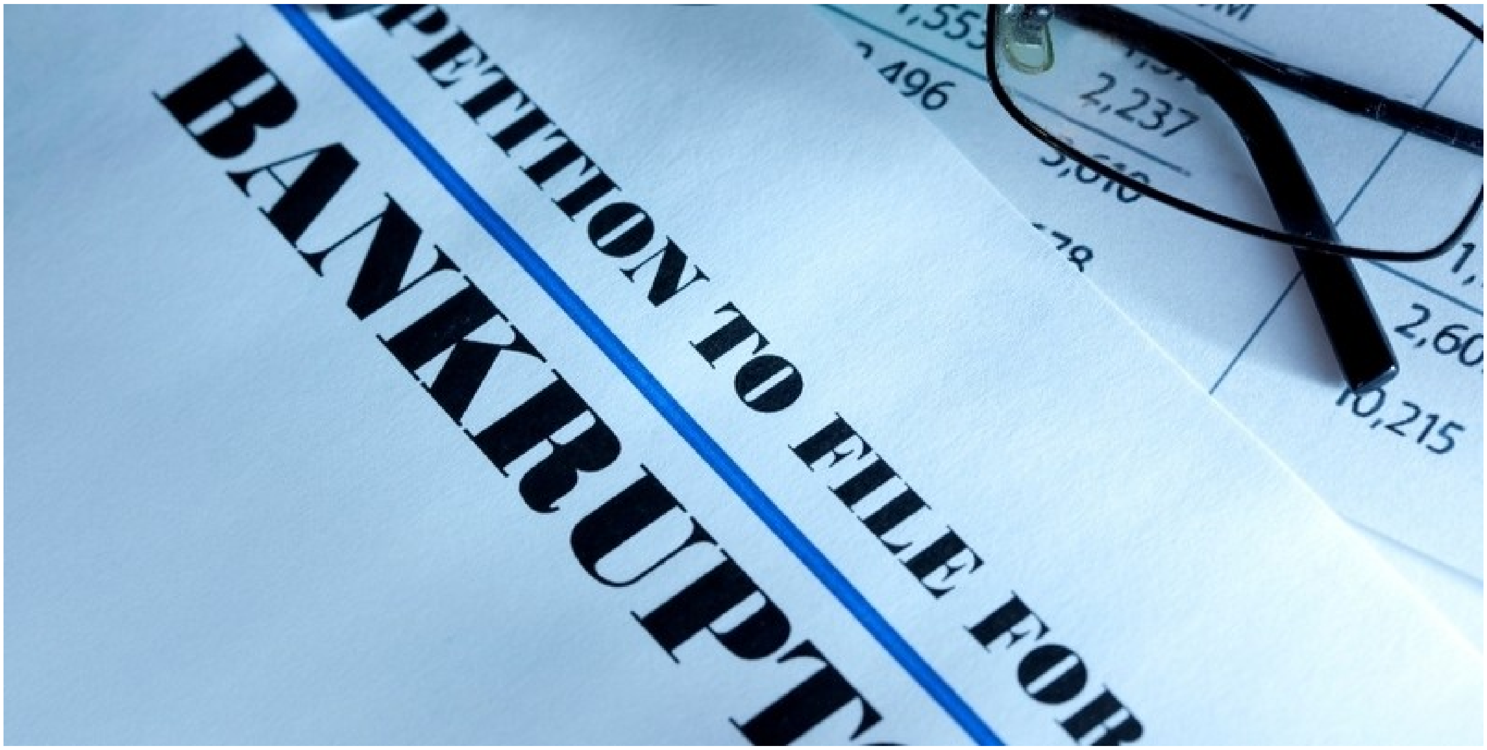
How advisers bounce back from bankruptcy

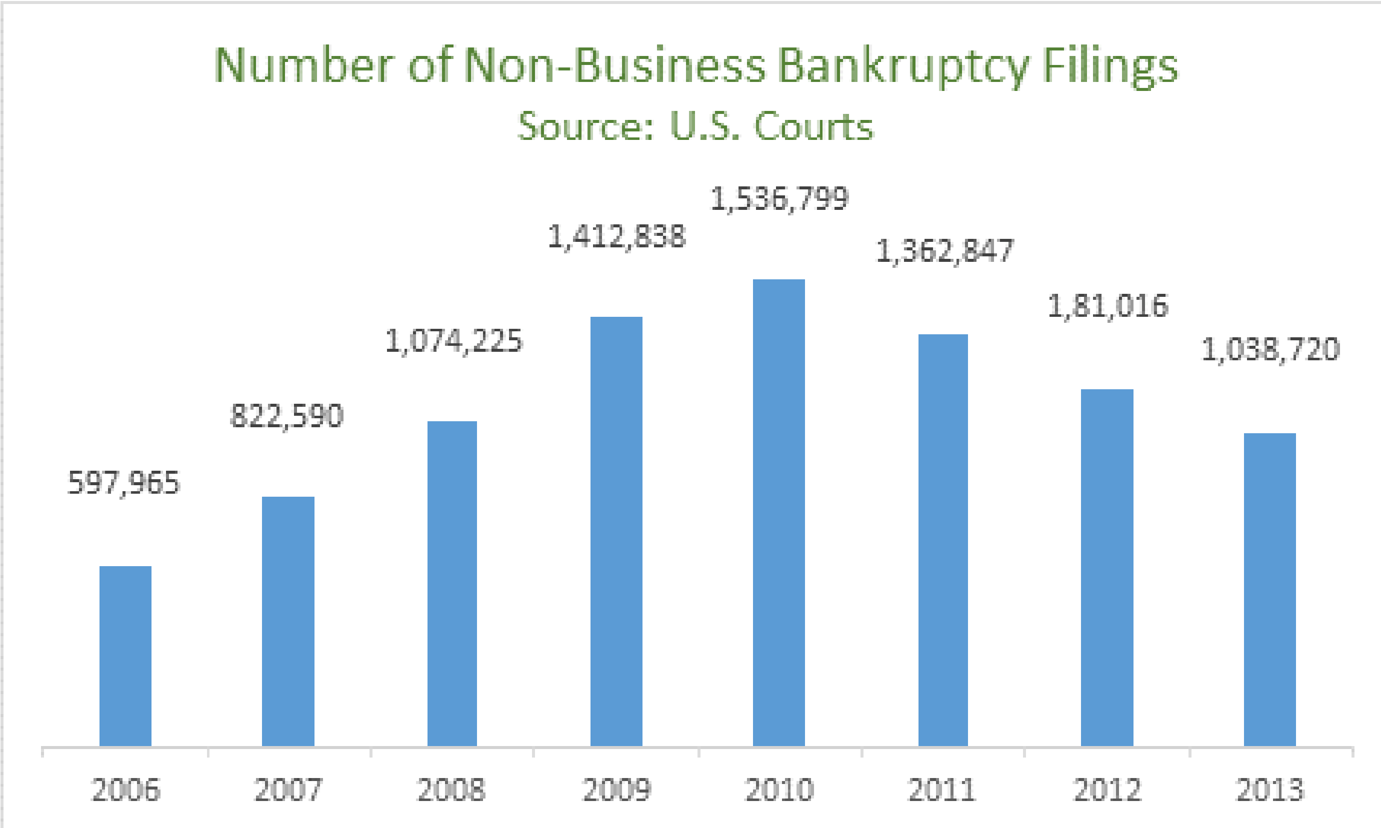


Advisers aren't immune to the financial strains that lead more than a million Americans to file for personal bankruptcy every year, though they may face some extra professional challenges after such a step.

“Financial professionals have to be so above reproach in this particular area because it would rightfully raise a question of whether a client should trust you with their money if you haven't been very responsible with your own,” said bankruptcy attorney Mark Buckley.

Advisers with a bankruptcy in their past should find a way to describe the filing to prospects or clients that shows it was a unique situation, not just that they were living beyond their means, said Mr. Buckley, who holds a certified financial planner designation but doesn't practice as a financial adviser.

Extraordinary circumstances sometimes force people into bankruptcy, he said. For instance, he's seen people declare bankruptcy because they had a child with special needs and were overwhelmed by medical bills. In another case, a client and his wife depended on two incomes, but she lost her job.



Unsurprisingly, the number of Americans filing for bankruptcy jumped during the nation's economic downturn beginning in 2008. The number of non-business bankruptcies filed in U.S. courts in 2010 reached 1.54 million, up from about 600,000 in 2006. Last year, there were just over 1 million non-business bankruptcies.

Overall, the face of bankruptcy has morphed in recent years and it's more likely than ever to resemble a financial professional.

Bankruptcy attorney Jay Fleischman of Shaev & Fleischman said he's worked with lots of financial advisers, insurance professionals and certified public accountants who have filed for bankruptcy, in some cases because their income “took a stumble” due to the vagaries of the market or real estate catastrophes.

“The public thinks that personal bankruptcy is largely the providence of the middle class or lower middle class,” he said. “Over the last five to six years that has been turned on its head.”

The typical bankruptcy filer now is far more likely to be more upper middle class or high-net-worth, as the economic collapse was felt more acutely by people who were making six and seven figures in 2006, he said.

“Bankruptcy has become far more regular for those who were doing just fine, making money, owning cars and houses, a high net worth, and then the bottom dropped out of their holdings,” Mr. Fleischman said. “They did what they could under the law to get rid of their debts.”

Personal bankruptcies typically are not plastered on the front page of newspapers, so to a large extent many clients and other associates may not even know about it. However, being forthright about it is usually the best plan, Mr. Fleischman said.

“I'm a big fan of transparency, especially in this day and age,” he said. “So many people have been through the ringer financially that bankruptcy doesn't have the same stigma that it did a decade ago.”

Self-employed professionals should make sure they have set up a tax escrow account to pay quarterly taxes on time, Mr. Fleischman said. About 80% of the self-employed professionals who come to him with issues have fairly significant past-due tax obligations.

Mr. Buckley recommends all his clients who have filed for bankruptcy enroll in a credit rebuilding program so they get their FICO credit score back up above 720.

“I encourage them to get a couple of credit cards and to make sure they use them in a responsible manner,” Mr. Buckley said.

He also recommends financial professionals think twice before filing for bankruptcy.

“It really should be a matter of last resort,” Mr. Buckley said. “When people call me, I try to explore whether they can downsize their housing, put kids in public schools or find other avenues to avoid bankruptcy.”

Under Certified Financial Planner Board of Standards Inc. policy, the names of professionals who file for bankruptcy are regularly published and a note is made in their public profile. It stays a part of their electronic record for 10 years.

The board used to investigate its professionals who filed for bankruptcy, but changed its policy as of July 2012, when the pace of adviser bankruptcies picked up. The board pursued only one bankruptcy case in 2008, and the number rose to 49 in 2011.

The CFP Board, which still investigates its professionals if they have a second bankruptcy filing, printed the names of 48 more CFP professionals last month who have filed for bankruptcy in recent years. About 215 professionals in total have been named in releases as having filed for bankruptcy, and the “vast majority” of those “remain active in the industry and continue to hold the CFP certification,” according to an e-mail from CFP Board spokesman Dan Drummond. Nearly all the bankruptcies on the list are personal.

The names of CFPs who have filed for bankruptcy are provided to make sure consumers have “adequate information” to decide whether to engage a particular financial planner to help with financial decisions, the board said in its April 18 release.