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Bankruptcy and your home

7 issues to consider

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BANKRUPTCY: PROTECTING YOUR PROPERTY

A common question raised by individuals facing potential bankruptcy is which of their assets will fall within their bankruptcy estate and in particular what will happen to their family, who are in occupation of the family home.

In short, all (or at least most) of the assets of an individual will be included within their bankruptcy estate and will vest automatically in the Trustee in Bankruptcy ("Trustee") on the making of a bankruptcy order against the individual (the "Bankrupt").

A Bankrupt's estate involves 'all property belonging to and vested in the Bankrupt at the commencement of the Bankruptcy.' This is a very wide definition and includes most forms of property, with the main exceptions being in relation to the tools of the Bankrupt's trade and such of his personal effects which are necessary to satisfy the basic domestic needs of the Bankrupt and his family.

This guidance will deal with the Bankrupt's interest in property within the UK and with the Trustee's powers in respect of that property.

1 The Bankrupt's home and possession proceedings

The largest asset in many bankruptcies will be the Bankrupt's home and the Trustee will be keen to realise his interest in this asset for the benefit of the Bankrupt's creditors. Conventionally, the Trustee (following his/her appointment) will approach the Bankruptcy and any co-owner seeking proposals to deal with his/her interest, either by purchase of the Bankrupt's share of the equity by the co-owner (sometimes by way of remortgage), purchase by a third party or a payment of all the bankruptcy debts and expenses.

It is a common misconception that the Trustee cannot sell the Bankrupt's property if the Bankrupt and/or his/her family are in occupation of the property (especially if they have children and/or dependents). This is not the case, although in the first year of the bankruptcy the court will have regard to the rights of occupation of the Bankrupt and his family. After the first year of the bankruptcy the court will assume that the interests of the Bankrupt's creditors outweigh all other concerns (including the occupation of the Bankrupt and/or his/her family) except in exceptional circumstances.

The exceptional circumstances which may enable the Bankrupt and his/her family to remain are varied, but normally relate to any essential adaptions or changes to the matrimonial home which cannot be easily reproduced in other properties to which they may be required to move to.

If the property in question is occupied by the Bankrupt on the date of the bankruptcy (referred to herein as the "Family Home"), the Trustee has a period of three years in which to deal with this property by:

1. **Realising his interest in the property (by either selling his interest to the Bankrupt or another party);**
2. **Applying for an order for possession and/or sale of the property; or**
3. **Alternatively applying for a charging order over the property.**

Should the Trustee fail to deal with the Family Home before the end of the three year period then the Bankrupt's interest in the Family Home ordinarily re-vests in the Bankrupt automatically and the Trustee will have lost the ability to realise his interest in that asset.

2 Jointly owned property

Quite often the Bankrupt has an interest in a jointly owned property, usually the Family Home. In such circumstances the bankruptcy will automatically sever any joint tenancy between the owners and crystallise the Bankrupt's separate equitable interest in the property in the bankruptcy proceedings. This means that, in the event of the death of the Bankrupt the property does not automatically pass to the surviving co-owner (as would occur pre-bankruptcy) but their interest remains in the bankruptcy estate.

The proportion of the respective interests in the property will be divided equally between the Bankrupt and the other co-owner unless there is an agreement between them which stipulates that the property is held by them in different proportions.

The Bankrupt's share of the equity will vest automatically in the Trustee as described above.

Upon the making of the Bankruptcy order the bankruptcy is automatically registered against the property at the Land Registry (if it is a registered title). Additionally, the Trustee is able to register a restriction against a jointly owned property to reflect his interest where the bankruptcy has not been automatically registered. This will alert any third party wishing to deal with the property of the Trustee's involvement (e.g. on sale). These restrictions can then be removed after the expiry of the three year "use it or lose it" period (in respect of the Family Home), or in the event that the Trustee's interest in the property is purchased by some third party, or the costs and debts of the bankruptcy are paid, e.g. by possession and sale of the property by the Trustee.

3 Dealing with co-owner's interests

Co-owners, most often spouses or civil partners, are usually the innocent victims of the loss of the Family Home as a result of their partners' bankruptcy.

However, their interest can be improved with proper consideration. Contributions to works on the Family Home or to its acquisition, maintenance or secured debt may all mean that the co-owners' interest exceeds the 50% value ordinarily ascribed. Preferably, such a different share of the equity should be reflected against the property's title at the Land Registry, but the failure to file any such notice does not always mean that their interest cannot be increased in negotiations with the Trustee.

Previous transfers of property assets from the Bankrupt, at first seemingly at an undervalue, can be for value when non-monetary consideration was provided. For example, matrimonial financial disputes are often settled on the basis of an agreement to transfer part of a joint owner's equitable interest in the Family Home to their partner.

There are various other subjective matters to be considered in negotiations with a Trustee and the prospect of losing your home is not always as bleak as it may initially seem.

4 Other residential property

As discussed above, all of the Bankrupt's assets vests automatically in the Trustee upon the making of a Bankruptcy order. The Trustee will usually take steps to value any property the Bankrupt may have, whether or not s/he resides in it, immediately following the Trustee's appointment and will then take steps to realise this interest if there is any equity available in excess of £1,000.

The three year limitation rule described above only applies to the Family Home and the Trustee is not required to take steps to realise his interest in any property owned or part-owned by the Bankrupt if he was not ordinarily resident there as at the date of the Bankruptcy order. Such property remains part of the bankruptcy estate until either the Trustee realises his interest in the property or alternatively until the Trustee raises sufficient funds from other sources to pay off the costs and debts of the bankruptcy in full (at which point he may be discharged as Trustee).

5 Low value family home

The Trustee will however be unable to obtain an order for possession and sale of the Family Home, if the value of the Bankrupt's share of the equity, after the estimated costs of sale and deduction of any co-owner's equitable interest, in the Family Home is less than £1,000.

6 Charges over the family home

If the Trustee is unable to realise his interest in the Family Home within three years he may apply to court for an order imposing a charge on the Family Home, for the benefit of the Bankrupt's creditors.

Once the charge is secured over the Family Home the bankrupt's interest in the Family Home reverts to the Bankrupt, subject to the charging order. The Trustee can either wait for the Bankrupt to sell the Family Home and take his share of the proceeds, or he can in the future apply for an order for possession and sale of the Family Home by way of enforcement of the charging order.

7 Disposing of property before bankruptcy

It is not uncommon for a Bankrupt's interest in the Family Home or other property to be transferred (quite often to their partner or another family member) either innocently or in anticipation of a bankruptcy order being made. This is sometimes done to "ring fence" that property from the subsequent bankruptcy proceedings.

However, such antecedent transactions are easily set aside by the Court upon the Trustee's application under certain circumstances.

As with possession proceedings, the Trustee will normally seek to negotiate his interest with the recipient of the transaction (which is quite often the partner who has received the Bankrupt's interest). if this is unsuccessful, under certain conditions the Trustee will issue proceedings to set aside the transaction against the Bankrupt's partner or other individual. The Trustee will also seek an order that his legal costs be paid by that individual.

However the insolvency legislation requires that upon such an application a number of factual circumstances must be proven by the Trustee, in the absence of which such an application would be unsuccessful. This can cause great difficulty for the Trustee in proceedings and for this reason it is usually preferable for both parties to reach a negotiated settlement.

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