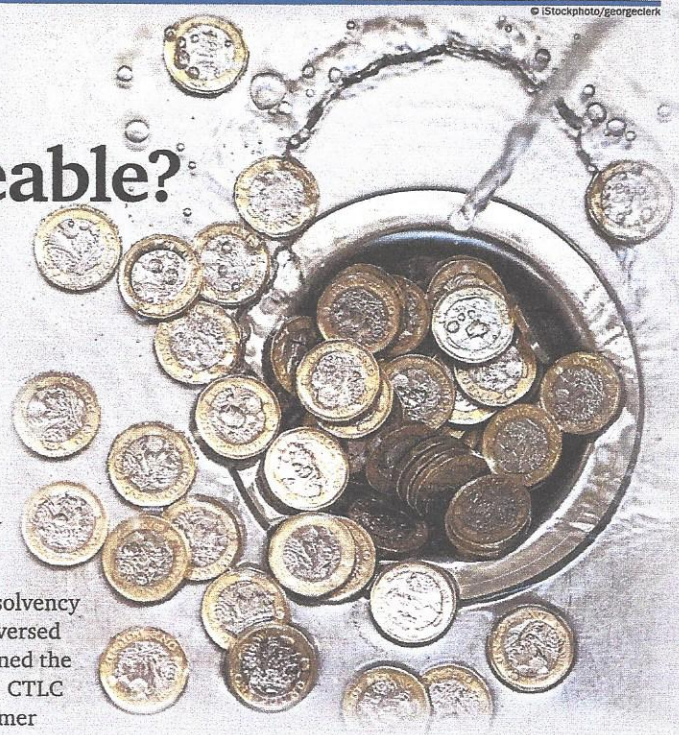
Is your settlement agreement unenforceable?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Robin Kingham provides an update on the status of Tomlin Order settlements in relation to consumer credit law

IN BRIEF

- *Gertner*—a long running case involving a guarantee, a strike-down of an IVA, and a bankruptcy petition—has had a major impact on consumer credit law.
- Litigators will need to consider this judgment carefully in order to ensure that any proposed settlement agreement does not inadvertently become subject to consumer credit regulation.

Significant consumer credit cases generally start as relatively small matters in the county court and gradually work their way up through the High Court to the Court of Appeal and, exceptionally, to the Supreme Court. The recent Court of Appeal decision in *CFL Finance Ltd v Laser Trust & Gertner* [2021] EWCA Civ 228, [2021] All ER (D) 115 (Feb) was very different.

Background

Mr Gertner was sued on a personal guarantee that he had given for a company loan. He defended the claim for the principal debt of £1.7m on the basis that the lender's director (ie who had granted the loan) had not been properly authorised by the lender. Mr Gertner also defended the claim for interest on a number of bases.

The claim was compromised and the settlement agreement included as a schedule to a Tomlin Order. Under the Tomlin Order, Mr Gertner was required to pay £2m over the course of approximately two years. Mr Gertner paid a significant portion of this but, nevertheless, defaulted on his payment obligations. CFL Finance Ltd then commenced bankruptcy proceedings against him.

After working its way up to the Court of Appeal on an insolvency issue (on which Mr Gertner was unsuccessful), the matter came before the Chief Insolvency and Companies Court Judge Briggs ([2019] CTLC 229). By then, consumer credit regulation had become an issue, with Mr Gertner alleging that the settlement agreement was in fact a regulated consumer credit agreement.

The main issue in the case had been been permitted to vote on the individual voluntary arrangement (IVA). Overturning the Chief Insolvency Judge, Marcus Smith J reversed that decision and overturned the bankruptcy order ([2020] CTLC 241). However, the consumer credit arguments were determined in favour of CFL by both Judge Briggs and Marcus Smith J.

CFL obtained permission to appeal to the Court of Appeal on the issue concerning the good faith of the potential voter in the IVA. While resisting that appeal, Mr Gertner also cross-appealed on the issue of consumer credit. CFL was ordered to give security for the costs of the appeal and, having failed to do so, the appeal was struck out. As a result, the case in the Court of Appeal proceeded on the sole ground relating to consumer credit regulation.

The crux of the case

Many litigators might be forgiven for failing to consider the possibility that their clients could be entering into regulated consumer credit agreements by settling litigation. The Court of Appeal's decision in *Gertner* clarifies that, in certain circumstances, that will nonetheless be the consequence. Since the necessary authorisations and formalities will not usually have been considered at the time of settlement, many settlements will be *prima facie* unenforceable by the 'creditor'.

As such, the all-important question in *Gertner* was whether the payment of settlement sums in instalments provided 'financial accommodation' within the meaning of section 9(1) of the Consumer Credit Act 1974 (CCA 1974). If so, the settlement agreement would amount to 'credit' and would fall within the scope of CCA 1974.

At first instance, Judge Briggs held that there was no credit because: (1) CCA 1974 did not apply to schedules to Tomlin Orders and, (2) in any event, the effect of the settlement was simply to reschedule Mr

In his judgment, Marcus Smith J overturned Judge Briggs' decision on the first point, explaining that he could 'see no reason why the fact that a contractual agreement is scheduled to a Tomlin Order would cause [CCA 1974] to cease to apply if it otherwise did apply'. However, he agreed with Judge Briggs that the settlement agreement did not provide credit, placing particular emphasis on the fact that any obligation under the original agreement (in this case, the guarantee) had been extinguished by and replaced with a fresh promise under the settlement agreement.

Whether CCA 1974 was conceptually capable of applying to the schedule to a Tomlin Order was not, technically, a question before the Court of Appeal. However, Newey LJ (with whom David Richards and Popplewell LJJ agreed) confirmed that CCA 1974 could apply to a schedule to a Tomlin Order in the same way that it would apply to any other contractual agreement.

On the question of whether this particular settlement agreement provided credit, Newey LJ reviewed the authorities and drew some threads together at para [45]:

CCA 1974 does not apply to an agreement where there is no consideration to allow a debtor more time to pay.

A debtor will not have provided consideration merely by giving up a defence which they recognise to lack even a fair chance of success.

CCA 1974 does not apply to an agreement where a debt is 'genuinely disputed' in its entirety on substantial grounds, provided that there is no question of the agreement defeating the application of CCA 1974 to the original claim (see *Holyoake v Candy* [2017]

In contrast, if a debtor does not dispute their indebtedness and the parties enter into an agreement pursuant to which, with consideration, the creditor accepts payments by instalments, there is a provision of 'credit' within CCA 1974.

The particular difficulty in this case was that while Mr Gertner had denied the entirety of his indebtedness, his defence lacked substance (at least insofar as the £1.7m principal was concerned).

The Court of Appeal concluded that, even where the original debt has been disputed, 'there must come a point at which the existence of a debt is sufficiently clear that an agreement providing for future payment will confer "credit" within the meaning of [CCA 1974]'. It was acknowledged that there was room for argument as to where the 'dividing line' is between a debt to which CCA 1974 could apply and a mere claim to which it could not. However, after offering two alternatives (a purely objective test and one which involved consideration of whether the debtor genuinely believed the defence to have merits), Newey LJ elected not to decide the point since it was not determinative of Mr Gertner's appeal. It was enough to say that Mr Gertner's purported debt to CFL was disputed on genuine and substantial grounds.

Consequences

In many situations, the consequences of this decision will be severe. For example, in most cases, the requirements of CCA 1974 as to documentation will not have been complied with and the creditor will require a court order under CCA 1974, s 127 in order to enforce the agreement. Further, it is likely that the creditor will have failed to provide statements and notices under CCA 1974, ss 77A and 86B. As a result, the agreement will be unenforceable until remedial action is taken; interest and charges accruing during the period of non-compliance will not be payable. Further, creditors who did not already hold the necessary permission from the Financial Conduct Authority (FCA) will require a validation order to enforce the settlement agreement.

However, it is important to consider the specific facts of each case carefully. For example, if the creditor is not acting 'in the course of business', the documentary requirements of CCA 1974 will not apply because the agreement will be classified as a 'non-commercial agreement' (CCA 1974, ss 74(1)(a) and 189(1)), and FCA authorisation will not be required because the creditor will not be acting 'by way of business' (section 22 of the Financial Services and Markets Act 2000). The unfair relationship provisions of CCA 1974, ss 140A-C will, however, still apply.

Summary

Determining whether CCA 1974 applies to any given settlement agreement is far from simple, not least because the Court of Appeal (one might say prudently) did not venture beyond the need to determine if the bankruptcy petition against Mr Gertner should be dismissed.

If there is a challenge to a settlement agreement under which the debtor provides consideration and the creditor provides time to pay a disputed debt, the real questions are:

- Which side of the 'dividing' line does a particular case fall between a genuine dispute or merely paying an effectively undisputed debt by instalments?
- If the settlement agreement is against a background of an effectively undisputed debt, what are the consequences on unenforceability and the unfair relationship regime? **NLJ**

Robin Kingham, barrister, Gough Square Chambers. Jonathan Kirk QC, Fred Philpott, and Lee Finch (all of Gough Square Chambers) acted for Mr Gertner (*www.goughsq.co.uk*).

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