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PPI compensation windfall of debtor discovered after completion of IVA belongs to creditors and not to debtor

*James Green (as Supervisor of Mr Wright's IVA) v.
James Patrick Wright
[2017] EWCA Civ 111*

Article by David Bowden

Executive speed read summary

A debtor entered into an IVA in 2007 and made all payments due under it for 5 years. His IVA supervisor then issued him with a certificate of completion. Included in the IVA proposal were debts owing to 2 banks – RBS and Barclays. After a past business review, those 2 banks paid the IVA supervisor £24,500 relating to mis-sold PPI. Those payments were made 8 months after the IVA had completed. The IVA supervisor applied to the court for directions as to what to do with the PPI payments. The county court and High Court said the PPI remediation payments had to be paid to the debtor. The Court of Appeal disagreed and has overturned those rulings. It has said that the trust created by an IVA survives a certificate of completion. The effect of its ruling is that the PPI windfall payment has to be distributed by the IVA supervisor to all the creditors in the proportions set out in the IVA proposal. It follows that the debtor will not be able to bank or spend this £24,500 windfall payment.

James Green (as Supervisor of Mr Wright's IVA) v. James Patrick Wright
[2017] EWCA Civ 111 1 March 2017
Court of Appeal, Civil division (Lords Justices of Appeal David Richards and Irwin)

What were the IVA proposals?

Mr Wright realised he was insolvent in the summer on 2007. Mr Green was appointed as a nominee and drew up proposals which were agreed at a creditor's meeting in October 2007. Mr Green was appointed as supervisor of Mr Wright's individual voluntary arrangement ('IVA'). Mr Wright was able to keep possession of his home and his car. Mr Wright made monthly payments due under his IVA regularly for 5 years. The IVA was governed by a set of Standard Conditions (as modified at the creditors' meeting) issued by R3 (the Association of Business Recovery Professionals).

In January 2013 the IVA supervisor issued Mr Wright with a certification of completion of his IVA. His IVA then came to an end.

How did the claim for PPI compensation arise?

Amongst Mr Wright's creditors were 2 banks – Barclays and Royal Bank of Scotland. These banks had loaned money to Mr Wright and at the same time they had sold him payment protection insurance ('PPI'). Following a past business review which the Financial Conduct Authority ordered these banks to carry out, the banks determined that the sales of PPI had one of more of the 'common failings' identified by the FCA's predecessor in title (the Financial Services Authority) in its Policy Statement PS 10/12 issued in August 2010.

The aggregate of the PPI remediation from the 2 banks was £24,500. As the banks were included as creditors in the IVA they paid the remediation to the IVA supervisor and not to the debtor. The IVA supervisor received the PPI payments in September and October 2013 some 9 months after the IVA had completed.

What does the Insolvency Act 1986 say?

A few definitions in the Insolvency Act 1986 ('IA') are critical when interpreting the debtor's IVA. These include:

- Section 253(1) defines an IVA as 'a proposal to [the debtor's] creditors for a composition in satisfaction of his debts or a scheme of arrangement of his affairs', and
- Section 382 defines 'bankruptcy debt' as 'any debt or liability to which the bankrupt is subject at the commencement of the bankruptcy or any debt or liability to which may become subject after the commencement by reason of any obligation incurred before the commencement'.

What do the Insolvency Rules 1986 prescribe about the procedure?

Part 5 of the Insolvency Rules 1986 ('IR') make these provisions on IVA procedure:

- **Rule 5.23(2)** provides that a proposal or a modification is approved if a majority of three quarters or more (in value) of those present and voting in person or by proxy have voted in favour of it,
- **Rule 5.34(1)** requires the supervisor, within 28 days after the final completion or termination of the IVA, to send to all creditors who are bound by it, and to the debtor, 'a notice that the arrangement has been fully implemented or (as the case may be) terminated', and
- **Rule 5.34(2)** provides that termination of the IVA occurs where the IVA has not been implemented in accordance with the proposal as approved by the creditors.

What happened in the case in the County Court before the deputy district judge?

On receipt of the £24,500 PPI payments, the IVA supervisor applied on 25 July 2014 to the County Court nearest to where the debtor resided, Burnley, for directions as to whether the PPI sums paid by the 2 banks to him were subject to the trust constituted by the debtor's IVA or not. Deputy District Judge Langley determined on 10 October 2014 that these PPI windfall payments were not subject to the IVA trust and could instead be released and paid to the debtor.

What happened on the first appeal in the Manchester High Court?

The IVA supervisor appealed the order made by Burnley County Court. His appeal was heard by HHJ Hodge QC in the Manchester High Court on 9 February 2015. In a 16 page ex tempore judgment, Judge Hodge dismissed the supervisor's first appeal - **[2015] EWHC 993 (Ch)**.

Whilst Judge Hodge noted that the 'case arises in somewhat unusual circumstances and appears to raise a novel question of law', he ruled that in his judgment 'creditors are no long to be treated as creditors for the purposes of the arrangement. They are no longer persons in whose favour a dividend can be declared, pursuant to the powers conferred by paragraph 49(1)'. He went on to say that 'once the arrangement has been satisfactorily concluded by the issue by the supervisor of a completion certificate, the debtor, it seems to me, is released from all debts subject to the arrangement. In my judgment, that release applies for all purposes of the arrangement and brings an end to the trusts affecting the arrangement assets.' His conclusion was that 'completion of the arrangement means what it says: that the arrangement has come to an end.'

What grounds of appeal did the Supervisor advance?

The Supervisor applied to the Court of Appeal for permission to bring a 2nd appeal on the basis that this case raised an important point of principle or practice. Lord Justice Lewison granted permission on the papers on 24 April 2015. At the hearing the supervisor advanced these 2 grounds of appeal:

- All the debtor's assets as at the date of commencement of the IVA (except his car and interest in his matrimonial home) were to be held on trust for the purposes of the IVA. This is the combined effect of paragraphs 26 and 28 of the IVA Conditions.
- The debtor was to make monthly contributions from his income for a period of 5 years at a rate specified in the IVA with provision for their variation in certain circumstances. A failure to pay to non-preferential creditors a minimum of 33 pence in the £ would constitute a default.

What arguments did the debtor make?

The debtor submitted that the 2 judges in the 2 courts below came to the correct result for the reasons that they gave. No respondent's notice was issued seeking to affirm the decision below on other grounds. The debtor submitted that properly construed the definition of 'Creditor' when read with the release in paragraph 9(2) meant that upon the issue of a certificate of completion, there ceased to be any beneficiaries of the trust and therefore necessarily the trust came to an end.

What had the Court of Appeal previously ruled in *NT Gallagher*?

The Court of Appeal had considered a broadly similar situation in relation to a corporate insolvency in which a company had entered into a company voluntary arrangement ('CVA') and then had entered into liquidation. The court had to consider what to do with a windfall payment there and whether it was to be paid to the CVA creditors in accordance with the terms of the CVA or whether it had to be paid to the liquidator to distribute *pari passu* to all the creditors.

In *Re N T Gallagher & Son Ltd* **[2002] EWCA Civ 404, [2002] 1 WLR 2380**, Lord Justice Peter Gibson gave the judgement of the court to which Ward and Dyson LJ agreed. He ruled that although the CVA did not use the word 'trust' it was common ground that it created a trust of certain assets. He held that the trust did survive the liquidation and that therefore sums recovered after the commencement of the liquidation in proceedings to enforce a claim, which was under the terms of the CVA property subject to the trust, were held on the terms of the trust and did not form part of the assets available in the liquidation.

What do the insolvency textbooks say on this?

Muir Hunter on Personal Insolvency at paragraph 3-202 said the correction of the decision of Judge Hodge was 'questionable' on grounds that included that the judge gave 'too little consideration to the fact that the whole basis of the IVA was that the debtor contracted to give assets belonging to him at the date of the IVA (therefore including potential PPI claims) to creditors in consideration for the release of his debts'.

What ruling did the Court of Appeal give?

The Court of Appeal allowed the IVA supervisor's appeal.

David Richards LJ started by considering the '*evident underlying purpose of the IVA*' which comprised a 'a moratorium on the enforcement by creditors of their claims' and in return the debtor was '*able to retain his matrimonial home and car*' with him also ageing to '*make available to the creditors all the other property that would have fallen into his bankruptcy estate on a bankruptcy commencing on the same date as the IVA and to make contributions from income over a period of 5 years*'. As to the PPI mis-selling claims, David Richards LR ruled that although these were '*unknown to the supervisor and creditors and maybe also to the debtor*' that nevertheless they were '*capable of being made at that date and were therefore in principle available to creditors*'. He noted that if the debtor had become bankrupt '*they would have remained part of his bankruptcy estate until realised and distributed among creditors or until disposed of by the trustee in bankruptcy*'.

As to *Gallagher*, David Richards LJ said that '*unlike the judge, I do derive assistance from the Court of Appeal's judgment in Gallagher*' and that '*if a fully constituted trust is to terminate, there need to be provisions requiring it to do so and specifying what is to happen to the trust assets*'. On examining the terms of the IVA, David Richards LJ ruled that creditors were '*fixed by reference to whether there was a debt or liability, or other obligation, owed to them as at the commencement of the IVA in October 2007*' and that whilst '*any established claim in respect of such debts... remains unpaid*' that the IVA supervisor not only remained a creditor but he could also '*remain a beneficiary of a trust for Creditors*'.

David Richards LJ then went on to consider whether it made any difference if the IVA had been terminated because the debtor did not keep up his payments or the position here where the IVA had completed. He ruled that the '*release of a debtor from a debt is not necessarily the same as the extinction or discharge of the debt, particularly in a bankruptcy context*'. He noted that '*once a certificate of completion is issued, the debtor is released from the debts and he ceases to be under any liability in respect of them*'. He ruled that the position '*is directly analogous to the position in a bankruptcy, and deliberately so, given that an IVA is an alternative to bankruptcy*'. Going on he said that '*completion of the IVA means that the debtor has fully performed all his obligations under the IVA and the minimum distribution has been made to creditors*' but that it did '*not mean that the trusts had come to an end*'.

The appeal judge ruled that there was '*no good reason why*' the trusts should come to an end. He said '*in view of the purpose of the IVA being in part to apply the debtor's property as at the commencement of the IVA (other than his home and car) in or towards payment of the Debts, there is every reason why they should not come to an end on issue of the certificate of completion*'. Finally he ruled that as with *NT Gallagher* that the '*difficulty facing the debtor is to show why a fully constituted trust created by the IVA should come to an end in these circumstances*'. On this David Richards LJ was clear concluding that in his view '*there being no express provision to that effect, the debtor has failed to show any reason*'.

What about the Guidance Note on PPI Mis-selling Claims?

A Guidance Note on PPI Mis-selling Claims was issued in April 2013 (revised February 2014) by the principal professional bodies involved in insolvency - R3, the Insolvency Practitioners Association, the Law Society and the Institutes of Chartered Accountants.

However the Court of Appeal said they had '*not found it of assistance*' because it did '*not directly address the issue in this case*'.

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