STATEMENT OF INSOLVENCY PRACTICE 3

INDIVIDUAL VOLUNTARY ARRANGEMENTS

INTRODUCTION

1. This statement of insolvency practice is one of a series issued by the Council of the Society with a view to harmonising the approach of members to questions of insolvency practice. It should be read in conjunction with the Explanatory Foreword to the Statements of Insolvency Practice.

2. The statement has been prepared for the sole use of members in dealing with individual voluntary arrangements for debtors in England and Wales. Members are reminded that SPI Statements of Insolvency Practice are for the purpose of guidance only and may not be relied upon as definitive statements. No liability attaches to the Council or anyone involved in the preparation or publication of statements of insolvency practice.

3. The Insolvency Act 1986 (IA 1986) and associated Rules set out a procedure which enables a debtor to make a proposal for a voluntary arrangement (IVA) with his creditors. The Rules (The Insolvency Rules 1986) specify two types of debtor:
"Case 1": an undischarged bankrupt;
"Case 2": not an undischarged bankrupt.

4. The guidance which follows is intended to give an overview of the practical steps to be taken when a member is contacted to consider, and possibly administer, such an arrangement. The relevant legislation is contained in sections 252-263 (inclusive) of the IA 1986 and rules 5.1-5.30 (inclusive) of the Rules, as amended by the Insolvency (Amendment) Rules 1987.

Basis of the Arrangement

5. The terms of the voluntary arrangement will be contained in the debtor's proposal, as modified, which is eventually approved by the creditors. A comprehensive and accurately drafted proposal is therefore fundamental to the arrangement. In view of the importance of the proposal the member should, where the circumstances are complex, consider whether it should be approved by a lawyer. The contents of the proposal are given further consideration in paragraph 14.

6. In dealing with an IVA the member should bear in mind his duty to ensure a fair balance between the interests of the debtor, his creditors and any other parties involved.

Initial Contact with the Debtor

7. The member's first contact with the debtor may arise in one of five different ways, as follows:

(a) the matter is referred to him by the court under section 273 IA 1986;
(b) the matter is referred to him by the Official Receiver (OR);
(c) the member is acting as the debtor's trustee in bankruptcy and considers that an IVA may be appropriate;
(d) the debtor submits a proposal for an IVA to the member without prior contact;
(e) the debtor consults the member about his financial situation generally and is advised that an IVA may be appropriate.

(Note that an application to the court for an Interim Order (IO) may not be made while a bankruptcy petition presented by the debtor is pending if the court has, under Section 273 IA 1986, appointed an IP to enquire into the debtor's affairs).

8. In any of these instances, the debtor should be told at the initial interview of the member's requirements to maintain independence. Consideration should be given to the need for separate representation for the debtor's spouse or family, and any third parties who may be involved in providing funds.

9. In instances where the assets are not already protected by a bankruptcy order or by the presentation of a debtor's petition the member should give consideration to the need for early action to protect the assets. This would involve the preparation of an estimated statement of affairs and an embryonic proposal so as to be able to make a quick application for an IO and any other Orders that may be desirable according to the nature of the assets. This statement of affairs can be amended and the proposal modified following the member's further enquiries into the position.

10. The member should consider the likely costs, including legal costs, of obtaining approval for an IVA, and make suitable arrangements for their payment. These arrangements could include third party guarantees.

11. When considering an application for an IO the court needs to be satisfied that:

(a) the debtor intends to make a proposal to his creditors;
(b) the debtor was an undischarged bankrupt or could have petitioned for his own bankruptcy when he applied for the IO;
(c) the debtor has made no previous application for an IO within the previous 12 months; and
(d) the nominee is qualified to act as an insolvency practitioner in relation to the debtor, and is willing so to act.

Therefore it is necessary for the member to establish that the above requirements are satisfied, both in relation to the debtor and his own position, and to consider any possible ethical restrictions (see appropriate RPB ethical guidance notes).

Statement of Affairs and Obtaining Additional Information

12. An accurate statement of affairs and a detailed assessment of the debtor's situation should be produced before the proposal is drafted. If this is not possible, this work should be undertaken after an application has been made for an IO or after it has been granted. The member should detail the nature and amount of all the debtor's assets and liabilities. His approach should cover the points listed below:

(a) Creditors

The member should obtain details of all known or possible liabilities including:
(i) guarantee liabilities;
(ii) claims for breach of contract, including claims in respect of faulty and incomplete work and hire purchase and leasing agreements;
(iii) creditors who are "associates" (as defined in section 435 IA 1986);
(iv) guarantors of the debtor's debts, including associates;
(v) unsecured creditors

He should also:

(vi) identify preferential creditors and try to establish whether they are likely to be paid in full;
(vii) identify any creditors who have commenced execution or any other legal process;
(viii) consider the possibility of early informal discussions with the key creditors to establish their views. These creditors will include any petitioning creditors and government bodies which might have preferential claims;
(ix) establish whether associates may consider withdrawing or deferring their claims;
(x) identify secured creditors (both partially and fully secured).

(b) Assets

If the debtor owns a business, the member should consider the manner in which that business is to be dealt with. Points to be borne in mind are:

(i) whether the debtor should continue trading, and if so, on what terms;
(ii) the implications of ROT claims;
(iii) what should happen if, despite all efforts, further loses are incurred, and
(iv) the probable requirements of certain creditors (eg. HMC&E, Inland Revenue and statutory undertakings) with regard to submission of future returns and payments;
(v) the most beneficial time for the debtor to cease trading bearing in mind work in progress, tax implications, and the beneficial realisation of stock and other assets;
(vi) immediate cash requirements of the debtor's business;
(vii) insurance, rent and other ongoing costs;
(viii) credit requirements/availability for his business;
(ix) the cash flow forecast.

If the debtor's business is to be continued a "business plan" should be produced to justify this decision.

(c) General

The member should enquire as to:

(i) possible transactions at an undervalue (sections 339 and 423 IA 1986);
(ii) payments which may be preferences (section 340 IA 1986);

(With regard to the above points, (i) and (ii), the member should consider whether outside monies should be injected to compensate creditors for the right to pursue such matters, which would exist in a bankruptcy).

(iii) liabilities which may be extortionate credit transactions, both those outstanding and paid (section 343 IA 1986);
(iv) form an opinion of whether the debtor is credible and making a full disclosure. The member should explain the consequences of making false representations;
(v) whether the debtor has been involved in any previous business failure, either individual or corporate, and if so the details of that failure and the debtor's responsibility for it;
(vi) the timetable for the IVA;
(vii) sums owed to the debtor by his associates, details of which should be included in the statement of affairs.

It should be noted that a Case 1 debtor who has delivered a statement of affairs under Section 273 or Section 288 need not deliver a further statement unless so required by the nominee.

Consideration of Alternative Arrangements

13. Throughout his consideration of the above factors the member should be forming his opinion of the appropriate method of dealing with the debtor's affairs. Although this will be partly a subjective review of the factors already referred to, the member should take into account:

(a) the debtor's attitude;
(b) the likelihood of the debtor adhering to the proposal;
(c) the extent of the control over the assets exercised by the debtor as opposed to the supervisor of theproposal (bear in mind that in an IVA the assets do not vest by law in the supervisor);
(d) the removal/absence of the restrictions imposed upon bankrupts.

The Proposal

14. In theory, the proposal will be submitted to the proposed nominee by the debtor prior to the application for an IO. However, in practice, the proposal will normally be drafted by the proposed nominee or the debtor's solicitor. It may then be amended by agreement between the nominee and the debtor at any time up to the presentation of the nominee's report to the court. After that time further modifications may only be proposed by creditors and any modifications made must have the consent of the debtor. In view of the importance of the contents of the proposal the member should, prior to submitting his report to the court, satisfy himself that the proposal, as modified, is drafted in such a way that the terms of the IVA can be clearly understood and that the arrangement is likely to proceed to a successful conclusion.

15. The proposal should include sections covering the following:

(a) the background to the arrangement, including details of the circumstances in which the debtor has become insolvent and of his relevant personal circumstances;
(b) the statement of affairs, which should include details of both business assets and liabilities and also personal assets and liabilities;
(c) the actual financial proposal to be put to the creditors. This section should include:

  (i) details of assets to be realised for the benefit of creditors and details of those which are to be excluded from the proposal, together with the reasons for the exclusion and whether alternatives are to be suggested;
  (ii) the debtor's proposal regarding future income over a specific period;
  (iii) whether third party funds are to be injected;
  (iv) the debtor's specific proposals with regard to any interest he may have in his dwelling house;
  (v) details of creditors to be included in the arrangement. It is important that every creditor or potential creditor including preferential creditors who will invariably form part of the arrangement should be considered, to minimise the possibility of some creditors not being bound by the terms of the IVA. Secured creditors should also be included if they are to form part of the proposal. If they are not, they should be provided with a copy of the proposal, since if this adversely affects such a creditor's security, their consent must be obtained. The date to which claims are to be calculated should be stated together with details of arrangement with regard to, if appropriate, secured creditors and hire purchase or leasing agreements;

(d) the intentions with regard to any business operated by the debtor stating in particular whether the business is to be continued, and if so, the extent to which, if any, the supervisor shall exercise any degree of control over the business. If the supervisor is not to exercise any degree of control, consideration should be given to specifically stating this in the proposal;
(e) the powers, duties and responsibilities of the supervisor. This will need to deal with the question of admission or rejection of claims and the basis on which the supervisor is to report to creditors;
(f) miscellaneous matters which under the Act or Rules need to be included.

16. Other matters which the member shall consider in relation to the contents of the proposal:

(a) whether a committee of creditors is to be appointed and if so what will be its powers, duties and responsibilities;
(b) what will happen to surplus funds arising, for example, from more beneficial trading than was originally envisaged, when the IVA is concluded;
(c) confirmation that when the terms of the IVA have been successfully completed the creditors will no longer be entitled to pursue the debtor for the balance of their claim;
(d) what will happen to unclaimed dividends or unpresented cheques when the IVA is concluded;
(e) how to deal with creditors who have not made claims;
(f) in the event of the arrangement not being successfully completed, and a bankruptcy ensuing, clarification of the amounts for which the creditors will be entitled to claim;
(g) the proposals with regard to maintenance orders or attachment of earnings orders in favour of the debtor's wife, and with regard to fines;

(h) in view of the fact that the assets do not automatically vest in the supervisor it may be advisable for the proposal to provide for such vesting or for the supervisor to be granted a charge over assets, or to be given some other suitable form of security or for a declaration of trust or power of attorney to be executed;

(i) the attitude to be adopted with regard to contingent creditors;
(j) the situation with regard to overseas creditors;

(k) the circumstances in which the supervisor is to present a petition for a bankruptcy order;
(l) the situation with regard to tax liabilities arising on disposal of the debtor's assets, or the future income of or gifts to the debtor from a third party, that are applied towards the payment of creditors' claims;
(m) the approach to be adopted in respect of inadvertently omitted creditors;
(n) the inclusion of power for the supervisor or any creditor's committee to be able to determine that an IVA has no future and petition for bankruptcy and authority to retain and use funds from the IVA for such costs.

The Interim Order

17. Before he can apply to the court for an IO the debtor must give written notice of his proposal to the intended nominee, and this must be acknowledged by the latter. Both the application for the Interim Order and the notice to the intended nominee must be accompanied by a copy of the proposal. A copy of the endorsed notice should be returned to the debtor and a further copy will be exhibited with an affidavit, which is to accompany his application to court for the IO. The affidavit must state the following:

(a) the reason for application;
(b) details of any execution or legal process which has been commenced against the debtor;
(c) that the debtor is an undischarged bankrupt or able to petition for his own bankruptcy;
(d) that no previous application for an IO has been made in the previous 12 months;
(e) that the nominee is qualified to act as an insolvency practitioner and is prepared to act in relation to the proposal.

The affidavit and application for the IO will be filed in court and the court will fix an appointment for hearing the application. The nominee, or his authorised representative, is entitled to attend the hearing and may wish to do so in order to express his views on the length of time needed to prepare his report and comments.

18. The applicant (which in Case 1 can be the debtor, trustee, or OR) must give at least two days notice of the hearing to the nominee. In addition, in Case 1 notice must be given to the debtor, trustee, or OR (whichever of these is not the applicant) and in Case 2, to any creditor who has presented a bankruptcy petition against the debtor.

19. The IO has the effect that, during the period for which it is in force, no bankruptcy petition relating to the debtor may be presented or proceeded with, nor may any other proceedings, execution or legal process be commenced or continued against the debtor or his property, except with the leave of the court.

20. In Case 1 the debtor, trustee or OR may apply for the IO but in Case 2 only the debtor may make an application. In Case 1, notice of the proposal must be given to the OR and trustee (if applicable) before the application is made to the court. Generally an IO will cease to have effect after 14 days from the day following the making of the Order, although, on good reason being shown, an extension may be granted by the court.

The Nominee's Report

21. The nominee's report to the court must be filed not less than two days before the IO ceases to have effect. In this report the nominee must state whether in his opinion a meeting of creditors should be convened to consider the proposal and, if so, propose the location and timing of such meeting.

22. To the report should be attached a copy of the debtor's proposal (as modified) and of the statement of affairs. If the nominee's opinion is that a meeting of creditors should not be summoned he must give reasons for his opinion. The report and enclosures should be filed in court and will be endorsed with the filing date. In Case 1 the nominee must send to the OR a copy of the proposal, together with his comments

and the statement of affairs. In Case 2 these items should be sent to any person who has presented a petition for a bankruptcy order.

23. It may be possible, with the approval of the court, for the nominee's report and his comments on the statement of affairs to be considered along with the application for an IO. Combining the two hearings in this way may result in an overall saving of both time and costs. If such approval is given, the nominee should request an extension of the IO to cover the period of the meeting, a fourteen day adjournment and the four days for delivering the report of the chairman of the meeting of creditors.

The Nominee's Comments

24. If the nominee reports that a meeting of creditors should be held he is required to set out his comments on the proposal and to annex them to his report to the court. The matters upon which the nominee will wish to comment will vary from case to case but where applicable they should include:

(a) the extent to which the nominee has investigated the debtor's circumstances;
(b) the basis upon which assets have been valued;
(c) the extent to which the nominee considers that reliance can be placed upon the debtor's estimate of the liabilities to be included in the IVA;
(d) information on the attitude adopted by the debtor with particular reference to instances where he has failed to cooperate with the nominee;
(e) the result of any discussions between the nominee and secured creditors or other interested parties upon whose cooperation the performance of the IVA will depend;
(f) details of any previous history of failures in which the debtor has been involved in so far as they are known to the nominee;
(g) an estimate of the result for the creditors if the IVA is approved, explaining why it is more beneficial for creditors than any alternative insolvency proceeding;
(h) the likely effect of the proposal's rejection by the creditors;
(i) details of any claims which have come to his attention which might be capable of being pursued by a trustee in bankruptcy but not by the supervisor, or which a trustee in bankruptcy would be in a better position to pursue.

The Meeting of Creditors

25. Having reported to the court that a meeting of creditors should be held, the nominee must then convene such a meeting, which must take place not less than 14 days after his report has been filed in court and within 28 days of its consideration by the court. 14 days notice of the meeting must be given to the creditors. The following points must be adhered to:

(a) The venue must be fixed with regard to the convenience of the creditors.
(b) The meeting is to be held between 10.00 and 16.00 hrs on a business day.
(c) The chairman of the meeting will be the nominee or another insolvency practitioner or an experienced member of the nominee's staff. Unless a proxy held by the chairman specifically directs him to vote in relation to an increase or decrease in the amount of the nominee's/supervisor's remuneration and expenses as proposed in the IVA, he shall not do so.
(d) Notice of the meeting must be sent to:

  (i) Case 1: every person who is a creditor of the bankrupt or would have been a creditor if the bankruptcy had commenced on the date of the notice;
  (ii) Case 2: all creditors specified in the debtor's statement of affairs and any other creditors of whom the nominee has knowledge.

(e) The notice of the meeting should enclose:

  (i) a copy of the proposal, as modified;
  (ii) the statement of affairs or a summary (including a full list of creditors and the amounts due);
  (iii) the nominee's comments on the proposal;
  (iv) a proxy form;
  (v) details of the rules regarding the requisite majorities at the meeting, as set out in Rule 5.18.

26. Before the meeting the nominee should take the following steps:

(a) record all proxies received, and details of claims;
(b) complete the meeting record as far as possible detailing the names and voting value of creditors;
(c) note all resolutions in advance and discuss with the debtor modifications suggested by creditors prior to the meeting;
(d) review the proposal in the light of creditors' responses and possible changes in circumstances;
(e) prepare a brief report for presentation at the meeting, summarising the debtor's proposal and outlining the likely effects of acceptance and rejection;
(f) consider voting rights and requisite majority (see Rules 5.17 and 5.18).

27. The chairman must decide the amount for which creditors are to be allowed to vote. Proxies to be used at the meeting may be lodged at any time, even during the course of the meeting.

28. After the chairman has presented his report to the meeting he should allow creditors an opportunity to make comments, ask questions or propose modifications to the debtor's proposal. The nominee should try to ensure that the debtor attends the meeting in order to answer questions and to give consideration to proposed modifications. If the debtor is not in attendance and modifications are proposed, the meeting will have to be adjourned (Section 258 IA 1986).

29. If modifications are proposed by a creditor the chairman should give careful consideration to the manner in which he will use specific instructions given to him by creditors to vote for either the acceptance or the rejection of the original proposal. If the particular words in the proxy form have not been deleted so as to entitle the proxy holder to vote only as directed, the proxy holder is entitled to vote or abstain on any modification at his discretion.

30. However, the chairman should bear in mind that, if a creditor is aggrieved that a vote on proposed modifications has been taken and a decision reached which might have been different if creditors represented by proxy had been present at the meeting or had been given the opportunity of amending their proxy, the aggrieved creditor may challenge the decision by an application to the Court under Section 262 IA 1986. Therefore the chairman may wish to consider an adjournment or suspension of the meeting to give him an opportunity to explain the circumstances to the creditor or creditors from whom he holds a proxy and to obtain their further instructions. The general requirements regarding proxies and company representation are set out in rules 8.1-8.7.

31. At the meeting the creditors will consider whether to approve the proposed IVA, with or without modifications. Each such modification must have the consent of the debtor and cannot include any proposal which would affect the right of a secured creditor to enforce his security, unless that particular creditor concurs. It is recommended that any such consent from debtor or creditor be obtained in writing. In addition, unless the creditor concerned agrees, the meeting may not approve an amendment where a preferential creditor is to receive either a smaller proportion of its debts than the other creditors in that class or settlement other than in priority to non-preferential debts.

32. The proposed modifications may include the conferring of the proposed functions of the supervisor on a qualified insolvency practitioner other than the nominee.

33. If a majority for approval of the IVA is not obtained the chairman may adjourn the meeting, and must adjourn if it is so resolved. The maximum period for adjournment is 14 days from the original meeting date, but within this period there can be more than one adjournment. The chairman must give notice to court that the meeting is adjourned and should consider the need to apply for an extension of the IO.

Administration Following the Meeting of Creditors

34. The chairman must report the result of the meeting to the court, to be filed within four days of the meeting. This report will state whether the IVA was approved or rejected and list any modifications made to it. It will also detail the resolutions taken at the meeting, the decisions reached, and list the creditors present or represented at the meeting together with how they voted. If the debtor comes under Case 1, the court, on receipt of the chairman's report, may decide either to annul the bankruptcy order or to give directions for the conduct of the bankruptcy.

35. The chairman must also give creditors notice of the outcome of the meeting. The notice should be accompanied by a VAT Bad Debt Relief claim form (but bear in mind the provisions of S.11 FA 1990). If an IVA is approved it binds every person who received notice of it. If the debtor was bankrupt the court may annul the bankruptcy order or give appropriate directions to implement the proposal.

36. After filing his report of the meeting with the court, the chairman must report to the Secretary of State, giving details of:

(a) the name and address of the debtor;
(b) the date the IVA was approved by creditors;
(c) the name and address of the supervisor;
(d) details of the court in which the report was filed; and
(e) the appropriate registration fee (Note: where he replaced another insolvency practitioner previously appointed, the supervisor must also give written notice of his appointment to the Secretary of State accompanied by the appropriate registration fee).

37. Once these formalities have been completed, the proposal should be implemented. It may be necessary to give undertakings to the OR or trustee (if appropriate) regarding their costs. The nominee (or other person proposed) is now the "supervisor" and he may apply to the court for directions if necessary.

38. An application may be made to the court that the IVA is unfairly prejudicial to a creditor or the debtor, or that there was a material irregularity at the meeting. The debtor, creditor, nominee, trustee or OR may make this application within 28 days from the date the report of the meeting was filed with the court. The court may revoke or suspend the approval given at the meeting or direct the party to summon a further meeting to revise the proposal. The supervisor should consider obtaining legal advice if the meeting's decision is challenged.

39. If the debtor fails to comply with any part of his proposals a supervisor should consider bankruptcy proceedings under section 264(1)(c) IA 1986. The proposal may also provide for the supervisor to be given power to determine that an IVA has no future (see para 16).

40. The supervisor should maintain accounts of his receipts and payments and records of all his acts and dealings (Rule 5.26). At least once every twelve months, from the date of his appointment, he must prepare copies of an abstract of his receipts and payments, together with his comments as to the progress of the administration. These are to be filed with the court and sent to the debtor and to the creditors bound by the proposal. The Secretary of State may require sight of the records and accounts at any time during or after the IVA.

41. The fees to be charged are those which were sanctioned in the terms of the proposal.

42. At the end of the arrangement the supervisor shall prepare a summary of all his receipts and payments and a report explaining any differences from the original proposal. This shall be sent, together with a notice that the IVA has been fully implemented, to all creditors, the debtor, the court and the Secretary of State within 28 days following the completion of the IVA.