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Gough Square Chambers' consumer credit column: March 2021

by Thomas Samuels, Gough Square Chambers

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Ruth Bala, Lee Finch, Sabrina Goodchild and Thomas Samuels are all specialist consumer credit counsel at Gough Square Chambers. On a regular basis, they will share their views with Practical Law Financial Services subscribers on topical developments or key issues relating to consumer credit.

In the March 2021 column, Thomas Samuels considers the recent decision in *CFL Finance Ltd v Gertner [2021] EWCA Civ 228*, which concerned whether Tomlin Orders are theoretically capable of extending "credit" within the meaning of the Consumer Credit Act 1974 (CCA).

Safe to settle?

Introduction

On 23 February 2021, the Court of Appeal handed down its long-awaited decision in *CFL Finance Ltd v Gertner [2021] EWCA Civ 228*. To the surprise of many, it not only confirmed Marcus Smith J's decision that Tomlin Orders are theoretically capable of extending "credit" within the meaning of the Consumer Credit Act 1974 (CCA), but concluded that the question gave rise to a genuine triable issue on the facts before it.

Understandably, the court's conclusions and analysis have caused some considerable interest amongst lawyers dealing with consumer credit issues on both sides. However, it is also of wider importance for all dispute lawyers engaged in negotiating and drafting Tomlin Orders to settle commercial litigation. The risk of inadvertently creating a credit agreement regulated by the CCA is now of real and understandable concern.

This column explains the rationale behind the decision and aims to provide a few helpful hints and tips for those considering its likely impact.

Background to the litigation

Mr Gertner had guaranteed a loan facility provided by CFL Finance Ltd (CFL) to a company with which he was involved, Laser Trust Ltd (Laser Trust). Following the company's default, CFL claimed against Mr Gertner for the £1.7 million alleged to be due and owing pursuant to the terms of the guarantee. Mr Gertner raised a number of defences to the claim under the guarantee. It was eventually settled by way of Tomlin Order, which provided for the debt under the guarantee to be repaid by Mr Gertner by way of instalments, with all capital and interest becoming payable on default. Having paid £1.5 million pursuant to the terms of the Tomlin Order, Mr Gertner then defaulted and the entire remaining amount of capital and interest became due.

Accordingly, CFL issued a bankruptcy petition against him. Mr Gertner argued before ICC Judge Briggs that the Tomlin Order was unenforceable as a regulated credit agreement pursuant to the provisions of the CCA. Judge Briggs rejected that argument and made the bankruptcy order sought by CFL.

On appeal (*[2020] EWHC 1241 (Ch)*), Marcus Smith J set aside the order on the ground that the proceedings should have been stayed to allow Mr Gertner's other creditors to consider a voluntary arrangement. In relation to the CCA point, Marcus Smith J considered that, although a Tomlin Order was theoretically an agreement capable of falling within the scope of the CCA, Mr Gertner's agreement clearly did not. He therefore dismissed the appeal.

Court of Appeal's analysis

CFL appealed against Marcus Smith J's decision and, at the same time, Mr Gertner cross-appealed on the CCA point. However, CFL's primary appeal was subsequently dismissed upon its failure to provide security for Laser Trusts' costs thereof, thereby leaving only Mr Gertner's cross-appeal to be determined.

As noted in the judgment, at [11], CFL did not participate or seek to make representations at the hearing. Accordingly, the court did not have the benefit of

contested argument (albeit it noted that arguments which might have been advanced by CFL were properly raised and addressed by Mr Gertner's counsel).

The court then considered the cross-appeal by reference to two questions:

- Did the CCA apply to the schedule to a Tomlin Order?
- Did the Tomlin Order in question provide Mr Gertner with credit?

On the first question, the court noted that it was well-established that the schedule to a Tomlin Order constituted a contractual agreement between the parties. While the order itself could be approved or rejected by the court, the terms in the schedule were not (at [26]).

It considered the difference of approach between Judge Briggs and Marcus Smith J. Judge Briggs has concluded that it was not, even in theory, possible for the schedule to a Tomlin Order to constitute a credit agreement under the CCA, largely on the basis of the "essential character" test set out by the Court of Appeal in *McMillan Williams v Range [2004] EWCA Civ 294*. In effect, because the purpose and function of the agreement was to settle a claim rather than to provide financial accommodation within the meaning of the CCA. However, Marcus Smith J differed in his approach, having concluded that there was no reason why the fact that an agreement was scheduled to a Tomlin Order should mean the CCA would not apply where it would otherwise.

The Court of Appeal preferred Marcus Smith J's analysis on the first issue. Without expressly rejecting the "essential character" test laid down in *McMillan Williams*, it noted that Mr Gertner's case was "very different" to that authority, where the issue had been whether the would-be debtor actually owed anything at all (at [30]).

In relation to the second issue, the court noted that Mr Gertner's position was that there had been "financial accommodation" within the meaning of section 9(1) of the CCA. The question was therefore whether a debt had been contractually deferred from time at which payment would otherwise have been earned, citing Sir Richard Scott V-C in *Dimond v Lovell [2002] 1 A.C. 284*.

The court noted that "credit" was clearly advanced in the case of refinancing, albeit it did not extend to mere forbearance (at [36]). Whether or not there was a contractually binding deferral depended upon the existence of consideration. On that point it was well-established that surrendering a "reasonable" legal claim or defence, believed to have a "fair chance of success", was capable of constituting binding consideration (at [37]). However, as per *McMillan Williams*, if it was not known at the time of the agreement whether or not the debtor would ultimately owe anything to the creditor, it could not be said that credit was being advanced (at [38]).

On the basis of those points, the court set out for broad propositions (at [45]):

- The CCA does not apply to agreements which are not supported by consideration.
- A debtor will not have provided consideration merely by giving up a defence which even he recognised lacked a fair chance of success.
- The CCA does not apply to an agreement by which the parties compromise genuinely disputed in its entirety on "substantial grounds" since, in those circumstances, it cannot be said whether the debtor in fact owed anything to the creditor before the claim was compromised.
- By contrast, if the debtor does not dispute that he owes money to the creditor and the two enter into a Tomlin Order, supported by consideration, for the debtor to pay in instalments, it is clear that the debtor will be provided with "credit" within the meaning of the CCA.

It was considered that, irrespective of the strength of Mr Gertner's defence to the original proceedings which led to the Tomlin Order, he had provided consideration for the compromise by agreeing to pay a £50,000 contribution to CFL's costs (at [46]). The court also considered if a creditor agreed to accept payment by instalments of a claim for immediate payment to which the debtor, in truth, had no defence, credit would be likely to be advanced (at [48]).

Ultimately, therefore, it concluded that "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 the CCA regardless of whether the debtor has denied that anything is due" (at [50]). However, in the absence of full adversarial argument on the issue, the court declined to reach any firm conclusion on where the dividing line falls between a debt (to which the CCA could apply) versus a mere claim (to which it would not) (at [51]-[52]).

Analysis

In some ways it is perhaps more important to understand what the Court of Appeal's decision does not mean. For example, it does not mean that all (or even most) Tomlin Orders will fall within the scope of the CCA as regulated credit agreements. Equally therefore, the fact that a particular party may have routinely entered into Tomlin Orders with individuals does not mean that they will be in the business of providing regulated credit and therefore in breach of the general prohibition under

section 19 of the Financial Services and Markets Act 2000 (FSMA).

Rather, the Court of Appeal's decision entails a more subtle analysis, which requires consideration of a number of factors applying comparatively well-established principles to schedules to Tomlin Orders. Primarily those factors relate to: (i) the existence of consideration, and (ii) whether the potential liability was sufficiently certain to justify a finding of deferral.

The complexity comes in the fact that those key factors are arguably in conflict with one another. Often, in order to establish consideration, a party must give up a claim or defence which is of some real value because it had a fair chance of success at trial. However, if the liability is to be sufficiently certain for there to have been a deferral, then it must be sufficient certainty about the basis of debt claimed. It is likely to be very difficult for litigators to take a realistic view on the risks because a view on the merits – on which the Court of Appeal's test largely relies – is just that: a matter of opinion on which different lawyers may reasonably disagree.

However, more problematic still are the issues of policy that flow from the decision. It would be concerning if a solicitor was reluctant to advise a client to settle on favourable terms as a result of nervousness about inadvertently entering into a consumer credit agreement without proper regulatory authorisation. To do so would result in an unenforceable credit agreement, which may produce a worse result for a client than having going to trial and losing.

Conclusion

Ultimately, however, litigators must seek to do their best with a difficult decision. Where settlement cannot be concluded by some other means, for example, a more straightforward consent order, that is likely to mean (at the very least) noting the risks presented by the decision but nonetheless advising that settlement is the best option.

All of the above said, as at the time of writing it is understood that CFL has sought permission to appeal further to the Supreme Court. As such, there remains the possibility that further clarity may yet be forthcoming.

Gough Square Chambers' consumer credit columns

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