

# Insolvency

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take hold and therefore will not significantly affect overall insolvency numbers until the latter end of 2011 and early 2012. However, the mix of solutions being utilised will change.

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Although debt relief orders (DROs) will continue to rise in 2011 as general awareness of the solution continues to grow, levels are unlikely to peak until 2013. While bankruptcy numbers look – on the face of it – to have fallen in recent months, it is important to note that when combined with DROs, personal insolvency num-



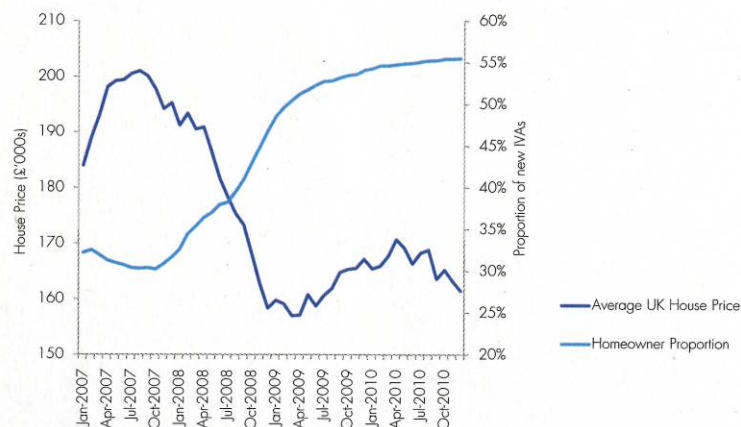
Some of the historical barriers to going bankrupt (sequestration) in Scotland have already been removed. Scottish debtors no longer have to wait for their creditors to take legal action against them to declare themselves bankrupt. As long as they fulfill certain requirements and owe a minimum of £1,500 they are able to apply for bankruptcy themselves via an insolvency practitioner. No matter what social stigma bankruptcy still holds, it is inevitable that this will make bankruptcy more accessible and will drive an increase in Scottish debtors opting for this solution in 2011.

A further change that will drive a shift in the mix of solutions in Scotland is the opening up of debt arrangement schemes (DAS) to be offered via commercial organisations. Having previously only been available via money advisers, this will broaden the reach of this solution, which in turn will drive up numbers. Creditors need to be ready to deal with this influx.

There are also some changes ahead for the trust deed which will bring potential benefits for consumers and creditors alike. A Trust Deed Protocol, similar to the IVA Protocol, will enter consultation in 2011. Having been formulated by a cross-industry working party including TDX, IPs, regulators, money advisers and bodies such as the AiB and the BBA, it is possible it will come into effect in 2011. It will drive changes to fee structure and distribution schedule, making the trust deed closer aligned to the IVA. As a result, creditors and consumers will see benefits, with consumers paying fairer and more sustainable fees, and creditors getting better returns, faster.

While 2011 may not hold any big changes when it comes to personal insolvencies, the backdrop of uncertain market factors means it will be a critical year in understanding insolvency returns. With the widely anticipated growth of the debt sale market and niche insolvency purchasers emerging, fully understanding insolvency volumes, returns and changes in the mix of solutions will be critical to ensuring optimal value and best management of this asset class. **CT**

## House Prices and Homeowners



Source: Halifax House Price Index  
Source: TDX Group

## Corporate insolvencies: hope floats

The figures for corporate insolvencies during 2010 have provided some hope. Last year saw a fall of almost a quarter in the number of firms going bust, according to PricewaterhouseCoopers (PwC). Figures reveal a total of 15,894 firms became insolvent in 2010. This was down from 19,512 the previous year, representing a 23 per cent dip.

"2010 has seen insolvency volumes stabilise as businesses are proactively managed in intensive care and options other than insolvency are pursued with vigour," says Mike Jervis, business recovery services partner at PwC. "However, UK businesses are certainly not out of the woods yet, as we expect looming public sector cuts to hit the bottom line of many public sector suppliers."

In the fourth quarter of last year, 3,605 firms became insolvent, but this was a six per cent decrease on the previous quarter, and a 19 per cent fall on the corresponding quarter of 2009. Despite the fact that 565 construction firms and 399 retailers entered insolvency last year, PwC said that all the worst affected sectors had shown a marked improvement compared with 2009's figures.

## Equity cures

Other market experts are not brimming with optimism for 2011. Mike Corner-Jones, managing director with Alvarez & Marsal, says that companies will need to explore equity cures or financial restructurings, although companies with good business plans will have access to capital markets, including high-yield bonds.

"There will be more restructurings this year than last, and a steady pipeline over the next couple of years," he comments. "The difficult macro-economic environment in Europe will pose problems for businesses that borrowed in 2007-08 with over-optimistic business plans."

Nick Oliver, a partner in Howes Percival's insolvency and corporate recovery group, believes history suggests that the number of formal insolvencies should rise as the economy emerges from recession. He points to the anticipated 'tsunami' of insolvencies, expected because of the relatively benign economic conditions, including interest rates and the current attitude of the banks, which are hiding latent problems.

"I think it is a safe bet that we will start to see both the personal and corporate numbers rise in 2011," Oliver explains. "Whether it will be a 'tsunami' or a gradual increase over an extended period depends to a large extent on how and when these benign conditions change. It is probably also a safe bet, based on the current conditions, that we will see a higher number of insolvencies with investigation and fraud type issues. Sadly, we are also likely to see a lot more 'burial' type liquidations, with no business that can be rescued and no assets that can be sold."

bers are still at an all-time high [see chart].

Creditors should also expect to see an increase in those seeking informal debt solutions in the second half of 2011. This will be driven by the continued lack of refinancing options and the commencement of government cuts, which will result in an increase in individuals turning to debt management plans (DMPs) as the natural first solution when they find themselves in financial difficulties.

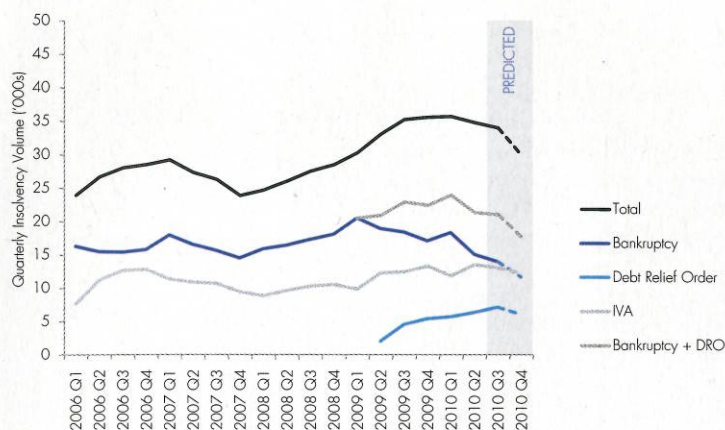
IVA numbers will remain steady through 2011 as the solution continues to be a safe haven for consumers, especially for homeowners who now represent close to 55 per cent of all accepted IVA proposals. Volumes in 2010 were five per cent higher than in 2009, partly supported by a lower IVA reject rate which TDX data shows has decreased by a staggering 67 per cent since 2007. This is testament to the hard work of all stakeholders in the industry in driving the IVA Protocol to deliver a closer alignment of the needs of debtors, insolvency practitioners (IPs) and creditors – something which the SIVA would not have achieved.

**Additional plans**

Although overall volumes look set to remain steady, creditors need to plan for returns from IVAs coming under increasing pressure (see box). Firstly, while the cost of living remains stubbornly high, disposable incomes will continue to fall unless salaries start to increase to keep pace. Indeed, the most recent CCCS expenditure guidelines suggest consumers will have £20-£30 less per month to pay creditors, and any future rises in interest rates – now frequently predicted for Q4 2011 or even sooner – will only add further pressure on the consumer wallet. With agreed dividends already at historic lows, these factors could combine and continue the downward trend in returns.

Secondly, the economic factors of continued high inflation and potential for interest rate rises combined with public and private sector job losses will put significant pressure on the sustainability of contributions from those already in an IVA. Fortunately, the IVA Protocol provides for changes

**Insolvency volumes**



Source: Insolvency Service

in both short-term and long-term circumstances. Providers, however, will need to ensure they have robust systems, processes and controls in place to monitor arrears, and proactively assist consumers to maintain or vary their plans accordingly.

Thirdly, equity release is also under pressure. The number of individuals entering an IVA who are homeowners has been steadily rising for some time. However, the reduction in house prices means less equity will be available to release. This will be further exacerbated by the continued lack of refinancing options for con-

sumers. As a result, while equity release may have been factored into an IVA four years ago when the housing market was more buoyant, much of it just is not going to materialise in the next 12 months as the plans come to their conclusion. TDX estimates that this could result in creditors facing a £40m shortfall in 2011 alone. (see graph page 36).

**Scottish solutions**

In addition to these economic influences, regulatory and industry changes will affect Scottish debtors, influencing the mix of solutions they utilise.

**What creditors can do**

**Know your customers.** Proactive use of the right data sources can enable creditors to quickly identify those individuals who are in financial difficulty. This is critical in reducing the time lag between an individual becoming insolvent and creditors updating account information, and can minimise credit risk while also ensuring the customer is treated appropriately.

**Know your third party providers.** Providers must have appropriate systems and processes to support the plans they manage. Relative performance between providers is significant, and only through having a comprehensive data-based view of supplier performance can targeted conversations take place to deliver improvement. This approach will ensure breakage is minimised during a prolonged period of hardship for consumers.

**Know your portfolio and provision appropriately.** All IVAs are not the same. We have observed that as the volume of IVAs begins to grow and the industry portfolio seasons, patterns are emerging that provide insight into the divergence of performance between IVA cases that on the surface appear homogenous. As a creditor it is possible to assess the appropriateness of your IVA provisioning at a segment level, factoring in plan variables, macro-economic conditions, customer demographic and supplier performance. It will also enable creditors to evaluate, if appropriate, the value and risk benefits of selling an IVA portfolio.

