

# **A study of the bankruptcy enforcement regime before and after the Enterprise Act 2002**

A report produced by The Insolvency Service.  
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# Section 1: Executive Summary

## 1.1 Introduction

This report looks at the results of surveys and case analysis carried out by The Insolvency Service. The aim of this work was to obtain information regarding the bankruptcy enforcement regime before and after the implementation of the Enterprise Act 2002.

On 1 April 2004, provisions of the Enterprise Act 2002 came into force that changed the bankruptcy enforcement regime. The main changes were:

### The introduction of Bankruptcy Restrictions Orders (BROs)

The Enterprise Act 2002 introduced provisions whereby the court can make a BRO, which is designed to provide better protection for the public and a civil alternative to prosecution, with a correspondingly lower level of proof. In short, a prosecution is designed to penalise whereas a BRO is designed to protect.

A BRO places restrictions on the most culpable bankrupts for between 2 and 15 years. Additionally, a bankrupt can offer a Bankruptcy Restrictions Undertaking (BRU) to the Secretary of State, who will consider the BRO matters in deciding whether to accept the undertaking. A BRU has the same effect as a BRO.

Where a BRO/BRU is in force, it is a criminal offence for the (former) bankrupt to:

- (a) act as a receiver or manager of the property of a company or on behalf of debentureholders;
- (b) act as an IP;
- (c) act as a director of a company, or directly or indirectly to take part in or be concerned in the promotion, formation or management of a company without the leave of court;
- (d) obtain credit of more than the prescribed limit; and
- (e) carry on business under a name other than that in which he was adjudged bankrupt without disclosing the name under which he was adjudged bankrupt.

### The abolition of offences under sections 361 and 362 of the Insolvency Act 1986 - 'failure to keep proper accounting records' and 'gambling and rash and hazardous speculation'

Instead, conduct of this nature will be addressed under the BRO regime.

In this report, the term 'BRO(s)' is used to cover Bankruptcy Restriction Orders and Bankruptcy Restriction Undertakings.

## **1.1 Introduction (continued)**

The Insolvency Service is undertaking a retrospective (ex-post) evaluation, i.e. after the adoption of the Enterprise Act 2002, to know better what happened after the implementation of the Act and to apprehend the real effects of the legislative action. The evaluation attempts to comprehensively assess whether, to what extent and how the provisions of the Enterprise Act 2002 met its policy objectives.

The Insolvency Service carried out an analysis of prosecutions in bankruptcy cases prior to 1 April 2004 (pre-Enterprise Act 2002), together with a survey of creditors. A similar exercise was undertaken as regards BROs obtained after 1 April 2004 (post-Enterprise Act 2002). This work was undertaken as part of the evaluation of the enforcement provisions contained in the Enterprise Act 2002, to assess whether the BRO regime provides more effective protection of the public and the commercial community.

## 1.2 Key Findings

### Overall bankruptcy enforcement action

- The overall level of enforcement action in bankruptcy cases has risen since the implementation of the Enterprise Act 2002.
- The level of BROs obtained has steadily risen since the BRO regime was introduced by the implementation of the Enterprise Act 2002.
- The level of BROs is lower than the level of disqualification action taken in corporate insolvencies.
- The average length of a BRO is around 5 years, which is broadly consistent with the average length of a disqualification order.
- To date, there have been no known breaches of BROs and it is anticipated that breaches will occur in less than 1% of BRO cases.
- Albeit that prosecution action is not designed to provide protection, just under 40% of creditors in bankruptcy cases where a criminal conviction was obtained thought that the criminal conviction provided protection to the business community, with 17% being unsure. Similarly, around 35% of creditors in bankruptcy cases where a criminal conviction was obtained thought that the criminal conviction provided protection to the general public, with 17% being unsure.
- Over 70% of creditors in bankruptcy cases where a criminal conviction was obtained stated that they would feel protected if the bankrupt's discharge had been suspended, or restrictions were imposed on the bankrupt. The most popular restrictions suggested by the creditors were restrictions on obtaining credit and running businesses.
- Just under half of the creditors in bankruptcy cases where a BRO was obtained thought that the BRO provided protection to the business community, with just under a quarter being unsure.
- Just over a third of creditors in bankruptcy cases where a BRO was obtained thought that the BRO provided protection to the general public, with just under a third being unsure.
- Less than a third of the general public agreed that the insolvency regime protected the public from dishonest or reckless bankrupts, with around a half being undecided. However, it appears that there is currently a lack of public awareness of the BRO regime.

## 1.2 Key Findings (continued)

### Overall bankruptcy enforcement action (continued)

- As regards The Insolvency Service's stakeholder organisations, around two-fifths of organisations deemed the sanctions that the Insolvency Service currently implements to deter and protect against financial wrongdoing as effective, and this has changed little since 2004.

### Bankruptcy enforcement action taken where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation

- Prior to the Enterprise Act 2002, a possible failure to keep proper accounting records or gambling and rash and hazardous speculation was identified in around 0.5% of bankruptcy cases. Since the implementation of the Enterprise Act 2002, the Secretary of State has given authority to proceed with a BRO application in a similar level of cases, where conduct comparable to possible offences under sections 361 or 362 of the Insolvency Act 1986 forms the basis for the BRO application.
- Prior to the Enterprise Act 2002:
  - No action was taken, because of insufficient evidence to support prosecution action, in just under 25% of cases where a possible failure to keep proper accounting records or gambling and rash and hazardous speculation was identified.
  - As regards the remaining cases, overall, convictions were obtained in around 35% of cases and a warning letter was issued in around 40% of cases (with a handful of cases still on-going).
  - The most common sentence imposed following a conviction of an offence under section 361 or 362 of the Insolvency Act 1986 was Community Service.
- In contrast, since the Enterprise Act 2002, because of the lower burden of proof, a BRO has been obtained in nearly all the cases where the Secretary of State gave authority to proceed with a BRO application, where conduct comparable to possible offences under sections 361 or 362 of the Insolvency Act 1986 formed the basis for the BRO application.
- The average length of a BRO obtained where the main misconduct was a failure to keep proper accounting records or gambling/rash and hazardous speculation (including unreasonable extravagance) is 5 years.

## 1.2 Key Findings (continued)

### **Bankruptcy enforcement action taken where there was evidence of a failure to keep proper accounting records or gambling and rash and hazardous speculation (continued)**

- Albeit that prosecution action is not designed to provide protection, around 12% of creditors in bankruptcy cases where a criminal conviction was obtained under sections 361 or 362 of the Insolvency Act 1986 thought that the criminal conviction provided protection to the business community, with 27% being unsure. Similarly, around 9% of creditors in bankruptcy cases where a criminal conviction was obtained thought that the criminal conviction provided protection to the general public, with 27% being unsure.
- Around 43% of creditors in bankruptcy cases where a BRO was obtained (where the main misconduct was a failure to keep proper accounting records or gambling/rash and hazardous speculation) thought that the BRO provided protection to the business community, with 24% being unsure. Similarly, around 32% of creditors in bankruptcy cases where a BRO was obtained (where the main misconduct was a failure to keep proper accounting records or gambling/rash and hazardous speculation) thought that the BRO provided protection to the general public, with 34% being unsure.

### 1.3 Methodology

The Insolvency Service analysed the prosecution action taken in bankruptcy cases in the two years prior to the implementation of the Enterprise Act 2002, i.e. 2002/3<sup>1</sup> and 2003/4.

Further, the creditors of bankrupts against whom prosecution action had been taken were asked to complete a questionnaire to ascertain whether creditors felt that the sentences imposed in respect of offences offered protection to the business community and the general public. The survey was undertaken in two stages:

- In 2004, The Insolvency Service undertook a postal survey of creditors in cases where prosecution action has been taken in respect of offences under sections 361 and 362 of the Insolvency Act 1986. The sample of creditors was drawn from cases where a conviction was obtained in the period 1 April 2000 to 31 March 2004. The cases were stratified by type of offence and age, and purposively sampled to choose a representative sample. Questionnaires were sent to all creditors in each sampled case.
- In 2005, The Insolvency Service undertook a postal survey of creditors in cases where prosecution action in respect of insolvency-related offences was undertaken. The sample of creditors was drawn from cases where a conviction was obtained in respect of an insolvency-related offence in the year ended 31 March 2004. The cases were stratified by type of offence and purposively sampled to choose a representative sample. Questionnaires were sent to all creditors in each sampled case.

The Insolvency Service has also analysed the BRO action taken in bankruptcy cases since the implementation of the Enterprise Act 2002, i.e. from 1 April 2004 onwards. Additionally, in 2006 and 2007, The Insolvency Service undertook a postal survey of creditors in cases where a BRO was obtained. The purpose of this survey was to ascertain whether creditors felt that the restrictions imposed under the BRO offer protection to the business community and the general public. The sample of creditors was drawn from cases where a BRO was obtained in 2004/5 and 2005/6. The cases were stratified by type of misconduct and age, and purposively sampled to choose a representative sample. Questionnaires were sent to all creditors in each sampled case.

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<sup>1</sup> 2002/3 refers to the year ended 31 March 2003, 2003/4 refers to the year ended 31 March 2004, etc.

### 1.3 Methodology (continued)

As regards the surveys of creditors, details of the response rates are shown in Table 1. Some respondents did not answer all the questions in the questionnaire. All percentages in this report have been calculated on the basis of the total responses received to a question.

Copies of the questionnaires can be found at Appendices 1 and 2.

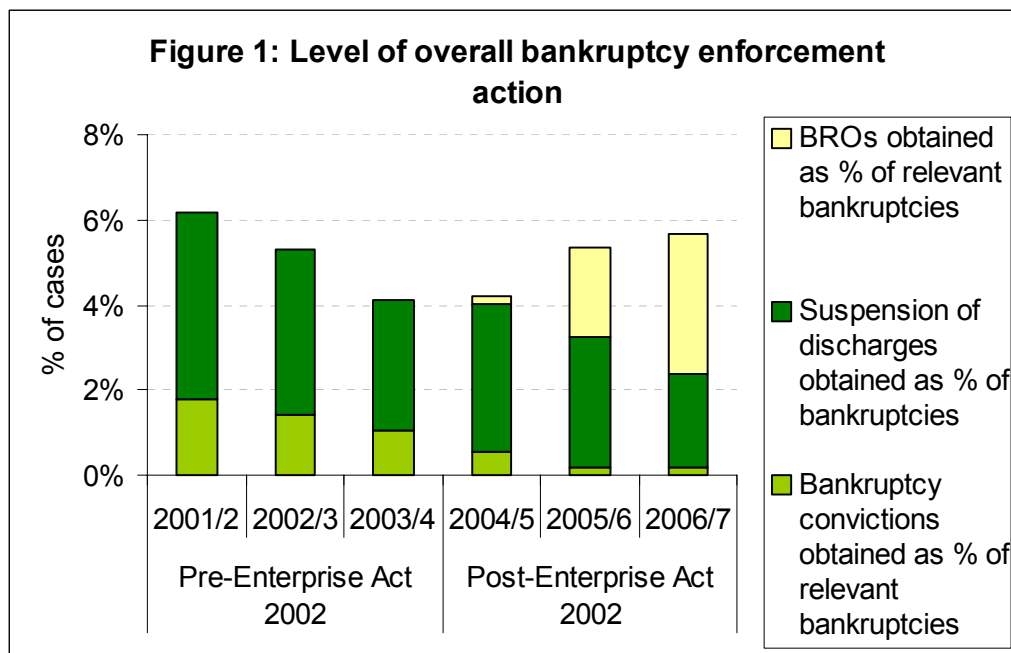
**Table 1: Response rates to surveys**

	<b>Sample size</b>	<b>Response rate (count)</b>	<b>Response rate (%)</b>
Creditors of bankrupts where prosecution action has been taken in respect of offences under sections 361 and 362 of the Insolvency Act 1986 in the 4 years ended 31 March 2004 (pre-Enterprise Act 2002)	244	41	<b>16.8</b>
Creditors of bankrupts where prosecution action had been taken in respect of bankruptcy offences in 2003/4 (pre-Enterprise Act 2002)	531	102	<b>19.2</b>
Creditors of bankrupts where a BRO had been obtained in 2004/5 and 2005/6 where the most serious misconduct was a failure to keep proper accounting records or gambling/rash and hazardous speculation (post-Enterprise Act)	497	90	<b>18.1</b>
Creditors of bankrupts where a BRO had been obtained in 2004/5 and 2005/6 (post-Enterprise Act 2002)	2,713	362	<b>13.3</b>

## Section 2: Results – overall bankruptcy enforcement action

### 2.1 Level of enforcement action

- Prior to the introduction of the BRO regime, the only enforcement action available in bankruptcy was prosecution and the power to suspend the discharge of a bankrupt who fails to co-operate with the Official Receiver or trustee.
- Where evidence of criminal misconduct comes to light, the Official Receiver submits a statement of facts to The Insolvency Service's Criminal Allegations Team who decide whether the case should be referred for criminal investigation. In some cases, no further action is taken where there is insufficient evidence of criminality.
- The overall level of enforcement action in bankruptcy cases has risen since the implementation of the Enterprise Act 2002<sup>2</sup> (see Figure 1).



<sup>2</sup> The level of convictions has been calculated as a percentage of the total number of bankruptcies lagged by 3 years. This is to reflect the time taken to secure a conviction. This time period is an estimate based on a case sampling exercise. The level of BROs has been calculated as a percentage of the total number of bankruptcy orders lagged by 9 months. This is to reflect the time taken to obtain a BRO/U from the date of the bankruptcy order. According to internal data held by The Insolvency Service, the average time taken to obtain a BRO/U in 2004/5, 2005/6 and 2006/7 is 6.9 months, 8.9 and 10.4 months respectively. Further, BRO/U action can only be taken in respect of conduct after 1 April 2004. Accordingly, the 2004/5 relevant bankruptcies represent the level of bankruptcies in the 3 months to 30 June 2004, and the relevant bankruptcies for 2005/6 are the level of bankruptcies in the year ended 30 June 2005.

## 2.1 Level of prosecutions and BROs (continued)

- The level of BROs obtained has steadily risen since the BRO regime was introduced by the implementation of the Enterprise Act 2002 (see Figure 1 and Table 2).

	<b>2004/5</b>	<b>2005/6</b>	<b>2006/7</b>
<b>Number of BROs</b>	<b>22</b>	<b>843</b>	<b>1,867</b>
Number of relevant bankruptcies <sup>3</sup>	9,060	40,840	56,537
<b>BROs as % of relevant bankruptcies</b>	<b>0.20%</b>	<b>2.06%</b>	<b>3.30%</b>

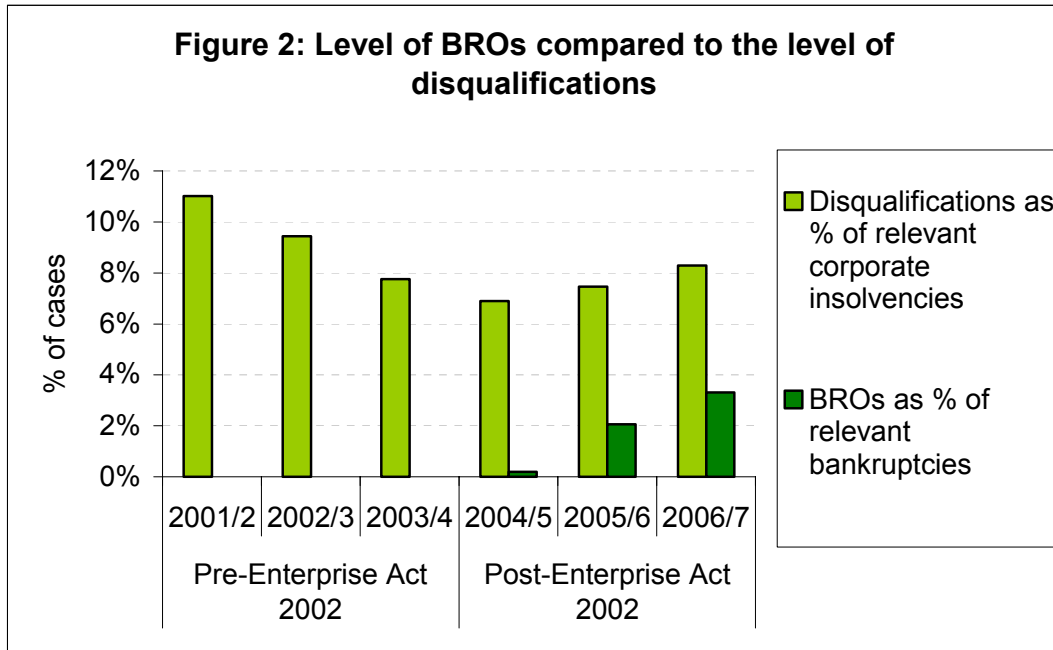
- In the Regulatory Impact Assessment for the Enterprise Act 2002, it was anticipated that BROs would be obtained in 7 – 12% of bankruptcy cases. This was based on the level of disqualification action at that time in corporate cases<sup>4</sup>. However, it was anticipated that BRO figures for the initial years would be lower than in future years as BRO action can only be taken in respect of conduct after 1 April 2004.
- Comparing the level of BROs and disqualification action<sup>5</sup>, it can be seen that the level of BROs is lower than the level of disqualification action (see Figure 2).

<sup>3</sup> Based on statistics published by The Insolvency Service (previously the DTI Statistics Directorate) (not seasonally adjusted). The number of bankruptcies has been lagged by 9 months. This is to reflect the time taken to obtain a BRO/U from the date of the bankruptcy order. According to internal data held by The Insolvency Service, the average time taken to obtain a BRO/U in 2004/5, 2005/6 and 2006/7 is 6.9 months, 8.9 and 10.4 months respectively. Further, BRO/U action can only be taken in respect of conduct after 1 April 2004. Accordingly, the 2004/5 relevant bankruptcies represent the level of bankruptcies in the 3 months to 30 June 2004, and the relevant bankruptcies for 2005/6 are the level of bankruptcies in the year ended 30 June 2005.

<sup>4</sup> This is based on the assumption that as the BRO provisions are broadly analogous to the provisions of the Company Directors Disqualification Act 1986, it is reasonable to expect that in percentage terms, the level of civil misconduct in bankruptcy cases would be similar to that seen in corporate cases. Therefore, it may be expected that a similar level of BROs will be achieved as disqualification orders.

<sup>5</sup> The level of disqualifications has been calculated as a percentage of the total number of corporate insolvencies lagged by 2 years, based on statistics published by The Insolvency Service (previously the DTI Statistics Directorate) (not seasonally adjusted). They include all insolvencies in which disqualification action can be taken, i.e. compulsory liquidations, creditors' voluntary liquidations, administrations and receiverships. The receivership figures include administrative receiverships and other receiverships, such as receivers appointed under the Law of Property Act 1925, which are not 'relevant'. However, the number of 'non-relevant' receiverships is not material and thus will have negligible impact. The number of disqualifications obtained has been lagged by two financial years to reflect the time taken to obtain a disqualification order from the date of the insolvency proceedings. According to statistics maintained by The Insolvency Service, the average time taken to obtain a disqualification order in 2001/2, 2002/3, 2003/4, 2004/5, 2005/6 and 2006/7 was 28, 24, 22, 25, 27 and 27 months respectively.

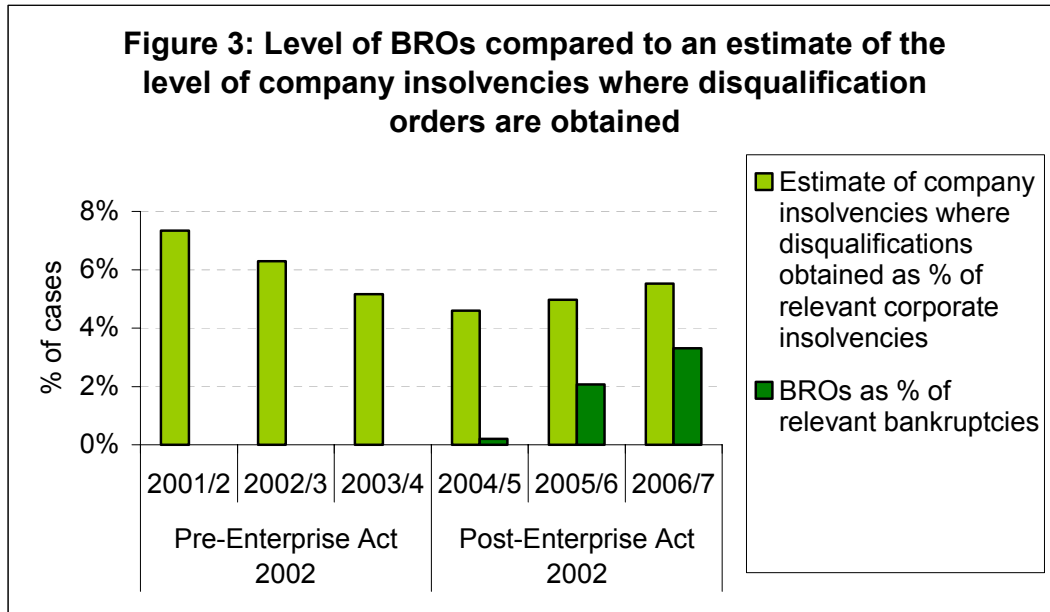
## 2.1 Level of prosecutions and BROs (continued)



- Further, disqualification orders can be obtained against more than one director in a company case. It is estimated that, on average, the ratio of company cases where disqualification action is taken to the number of disqualification orders/undertakings is 2:3<sup>6</sup>. The level of BROs is still lower compared to an estimate of the level of company insolvencies where disqualification orders are obtained, but the difference on a case-basis is less than the difference on an order-basis (see Figures 2 and 3).

<sup>6</sup> A sample of disqualification cases in 2006/7 shows that 591 disqualification orders/undertakings were obtained in connection with misconduct in 403 corporate insolvencies.

## 2.1 Level of prosecutions and BROs (continued)



- An interim BRO can be applied for in the period between the application for a BRO and the hearing date. The court can grant an interim BRO if there are prima facie grounds to suggest that a BRO will be granted and it is in the public interest to make an interim order. An interim BRO comes into force the day it is made and has the same effect as a BRO.
- No interim BROs were obtained in the first year of the BRO regime, but 119 have been obtained thereafter (see Table 3).

**Table 3: Level of interim BROs**

	2004/5	2005/6	2006/7
<b>Number of interim BROs</b>	<b>0</b>	<b>47</b>	<b>72</b>
Number of BROs	22	843	1867
<b>Interim BROs as % of BROs</b>	<b>0.00%</b>	<b>5.58%</b>	<b>3.86%</b>

## 2.1 Level of prosecutions and BROs (continued)

- An application for a BRO must usually be made within 12 months of the bankruptcy order<sup>7</sup>. Until February 2006, the guidance to Official Receivers was that where there was a gap between the first anniversary of the bankruptcy order and the hearing of the BRO application, an application should be made for an interim BRO. The Insolvency Service sought Counsel's opinion on this matter. As a result, new guidance was issued to Official Receivers in February 2006, advising that an application for an interim BRO is not always necessary and the decision to make such an application should be made on a case-by-case basis, taking into account the nature of the allegations, the length of the gap between the anniversary and the substantive BRO hearing, and the 'damage' to the bankrupt<sup>8</sup>. This may explain why the level of interim BROs has fallen in 2006/7 compared to the previous year.
- As regards the 119 interim BROs obtained in the 3 years ended 31 March 2007, substantive BROs have been made in all except 7 cases. The BRO application was withdrawn in 5 cases due to new evidence arising after the interim BRO was obtained which meant that it was not in the public interest to proceed with the BRO application. The BRO proceedings are on-going in the remaining 2 cases.

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<sup>7</sup> Schedule 4A of the Insolvency Act 1986

<sup>8</sup> There are Human Rights considerations, as the bankrupt has not received a fair trial when the court grants an interim BRO and there is no mechanism for compensation as there is with other kinds of injunctions.

## 2.2 Results of prosecutions and BROs

- Both before and after the Enterprise Act 2002, the most common sentence imposed following conviction of a bankruptcy-related offence is community service (see Table 4). It should be noted that compensation or confiscation orders may also have been made, but these are not included as they are not recorded on The Insolvency Service's internal database.

**Table 4: Breakdown of sentences imposed following conviction of a bankruptcy-related offence (excluding compensation/confiscation orders)<sup>9</sup>**

Sentence imposed	Pre-Enterprise Act 2002 <sup>10</sup>	Post-Enterprise Act 2002 <sup>11</sup>
Community service	37%	45%
Prison sentence	24%	18%
Conditional discharge	15%	18%
Fine	15%	8%
Other	9%	12%

- The average length of a BRO is around 5 years, which is broadly consistent with the average length of a disqualification order (see Table 5).

**Table 5: Length of disqualification orders and BROs**

		years					
		Pre-Enterprise Act 2002			Post-Enterprise Act 2002		
		2001/2	2002/3	2003/4	2004/5	2005/6	2006/7
Length of Disqualifications	<b>Median</b>	5	5	5	5	5	5
	<b>Average</b>	5.4	5.4	5.2	5.5	5.2	5.5
Length of BROs	<b>Median</b>				5	5	4
	<b>Average</b>				5.5	5.3	4.8

<sup>9</sup> Where a bankrupt was convicted of more than one offence, only the sentence imposed for the most serious offence has been included.

<sup>10</sup> Analysis of convictions imposed in the year ended 31 March 2002

<sup>11</sup> Analysis of convictions imposed in the three years ended 31 March 2007.

## 2.2 Results of prosecutions and BROs (continued)

- To date, there have been no known breaches of BROs.
- Based on breaches of disqualification orders<sup>12</sup> and offences under the Insolvency Act 1986 that are comparable to a breach of a BRO<sup>13</sup> prior to the Enterprise Act 2002, it is expected that breaches will occur in less than 1% of BROs (see Tables 6 and 7).

**Table 6: Breaches of disqualification orders (measured by the level of prosecutions under Section 13 of the Company Directors' Disqualification Act 1986 – Contravention of a Disqualification Order)**

	2001-2002	2002-2003	2003-2004
<b>Number of prosecutions under Section 13 of the Company Directors' Disqualification Act 1986<sup>14</sup></b>	<b>8</b>	<b>12</b>	<b>9</b>
<b>Total number of disqualification orders</b>	1,761	1,594	1,367
<b>Section 13 prosecutions as % of disqualifications<sup>15</sup></b>	<b>0.45%</b>	<b>0.75%</b>	<b>0.66%</b>

<sup>12</sup> Section 13 of the Company Directors' Disqualification Act 1986 sets out the criminal penalties for acting in the contravention of a disqualification order. The frequency of convictions under this offence is an indication of the level of breaches of a disqualification order.

<sup>13</sup> A BRO makes it a criminal offence for a bankrupt to:

- (a) Act as a receiver or manager of the property of a company or on behalf of debentureholders (s31 IA86);
- (b) Obtain credit of more than the prescribed limit (s360 IA86);
- (c) Carry on business under a name other than that in which he was adjudged bankrupt without disclosing the name under which he was adjudged bankrupt (s360 IA86);
- (d) Act as an IP (s390 IA86); or
- (e) Act as a director of a company, or directly or indirectly to take part in or be concerned in the promotion, formation or management of a company without the leave of court (s11 CDDA86).

<sup>14</sup> Information extracted from The Insolvency Service's internal database.

<sup>15</sup> The level of s13 prosecutions has been compared directly to the number of disqualifications obtained in the same period. However, it is likely that there is a time lag, i.e. the s13 offences relate to disqualification orders obtained in previous periods. However, as the level of s13 offences is negligible, this should have minimal impact.

## 2.2 Results of prosecutions and BROs (continued)

<b>Offence</b>	<b>Number of prosecutions<sup>16</sup></b>		
	<b>2001-2002</b>	<b>2002-2003</b>	<b>2003-2004</b>
<b>Section 11 of the Company Directors' Disqualification Act 1986</b>	35	22	19
<b>Section 360 of the Insolvency Act 1986</b>	48	44	30
<b>Section 390 of the Insolvency Act 1986</b>	Nil	Nil	Nil
<b>Section 31 of the Insolvency Act 1986</b>	Nil	Nil	Nil
<b>Total</b>	<b>83</b>	<b>66</b>	<b>49</b>
<b>Total no. of relevant bankruptcy orders<sup>17</sup></b>	20,508	21,479	21,961
<b>Offences as % of relevant bankruptcy orders</b>	<b>0.40%</b>	<b>0.31%</b>	<b>0.22%</b>

<sup>16</sup> Information extracted from The Insolvency Service's internal database.

<sup>17</sup> The number of bankruptcies has been lagged by 3 years to reflect the time taken to secure a conviction. This is to reflect the time taken to secure a conviction. This time period is an estimate based on a case sampling exercise.

<sup>18</sup> A BRO makes it a criminal offence for a bankrupt to:

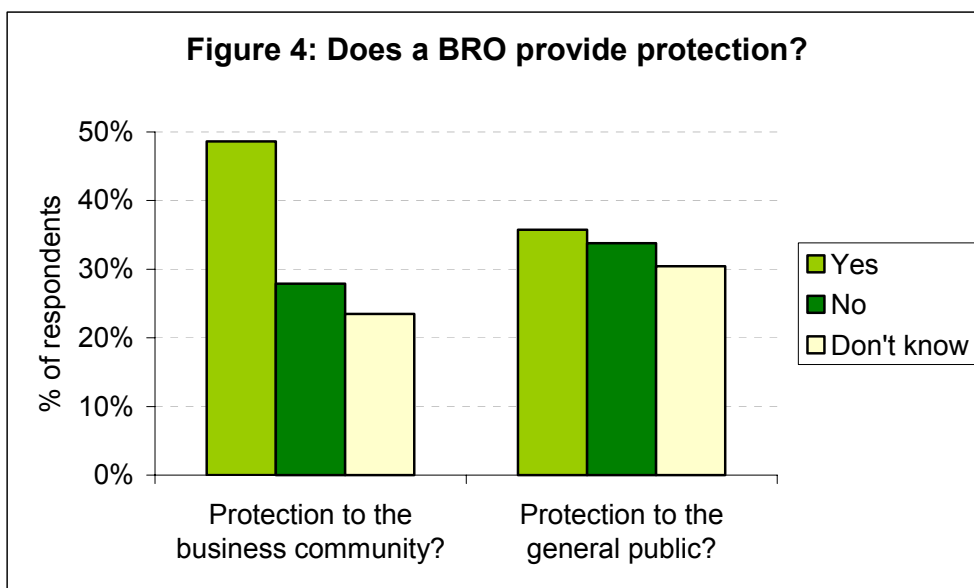
- (a) Act as a receiver or manager of the property of a company or on behalf of debentureholders (s31 IA86);
- (b) Obtain credit of more than the prescribed limit (s360 IA86);
- (c) Carry on business under a name other than that in which he was adjudged bankrupt without disclosing the name under which he was adjudged bankrupt (s360 IA86);
- (d) Act as an IP (s390 IA86); or
- (e) Act as a director of a company, or directly or indirectly to take part in or be concerned in the promotion, formation or management of a company without the leave of court (s11 CDDA86).

## 2.3 Creditor satisfaction with BROs

- As stated previously, BROs are designed to provide protection for the public and a civil alternative to prosecution, with a correspondingly lower level of proof. In short, a prosecution is designed to penalise whereas a BRO is designed to protect.
- The Insolvency Service carried out a survey of creditors in bankruptcy cases where a criminal conviction had been obtained against the bankrupt in connection with the bankrupt's conduct prior to or during his/her bankruptcy. The purpose of the survey was to establish whether, albeit that prosecution action is designed to penalise not protect, creditors felt that such prosecution action provided any protection to the business community and more generally, the general public. A survey was then carried out of creditors in bankruptcy cases where a BRO had been obtained to establish whether such creditors felt that the BRO offered any such protection (see Section 1.3 for further details).
- Over 70% of creditors in bankruptcy cases where a criminal conviction was obtained stated that they would feel protected if the bankrupt's discharge had been suspended, or restrictions were imposed on the bankrupt. The most popular restrictions suggested by the creditors were restrictions on obtaining credit and running businesses.
- This suggests that the introduction of the BRO regime should make creditors feel protected, and this conclusion is partially supported by the results of the surveys.
- Albeit that prosecution action is not designed to provide protection, just under 40% of creditors in bankruptcy cases where a criminal conviction was obtained thought that the criminal conviction provided protection to the business community, with 17% being unsure. Similarly, around 35% of creditors in bankruptcy cases where a criminal conviction was obtained thought that the criminal conviction provided protection to the general public, with 17% being unsure.
- Just under half of the creditors in bankruptcy cases where a BRO was obtained thought that the BRO provided protection to the business community, with just under a quarter being unsure (see Figure 4).

## 2.3 Creditor satisfaction with BROs (continued)

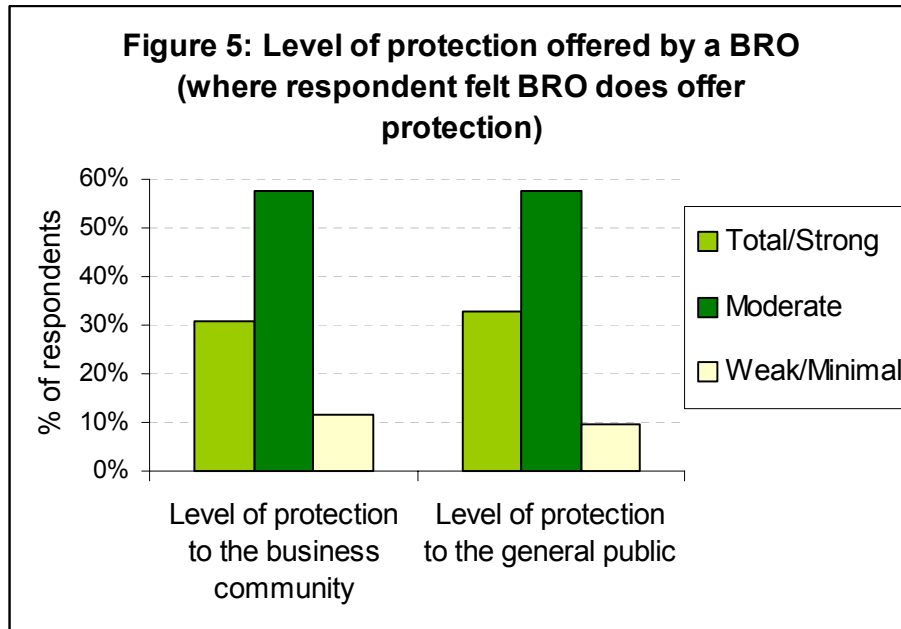
- Creditors in bankruptcy cases where a BRO was obtained who had business dealings with the bankrupt were as likely to believe that a BRO offered protection to the business community, compared to creditors who had no business dealings. However, creditors in bankruptcy cases where a BRO was obtained who had no business dealings were more likely to express no opinion<sup>19</sup>.
- Just over a third of creditors in bankruptcy cases where a BRO was obtained thought that the BRO provided protection to the general public, with just under a third being unsure (see Figure 4)



<sup>19</sup> The surveys showed that 51% of creditors who had business dealings with the bankrupt agreed that the BRO provided protection to the business community, with 14% providing a 'don't know' response. As regards of creditors who had no business dealings with the bankrupt, 50% agreed that the BRO provided protection to the business community, with 23% providing a 'don't know' response.

## 2.3 Creditor satisfaction with BROs (continued)

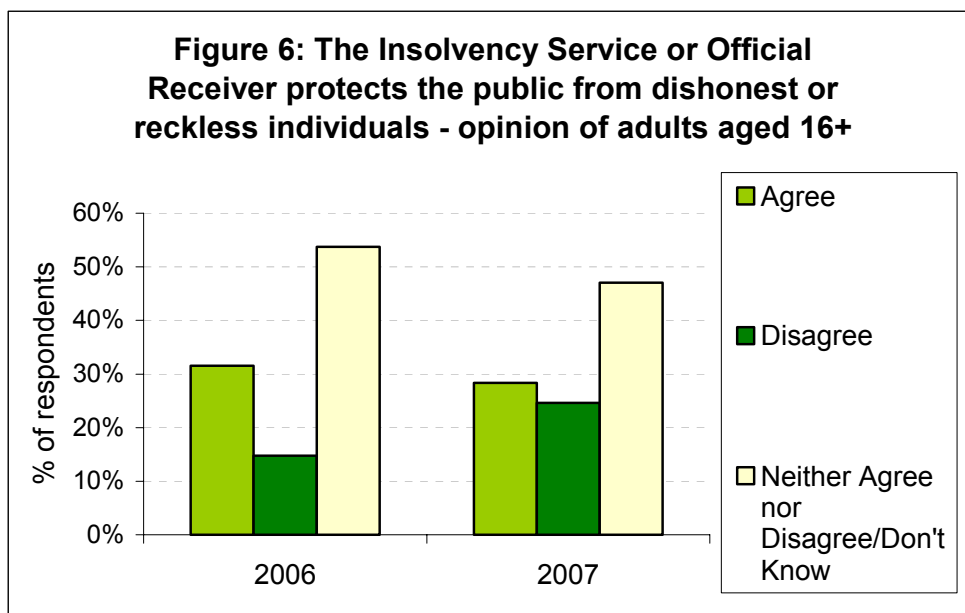
- Creditors who feel that a BRO does provide protection to the business community and general public are most likely to rate the protection as moderate (see Figure 5).



- The Insolvency Service has also carried out other survey/case studies to ascertain whether the introduction of BRO regime has impacted on the perceived level of protection offered by the insolvency enforcement regime.
- A case study of creditors in 2004 (the year in which the Enterprise Act 2002 was implemented) showed that 28% of bankruptcy creditors felt that the insolvency regime protected the public from dishonest or reckless individuals, with 23% being undecided. A case study of creditors in 2005 produced broadly the same results. Therefore, at that stage, it would appear that the introduction of the BRO regime had not yet made creditors feel more protected.

### 2.3 Creditor satisfaction with BROs (continued)

- Surveys of people aged 16 or over carried out in 2006 and 2007 (post-Enterprise Act 2002) showed that less than a third of the respondents agreed that the insolvency regime protected the public from dishonest or reckless bankrupts, with around a half being undecided (see Figure 6). In these surveys, respondents were also asked whether they had heard of BROs - 21% and 17% thought they had heard of them in 2006 and 2007 respectively, but no-one accurately described what they were. Therefore, it appears that there is currently a lack of public awareness of the BRO regime. However, this may change as the number of BROs in force increases.



## 2.3 Creditor satisfaction with BROs (continued)

- The Insolvency Service has carried out surveys<sup>20</sup> in 2004, 2006 and 2007 to ascertain the level of confidence in the enforcement regime amongst The Insolvency Service's stakeholder organisations<sup>21</sup>. Organisations were asked how effective The Insolvency Service sanctions<sup>22</sup> were deemed to be as protection against financial wrongdoing. This opinion covered both corporate and individual provisions. In 2007, around two-fifths of organisations deemed the sanctions that the Insolvency Service currently implements to deter and protect against financial wrongdoing as effective, and this has changed little since 2004. This static trend disguises some difference of opinion between different respondent groups. For example, whilst organisations in insolvency areas have felt that sanctions as a deterrent are becoming less effective, the opposite has been felt in non-insolvency areas. A similar pattern has emerged amongst different types of organisation, with insolvency practitioners and local authorities becoming more positive, and solicitors and accountants less positive. In the 2006 and 2007 surveys, respondents were also asked what The Insolvency Service could do to increase the level of protection from financial wrong-going; the most popular answer was to take action in more cases.
- Both before and after the Enterprise Act 2002, the level of complaints received by The Insolvency Service are minimal. Analysis of The Insolvency Service's complaints register shows that prior to the Enterprise Act, around 0.2% of the complaints received were about investigation matters<sup>23</sup>; post-Enterprise Act 2002, such complaints are around 0.4% of all complaints received<sup>24</sup>. Around half of these complaints were upheld both before and after the Enterprise Act 2002.

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<sup>20</sup> The Insolvency Service commissioned GfK NOP to carry out the surveys.

<sup>21</sup> The stakeholder organisations fall into two broad categories, defined as follows:

- Advisors - these are organisations which advise individuals and senior business personnel regarding their own bad debts or dealing with bankruptcy/insolvency of their clients; and
- Non-advisors - these are organisations that have a responsibility for understanding the process of dealing with bad debts and maybe petitioning for or taking part in the bankruptcy or insolvency of any clients

<sup>22</sup> The Insolvency Service's 'sanctions' include Bankruptcy Restrictions Orders/Undertakings, Disqualification Orders/Undertakings and reporting to a prosecution authority in respect of allegations of criminality.

<sup>23</sup> In the three years ended 31 March 2004, there were 1,164 complaints in The Insolvency Service's complaints register. Two of these complaints related to investigation matters – one from a creditor complaining that he had not been kept informed (upheld) and another from a creditor complaining that no enforcement action had been taken against a bankrupt (not upheld).

<sup>24</sup> In the three years ended 31 March 2007, there were 1,381 complaints in The Insolvency Service's complaints register. Five of these complaints related to investigation matters – four from creditors complaining that no enforcement action had been taken against bankrupts (two complaints upheld) and one from a bankrupt about BRO proceedings being taken against him (not upheld).

## **Section 3: Results – bankruptcy enforcement action taken where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation**

### **3.1 Level of cases where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation**

- Prior to the Enterprise Act 2002, there existed two offences under sections 361 and 362 of the Insolvency Act 1986 - 'failure to keep proper accounting records' and 'gambling and rash and hazardous speculation' respectively. Where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation, the Official Receiver would submit a statement of facts to The Insolvency Service's Criminal Allegations Team who would decide whether the case should be further investigated.
- Prior to the Enterprise Act 2002, a possible failure to keep proper accounting records or gambling and rash and hazardous speculation was identified in around 0.5% of bankruptcy cases (see Table 8).

### 3.1 Level of cases where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation (continued)

**Table 8: Level of cases where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation prior to the Enterprise Act 2002**

Offence	Number of submissions <sup>25</sup>	
	2002-2003	2003-2004
Failure to keep proper accounting records (s361)	23	19
Gambling and rash and hazardous speculation (s362)	98	100
<b>Total</b>	<b>121</b>	<b>119</b>
Number of statement of facts submitted <sup>26</sup>	747	424
<b>S361/2 submissions as % of submissions</b>	<b>16.20%</b>	<b>28.07%</b>
Number of relevant bankruptcies <sup>27</sup>	23,580	25,856
<b>S361/2 submissions as % of relevant bankruptcies</b>	<b>0.51%</b>	<b>0.46%</b>

<sup>25</sup> Information extracted from The Insolvency Service's internal database.

<sup>26</sup> Information extracted from The Insolvency Service's internal database. A Statement of Facts is submitted by an Official Receiver to The Insolvency Service's Criminal Allegations Team where there is evidence of any possible criminal misconduct.

<sup>27</sup> Figures based on statistics published by The Insolvency Service (previously the DTI Statistics Directorate) (not seasonally adjusted). The number of bankruptcies has been lagged by 9 months to reflect the time taken to submit a statement of facts. This time period is based on the results of a case sampling exercise.

### 3.1 Level of cases where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation (continued)

- The Enterprise Act 2002 repealed the offences under sections 361 and 362 of the Insolvency Act 1986. Instead, conduct of this nature is now addressed under the BRO regime.
- Where an Official Receiver believes that a BRO application is appropriate, the matter is referred to The Insolvency Service's Authorisations Team. This team then decides whether an authority to proceed with a BRO application (ATP) should be issued on behalf of the Secretary of State.
- Since the implementation of the Enterprise Act 2002, the level of ATPs where conduct comparable to possible offences under sections 361 or 362 of the Insolvency Act 1986 is the main allegation is now at a similar level as section 361/2 submissions (see Table 9 and Figure 7).

**Table 9: Level of Authorities to Proceed (ATPs) issued where the main misconduct was a failure to keep proper accounting records or gambling/rash and hazardous speculation (including unreasonable extravagance)**

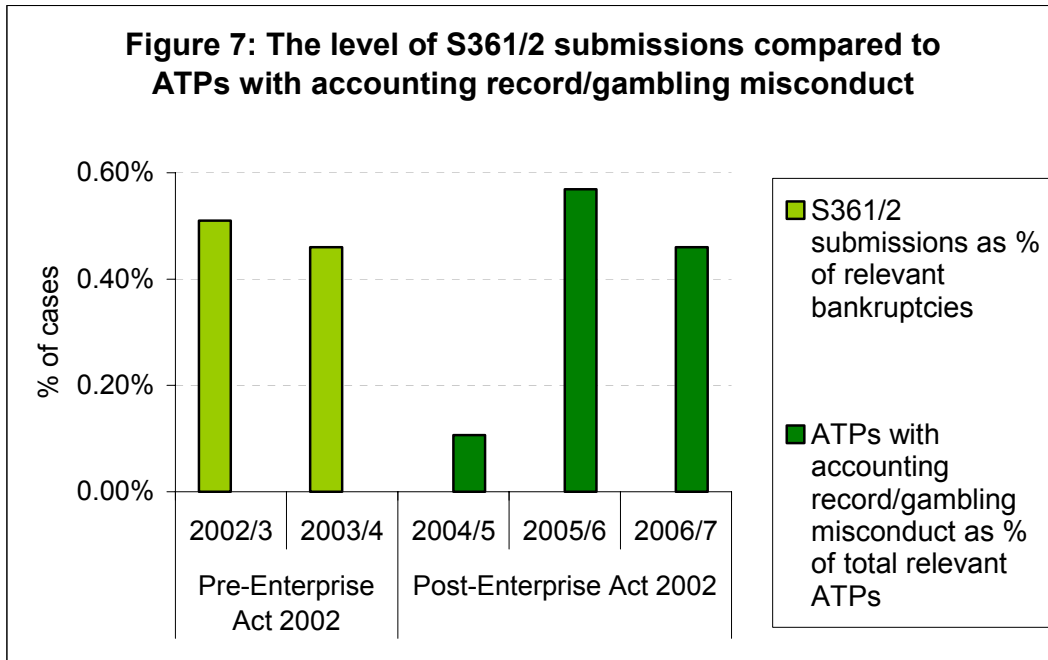
Misconduct <sup>28</sup>	Number of ATPs <sup>29</sup>		
	2004/5	2005/6	2006/7
Failure to keep proper accounting records	1	33	15
Gambling/rash and hazardous speculation (including unreasonable extravagance)	12	204	250
<b>Total</b>	<b>13</b>	<b>237</b>	<b>265</b>
Total number of ATPs issued	59	1,129	1,936
<b>ATPs with accounting record/gambling misconduct as % of all ATPs</b>	<b>22.03%</b>	<b>20.99%</b>	<b>13.69%</b>
Number of relevant bankruptcies <sup>30</sup>	9,060	40,840	56,537
<b>ATPs with accounting record/gambling misconduct as % of total relevant bankruptcies</b>	<b>0.03%</b>	<b>0.50%</b>	<b>0.46%</b>

<sup>28</sup> This is where the main misconduct is either a failure to keep proper accounting records or gambling/rash and hazardous speculation/unreasonable extravagance.

<sup>29</sup> Figures extracted from The Insolvency Service's internal records.

<sup>30</sup> Based on statistics published by The Insolvency Service (previously the DTI Statistics Directorate) (not seasonally adjusted). The number of bankruptcies has been lagged by 8 months. This is to reflect the time taken between an ATP being issued from the date of the bankruptcy order. According to internal data held by The Insolvency Service, the average time taken between the bankruptcy order and an ATP being issued in 2004/5, 2005/6 and 2006/7 is 5.8, 7.9 and 8.6 months respectively. Further, BRO/U action can only be taken in respect of conduct after 1 April 2004. Accordingly, the 2004/5 relevant bankruptcies represent the level of bankruptcies in the 4 months to 31 July 2004, and the relevant bankruptcies for 2005/6 are the level of bankruptcies in the year ended 30 July 2005.

### 3.1 Level of cases where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation (continued)



- The low level of ATPs seen in 2004/5 is because BRO action can only be taken in respect of conduct after 1 April 2004 (see Figure 7).

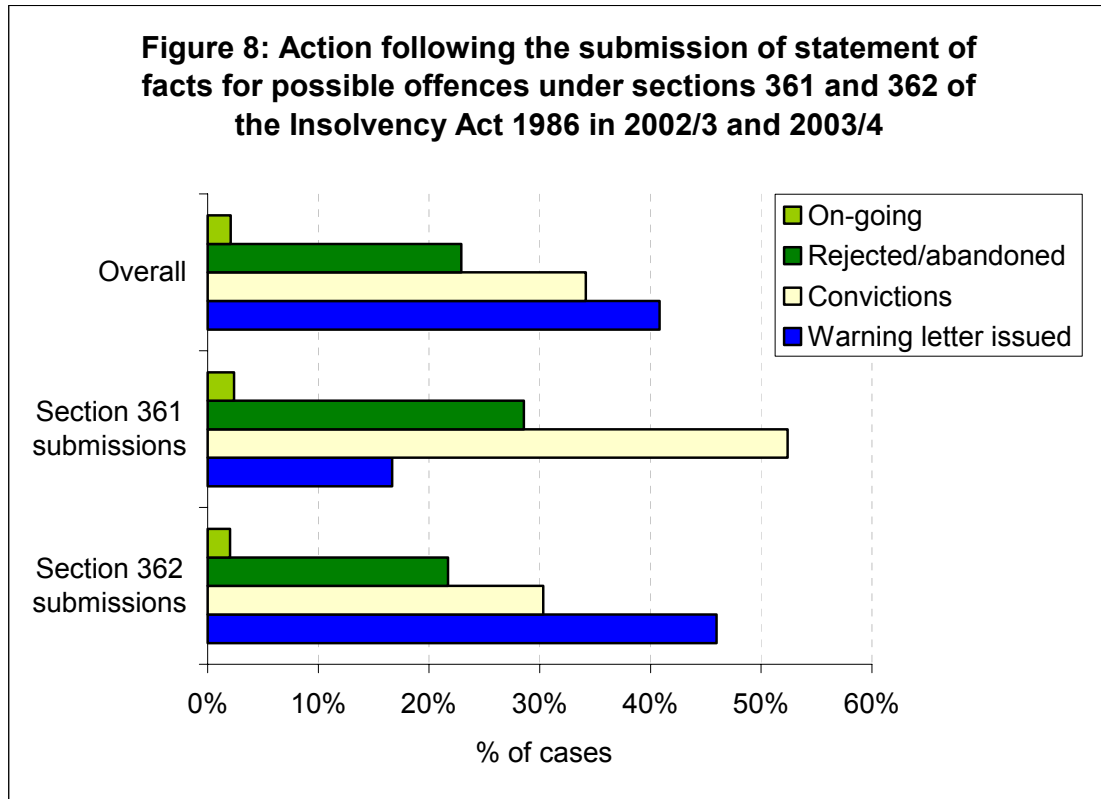
### **3.2 Action taken in cases where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation**

- As detailed in Section 3.1, evidence of a possible failure to keep proper accounting records (which would constitute a possible offence under section 361 of the Insolvency Act 1986) or gambling and rash and hazardous speculation (which would constitute a possible offence under section 362 of the Insolvency Act 1986) was identified in around 0.5% of bankruptcy cases. In such cases, the Official Receiver would submit a statement of facts to The Insolvency Service's Criminal Allegations Team who would decide whether the case should be referred for criminal investigation. A submission of a statement of facts could ultimately lead to conviction, a warning letter being issued to the bankrupt<sup>31</sup> or no further action. Action would not be taken if there were insufficient evidence to support prosecution action.
- Analysis of submissions regarding a possible offence under sections 361 and 362 of the Insolvency Act 1986 in 2002/3 and 2003/4 shows that, overall, no action was taken in just under 25% of these cases due to insufficient evidence to support prosecution action (see Figure 8).
- As regards the remaining submissions, overall, convictions were obtained in around 35% of cases and a warning letter issued in around 40% of cases (with a handful of cases still on-going) (see Figure 8).

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<sup>31</sup> A warning letter is a letter from the Secretary of State to acknowledge that a criminal offence may have been committed but due to the public interest criteria (e.g. ill health or potential unreliability of witnesses), the facts will not be prosecuted or subject to criminal investigation.

### 3.2 Action taken in cases where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation (continued)



- Following a submission of a statement of facts regarding a possible offence under section 361 or 362 of the Insolvency Act 1986, a conviction is more likely in respect of a section 361 offence (see Figure 8).

### 3.2 Action taken in cases where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation (continued)

- The most common sentence imposed following a conviction of an offence under section 361 or 362 of the Insolvency Act 1986 was Community Service (see Table 10).

**Table 10: Sentences imposed following convictions of an offence under section 361 or 362 of the Insolvency Act 1986**

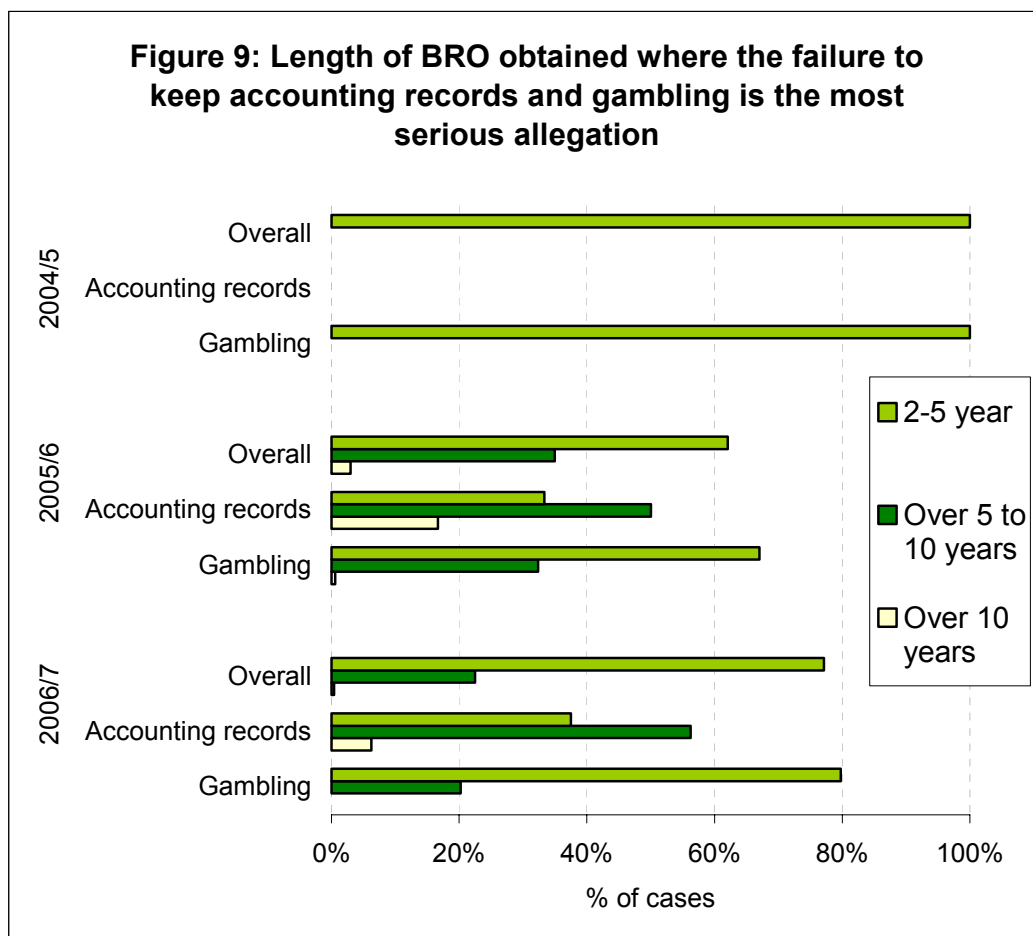
Sentences imposed on convictions	Section 361 convictions	Section 362 convictions	Total
Community Service	9	29	38
Conditional discharge	3	16	19
Fine	8	1	9
Probation/Rehabilitation Order	-	6	6
Prison sentence	2	4	6
Absolute discharge	-	2	2
Suspended sentence	-	2	2
<b>Total</b>	<b>22</b>	<b>60</b>	<b>82</b>

- As regards the 515 ATPs for BROs issued where the main misconduct was a failure to keep proper accounting records or gambling/rash and hazardous speculation (including unreasonable extravagance) in the three years ended 31 March 2007, to date an order has been obtained in all but 2 cases. This is due to the lower burden of proof required in the civil BRO proceedings compared to criminal proceedings.
- The average length of the BRO obtained was 5 years<sup>32</sup>.

<sup>32</sup> The average length of a BRO where the most serious misconduct was a failure to keep proper accounting records or gambling/rash and hazardous speculation was 5 years, 5.4 years and 4.6 years for 2004/5, 2005/6 and 2006/7 respectively.

### 3.2 Action taken in cases where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation (continued)

- A longer BRO is more likely to be imposed where the main allegation relates to a failure to keep accounting records compared to gambling (see Figure 9). This is consistent with the greater likelihood of securing a conviction following a submission of a statement of facts regarding a possible offence under section 361 compared to a section 362 offence pre-Enterprise Act 2002 (see above).



### **3.3 Creditor satisfaction with enforcement action taken where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation**

- The Insolvency Service has carried out a survey of creditors in bankruptcy cases where a criminal conviction has been obtained against the bankrupt under sections 361 or 362 of the Insolvency Act 1986 - 'failure to keep proper accounting records' and 'gambling and rash and hazardous speculation' respectively. The purpose of the survey was to establish whether, albeit that prosecution action is designed to penalise not protect, such creditors felt that such prosecution action provided any protection to the business community and more generally, the general public. A survey was then carried out of creditors in bankruptcy cases where a BRO had been obtained where the most serious misconduct was a failure to keep proper accounting records or gambling/rash and hazardous speculation (including unreasonable extravagance) to establish whether such creditors felt that the BRO offered any such protection (see Section 1.3 for further details).
- Albeit that prosecution action is not designed to provide protection, around 12% of creditors in bankruptcy cases where a criminal conviction was obtained under sections 361 or 362 of the Insolvency Act 1986 thought that the criminal conviction provided protection to the business community, with 27% being unsure. Similarly, around 9% of creditors in bankruptcy cases where a criminal conviction was obtained thought that the criminal conviction provided protection to the general public, with 27% being unsure.
- Around 43% of creditors in bankruptcy cases where a BRO was obtained (where the main misconduct was a failure to keep proper accounting records or gambling/rash and hazardous speculation) thought that the BRO provided protection to the business community, with 24% being unsure (see Figure 10).
- Similarly, around 32% of creditors in bankruptcy cases where a BRO was obtained (where the main misconduct was a failure to keep proper accounting records or gambling/rash and hazardous speculation) thought that the BRO provided protection to the general public, with 34% being unsure (see Figure 10).

### 3.3 Creditor satisfaction with enforcement action taken where there was a possible failure to keep proper accounting records or gambling and rash and hazardous speculation (continued)

