A guide to individual voluntary arrangements

Introduction

A voluntary arrangement for individuals in England and Wales is a procedure whereby a scheme of arrangement, usually involving delayed or reduced payment of debts, is put forward to creditors. Such a scheme requires the approval of the court, and is under the control of a supervisor. Provisions for similar procedures exist in Northern Ireland and Scotland, which are discussed in more detail below.

Prior to the introduction of voluntary arrangements in 1986, an individual who was unable to pay his creditors might attempt to ignore the situation and hope that no creditor raised a petition for his bankruptcy. Other than taking matters into his own hands and filing for his own bankruptcy the only course of action open to a debtor was contained in the Deeds of Arrangement Act 1914. This allowed a debtor to come to an arrangement with his creditors based on reduced or delayed debt repayments but did not prevent a dissenting creditor petitioning for the debtor's bankruptcy. As a result, such arrangements came to be used less and less frequently. The provisions relating to the more effective and legally binding system of individual voluntary arrangements are now to be found in the Insolvency Act 1986.

Interim order

If protection from hostile creditors is needed an application is made to the Court for an interim order. The application may be made by the debtor or, if the debtor is an undischarged bankrupt, either by the debtor, the trustee of his estate or the Official Receiver. The purpose of the interim order is to protect the debtor's property while the proposal is being considered. During the period after the application is submitted the Court may stay any legal processes against the debtor and, if the debtor is an undischarged bankrupt, an interim order may contain provisions for the conduct of the bankruptcy.

The Court will grant an interim order only if it is satisfied that the debtor intends to submit a proposal to his creditors and that, on the day of making the application, he was an undischarged bankrupt or was in a position to petition for his own bankruptcy. An order will not be granted if the debtor has made a similar application within the previous 12 months. It is not necessary at this stage for the proposal to be set out in detail but in many cases the proposal is prepared before the application for the interim order is made.

Once an interim order has been granted, the debtor is protected from bankruptcy petitions and, unless the Court gives leave, no other legal action may be commenced or continued against the debtor. Unless the nominee or the debtor applies for an extension, the order expires after 14 days.

The proposal

The debtor must prepare a proposal explaining why an arrangement is desirable and why the creditors may be expected to agree to it. The proposal is submitted to a 'nominee', who must be an insolvency practitioner, for his consideration and comments. In practice, the nominee will have assisted in preparing the proposal. The proposal must contain details of the assets to be included (or excluded) and any assets to be provided by others. Details must also be given of the nature and amount of the debtor's liabilities (noting those guaranteed by others), the extent to which there may be claims from secured, preferential or associated creditors and the manner in which claims are proposed to be dealt with. The proposal must also state whether in the event of bankruptcy, there could be claims relating to transactions at an undervalue, preferences or extortionate credit transactions.

The proposal must set out the proposed duration of the voluntary arrangement, when creditors may expect a distribution and how much they may expect to receive. Estimates of the remuneration and expenses of the nominee and the supervisor must also be disclosed, together with details of the supervisor's role and qualifications. (Once a voluntary arrangement is approved the person carrying out the function of the nominee becomes known as the supervisor.)

In addition to the information required to be disclosed by the insolvency rules the proposal should also include a brief explanation of the background to the debtor's predicament and his plans, if any, for the future. The proposal should be realistic, informative and achievable.

Nominee's report

The nominee must submit a report to the Court giving his views as to whether the proposal is worthy of being considered by creditors. Where an interim order has been made it must be submitted not less than two days before the interim order expires based on information provided by the debtor. The report is placed on the Court file and may be inspected at any time by any creditor. The nominee must state whether, in his opinion, a meeting of the creditors should be called to consider the proposal and, if so, the date, time and place of such a meeting. If the Court is satisfied that a meeting should be held, the period of the interim order will be extended accordingly but the meeting must take place between 14 and 28 days after the nominee submits his report. Notice must be sent to all known creditors at least 14 days before the meeting, accompanied by copies of the proposal and a statement of affairs (including a list of creditors), the nominee's comments on the proposal and a proxy form. Notice of the meeting does not have to be advertised.

Creditors' meeting

The creditors' meeting to approve the proposal must be held at a convenient venue for the creditors between 10.00am and 4.00pm on a business day and must be chaired by the nominee or his substitute (who must be suitably experienced).

Creditors are entitled to vote provided written notice of their claims have been submitted to the chairman either before or at the meeting. There is no requirement for proxy forms to be submitted prior to the meeting – they may be taken by the proxy holder to the meeting. Votes are calculated according to the amount of a creditor's debt but votes of secured creditors are calculated on the unsecured part of their debts only.

At the meeting, a resolution to approve or modify the proposal requires a majority of three-quarters in value of the creditors present (in person or by proxy) and voting. Other resolutions may be passed by a simple majority. However, a resolution will be invalid if those who vote against it include over half in value of the independent creditors, i.e. creditors who have no connection with the debtor.

The meeting may be adjourned (as many times as may be required) until the proposal is either accepted or rejected but no adjourned meeting may be held more than 14 days after the original meeting. The meeting may approve the proposal as presented, or may approve it with any modifications as agreed by the debtor (including a change of supervisor). Once the creditors at the meeting approve the arrangement every person who had notice of and was entitled to vote at the meeting, whether or not he actually did so, is bound by the agreement. The meeting cannot, however, affect the rights of secured or preferential creditors without their consent.

The chairman must prepare a report on the meeting and file a copy with the Court. He must also inform all those who were given notice of the meeting whether or not the proposal was accepted, and if so whether it was modified. If the proposal is approved, the chairman must lodge details of the arrangement with the Secretary of State for inclusion in a register available for public inspection.

Challenge of decisions

Within 28 days of the report on the creditors' meeting being filed with the Court or in the case of a creditor who only subsequently becomes aware of the arrangement within 28 days of finding that out an application challenging the decision may be made either by the debtor, a person entitled to vote at the meeting, the nominee or any person who has replaced him, or the trustee of the estate or the Official Receiver if the debtor is an undischarged bankrupt. The challenge may be made on the grounds that the arrangement approved at the meeting unfairly prejudices the interest of a creditor or that there has been some material irregularity at, or in relation to, the meeting. If the Court upholds the challenge it may give instructions that a further meeting should be held to consider a revised proposal or that the meeting be reconvened to hear the original proposal again.

The supervisor

The supervisor takes charge of the assets included in the voluntary arrangement and takes steps to agree creditors' claims so that the proposed distribution may be effected. The supervisor may have other duties including monitoring progress as set out in the proposal. He is also required to keep accounts and records of his transactions during the term of the arrangement. At a maximum of 12 monthly intervals, the supervisor must prepare a summary of receipts and payments which must be sent, within two months, to the Court, the debtor and those creditors bound by the arrangement. In addition to this summary the supervisor must include a report commenting on the progress made. The supervisor acts under the supervision of the Court and may apply to the Court for direction on any matter relating tot he voluntary arrangement.

Completion of the voluntary arrangement

Once the arrangement has been completed, the supervisor reports on the implementation of the arrangement and any variation from the proposal must be explained. The report must also summarise the receipts and payments made by the supervisor.

Some questions answered

Should a creditor accept the debtors proposal?

Although the Act provides an insolvent individual with the framework necessary to come to an arrangement with his creditors, there has been a tendency for some debtors to propose a voluntary arrangement merely to avoid the stigma of bankruptcy. Upon receiving notice of such a proposal the creditor should consider the matter very carefully, attend the meeting and question both the debtor and the nominee thoroughly. If the proposal appears to be genuine and have a reasonable chance of success, particularly if the return to creditors is likely to be better than if bankruptcy, a creditor should tend to be in favour. If, however, it is clear that the proposal is ill founded and has very little chance of success, a creditor should oppose the arrangement and petition for bankruptcy.

In practice, voluntary arrangements have failed to gain the necessary support because creditors believe there may have been fraud or other irregularities and that the supervisor is powerless to investigate.

What should a creditor ask about the nominee and supervisor?

In assessing the merits of a proposed voluntary arrangement a creditor should have regard to the professional standing of the nominee and the extent to which the proposal outlines the duties and responsibilities of the supervisor. A creditor should be concerned that the arrangement provides the supervisor with sufficient authority to take appropriate action if the debtor fails to fulfil his obligations. Experience over the past few years has shown that there can be difficulties in ensuring that debtors comply with the terms of the arrangement.

Should creditors form a committee?

The Act does not provide for the formation of a creditors' committee in relation to an individual voluntary arrangement. As creditors' committees are widely used in other situations (in liquidations, administrations and receiverships) to sanction procedures and monitor progress, the creditors considering a proposed voluntary arrangement may wish to establish their own informal committee. Such a committee, however, will have little authority unless agreement can be reached between all parties as to its powers, duties and responsibilities.

Why and when do voluntary arrangements fail?

Even though a voluntary arrangement receives the necessary creditors' approval it may still fail due to the debtor losing interest in the scheme or refusing to co-operate further and what causes failure should be clearly defined in the proposal. Alternatively, it can be altered at a later date with creditors' agreement.

Does a voluntary arrangement protect a debtor from future bankruptcy petitions?

Although creditors may agree to a voluntary arrangement, the debtor is not protected from future bankruptcy petitions. If the debtor fails to abide by the requirements of the arrangement the supervisor or the creditors may petition the Court for a bankruptcy order. In addition the debtor may incur further credit after the implementation of the arrangement. New creditors are not parties to the voluntary arrangement and are therefore entitled to petition for the debtor's bankruptcy.