

Response to Consultation on Insolvency changes for Payment and Electronic Money Institutions (January 2021)

This response is provided by a working group of the Centre for Commercial Law at the University of Aberdeen. The working group consists of Dr Alisdair MacPherson, Mrs Donna McKenzie Skene and Dr Burcu Yüksel Ripley.

General Comments

We are pleased to respond to this consultation. We agree that there is merit in making the proposed changes as soon as possible, rather than awaiting the conclusion of the Payments Landscape Review. However, the changes covered by this consultation should also be considered as part of that wider review, to determine whether further changes require to be made and to make sure that this area joins up appropriately with other reforms proposed as part of the review. For example, there are connections with the content of the recent Call for Evidence on Access to Cash (to which we also provided a response).

We note that particularities of Scots law do not appear to have been fully taken into account in the changes proposed in the consultation. Given that the proposals would also apply in Scotland, we believe that it is necessary to address the issues regarding Scots law that we refer to below.

Question 1 – Do you have any comments on the proposal to introduce a Special Administration Regime for Electronic Money and Payment Institutions?

We support the proposal to introduce a Special Administration Regime for Electronic Money and Payment Institutions. We agree that it is appropriate to deal with these institutions in a similar way to investment banks, which set a precedent that can be followed. It is sensible to use a modified version of the regime for investment banks as a model here. However, in practical terms, a set of regulations with the provisions included in full would be preferable to an abbreviated version only showing the modifications of the other regime.

Other aspects of the proposed Special Administration Regime, such as the suggested objectives, appear reasonable.

Question 2 – Do you have any comments on the proposed distribution principles?

We agree with the indicated pro rata approach to treatment of shortfalls. This is easily understandable and seems the most straightforward way of dealing with the matter.

In terms of bar dates, we support the notion that the special administrator would have some discretion regarding setting deadlines. However, we consider that there is some merit in specifying a minimum time period that the deadline must comply with (i.e. the deadline set by the special administrator could not be sooner than this time period). A minimum time period would provide an extra element of fairness to the reasonableness test, avoid deadlines that are difficult to meet and give an initial element of notice to customers (including consumers).

Question 3 – Do you have any comments on the proposed transfer provisions?

The proposed transfer provisions seem reasonable. We are not aware of any significant difficulties with respect to the novation of contracts or other transfer issues in the context of investment banks (post-2016 review). Again, this is an example of an advantage of drawing upon and modifying an existing regime.

Question 4 – Do you have any comments on the proposal to extend the remaining provisions of Part 24 of FSMA to Electronic Money and Payment Institutions?

We note that reference is made to the FCA having the power to participate in proceedings for trust deeds for creditors in Scotland. However, there are other respects in which there is need for more attention to be paid to particular aspects of Scots law (which differ from the rest of the UK).

In relation to bankruptcy, there is no mention of sequestration (which is the Scots law version of bankruptcy) at paras 5.10-5.11 of the consultation paper. Sequestration is principally provided for by the Bankruptcy (Scotland) Act 2016. We note that ss 372-374 of the Financial Services and Markets Act 2000 do refer to sequestration and the 2016 Act and such references should be applied to Electronic Money and Payment Institutions too.

The proposal at para 5.12 appears to exclude the possibility of the FCA applying to set aside transactions to defraud creditors under Scots law. The reference seems to be to s 423 of the Insolvency Act 1986, although this is not specifically mentioned, which applies only to England and Wales. We note that FSMA 2000, s 375, refers only to s 423 of the 1986 Act and the equivalent provision for Northern Ireland under the Insolvency (Northern Ireland) Order 1989. Consideration should be given as to whether the FCA ought to have an equivalent power to apply for the setting aside of relevant transactions under Scots law. The closest equivalent to s 423 under Scots law is provided for by the common law. However, it may be worthwhile to assess whether the FCA should be able to utilise ss 242 and 243 of the Insolvency Act 1986 for Scots law (and also ss 238 and 239 in relation to England and Wales). Reforms along these lines may be desirable.

Additional Comments

In Annex A of the consultation paper, “insolvency rules” are defined in Reg 4 as “rules made under section 411 of the IA 1986 as applied and modified by regulation”. This excludes individual insolvency rules for England and Wales (see s 412 of the 1986 Act). It also excludes rules for non-corporate insolvency in Scotland, which means that the rules for partnerships and trusts in Scotland (as well as for individuals) are excluded. Trust estates and partnerships are dealt with using sequestration in Scots law (rather than corporate insolvency processes). As such, if it is intended that the provisions should apply to these forms of business vehicle, the definition should be amended.

More broadly, given that para B.20 of Annex B indicates that the Regulations will apply to partnerships, there is a need for reference to be made to the Bankruptcy (Scotland) Act 2016 and other provisions applicable to partnerships in Scots law. These references are also necessary if trusts in Scots law are to be fully included.

With respect to Annex C (Supplementary Annex), there are references throughout to specific rules within the Investment Bank SAR Rules. The numbered rules referred to are the rules for England and Wales. For Scotland, there are different rules (Investment Bank Special Administration (Scotland) Rules 2011/2262) and the rule numbers do not match up directly with the rules for England and Wales. As per para C.5.1, we are aware that there are ongoing discussions with the devolved administrations

of Scotland and Northern Ireland. However, if there are to be specific rules for Scotland and reference is to be made to the equivalent investment bank rules, the references should be to the Scottish rules.

Also in Annex C, at paras C.20 and C.22.1, we note that there is a suggestion that trust assets cannot be subject to a security interest. However, in some circumstances, such assets can be encumbered by security rights e.g. if trust property is expressly identified as the security property by the trustees in a transaction.

We note that there are some problems with the Investment Bank Special Administration Regulations 2011 as regards Scots law. Regulation 2(2) refers to the definition of “fixed security” in s 47(1) of the Bankruptcy and Diligence etc (Scotland) Act 2007. However, s 47 of the 2007 Act is not yet in force and will now probably never be introduced. Instead, a reference should be made to the definition of fixed security in s 70 of the Insolvency Act 1986 (or even to the equivalent definition in s 486 of the Companies Act 1985, which is also still in force).

Regulation 24 of the 2011 Regulations deals with limited liability partnerships and applies Sch 3; however, the Schedule only refers to the Limited Liability Partnerships Regulations 2001. It would seem that it should also refer to the Limited Liability Partnerships (Scotland) Regulations 2001, given that the 2011 Regulations are intended to apply to Scottish LLPs too.

Regulation 25 of the 2011 Regulations provides that Sch 4 applies where an investment bank is formed as a partnership but that the regulation does not apply to partnerships constituted under the law of Scotland. That is understandable because Sch 4 relates to the Insolvent Partnerships Order 1994, which does not apply in Scotland. However, it seems to us that for Scottish partnerships, there should be equivalent provisions for Scots law which refer to, inter alia, the Bankruptcy (Scotland) Act 2016.