|  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Title: **Bankruptcy and Insolvency fees increase order 2015/16**  IA No: BIS INSS15002    Lead department or agency:  The Insolvency Service  Other departments or agencies:  Department for Business Innovation and Skills | |  | | --- | | Impact Assessment (IA) | | Date: 030/9/2015 | | Stage: Final | | Source of intervention: | | Type of measure: | | Contact for enquiries: David Miller 0207 637 6445, Angela Crossley 0207 637 6660 | |  | |  | |  | |  | |  | |  | |
| Summary: Intervention and Options | **RPC Opinion:** |
|  | |

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Cost of Preferred (or more likely) Option | | | | |
| Total Net Present Value | Business Net Present Value | Net cost to business per year (EANCB on 2009 prices) | In scope of One-In, Two-Out? | Measure qualifies as |
| 0 | 0 | N/A | No | N/A |
| What is the problem under consideration? Why is government intervention necessary?  Lower caseloads for official receivers (officials dealing with the administration of bankruptcies and companies in compulsory liquidation) than forecast is leading to a forecast operational deficit of around £1.2m in 2016/17. The problem under consideration is the need to raise fees to cover costs. In addition, the fees need to be set in such a way as to comply with "Managing Public Money" principles. Government intervention is the only means available for raising income for the Insolvency Service, if this it not possible the deficit would continue to be funded by the Department of Business, Innovation and Skills and ultimately by taxpayers. | | | | |

|  |
| --- |
| What are the policy objectives and the intended effects?  The main objective is to increase fees in order to eliminate deficits and cover costs. The intended effect is a shift from taxpayers subsidising the operational deficit to increasing income which will aid full cost (but no more) recovery.  The other objective is to reduce the reliance on cross subsidisation of cases and arrange for income from individual cases to more closely match costs. Here the intended effect is to create a fairer and more transparent funding structure for official receiver cases. |

|  |
| --- |
| What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)  (0) Do nothing – The insolvency fees in the next financial year would remain unchanged. Even allowing for continued efforts of cost reduction, with current caseload levels and the anticipated decline in future case numbers, the gap between case administration fees and the cost of carrying out official receiver work would mean that deficits would persist.  (1) Increase case deposits and case administration fees. Change the Secretary of State fee bands.  Option 1 is the preferred option. This option would remove the losses incurred by the Official Receiver in administering insolvency cases; benefit taxpayers (subsidies would be reduced) and it would reduce the reliance on cross subsidy for official receiver cases, making the funding of cases more compliant with “Managing Public Money” principles. |

|  |
| --- |
| Will the policy be reviewed? It willbe monitored internally. If applicable, set review date: 04/2016 |

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| Does implementation go beyond minimum EU requirements? | | | N/A | | | |
| Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base. | **Micro**  Yes | **< 20**  Yes | **Small**  Yes | **Medium**  Yes | | **Large**  Yes |
| What is the CO2 equivalent change in greenhouse gas emissions?  (Million tonnes CO2 equivalent) N/A | | | Traded:       0 | | Non-traded:       0 | |

I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) that the benefits justify the costs.

|  |  |  |  |
| --- | --- | --- | --- |
| Signed by the responsible : | Anna Soubry | Date: | 19th Oct 2015 |

# Summary: Analysis & Evidence Policy Option 1

Description: Increases to deposits and administration fees in bankruptcy and company winding ups. Changes to the Secretary of State fee

FULL ECONOMIC ASSESSMENT

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Price Base Year 2015 | PV Base Year 2015 | Time Period Years 10 | Net Benefit (Present Value (PV)) (£m) | | |
| Low: -8.61 | High: 8.61 | Best Estimate: 0 |

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| COSTS (£m) | Total Transition   (Constant Price) Years | | Average Annual  (excl. Transition) (Constant Price) | Total Cost  (Present Value) | |
| Low | N/A | N/A | 2.5 | 21.6 | |
| High | N/A | 3.5 | 30.2 | |
| Best Estimate | N/A | **2.0** | 17.3 | |
| Description and scale of key monetised costs by ‘main affected groups’  Petitioners will incur a greater cost to commence insolvency proceedings estimated to be around £0.51m per year. Of these creditors who wish to petition for a debtors bankruptcy will incur an increased cost of initiating bankruptcy proceedings of around £0.26m. Those who wish to petition to wind up a company will incur an increased cost of around £0.25m. There will be a cost to the insolvency service from the reduction in the SOS fee of between £2.0m and £3.0m this is transferred to other creditors. | | | | | |
| Other key non-monetised costs by ‘main affected groups’  There will be no non-monetised costs from this proposal. | | | | | |
| BENEFITS (£m) | Total Transition   (Constant Price) Years | | Average Annual  (excl. Transition) (Constant Price) | Total Benefit  (Present Value) | |
| Low | N/A |  | 2.5 | 21.6 | |
| High | N/A | 3.5 | 30.2 | |
| Best Estimate | N/A | **2.0** | 17.3 | |
| Description and scale of key monetised benefits by ‘main affected groups’  The Insolvency Service will benefit from an increase in income of approx. £1.4m, this income raised via higher administration fees is effectively a transfer from creditors. Creditors will benefit from a reduction in the assets paid out via the SOS fee, estimated to be between £2.0 and £3.0m per year. This reduction in SOS fee is a transfer from the Insolvency Service to creditors. | | | | | |
| Other key non-monetised benefits by ‘main affected groups  The changes will lead to a more transparent funding structure for the Insolvency Service where the costs of administering cases more closely matches the income received. | | | | | |
| **Key assumptions/sensitivities/risks** Discount rate (%) | | | | | 3.5 |
| Creditors and others may be unwilling to pay the increased costs to petition individuals for bankruptcy or to put companies into compulsory liquidation, we assume this impact is minimal as case numbers don’t appear to be price sensitive.  There is a risk that forecasted case numbers will differ significantly from actual cases numbers putting at risk the public money that will be needed to offset any deficit. | | | | | |

BUSINESS ASSESSMENT (Option 1)

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Direct impact on business (Equivalent Annual) £m: | | | In scope of OITO? | Measure qualifies as |
| Costs: N/A | Benefits: N/A | Net: N/A | No | N/A |

**Evidence base**

**Policy background**

1. The costs of administering bankruptcies and compulsory liquidations are recouped from deposits payable to enter the insolvency process and charges against assets realised in insolvency cases. The Insolvency Service is has been incurring operational deficits due to continuing falls in the number of individuals entering bankruptcy and companies going into compulsory liquidation. Although the Insolvency Service continues to reduce costs, for example a reduction in staff costs of £32m and estate costs of £5m between 2010/11 and 2014/15, falling case numbers mean there is a higher share of fixed costs per case, which cannot be easily or quickly remedied. Even with ongoing programmes to reduce estates and staff costs, the steep fall in case numbers means there remains a deficit, which is funded by BIS/the taxpayers.
2. As a result, the Insolvency Service proposes increases to certain insolvency case deposits and fees to offset the costs of administering insolvency cases. These increases will work alongside the Insolvency Service’s efficiency plans and other changes to prevent an operational deficit in 2016/17.
3. The legal basis for the fees relating to company and individual insolvency proceedings is set out in the Insolvency Act 1986 S 414 and S415 respectively, which provide that in respect of the performance by the official receiver or the Secretary of State of functions under the relevant parts of the Act, such fees shall be paid as the Lord Chancellor may, with the sanction of the Treasury, by order direct.
4. The Enterprise Act 2002 modernised the financial regime of the Insolvency Service by simplifying the fee structure and ensuring increased transparency and was preceded by an extensive consultation exercise. A Regulatory Impact Assessment was prepared for the Enterprise Act 2002. The changes proposed by this instrument are designed to maintain the principles of the financial regime introduced by the principal Order of the Act and in particular, that fees are set to match cost. Therefore no public consultation is proposed in respect of these fees increases. These changes are only to take place in England and Wales.

[[1]](#footnote-2)**Problem under consideration**

1. The number of bankruptcy cases has reduced significantly in the last few years. In 2008 there were 67,428 bankruptcy cases, and by 2014 the number had reduced to 20,322. Numbers are still falling. Overhead and staffing reductions have not been able to keep pace with the steep decline in case load resulting in a higher fixed cost per insolvency case. The Insolvency Service has significantly reduced costs,and continues to do so through a portfolio of projects that have delivered, at 31 March 2014, total savings realised of £7.1m compared to 2011–12 baseline data. However there still remains an operational deficit which will persist if no action is taken. There is a need for increases to certain insolvency charges to better balance costs and fees, which will work alongside the Insolvency Service’s efficiency plans, to prevent a deficit in 2016/17
2. The last significant changes in fees and deposits in April 2014 were intended to remove the operational deficit by 2015/16 but a sharper than forecast reduction in case loads has led to the need to increase fees and deposits to avoid incurring a deficit in 2016/17.
3. Table 1 shows the expected level of income based on the 2014 fees order forecasts with the current budgeted forecasts without any change to fees and deposits in November 2015:

Table 1: Impact on income of revised caseload forecasts

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Year** | **Case load forecast (Basis for April 14 fees order)** | **Forecasted Income (£m)** | **Case load (current)** | **Forecasted Income (£m)** | **Difference in forecasted income (£m)** |
| 2016/17 | 22,500 | 31.815 | 14,000 | 19.796 | 12.0 |

1. Table 1 showed there will be £12m less income in 2016/17 than previously forecasted. To counter the reduction in income greater reductions in staffing and estate costs have occurred but have been unable to keep pace with the fall in case numbers. In the absence of a change in fees the official receiver services will incur a deficit in 2016/17 of £1.22m.
2. At present, after the petition deposit is paid, the cost of administering the case (the administration fee) fee is recovered from assets realised by the Official Receiver, with any surplus funds being distributed to creditors. But it is often the case that there are insufficient assets to cover the administration fee. Indeed analysis of Insolvency Service case data indicates that around 50 per cent of cases do not have any assets from which a payment toward the administration fee can be made. Where there are insufficient or no assets, the administration costs are covered by a separate Secretary of State (SOS) fee, charged on those cases with sufficiently high asset levels. This means that there is cross-subsidisation between insolvency cases to cover costs.
3. Cross subsidisation is against the Managing Public Money Principle, set out by HM Treasury that fees should cover the cost of the work carried out and that all users of a given service should pay the same[[2]](#footnote-3). To reduce cross subsidisation, changes are necessary to the administration fee, deposits and the Secretary of State fee.
4. Therefore this fees order is aimed at solving two problems:

* Removing the operational deficit on official receiver work
* Reducing the cross subsidisation of official receiver cases whilst looking at longer term options to change the structure completely

1. In accordance with Managing Public Money principles, the Insolvency Service is required to carry out an annual review of the charging levels for its fee funded businesses.

**Rationale for Intervention**

1. The economic rationale for government intervention in insolvency and bankruptcy cases is that it is necessary to ensure a collective approach is taken by creditors when dealing with those companies in financial distress in response to the ‘prisoner’s dilemma’ faced by creditors. That is, in the event of a default, each creditor will have the incentive to be the first one to collect the assets of the insolvent. This approach will force the debtors to sell the assets piece by piece in order to pay each creditor in turn. However, creditors collectively might be able to get more if they took a coordinated strategy to divide and sell the assets or re negotiate loans and debts.
2. Managing the insolvency process comes at a cost, both to the courts[[3]](#footnote-4) from making bankruptcy and insolvency orders and to official receivers from dealing with cases. These costs should normally be covered by creditors who are the direct beneficiaries from the overall coordinated insolvency process, and HM Treasury rules set out in Managing Public Money, require fees to be set to cover costs. However the operational deficit in official receiver cases means this is not the case at present and that the tax payer is subsidising the cost for creditors. Government intervention is necessary to restore the balance of payments from the tax payer to creditors.

**Policy Objective**

1. The objective of the policy is to mitigate deficits to the Insolvency Service arising from the Official Receiver business by shifting the burden of funding from tax payers to creditors, who are the ultimate beneficiaries of the policy.
2. At the same time reducing cross subsidisation of official receiver cases should return more assets to creditors and ensure the cost of administering bankruptcy and winding up companies is related to the received income from these cases. Thereby complying with HM Treasury rules on managing public money.
3. Finally, in line with the current fees structure and charges which came into force on 1 April 2004 under the Enterprise Act 2002, the objective of the policy is also to produce an insolvency funding regime which is fairer, simpler and more transparent.

**Description of options considered (including do nothing)**

1. Two options have been considered:
   * Option 0 – Do nothing
   * Option 1 – Increase case deposits, administration fees and change the Secretary of State fee bands from 16 November 2015

**Option 0: ‘Do nothing’**

1. The insolvency fees and deposits in the next financial year would remain unchanged.
2. This would mean that the gap between income from deposits and fees and costs incurred in administering insolvency cases would continue to be in deficit, estimated to be £1.22m in 2016/17. Those costs would ultimately be passed to the taxpayer as the resulting deficit would have to be funded from departmental budgets. Without action, the Insolvency Service would continue to:
   * not comply fully with Government fees and funding guidance
   * be vulnerable to extreme fluctuations in insolvency case numbers
   * be vulnerable to changes in asset levels in insolvency cases; and
   * incur a mismatch between income and costs

**Option 1: Increase case deposits, case administration fees and change the Secretary of State fee bands**

1. This option would increase certain deposits to enter insolvency and the fees charged in insolvency cases. The changes to the SOS fee will mean creditors receive larger dividends payments following the completion of the Insolvency proceeding. The new fees would only be payable for petitions that begin on or after 16 November 2015. The details of the proposed changes for each type of fee/deposit are:

**Bankruptcy Creditor Petition Deposit[[4]](#footnote-5)**

1. Where a person is owed money[[5]](#footnote-6) by an individual or unincorporated trading entity, they may apply to the court for a bankruptcy order (‘creditor petition bankruptcy’) and it is proposed to raise the deposit payable, from £750 to £825.

**Compulsory Winding-up Deposit (companies)**

1. A company, its directors, or the creditors of a company (among other persons) may apply to the court for the company to be wound up (’compulsory winding up/ liquidation). It is proposed that the deposit payable should be increased, from £1,250 to £1,350. All of these deposit charges are payments made by relevant parties to commence bankruptcy or compulsory liquidation. In cases where there are sufficient assets to cover costs, these deposits will be repaid in priority.
2. The significant increases in the deposits are needed to reduce the cross subsidisation of cases.

**Bankruptcy Debtor / Creditor Petition Administration Fee**

1. Where a Bankruptcy or Winding-Up Order is made by the court, the administration of the insolvency proceedings is undertaken by the Official Receiver. The total costs of the Official Receiver (which are partly covered by the petition deposit) are met through ‘case administration fees’ charged against the assets realised in insolvency cases. It is proposed to increase the case administration fee charged in all bankruptcy cases (both debtor and creditor petition bankruptcies) from £1,850 to £1,990 and the fee in compulsory liquidations from £2,400 to £2,520.
2. The increases reflect the higher fixed cost per case that results from lower case numbers.
3. A summary of the proposed increases are in table 2 below.

**Table 2: Deposit and Administration Fee Increases from 16 November 2015**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Type of Charge** | **Current Amount** | **Revised Amount** | **% Increase** | **Date of last increase** | **Inflation/forecast inflation since last fee change[[6]](#footnote-7) %** |
| Bankruptcy Creditor Petition Deposit | £750 | £825 | 10.0 | April 2014 | 1.7 |
| Compulsory Winding-up Deposit (Companies) | £1,250 | £1,350 | 8.0 | April 2014 | 1.7 |
| Bankruptcy Debtor Petition Administration Fee | £1,850 | £1,990 | 7.6 | April 2014 | 1.7 |
| Bankruptcy Creditor Petition Administration Fee | £1,850 | £1,990 | 7.6 | April 2014 | 1.7 |
| Compulsory Winding-up Administration Fee (Companies) | £2,400 | £2,520 | 5.0 | April 2014 | 1.7 |

1. The objective of the April 2014 fees order was also to remove the official receiver deficit and fees increase and those changes were made in the context of fees remaining unchanged for a number years as shown in table 3.

**Table 3: Fee changes introduced April 2014**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Type of Charge** | **Current Amount** | **Revised Amount** | **% Increase** | **Date of last increase** | **Inflation from the last fee increase to April 14 %** |
| Bankruptcy Creditor Petition Deposit | £700 | £750 | 7.1 | June 2011 | 7.3 |
| Compulsory Winding-up Deposit (Companies) | £1,165 | £1,250 | 7.3 | June 2011 | 7.3 |
| Bankruptcy Debtor Petition Administration Fee | £1,715 | £1,850 | 7.9 | April 2007 | 22.58 |
| Bankruptcy Creditor Petition Administration Fee | £1,715 | £1,850 | 7.9 | April 2007 | 22.58 |
| Compulsory Winding-up Administration Fee (Companies) | £2,235 | £2,400 | 7.4 | April 2010 | 12.2 |

1. Table 2 and 3 show that even after accounting for the administration fee changes made in April 2014, the fee charged by the insolvency service as the cost of administering bankruptcy in 2015/16 will still be lower in real terms than it was in April 2007. While in the case of companies the cost of administering the case will be lower in real terms in 2015/16 than in April 2010.

**Changes to Secretary of State Fee**

1. The Secretary of State Fee is a cost recovery mechanism that is charged on bankruptcy and compulsory liquidation cases with significant assets. A proportional amount of the assets realised within different bands is taken as a fee up to a cap of £80,000. The fee is designed to subsidise the cost of other cases where the realised assets were insufficient to meet the administration costs of the case. The current bands were introduced for Insolvency Orders made after 6 April 2010.
2. Table 4 shows the current and proposed new structure for the SOS fees.

**Table 4: Current and new Secretary of State Fee bands**

|  |  |  |
| --- | --- | --- |
| **Applicable SoS Fee** | **Current** | **Proposed** |
| First £2,000 (£2,500 company) | 0% | No change |
| Next £1,700 | 100% | 75% |
| Next £1,500 | 75% | 50% |
| Next £396,000 | 15% | No change |
| Remainder[[7]](#footnote-8) | 1% | No change |

1. The proposed increases would only apply to new insolvency cases from commencement of the new Fees Order (expected to be 16 November 2015), there would be no retrospective charging or other similar provision.
2. The new SOS fees would only be charged where the insolvency petition was made on or after 16 November 2015. Cases commenced prior to this but still in progress would still be charged under the previous bands.
3. All other things equal the lower bands will reduce the average amount of SOS fee received per case and by assumption reduce the degree of cross subsidisation of cases.

**Monetised and non-monetised costs and benefits of preferred option;**

**Costs and Benefits of Changing Fee and Deposits**

1. This IA will discuss the impacts on groups including creditors, debtors and the Insolvency Service. Creditors can be quite a wide group including businesses, HMRC, Local Authorities, employees and consumers. Where possible this IA will describe the impact on different types of creditors. Taxpayers will also be affected by the changes and this impact will be discussed alongside that of the Insolvency Service.
2. The IA will use the current forecasts for official receiver case loads show in table 5.

**Table 5: Current caseload forecast for bankruptcy and compulsory winding up orders**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Year** | **Debtor Petitioner Bankruptcy** | **Creditor Petitioner Bankruptcy** | **Compulsory Company Winding up Orders** | **Total** |
| 2016/17 | 8,000 | 3,500 | 2,500 | 14,000 |

**Insolvency Service/Government cost and benefits**

**Benefits to Insolvency Service**

1. The lower than forecast caseloads has resulted in lower income for the Insolvency Service than predicted. Table 1 showed the significant reduction in income that resulted from the large drop in caseloads. Increasing the fees will enable the Insolvency Service to increase income from cases and to avoid incurring a deficit in 2016/17. Table 6 shows the impact on income from the fee changes versus the current forecasts income levels using the current case load forecasts.

**Table 6: Increased income received by Insolvency Service from changes**

|  |  |  |  |
| --- | --- | --- | --- |
| **Year** | **Current forecasted income £m** | **Forecasted new income following the changes £m** | **Increase in income from the changes £m** |
| 2016/17 | 19.796 | 21.196 | 1.4 |

1. Overall the changes will increase income to the Insolvency Service by approx. £1.4m in 2016/17. The appraisal period for this policy is 10 years but no forecasts are available on the level of income after 2016/17 so the £1.4m increase in 2016/17 has been projected to remain flat for the remainder of the appraisal. Again in accordance with Managing Public Money fees and charges are reviewed on an annual basis to ensure they cover cost.
2. The increase in income via the greater administration fee is a transfer from creditors to the insolvency service. The greatest beneficiaries will be business and the public sector creditors such as HMRC and local authorities.
3. The reduction in the deficit will reduce the reliance on taxpayers to fund the operations of official receiver services.

**Costs to the Insolvency Service**

1. The marginal transition costs associated with the implementation of this legislation are negligible for the Insolvency Service, as the cost of updating would be the same as notifying the stakeholders of no change - all material would have to be updated to reflect the new fiscal year regardless of whether or not there were any changes.

**Benefit to Creditors**

1. The new SOS fee bands will reduce the money taken by the Insolvency Service from cases where the costs of administering them are fully cost recovered. Cases with relatively small levels of assets will receive the greatest benefit with more assets paid to creditors. Analysis of administrative data held by the Insolvency Service estimates that when taken the average SOS fee is around £1,450 and that following the changes to the fee banding creditors will benefit by between £2 and £3m less being taken in fee payments. The increased returns to creditors are an economic transfer from the insolvency service to creditors.
2. Cases with significant assets that pay the SOS fee are also likely to be administered by an Insolvency Practitioner (IP). It is possible that a proportion of the returned assets to creditors from the changes in the SOS fee will be paid to IPs in fees.

**Costs to petitioners**

1. Petitioners will have to incur higher costs from the increase in deposits to initiate bankruptcy proceeding or to wind up a company. It is possible to estimate the net impact on petitioners from the higher costs by combining the forecasted case load numbers in tables with the change in deposit levels for bankruptcy and company compulsory winding up orders. The breakdown of these costs by the type of deposit is shown in Table 7.

**Table 7**: Increased cost to petitioners from higher deposits

|  |  |  |  |
| --- | --- | --- | --- |
| **Year** | **Creditor Petitioners Deposits £m** | **Compulsory Company Winding Up Orders £m** | **Total £m** |
| 2016/17 | 0.262 | 0.250 | 0.512 |

1. The higher deposits will cost bankruptcy creditors around £0.26m per year. HMRC is the largest single creditor in many insolvencies, the impact upon this Department is included as part of the costs upon creditors. Internal Insolvency Service statistics[[8]](#footnote-9) show that HMRC is a petitioning creditor in 40 per cent of bankruptcy cases, this would mean HMRC paying an additional £75 in creditor bankruptcy cases or £0.11m per year in additional costs to petition. Around a further 5 – 10% of cases come from local authorities who based on forecasted case load would have to pay an additional £0.01 to £0.03m.
2. A company petition can be initiated by creditors, directors or the company itself so the extra cost of the petition will be shared amongst these petitioners. Creditors account for the majority of other petitions with companies and directors on their own account, accounting for less than 5 per cent. Therefore the cost to creditors from higher company petition deposits is likely to be £0.24m. Of this HMRC is the petitioner in the majority of cases (around 56 per cent) meaning they will incur an additional cost of approximately £0.13m.
3. Petitioning creditors receive the repayment of their deposits from assets available in the estate, in the order of repayments they receive payment ahead of dividends to creditors so at least some of this cost will be repaid to petitioners. Therefore the figures presented are the maximum amount of money that could be paid by petitioners.

**Overall impact on Creditors**

1. Overall creditors should be better off following the changes with the benefit of lower payments of SOS fees greater than the higher cost of deposits and administration fees. After accounting for companies and directors on their own account petitioners, based on current forecasts it will cost creditors an additional £0.5m creditor bankruptcy petitions and company winding up petitions, while creditors are likely to be paying between £2 and £3m less in SOS fee payments.
2. This overall benefit to creditors may mask a different impact on particular types of creditors. For example it is possible that creditors that incur the majority of the costs of the higher petitions may not receive the majority of the benefit from the lower SOS fee.

**Impact on cross subsidisation**

1. Reducing the cross subsidisation requires that the cost per case be reflected in the fee charged. The significant number of cases with zero assets means that to cover the costs of administering these cases more payment is required to initiate proceedings. The Insolvency Service is taking three steps to reduce the cross subsidisation of official receiver cases:
   * By increasing the upfront deposit paid by petitioning creditors
   * By increasing the deposits by a greater amount than the increase in administration fees
   * By decreasing the proportion of assets that are used to pay the SOS fees
2. The payment of the deposit is deducted from the cost of the administration fee so even cases with no assets to realise will pay more towards the cost of administering the case. This reduces the need to rely on cases with substantial assets to cross subsidise the significant number of cases with insufficient assets to cover costs.
3. The greater increase in deposits versus the administration fee means a greater share of the cost of administering cases is paid at the commencement of a case and a reduced need to rely on asset realisation from the estate to pay the remaining administration fee. This reduction in cross subsidisation is shown in Table 8.

**Table 8: Changes** in the proportion of the cost of administering bankruptcy covered by deposit

|  |  |  |
| --- | --- | --- |
| **Type of case** | **Current percentage of administration costs covered by deposits %** | **New percentage of administration cost covered by deposits %** |
| Creditor petitioned bankruptcy | 40.54 | 41.46 |
| Compulsory Company Winding Up Orders | 52.08 | 53.57 |

1. Reducing the amount of fees that are paid via the SOS bands will all other things equal reduce the average SOS fee. The average SOS fee from across company and bankruptcy cases is estimated to be £1,450[[9]](#footnote-10). Following the changes to banding and using the current caseload forecasts it is estimated that the average SOS fee will decrease to £1,328. The lower level of the fee means more of the income required by the Insolvency Service to administer the cases would be coming from each case and not relying as heavily on cases with significant assets to cross subsidise those with minimal or no assets.
2. In addition, there is a significant project underway which is modelling longer term options to reduce cross subsidy further. There is a need to ensure that any new fee structure provides for a financial regime that meets the needs of its users and takes account of the principles in Managing Public Money.

**Risk and assumptions**

**Risks**

1. Creditors and others may be unwilling to pay the increased costs to petition individuals for bankruptcy or to put companies into compulsory liquidation. Evidence from recent fee changes (Annex A) shows that there may be a weak relationship between fee changes and case numbers, meaning cases may drop by more than forecasted due to the increase in petitioning costs. But we do not believe this effect will be large due to pre-existing trends having the bigger impact on case numbers.
2. If cases continue to have few assets, raising the case administration fee could increase the level of bad debt write off and ostensibly this would not reduce the deficit. Current information is that fee recovery is increasing so this is a small risk.
3. If there is a repeat occurrence of a significant difference between forecasted case load and actual cases then fees and deposits may not yield enough income to eliminate the official receiver deficit.

**Assumptions**

1. This Impact Assessment assumes that the deposits and fees are increased from 16 November 2015 and there are no increases in subsequent years. The Insolvency Service reviews its fees every year and this increase does not mean there will be no change for 2016/17 or subsequent years but any such subsequent increases have not been assumed to occur.
2. The forecast model shows cases declining and it is assumed that cases will decline to a level of 14,000 cases per annum in 2016/17 and stabilise at this level. This is only an estimate and the numbers could rise or fall. There is a fixed cost element to the activity of the Insolvency Service, so if there are a significantly fewer cases there may have to be a proportionally higher increase in fees, spread across the fewer number of cases. The actual number of cases will be monitored as part of the annual review of fees.

**Direct costs and benefits to business calculations (following OITO methodology);**

1. The changes to fees and deposits are not the result of any change in regulatory scope and are the result of lower case numbers leading to higher fixed cost per case. The changes to the SOS are required to reduce the cross subsidisation of cases and ensure compliance with Managing Public Money principles. The changes will result in a net benefit to creditors as the cost of increased deposits will be less than the assets returned to creditors via reduction in the SOS banding. In accordance with the Better Regulation Framework, these measures are not within scope of one-in, two-out as they relate to changes in fees and charges that are not related to any change in regulatory scope.

**Small and Micro Business Assessment**

1. The Better Regulation Framework requires consideration of an exemption to all new regulations for small and micro business because of the often disproportionate impact on these types of business of new regulation. This assessment will describe the impact on small and micro business creditors and insolvency practitioners from this change in fees and deposits.

**Business Creditors**

1. The impact assessment described how creditors will be better off following these changes with the reduced SOS fee returning more assets to creditors than they will have to pay out in higher petition deposits. Exempting small and micro business from these changes would prevent this benefit being realised and would undermine a fundamental principle of insolvency legislation of treating all creditors within a given class equally.
2. The overall costs of higher petition deposits were estimated to be around £0.51m. The IA showed that just over half of this cost will be incurred by large public bodies such as HMRC and Local Government. Large businesses, banks and debt recovery agencies will incur a significant amount of the remaining costs to creditors from these changes meaning small and micro business creditors are only likely to incur a small share of the additional costs.
3. The changes to the SOS fee will mean a reduction in the amount paid and all other things equal higher amounts of assets available to be paid to creditors. The distribution of funds to creditors follows a prioritisation set out in statute. The groups include secured creditors (often banks), preferential creditors such as former employees, floating charge holders (again usually banks) and unsecured creditors including HMRC and other businesses. The benefits from the lower SOS fees are likely to be greater for creditors that are higher up the prioritisation scale. Secured creditors and floating charge holders are often large businesses as are HMRC and Local Government. Small and micro business creditors are therefore likely to receive a small share of the benefits of the lower SOS fee.
4. Therefore we can tentatively conclude that small and micro business creditors are likely to incur a share of the cost and benefits that are proportionate to their size.

**Insolvency Practitioners**

1. R3, the Association of Business Recovery Professionals which represents 97% of IPs, estimate that 46% of its members can be classified as micro and small businesses. The fee changes are unlikely to affect insolvency case numbers, therefore no significant impacts are expected on insolvency practitioners in small and micro businesses.
2. In addition, insolvency practitioners have a choice about which insolvency cases they take on and tend to administer those cases where there are sufficient assets to meet costs. Any familiarisation and implementation costs for insolvency practitioners would be negligible and would be absorbed through existing guidance arrangements, training programmes and continuing professional development.
3. The measures are not expected to have any other impacts on equality, competition or the justice system other than those described above.

.

**Annex A**

**Impact of fee changes on Bankruptcy and Company Compulsory Winding Up Orders**

**Table 9: Bankruptcy and Company Compulsory Winding Up Orders, 2008 to latest**

|  |  |  |  |
| --- | --- | --- | --- |
| **Year** | **Debtor Petitioned Bankruptcy** | **Creditor Petitioned Bankruptcy** | **Company Compulsory Winding Up Orders** |
| 2008 | 56,600 | 10,828 | 5,494 |
| 2009 | 63,804 | 10,866 | 5,643 |
| 2010 | 50,631 | 8,542 | 4,792 |
| 2011 | **34,073** | **7,803** | **5,003** |
| 2012 | 25,192 | 6,595 | 4,261 |
| 2013 | 19,194 | 5,377 | 3,632 |
| 2014 | 15,551 | **4,771** | **3,741** |
| 2015 Q1 | 3,143 | 1,062 | 904 |
| 2015 Q2 | 2,907 (provisional) | 1,034 (provisional) | 765 (provisional) |

Previous deposit increases occurred in June 2011 and April 2014 and are highlighted in table 9. It is difficult to definitively say that deposit increases will not impact on case numbers but there does not appear to be strong effect as pre-existing downwards trends appear to account for much of the changes in case numbers and in the case of compulsory liquidations caseload increased following the fee increase. Therefore we tentatively conclude that the increases in November 2015 deposit changes will not have a significant negative effect on case numbers.

1. Based on 2010/11 asset realisations [↑](#footnote-ref-2)
2. HM Treasury, Managing Public Money, amended July 2013, originally published 2007, paragraph 6.3.6. [↑](#footnote-ref-3)
3. Debtors petition cases are due to become an administrative rather than a court based procedure in April 2016 [↑](#footnote-ref-4)
4. An individual who wishes to petition the court for their own bankruptcy (‘debtor petition bankruptcy’) must pay a deposit of £525 and this will remain unchanged. [↑](#footnote-ref-5)
5. If the creditor (or jointly with other creditors) is owed more than £5000 they can pay a deposit to initiate bankruptcy. [↑](#footnote-ref-6)
6. The forecasted GDP deflator has been used for price change for the FY 2014/15. [↑](#footnote-ref-7)
7. The forecasted GDP deflator has been used for price change for the FY 2014/15. [↑](#footnote-ref-8)
8. Up to a maximum fee of £80,000 [↑](#footnote-ref-9)
9. Insolvency Service statisticians analysis of Insolvency data [↑](#footnote-ref-10)