paper communications and physical meetings.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

- 3.1 The reservation of insolvency in paragraph C2 of Part II of Schedule 5 to the Scotland Act 1998 results in a split in competence in this area between the UK and Scottish Parliaments. CVAs and administration are reserved matters while receivership (subject to minor exceptions) is a devolved matter. Winding up is an area of mixed competence: the legal effect of winding up is reserved to the UK Parliament but the process of winding up is excepted from the reservation. The power to make rules under section 411 of the Act is similarly split between the two administrations: insofar as the power enables the making of rules relating to receivership and the devolved aspects of winding up, it has transferred to the Scottish Ministers by virtue of section 53 of the Scotland Act 1998. Insofar as the power enables the making of rules relating to CVAs and administration, the power remains with the Secretary of State.
- 3.2 In order to facilitate the making of rules relating to the mixed-competence area of winding up in one instrument, an order under the Scotland Act 1998 was made earlier this year. The Scotland Act (Insolvency Functions) Order 2018 SI 2018/174 effects a mutual transfer of the rule-making function under section 411 of the Act in the area of winding up, and enables the making of all of the rules in this area by either a Minister

of the Crown or the Scottish Ministers, with the consent of the other administration. For the purposes of this project, it was agreed that the rules on winding up would be made by the Scottish Ministers, with the consent of the Secretary of State.

- 3.3 The new Scottish insolvency rules will accordingly be made up of two instruments: a Statutory Instrument – the I(S)CVAAR, to be made by the Secretary of State - dealing with CVAs and administration; and a Scottish Statutory Instrument – the Insolvency (Scotland) (Receivership and Winding Up) Rules 2018 (“I(S)RWUR”), to be made by the Scottish Ministers - dealing with receivership and winding up.
- 3.4 Although the I(S)CVAAR make provision in relation to CVAs and administration and the I(S)RWUR make provision in relation to winding up, there are three rules contained in the I(S)CVAAR which make provision relating to the devolved elements of winding up. The consent of the Scottish Ministers has accordingly been obtained – in accordance with the Scotland Act (Insolvency Functions) Order 2018 - to the inclusion within the instrument of rules 1.33 and 1.34 (relating to opted-out creditors) and rule 7.2 (relating to the conversion of insolvency proceedings under the EU Regulation).
- 3.5 The I(S)CVAAR do not include rules relating to the insolvency of Limited Liability Partnerships in Scotland. Nor do they deal with Special Administration Regimes or other specialised insolvency regimes. The re-cast rules will accordingly save the application of the 1986 Rules in respect of Limited Liability Partnerships.
- 3.6 The Act is a large and complex piece of legislation which brought together corporate insolvency procedures and which has been heavily amended since it was made. In relation to different insolvency proceedings there is a lack of consistency in what is contained in the Act and what needs to be contained in the I(S)CVAAR to supplement the Act. Users of the I(S)CVAAR need to relate individual rules to the sections of the Act which they complete or complement. In order to assist the users there are a number of non-legislative notes in the I(S)CVAAR. These are contained in square brackets and are labelled as notes. These have a number of purposes. For example they draw the user’s attention to those provisions in the Act which a particular rule complements. In rule 1.2 (definitions) there are pointers to definitions that are found in different places in the Act and which in some cases are applied by the I(S)CVAAR for other purposes. There are also notes which refer the reader to things which are not in the Rules, for example where a note refers to an article of the EU Regulation. Finally there are notes which point the user to other parts of the I(S)CVAAR that are relevant to an individual rule or a Part of the I(S)CVAAR such as the pointers to information required in documents by Part 1.
- 3.7 We recognise that the use of notes to such an extent is unusual, however when developing the rules stakeholders have informed the Department that they find these useful.

Matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business (English Votes for English Laws)

- 3.8 As the instrument is subject to negative resolution procedure there are no matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business at this stage.

4. Extent and Territorial Application.

- 4.1 The extent of this instrument is Scotland.
- 4.2 The territorial application of the instrument is Scotland.

5. European Convention on Human Rights

- 5.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

6. Legislative Context

- 6.1 The I(S)CVAAR provide the procedural framework for insolvency proceedings under Parts 1 and 2 of the Insolvency Act 1986 (“the Act”). They prescribe matters required by the Act and set out the procedural rules to be followed in the conduct of CVAs and administration proceedings in Scotland.
- 6.2 The rules are closely modelled on the procedural rules for CVAs and administrations in the Insolvency (England and Wales) Rules 2016 which were re-cast and re-stated in 2016 ([SI 2016/1024](#) as amended) and commenced on 6 April 2017.
- 6.3 The I(S)CVAAR will give effect to policy changes made to the Act by the SBEEA.

7. Policy background

What is being done and why?

- 7.1 The first purpose of the I(S)CVAAR is to consolidate the existing instruments which together comprise the 1986 Rules and provide the procedural rules for CVAs and administrations in Scotland. This will better meet the needs of users, including the judiciary, insolvency office-holders, creditors and public officials.
- 7.2 The second purpose is to update the 1986 Rules both in terms of their structure, language and style of the drafting. Modernised language and gender neutral drafting have been used in the I(S)CVAAR and the rules have been drafted in a simpler fashion to make them easier for users to understand and apply. Undue repetition has been avoided through the greater use of common parts that apply to both CVAs and administrations, such as the decision making provisions of Part 5 that will apply to both procedures in the future. Repetition has also been avoided by the wider use of standard content provisions for notices and documents.
- 7.3 One further significant change is the approach taken of prescribing content for notices and documents in the rules themselves rather than statutory forms. This builds in a significant degree of future-proofing as there will be less need for amendment to accommodate advances in technology, business practice and to enable e-delivery.
- 7.4 I(S)CVAAR has been developed alongside the I(S)RWUR which will provide the procedural rules for receivership and winding up in Scotland, with the aim of using similar modernised language, layout and common parts such that users find the instruments complement one another.
- 7.5 The third purpose is to modernise and give effect to policy changes, some of which result from amendments made to the Act by the SBEEA. These changes result from deregulatory initiatives such as the Red Tape Challenge, and many of which were put forward by a range of stakeholders. The policy impetus for all these measures was to remove unnecessary regulatory burdens to reduce the cost of administering insolvency

proceedings. Reducing costs will benefit creditors in the form of improved dividend returns.

- 7.6 As business practice has developed, particularly as a consequence of technological advances, amendments to the law have, at times, been slow to follow. This has meant users have not always been able to take advantage of the quickest, most cost-effective or convenient methods of achieving certain tasks. In the context of insolvency proceedings this is particularly prevalent in the ways insolvency office-holders communicate with creditors and other parties. A number of policy changes have therefore been made and the main changes are summarised below.

7.7 Electronic communication

Where a debtor and a creditor have been customarily corresponding electronically prior to insolvency, under the 1986 Rules an insolvency office-holder could not continue to correspond in that way without first obtaining the creditor's written consent. Stakeholders stated that this is a big barrier to e-communications and did not reflect the way the business world operated (even more so than in 2010 when e-communications were first permitted by the Insolvency (Scotland) Amendment Rules 2010). The I(S)CVAAR change this so that where electronic communication was customarily used pre-insolvency, then that method of communication can continue post-insolvency. This will encourage e-communication, which is generally cheaper and speedier than traditional post.

7.8 Use of websites

Under the 1986 Rules an office-holder who wants to put all future documents on a case on a website after only an initial notice to creditors must obtain an order of the court. This requirement has been removed and the I(S)CVAAR permit an office-holder to send a notice to creditors stating that all future documents will be made available on a website, subject to certain exceptions.

7.9 Statements of Affairs

Statements of affairs contain full details of all creditors, including their names and addresses, and the amounts of their claims. These details will include any employees or ex-employees owed money by the insolvent company for wages or similar payments, and also any customers who may have made advance payment for goods or services. In administrations the statement of affairs must be filed with the Registrar of Companies, which leads to those details being placed in the public domain. This has led to concerns over protection of privacy and identity theft.

New provisions now require that where a statement of affairs is to be filed with the Registrar of Companies, details of employees, ex-employees, and customers who are consumers must be contained within a separate schedule, and only a summary will appear in the body of the document. That schedule will be removed before the statement of affairs is filed with the Registrar.

7.10 Removing meetings of creditors

Amendments made to the Act by SBEEA remove meetings as the default mechanism for seeking decisions from creditors in insolvency proceedings. In many cases the office-holder will be able to use a process of deemed consent, where they write to creditors with a proposal. Provided they do not receive objections from 10% or more of creditors by value then the proposal will be deemed to be approved. In the event that 10% or more of creditors object to the proposal then the office-holder will use an

alternative decision-making process, such as a virtual meeting, correspondence or electronic voting.

I(S)CVAAR specifies what types of alternative decision-making processes may be used. The form the alternative decision-making process takes in respect of a particular decision will be at the discretion of the office-holder, with limited exceptions. An officeholder may only call a physical meeting of creditors if this has been requested by 10% or more by value of the creditors, or 10% of the total number of creditors, or 10 individual creditors. It is open to creditors to make this request at any time they are asked to make a decision. This means that the expenses of calling a physical meeting will be incurred and charged to the insolvency estate only where creditors have asked for this to happen, so unnecessary charges will be prevented. The thresholds for requiring a physical meeting of creditors are contained within the primary legislation.

7.11 Opting out of further correspondence

Currently the Act (and hence the 1986 Rules) require the office-holder to send all notices, reports etc., to all known creditors. Even where a creditor has no further interest in a case and wants no further information on it— for example if there is little or no likelihood of a financial return — they cannot ask the office-holder to omit them from future mailings. The amendments to the Act to which the Rules give effect allow a creditor to opt out of receiving further correspondence, therefore relieving the office-holder of the expense of sending notices and the creditor of the expense of dealing with them. Notices of intended dividends will not be subject to the opt-out and creditors will retain the ability to opt back in to receiving notices.

7.12 Allowing an administrator to pay a dividend in respect of a debt of less than £1,000 without the need for the creditor to submit a formal claim

To receive a dividend in administration, a creditor must first submit a claim to the administrator, which must contain prescribed information. The office-holder may ask for further evidence from the creditor if thought necessary. Such claims must be scrutinised by the office-holder prior to distribution of any dividend. New provisions in the I(S)CVAAR allow an administrator to rely on information contained in a company's statement of affairs or accounting records, and to pay a dividend without the need for the creditor to submit a claim but only where the debt in question is below the prescribed limit of £1,000.

8. European Union (Withdrawal) Act/Withdrawal of the United Kingdom from the European Union

8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act.

9. Consolidation

9.1 The I(S)CVAAR will consolidate the procedural rules for CVAs and administration which are currently contained in the 1986 Rules, together with the various amending instruments made since the 1986 Rules came into force.

10. Consultation outcome

10.1 The I(S)CVAAR have not been subject to a formal public consultation, however they have been developed following detailed discussion with a working group drawn from

insolvency practitioners, lawyers and a regulator with expertise in the law and practice of all forms of Scottish corporate insolvency.

- 10.2 The rules are closely modelled on the Insolvency (England and Wales) Rules 2016 which were the subject of an extensive programme of consultation and engagement with a range of parties affected by insolvency. Such parties included: the insolvency profession, creditor representatives, insolvency regulators and public bodies. Scottish practitioners have expressed a desire for the two sets of rules to mirror one another insofar as is reasonably practicable, taking account of variations in Scots law and practice.
- 10.3 Whilst CVAs and administrations are reserved matters, the I(S)CVAAR have been developed in close consultation with Scottish Government officials given that the I(S)CVAAR are intended to sit with, and complement, the I(S)RWUR.

11. Guidance

- 11.1 Throughout the programme of engagement outlined above, the Insolvency Service has met with and corresponded with interested parties to discuss and provide information relating to the I(S)CVAAR including highlighting the differences between the I(S)CVAAR and the 1986 Rules and what they would mean in practice. The Insolvency Service will continue to engage with stakeholders as they prepare themselves for commencement of the I(S)CVAAR.

12. Impact

- 12.1 The impact on business, charities or voluntary bodies relates to their capacity as creditors in insolvency proceedings and is deregulatory. The efficiency savings delivered by the I(S)CVAAR will result in lower costs in dealing with the administration of company voluntary arrangements and administrations in Scotland. This in turn should lead to better returns to creditors.
- 12.2 The impact on the public sector relates to the public sector as a creditor in insolvency proceedings. In such cases, the public body should also benefit from the same better returns as other creditors.
- 12.3 A full impact assessment has not been produced as the savings are anticipated to be less than £1M per year.

13. Regulating small business

- 13.1 The legislation is deregulatory and applies to activities that are undertaken by small businesses.

14. Monitoring & review

- 14.1 The effectiveness of both the (S)CVAAR and I(S)RWUR will be borne out by their ability to facilitate and achieve more effective, efficient and transparent insolvency processes and, in doing so, deliver savings to business. The Rules will be reviewed within 5 years after they come into force on 06 April 2019. Should it be decided that the legislation is no longer fit for purpose following this review; the legislation will be amended accordingly.

15. Contact

- 15.1 Mike Chapman at the Insolvency Service telephone: 020 7291 6765 or email: mike.chapman@insolvency.gsi.gov.uk can be contacted with any queries regarding the instrument.
- 15.2 Dean Beale, Director of Strategy & Change at the Insolvency Service telephone: 020 7291 6744 or email: dean.beale@insolvency.gsi.gov.uk can confirm that this Explanatory Memorandum meets the required standard.
- 15.3 Kelly Tolhurst MP, Parliamentary Under Secretary of State, Minister for Small Business, Consumers and Corporate Responsibility can confirm that this Explanatory Memorandum meets the required standard.