SHERIFFDOM OF GLASGOW AND STRETHKELVIN AT GLASGOW

[2021] SC GLW 013

GLW-SQ237-19

JUDGMENT OF SHERIFF ALAYNE E SWANSON

in the sequestration of

MR GORDON DUFFIELD SMITH formerly residing at 4 Lockhart Court, Newton Mearns, Glasgow G77 5FT and now at Flat 5 Lilybank Terrace, Glasgow, G2 8RX

Applicant

APPLICATION IN TERMS OF SECTION 31(6) OF THE BANKRUPTCY (SCOTLAND) ACT 1985

against

THE ACCOUNTANT IN BANKRUPTCY, 1 Pennyburn Road, Kilwinning, KA13 6SA Trustee of the sequestrated assets of MR GORDON DUFFIELD SMITH residing at 4 Lockhart Court, Newton Mearns, Glasgow, G77 5FT conform to Award of Sequestration issued by the Accountant in Bankruptcy dated 12 October 2012

Respondent

Applicant: Jaap
Respondent: Lloyd

GLASGOW, JUNE 2020

The sheriff having resumed consideration of the cause upholds the respondent's fourth and fifth pleas in law and dismisses the application; awards the expenses of the application to the respondent and allows an account of said expenses to be given in and remits same, when lodged, to the auditor to tax and report thereon.

The Facts

[1] Parties are not in dispute about the relevant facts. The Applicant was sequestrated by the Accountant in Bankruptcy ("AIB") on 12 October 2012. The Applicant was discharged from sequestration by operation of law on 12 October 2013.

[2] On or about 2 October 2007 the Applicant received advice from a financial advisor to invest in a pension investment which turned out to be a poor investment. The Applicant suffered a considerable loss. The Applicant later made a complaint to the Financial Conduct Authority ("FCA") on or around 30 June 2017 that he had been mis-sold the investment. The FCA found in his favour and awarded compensation. Because the financial advisor was by then in liquidation the compensation was paid directly by the FCA under the Financial Services Compensation Scheme ("FSCS"). The compensation was paid to Wylie and Bissett the AIB's appointed agents and has been held by them pending resolution of this case in which the Applicant seeks an order in terms of section 31(6) of the Bankruptcy (Scotland) Act 1985 ("the 1985 Act") finding that the sum of compensation awarded to the Applicant does not vest in the Permanent Trustee.

Discussion

[3] Because of the Covid-19 restrictions the debate in this case proceeded by written submissions and I am grateful to both agents for the clarity with which their respective positions are set out in the submissions lodged. The written submissions are available in process and for that reason I have given here only a brief summary of the arguments.

[4] The question comes down to an analysis of when the obligation to pay compensation came into existence.

[5] Mr Jaap argued that the compensation did not vest in the Respondent at the date of sequestration. Section 31(6) of the1985 Act allows any person claiming an interest to any estate claimed by the permanent trustee to apply to the court for the estate to be excluded from such vesting. His argument relies on the submission that the Applicant had no right to compensation at the date of the sequestration. He submits that at the date of sequestration there was no obligation on the FSCS to pay the compensation; the obligation on FSCS to pay the compensation arose for the first time on or around 30 June 2017 which was the date on which FSCS notified the Applicant that they had concluded their investigations and found in his favour. Mr Jaap does not characterise the obligation as being a contingent one.

[6] On the other hand on behalf of the Accountant in Bankruptcy ("AIB") Mr Lloyd submits that as at the date of sequestration the right to compensation was a contingent one; firstly upon a claim being made and secondly upon an adjudication in favour of the Applicant. The Applicant's submission of a claim purified the first contingency and the FSCS decision in the Applicant's favour purified the second contingency.

[7] Before turning to the question as to whether the right to compensation was a contingent right as at the date of sequestration the first point to make is that it is clear that neither the discharge of the debtor nor the discharge of the trustee ends the sequestration process unless there is a discharge on composition or the creditors are paid in full.[1]

[8] In the case of *Alison Donnelly* v *Royal Bank of Scotland plc* (GLA-CA115-14 11 February 2016) Sheriff Reid explains clearly the way in which the debtor's estate is ring-fenced. If

[1] Donnelly v RBS paragraph 53; AIB v Stephen [2017] SAC (Civ) 4.

following the discharge of a debtor an asset is discovered which properly forms part of the insolvent estate because that estate remains ring-fenced and preserved for the purpose of being distributed among the unsatisfied creditors the debtor's trustee is entitled to ingather that asset for distribution to the unsatisfied creditors. The question in that case, as here, was whether the liability originated pre-insolvency. If it did then there is no barrier to treating the compensation as an asset in the insolvent estate regardless of the discharge.

[9] What is the nature of a contingent obligation? Obligations may be pure, future or contingent. An obligation is pure when, as in the case of debt instantly payable, fulfilment is due at once. A future obligation will become exigible either on a fixed date or on the occurrence of some event (like death) which is certain to happen; the debt exists but cannot be enforced until the day of payment arrives. An obligation is contingent when it is subject to a suspensive or resolutive condition. There is a suspensive condition when the obligation will arise only on the occurrence of an event which might or might not happen or at some period (for example the attainment by the creditor of a certain age) which may never arise. A resolutive condition is where an obligation is at once exigible but will cease to be exigible on the occurrence of a certain event.[2]

[10] As Lord Drummond Young recognised in the case of *Liquidator of Ben Line Steamers Ltd*, *Noter* 2011 SLT 535 obligations can find their source or origin in a binding regulatory statutory scheme that was in existence prior to insolvency. The contingent obligation must "originate in a contract (or other source such as statue) that was in existence at the date of the insolvency".[3]

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[2] Gloag and Henderson: The Law of Scotland 14th Edition paragraph 3.12.
[3] Ben Line Steamers paragraph 23.

[11] The Financial Services and Markets Act 2000 makes provision about the regulation of financial services and markets including the creation of the Financial Conduct Authority ("FCA") to oversee authorised persons carrying on regulated activities. Authorised persons are subject to multiple obligations including the obligation to comply with adjudications by the Financial Ombudsman Service. Consumers are defined inter alia as persons who have used regulated financial services including investment in financial instruments who have relevant rights or interests in relation to any of those services or financial instruments. That is defined as a right or interest derived from or directly attributable to the services. A claim in relation to a mis-sold investment must fall within that category. The authorised person is obliged by the FCA to give investment advice which is suitable for the client and, in particular, in accordance with the client's risk tolerance and ability to bear losses.[4] The question to be answered here is at what point the Applicant had a relevant right or interest in the services provided in 2007.

[12] In the case of *Ben Line Steamers Ltd* Lord Drummond Young observes that the concept of a contingent obligation in Scots law was in its essence relatively simple; it was an obligation where enforceability was dependent on the occurrence of a future event that might or might not occur. In his view the obligation is existing the moment it is entered into but its enforceability is dependent on the existence of the uncertain event. In other words a contingent obligation involves an existing legal relationship even if the outcome of that relationship is not clear. The critical point is that some sort of obligation normally either contractual or statutory is required before there can be said to be a contingent obligation. The contingency may arise from the existence of a liability to the exercise of a power by

[4] Rule 9A 2 of the FCA's Conduct of Business Sourcebook.

another person such as a determination whether the obligation is or is not due or to determine its amount. The existence of the power creates correlative liability in the debtor. It is immaterial that the power involved is a double power in the sense that the creditor can exercise one power to enable itself to exercise a second power.

[13] From that definition it is clear that the obligation to recompense a consumer for a mis-sold investment comes into existence when the authorised person becomes subject to the statutory scheme imposed by the 2000 Act in relation to services provided to the consumer. The contingencies are two fold. Here the obligation was contingent firstly on the occurrence of the making of a consumer complaint and secondly on the adjudication of the complaint in favour of the consumer but the authorised person and the consumer had already committed to the statutory regulatory scheme as a the date of insolvency. In that event the debtor's right to enforce the obligation (albeit only through the regulatory scheme) constitutes an asset that forms part of the insolvent estate.[5] The contingencies are purified by submission of a complaint and the decision to uphold it and make redress.

[14] Neither the time it takes to purify nor the likelihood of the contingency occurring are relevant. In the *Ben Line Steamers* case the contingency was not purified for six years. The important point is that the debtor has committed and subjected itself to the necessary relationship or scheme thereby exposing itself to the exercise of that power and the resulting contingent liability. Lord Neuberger expresses it thus in the case of *Re Nortel GmbH*[6]:

> "I would suggest that, at least, normally, in order for a company to have incurred a relevant 'obligation' — it must have taken, or been subject to, some step or combination of steps which (a) had some legal effect (such as putting it under some legal relationship) and which (b) resulted in it being vulnerable to the specific liability in question—"

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[5] Donnelly v RBS paragraph 89.
[6] [2014] AC 209.

[15] When dealing with contingent obligations a distinction can be drawn between the time when the obligation comes into existence and the time when it becomes enforceable (or exigible to use Professor Gloag's wording). The contracts with which Sheriff Reid was dealing were inter alia contracts of loan and he envisaged that the obligation of payment might be contingent upon a valid demand for payment having been issued. On issue of the demand the obligation became enforceable but it was in existence prior to that. He concludes that an obligation is treated as being in existence from the moment it is entered into albeit its enforceability may be contingent upon the occurrence of another event.[7] The other way of expressing that is that the obligation comes into existence when the debtor has committed himself to it. By providing the regulated services as an authorised person the financial adviser had no choice but to commit himself to the statutory regime.

[16] To use Sheriff Reid's words: the fundamental issue is the authorised person's liability to pay compensation for alleged mis-selling finds its source or origin in the duties incumbent upon it under a statutory scheme that was in existence and to which the authorised person was bound prior to the date of the debtor's insolvency.

Decision

[17] For these reasons I find that the obligation to pay compensation was a contingent obligation in existence at the date of sequestration. Being therefore part of the debtor's insolvent estate in terms of section 31 of the 1985 Act it vested in the trustee as at the date of sequestration. I shall uphold the respondent's third, fourth and fifth pleas and dismiss the

[7] Donnelly v RBS paragraph 92.

application. The written submissions did not deal with the question of expenses but as the respondent has been wholly successful it is appropriate to award the expenses to her and allow an account to be lodged.