PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT

Fifteenth Delegated Legislation Committee

DRAFT INSOLVENCY (AMENDMENT) (EU EXIT) REGULATIONS 2018

Thursday 24 January 2019

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Monday 28 January 2019

The Committee consisted of the following Members:

Chair: James Gray

Clwyd, Ann *(Cynon Valley)* (Lab)
† Cowan, Ronnie *(Inverclyde)* (SNP)
Coyle, Neil *(Bermondsey and Old Southwark)* (Lab)
† Esterson, Bill *(Sefton Central)* (Lab)
† Hall, Luke *(Thornbury and Yate)* (Con)
† Harris, Rebecca *(Lord Commissioner of Her Majesty's Treasury)*
† Masterton, Paul *(East Renfrewshire)* (Con)
† Morris, David *(Morecambe and Lunesdale)* (Con)
† O'Brien, Neil *(Harborough)* (Con)
† Perkins, Toby *(Chesterfield)* (Lab)
† Robinson, Mary *(Cheadle)* (Con)
† Smith, Nick *(Blaenau Gwent)* (Lab)
† Tolhurst, Kelly *(Parliamentary Under-Secretary of State for Business, Energy and Industrial Strategy)*
† Turley, Anna *(Redcar)* (Lab/Co-op)
† Warman, Matt *(Boston and Skegness)* (Con)
† Williamson, Gavin *(Secretary of State for Defence)*
† Wragg, Mr William *(Hazel Grove)* (Con)

Kevin Candy, Robert Cope, *Committee Clerks*

† attended the Committee

Fifteenth Delegated Legislation Committee

Thursday 24 January 2019

[JAMES GRAY *in the Chair*]

Draft Insolvency (Amendment) (EU Exit) Regulations 2018

11.30 am

The Parliamentary Under-Secretary of State for Business, Energy and Industrial Strategy (Kelly Tolhurst): I beg to move,

That the Committee has considered the draft Insolvency (Amendment) (EU Exit) Regulations 2018.

It is a pleasure to serve under your chairmanship, Mr Gray. The regulations, which were laid before the House on 19 November 2018, address issues in UK insolvency law that will arise in the event that we leave the European Union without a deal. Cross-border insolvency is an area in which, as legal and insolvency professionals in the private sector have rightly and firmly pointed out, the EU system is greatly beneficial. If we are to ensure the best outcomes for all parties involved, it is important that insolvencies are dealt with as expediently as possible. The sooner a business in distress is dealt with, the more likely it is that it can be saved. When that is not possible, the simpler and clearer the insolvency process is, the more likely it is that the assets will be realised efficiently and money returned to creditors.

EU law achieves that goal by providing a framework for mutual cross-border co-operation on insolvency matters through the EU insolvency regulation. That is based on main proceedings in a single member state, eliminating the need to start proceedings in other member states where there may be assets to deal with. It is in the interests of both the UK and the EU to retain that system, and the Government have been clear, with the support of the UK insolvency sector, that we wish to continue it. However, it would be irresponsible of us to not plan for all possible outcomes, including leaving the EU without a deal. We have laid this instrument before the House to ensure that the UK's insolvency regime continues to function effectively after exit day even if we leave the EU without a deal.

As I have already suggested, the EU insolvency regulation ensures that member states automatically recognise an insolvency order made in an EU country. That helps the insolvency practitioner dealing with the case to recover assets as quickly as possible and return as much money as possible to creditors. However, EU law also contains a provision to ensure co-operation between all the different parties in an insolvency, including insolvency practitioners and courts in different member states where necessary. It ensures that individual member states' own laws are respected. For those protections to operate, they must apply to everyone. Unfortunately, once we leave the EU, that will not be the case in the UK.

As we leave the EU, the European Union (Withdrawal) Act 2018 will retain a version of the EU regulation in UK law, but the safeguards that the regulation provides will no longer operate correctly: as the UK will no longer be a member state, the remaining member states will no longer be bound to recognise our insolvency proceedings or co-operate with us. While office holders in insolvency cases originating from EU member states could make use of the UK's retained EU insolvency regulation to lay claim to assets here, they would not necessarily be bound by the EU regulation rules when dealing with those assets in EU states, nor would they be bound by EU rules to recognise the claims of UK creditors.

Senior members of the insolvency professional sector have argued that reciprocity is an essential part of continuing with this legislation. Without a deal, it is vital that we do not continue indefinitely to apply EU rules that could override our own laws and prevent us from dealing effectively with insolvencies in the UK. To reflect that, the instrument repeals the majority of the EU insolvency regulation, keeping only the small part necessary to make sure we do not lose any existing rights to open insolvency proceedings in the UK. We are retaining the categories of proceedings under the EU insolvency regulation to assist the acceptance of UK insolvencies in EU countries in future, continuing with concepts and language that the courts in the EU will recognise.

The instrument continues to apply the current EU laws to existing cases in which main insolvency proceedings are already open on exit day, but as a safeguard for those existing cases, since we cannot assume that the EU member states will continue to apply the same rules where the UK is concerned, the courts may disapply the EU rules where they lead to a different outcome than would have been the case before we left, and where that prejudices creditors or others with an interest in an insolvency. In such cases, the court will be allowed instead to apply the powers in the UK's Cross-Border Insolvency Regulations 2006 or to make some other appropriate order to resolve the situation.

That brings me to the concerns raised by the Joint Committee on Statutory Instruments. It has suggested that these saving provisions lack clarity, are defectively drafted and make unexpected use of the powers in the European Union (Withdrawal) Act 2018. Officials have worked closely with the JCSI to explain why it is necessary that the courts have a broad power, rather than something narrower. Detailed examples were provided to the JCSI to demonstrate some of the many different situations in which the power might be needed. In its report, the JCSI commented that those examples were helpful, and it expressed its gratitude.

These situations can be complex. For example, suppose that the main insolvency proceedings are opened against a company before exit day in another EU member state. They will be governed by the EU insolvency regulation. One of the requirements of that regulation is that an insolvency practitioner who is dealing with the case must inform EU creditors as soon as the insolvency proceedings are commenced. The regulation also says that the notice should provide the creditors with details of how to make a claim. That is important as there can be time limits on making claims in insolvency. However, after exit day the requirement to provide notice of the insolvency will no longer apply to UK creditors, because the requirement is limited to those creditors in member states and the UK will no longer be an EU member state after exit day. In consequence, UK creditors may not find out about the existence of an insolvency proceeding

in time to make valid claims, and if nothing is done their claims may be rejected. At the same time, the insolvency practitioner would be permitted—under the retained version of the EU insolvency regulation that the withdrawal Act will include in our UK law—to seize any of the company's assets here in the UK to repay creditors who have made valid claims. That is clearly unacceptable.

Under the proposed amendment in these regulations, the court can consider that the interests of UK creditors are being materially prejudiced, and make an appropriate order as it sees fit. For example, it could freeze the company's UK bank account until the office-holder accepts the UK creditors' claims. I think we can all agree that that would be a fair and just outcome.

Further examples were included within the JCSI's published report. The provisions provide the court with the necessary discretion to deal with scenarios such as that, and other unexpected outcomes from the interaction of UK insolvency law following exit with the domestic law of the remaining EU member states. As the UK cannot exercise any control over those other states' laws, a broader power for the courts to step in is both necessary and appropriate. This does not create a new power that the courts would be unfamiliar with. Insolvency law already contains similar provisions and powers for the courts in other cases where broad discretion is necessary. The power safeguards individuals and businesses who have an interest in an insolvency. It is the best way to ensure that, where they could be treated less favourably after EU exit than before we left, the courts will be able to step in.

The instrument also amends the Employment Rights Act 1996 and the Pension Schemes Act 1993, which set out protections for employees following the insolvency of their employer. The protections remain unchanged and the effect of the instrument in this area is to ensure that the current financial support given to UK-based employees when their employer in the EU becomes insolvent will continue after exit day.

In the absence of a Northern Ireland Executive, the instrument updates and makes similar changes to the law on insolvency and employment rights in Northern Ireland, on behalf of the Northern Ireland Government. That includes updating Northern Ireland employment legislation in this area, where there had been no opportunity to mirror a previous amendment made to British law in 2017. I commend the regulations to the Committee.

11.39 am

Bill Esterson (Sefton Central) (Lab): I thank the Minister for her analysis of the regulations' effects. She got quickly to the point that mutual recognition between the UK and the EU is not guaranteed if we leave with no deal. Under the terms of the withdrawal Act we would be giving one-way recognition of EU appointments and judgments. The statutory instrument would give our Government the opportunity, should they need it, to withdraw that recognition. I will tease out one or two points surrounding that intention.

People in the profession do not want the Government to have to use the power—I dare say that the Government do not want to use it either. They want the Government to secure a deal so that the existing system of mutual recognition continues, and they argue that no deal should be avoided. We often do the same in Committees such as this one, but we recognise what would happen in the event of no deal.

People in the profession have made the point to me that the Government have the power to create a level playing field for the UK profession if they are unable to obtain the deal that they are looking for. The SI is not a mechanism for maintaining the current system; it deals only with problems that could arise from not having a mutual recognition deal. I urge the Minister to take on board their point that in the event of no deal the Government should try to re-establish mutual recognition as quickly as possible so that the provisions in the SI will never be needed.

The Minister referred to the Joint Committee on Statutory Instruments' concerns about the clarity of the regulations, potential defective drafting and the fact that they deliver broad powers rather than narrow ones. She gave various examples of what could happen without the kind of mutual agreement that I referred to. I think the Joint Committee, like the Opposition, would call for every effort to be made to achieve mutual recognition as soon as possible. Can the Minister say what work has been carried out to try to establish that mutual recognition in the event of no deal? Such work is effectively what the sector is calling for.

What indications has the Minister had from the EU about its intentions to maintain the status quo and to reciprocate what she proposes in the regulations, which is that we will continue to recognise the appointments and jurisdiction of EU courts in insolvency proceedings? Has she had an indication that that arrangement will be reciprocated in the event of no deal? What discussions have her officials had with EU Governments or the Commission?

As far as I understand it, the SI enables the Government to remove automatic recognition of foreign practitioners and recognition of court decisions. We have an extremely well regarded, strong and economically successful insolvency regime in the United Kingdom, and it is important that we continue to do so. Maintaining confidence in it is extremely important to our economy as a place for businesses to come to restructure, and for creditors in insolvency cases to recover what they are due effectively and successfully. It is important that we avoid a long-term shift away from a lot of that work being based in the United Kingdom, so those guarantees from the EU are extremely important.

A point made to me by people in the profession was that some people in the insolvency profession across the continent of Europe may see an opportunity to increase the amount of work that they can obtain at the expense of the UK profession. They may not be particularly concerned about reciprocity or about getting the EU to continue mutual recognition. I urge the Minister to address that point when she answers my question about the progress made towards achieving mutual recognition.

Further to paragraph 2.10 of the explanatory memorandum, will the Minister explain the implications of the draft regulations for the Pension Protection Fund? What is changing? I did not entirely get a sense from her speech of what assurances are in place to protect employees. Sadly, in recent years there have been some very high-profile cases that have made a significant call on the fund—the BHS insolvency springs readily to mind.

[Bill Esterson]

Clearly we need to ensure that the fund is not undermined in any way, shape or form by what is happening, and that the draft regulations will protect workers in the event of a no-deal exit.

As paragraph 2.14 notes,

"the UK will no longer be an EU member State."

What are the implications for employees of companies that operate in more than one jurisdiction, or where there is foreign ownership of a UK subsidiary? That may be a relatively easy question but, again, I did not quite get a sense of the answer from the Minister's speech.

Paragraph 3.7 refers to the main thrust of the draft regulations:

"the lack of reciprocity after exit day."

That is an argument for preventing no deal at all costs, but there is real concern about the fact that we can continue to offer recognition of EU operations in insolvency but we cannot require member states to recognise UK insolvency judgments. The explanatory memorandum sets out the challenge clearly. I would be grateful if the Minister addressed exactly what progress has been made towards overcoming the lack of mutual recognition.

As ever in Delegated Legislation Committees, there are matters of consultation and impact assessment to consider. I understand that there has been informal discussion, and having spoken to people in the sector, I think it is fair to say that they are as happy as it is possible to be—in this case, if not in all cases—with what is being proposed in the event of no deal. However, they stress that the draft regulations are only a stopgap. As the insolvency body R3 stated in its 2017 Brexit recommendations, it is extremely important that a mechanism be put in place as quickly as possible that provides the same benefits as the European insolvency regulation and the recast Brussels regulation.

R3 also noted how much money is recovered as a result of UK insolvency actions. One of its case studies was Nortel, which entered insolvency proceedings in 2009. A total of £1.5 billion was returned to creditors as a result of the work carried out by insolvency practitioners and their agents, where the insolvency was based in the UK. That compares with a total of £4 billion a year returned to creditors in the UK, including to the UK Government through HMRC. I therefore find it quite remarkable that the Government say there is no business impact worthy of an impact assessment—that they regard the impact as below the de minimis level. My calculation is that £4 billion is a little more than the £5 million de minimis level. Yet again, a regulation has a significant business impact but the Government do not carry out an impact assessment.

I will not go through the entire way in which the EU carries out its impact assessments; it does things rather differently. Those of the Committee who were here on Monday will have heard me read them out on that occasion. It is on the record and I do not need to do it again. The Minister may refer to it and I would have hoped she would have done so before today's meeting.

Nick Smith (Blaenau Gwent) (Lab): Definitely don't want to go through that again.

Bill Esterson: My dear and hon. Friend the Whip is extremely grateful that I will not repeat myself in full. The point is that the EU looks at the wider impact on the economy of similar regulations when the EU implements them. The Government's very narrow interpretation of an impact assessment is shown in all its inadequacy by the comparison of that £4 billion per year with the £5 million de minimis level.

We will not oppose the statutory instrument; the Minister has given satisfactory answers, including to the concerns raised by Joint Committee on Statutory Instruments. We must hope that we do not end up having to apply this instrument or numerous other regulations we have dealt with recently; I know the Minister shares that hope. I await with interest her response, in particular on the work that is going on to ensure that mutual recognition carries on as seamlessly as possible, to support the very important part of our economy that is our insolvency sector.

11.52 am

Kelly Tolhurst: I thank the hon. Member for Sefton Central for his comments and contribution to the debate. We remain optimistic about reaching a deal of mutual benefit to the UK and the EU, but it is important to maintain our regulatory and legislative framework for dealing with insolvency should we leave without a deal. That is why we introduced this instrument.

The Department has consulted with the profession and spoken to some of the groups to try to ensure that that the statutory instrument will work as well as possible. Obviously, we have consulted R3, which the hon. Gentleman mentioned. As I outlined, we are very much focused on delivering a deal.

The hon. Gentleman is quite right that the statutory instrument relates entirely to things happening in the UK, but does not enable us to have any influence on or dictate to EU member states how they treat UK orders in the event of no deal.

Bill Esterson *indicated assent.*

Kelly Tolhurst: I see the hon. Gentleman understands that point.

As the hon. Gentleman will know, in what we have laid out as our future economic relationship in a deal, our focus is on ensuring that we are able to deal with mutual recognition and reciprocal status going forward if a deal is to be had. We recognise, with the profession, that if we can come to an agreement in this area in a deal situation, that would be in everyone's best interest. With a deal, we would continue our civil judicial co-operation, including on cross-border insolvency. That is in the best interests of both the UK and the EU, as he outlined. However, it is not possible for us to unilaterally continue with the co-operation on cross-border insolvencies; we can achieve the benefits that both sides currently enjoy only through a mutual recognition agreement with the EU. The declaration on the future relationship was clear that it would include wide-ranging agreements on trade, including trade in professional and business services and the framework necessary to support that.

We will continue in those endeavours, but this SI is intended to ensure that, in a no-deal situation, UK law provides clarity for the profession and that we are able

to operate on day one. After that date, it would be down to us to bring any further changes to our insolvency regulations that are not in the scope of the draft regulation to the House, as we see fit. After leaving, there may be things that come up that we might need to change, but that would be done in the course of standard business.

Regarding the hon. Gentleman's concerns about the Pension Protection Fund, I assure the Committee that the Prime Minister and the Government have been clear that we will not row back on workers' rights through the withdrawal Act. Employees living and working in the UK for a company registered here or in the EU will continue to receive redundancy-related payments from the national insurance fund where their insolvent employer cannot make them, as they do now. The draft regulations ensure that the law in this area is clear and can operate correctly when we are no longer an EU member state. One of the limitations is that within this SI we cannot guarantee for workers in EU states, how EU member states will deal with the employees working in those states. What we can do, as laid out in this SI, is to ensure that people working in the UK, be it for EU companies operating in the UK or UK companies, will still have those protections as they are now for UK workers.

On the hon. Gentleman's questions about the impact assessment, we have been in this situation many times over recent months and I know it is a particular concern for him. However, for this particular SI we have assessed the direct cost of to business in terms of the costs of insolvency and have estimated that the direct cost would be £2.7 million, due to the extra costs that may arise when practitioners need to open cases in EU member states, which they do not currently have to do under EU regulations.

Nick Smith: I do not know whether this is the case, but if there is a no-deal Brexit, will EU-based employers pay the levy into the Pension Protection Fund?

Kelly Tolhurst: EU member states will be operating under the current EU regulations as they stand, according to how they have implemented those rules in their own states. We currently submit to the levy here, so workers in the UK, whatever their nationality, will still be entitled to all of the same protections and benefits that exist today. With regard to how individual member states implement the EU regulation, we cannot guarantee how they will interpret a UK no-deal situation. We hope EU member states will treat all UK workers in the same way as we will treat people working in the UK, but that is something we cannot dictate. Does that give some clarity?

Nick Smith: No, the Minister did not absolutely clear up the matter for me. Will she check whether EU-based employers will continue to pay the levy into the pension protection fund on behalf of UK employees should we leave without agreement?

Kelly Tolhurst: I apologise if I was not clear. Perhaps I was trying to explain the matter in a more complicated way. Yes, they will all pay the PPF levy. I was simply trying to highlight that we here can expressly say we are making sure that all people working in the UK, no matter what their nationality, will be afforded all protections. What we do not have any control over is future changes that might occur in other member states and in EU regulations in a no-deal situation. At that point we will be regarded as a third country, but under the current regulations they will still pay into the fund.

The changes proposed in the draft regulation go some way to protecting the UK insolvency market in the event of a no deal. They ensure that citizens, businesses and the insolvency profession will not be disadvantaged by unilaterally retaining EU rules when reciprocal and necessary safeguards would not be guaranteed by the EU. The proposed changes provide certainty and clarity regarding cross-border insolvency cases with the EU following exit.

The regulations also ensure that protections for UK employees of insolvent employers are maintained after the UK exits the EU: something we all agree is vital. The instrument is essential to repeal the majority of EU insolvency regulations from UK law and to retain the status quo for employment rights in the UK. I hope I have been able to answer all the questions and I commend the regulations to the Committee.

Question put and agreed to.

Resolved,

That the Committee has considered the draft Insolvency (Amendment) (EU Exit) Regulations 2018.

12.3 pm

Committee rose.