

Guidance Note on Payment Protection Insurance Mis-Selling Claims in Trust Deeds & Sequestrations

1. Background

- 1.1 Payment protection insurance ('PPI') is intended to cover a borrower's unexpected loss of income as a result of redundancy, accident, illness or some other specified event, and a consequent inability to pay loan, mortgage, credit card or other credit repayments. It was sold by many financial institutions as part of a lending package or a credit card arrangement. It transpires that many of these policies were mis-sold.

The Financial Conduct Authority explains in its guidance to consumers 'How to claim for mis-sold PPI' that the mis-selling arose for a range of reasons including:

- the debtor had been pressured into taking out PPI;
- it had not been made clear that PPI was optional;
- the debtor had been advised to take out PPI but it was not suitable
- the policy had been added to the debtor's loan without his knowledge;

- 1.2 The purpose of this note is to provide guidance to office holders who are dealing with Trust Deeds or sequestration cases about the issues that may arise where the debtor may have been mis-sold PPI.

- 1.3 This guidance does not constitute legal advice nor does it seek to instruct or direct IPs in the administration of their insolvency cases. The bodies issuing this guide do not accept any liability in respect of actions that IPs may take in accordance with it, as it must be for each IP to be satisfied that his conduct meets the legal and professional requirements placed upon office-holders. Notwithstanding the above, IPs should have regard to the regulatory as well as legal consequences of their actions.

- 1.4 This guidance is issued jointly by:

Insolvency Practitioners Association
The Institute of Chartered Accountants in England & Wales
The Association of Chartered Certified Accountants
The Institute of Chartered Accountants of Scotland
Chartered Accountants Ireland
Solicitors' Regulatory Authority
Association of Business Recovery Professionals (R3)
Debt Resolution Forum

2. Asset at Commencement of Insolvency or a windfall?

Sequestration

- 2.1 Where a PPI policy has been sold to a debtor prior to the date of the sequestration the mis-selling claim vests in the trustee in sequestration because the mis-selling took place prior to sequestration. Discharge of the debtor makes no difference.

Trust Deeds

- 2.2 In broad terms the Trust Deed document will normally provide that assets that would have vested in a sequestration are conveyed to the Trustee for the benefit of the creditors. It follows therefore that the provisions of 2.1 above apply.
- 2.3 The Trustee must be guided by the specific terms of the Trust Deed. If there is any doubt about their effect the Trustee should take legal advice.

Sequestration and Trust Deeds

- 2.4 In the rare event that the mis-selling took place after the commencement of the sequestration or after the Trust Deed was signed but before discharge of the debtor and a payment under the claim is made to the debtor, it is likely that the payment would be classed as acquirenda.

3 Set-Off

- 3.1 In some cases the lenders who agree to pay compensation seek to apply set-off. Where this happens it is for the office holder to take such steps as he or she deems appropriate to ascertain whether set-off should apply.
- 3.2 Set off can be a complex area of law. The application of set off in Scotland is wider in insolvency than in a solvent situation and depends, amongst other things, upon:
- i. the nature of both the original debt and the mis-sold PPI proceeds - debts which are set off do not have to be of the same nature. A claim for money may be set off against, for example, a claim for delivery of goods; and
 - ii. the identity of the parties (which may be complicated where the mis-sold PPI product and the loan/advance have been provided by different companies within or without the lenders' group structures (particularly given the prevalence of insolvency debt sales resulting in the identity of the owner of the debt having changed from that of the PPI mis-selling party)) but note that the debtor and creditor must be in the same capacity.
- 3.3 Set off does not apply automatically in Scotland and needs to be pled. Office holders should not assume that either any rights of set off exist or, if they do, that they will be relied upon. They should also wait for the right to be specifically pled by the creditor. If set off has not been pled, there is no automatic right of set off and no obligation on the office holder to investigate whether a creditor may be entitled to set off.
- 3.4 It is possible for a party by agreement to exclude his right of set off unless that agreement is structured in such a way as to create a preference over the general body of creditors.
- 3.5 Where set-off is applicable the office holder should consider the effect on creditor claim values and upon past and future distributions taking account of the sums involved and of the costs of any corrective action. Where there is certainty about the amounts to be set-off, the office holder should adjudicate on creditor claims accordingly.
- 3.6 Wherever possible, dividends to other creditors should not be withheld pending determination of set-off issues, unless there are reasonable grounds for doing so.
- 3.7 As highlighted above, set-off can be a complex area of law. Office holders should consider seeking legal advice regarding set off.

4 Power and Obligation to make PPI mis-selling claims - Open Cases

- 4.1 An office holder has a duty to realise the assets of an estate to which he has been appointed. This duty is tempered by:
- i. the extent to which the costs of realisation absorb the proceeds;
and
 - ii. the availability of funds to pursue a claim. Office holders should be aware however, that some claims companies are prepared to operate on a “no win no fees” basis. Practitioners should be aware that a “win” for this purpose might constitute a settlement resulting in a set off and reduction in the creditor’s claim, thus there is no cash realisation.
- 4.2 An office holder has no obligation to pursue a PPI mis-selling claim if he can demonstrate that there would be little or no benefit to the estate after accounting for costs including those incurred by the debtor. The office holder should document his deliberations and hold these on file. However, he does have an obligation to consider whether or not any potential claims exist. Office holders are reminded that costs properly incurred by the debtor (with the approval of the office holder) in connection with a PPI mis-selling claim which result in a realisation to the estate should be reimbursed by or subject to an indemnity from the estate.
- 4.3 Office holders have a duty to progress PPI cases as quickly as possible. However, sequestration cases may be kept open beyond the discharge of the debtor in order to allow the office holder to finalise PPI issues provided it is cost effective to do so and an assessment of the claim and likelihood of success has been carried out.

A Trust Deed survives the discharge of the debtor. It follows that where the debtor has provided all the information necessary to pursue a PPI mis-selling claim, where the office holder is satisfied that due provision has been made for his fees (see 4.4) and it has been arranged with the financial institution involved that any proceeds of a claim should be paid to the Trustee or the Trustee has secured payment in some other way (e.g. by taking an assignation of the claim), there is no need to delay the debtor’s discharge.

- 4.4 Where a debtor receives payment direct from the financial organisation (whether the debtor has disclosed to the office holder the existence of mis-selling or not), the financial organisation may have an obligation to compensate the insolvent estate if it can be demonstrated the financial organisation made the payment to the debtor in the knowledge of the debtor's insolvency.

5 Power and Obligation to make PPI mis-selling claims - Closed Cases

Sequestration

- 5.1 In a sequestration if all the known assets have been realised and if available funds have been distributed and the Trustee has received his discharge, he has no locus to act.
- 5.2 In the event an office holder becomes aware of funds which have vested in the office holder as trustee either at the date of sequestration or as acquirenda but which are not discovered until after the office holder has been discharged, the office holder may apply to the court to be re-appointed by a sheriff, to authorise them to act. In considering whether to apply for their reappointment, the office holder should first consider the anticipated cost of the application action and the administration costs for ingathering the funds against any anticipated benefit to the debtor's creditors. If the action is deemed not to be cost effective and would not result in a reasonable

reversion to the creditors, the office holder should not seek their reappointment and the funds will revert back to the debtor.

- 5.3 Unless the sequestration is revived a former Trustee does not have a duty to seek out PPI mis-selling claims in closed cases.

Trust Deeds

- 5.4 In a Trust Deed, if all the known assets have been realised, available funds have been distributed and the Trust has terminated, the Trustee will have no locus to act.

- 5.5 Once a Trust has terminated, it cannot be revived.

6 Power and Obligation to make PPI mis-selling claims - New Cases

- 6.1 Office holders should consider whether PPI is a potential asset in the initial stages of their case administration. Debtors should be asked at an early stage about possible claims in connection with PPI mis-selling and appropriate enquiries should be made. A questionnaire suitable for completion by the debtor is available from the Financial Ombudsman Service¹.

- 6.2 Trustees should explain in the first communication to creditors how potential PPI mis-selling claims are to be dealt with.

7 Taxation

- 7.1 Compensation for mis-sold PPI usually but not necessarily, comprises a repayment of the premiums, contractual interest thereon, statutory interest and costs. Any statutory interest is subject to tax at the debtor's marginal rate applicable at the date of receipt of the compensation. This liability to tax is the debtor's but on the principle that the debtor should not be out of pocket, office holders should indemnify the debtor against such liability, if it has not already been deducted by the payer by retaining tax on interest at the basic rate before making any distribution to creditors. Office holders should notify the debtor of the amounts of interest received and of any tax paid by the financial institution directly to HM Revenue & Customs.

- 7.2 In most cases the marginal tax rate will not be known as it depends upon the debtor's overall taxable income in the relevant fiscal year. In order to make provision for the tax liability arising on the statutory interest it is an acceptable (though not required) practice that tax, if not already deducted, is deducted by the IP and paid to HM Revenue & Customs at the basic rate (currently 20%). The debtor should be notified of the payment and be asked to inform the Trustee, within a specified time period, if the debtor is a higher rate taxpayer. In the absence of a response from the debtor, the IP is entitled to assume that payment to HM Revenue & Customs at the basic rate is sufficient. Where deemed necessary by the office holder, a sum representing any additional higher rate tax may be held pending confirmation of the debtor's marginal rate for the relevant tax year.

- 7.3 It is understood that as a means of resolving the tax position HM Revenue & Customs is agreeable to office holders applying to: **Inspector of Taxes, Local Compliance – SME, Elgin House, Edinburgh Tel: 03000 561522** for a Unique Tax Reference (UTR) to be used for all their cases when paying any tax deducted in these circumstances. Payments should be accompanied by a schedule setting out the details of the taxpayers involved.

¹ http://financial-ombudsman.org.uk/publications/technical_notes/ppi.html

8 Office holders' Fees and Costs

- 8.1 In sequestration the Trustee's ability to charge fees and recover costs will be subject to the provisions of the Bankruptcy (Scotland) Act 1985 and SIP 9 (Scotland).
- 8.2 In Trust Deeds provision for the Trustee to charge fees and recover costs will be set out in the Trust Deed document. The Trustee must comply with the terms of the Trust Deed, with the provisions of SIP3A (Scotland) and with SIP9 (Scotland).
- 8.3 Where the basis of the office holders remuneration has been fixed as a percentage of realisations, these fees can only be charged on actual receipts into the estate from mis-selling claims, net of any deductions for set-off. Where a level of fee has been agreed at the outset and the Trustee subsequently becomes aware that there is a mis-selling claim to be pursued he may seek approval from the creditors of an additional fee. In such circumstances the Trustee will be subject to the normal fee approval procedures.
- 8.4 Office holders may only recover the cost of obtaining generic legal advice which meets the requirements of a Category 1 disbursement under SIP9. In particular the office holder should be able to clearly demonstrate that the legal advice has been sought with the intention of applying it to the case in question. If the requirements of SIP9 are not met then the cost of the advice should be absorbed by the office holder's firm.

9 Claims Companies

- 9.1 It is for the office holder to determine whether or not it is appropriate to instruct a claims company to pursue potential PPI mis-selling claims and he should be able to demonstrate that the costs are reasonable. Office holders should be aware that claims management companies may operate on a no win no fee basis and should consider utilizing this to minimize cost to the estate. Any reasonable cost arising should be paid out of the sum realised from the mis-selling claim and not be borne by the debtor. The cost should be treated as an expense of realisation.
- 9.2 Where a claims company is instructed it is important that the office holder is satisfied that the procedures adopted result in the debtor being treated in a fair and reasonable manner.
- 9.3 Where the debtor instructed the claims company, without the knowledge of the Trustee, payment of the costs involved will depend on the particular circumstances of the case and the contracts entered into.
- i. Where the debtor instructed the claims company prior to sequestration or prior to the signing of the Trust Deed, the claims company will generally have an unsecured claim in the estate.
 - ii. the debtor should not have instructed the claims company after the insolvency and the office holder is not bound to adopt any contract entered into by the debtor.
 - iii. The office holder may consider adopting a contract previously entered into by the debtor with a claims company if they believe that the cost is reasonable and value will be realised for the estate.
- 9.4 Where the office holder or his firm receives commission for the introduction of a debtor to a PPI mis-selling claims company this should be disclosed and treated as an asset of the estate in accordance with the Code of Ethics for Insolvency Practitioners.

10. **Prescription**

- 10.1 Office holders should be aware that claims may be subject to the effects of the Prescription and Limitation (Scotland) Act 1973. Prescription is a complex area of law and if office holders discover that prescription may be an issue it is recommended that they seek legal advice.

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