



A creditor's guide to bankruptcy

September 2022

A licensed insolvency practitioner ('IP') has given you this because you, or your business, may be owed money by a private individual or sole trader who has become bankrupt.

This guide aims to help you understand your rights as a creditor and to describe how best these rights can be exercised. It is intended to relate only to England and Wales. It is not an exhaustive statement of the relevant law or a substitute for specific professional or legal advice.

We have made every effort to ensure the guide is accurate, but R3 cannot accept responsibility for the consequences of any action you take in reliance on its contents. If, having read the guide, you remain in any doubt about your rights, you should consult a licensed insolvency practitioner or solicitor.

We hope that you will read this guide carefully and consider whether taking an active role as a creditor in this case could benefit you or your business.

What is bankruptcy?

Bankruptcy is a formal insolvency procedure available to an individual to deal with their debts. Only individuals can be made bankrupt. Bankruptcy does not apply to companies or partnerships, although individual members of a partnership can be made bankrupt. The administration of a bankruptcy estate is carried out by a trustee, who is an officer of the court and therefore has a duty to act fairly and reasonably.

The trustee will be the official receiver ('OR') or a licenced insolvency practitioner (IP). When a person becomes bankrupt, the control of the assets, with certain exceptions, passes to the trustee whose function is to realise them if it is commercially viable to do so and distribute the proceeds to creditors (after payment of the costs of dealing with the bankruptcy, subject to approval) and in a prescribed order of priority. If the person has no or limited assets you will not get your money back.

How is an individual made bankrupt?

There are three main ways into bankruptcy:

- A debtor can apply for their own bankruptcy. Here the individual makes a bankruptcy application which is determined by an adjudicator through a government online portal (and not by the court). The cost of an application is £680;
- One or more of the individual's creditors can apply to court to make someone bankrupt. Presently, the creditor(s) can petition for an individual's bankruptcy if they are individually or jointly owed £5,000 or more in respect of a debt that is not disputed; and
- The supervisor of a failed voluntary arrangement may present a bankruptcy petition. An application is made to the court.

Where it is a creditor(s) application, either:

- A statutory demand will have been served on the debtor who has, within 21 days from receipt, failed to either pay the debt due to the creditor or reach a reasonable agreement to pay the creditor; or
- Where an enforcement process is returned unsatisfied.

The court fee to make someone bankrupt is set annually by government. As of 1 May 2022, it is £990 for the petition deposit and £302 for court costs. If at the hearing of the bankruptcy petition the court is satisfied that bankruptcy process has been properly complied with, the court can make the bankruptcy order.

Who is appointed to deal with the bankruptcy estate?

Once a bankruptcy order is made, unless the court appoints an IP as trustee on the making of the bankruptcy order, for example where the petitioning creditor was the supervisor of a voluntary arrangement, the court will appoint the OR to administer the bankruptcy estate. The OR is a civil servant and an officer of the court. The OR will remain in office unless either:

- The majority of creditors (50% or more by value of creditors) support a particular IP to replace the OR; or
- 25% of creditors request a decision making procedure and creditors resolve that the OR is replaced as trustee; or
- The OR considers the case requires the skills and expertise of an IP.

It should be noted that upon making of the bankruptcy order by the court, the OR will charge a fee of £6,000 to meet the costs of the OR's operation.

This guide assumes that a licenced insolvency practitioner has been appointed trustee. You can find information on when the OR acts as trustee [here](#).

What is the effect of the bankruptcy order on the individual?

The bankrupt's assets vest in the trustee. The bankrupt loses any rights to their assets apart from any equipment needed by them in their business or job, and basic domestic equipment such as clothes, bedding and furniture, and certain pension rights.

The trustee's role is to realise the bankrupt estate's interest in the assets if is commercially viable to do so. Interest in the assets can be realised in one of three ways, a third party can purchase the interest, the bankrupt can sell the asset and pay over proceeds to the trustee or the trustee can take possession of the asset to sell. The third option is likely to require court intervention and can be expensive.

There are special rules regarding a property in which the bankrupt, their spouse or former spouse reside at the date of the bankruptcy order. The trustee has three years from the date of the bankruptcy order to deal with the interest in it. If the trustee does not do so within that time, the interest in the property will revert to the bankrupt. If the interest in the property is less than £1,000 the trustee would not be able to take legal action to realise the interest.

For any residential property where there are occupants other than the bankrupt, the trustee would normally wait 12 months before taking legal action in order to satisfy the court.

If the bankrupt has surplus income above their needs and those of their dependants, the individual may be required to make contributions to their creditors for up to three years.

There also are powers available to the trustee enabling them, in certain circumstances, to claim assets from third parties where they have been transferred for no or at undervalue or where creditors have been paid in preference to other creditors prior to the bankruptcy.

The trustee may also claim any asset acquired by the bankrupt after the bankruptcy order, prior to the bankrupt's discharge, such as assets left to them in a will.

The bankrupt can carry on its business and continue to work but with the following restrictions:

- The bankrupt must not obtain credit of more than £500 from anyone without telling that person that they are an undischarged bankrupt.
- The bankruptcy must not carry on business under a name different from that under which they were declared bankrupt without disclosing the fact that they are an undischarged bankrupt.
- The bankrupt must not act as a director of a company or be involved in its management without the court's consent.

It's a criminal offence if the bankrupt breaks these restrictions.

Bankruptcy restrictions generally end when the bankrupt is 'discharged' which is usually 12 months after the date of the bankruptcy order and is usually automatic.

There are exceptions to this and a bankrupt's discharge can be suspended where the bankrupt continues to fail to comply with obligations or if it was a criminal bankruptcy order made. You can check the discharge date online using The Insolvency Service Register.

Discharge only releases the bankrupt from the restrictions of bankruptcy. The assets remain in the bankruptcy estate to be dealt with by the trustee.

Once discharged, the bankrupt is released from their bankruptcy debts (see below for exceptions), and can begin to trade again or be a company director without the restrictions mentioned previously.

However, if the bankrupt's conduct has been irresponsible or culpable in some way, they may have restrictions imposed on them for up to 15 years, notwithstanding their discharge.

The bankruptcy order will not release the bankrupt from all debts, some debts are excluded and are known as non-provable debts such as those arising from fines, student loan debts, arrears of a debt due in family proceedings, confiscation orders.

In addition to these non-provable debts not being released on discharge, there are a category of debts that although provable in the bankruptcy are not released on discharge, for example debts incurred through fraud; a debt in respect of personal injury damages, a debt to the Social Fund.

After the bankrupt has been discharged, they do not have any right to take back from the trustee any property that is part of their estate in the bankruptcy. However, if there is a surplus after payment of all creditors in full plus interest, then this is returned to the bankrupt. In the meantime, the trustee will continue to hold those assets and apply them to the bankrupt's creditors.

What is the effect of the bankruptcy order on unsecured creditors?

After a bankruptcy order has been made, a creditor in respect of a debt provable in the bankruptcy, will not be able to take further action for repayment, except with the leave of the court.

What are the powers of the trustee?

The trustee's powers are set out in law (Schedule 5 of the Insolvency Act 1986) and include the power to sell the bankrupt's assets; to carry on the bankrupt's business; to bring and defend legal proceedings; and to pay dividends to the bankrupt's creditors. The trustee also has investigatory powers. It should be noted that even with these powers, the cooperation of the bankrupt or a third party is key, whether that is by providing information or delivering up assets. Without such cooperation, it may well be that the trustee will need court intervention which is costly and not always viable. Creditors can also help by providing any information they may have that they feel might assist the trustee.

Does the trustee pay unsecured creditors the money owed to them?

Secured and preferential creditors debts are paid before unsecured creditors. Secured creditors are those that have some form of security over the bankrupt's assets (for instance a mortgage on a property or finance on a vehicle). Secured creditors are entitled to be repaid their debt out of the proceeds of sale of the secured asset in priority to other creditors.

Preferential creditors are a special category of unsecured creditor. Preferential creditors consist mainly of certain debts due to employees and the redundancy payments service and, in insolvency procedures commencing after 1 December 2020, there is a secondary class of preferential creditor for certain HMRC debts. In addition to VAT, these are debts that relate to the following taxes (where the business is required to deduct taxes from payments they make to another other person and pay those deductions to HMRC and the payment to HMRC is credited against the liabilities of the other person):

- Pay As You Earn (PAYE) Income Tax
- Employee National Insurance contributions (NICs)
- Construction Industry Scheme deductions

Preferential creditors are paid in priority to all other unsecured creditors.

The trustee will pay a dividend to unsecured creditors if enough funds have been realised from the bankruptcy assets after paying costs, secured creditors, and preferential creditors.

In summary, the monies realised from the sale of the bankrupt's estate (assets) are used in the following order of priority:

1. Costs of the bankruptcy which include (but are not limited to)
 - a. Official Receiver costs
 - b. Bank charges
 - c. Tax due on realisations
 - d. Petitioning creditor costs

- e. Trustee expenses and disbursement (which may include legal costs)
 - f. Trustee remuneration
2. Debts to preferential creditors;
 3. All other unsecured creditors;
 4. Statutory Interest.

When claims have been adjudicated or provided for, the trustee will declare a dividend. The dividend will be a percentage (pence in the pound) of each creditor's total claim, based on the total cash available for distribution to the creditors and the total of all creditors' claims. All unsecured creditors are treated equally.

Six months after writing off the debt in your account you can claim back debt relief from HM customs and Excise for VAT you have paid.

How do I make a claim in the bankruptcy?

The trustee will write to all known creditors asking them to submit their claims. You should submit your claim to the trustee in writing within the specified time limit. You should also send enough supporting evidence of your claim, for example copy statements, invoices, correspondence etc to allow the trustee to decide whether your claim is valid. The trustee will not necessarily acknowledge receipt of your claim.

You may claim interest on your outstanding debt up to the date of the bankruptcy order if your debt bore interest; if it was payable at a previous date under a written instrument; or if you had previously demanded it in writing with notice that you would claim interest.

If all creditors are paid in full, statutory interest is payable at 8% per annum from the date of the bankruptcy order to the date payments are made subject to there being sufficient funds. (Interest will be adjusted to take into account interim payments).

If you believe that you have an interest in any of the bankrupt's assets, let the trustee know and provide full details.

How will the trustee adjudicate any claim?

The trustee will consider your claim and any supporting information. The trustee will compare your claim to the bankrupt's records and any other available information; they may discuss the claim with the bankrupt. The trustee may ask you for additional information or evidence if they think that you have not sufficiently proved your claim. For example, if you have supplied goods to the bankrupt, the trustee may ask you to provide copies of signed delivery notes.

The trustee may agree your claim in full, or in part, or they may reject your claim if they do not think it is valid.

What can I do if I believe the trustee has unfairly rejected my claim?

The trustee will give you the opportunity to provide information to support your claim and to discuss any issues. Once you have received a formal notice of rejection you can appeal to court within 21 days of rejection. After 21 days, if you do not apply to the court, the adjudication is final.

Does the trustee have to fulfil contracts entered into by the bankrupt prior to his appointment?

No. The trustee may decide not to fulfil a contract if it does not benefit creditors as a whole. If a trustee chooses not to fulfil a contract, the other party may have an unsecured claim in the bankruptcy for breach of contract.

Is the trustee liable for sums due under contracts entered into by the bankrupt after the bankruptcy?

No. The bankrupt can continue to trade after the bankruptcy order (subject to the bankruptcy restrictions). Any new debts created cannot be claimed in the bankruptcy.

As an unsecured creditor, what information am I entitled to?

The OR must send at least one report to creditors after their appointment. This will usually contain a statement of affairs completed by the bankrupt showing details of their assets and liabilities.

The trustee must send annual progress reports to creditors until the bankruptcy is complete at which time the trustee will send a final progress report.

How can I help the trustee to achieve the best possible outcome for creditors?

The unsecured creditors can form a creditors committee to help the trustee (see below). You should also tell the trustee if you believe that the bankrupt has assets, income or business interests that they have not disclosed, or if you think you may have any information that might be useful to the trustee.

Can the unsecured creditors form a creditors' committee?

Where the OR is not acting as trustee, yes, the creditors have the right to appoint a committee which must consist of at least three or not more than 5 creditors.

The creditors' committee's main roles are to monitor the trustee, represent the general body of creditors and approve the trustee's remuneration. The first meeting of the committee must be called by the trustee within six weeks of its establishment and subsequent meetings will be held as agreed, requested or needed.

The trustee must report to the committee on the progress of the bankruptcy at least every six months unless the committee directs otherwise.

If no creditors' committee has been previously formed, the trustee must invite creditors to form a committee when any decision of the creditors is sought. Creditor committee members are not paid.

R3 has produced a separate guide explaining insolvency creditors' committees, which is available [here](#) or from the person who gave you this guide.

How is the trustee's fee determined?

The creditors' committee (if there is one) or the general body of creditors agree the trustee's fee, failing which it will be determined in accordance with the statutory scale or fixed by the court. The fee can be fixed:

- As a percentage of the assets realised or distributed (or both); or
- By reference to the time spent properly spent by the trustee and their staff taking into account the complexity of the case; any exceptional responsibility borne by the trustee; the effectiveness with which the trustee carries out their duties; and the value and nature of the bankrupt's assets; or
- As a set amount
- A combination of the above is also appropriate.

R3 has produced a separate guide explaining insolvency officeholders' remuneration, which is available [here](#) or from the person who gave you this guide.

When does the trustee cease to act?

The trustee may continue to act after the bankrupt has been discharged if they need to continue in office, for example if there are still assets to realise or creditors' claims to be agreed.

Also, the trustee may cease to act before the bankrupt has been discharged if they have completed their work by that time.

What should I do if I'm just dissatisfied with the trustee's handling of the case?

You should first contact the trustee to try to resolve the problem. If you are still not satisfied, you can submit a complaint to the IP's regulator via the [Insolvency Service complaints portal](#).

R3 is the UK's leading trade association for licensed insolvency practitioners and business recovery professionals. R3 does not license or discipline its members; this is the responsibility of the practitioner's regulatory body. The regulatory bodies are:

The Institute of Chartered Accountants in England and Wales

Tel: 01908 248100 www.icaew.co.uk

The Insolvency Practitioners Association

Tel: 0330 122 5237 www.ipa.uk.com

The Institute of Chartered Accountants of Scotland

Tel: 0131 347 0100 www.icas.org.uk

Chartered Accountants Regulatory Board

Tel: 028 9043 5858 www.carb.ie/en/CARB/

Disclaimer

Information in this guide is intended to provide an overview only and relates to Company Voluntary Arrangements in England and Wales. It is not a replacement for seeking advice specific to your circumstances.