Guide to Personal Insolvency

Maximise your potential

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Personal Insolvency

If an individual ("the debtor") is unable to pay his or her debts when they fall due they can be described as insolvent. The debtor may want to consider one of the following options to help resolve their financial difficulties and deal with the claims of their creditors.

We are able to assist debtors in deciding which, if any, of the procedures best suits their circumstances.

Options

Individual Voluntary Arrangement (IVA)

An IVA is an alternative to bankruptcy and it can give the debtor more control over his/her assets than bankruptcy. It is a legally binding contract between the debtor and his/her creditors. The terms of an IVA may be flexible, but creditors do expect their prospects of recovering money to be at least as good as in a bankruptcy. Creditors will expect the arrangement to contain sanctions (such as a right to bankrupt the debtor) if the debtor does not fulfil his/her part of the IVA..

An IVA usually results in the debtor paying contributions to a Supervisor over a period of five years. Alternatively, sometimes an agreement can be reached for a one off payment, for example from a third party, which facilitates a much shorter period of arrangement.

We are able to assist debtors with IVAs. Further information is available in our Guide to Individual Voluntary Arrangements which is on our website.

Bankruptcy

Bankruptcy may be suitable for a debtor who cannot pay back his/her debts in a reasonable period of time. The debtor or his/her creditors can petition for bankruptcy. Once a debtor is declared bankrupt a trustee in bankruptcy realises the debtor's assets and deals with the debtor's creditors. The debtor may be required to pay over surplus income to his/her trustee for a period of 3 years. Bankruptcy normally lasts for a period of 12 months and during this time there are certain restrictions on the debtor.
□As licensed Insolvency Practitioners we are qualified to act as trustees, although, a debtor has no influence over who is appointed as their trustee as this is for the official receiver or creditors to decide.

Further information is available at www.gov.uk/bankruptcy

Advantages / Disadvantages of IVAs

The main advantages of an IVA are:

- It is a legally binding agreement between the debtor and his/her creditors. The debtor may not be required to pay his/her creditors in full and will be discharged from their liabilities at the end of the arrangement provided that he/she has complied with the terms of the IVA
- It can give the debtor more control over what happens to his/her assets. For example, it may be possible to agree that the debtor's home is excluded from the arrangement
- If the debtor runs a business or is a company director he/she is likely to be able to continue to trade
- Creditors and debt collection agencies will usually stop contacting the debtor shortly after the IVA is approved and will deal with the supervisor
- There are some occupations such as accountants, police officers and certain public offices where a bankrupt might lose their employment, however, the employer or professional body will usually accept the debtor continuing in employment whilst subject to an IVA

The main disadvantages of an IVA are:

- If the debtor does not or cannot comply the terms of the IVA the supervisor of the arrangement may have to take action that could result in the debtor being made bankrupt
- If an IVA is not approved then creditors can continue to pursue the debtor and this may result in a creditor petitioning for the bankruptcy of the debtor
- The debtor is likely to be required to pay a fee to cover the cost of the initial advice and the work that the nominee undertakes. If the IVA is not approved the fee will not be refunded
- The duration of an IVA is typically five years.It can be difficult to predict what might happen during this time. If circumstances change the debtor may not be able continue to comply with the terms of the IVA. If it is not possible to agree a variation with the creditors then the supervisor may have to petition for the debtor's bankruptcy
- Whilst the debtor may be able to agree with his/her creditors that their home will be excluded from the arrangement, creditors may require that the debtor remortgages his/her property and pay over this sum for the benefit of creditors. If the debtor is not able to do this or cannot afford the increased mortgage payments then he/she may lose their home.

- Debtors who rent their home they may find that the tenancy can be terminated when a debtor enters into an IVA. However, the landlord may chose not to exercise this right especially if rental payments are up to date

- There is a central register of IVAs that can be searched by anyone. The debtor's credit rating is likely to be affected for six years and the debtor's ability to obtain credit, even after an IVA has been successfully concluded, will be impaired

- The debtor's bank may not allow the debtor to continue to operate their existing bank account and may require them to open a basic bank account without credit facilities

- If the debtor inherits or benefits from any other windfall during the IVA then normally the supervisor will claim that for the benefit of creditors.

Advantages / Disadvantages of Bankruptcy

The main advantages of bankruptcy are:

- Once the debtor is discharged from bankruptcy it releases the debtor from most debts owed at the date of the bankruptcy order

- Creditors and debt collection agencies will usually stop contacting the debtor shortly after the bankruptcy order is made and will deal with the trustee in bankruptcy

- In most cases the debtor will receive his/her discharge from bankruptcy within 12 months

- The debtor can only be asked to contribute surplus income for a maximum period of three years whereas in an IVA this requirement is typically five years

The main disadvantages of bankruptcy are:

- The bankrupt's residential property forms part of the bankruptcy estate available to the trustee. The trustee will also claim other assets, aside from assets required for basic domestic living, for the benefit of the bankrupt's creditors

- The bankrupt will be required to pay over to the trustee surplus monthly income for a period of up to three years for the benefit of his/her creditors

- The debtor's bank account will be frozen.However, the debtor will be able to open a basic bank account

- The bankruptcy is filed at a central register that can be searched by anyone. The debtor's credit rating will be affected for six years

- A bankrupt cannot obtain credit of more than £500 without informing the lender of his/her bankruptcy

- Without leave of the court, a bankrupt cannot act as a director of a company or be involved in the management, formation or promotion of a limited company

- If the bankrupt is self-employed his/her business will normally be closed down and employees dismissed

- There may be an impact on the bankrupt's earning potential especially if the bankrupt is an accountant, police officer or holds certain public offices. A bankrupt cannot act as a trustee of a charity whilst bankrupt

- If the bankrupt inherits or benefits from any windfall during the period of bankruptcy the trustee will be entitled to claim this for the benefit of creditors

- If a debtor petitions for their own bankruptcy they will need to pay a fee to the court of £680

Other personal insolvency options

Debt relief orders (DRO)

DROs are available to debtors who; owe less than £30,000, do not have surplus income and do not own their home. Once in place creditors cannot recover their money without the court's permission and debtors are usually discharged from their debts after 12 months.

To obtain a DRO debtors need to apply through an authorised debt adviser such as the Step Change charity http://www.stepchange.org (and other providers).

Further information about DROs can be found at https://www.gov.uk/government/publications/getting-a-debt-relief-order

Administration order

An administration order is a way for a debtor to deal with debt if they have a County Court or High Court judgement against them and they cannot pay it in full. The debt must be less than £5,000. The debtor makes a monthly payment into their local court. The court will divide this money between the debtor's creditors. The creditors listed on the administration order cannot take any further action against the debtor without the court's permission.

Debt management plan (DMP)

DMPs are an agreement between the debtor and his/her creditors to pay their debts in full over period of time. It is not legally binding and it does not normally enable a debt write off.   Debtors are still liable for the full balance of their debts.

A DMP is usually used when either a debtor can only afford to pay his/her creditors a small amount each month or if a debtor has short-term financial problems but will be able to make payments within a few months.

We do not administer DMPs but the charity Step Change http://www.stepchange.org/ (and other providers) can assist people with such plans.

Further information

Please contact one of our team for more information or to discuss any financial difficulties you may be experiencing.

All our insolvency practitioners are licensed to act practitioners by the ICAEW. They are supported by qualified experienced staff.

Meet the Team

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