

Dealing with individuals and companies in financial difficulties

Introduction

Insolvency is when a business does not have enough assets to pay its debts. Businesses predict what we need, and then supply it. But it is a prediction – therefore running a business means there is a risk of failure. Each business has a particular legal form. Small businesses such as sole traders (one person ownership) and partnerships are run by individuals and have unlimited liability.

Unlimited liability means that, if the business cannot meet its commitments, the personal property of the owner can be taken to pay its debts. In a limited company, the most the owners will lose is the value of their shares.



Dealing with Insolvency

Every insolvent business could be closed down. However, this would be very wasteful as, with help, many businesses could still be productive. Many businesses fail through cash flow problems. A profitable business, with full order books, may not be able to pay its suppliers because its own customers have not paid. Suppliers may insist on payment and cause insolvency.

The Insolvency Service deals with one type of business insolvency – compulsory liquidation. If a company owes money it cannot pay, the business can be closed by the courts – it is ‘wound up’. When this happens, the Insolvency Service makes sure that the assets of the business are used to pay back money the business owes to its creditors. The Service also has to distinguish between bad luck and bad behaviour.

If it thinks the business has failed due to bad or improper behaviour by a company’s directors, it can make sure that the directors are punished by the courts.

There are alternatives to this type of insolvency. An independent professional – (an insolvency practitioner) can either try to rescue the business through a process called Administration. Or they can arrange for the orderly distribution of assets through a process called Company Voluntary Arrangement (CVA).

Individuals

Insolvent individuals can be declared bankrupt by the courts. Bankruptcy means a fair distribution of assets to creditors. The Insolvency Service manages the process to distribute the assets. They also check to make sure there has been no improper behaviour. Bankrupts who have acted illegally or improperly can be restricted from business activity by the courts.

An individual with debts could propose to pay repay their creditors over a fixed period of time. With the help of an insolvency practitioner and permission from the courts, a legally binding agreement -Individual Voluntary Arrangement (IVA) can be arranged. An IVA is an alternative to bankruptcy for individuals.

Conclusion

The Insolvency Service provides the systems to make sure assets are distributed fairly for both individual and business failure for the benefit of creditors.

