



RESIDENTIAL POSSESSION PROCEEDINGS AND TENANT INSOLVENCY

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1. In the current economic climate personal insolvency is common place. According to the official figures, the number of personal insolvencies has risen from about 8,000 per quarter in 2002, to a peak of about 35,000 per quarter at the beginning of 2010. The current trend is a gradual reduction, the second quarter of 2012 seeing 27,390 personal insolvencies. In the last 12 months there have been 115,407 personal insolvencies: 35,456 bankruptcy orders; 30,816 debt relief orders; and 49,135 individual voluntary arrangements.
2. This is not surprising: The Consultation Paper produced by the Department for Constitutional Affairs in July 2004 "*A Choice of Paths – Better option to manage over-indebtedness and multiple debt*" (CP23/04) estimated that in 2002 net lending rose by almost £10bn per month and that adults in this country owed about £18,000 each. The paper predicted that if, in the context of "the historically high levels of borrowing", there should be "an economic downturn ... a far greater number of people would be at risk of financial difficulties".
3. Naturally, a tenant who is insolvent, or approaching insolvency, may well not pay the rent and consequently tenant insolvency often triggers a claim for possession on the ground of rent arrears.

Personal insolvency

4. **Bankruptcy** is a court-based insolvency procedure governed by Part IX of the Insolvency Act 1986. The process is commenced by the filing and service of a petition. A petition may be presented by the debtor himself, an unsecured creditor, and in the event of non-compliance with the terms of an individual voluntary arrangement, the supervisor of the arrangement or one of the creditors bound by the arrangement.
5. The effect of the bankruptcy order is that any dispositions of the bankrupt's estate are void (section 284), and upon appointment of a trustee, the bankrupt's estate vests in the trustee by operation of law (section 306). In general terms the debts and liabilities of the bankrupt at the commencement of the bankruptcy are provable in the bankruptcy, and paid from the bankruptcy estates assets pro rata.
6. More specifically in relation to claims for possession, section 283(3A) excludes from the bankrupt's estate:
 - i) An assured tenancy or an assured agricultural occupancy under the Housing Act 1988, the terms of which prohibit an assignment;
 - ii) A protected tenancy under the Rent Act 1977 in respect of which no premium can be lawfully required as a condition of assignment;
 - iii) A tenancy of a dwelling-house by virtue of which the bankrupt is a protected occupier under the Rent (Agriculture) Act 1976 and the terms of which inhibit an assignment;
 - iv) A secure tenancy, within the meaning of the Housing Act 1985 which is not capable of being assigned other than as mentioned in section 91(3) of that Act.

In very general terms, most residential tenancies are regulated under the Housing Acts or Rent Acts and usually do prohibit assignment, and consequently many residential tenancies are excluded from the bankruptcy estate.

7. However, any such tenancy may form part of the bankrupt's estate if the trustee serves notice to that effect under section 308A of the Insolvency Act.



8. **Debt relief orders** are a creature of the Tribunals, Courts and Enforcement Act 2007, adding Part 7A and Schedule 4ZA into the Insolvency Act 1986. The DRO is part of a legislative programme of “debt-solution” procedures which include debt repayment plans, administration orders, and individual voluntary arrangements. In the words of Mummery LJ in *Secretary of State v Payne* [2010] EWCA Civ 1431:

“15. The scheme, structure and purpose of DROs broadly reflect the regime of bankruptcy orders: the effect of the order is to stay enforcement of the debts by creditors and the debts are discharged after a specified period (one year in the case of a DRO). While the order is in force the debtor is subject to similar restrictions and obligations as in bankruptcy. The main differences are that the DRO process does not require the intervention of the court and it is accessible to people who do not have the financial means to pay the higher fee for access to the bankruptcy procedure, i.e. debtors who cannot afford to make themselves bankrupt. It is less elaborate, being initiated administratively by the Official Receiver on the application of the individual debtor via a debt adviser who is an “approved intermediary” and upon the basis of specified criteria as to assets, income and liabilities. Unlike bankruptcy there is no trustee in whom the assets of the assets of the debtor are vested for distributions to creditors. DROs are thus meant for those overburdened with debt who have relatively low levels of liabilities, no assets in excess of £300 in value and no monthly surplus income over £50 with which to come to an arrangement with creditors. The applicant must not have been the subject of a DRO within the previous six years...”

9. In more detail:

- i) An individual who is unable to pay his debts may apply for a DRO in respect of a qualifying debt (section 251A(1)) which is unsecured and for a liquidated sum. The application is made electronically;
- ii) The application is made to the Official Receiver through an approved intermediary, and must set out the assets, liabilities, income etc of the debtor (section 251B). The debts must not exceed £15,000, and the debtor’s monthly surplus must not exceed £50, and the debtor must not have property in excess of £300 (schedule 4ZA);
- iii) The Official Receiver may grant the DRO if the application is in order, may exercise a discretion to refuse to grant a DRO if the application contains errors or misrepresentations, and must refuse the application in prescribed circumstances (e.g. debtor able to pay debts, debt not a qualifying debt, not resident in UK, not subject to other insolvency process) (section 251C & Schedule 4ZA);
- iv) If a DRO is made, it is entered in a register, and the DRO itself lists on its face the debts in respect of which it was made (section 251E). A creditor listed in the DRO may object (section 251K & 251M);

10. **Individual voluntary arrangements** are, in effect, a debt repayment plan between a debtor and the majority of his creditors which is given statutory force and protection under Part VIII of the Insolvency Act.

11. Upon a proposal being approved by a meeting of creditors, the approved arrangement takes effect as if made by the debtor at the meeting, and binds every person who in accordance with the rules was entitled to vote at the meeting or would have been so entitled if he had notice of it, as if he were party to the arrangement (section 260).

Moratorium on legal proceedings

12. **Bankruptcy** Section 285 provides for a moratorium on legal proceedings whilst a bankruptcy petition is pending and after a bankruptcy order has been made:

“285(1) At any time when proceedings on a bankruptcy petition are pending or an individual has been adjudged bankrupt the court may stay any action, execution or other legal process against the property or person of the debtor or, as the case may be, of the bankrupt.



285(2) Any court in which proceedings are pending against any individual may, on proof that a bankruptcy petition has been presented in respect of that individual or that he is an undischarged bankrupt, either stay the proceedings or allow them to continue on such terms as it thinks fit.

285(3) After the making of a bankruptcy order no person who is a creditor of the bankrupt in respect of a debt provable in the bankruptcy shall:

- (a) have any remedies against the property or person of the bankrupt in respect of the debt, or
- (b) before the discharge of the bankrupt, commence any action or other legal proceedings against the bankrupt except with the leave of the court and on such terms as the court may impose. This is subject to sections 346 (enforcement procedures) and 347 (limited right to distress).

285(4) Subject as follows, subsection (3) does not affect the right of a secured creditor of the bankrupt to enforce his security.”

13. **Debt relief orders** Section 251G provides:

“251G(1) A moratorium commences on the effective date for a debt relief order in relation to each qualifying debt specified in the order (“a specified qualifying debt”).

251G(2) During the moratorium, the creditor to whom a specified qualifying debt is owed:

- (a) has no remedy in respect of the debt, and
- (b) may not:
 - (i) commenced a creditor’s petition in respect of the debt, or
 - (ii) otherwise commence any action or other legal proceedings against the debtor for the debt, except with the permission of the court and on such terms as the court may impose

251G(3) If on the effective date a creditor to whom a specified qualifying debt is owed has any such petition, action or other proceedings as mentioned in subsection (2)(b) pending in any court, the court may:

- (a) stay the proceedings on the petition, action or other proceedings (as the case may be), or
- (b) allow them to continue on such terms as the court thinks fit.

251G(4) In subsection (2)(a) and (b) references to the debt include a reference to any interest, penalty or other sum that becomes payable in relation to that debt after the application date.

251G(5) Nothing in this section affects the right of a secured creditor of the debtor to enforce his security.”

14. **Individual voluntary arrangement.** A debtor may apply to the court for an interim order protecting his position for a period of 14 days pending the making of a proposal. Under section 252(2):

“An interim order has the effect that, during the period for which it is in force:

- (a) no bankruptcy petition relating to the debtor may be presented or proceeded with,
 - (aa) no landlord or other person to whom rent is payable may exercise any right of forfeiture by peaceable re-entry in relation to premises let to the debtor in respect of the failure by the debtor to comply with any term or condition of his tenancy of such premises, except with the leave of the court, and



(b) no other proceedings, and no execution or other legal process, may be commenced or continued and no distress may be levied against the debtor or his property except with the leave of the court.”

Leave of the Court required to commence legal proceedings

15. Where the leave of the Court is required to commence legal proceedings (i.e. under section 285(3) (bankruptcy), section 251G(2) (debt relief orders), and section 252(2) (individual voluntary arrangements):
 - i) The relevant court is the court seized of the bankruptcy proceedings (not necessarily the court in which you want to issue your possession proceedings);
 - ii) It is probably the case that proceedings commenced without leave are not a nullity, and leave can be granted retrospectively (see *Bank of Scotland (t/a Birmingham Midshires) v Breytenbach* [2012] BPIR 1, following *Bristol & West Building Society v Saunders* [1997] BCC 83). However the point is not without some jurisprudential uncertainty (see for instance HHJ Kershaw in *Re Taylor* [2007] Ch 50, distinguished in *Brytenbach*), and furthermore it is not necessarily the case that the court would be sympathetic to a retrospective application.
16. Where the Court has power to stay or impose terms on existing proceedings (i.e. under section 285(2) (bankruptcy) & 251G(3)) (debt relief orders), the discretion is exercised by the court seized of those proceedings.

Application of the moratorium in residential possession proceedings

17. The issues have recently been reviewed by the Court of Appeal in *Sharples v Places for People Homes Limited* [2011] EWCA Civ 813 ([2012] 1 All ER 582, [2012] L&TR 9, [2012] 2 WLR 584).
18. In that case the Court of Appeal considered conjoined appeals by Miss Sharples and Mr Godfrey. Both Miss Sharples and Mr Godfrey were assured tenants:
 - i) Possession proceedings were brought against Miss Sharples for arrears of rent, on mandatory grounds. A bankruptcy order was made against her on 15 May 2009, and an outright possession order made against her on 19 May 2009; and
 - ii) Possession proceedings were brought against Mr Godfrey for arrears of rent, on discretionary grounds. A debt relief order was made on 27 April 2009, and on 12 August 2009 a possession order was made, conditionally suspended upon payment of the arrears by instalments plus the continuing rent, plus judgement for the arrears.
19. The arguments of the tenants were:
 - i) Possession proceedings are the means by which a landlord forces a tenant to pay rent arrears, and consequently if the tenant pays in order to avoid re-possession, the landlord gains an advantage over other creditors. If the tenant does not pay, and a possession order is made and executed, the tenant is obliged to give up the home which the legislature had intended to protect from the consequences of bankruptcy by virtue of section 283(3A) (above);
 - ii) Similarly, the primary purpose of a possession order suspended on terms as to payment of rent is to obtain the payment of arrears of rent; the suspended order is discharged if the arrears are paid. The whole purpose of a DRO would be undermined if a landlord were permitted to pursue a possession claim for arrears of rent, despite the arrears of rent being included in the DRO;



- iii) Referring to section 285(3) and/or 251G, where the ground for possession was arrears of rent, and those arrears are provable in the bankruptcy, then the order for possession is a remedy against the bankrupt's property "in respect of that debt";
 - iv) If arrears of rent are provable in the bankruptcy, they are not "lawfully due" under the provisions of grounds 8, 10 and 11 of the Housing Act 1988;
 - v) It was unreasonable to make a possession order in relation to arrears which the tenant would be discharged from pursuant to the bankruptcy/DRO regime; and
 - vi) That, pursuant to the Human Rights Act 1998, section 285(3) ought to be interpreted in a manner which gave effect to article 8 of the ECHR (right to respect for private and family life);
20. The Court of Appeal reviewed *Ezekiel v Orakpo* [1977] 1 QB 260, *Razzaq v Pala* [1997] 1 WLR 1336, *Harlow District Council v Hall* [2006] EWCA Civ 156 and concluded:
- i) The grant of a tenancy, including an assured tenancy, creates a proprietary interest in the tenant which is an incumbrance on the landlord's title. An order for possession is a remedy which restores to the landlord full proprietary rights, including rights of occupation (paragraph 63);
 - ii) Failure to pay rent is a breach of a contractual obligation. Neither forfeiture, nor a court order for possession, nor recovery of possession, nor an order for bankruptcy eliminates the personal indebtedness (paragraph 63);
 - iii) It therefore follows, as a matter of general principle, that an order for possession of property, whether let under an ordinary contractual tenancy, or a secure or assured tenancy, is not a remedy "in respect of" the debt represented by the rent arrears which gave rise to the entitlement to the order for possession (paragraph 63);
 - iv) The Court did not accept that the object of a claim for possession for arrears of rent and an order for possession made in those proceedings was to secure payment of the arrears (paragraph 65). The Court distinguished between motive (which may vary from case to case), and the object of a claim for possession (which was to restore the landlord to possession), and pointed out that a possession order was not a coercive procedure to achieve payment;
 - v) If the tenant chose to pay the arrears (from income), rather than face re-possession, that did not disadvantage other creditors who prove in the bankruptcy (paragraph 70). The tenant's income does not form part of the bankruptcy estate unless a notice is served by the trustee claiming it as after-acquired property (section 307), or an income payments order is made (section 310);
 - vi) Article 8 was engaged, but did not provide any basis to provide that bankrupt tenants should be placed in a more advantageous position than other tenants who owe arrears of rent (paragraph 72);
 - vii) However, where arrears will be discharged under a DRO/bankruptcy, it may be unreasonable to suspend a possession order upon repayment of those arrears (paragraphs 80 & 81), but it did not therefore follow that no possession order should be made (paragraph 82), but an order might be suspended upon payment of current rent (paragraph 83).
21. Lord Justice Etherton summarised (at paragraph 95):
- "(1) An order for possession of property subject to a tenancy, including an assured tenancy, on the ground of arrears of rent, which are provable in the bankruptcy of the tenant, is not a "remedy ... in respect of that debt" within IA s. 285(3)(a);*



(2) that is so, whether the order is an outright order for possession or is a conditional suspended possession order;

(3) IA s.285(3)(b) is implicitly limited to legal proceedings against the bankrupt "in respect of that debt"; that is to say, it is qualified in the same way as s.285(3)(a);

(4) accordingly, proceedings for an order for possession of property subject to a tenancy, including an assured tenancy, on the grounds of rent arrears, in which no claim is made for arrears provable in the tenant's bankruptcy, are not subject to the automatic stay in IA s.285(3)(b);

(5) an order for possession of property subject to a tenancy, including an assured tenancy, on the ground of arrears of rent, which are the subject of the tenant's DRO, is not a "remedy in respect of the debt" within IA s.251G(2)(a), whether the order is an outright order for possession or is a conditional suspended possession order;

(6) proceedings for possession of property subject to an assured tenancy on the ground of rent arrears, which are provable in the tenant's bankruptcy or are the subject of the tenant's DRO, should not normally be stayed under IA s.285(1) or (2) or IA s.251G(3);

(7) on the hearing of such proceedings, no order can be made for payment of such arrears; nor should a suspended order for possession be made conditional on payment of such arrears, but it should be made conditional on payment of any other arrears (i.e. those not provable in the bankruptcy or subject to the DRO) and current rent..."

22. So far as individual voluntary arrangements are concerned, under section 252(2) there is no equivalent to section 285(3)(a), and following the reasoning of the Court of Appeal in *Sharples* there does not appear to be any basis to imply any limitation to the plain meaning of the words. It appears therefore that it would not be possible to obtain a possession order within the 14 day IVA moratorium, except with the leave of the court.

Conclusion

23. It can be seen that in most cases the bankruptcy of a residential tenant should not inhibit the court from making a possession order in appropriate circumstances. However the terms of the order, and particularly the terms of any suspended order, will need careful consideration and it may prove impossible to recover arrears that have accrued prior to the date of the bankruptcy/DRO.

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