

## **BANKRUPTCY: ASPECTS OF REALISING THE DWELLING**

**The ILA's Technical Committee wishes to draw members' attention to 3 recent decisions relating to the bankrupt's dwelling:**

**the first (*French v Barcham*), relating to equitable accounting on sale;**

**the second (*Barrett v Barrett*), involving the refusal of the court to enforce an agreement the purpose of which was to insulate the property from bankruptcy; and**

**the third (*Brittain*), where a trustee failed to establish that the bankrupt had owned the entirety of the property but left open to the trustee certain other remedies to achieve the same result.**

### **1. *French v Barcham* [2008] BPIR 857: Occupation rent & TLATA 1996**

In the typical case, the trustee in bankruptcy applies for possession and sale of the matrimonial home which the non-bankrupt spouse occupies with her family, with or without the bankrupt. As part of the accounting for the proceeds of sale, the wife raises an "equity", namely, that she should be given credit for her contribution to payments of mortgage principal and/or interest, usually made during the bankruptcy period. As a defensive equity, the trustee counter-applies for an allowance in respect of an occupation rent. Often, in economic terms, the one will cancel out the other.

In the ILA's technical bulletin on the decision of the HL in *Stack v Dowden* (# 108 of 2007, August 2007), we reported that both Lord Neuberger and Baroness Hale agreed that, in respect of occupation rent, the old doctrine of equitable accounting had been replaced by ss.12-15 Trusts of Land and Appointment of Trustees Act 1996 (TLATA). This had been considered subsequently and followed by the Court of Appeal in *Murphy v Gooch*. Certainly, as regards a joint owner who had been excluded from occupation (which was the case in *Stack v Dowden* and *Murphy v Gooch*, both of which were cases between unmarried cohabitantes where no bankruptcy had intervened), the observation holds good.

However, as between the trustee in bankruptcy succeeding to a bankrupt's beneficial interest under a trust of land, and the non bankrupt joint trustee, that view could operate to the disadvantage of the bankruptcy estate. In *French v Barcham*, the proposition appealed to the district judge at first instance, who held that a trustee in bankruptcy was not a beneficiary entitled to occupy land under TLATA, with the consequence that he was not entitled to any compensation under section 13(6) of TLATA (or occupation rent) because the former practice had been wholly replaced by the statutory compensation regime contained in TLATA following *Stack v Dowden*. If correct, this would mean that a trustee in bankruptcy would have no defensive equity against a claim for credit for mortgage/interest repayments.

On appeal by the trustee in bankruptcy of Mr B, it was common ground that the trustee was entitled to the benefit of the bankrupt's interest in the land, but was not entitled to occupation, so could not be excluded nor be able to seek statutory compensation for exclusion under s.13(6) of TLATA. For the trustee, it was argued that the district judge was wrong in concluding that an occupation rent (or compensation in TLATA language) was payable only where s.13(6) of TLATA applied. A trustee in bankruptcy of a beneficiary under a trust of land might have no right of occupation under s.12 TLATA, but that should not exclude him from compensation for the continued occupation of the property by Mrs B.

On the other hand, Mrs B contended that the former practice requiring that credit be given for an occupation rent from the party in continuing occupation no longer applied, following TLATA as interpreted in *Stack v Dowden*, because a trustee in bankruptcy (unlike the bankrupt himself) had no right to occupy and could not be excluded, with the consequence that the statutory conditions for compensation (or occupation rent) did not arise.

In his judgment, Blackburne J (at paragraphs 18 to 21) stated that ss.12 to 15 of TLATA were not an exhaustive regime for compensation for exclusion of a beneficiary from property held subject to a trust of land. It was common ground that a trustee in bankruptcy had no right of occupation, so statutory compensation did not arise. However, just because there was no statutory right of compensation, it did not follow that Mrs B was not liable to be charged with an occupation rent from the time that the bankrupt's interest vested in the trustee and nothing in *Stack v Dowden* led to a different conclusion. *Stack v Dowden* was a case concerning the property rights of a cohabiting couple (as was *Murphy v Gooch*), and the decision addressed the circumstances before the court. The judge commented upon Lord Neuberger's observation (at paragraph 150 of *Stack v Dowden*), that the court's power to order payment to a beneficiary excluded from the property was, indeed, governed by ss.12 to 15 of the 1996 Act which applied only where the beneficiary claiming compensation for exclusion would otherwise have been entitled to occupation, but it did not follow that the trustee could not establish an entitlement to compensation in the nature of an occupation rent. The statutory scheme did not apply in the instant case, and the party who was not in occupation (the trustee) should not be denied compensation if the court's equitable jurisdiction would provide it (which it did).

Blackburne J went on to consider the various alternative submissions as to the nature of the relief which should be ordered. At paragraph 34 Blackburne J stated '*The essential point, in my view, is that when on inquiry it would be unreasonable, looking at the matter practically, to expect the co-owner who is not in occupation to exercise his right as a co-owner to take occupation of the property, for example because of the nature of the property or the identity and relationship to each other of the co-owners, it would normally be fair or equitable to charge the occupying co-owner an occupation rent.*' Whether Mrs B should be charged with an occupation rent was ultimately a matter for the court's discretion, and her half share in the net proceeds of sale was liable to be debited

with half of the property's letting value from the time the bankrupt's interest vested in the trustee.

This decision provides useful clarification of what would otherwise have become an unintended heresy in bankruptcy cases. For trustees in bankruptcy, the lesson must be to emphasise that the entitlement to the benefit of an occupation rent compensation is a matter of equitable relief and is at the court's discretion. Trustees should guard against raising false expectations in the non bankrupt co-owner that such a claim might not be made (which could operate as an estoppel against the trustee).

Finally, members might also wish to note:

(a) Counsel for the trustee in bankruptcy conceded that the claim for occupation rent should not exceed the level of credit allowed to Mrs B in respect of mortgage/interest repayments. However, it is an interesting question as to whether the claim for an occupation rent merely acts as a set off or can result in a balance owing to the trustee. In principle, if the mortgage repayments are small and the notional occupation rent high, there seems to be no reason in principle why the result of the account should not result in a credit in the overall account in favour of the bankruptcy estate.

(b) There appears to be no reason in principle why a claim for occupation rent should not be self-standing, i.e. not used merely as a defensive equity (in response to a claim for credit for payments of mortgage principal and/or interest) but, in an appropriate case, as a sword claiming a portion of the proceeds of sale otherwise payable to the non-bankrupt spouse.

(c) In theory, the effect of the operation of the "use it or lose it rule" should be that these principles will not have such a substantial bearing on the equitable accounting in these cases because the number of cases where there is a lengthy period between bankruptcy and sale should be fast-diminishing. However, the conjunction of a static housing market and falling values means that the old doctrine might yet have a new lease of life.

## 2. ***Barrett v Barrett* [2008] EWHC 1061 (Ch); [2008] BPIR 817**

This was a decision of David Richards J, who rejected an appeal against a decision to strike out the claim of a former bankrupt (TB) against his brother (JB) for a declaration that JB held the proceeds of sale of a property on trust for TB. The decision turned on the rule that a party will not be permitted to rely on an unlawful agreement to establish his claim. The unlawfulness arose in the context of s333 IA 1986 (after acquired property). It is not a case about bankruptcy itself.

JB had bought TB's property from TB's trustee in bankruptcy and became sole registered proprietor in 1995. When JB sold it 9 years later, TB sought the declaration that the proceeds of sale were held on trust for him on the basis that TB had paid the mortgage and other expenses of the property, and that JB was a mere nominee and held the

property on trust for TB. TB pleaded an agreement to that effect between himself and JB (which JB denied), the purpose of which was to evade his bankruptcy obligations and to avoid the property being repossessed by TB's trustee as after acquired property under s333(2) IA 1986. In order to make his case, TB had to rely on that purpose, which was unlawful and, following *Tinsley v Milligan* [1994] 1 AC 340 HL, the claim was unenforceable and was bound to fail.

TB's alternative claim was that the payment of mortgage instalments conferred a constructive trust in his favour. Following dicta in *Stack v Dowden* (supra), mortgage instalment payments were not the equivalent of direct contributions to the purchase price and, in the absence of an agreement that they should confer a beneficial interest, that claim failed. The only agreement in evidence was the one designed to unlawfully conceal the asset from TB's trustee.

### 3. ***Brittain v Courtway Estates Holdings SA (and another)* [2008] EWHC 1791 (Ch)**

In *Brittain v Courtway Estates*, Evans-Lombe J was required to resolve competing claims between a trustee in bankruptcy of a bankrupt (R), that the property was beneficially owned by R and vested in the trustee, with those of his spouse as the sole beneficiary of the shares in the company which was the registered proprietor (CEH). There was another competing claim by the second respondent (S) which depended on establishing a transfer of the shares in CEH to him (which did not succeed).

As to the wife's claim to the property (via her beneficial interest in the shares of CEH), the trustee's evidence was that the purchase monies had come from a settlement by R on his spouse. The judge found that the intention had been to ensure the property never became part of the bankrupt's estate (which had been achieved), but left open the question whether the trustee might seek to overturn the transaction as a fraud on creditors under s423 IA 1986 (see paragraphs 50 and 59, described as a "simple remedy") when making no order on the trustee's application.

The case report is notable for the judge's scepticism as to some of the evidence before the court, including (at paragraph 48) that the bankruptcy itself was a contrivance to enable the debtor to evade his debts, whilst preserving his assets in the form of property vested in others to which he would continue to have access.