

Tony Hagerty from packager and bankruptcy remortgage specialist, Capital Link, shows brokers how changes to bankruptcy law can lead to new opportunities to help clients.

A wise man once said that 'there is nothing new under the sun'. Now I'm not going to contradict the philosopher who came up with this quote, but I think it would not be too contentious to suggest that in the mortgage market, like any other field of endeavour, what marks out the leaders, is their ability to spot new trends, new markets or just new ways of doing things. In the mortgage industry, the sub prime market did not exist much before 1997 and yet its development had a huge impact and most mortgage brokers cannot imagine a business without it.

Whilst this has spawned lenders, specialist packagers and brokers, the new niche I want to talk about is much smaller but will have a significant impact on clients, brokers and lenders in the years to come. Welcome to the world of bankruptcy and the role that brokers can play in helping bankrupt people.

Keen to remove some of the stigma of bankruptcy, the government made significant changes to the laws on personal insolvency. On 1st April 2004, the Enterprise Act 2002 became law.

Under this Act, where it is the individual's first bankruptcy, the main change is that the period before automatic discharge has reduced from three years to one year. This was part of a government policy to reduce the stigma of bankruptcy. Bankruptcy is no longer considered to be the death knell of financial independence that it was. People who could previously look forward to an extended period of supervision and leper like treatment could now rebuild their lives much sooner than ever before.

Equally significant are changes to the rules relating to assets held by a bankrupt at the time the order is made. Under the old rules, when the bankruptcy order was made, certain assets, which had a value at the time of the bankruptcy order, were transferred to the trustee appointed to administer the bankruptcy. The trustee was required to realise the asset on behalf of the creditors. In the case of a homeowner, the asset is the bankrupt's share of the equity held in the home. Sadly for the bankrupt there was no limit placed on the time the trustee had to realise this asset by selling the home. This meant that there was no urgency or pressure on the trustee to take action. While it did mean that a bankrupt might feel more secure being able to live in the home, it invariably worked against him as property values tend to increase over the long term. Because the amount of the equity held was based on a percentage of the amount of the property owned by the bankrupt at the time of the order, the knock on effect was that the amount of money due to the trustees could also increase. If this wasn't bad enough for the already beleaguered bankrupt, creditors were entitled to interest on the debt owed to them (referred to as statutory interest). Therefore the debt would actually increase in monetary terms for each year the asset was not realised to pay off creditors. Finally, not to be left out, the Treasury via the Insolvency Service, levy 'Ad Valorem' duty at between 15% and 17% on all monies paid into the

Insolvency Services' account from bankruptcy realisations. This is simply another form of taxation, designed to fund the operation of the Insolvency Service. There are documented cases where discharged bankrupts found that, although the value of the original bankruptcy was relatively low, after adding statutory interest for sometimes as long as twenty years, the total amount payable became more than the value of the equity in their home.

The Enterprise Act, where it deals with bankruptcy, means that people who find themselves bankrupt will be able to 'start again' after a much shorter period of time. The new act also recognises the inherent unfairness of the previous law. From April 2004, for all new bankruptcies, the trustee has a maximum of three years from the date of the BANKRUPTCY ORDER to realise the value of any asset or face handing it back to the bankrupt. Clearly trustees have to take steps to realise the asset within the three-year time limit, or face the possibility of a negligence action against them,

Currently, over a thousand individuals per week are going bankrupt, with many of them being homeowners. There is an opportunity for brokers to assist clients who find themselves in this position.

Brokers will almost certainly come across a great many people who need their help in finding the money to 'buy back' the beneficial interest (equity) in the part of their home owned by them before the bankruptcy. Failure to do so could result in their home being repossessed when they have been paying their mortgages on time every month. However, taking this work on means negotiation with not only the trustees in bankruptcy but also the client's own solicitors and not every solicitor has the technical knowledge of bankruptcy necessary to be effective.

As Julian Sampson, Partner at Wright & Wright Solicitors, comments,

"A sound working knowledge of insolvency law is crucial for every solicitor dealing in conveyancing, but from my experience advising lenders, a little knowledge has proven to be a dangerous thing and this is a problem which arises most frequently amongst lenders operating in the non-conforming market.

It is crucial that any solicitor has sufficient expertise to advise the lender where their lending policies are at conflict with the Enterprise Act. It is also important that the solicitor works with a team such as Capital Link who can negotiate properly and forcibly with trustees to ensure clients are not being hoodwinked into a bad deal. trustees do not advertise the loopholes in the regulations to which they are beholden and an understanding of these can be a real money-saver for the client."

To be effective for clients in this market requires a knowledge of bankruptcy as well as the time to negotiate with professionals for an outcome that might take some time. It is vital brokers get specialist help at the earliest opportunity to avoid unnecessary costs to their clients. It is not necessary to employ

expensive, hourly paid solicitors to achieve this. In many cases, significant amounts can be saved by dealing with a firm who understand the processes and keep up to date with changes in bankruptcy law and practice as and when they occur, ensuring the advice given is up to date and relevant.

However as Mike Simister, a licensed insolvency practitioner and solicitor, with Lines Henry Insolvency Practitioners, who also acts as a trustee, warns,

“Often the only asset in a bankrupt’s estate will be their share in their home. Trustees will normally try to negotiate a settlement with the bankrupt and their family without resorting to possession proceedings. The law concerning this area is complex. It is vital that lenders and advisers understand the constraints on the trustee, so as to be able to give realistic advice to their client. The trustee’s costs, which come out of the estate, can rise significantly where advisers don’t have the technical knowledge to be able to advise their client properly. This is not an area to merely dabble in. Advisers need to be prepared to learn about a technical area of the law.”

Using a specialist like Capital Link to negotiate and broker a deal for your client need not be costly. There are a number of savings to be made in achieving an annulment of the bankruptcy and giving clients the security of ‘owning’ their homes again. Annulments take longer by the nature of their complexity and the fact that a court hearing is necessary. A professional firm will ensure that all matters relating to the annulment are dealt with on behalf of clients, including but not limited to making sure the client is represented in court by lawyers with bankruptcy experience.

Clearly, given the new time frame by which trustees must act, there is now significant urgency in dealing with these matters on behalf of clients who find themselves facing the very real threat of losing their homes unless they are able to buy it back from the trustee. In reality it is not difficult to find a mortgage for clients who have been bankrupt, the difficulties can arise when you deal with the trustees. Clients are often unaware of the amount they require and a broker can find him or herself acquiring a remortgage or loan that is either insufficient or too much. This is likely to cause the trustee irritation and a loss of patience. Do not be fooled into thinking that the trustee cannot have the clients evicted just because they are paying their mortgage. He can and he will. For the simple reason that he has no choice.

Brokers will come across clients in this situation more times than they currently imagine. It is an ideal opportunity to combine additional and significant business opportunities with the chance to help people who genuinely need it.