

Bankruptcy Procedures in the UK

Business Information Factsheet BIF171
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Here for Business



Introduction

Sole traders and individual members of ordinary business partnerships are personally liable for the debts of their business. If they have debts they cannot meet, they may consider - or be forced into - bankruptcy.

This factsheet explains what bankruptcy means and the implications it has for individual business owners. It explains the bankruptcy procedures in England and Wales and outlines the variations in Scotland and Northern Ireland.

Bankruptcy only applies to individuals. It should not be confused with insolvency procedures that apply to limited companies or limited liability partnerships. Insolvency procedures used for companies are dealt with in a separate factsheet, BIF199 Company Insolvency and Liquidation.

What is bankruptcy?

Bankruptcy provides insolvent individuals with a way of dealing with overwhelming debt. A person is considered to be insolvent if either of the following conditions apply:

- They cannot pay a specific debt when it is due.
- Their assets (the things they own that could be sold to pay their debts) are worth less than the total amount they owe their creditors.

Bankruptcy is a legal procedure that arranges for creditors to be paid, in full or in part, by the sale of the bankrupt individual's assets. If they have no assets, bankruptcy proceedings allow most of their unsecured debts to be written off.

Becoming bankrupt can have serious implications for individuals:

- Their personal and business assets may be sold.
- They may find it difficult to obtain credit in the future.
- They will almost certainly have to close any business they run, as it will be stripped of its assets.
- They cannot act as a company director while bankrupt.
- Their personal details will be published on a statutory insolvency register that anyone can search online.



The process for declaring bankruptcy In England and Wales, bankruptcy proceedings start when either:

- An individual applies to declare themselves bankrupt. The application can be made online and a decision about the application is made by an adjudicator employed by the Insolvency Service rather than by a court. The fee for a bankruptcy application is £680.
- One or more creditors who are owed at least £5,000 apply to a court to declare an individual bankrupt.
- An insolvency practitioner applies to the court for a bankruptcy order against an individual who has broken the terms of an individual voluntary arrangement (IVA). An IVA is an alternative option for paying off debts. Go to www.gov.uk/options-for-paying-off-your-debts/individual-voluntary-arrangements for more information.

If the adjudicator or the court decides to make an order declaring the individual bankrupt, it will be published in the 'London Gazette' (the official publication for legal notices) and may also be advertised in other ways. Notice of the bankruptcy will be given to local authorities, utility suppliers, courts, sheriffs, bailiffs, Land Registry, National Savings and Investments (premium bonds) and any relevant professional bodies.

The official receiver will then investigate the bankrupt individual's financial affairs and make enquiries to discover any assets or liabilities that the bankrupt individual has. This is likely to involve contacting banks, building societies, mortgage, pension and insurance companies.

Duties of bankrupt individuals

Bankrupt individuals are legally required to:

- Pass on any requests for payment from their creditors to the official receiver.
- Provide information and attend interviews or meetings about their financial dealings.
- Submit a full list of their assets and liabilities.
- Hand over all their assets, along with all account books, records, bank statements, insurance policies, other financial papers and records relating to property.
- Provide information about any assets or income obtained during the bankruptcy.
- Attend court if required to do so.
- Immediately cease using bank, building society, credit card and other accounts.

Seizure of assets

So that payments can be made to creditors, a qualified insolvency practitioner known as a 'trustee' is appointed to seize and sell the bankrupt individual's business and personal assets, including house, car and personal possessions (with some exceptions, such as items deemed 'the tools of the trade', as well as essential domestic and personal items). In some cases the official receiver acts as trustee.

If a bankrupt individual owns a property jointly with a partner, control of the bankrupt individual's share passes to the trustee, who may have to sell it to pay the debts. In some circumstances it is possible to delay the sale of a family home until after the end of the first year of bankruptcy to allow time to make other living arrangements.

The trustee also has certain powers regarding property that does not belong to the bankrupt individual. For example, if a bankrupt individual has sold property to a friend or relative for less than it is worth, the trustee can apply to the court for its seizure.

Deductions from income

In addition to seizing assets, trustees can ask the bankrupt individual to enter into an income payment agreement (IPA), which is a legally binding written agreement to make regular payments to the trustee for a specified period.

If the bankrupt individual does not agree to an IPA, the trustee can apply to the court for an income payment order (IPO), which deducts a proportion of any income the bankrupt individual earns to help pay off their debts.

Both IPOs and IPAs can last for a maximum of three years. If an individual is discharged from bankruptcy before the IPO or IPA ends, they must still continue to make the required payments for the specified period.

Pension savings in a pension scheme approved by HM Revenue & Customs (HMRC) are exempt from seizure. However, payments made to an individual from a pension scheme are treated as income and can therefore be made subject to deductions under the terms of an IPA or IPO.

Payment of creditors

Creditors must make a formal claim for the amount they are owed. There is a strict order of precedence for payments to creditors:

- The administrative costs of the bankruptcy process, which will be normally be around £8,000 plus 15% of the total value of assets received.
- Trustees' fees and expenses.
- 'Preferential creditors', for example employees.
- Other unsecured creditors, for example firms that have supplied goods and services to the failed business, financial institutions that have made unsecured loans or given credit, and any other individuals to whom the bankrupt person owes money. This also includes HMRC.

Secured creditors, for example banks and other lending institutions with a legal interest (called a charge) in a debtor's property, do not usually have to rely on the trustee for repayment of the debt. They can sell the asset that was provided as security for the debt to release the money they are owed. However, if insufficient money is raised from the sale, the secured creditor can claim the balance from the trustee as an unsecured creditor.

Restrictions during bankruptcy

A bankrupt individual must not:

- Trade under any name other than that under which they were made bankrupt.
- Act as a company director or promote, manage or form a limited company without the court's permission.
- Hold certain public offices.
- Act as a trustee of any charity or pension fund.
- Write cheques, knowing they will be dishonoured.
- Obtain an overdraft or open a new bank or building society account without declaring their bankruptcy.
- Obtain credit for more than £500 (for example, hire-purchase agreements), either alone or jointly with another person, without first disclosing that they are bankrupt.
- Make direct payments to their creditors.

A bankrupt individual may, however, carry on a business as a sole trader, providing they comply with all the restrictions above. Failure to comply could result in their arrest or delay their discharge from bankruptcy.

When does bankruptcy end?

Bankruptcy ends when the individual is 'discharged' from bankruptcy. This normally happens automatically one year after the date of the bankruptcy order. However, discharge from bankruptcy can be delayed if the individual has not co-operated or carried out their duties during their period of bankruptcy.

Any assets seized by the trustee that remain unsold when the bankruptcy is discharged remain in the control of the trustee and can still be sold to pay creditors.

Once a person is discharged, the restrictions during bankruptcy no longer apply. Provided the individual is not subject to an additional court order, they may borrow money and carry on a business as before. However, bankruptcy can remain on a person's credit record for six years, so, in practice, they may find it difficult to get a loan.

An individual's details will remain on the Insolvency Register for three months after they have been discharged from bankruptcy.

Bankruptcy in Scotland

The insolvency procedure for individuals in Scotland (often referred to as 'sequestration') is very similar to that in England and Wales. However, there are some key differences, including the following:

- Individuals must owe at least £1,500 to apply for their own bankruptcy. They can do so through Accountant in Bankruptcy (AiB), Scotland's insolvency service. People on a low income with few assets or savings can apply for bankruptcy under the Minimal Asset Process (MAP), in which case they may be discharged from bankruptcy after only six months.
- A creditor must be owed at least £3,000 in order to apply to the Sheriff Court to make someone bankrupt.

Business owners in Scotland can get more information and guidance from the AiB website at www.aib.gov.uk and from the Scottish Government at www.mygov.scot/bankruptcy/overview.

Bankruptcy in Northern Ireland

Insolvency procedures in Northern Ireland are almost the same as in England and Wales. However, there are some minor differences. For example, 'preferential debts', which are repaid before most other debts, include wages owed by the bankrupt individual in the four months before the date of the bankruptcy order and contributions to occupational pension schemes. Guidance about bankruptcy in Northern Ireland is provided by the Department of the Economy at www.economy-ni.gov.uk/topics/insolvency-and-bankruptcy/bankruptcy-northern-ireland and by nidirect at www.nidirect.gov.uk/articles/bankruptcy.

Alternatives to bankruptcy

Business owners should only consider bankruptcy as a last resort. There are several alternatives to bankruptcy that allow business owners to pay off part or all of their debts in instalments. Some of these arrangements allow debts to be written off after a specified period and prevent creditors from taking legal action to recover what they are owed.

For more information about alternatives to bankruptcy, go to:

- England and Wales: www.gov.uk/options-for-paying-off-your-debts.
- Scotland: www.aib.gov.uk/debt/deal-debt.
- Northern Ireland: www.economy-ni.gov.uk/articles/alternatives-bankruptcy.

Further information

BIF037 Making a Small Claim to Recover an Unpaid Debt

BIF150 Selling Your Business

BIF199 Company Insolvency and Liquidation

BIF294 Administration and Company Voluntary Arrangements

Useful contacts

The Insolvency Service is a statutory body that provides information on insolvency, redundancy and related matters in England and Wales.

Tel: 0300 678 0015

Website: www.gov.uk/government/organisations/insolvency-service

Accountant in Bankruptcy (AiB) administers bankruptcy and insolvency processes in Scotland. It publishes information about bankruptcy.

Tel: 0300 200 2600

Website: www.aib.gov.uk

The Insolvency Service for Northern Ireland is part of the Department for the Economy. It is responsible for administering bankruptcy and corporate insolvency in Northern Ireland. It provides information about bankruptcy and liquidation.

Tel: (028) 9054 8531

Website: www.economy-ni.gov.uk/articles/creditors-bankrupt

Business Debtline is a charity that provides self-employed people with free advice and information about debt problems. It covers England, Wales and Scotland.

Tel: 0800 197 6026

Website: www.businessdebtline.org

Citizen's Advice provides free advice and information on managing debt.

Website: www.citizensadvice.org.uk

National Debtline is charity that provides an independent debt advice service.

Tel: 0808 808 4000

Website: www.nationaldebtline.org

StepChange Debt Charity provides advice and debt management plans.

Website: www.stepchange.org

The Debt Advice Foundation is a charity offering free, confidential support and advice to sole traders and consumers on any aspect of debt.

Tel: 0800 043 4050

Website: www.debtadvicefoundation.org

The Insolvency Practitioners Association (IPA) is a membership body for practitioners of insolvency-related work in the UK. It has an online directory of insolvency practitioners.

Website: www.insolvency-practitioners.org.uk

R3 (Association of Business Recovery Professionals) is a professional association for insolvency practitioners, lawyers turnaround specialists and restructuring experts in the UK. It has an online directory of practitioners and legal advisors.

Website: www.r3.org.uk

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