

The bankrupt's home – before and after the Enterprise Act 2002: follow-up report

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Section 1: Executive Summary

1.1 Introduction

Under provisions introduced on 1 April 2004, the Enterprise Act 2002 ('EA') made a number of significant changes to the process of bankruptcy. The Insolvency Service has carried out a retrospective evaluation to consider what has happened since the implementation of the Act and to assess the real effects of that legislation.

This report updates the results of an earlier case-sampling exercise looking at the way in which a bankrupt's interest in a family home has been dealt with¹. It is a follow-up to the Insolvency Service's evaluation of the personal insolvency provisions of the EA which was published in November 2007².

Prior to the EA, the time scale within which a bankrupt's interest in a property could be dealt with was opened-ended. Instead of this, the EA provided that where a bankrupt has an interest in a family home, the trustee must take action to deal with that interest within 3 years, otherwise that interest will revert to the bankrupt at the end of this period (unless an application for an extension of time is made).

In more detail, the EA provides that a bankrupt's interest in a family home will re-vest in the bankrupt after 3 years unless one of the following events occurs before that date:-

- the trustee realises the bankrupt's interest;
- the trustee applies for an order for possession and/or sale;
- the trustee applies for a charging order;
- the trustee and the bankrupt agree that the bankrupt shall incur a liability in consideration of which the bankrupt's interest shall cease to form part of his estate; or
- the trustee sends notice to the bankrupt that he considers that the continued vesting of the dwelling-house in the bankrupt's estate will be of no benefit to creditors or that re-vesting will facilitate a more efficient administration of the bankrupt's estate.

¹ An interest in a family home is defined as a property interest that falls under the definition of a 'qualifying interest' under the Enterprise Act 2002. A 'qualifying interest' is a bankrupt's interest in a dwelling house that is the sole or main residence of the bankrupt, the bankrupt's spouse or civil partner, or former spouse or former civil partner.

² The evaluation reports are available at:-

<http://www.insolvency.gov.uk/insolvencyprofessionandlegislation/legislation/evaluation/finalreport/home.htm>

The three-year period commences on the date of the bankruptcy order or, if the bankrupt does not inform the official receiver or any insolvency practitioner acting as trustee of their interest within 3 months of the bankruptcy order, the date that the official receiver or other trustee becomes aware of the interest³.

The main reasons for the EA changes were:-

- to provide some certainty to the bankrupt, the trustee and the creditors as to the time scale within which the bankrupt's home will be dealt with, as previously that time scale was open-ended;
- to provide a balance between the interests of the bankrupt (and his/her family) and their creditors by providing ample time for the disposal by the trustee of the bankrupt's interest in his/her sole and principal residence in the most appropriate manner; and
- to help lift the stigma of bankruptcy.

To consider the impact of the family home provisions of the EA and to consider whether the EA has met its policy objectives, the Insolvency Service carried out an analysis of the way in which property interests were dealt with in a sample of cases commencing before 1 April 2004 (pre-EA) and after that date (post-EA).

That research was undertaken to assess whether the new regime provides certainty to the bankrupt, the trustee and creditors as to the time scale within which the family home will be dealt with, and whether that time scale is sufficient for the disposal by the trustee of the bankrupt's interest in his or her sole and principal residence in the most appropriate manner.

At the date of the original report, a significant number of property interests in the post-EA sample of bankruptcies had not yet been realised and these cases have therefore been revisited.

The original report recommended that the Insolvency Service complete the post-EA case sampling exercise as regards a bankrupt's interest in a family home to obtain full post-EA information on:

- how often, and why, property interests are not dealt with within 3 years from the bankruptcy order;
- the overall timeliness of dealing with property interests;
- how often methods of dealing with a property interest which could be said not to offer certainty to the bankrupt, the trustee or creditors are used, and why;

³ The Enterprise Act 2002 also contains transitional provisions for cases where the bankruptcy petition was presented before 1 April 2004 where there is a bankrupt's interest in a family home. The transitional provisions state that such interests must be dealt with by 31 March 2007 (unless an application for an extension of time is made) - otherwise, the interest reverts to the bankrupt on this date.

- the effect of the re-vesting provisions; and
- the effect of the 'de-minimis' provisions.

Because of difficulties in obtaining full financial information (for example on sale prices, the extent of secured claims and consideration received) this report focuses largely on the methods used to realise bankrupts' property interests and the timeliness of such realisations.

Following similar exercises in 2004/05 and 2006/07, the Insolvency Service has this year undertaken further surveys of bankrupts, businesses and the general public to obtain a cross section of views regarding attitudes to bankruptcy and in particular whether there is a stigma attached to bankruptcy, and if so, the reasons why. The full results of those surveys will be published shortly but the final section of this report briefly considers the extent to which the possible loss of the family home contributes to any stigma associated with bankruptcy.

1.2 Key Findings

- The study period coincided with a significant general increase in mortgage possessions in the housing market which is likely to have had any impact on the overall results. Around one-fifth of the properties in the pre-EA sample were subject to repossession orders, this rose to more than a third of the post-EA cases and this makes it difficult to isolate any impact that the EA may have had on the ways in which a family home has been dealt with.
- The main methods for realising property interests were the same in both samples, but there were some noticeable changes in the breakdown of realisation methods, which in part are likely to have been influenced by general conditions in the housing market.
- More than a quarter of property interests in the pre-EA sample were dealt with through a voluntary sale on the open market, this fell to around 10% of the post-EA cases. The fall in the proportion of voluntary sales is matched by the rise in the proportion of mortgage possessions that were identified, though the general rise in repossessions may also have had an impact on changes in the use of other realisation methods.
- The percentage of property interests realised through an agreement with the trustee in bankruptcy fell from around two-fifths among the pre-EA bankruptcies to just under a third of the post-EA cases. Meanwhile, the proportion of cases dealt with under the Insolvency Service's low-cost conveyancing scheme (LCCS) rose from 4% to 10%. This is likely to largely be a reflection of the increased number of cases in which the official receiver rather than an insolvency practitioner acted as trustee among the post-EA sample compared to the pre-EA cases (among the post-EA sample the official receiver acted as trustee in 36% of cases compared to 23% of the pre-EA bankruptcies). The general rise in repossessions, the policy of the Insolvency Service in dealing with bankruptcy assets, and general conditions in the housing market are also likely to have had an influence on these results.
- The proportion of cases in which the trustee took action through the court for possession and/or sale remained similar in both time periods at around 5%.
- There was a very slight increase in the proportion of property interests that re-vested in the bankrupt/former bankrupt from 2% of cases in the pre-EA sample to 3% of the post-EA bankruptcies.
- The use of charging orders was minimal in both periods.

- The average time taken to deal with property interests fell from around 2 years among the pre-EA bankruptcies to 20.5 months among the post-EA cases.
- There was a significant rise in the proportion of property interests that were dealt with within 3 years of the making of a bankruptcy order among the post-EA sample relative to the pre-EA cases. Some 97% of property interests in the post-EA sample were dealt with within 3 years of the making of a bankruptcy order, the corresponding figure among the pre-EA bankruptcies was around 75%.
- The family home provisions of the EA, however, do not appear to have had any impact on reducing the stigma associated with bankruptcy. This is largely because a much higher proportion of bankrupts surveyed in 2009, who consider that there is a stigma associated with bankruptcy, thought that the potential loss of the family home was a reason for the creation of stigma compared to previous surveys in both 2004 and 2006. The views in this area among businesses and individuals who consider that bankruptcy carries a stigma showed relatively little change over the same period.

1.3 Methodology

The full methodology is set out in the original report. In summary, the Insolvency Service has carried out a case sampling exercise to obtain information about the realisation of property interests in bankruptcies commencing both before and after the implementation of the family home provisions of the EA. To ensure cross-country coverage, information on the realisation of property interests was gathered from an official receiver's office⁴ from each of the Insolvency Service's operational regions.

Table 1 summarises the sample framework. These figures exclude cases from the original samples in which the bankruptcy order was annulled or the costs and debts of the proceedings were paid in full and also those cases where there was insufficient information on property realisations.

Table 1: Sample sizes		
Size of sample where information was available on:	Property interests in y/e 31/8/03 (pre-EA)	Property interests in y/e 31/8/05 (post-EA)
Whether property interest dealt with	419	685
Realisation method	415	685
Timeliness of realisation (excluding repossessions)	330	429

⁴ The offices sampled were Birmingham A, Blackpool, Bournemouth, London A, Newcastle, Northampton and Reading.

Section 2: Results

2.1 The realisation of bankrupts' interests in a family home – method

The most common methods identified in both samples for dealing with bankrupts' family home interests were as follows:-

- Agreement with the trustee in bankruptcy – the debtor or a third party agrees to purchase the bankrupt's interest in the property from the trustee.
- Repossession order – the property is repossessed by the mortgagee.
- Voluntary sale of the property on the open market – the property is sold and the trustee receives the value of the bankrupt's interest in the property for the benefit of creditors.
- LCCS – the debtor or a third party agrees to purchase the bankrupt's interest in the property from the Official Receiver acting as trustee.
- Order for possession and/or sale – the trustee takes action through the court to obtain an order for possession and/or sale of the property.

As shown in Figures 1 and 2 below, there have been some changes in the breakdown of realisation methods. The general increase in mortgage possessions over the period of study, however, makes it difficult to assess the extent to which the provisions of the EA may have impacted on the ways in which property interests have been dealt with. Moreover, rather than changing the ways in which property interests were realised, the Act was primarily concerned with limiting the time available to a trustee to deal with, or take action to secure, property interests for the benefit of a bankrupt's creditors.

As highlighted in the original report, the study period coincides with a general and significant increase in mortgage possessions since around the first half of 2004, a trend which continued in both 2007 and 2008⁵. The results summarised below reflect that general trend – while around a fifth of properties were repossessed by the mortgagee in the pre-EA cases, this figure rose to over a third for the post-EA bankruptcies.

⁵ The Council of Mortgage Lenders reported around 40,000 possessions in 2008 compared with some 26,000 possessions in 2007.

Figure 1: Pre-EA realisation methods

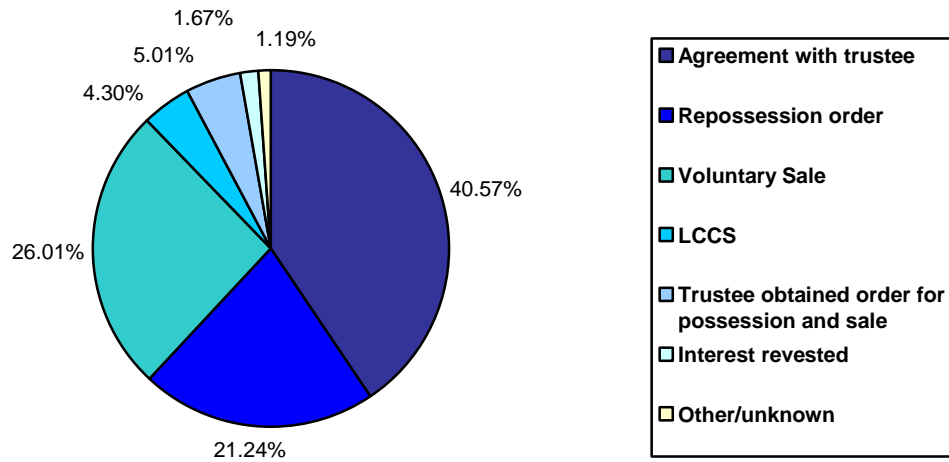
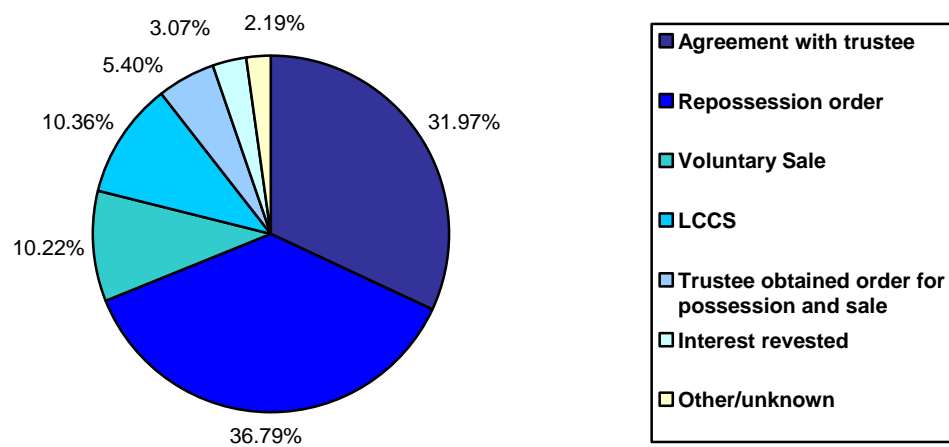


Figure 2: Post-EA realisation methods



The rise in mortgage possessions is also likely to have significantly contributed to the relative changes in realisation methods, in particular to the fall in the percentage of property interests that were realised through a voluntary sale on the open market. Indeed, at a time when the proportion of repossessions rose by nearly 16% points, the proportion of voluntary sales fell by a similar figure.

The other major changes highlighted above are the relative decline in the proportion of property interests realised through agreement with the trustee and the rise in the percentage of cases dealt with under the LCCS. Again, the relative increase in the number of mortgage possessions may have

contributed to the decline in the proportion of cases in which the bankrupt's interest in a property was purchased from the trustee. Although these results can also be explained by the relative increase in the number of bankruptcies in which the official receiver rather than an insolvency practitioner acted as trustee - among the post-EA sample the official receiver was trustee in 36% of cases, compared to 23% of the pre-EA bankruptcies.

The proportion of cases in which the property interest re-vested in the bankrupt were relatively low in both the samples, though this figure was slightly higher among the post-EA cases. This is perhaps more likely to be a reflection of underlying conditions in the housing market and the economy generally rather than any suggestion that the trustee was unable to adequately deal with the property in the 3 years set out by the Enterprise Act.

As explained in the original report, although the EA aims to ensure that in almost all cases the property interest is dealt with within 3 years of the bankruptcy order, there are instances where the method of dealing with the property interest may not be considered to offer certainty to the bankrupt, trustee or creditors. This is because in some cases, the way the property interest is dealt with involves changing the nature of that interest, which will require action in the future to actually realise the property interest.

Although the significant number of mortgage possessions identified in both samples impairs the drawing of firm conclusions about the impact of the EA, it would appear that the methods of realising a property which could be said not to offer certainty have been relatively little used:-

- no cases have been identified either before or after the EA where the trustee and the bankrupt agree that the bankrupt shall incur a liability in consideration of which the bankrupt's interest shall cease to form part of their estate;
- the proportion of cases in which the trustee obtained an order for possession and/or sale was similar in both periods at around 5%.
- both before and after the EA, the trustee has applied for/obtained a charging order in less than 1% of cases (2 charging orders were identified in the pre-EA sample and 4 among the post-EA sample).

Of course, the EA provisions aim to provide a balance between the interests of the bankrupt (and their family) and their creditors by providing sufficient time for the disposal by the trustee of the bankrupt's interest in their sole and principal residence in the most appropriate manner. Essentially, the EA seeks to ensure that an interest in a property is still an asset of the estate, and creditors will receive a return (where there is equity in the property) from the timely realisation of this asset.

Prior to the EA, all property interests were eventually realised unless the property interest was disclaimed (a property interest may still be disclaimed where that is the most appropriate course of action post-EA). Under the EA, a property interest can re-vest in a bankrupt if either the trustee sends notice to the bankrupt that he considers that the continued vesting of the dwelling-

house in the bankrupt's estate will be of no benefit to creditors of that the re-vesting will facilitate a more efficient administration of the bankrupt's estate, or of the trustee fails to deal with the property interest within the 3 year period.

The proportion of cases in which the property interest re-vested in the bankrupt did show a slight increase in the post-EA sample compared to the pre-EA cases, but these provisions only applied in around 3% of cases. Again, this change is likely to perhaps be a reflection of underlying economic and market conditions which have seen a general decline in house prices, a rise in cases of negative equity and an increase in mortgage possessions. That the re-vesting provisions have only been applied in a small number of cases also appears to reflect that where there is value in the property, even if of a relatively low value, then steps are being taken to realise that interest for the benefit of creditors, and this is evidenced by the rise in the proportion of cases dealt with under the LCCS.

2.2 The realisation of bankrupts' interests in a family home – timeliness

For each of the cases in both samples, the date that the property interest was realised (where known) was noted and compared to the date of the bankruptcy order to give a measure of timeliness⁶.

In all this information was available in 419 of the pre-EA cases and 680 of the post-EA bankruptcies. Setting aside those cases where the property was repossessed by the mortgagee⁷ and the trustee therefore had no control over the realisation, information on timeliness was available in 330 of the pre-EA cases and 429 of the post-EA bankruptcies.

The results are summarised below, but as noted in the original report the transitional provisions of the EA (see section 1.1) may have affected the timeliness of realisations among the pre-EA bankruptcies, as trustees were required to take action to avoid the interest re-vesting in the bankrupt on 31 March 2007.

Excluding those cases where the property was repossessed, among the pre-EA sample the average time taken for a property interest to be realised was 714 days (just under 2 years) and this fell to an average of 615 days (around 20.5 months) for the post-EA cases.

As demonstrated in Figure 3, the most marked change between the two periods is that around 97% of realisations among the post-EA sample were effected within 3 years of the bankruptcy order being made; whilst among the pre-EA cases some 25% of realisations occurred more than 3 years after the date of the bankruptcy order.

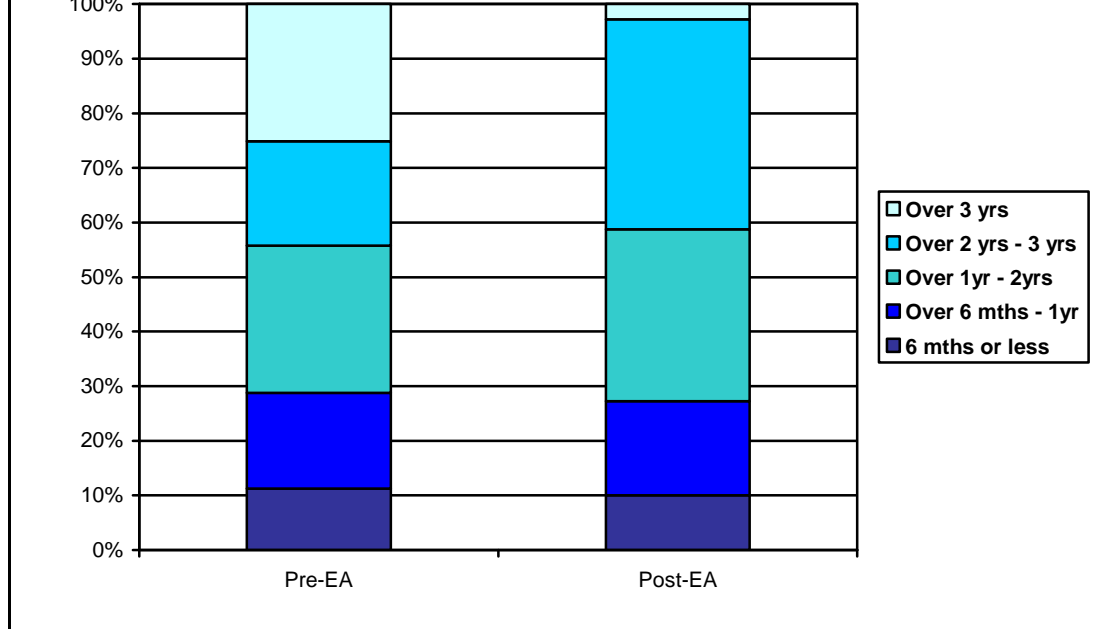
These figures and the methods of realisation identified in section 2.1 suggest that the legislation has had the desired affect of introducing greater certainty as to the time period within which a bankrupt's interest in the family home will be dealt with.

Among the post-EA sample, in only 12 of the 429 cases for which timeliness information was available did the realisation occur more than 3 years from the date of the bankruptcy order. The precise reasons why these realisations took more than 3 years are not known, and it may be that the trustee was not made aware of these property interests within 3 months of the date of the bankruptcy order, but in 7 of these cases a sale occurred with the agreement of the trustee, in 4 cases the trustee obtained an order for possession and/or sale and in the remaining case the debtor remortgaged.

⁶ For convenience, the number of days was calculated on the assumption of a 360-day year consisting of twelve 30-day months

⁷ For completeness and by way of comparison, the average time for a property to be repossessed by the mortgagee among the pre-EA cases was 418 days and the corresponding figure for the post-EA sample was 469 days.

**Figure 3 :Timeliness of property realisations
(excluding repossessions)**



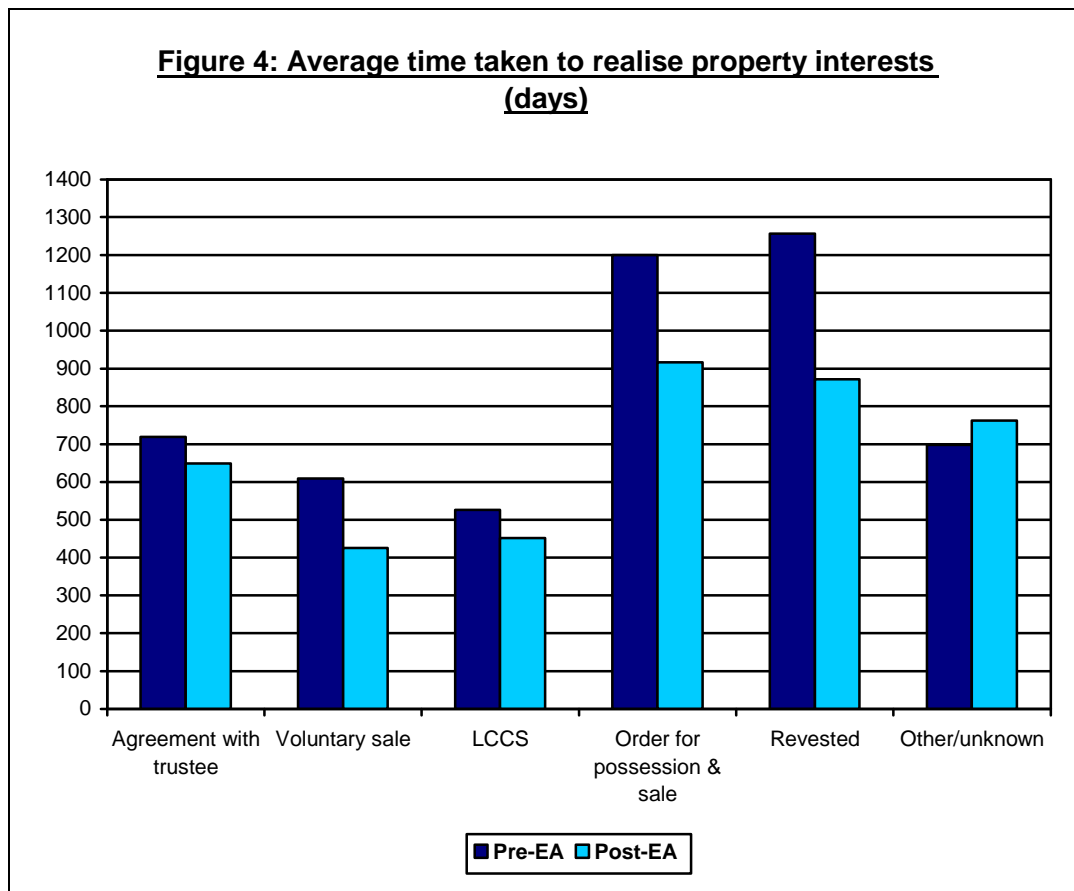
The timeliness data was further analysed to consider the average timeliness for each of the methods of realisation identified in section 2.1, and Figure 4 shows the average number of days taken to realise property interests under each of the main methods of realisation (excluding mortgage possessions).

For each of the individual methods of realisation shown in Figure 4, the average realisation time was lower among the post-EA sample than the pre-EA cases; and in both time periods the average realisation times were lowest where the property interest was dealt with under the more common means of realisation, that is to say by agreement with the trustee, through a voluntary sale or a transfer under the LCCS.

The Insolvency Service's internal policy⁸ is that action should not be taken to proactively seek to re-vest properties until at least 2 years and 3 months has passed since the date of the bankruptcy order, although any reasoned requests from the bankrupt for earlier re-vesting should be considered. As this is an internal policy it would not be binding on an insolvency practitioner acting as trustee. Among the pre-EA sample, 7 cases were identified in which the property interest re-vested in the bankrupt and the average time taken for the re-vesting was around 3.5 years. That average fell to under 2.5 years for the 21 cases in the post-EA sample in which re-vesting occurred. These

⁸ The Insolvency Service's policy is set out in Chapter 33 (Bankrupt's interest in the family home) of its technical manual, which is available at:- <http://www.insolvency.gov.uk/freedomofinformation/technical/TechnicalManual/Default.htm>

results therefore appear to be consistent with the general policy adopted by the Insolvency Service.



2.3 Stigma of bankruptcy

This section briefly considers whether providing greater certainty as to the time scale in which a bankrupt's interest in a family home may be realised has helped to lessen the stigma associated with bankruptcy.

To understand attitudes to bankruptcy generally, and to consider the reasons why there may be a stigma associated with the procedure, the Insolvency Service has carried out a series of surveys of bankrupts, businesses and the general public since 2004. The earlier results are subject to separate reports⁹ and findings from the 2009 surveys will be published shortly.

Previous reports have identified that a majority of bankrupts, individuals and businesses consider that there is a stigma associated with bankruptcy. As demonstrated in Table 2, the latest results show that this is the still case, but the proportion of bankrupts, businesses and individuals who agree that bankruptcy carries a stigma were all lower in 2009 than in both 2004 and 2006.

Year	Overall	Bankrupts	Business	Individuals
2004	71%	83%	77%	53%
2006	67%	85%	72%	45%
2009	64%	77%	70%	43%

In terms of the effects of bankruptcy, the overall opinion¹⁰ has been that difficulties in obtaining a bank account, being unable to repay creditors, and an adverse impact on credit rating, are the main reasons why stigma exists.

Attitudes as to whether the possible loss of the family home contributes to stigma have been rather mixed between the three surveyed sectors and have shown some changes over time as demonstrated in Table 3.

⁹ See "Attitudes to Bankruptcy" and "Attitudes to Bankruptcy Revisited" - <http://www.insolvency.gov.uk/insolvencyprofessionandlegislation/policychange/policychange.htm>

¹⁰ The overall opinion is the combination of the survey results of bankrupts, individuals and businesses, and is an average of these sectors' responses, i.e. each sector has been given equal weighting.

Table 3 – Those who consider that the possible loss of the family home contributes to the stigma associated with bankruptcy

Year	Overall	Bankrupts	Business	Individuals
2004	67%	50%	83%	69%
2006	64%	49%	82%	62%
2009	75%	80%	80%	65%

Results among the business sector and the general public on whether the potential loss of the family home contributes to the stigma associated with bankruptcy have shown little change since 2004. The perception among bankrupts though had clearly changed in 2009 compared to both of the earlier years and those results appear somewhat puzzling.

The percentage of bankrupts who considered that there is a stigma associated with bankruptcy fell from 85% in 2006 to 77% in 2009, yet there was a marked rise in 2009 in the proportion of bankrupt respondents who agreed that the possible loss of the family home contributed to the creation of that stigma.

As the EA reforms were introduced in 2004, and there was no change in the legislative position regarding the realisation of property between 2006 and 2009, the reasons for these results among bankrupts are not wholly clear. While these results have not been tested, sample sizes and bias may have played a part; but this change could also perhaps be due to an increase in the number of bankrupts surveyed who had property interests, underlying conditions in the economy and housing market, and perhaps greater general uncertainty about the future.

Of course, a bankrupt's interest in the family home is potentially an asset in the bankruptcy proceedings to be realised for the benefit of creditors and this position was not changed by the EA which simply sought to introduce a statutory time scale for dealing with such property. On the basis of these results it therefore seems feasible to suggest that it is the possible loss of the home itself, and not necessarily the time scale in which it is dealt with, that is the principle contributor to perceived stigma. Overall though, the Service considers that the time scale introduced by the EA is more appropriate in balancing the interests of debtors and their creditors than the previously open-ended position.

Appendix 1: Realisation Methods

	Agreement with trustee	Repossession order	Voluntary sale	LCCS	Trustee obtained order for possession and/or sale	Interest re-vested	Other	Unknown
Pre-EA (419 cases)	170	89	109	18	21	7	1	4
Post-EA (685 cases)	219	252	70	71	37	21	15	0

Appendix 2: Timeliness of realisations

Average time taken (number of days) to realise property by method of realisation

	Method of realisation						Overall
	Agreement with trustee	Voluntary sale	LCCS	Trustee obtained order for possession and/or sale	Re-vested	Other/unknown	
Pre-EA	719	609	526	1,200	1,256	698	714
Post-EA	649	426	452	917	871	762	615

Number of realisations by time period

	6 months or less	Over 6 months – 1 year	Over 1 yr – 1.5 yrs	Over 1.5 yrs – 2 yrs	Over 2 yrs – 2.5 yrs	Over 2.5 yrs – 3 yrs	Over 3 yrs
Pre-EA	37	58	49	40	39	24	83
Post-EA	43	74	73	62	74	91	12

Timeliness by method of realisation

	Agreement with trustee		Voluntary sale		LCCS		Trustee obtained order for possession and/or sale		Interest re-vested		Other/unknown	
	Pre-EA	Post-EA	Pre-EA	Post-EA	Pre-EA	Post-EA	Pre-EA	Post-EA	Pre-EA	Post-EA	Pre-EA	Post-EA
6 mths or less	17	11	15	13	4	18	0	0	1	1	0	0
Over 6 mths – 1 yr	27	34	27	22	4	15	0	0	0	1	0	2
Over 1 yr – 2 yrs	52	77	26	22	5	24	3	6	0	3	3	3
Over 2 yrs – 3 yrs	35	90	22	13	2	14	2	23	0	16	2	9
Over 3 yrs	39	7	19	0	3	0	16	4	6	0	0	1