citizens advice bureau

CAB evidence briefing June 2009

Out of order

CAB evidence on the use of charging orders and orders for sale in debt collection

Introduction and summary

Citizens Advice is concerned about the growing use of charging orders by creditors. A charging order is a way of enforcing a previously unsecured debt by securing it against the debtor's property. A creditor with a charging order can then apply to the court for an order for sale to recover the debt by forcing the sale of the property.

Since 2000 there has been a staggering 722 per cent increase in the number of charging order applications by unsecured creditors. Around 74 per cent of the 132,000 applications in 2007 resulted in charging orders being made.[1]

But CAB evidence shows that some creditors are using the threat of court action followed by a charging order to intimidate people in financial difficulties to pay more than they can reasonably afford. The growing ease with which creditors are obtaining charging orders is undermining good debt collection practices. It rewards lenders who will not accept reasonable repayment offers from people in financial difficulties who are doing everything they can to deal with their debt problems.

Moreover, bureaux are now reporting that creditors are asking the court to enforce charging orders by an order for sale. Although the instances of people losing their homes because of previously unsecured debts are rare, we are concerned that creditors are attempting to test the existing weak legal protections for debtors.

Fortunately, the Government will not now be going ahead with reforms that would make charging orders easier for creditors to get. But this also means that there will also be no review of the current safeguards for debtors. The experience of CAB debt clients suggests that the Government needs to set new and fairer enforcement thresholds that creditors must prove before taking enforcement action through the courts. Citizens Advice believes that this should be based on the principle that people in debt who are doing their best to repay their debts should be protected from further debt collection or enforcement action.

1 Ministry of Justice, *Judicial Statistics, 2007.*

Inside

An introduction to charging orders and orders for sale

A charging order is a means of enforcement. It secures a previously unsecured debt against an asset owned by the debtor. Usually charging orders are secured against the debtor's home. This does not work in quite the same way as a mortgage as the charging order does not give the creditor an immediate right to take possession of the debtor's home. Creditors, however, can ask the court to enforce the charging order with an order for sale, which would force the debtor to sell their house in order to pay the creditor off.

Charging orders can only be granted in respect of judgment debts, where a court has already held that a debt is legally owed and payment is due. Section 1 of the Charging Orders Act 1979 makes it clear that a charging order is a way for creditors to enforce a court judgment where a debtor fails to make payment when ordered by the court or falls behind with instalments. Indeed Section 1 has been interpreted as meaning that where a court has allowed a debtor to a judgment debt pay by instalments a charging order can only be made where the debtor has fallen behind with those instalments.[2]

In 2003, the then Lord Chancellor's Department, (now Ministry of Justice) published the *Effective Enforcement* White Paper, setting out proposed reforms of enforcement law. The proposals included changes to legislation governing enforcement of judgment debts by charging orders and orders for sale. One of the proposals was to allow creditors to obtain a charging order even though the debtor was repaying the debt by instalments. The other was to establish a provision for secondary legislation to introduce safeguards for debtors on both charging orders and orders for sale. The White Paper expressed a view that they would probably not need to use this provision.

The Government believed that these changes were needed because the current law allowed debtors with large judgment debts to pay off their debts in very small instalments, but it did not provide the lender with the security that the whole debt could be paid off if the property was sold. They refuted arguments made by the debt advice sector, including Citizens Advice, that improving access to charging orders by creditors could allow them to effectively secure unsecured debts.

These proposals were duly enacted as Sections 93 and 94 of the Tribunals, Courts and Enforcement Act (TCE) 2007. On 17 March 2009, Bridget Prentice MP, the Parliamentary Under-Secretary of State at the Ministry of Justice (MoJ), announced in a written Ministerial Statement that the Government would not be implementing Part 4 of the Tribunals, Courts and Enforcement Act 2007, including sections 93 and 94. The decision not to proceed with implementing section 93 was welcome, but the opposite was true for section 94.[3]

Are charging orders too easy to get?

CAB evidence shows how borrowers who have responded to a county court money claim by admitting the debt and asking for time to pay find instead that the court have granted the creditor a forthwith judgment (that is, immediate payment of the debt in full). This allows the creditor to apply for enforcement immediately and thus bypasses the limited protection provided by section 1 of the Charging Orders Act 1979.

> A lone parent told a CAB in the West Midlands that one of his creditors would only accept his repayment proposal if he did not contest their application for a charging order against his property. The client was suffering from extreme stress,

2 *Ropaigealach v Allied Irish Bank PLC* [2001] EWCA Civ 1790.
3 *In too deep – the experience of CAB debt clients*, Citizens Advice, 2003.

as he felt he was doing everything in his power to resolve the situation but the creditors were not assisting him.

A woman sought advice from a CAB in South-East Wales about multiple debts. One of her creditors wrote to her to tell her that they would be taking county court action, which would be enforced by means of a charging order. The letter invited her to submit 'reasonable proposals', however, when telephoned it was made clear that reasonableness was payment in full or a charging order. The company also tried to convince the client that they already had a county court judgment they could enforce, when this was not the case.

A Hampshire CAB reported that a 68 year old man sought help with debts totalling £46,000. The CAB helped him make offers to all his creditors on an equitable basis. One of his creditors, a major credit card company, rejected the offer of £99.04 which would clear the debt in nine years. They insisted that they would only accept contractual repayments. If this was not possible, they would take recovery action. The CAB felt that as the client was a homeowner, it was a policy decision to try and get unsecured borrowing secured.

The 2003 *Effective Enforcement* White Paper stated that the missed instalment requirement was a 'major loophole that allows judgment debtors, paying off their debt in small instalments which are not reviewed regularly… to benefit from the sale of a property without paying off the debt'.[4] It would seem that judges dealing with money debt cases have increasingly come to accept this argument, particularly where the client's offer will not clear the debt within a reasonable period, if ever. For example:

A CAB in South-West Wales was helping a couple with their debt problems. The wife was severely disabled, and her husband was caring for her and working in a low paid job. One creditor, refused to accept the CAB's offer and went to county court with the intention of getting a forthwith judgment. The CAB helped the clients to respond to the court claim and make an offer, but the judge decided to make a forthwith judgment, stating that it would take too long to repay the debt at the amount the clients had offered. The creditor then went on to apply for an interim charging order. The clients were already struggling to maintain payments on a secured loan and mortgage and were now under threat of losing their home due to another charge being placed on their property. This had caused great relationship strain and stress for the couple.

CAB evidence also shows how it has recently become harder for those debtors who have been granted an instalment order to avoid a charging order if the creditor subsequently applies for one. In the past where a debtor had not defaulted on an instalment order, they had good grounds to challenge a charging order application successfully. Even where a debtor had fallen behind with payments, they could try to head off enforcement action by asking the court for further help before the creditor applied for a charging order.[5] CAB advisers, however, are now seeing cases that suggest this legal safeguard has started to slip. It seems that some creditors may be taking advantage of incorrect information in the 2008 HM Treasury *Green Book*, which contains relevant civil legislation and rules, about the application of Section 93 of the TCE Act:

4 *Effective Enforcement: Improved methods of recovery for civil court debt and commercial rent and a single regulatory regime for warrant enforcement agents*, Lord Chancellor's Department, 2003.

5 Section 86 of the County Courts Act 1984 provides that where a court makes an instalment order, execution shall not be issued until after a default in payments under the order. The Court of Appeal has interpreted this to include charging order applications – *Ropaigealach v Allied Irish Bank PLC* [2001] EWCA Civ 1790. If a debtor defaults on an instalment order, they can generally apply to the court to have a new instalment order at the court's discretion.

A Berkshire CAB reported that a working lone parent had made arrangements with her creditors to pay reduced payments on debts totalling £56,000. This included a bank debt of £21,000. The bank had obtained a county court judgment in February 2008 and had agreed to accept instalments of £47.21 per month. The client had not missed a payment. Nevertheless, in November 2008, the bank applied to the court for the order to be varied from payment by instalments to payment in full forthwith to allow them to apply for a charging order. Their justification for this was that it would take 38 years for the debt to be repaid in full at that rate and this was unacceptable, and that the client's financial circumstances *might* have changed since the court order was made. The judge did not make a forthwith order, but instead allowed the bank to apply for a charging order, even though the instalment order was still in place and being adhered to. Using money from her mother, the client then made an offer of £12,600 in full and final settlement of the debt, which was rejected. The client then had to appeal the judge's decision, at a cost of £120, plus a further unspecified cost for a transcript of the circuit judge's decision.

A Somerset CAB had been helping a woman with her debts since November 2007. As she had no available income for her creditors, the CAB had helped her make token payments of £2 per month to all her creditors. In March 2008, one creditor, a building society, issued a court claim, and judgment was made to be paid by instalments of £2 per month. The client maintained payments but the debt was passed to the building society's solicitors, who immediately applied for a charging order stating that the client had not made payments. Armed with evidence from the client that payments had indeed been made, the CAB contacted the solicitors requesting that the hearing for the final charging order was withdrawn. The solicitors told the CAB that it was too late to stop the hearing, but on the evidence provided they would not pursue the final charging order. The day before the hearing, the CAB received a letter from the solicitors stating that they would ask for the final order and costs. The CAB wrote to the court explaining the above. The judge did not award the final charging order and costs were passed back to the solicitors.

This suggests that both creditors and judges have been working round existing legal safeguards for debtors to put the *reasonable security* argument into effect even before Section 93 of the TCE Act had commenced. Consequently, we believe that the MoJ announcement not to proceed with Section 93 is likely to make fairly little difference in practice and creditors will still find charging orders easy to get.

The problem here is that in deciding not to implement Section 93 *and* Section 94 of the TCE Act, the Government will not be doing anything to introduce new safeguards for debtors on the use of charging orders by creditors. This is a matter of grave concern for Citizens Advice, as we believe that the current law on charging orders leaves debtors too exposed to both possible unfair treatment and a looming threat to their homes from unsecured creditors. In the next section we will set out the reasons for these concerns.

Charging orders and debt collection practices

It has been argued that creditors merely use charging orders as a way of 'securing their position'. As long as they 'do not resort to the use of orders for sale except in extreme circumstances', debtors will not suffer undue

detriment as a result.[6] From this perspective, the main policy challenge to the existing charging order arrangements is the need to protect debtors from enforcement related costs that are disproportionate to the size of the debt. The regulations that the MoJ intended to introduce under Section 94 would have imposed minimum financial thresholds below which a judgment creditor would not be able to apply for a charging order.

Charging orders on small debts

Although these proposals are not now being taken forward, CAB evidence continues to highlight cases where creditors have sought and been granted charging orders for relatively small debts.

> A Wiltshire CAB reported that a debt purchase company threatened a couple with charging order proceedings for a credit card debt totalling £690. The CAB noted that the debt purchase company seemed to have moved swiftly to an interim charging order without pursuing other means of getting repayment proposals for a very small debt.

> A CAB in North-West Wales reported that their client was faced with a charging order for a store card debt of £852. The court had ordered in May 2008 that the client should pay the debt at a rate of £10 per month. The creditor, however, asked the court for a redetermination of the order and a hearing was set for 21 July 2008 at the client's local county court. The creditor advised the client not to attend and consequently, an order was made that the client should pay the full balance forthwith. The client told the CAB that he did not receive notice of this order and continued to pay instalments. However, as the client had defaulted on the court order, the creditor applied for a charging order for the sum of £852.

Pressurising debtors to pay in full

Citizens Advice would welcome measures to prevent creditors from securing smaller debts by charging order, but we do not believe that this alone could amount to what the Government had described as 'protection for genuinely vulnerable debtors from unduly vigorous pursuit by overzealous creditors'.[7] This is because rather than just securing the creditor's position, charging orders form part of a debt collection process that can be used to put disproportionate pressure on people in financial difficulties to pay more than they can afford to their creditors. Despite regulatory guidance from the Office of Fair Trading (OFT) that defines 'pressuring debtors to pay in full, in unreasonably large instalments or to increase payment when they are unable to do so'[8] as an unfair business practice as defined in section 25 of the Consumer Credit Act 1974, CAB evidence continues to highlight cases of creditors using the threat of court action and a charging order to do just this.

> A CAB in South-East Wales saw a 31 year old lone parent who was working part time and in receipt of tax credits. She was up to date with payments on her mortgage, council tax and utility bills but had some county court judgments subject to arrangements, which were also up to date. She also had several non-priority debts including a £2,000 personal loan on which she had an agreement in place with the lender to pay £40 per month. However she then received a letter from a debt collection firm telling her that the debt had been sold to them. The woman contacted them to continue the offer of £40 per month but they told her they wanted £350 per month, which she could not afford. They also told her that the law said she needed to clear her account in six months or they would go for a charging order on her property. They also told her that if the first

6 Tribunal, Courts and Enforcement Bill: Regulatory Impact Assessments, Department for Constitutional Affairs, 2006.
7 Tribunal, Courts and Enforcement Bill: Detailed policy statement on delegated powers, Department for Constitutional Affairs, 2007.
8 *Debt collection guidance: Final guidance on unfair business practices*, OFT, 2003.

payment was not made by the end of the month they would go for a charging order on her property.

A CAB in Yorkshire saw a 34 year old man who lived with his wife and two children in their own house with significant secured debt and no equity. The man came to the bureau after his wife tried to commit suicide because of debts and he discovered the extent of their debt problem. They had no surplus income but offered a token £1 per month to all their creditors. One of the creditors, a credit card provider, refused to accept the offer and instructed a debt collector who ignored correspondence from both the man and the bureau and demanded increased payments. The debt was eventually sold on to another debt collector who threatened bankruptcy and also went for a county court judgment, charging order and order for sale. They refused to accept any payment plan, ignored correspondence from the bureau and the client's circumstances.

Taking court action despite disputing liability

In a parallel of some of the arrears management practices in mortgage and secured loan markets that made a pre-action protocol necessary, some creditors are using the court process not as a means of pursuing 'won't pays' or trying to resolve genuine disputes, but as a tactic to intimidate debtors to pay unaffordable amounts. Indeed CAB evidence also highlights cases where a creditor has taken court action where the debtor was actively disputing liability for part of the debt.

A Cheshire CAB reported that a self-employed man had experienced temporary problems with his business and had built up a £9,000 overdraft. He was also going through the process of reclaiming disputed bank charges. This process had been frozen because of the OFT test case. But the bank continued to add interest to the overdraft and the debt grew from £9,000 to £17,000. He had complained to the Financial Ombudsman Service (FOS) about the excessive charges. The bank subsequently offered a settlement, which the client was advised by FOS not to accept as the case was still being investigated. Although the Ombudsman had not finished investigating the case, the bank issued a court claim and then charging order proceedings. The man was completely unaware of the implications of a charging order in relation to his credit rating. This came to a head when he was informed that a new lease agreement for a car could not go though because he had a poor credit rating. He was very concerned that the court action would have an adverse impact on his business if he were unable to continue to lease cars.

In each of these cases it seems clear that the creditor's pursuit of a charging order has serious implications for the debtor. Firstly, it exposes people in financial difficulties to additional costs and charges that increase overall indebtedness and make the debt problems more difficult to resolve.

A CAB in the West Midlands reported that a married woman received a court claim for £1,652.87 owing to a store card company. The client agreed that she owed the money, but did not respond to the court claim. A forthwith order was made. Shortly afterwards, the client received a bonus from work and sent a cheque by first class post for the full amount to the solicitors dealing with the debt on 16 March 2008. However, on 25 March 2008 they told the client that they had received the cheque, but it was too late to stop charging order proceedings. They now wanted an additional £433.35 for court fees and

costs. The solicitors did not cash the client's cheque and continued with the application on 18 March 2008. The hearing for the final charging order was on 29 September 2008, which the client attended. The judge felt that the solicitors had acted too quickly in trying to enforce the debt, that the costs they had tried to charge client for making the application were excessive and could not understand why they did not withdraw the application. However, as they did have the right to enforce the debt immediately, he said that the client should pay £211 costs. The client had been extremely stressed while waiting to go to court for the final charging order hearing. In this time, she had struggled to keep the money available for six months and had to open a separate bank account to ensure the creditor could still claim it so she could prevent the final charging order being made. The CAB noted that if the solicitors had cashed the cheque as soon as they had received it, the debt should have been removed from the Register of Judgments. However, the entry remained and would affect her ability to obtain credit in the future.

Secondly, the creditor's recourse to court action may push up the borrower's credit costs or restrict access to credit in other sectors of the credit market. The existence of a charging order may also make it more difficult for a mortgage borrower to remortgage with another lender, perhaps at the end of a fixed rate deal, unless they can find the funds to clear the whole debt covered by the charging order. Finally, these debt collection tactics may add considerably to the stress and anxiety often experienced by people in financial difficulties. In our 2003 evidence report *In too deep*, we highlighted how 62 per cent of the CAB clients we surveyed about the impact of debt of their family life told us they were suffering from stress anxiety or depression. Over 40 per cent of these (25 per cent of all the CAB clients surveyed) had sought treatment from their GP as a result.[9] In addition to the obvious immediate *human* cost of debt related stress is the wider social cost of treatment and lost productivity from stress related work absence. The Government has estimated that workdays lost as a result of debt may cost the UK economy as much as one per cent of GDP.[10]

For many years, Citizens Advice has argued that minimising these additional costs means dealing with debt problems, and multiple debt problems in particular, in a coordinated and sustainable way. Indeed the essence of money advice practice is to help people in financial difficulties to make repayments to all their creditors that they can afford to maintain over time. For some years the money advice sector has been working with the credit industry to develop an objective measure of reasonable affordability through the common financial statement methodology.[11] This has been adopted into both the Banking Code and the Finance and Leasing Association Lending Code as the *good practice* basis for negotiating debt repayments.

Disregarding good practice

The cases presented above show that creditors are not always following good practice. More to the point, CAB evidence highlights multiple debt cases where a single creditor has taken court action and applied for a charging order when all the other creditors have been prepared to accept a reasonable offer.

A Lincolnshire CAB reported that a married man with two children on a low wage sought help with credit debts of £34,400. The CAB produced a financial statement and made pro-rata offers to the creditors. The offers were a substantial proportion of his income as his wife was working which enabled him

9 *In too deep: CAB clients' experience of debt*, Citizens Advice, 2003.
10 *Fair, clear and competitive: The consumer credit market in the 21st century*, Department for Trade and Industry, 2003.
11 See moneyadvicetrust.org.uk for an explanation of the common financial statement.

to free up money for his debts. All his creditors accepted the client's offers except a building society, to whom the client owed about £9,000. They did not respond to CAB correspondence, and passed the debt to a debt collection agency who also did not answer letters from the CAB. The debt collection agency phoned the client continually, but when he asked them whether they had received the CAB's letter and financial statement, they refused to tell him. The debt was then passed to the building society's legal department, who sent a letter threatening court action and other charges amounting to £414. When they had obtained a judgment, the building society then proceeded to obtain a charging order against the client, although he had been paying £80 per month and that was all he could afford. The judge hearing the application asked the building society's representative to convey his 'disapprobation' of their behaviour, particularly as all the client's other creditors had behaved in a reasonable manner.

We are concerned that the seemingly growing ease of obtaining charging orders increasingly undermines the good practice principles implicit in initiatives like the common financial statement. Creditors are more likely to stop complying with good practice commitments if they believe that other creditors are gaining an advantage from doing the same thing. Moreover, many of the charging order cases bureaux see involve debt purchase companies who are looking to maximise returns and who may not be restrained by the same reputational concerns as some high street lenders. Here the growth of charging orders does not just undermine existing good practice standards, but may also herald the growth of business models that are based on more aggressive debt collection practices. This is perhaps captured in a quote from the website of a legal firm explaining the benefits of charging orders for its potential customers:

"If you have purchased debt at or have written it down to a fraction of its face value you are into serious profit".

As such, the growth in charging orders exposes a serious gap between court enforcement processes and the requirements of the OFT debt collection guidance and voluntary industry codes. Citizens Advice believes that this gap needs to be closed by narrowing the circumstances in which creditors can be granted charging orders. This need is becoming more pressing as we are starting to see more cases of creditors attempting to enforce their charging order by asking the court for an order for sale.

Orders for sale

Before 2008, bureaux had reported very few cases about orders for sale to Citizens Advice. Although the number of cases we are seeing is very small, these appear to be concentrated amongst certain creditors, suggesting that these firms have decided to use the order for sale procedure as a business practice to collect outstanding unsecured debts. In many of the cases, creditors are asking for orders for sale on relatively small debts:

A Sussex CAB saw a 65 year old man in receipt of incapacity benefit and disability living allowance at an advice session at the local county court. He was there for an adjourned order for sale hearing brought by his bank. He had originally had an overdraft of about £15,000 and had been paying this off at a rate of £35 per month via a debt management company. The client had been diagnosed with diabetes which had affected his sight, heart and kidneys, the latter requiring dialysis. He had attended a previous order for sale hearing, which had been adjourned for the client to provide evidence of sums due under an inheritance which would more than cover the outstanding debt. He had not

been able to produce it and the bank was pushing for the order for sale although the client had increased his offer of payment from £35 to £50 per month. The stress of trying to deal with this problem had caused the client further stress and health problems. The loss of his home would mean he would have to move the home dialysis equipment he had recently installed.

A CAB in the West Midlands reported that a single disabled man suffering from chronic depression and anxiety owed £12,000 to a number of unsecured creditors. One of his creditors, a debt purchase company had obtained a county court judgment in early 2007, a charging order in August 2007 and an order for sale in December 2008. The man was due to be evicted on 12 May 2009. On 11 May 2009, he sought advice from the CAB who helped him apply to suspend the warrant of eviction. The client stated that he could not recall receiving any letters or court documents prior to receiving the warrant of eviction, and offered to pay the debt off by instalments of £10 per week, with the help of his mother. The CAB represented the man in court. Although he could not prove that the letters and court documents had not been received, the district judge noticed that whilst the judgment was for £4,701.81, the debt purchase company had wrongly added statutory interest on a debt below £5,000 when the charging order was made. The judge therefore discharged the order for sale.

A Greater Manchester CAB saw a 37 year old woman who had suffered a stroke in December 2007. She owed a bank £9,207.77. The debt was subject to a county court judgment and a charging order. Although the client had since returned to work, her partner was unable to work due to depression and was on benefits. The client had been paying £50 per month to the bank, but they wanted payments of £327.65 per month. The CAB assessed her income and expenditure and offered £60 per month. The bank rejected this and threatened order for sale proceedings. The CAB helped the client budget so that she could make a higher offer of £110 per month. Again this was rejected and the bank went ahead with a claim for an order for sale. The CAB contacted the bank to explain the client's and her partner's health problems, but they refused to accept less than £344.07 per month, insisting there was sufficient equity to repay the debt. The client was so worried about the possible loss of her home that she negotiated payments of £320 per month with the bank's solicitors to stop the hearing. She could only afford to do so because her family were able to help her. The payments to the bank were actually higher than her mortgage and secured loan instalments.

A Yorkshire CAB saw a Pakistani man who had a charging order as a result of two debts totalling £6,900 to claims management companies. He had tried to dispute the debt, but was unable to get legal help as he failed the sufficient benefit test. The company obtained an order for sale and had now applied for a warrant of eviction. The client, who was married with six children under 18, was on income support and had little capacity to repay the debt. If the warrant went ahead, he and his family would be homeless.

We understand that many of these applications fail, but some have been successful. However we are concerned that after seeing the safeguards for debtors against charging orders slip, creditors are taking the logical next step of undermining the safeguards protecting debtors against orders for sale.

As set out in the 2003 *Effective Enforcement* White Paper, these safeguards at least appear to be extensive. But on closer inspection, they seem to provide debtors with only weak protection that may not stand up to concerted legal challenge by creditors. The case which sets out the circumstances in which courts will grant an order for sale is the Court of Appeal decision in *Bank of Ireland Home Mortgages Ltd v Bell*.[12] This confirms an earlier High Court ruling that section 15 of the Trusts for Land and Appointment of Trustees Act 1996 requires courts to consider the interests and the welfare of the debtor, other members of the debtor's household, and dependent children in particular, when considering a creditor's application for an order for sale.[13]

There are, however, a number of prior legal authorities stating that 'save in exceptional circumstances, the wish of the person wanting the sale [that is, the creditor]… would prevail…'.[14] The effect of the 1996 Act was to *rebalance* the competing interests of creditor and debtor towards the debtor; but this arguably starts from a very low base of protection given the presumption that the creditor's interests should prevail. So the effect of the judgment in *Bell* is to set out the limited nature of the safeguard for debtors provided by the 1996 Act. This is stated by Lord Justice Gibson as follows:

> "The 1996 Act… appears to me to have given scope for some change in the court's practice. Nevertheless, a powerful consideration is and ought to be whether the creditor is receiving proper recompense for being kept out of his money, repayment of which is overdue… In the present case it is plain that by refusing sale the judge has condemned the bank to go on waiting for its money with no prospect of recovery… That seems me to be very unfair to the bank".

As a result, a single homeowner without dependent children may have very little protection under the law. For other owner-occupiers, including non-debtors and dependent children, protection is at best contingent on the interests of creditors. This suggests that the main safeguard for debtors is not an absolute or even conditional right, but rests on the discretion of the court to make or not make a charging order or order for sale based on the facts of each case.

Here it is clear that both the Charging Orders Act 1979 and Section 71(2) of the County Court Act 1984 give the court wide discretion to refuse an order for sale or suspend it on terms that the debtor repays by instalments. Guidance on the Civil Procedure Rules advises judges that ordering sale is 'an extreme sanction' and a 'draconian step to satisfy a simple debt' and all circumstances would have to be considered. But the guidance then goes on to state that sale is likely to be ordered 'in a case of the judgment debtor's contumelious neglect or refusal to pay or in a case where in reality without a sale the judgment debt will not be paid'.[15]

It is the last part of this that concerns us, as bureaux see many cases where people who have fallen into financial difficulties are only able to make relatively small or even token payments towards their debts that might take many years to clear as a result, as highlighted in the recent Citizens Advice report, *A life in debt*.[16] People in these circumstances might be doing their best to deal with their debt problem by seeking the help of a money adviser and offering to pay their creditors as much as they can afford. Yet the law appears to offer them almost no protection should a creditor make a determined effort to enforce the debt against their home. As a result the very low number of orders for sale currently granted by the court is probably more the result of creditors considering possible

12 *Bank of Ireland Home Mortgages Limited v Bell* [2000] EWCA Civ 426.
13 *Mortgage Corporation v Shaire* [2000] EWHC Ch 452.
14 Ibid.
15 Supreme Court Practice – guidance on Civil Procedure Rules at paragraph 73.10.1.
16 *A life in debt: The profile of CAB debt clients in 2008*, Citizens Advice, 2009.

reputation damage and the understandable reluctance of judges to take people's homes away for unsecured debt.

Citizens Advice believes that this situation of contingent and uncertain protection for debtors is unacceptable. It also may not be sustainable given the rapid growth in charging orders and the growing practice of banks and other large commercial credit providers of selling debts on collection specialists that may not have the same reputation concerns. Section 93 and 94 of the TCE Act would have provided some administrative protection by setting financial thresholds for charging orders and orders for sale, but only at the serious danger of making these orders a more likely outcome for any debt above the threshold set by regulations. There is still a need for a more fundamental policy review of the way that the law currently allows unsecured creditors to enforce against the homes of debtors.

Principles for a fairer and more transparent framework for enforcement and protection from enforcement

Citizens Advice believes that the law on enforcement of unsecured debt against individuals needs to change to a more explicit framework of rights and responsibilities. This would rebalance the way that courts weigh the interest of debtors and creditors. This should have the explicit primary aim of protecting the homes of people in financial difficulties balanced by the need to allow creditors to enforce, but in a more tightly defined set of circumstances than in the current law.

Citizens Advice believes that where someone with a debt problem has done their best to deal with this by seeking advice and then offering to pay what they can afford, creditors should not be allowed to take further collection or enforcement action against them, except in a very limited number of tightly defined circumstances outlined below.

What would this mean for charging orders and orders for sale in practice?

Firstly this would re-establish charging orders as a remedy that is only available following default of a payment arrangement. The growing practice whereby creditors are able to secure often-small debts through the courts as a matter of course would stop.

Secondly restrictions on the use of charging orders and orders for sale would mean that commercial consumer credit agreements must be treated differently to other debts. **We believe that enforcement by charging order for consumer credit agreements should only be available where the debtor obtained credit fraudulently or has wilfully and persistently refused to engage with the debt problem.** The commercial interest of the creditor would no longer be viewed as a reasonable sole basis to enforce against the debtor's home. We believe that there are very good reasons for this fundamental change from the current position:

- Commercial consumer credit lenders can choose whether to lend or not and can price credit to the risks of default.
- Creditors can, if they wish, offer loans that are secured from the outset. These are generally priced at a lower rate of interest than unsecured debts to reflect the lender's security.
- Charging orders currently allow creditors to secure their debt against the home of the debtor, but at unsecured interest rates that may be considerably higher than interest rates on secured lending. Although court judgments in respect of consumer credit agreements should not carry statutory interest, fixed term credit agreements will often roll future interest payments into the judgment. Furthermore, many credit

agreements contain clauses allowing the creditor to continue to charge interest at the contractual rate after judgment.

- The Government has recently accepted that extra rules and safeguards are necessary for court action to enforce arrears on secured lending by means of a pre-action protocol.[17] It has also announced a further review of the way secured consumer credit agreements are regulated[18], and the OFT has recently consulted on specific guidance on the way secured loans are sold and enforced.[19] Allowing creditors to easily secure previously unsecured debts would seem to undermine this protection.
- Where consumers choose to take out credit on an unsecured basis, they should be able to feel confident that their home is safe if they behave reasonably towards their creditors. Both the Banking and the Finance and Leasing Association Lending Codes require subscribers to treat customers in financial difficulties positively and sympathetically. Lenders are also required to accept the common financial statement as an objective basis for negotiating affordable debt repayments. The growing use of charging orders and applications for orders for sale by some creditors seems out of step with these commitments.

What about non-consumer credit agreements?

In contrast, Citizens Advice accepts that there may be a case for allowing other types of unsecured creditors to secure debts by a charging order even where a debtor has offered to pay what they can afford. For example:

- Involuntary debts, where the creditor has no choice but to continue to provide a service, for example, water charges, where water companies cannot disconnect domestic supplies for non-payment.
- Some specified public debts, such as council tax and child support.

However, we believe that charging orders should only be available for debts above a financial threshold. This could be set separately for each type of debt in relation to a number of charging periods outstanding.

Even in these cases, we believe that enforcing the charging order by an order for sale will be unreasonable where the debtor is making what payments they can afford in light of their other essential commitments. **Citizens Advice believes that where a debtor has engaged with their debt problem, the court's power to order sale should be reserved solely for those cases where the creditor would suffer undue hardship by having to wait for their money.** The notion of hardship should be defined as personal hardship suffered by the debtor or members of their household, and should exclude legal persons' such as incorporated firms and partnerships, unless they are a small business.

This would ensure that creditors' commercial interests could not come in through the back door. This could include debts arising from private legal action where the claimant is an individual (for example, enforcement of non-payment of employment tribunal awards) and child support debts where non-payment would cause hardship to children or the resident parent. In such cases the court should retain discretion to not make an order, or suspend its operation as is reasonable on the circumstances of the case.

17 The Pre-Action Protocol for Possession Claims based on Mortgage or Home Purchase Plan Arrears in Respect of Residential Property came into force on 19 November 2008.
18 *Prime Minister unveils real help for consumers*, BERR (now Department for Business, Innovation and Skills (BIS)) press release, 17 March 2009.
19 *Second charge lending guidance for brokers and lenders*, OFT, 2009.

What about bankruptcy?

The 2003 *Effective Enforcement* White Paper argues against placing further restrictions on access to charging orders on the grounds that this would almost certainly lead to an increased use of creditors' petitions for bankruptcy to enforce debts. While this is probably true as a practical observation, we believe that it is entirely specious as a policy argument. If it is fair to restrict access to charging orders, then it will also be fair to restrict access to creditors' petitions for bankruptcy. At present a creditor can petition the court to make a debtor bankrupt where the debt is over £750, a very small amount for a serious enforcement sanction that can mean the debtor losing their home and becoming subject to significant additional bankruptcy costs. For example:

> A CAB in South-East Wales saw a single disabled woman on income support and disability living allowance. She was a homeowner with a small mortgage and equity of about £60,000. She had a debt of £1,600 which had been acquired by a debt collection agency. The client offered £10 per month to the debt collection agency's solicitors, but this was rejected and they commenced bankruptcy proceedings. As a last resort, the CAB offered a voluntary charge on the client's flat. The solicitors agreed. However they wanted their costs of about £5,000 added to the debt, so that the sum secured by the charge would rise to £6,500, and interest would accrue. Although there had been three court hearings for the bankruptcy petition, all of which have been adjourned, the CAB felt that the solicitors had exaggerated their costs, but was concerned that it would be difficult to challenge them. To do so might well jeopardise the voluntary charge, leading to the client's bankruptcy and eventual loss of her home. The CAB was also concerned that the costs in pursuing this debt by bankruptcy action were disproportionate relative to the amount owed.

We understand that the Insolvency Service proposes to increase this limit but, as we have argued with charging orders and orders for sale, a higher financial threshold will not guarantee fair and reasonable enforcement practices. **Therefore Citizens Advice believes that the enforcement principles we have set out above should also apply to creditors' petitions for bankruptcy.**

Here we believe that the law is already behind public perceptions for fairness. For instance, a recent decision of the Local Government Ombudsman held that a local authority had acted unfairly in petitioning for bankruptcy to enforce a council tax debt even though they had the legal power to do so.[20] The Ombudsman ruled that the local authority should have considered whether the costs and hardship that could result for the debtor were proportionate to the debt.

Conclusions and recommendations

The experience of the CAB service on charging orders and orders for sale demonstrates that the Government's rationale for the changes to legislation on these methods of enforcement contained in the *Effective Enforcement* White Paper are deeply flawed. Nevertheless, our evidence shows that changes to legislation are needed if the rights of creditors and debtors are to be better balanced. What we are proposing is a form of pre-enforcement protocol, which will bring closer together regulatory guidance on the way in which creditors should treat people in financial difficulties and the judicial enforcement processes in the courts. Equally we believe that more limited access for creditors to enforce unsecured debts against the homes of debtors may help to improve lending practices.

20 Wolverhampton City Council (06B16600) Local Government Ombudsman, 31 March 2008.

Our recommendations are set out below:

Changes to charging order and order for sale legislation

Citizens Advice believes that a number of changes are needed to enforcement legislation to ensure that charging orders and orders for sale become a last resort.

- **The Government should introduce new measures to set minimum financial thresholds for charging order applications. Different thresholds should apply for consumer credit and non-consumer credit debts.**
- **Lenders should be prevented from obtaining orders for sale on consumer credit agreements, except in exceptional circumstances.**
- **The law should be clear that orders for sale should only be granted in cases where the debtor wilfully refuses or culpably neglects to pay, or where the judgment creditor would suffer undue personal hardship from non-enforcement of the debt.**

Ensuring that debtors are protected from harsh debt collection and enforcement action where they are paying what they can afford

The reforms we have outlined above will not be effective without some safeguards to protect debtors from harsh debt collection and enforcement action. As our evidence shows, creditors accept that a debtor is offering the most they can afford to pay, but will continue to pressurise them to pay more via collection or enforcement activity, either by means of a court claim or a creditor's bankruptcy petition. As a result, we do not believe that the decision on acceptable repayments should be left solely in the hands of creditors. Citizens Advice believes that this is a proper matter for regulation. Therefore we propose the following three measures.

- **Firstly, the Government should bring the common financial statement method (or something similar) into the debt collection guidance issued by the OFT under section 25 of the Consumer Credit Act 1974.** This would in theory impose no cost on businesses who have already agreed to adopt this scheme – but it would carry the prospect of enforcement action for non-compliant firms which does not currently exist.
- **Secondly, the Government should implement the debt management scheme provisions of the Tribunals Courts, and Enforcement Act 2007.** This would enable debtors to make affordable repayments to their creditors which are binding and would restrict creditors' rights to enforcement action. This would allay many of the concerns raised in this paper, but there is a potential loophole in that section 122 of the Act would allow creditors to appeal against being included in a scheme, and section 116 allows the creditor to ask the court's permission to enforce the debt. The Act provides no guidance on how the court should deal with such applications, leading to the concern that they would follow the principle that the creditor's interest should usually prevail that underpins the law relating to charging orders and orders for sale.
- **Finally, bankruptcy legislation should be amended to limit the circumstances in which creditors can petition for bankruptcy to cases of borrower fraud and cases where borrowers have willfully or culpably neglected to engage with a creditor's demands for payment.**

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Published by

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