

Personal Insolvency update

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Personal insolvency numbers steady... but what next?

The number of people who became bankrupt or entered into an Individual Voluntary Arrangement (“IVA”) in 2007 was slightly lower than the record numbers seen in 2006. Within this, bankruptcy orders (at 64,480) were 2.4% higher than in 2006 while IVAs (at 42,165) were 4.9% lower. For those of us who have been involved in the great IVA debate which has been raging over the last year, the fall in IVA numbers will come as no surprise. It is worth noting that the quarterly figure of 9,188 IVAs for the last quarter of 2007 is a decrease of 27.3% on the corresponding quarter of 2006.

insolvencies this year. After a couple of years of no appreciable growth in unsecured personal lending, there was a pronounced increase towards the end of 2007. This may well reflect the difficulties in remortgaging towards the back end of the year both as a result of the credit crunch effect as well as a stagnating property market.

So are we likely to see falling numbers for personal insolvency this year? Probably not. It will be interesting to monitor these statistics (and we will be doing that!) but we would expect there to be an overall increase particularly later this year given the very high levels of personal debt, higher mortgage repayments and some sharp rises in outgoings such as heating bills and petrol costs. The media often quote average debt levels (both unsecured and secured) per adult or per household and actually those (not very dramatic) numbers can mask the real issues. It is the skewed distribution of debt, not the average figure, which is causing huge problems. Hence surveys in recent months indicating that one in four are now struggling with unmanageable debts and that 9% of Britain’s mortgage holders may be considered sub-prime by lenders.

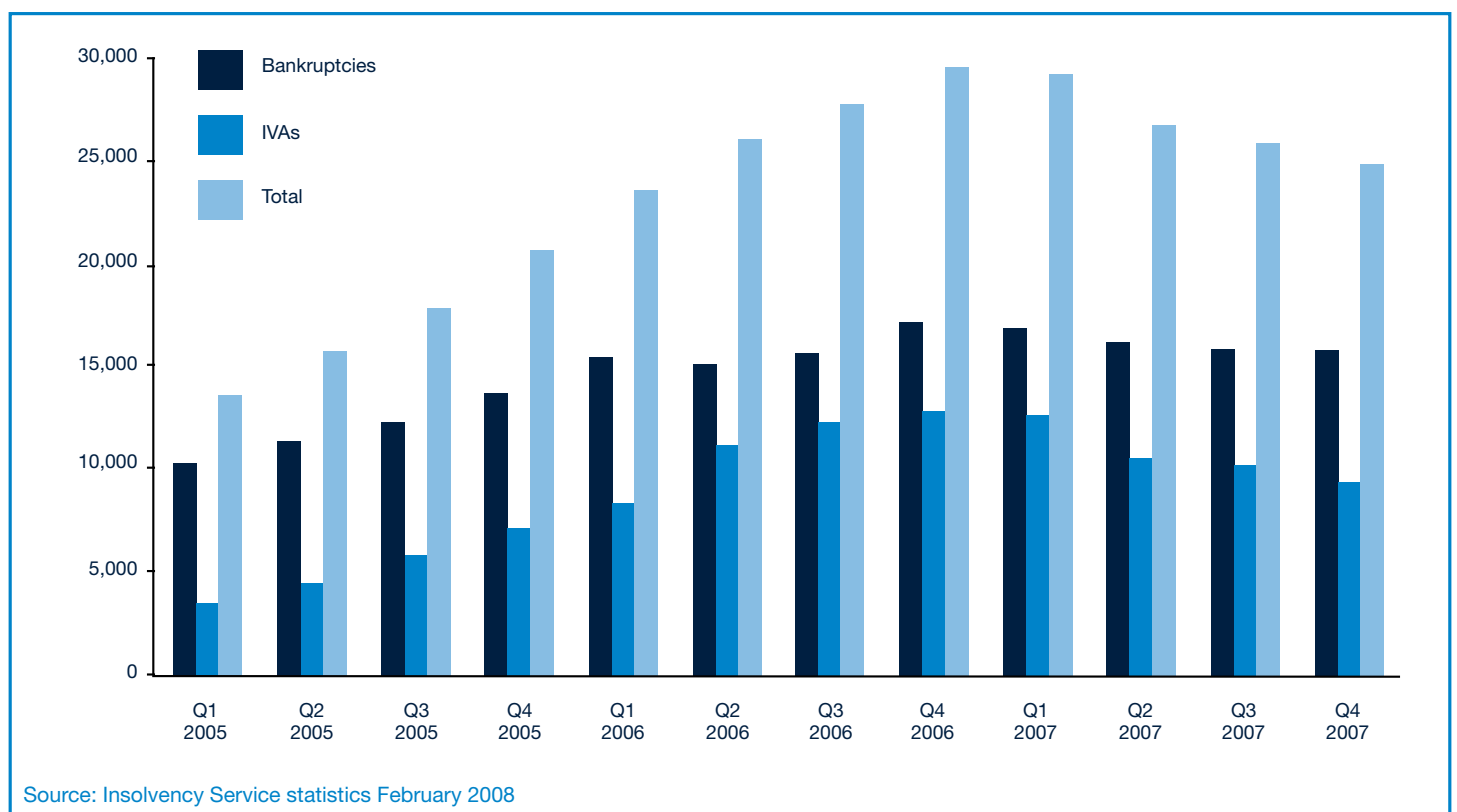
‘the fall in IVA numbers will come as no surprise’



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For much of last year, many over-indebted consumers relied on remortgaging to stave off bankruptcy but the credit crunch put a spanner in the works as lenders tightened their lending criteria. This has led to the most financially stretched consumers reverting to more expensive borrowing on credit cards and loans which may well result in rising numbers of personal



Courts support creditors' rights to payment

The recent case of *Foyle & Foyle v Turner* has shown that the court will take a firm stance when considering whether the matrimonial home should be sold to pay creditors' claims.

Mr & Mrs Foyle were adjudged bankrupt in 1991. The trustee in bankruptcy reached an agreement in principle to sell his interest in the property to the Foyles' daughter in 1993, but payment was not received. The trustee vacated office and the Official Receiver became trustee. By 2003 the property had significantly increased in value and Charles Turner of PwC was appointed trustee to deal with the property interest. He obtained an order for possession and sale in 2004.

The Foyles appealed the decision, claiming that it contravened their entitlements under the Human Rights Act 1998. They also contended that the 13-year delay in dealing with the property was an "exceptional circumstance" which overrode the statutory presumption in favour of creditors' rights.

The judge determined that there had been no breach of the Foyles' human rights, including the right to respect for private and family life and home. A balance had been struck by Parliament in the Insolvency Act 1986 between the interests of a bankrupt's family and his creditors which sufficiently addressed this principle.

'court will take a firm stance when considering whether the matrimonial home should be sold to pay creditors' claims'

The delay in realising the property was not an "exceptional circumstance". It was held that an exceptional circumstance must be something out of the ordinary run of events and a bankrupt could not resist the trustee's realisation of his estate simply because the creditors may not have shown much interest since the Bankruptcy Order was made.



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Discharge and the Enterprise Act – an easy ride for debtors?

The Enterprise Act introduced early discharge and reduced the automatic discharge period from three years to a maximum of one year. It is now common for bankrupts to be discharged within eight or nine months.

Opinion will be split on whether the Insolvency Service can properly investigate a bankrupt's affairs in that timeframe whilst current case volumes stretch their resources.

While this probably does not create an issue in the majority of bankruptcies, problems can occur in those cases passed to a trustee. Situations can arise where a trustee is appointed only shortly before the application for early discharge is made, giving him little time to form a view as to whether it is indeed prudent to consent to the application.

The most obvious implication is on after acquired assets. The trustee may claim "windfall" assets before discharge, but there is now a very narrow window of opportunity. A sportsman, whose bankruptcy was dealt with by PricewaterhouseCoopers, openly waited until discharge before seeking lucrative employment as a coach in order to avoid an Income Payment Order.

The Enterprise Act... should not allow those who can pay to avoid their obligations.

The Enterprise Act's aim to give those in debt a second chance may be commendable but it should not allow those who can pay to avoid their obligations.



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IVA Protocol



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'In theory, an IVA proposal labelled as a SCIVA will be accepted by creditors and their agents without query.....'

The long-awaited IVA Protocol came into effect on 1 February 2008. Its purpose is to agree a format for a Standard Consumer IVA (or SCIVA – pronunciation variable), which in turn aims to avoid numerous modifications and to reduce rejections. In theory, an IVA proposal labelled as a SCIVA will be accepted by creditors and their agents without query as it will give an assurance that it complies with the terms of the Protocol. In particular, the proposal will be based upon generally accepted household expenditure guidelines, confirmed asset levels (particularly the matrimonial home), assured levels of sustainable income, and readily determined debts. Because SCIVA proposals cannot be based upon variable income and unascertained debts, such as Schedule D tax, it will not readily apply to the self-employed. The usual IVA procedure will be available to those to whom a SCIVA does not apply.

The Protocol specifies what the Insolvency Practitioner must do but, in the view of many IPs, does not commit creditors to a particular response. Two particular issues stand out. Firstly, the Protocol cannot, under competition laws, dictate what the fee basis or quantum should be. Secondly, some creditors still require a minimum dividend to be offered.

It had been hoped that the Protocol would oblige creditors to remove this particular hurdle, but this has not happened. Creditors therefore will still need to check that each proposal has an acceptable fee basis and, if appropriate, offers at least their minimum dividend. If creditors reject an IVA they are obliged to give a reason to the IP.

The Protocol is an interesting concept, and largely attempts to anticipate the Simple IVA law which will come into effect, subject to the usual process, either this October or April 2009. It is a voluntary code, but breaches could lead IPs to face disciplinary charges from their regulators. It was apparent at the conference to launch the Protocol that IPs are still rather suspicious of creditor motives, and that they view the matter as rather one-sided. There will undoubtedly be teething problems but the real concern is what happens if one or other of the two sides does not enter into the spirit of the Protocol: there are many unresolved issues, such as fees and hurdle rates, and given the wide range of IP attitudes, and the varied creditor requirements, there is ample opportunity for confusion and accusation.

The measure of success must be an agreement amongst all interested parties that the SCIVA process serves as a reasonable solution for financially distressed individuals, and that these individuals are not denied that solution by arbitrary conditions, nor are they sold a product that does not serve their needs. In the battle over fees and minimum dividends, it is often forgotten that someone's future is at stake.



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