

The Spiralling Costs of Bankruptcy

During the past year the costs of bankruptcy, have experienced a dramatic increase.

This article will examine in more detail the increased costs of bankruptcy and their effect on a debtor seeking to annul a bankruptcy order by payment of the debts and expenses in full.

Increase in minimum petition debt to £5,000

The first significant change took place on 1 October 2015 when the minimum level of debt owed to a creditor to enable them to present a bankruptcy petition was increased from £750 to £5,000. The level had remained at an historically low level for a long time, and was undoubtedly due for review. However it was the level of increase that was surprising. For a creditor to issue a bankruptcy petition, they must be owed at least £5,000. This means that a diligent debtor will, in order to prevent a bankruptcy order being made, have to pay both the increased level of debt together with the increased petition costs (about which more below). For a debtor who has received a bankruptcy petition, this presents a much more difficult hurdle to overcome than the relatively modest figures involved in the past.

Petition costs increase

Unfortunately it is not only the petition debt that has increased. The costs of presenting a bankruptcy petition have also seen a substantial hike. The increase applies from 21 July 2016, to all bankruptcy and compulsory winding-up orders made on petitions presented after that date.

Taking a creditor's bankruptcy petition as an example, on presentation of the petition the bankruptcy deposit has increased from £825 to £990. In addition to this, on the making of a bankruptcy order, the bankruptcy administration fee has increased from £1,990 to £2,775. These are significant increases in bankruptcy costs. However, the biggest change is the new general fee of £6,000. That fee will be payable on the making of a bankruptcy order. Previously the fee was calculated by reference to a sliding scale based on the assets realised in the case only.

The new general fee should not be confused with a further new fee which is payable to the Official Receiver where he acts as trustee/liquidator. This new fee is calculated as 15% of the value of the assets realised and is payable in addition to the general fee. In the case of a creditor's petition, the initial costs that are payable on the making of a bankruptcy order look like this:

1.	Petitioning Creditor's Costs (estimate)	£ 1,000.00
2.	Official Receiver's Deposit	£ 990.00
3.	Official Receiver's Administration Fee	£ 2,775.00
4.	Official Receiver's General Fee	£ 6,000.00
		£10,765.00

Annulment will become more expensive

Assuming that the debtor has only one creditor of the minimum amount i.e, £5,000 this means that a debtor wishing to pay off the bankruptcy order, would need to find a figure in excess of £10,765 (not including the debtor's own legal costs), in order to annul the bankruptcy order.

The annulment of a bankruptcy order by payment of the debts and expenses in full is a common occurrence. Following the making of a bankruptcy order the bankrupt's bank accounts will be frozen. They will encounter considerable difficulties in raising the funds to enable the bankruptcy order to be annulled. The recent increases in bankruptcy fees will only serve to make that task more difficult.

Individual Voluntary Arrangement

An Individual Voluntary Arrangement ("IVA") is often used as an alternative to annulling the bankruptcy order based on payment of the debts and expenses in full. A proposal which is approved by creditors post-bankruptcy will lead to an annulment of the bankruptcy order being made under section 261(2) of the Insolvency Act 1986.

Where the bankruptcy order is annulled following the approval of a voluntary arrangement pursuant to s 261 of the Insolvency Act 1986, the increased expenses incurred by the Official Receiver in relation to the bankruptcy estate remain a charge on the property of the former bankrupt (Rule 5.26), and will need to be provided for in the debtors proposal.

Possible savings of new fees?

Following bankruptcy, if the bankrupt acts quickly in seeking an annulment, it may still be possible to achieve savings in the Official Receiver's costs. In the case of quick annulments funded with genuine third party funds, it has been suggested that the Official Receiver may substitute a fee based on time costs instead of the full general fee of £6,000.

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It should be emphasised that these are early days and detailed guidance is likely to be issued by the Insolvency Service as to the way in which these new charges will be charged to the estate and within what time scale any reductions will be allowed.

Annulment and Insolvency Service Account fees

The charging of Insolvency Service Account ("ISA") or Department of Business Innovation and Skills ("DBIS") fees to a bankruptcy estate has also been contentious in relation to annulment applications for bankruptcy orders made prior to the recent changes introduced in July 2016. One particular area of dispute concerns the use of third party monies to save ISA fees in the case of annulment applications based on payment of the debts and expenses in full. The Insolvency Service has challenged such savings where third party monies have been used to discharge the debts and expenses of the bankruptcy rather than realising assets available within the bankruptcy estate. It is understood that there are cases pending on which judicial guidance is awaited as to the application of ISA fees in such circumstances. This is an area where guidance from both the Court and the Insolvency Service is awaited and is likely to have a significant impact on the way in which costs will be charged to bankruptcy estates.

The whole bankruptcy process has become considerably more expensive. In addition to the increased costs to be levied to the bankruptcy estate by the Official Receiver, there is also the additional challenge to the annulment of bankruptcy orders by the use of third party funds to pay the debts and expenses in full. If the Insolvency Service is successful in its challenge to the saving of ISA fees where third party monies are used, then this will add a significant further cost to a bankrupt wishing to annul the bankruptcy order.

A bankruptcy order has always been something which if at all possible should be avoided. Despite the perception that the stigma of bankruptcy has been removed, the financial implications of bankruptcy remain severe. The dangers and costs of a bankruptcy order being made should not be underestimated even in circumstances where the debtor disputes the creditor's claim. In those situations it is better to take a step back and take specialist insolvency advice.

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