On Reform of the Process to Apply for Bankruptcy and Compulsory Winding Up
Introduction

ICAS regulates approximately 77% of insolvency practitioners (IPs) who take appointments in Scotland. ICAS also regulates 7 appointment taking IPs who are based in England & Wales, and one who is based overseas.

As personal insolvency in Scotland is devolved we have restricted our comments on the proposed personal bankruptcy reforms in England & Wales to generic comments. Our main focus is in relation to corporate insolvency.

We offer the following comments:

Personal bankruptcy

1. In principle ICAS supports the proposal in personal insolvency that where a debt is not in dispute there is no requirement for the courts to be involved either on the debtor’s own application or that of a third party. Care would have to be taken however to verify that there is no dispute. The Scottish system, whereby a debtor can apply directly to the Accountant in Bankruptcy (AiB) for the debtor’s own bankruptcy on payment of a non-refundable fee of £100, works well. It would seem that a similar process could be effected in E&W with the application being made direct to the Official Receiver who would have responsibility for administering the bankruptcy and for retaining documents for inspection for specified periods.

2. Where a creditor or third party can demonstrate that the debt is not in dispute and the debt is below a specified threshold there should be provision for that party to apply to the Official Receiver in a similar manner as a debtor can do on his own application under 1 above. It would not be sufficient for the creditor to state that the debtor had not submitted any objection to the debt since the “ostrich” syndrome is well documented and debtors will frequently not respond to correspondence about debt.

3. An action by a creditor for recovery of a debt is not a process consented to by the debtor. ICAS is of the view that creditor applications, in circumstances in which there is no written acknowledgement from the debtor that the debt is due, should proceed through the courts and that there is merit in continuing to require that the applicant should prove to the court that the debt is due. The applicant should be required to demonstrate what steps have been taken to recover the debt. Where the debtor has not confirmed the debt in writing we believe that only the court should have the discretion to decide on whether or not bankruptcy should be awarded.

4. We are concerned about the possibility of further debt being incurred if the debtor is permitted to pay by instalments but cannot have his bankruptcy application granted until the whole payment has been made. In addition the issues identified in circumstances in which the debtor either changes his mind or is unable to meet all the instalments could be avoided if the debtor was required to wait until he is in a position to make full payment before applying for bankruptcy.

5. ICAS is also concerned at the proposal that debtor applications can be made electronically. What safeguards are to be implemented in debtor applications to ensure that it is the debtor who is applying and that what he asserts is true? In addition the government should be endeavouring to ensure that debtors have sought appropriate advice prior to taking such a significant decision, how will this be achieved with electronic applications?

6. ICAS does not believe that it is reasonable to assume that most businesses have access to a computer and the internet. There are large numbers of micro businesses that do not have such
access and which would be reluctant or unable to pay for a third party to act for them. Postal applications must be allowed.

7. Where more than 4 months has elapsed from the date of serving a statutory demand the creditor should be required to re-serve it before making an application for bankruptcy.

**Corporate insolvency in Scotland**

8. The system of applying to the court for the winding up of companies in Scotland has not in our view been demonstrated to be a great burden on the courts. The structure is in place and it would seem unnecessary to consider setting up a new body to deal with applications for winding up companies in Scotland. It is suggested that BIS should make enquiries of the Scottish Courts to assess the extent of court time to inform on the merits of maintaining the status quo in Scotland.

9. ICAS takes the view that all creditor petitions should be submitted to court for the reasons stated in the following paragraphs. Our responses are primarily predicated on this stance.

**Question 26**

*Do you think a third party applicant should be able to request to withdraw its application at any time up to the point at which it is determined?*

10. Yes. Creditors ought to be allowed to retain control over documents that they have served. There can be many reasons for not wishing to proceed.

**Question 28**

*How important is it for the reforms proposed in this document that there is a Liquidator of Last Resort for Scotland?*

11. Given the current insolvency processes for winding up a company in Scotland, it is our view that it is not essential for there to be a Liquidator of Last Resort (“LLR”) in Scotland.

12. The reasons for the proposal to introduce a LLR in Scotland are not specifically stated in the consultation document but we assume that it may be deemed to be in the public interest for all insolvent companies to be subject to investigation as part of a formal insolvency process. There appears to be no suggestion that the proposals are aimed at improving recoveries for creditors from insolvent companies which sought to avoid a formal liquidation process.

13. The current proposals appear to suggest that, if they were applied to Scotland, then the LLR would be automatically appointed by an Adjudicator in all liquidations irrespective of whether or not the debtor company has any assets.

14. At present in Scotland if a debtor company is known to have assets then a creditor can petition the Court for the company to be wound up in the hope of recovering some of the debt but also in the knowledge that the company’s affairs and directors’ conduct will be investigated by an experienced insolvency practitioner as part of the insolvency process. The creditor will, therefore, seek to appoint an insolvency practitioner of their choosing to act as Liquidator of the company and the creditor will know that they will not incur any further costs relating to the winding up. It is our view that this current procedure works well and we see no obvious reason for change.

15. In the case of debtor companies which have no assets creditors will not normally petition as formal liquidation cannot be funded. Many of these companies will apply to the Registrar of Companies to be struck off and dissolved in terms of section 1003 of the Companies Act 2006. There is a requirement for the application to be notified to all creditors who can then object and if appropriate seek that the company is wound up.
16. In such circumstances, as stated above, it would be unusual for a creditor to petition the court for the company to be wound up. The general exception to this is HMRC where, if it considers a formal liquidation to be in the public interest, then HMRC will agree to underwrite the costs of the liquidation. In such cases the company’s affairs and directors conduct will be subject to investigation. We would suggest that an exercise be carried out to establish from the Registrar of Companies the number of objections raised to section 1003 applications and the extent to which such objections are lodged by HMRC.

17. There are companies struck off and dissolved under section 1003 which are insolvent but where no objection was lodged but the extent to which all these require to be investigated is open to debate. If the Scotland Bill is passed in its current form and compulsory winding up in Scotland is re-reserved to Westminster then the consultation proposals would mean that creditors could apply to wind up companies with no assets thereby requiring the public purse to fund the liquidation. This could lead to a raft of applications which would be a significant increased burden on the public purse. This would not only be for the cost of the winding up but possibly also costs falling on the Insolvency Service Disqualification Unit who could potentially be getting significantly more directors conduct reports to deal with at a time when their resources appear to be extremely stretched.

18. It is our view that unless there is evidence to suggest that there is an urgent need for an investigation to be carried out into the company’s affairs it would appear that the proposals would give rise to unnecessary cost to taxpayers. Consequently any LLR should deal only with cases where a legitimate and urgent need to investigate a company’s affairs can be demonstrated (eg known transfer of business and assets to “phoenix” company).

19. It is our view that an exercise is required to quantify the numbers of companies that simply stop trading, to establish the value of available assets and the extent of liability of those companies, and the extent to which creditors object to applications by companies for voluntary dissolution and striking off.

20. The Registrar of Companies is in a unique position to be able to monitor companies that perhaps should be liquidated rather than being struck off. We are not aware whether or not any checks are carried out by the Registrar of Companies to ascertain whether in effect liabilities are being avoided since the application for striking off does not require any current financial information to be provided. It is our view that consideration should be given to increasing the requirements for voluntary striking off applications to include a current financial statement or statement of affairs for the company in order to assess if there are any grounds for objecting to the application and further investigation being merited.

21. It is our current view, however, that there may be a limited number of cases in Scotland where a LLR would be required but it is questionable whether the number would justify the cost of setting up a separate body with the required expertise. If there are cases where investigation of a company’s affairs is merited than the Insolvency Service could appoint an experienced insolvency practitioner to act as Liquidator, as is the case in certain circumstances at present.

**Question 29**
*If you think that it is important that there is a Liquidator of Last Resort, which organisation do you think should provide that office and how should it be funded?*

22. If a Liquidator of Last Resort is required there is no obvious existing organisation in Scotland which could fulfil the role. Consideration could be given to an arrangement whereby the Insolvency Service would operate a panel of IP firms engaged on a structured fee basis to deal with such cases, thereby curtailing the cost to the public purse.
Question 30
Do you think that the Adjudicator’s role should be limited to determining applications for winding up on the grounds that the company is unable to pay its debts or where the company has passed a valid special resolution that it be wound up? If not, would you please explain your reasoning.

23. It is our view that all creditor petitions should be presented through the Court where the experience and knowledge to deal with matters of potential dispute and conflict is already available.

24. The experience in Scotland is that before presenting a winding up petition to Court including seeking settlement proposals from the debtor a creditor will have largely exhausted all other avenues for trying to recover the debt. Also the winding up petition will normally proceed on the basis of an expired charge for payment (following a court decree) or an expired statutory demand and so by that time the debtor will have had ample opportunity to either make acceptable settlement proposals or to dispute the debt. As a result the role of the proposed Adjudicator to try to facilitate an agreement between the debtor and creditor is considered to be unnecessary.

25. We also have concerns about how quickly the process for creditor applications could be progressed by an Adjudicator and how easily the debtor company could seek to delay matters by disputing the application. This could cause a particular problem if the creditor was concerned about the possible dissipation of assets and was seeking the appointment of a Provisional Liquidator – in this case it appears the matter would end up in Court anyway so the Adjudicator may end up being an unnecessary additional step in the process. This, however, may be an area where the Law Society of Scotland may be better placed to comment.

26. As regards reducing the Court’s involvement, the system of applying to the court for the winding up of companies in Scotland has not in our view been demonstrated to be a great burden on the courts. The structure is in place and it would seem unnecessary to consider setting up a new body to deal with applications for winding up companies in Scotland. It is suggested that the Insolvency Service should make enquiries of the Scottish Courts to assess the extent of court time spent dealing with winding up petitions to inform the merits of maintaining the status quo in Scotland.

27. If it were shown that there was an onerous burden on the Courts in dealing with winding up petitions then there could be an argument for non – contentious applications (by directors / company) to go through the proposed Adjudicator route but that all contentious (creditor petitions) should still go through the Court - this would largely mirror the current position as regards sequestrations with debtor applications being submitted to the Accountant in Bankruptcy but creditor petitions to the Court.

Question 31
Are you able to suggest the proportion of petitions that are currently presented to the courts on grounds other than the company’s inability to pay its debts; the company having passed a valid special resolution that it be wound up; and that winding up is just and equitable?

28. We do not have access to this information. The information on the extent to which winding up petitions in Scotland presented to the Court are not based on the company’s inability to pay its debts should be obtained from the Courts. We believe, based on anecdotal evidence, that the number of such petitions represents a very small proportion of the total number of winding up petitions presented.
Question 32
Who do you think should be responsible for communicating notice of the winding up application to the company and eliciting its response to the proceedings?

29. It is our view that, as presently is the case, the creditor should be responsible for communicating the notice of the winding up application to the company. As previously mentioned it is our view that in Scotland a creditor will have exhausted all other options for recovering the debt prior to submitting a winding up petition and, providing there is evidence that the debtor company has been made aware of the application (which in our view should be through service by Sheriff Officers), they should not then have a responsibility to elicit a response from the debtor company. It may be that an Adjudicator could seek to obtain such a response but not at the cost of the creditor being unable to proceed with the application within any agreed statutory timescale.

Question 33
Who should send notice to specified interested parties?

30. It is our view that the creditor should be responsible for communicating notice of the winding up application to interested parties. If an Adjudicator is in office notice could include sending a certified true copy of the application to the Adjudicator. This mirrors the current arrangement for sequestrations in Scotland where a copy of the creditor petition requires to be sent to the Accountant in Bankruptcy.

Question 34
When should notice be sent to these interested parties?

31. It is our view that the notice should be sent to all interested parties within two working days of the communication of the winding up application to the debtor company.

Question 35
Do you think that a winding up application should be advertised under these new proposals? If yes, please provide reasons for your answer.

32. It is our view that a winding up application should be advertised as at present. It is accepted that the advertising of an application could have a detrimental effect on a company but the instruction to advertise by the Court will only occur after it is satisfied that the creditor is legally entitled to present the winding up application (i.e there is a genuine debt due to the creditor). As a result in most cases the directors of the debtor company will already have had ample opportunity to resolve matters long before the stage of advertising a winding up application is reached. If the requirement to advertise were withdrawn then other creditors of the company may be continuing to supply unaware of the possible liquidation and this could potentially leave them with an increased irrecoverable debt – by advertising the application such suppliers would at least get the opportunity to make their own commercial decisions on whether or not to continue to supply the company.

33. In addition the knowledge that a winding up application will be advertised may act as an incentive for directors, who wish to retain their company, to pay their debts.

Question 36
Can you foresee any circumstances in which it would be appropriate for the Adjudicator to seek further information from the applicant? If yes, please provide details and suggest how frequently this might occur.

34. Where an Adjudicator is in office there may be circumstances where the information provided by the applicant is incomplete and so any missing information may be requested but we are not able to comment on the frequency in which such circumstances may arise.
Question 37
What period of time should be sufficient for a company to communicate to the Adjudicator its opposition? 14 days? More? Or less?

35. At present a company has eight days after a winding up petition has been advertised to lodge answers in Court regarding the winding up and it is our view that, given the serious nature of the creditor action, that this timescale should be sufficient for any diligent director to take appropriate action to dispute the debt or contact the creditor to make settlement proposals.

Question 38
Do you think that a creditor should be able to request to withdraw its application at any time up to the point at which it is determined?

36. Yes – this is currently the position where a creditor can ask the Court to dismiss the petition if payment has been received, or if it has become apparent that the debtor company has no assets and the creditor does not wish to incur further cost in pursuing the debt.

Question 39
Should any appeal against the decision of the Adjudicator be made in the first instance to the county court, or is there a benefit in retaining the existing provision that allows an appeal to be made in the first instance, in certain circumstances, to the High Court?

37. Where an Adjudicator is in office if there is any appeal against the Adjudicator’s decision then that should be made to the Sheriff Court or, in the case where the debtor company’s share capital is £120,000 or more, to the Court of Session.

Conclusion

In the past 3 to 5 years the Scottish Courts have developed improved systems for handling liquidations, a number of Sheriffs now specialise in insolvency and provision has been made so that certain cases are heard by the commercial courts. We are firmly of the view that petitions at the instance of creditors require to be considered by the courts as only then can it be demonstrated that matters have been given detailed consideration at an appropriate level of expertise. If creditor petitions were removed from the courts the degree of investment made by the justiciary would be wasted. The court system in Scotland for corporate insolvency works well and we can see no justification for changing it.

We have not seen any evidence to support the need for a Liquidator of Last Resort in Scotland. We believe that where companies that do not have any assets require, in the public interest, to be liquidated then the most appropriate and cost effective way of achieving this is for an insolvency practitioner to be appointed funded by the State.

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