Family loans and intervener claims: taking the bank of mum and dad to court

Alexander Chandler, *Barrister, 1 King's Bench Walk, London*

Alexander Chandler is recommended as a leading junior in matrimonial finance by Chambers and Partners ("a rising star") and the Legal 500. He also specialises in TOLATA and Schedule 1 claims, and sits as an arbitrator, deputy district judge in civil and family and as a BTAS panel member.

An article in the *Guardian* reported that a majority (64%) of first-time buyers now receive help from their parents in raising a deposit. 'The bank of mum and dad has', the *Guardian* noted:

> '… a fantastic reputation as a lender. Long borrowing agreements, no interest to pay, flexible repayment schedules that are sympathetic to the financial setbacks and unexpected expenses we all face. Yes, the bank of mum and dad really has much to recommend it.' (*Guardian*, 17 April 2015)

Until, one might add, the breakdown of the child's marriage, when the lending criteria tighten and an advance of money previously understood (rightly or wrongly) to be a soft loan or gift magically crystallises into hard debt due for repayment.

What steps should be taken when this happens, typically where one spouse asserts in Form E that a family member is calling in a significant liability which the other party disputes? Is it necessary to embark on a full '*TL v ML*' investigation of the facts, with the family member/creditor invited or ordered to intervene, as if they were asserting a beneficial interest in matrimonial property? Or can the issue be resolved in a more proportionate way?

The problem with intervener cases

Anyone who has acted in an intervener case will know, firstly, that joining a third party inevitably leads to delay and expense; secondly, that the stakes are high. It is, if anything, too easy to obtain the court's direction that a non-party should be 'invited to intervene' or, in some cases, that the court of its own motion might join a third party (FPR Pt 9.26B(4). The threshold for joining a third party is not a rigorous one ('… if it is desirable': FPR Pt 9.26B; cf. 'necessity' test for expert evidence: FPR Pt 25.4(3)). However, the consequence may be satellite litigation which exceeds the cost of the primary financial remedy claim, with three parties pleading their cases, filing witness statements, providing disclosure by list and a preliminary hearing which often (due to the number of witnesses) takes 3 days or more.

The benign presumption in financial remedy proceedings that each party pays their own costs (FPR Pt 28.3(5)), and the rule that only open offers are taken into account (FPR Pt 28.3(8), do not apply to intervener claims. *Calderbank* offers are admissible and, while the court starts with a 'clean sheet', the fact that one party has been successful will often be the decisive factor on costs (*Baker v Rowe* [2009] EWCA Civ 1162, [2010] 1 FLR 761, at para [25]). Careful instructions therefore need to be taken at an early stage from a client whose defence to repaying a loan to her in-laws might be no more than wishful thinking. Given that the trial of the preliminary issue may take significantly longer than the final hearing of the financial remedy claim, the losing party may face a ruinously high bill to pay.

Does *TL v ML* require a creditor to intervene?

At the risk of repeating judicial guidance that is generally well-known, in *TL v ML and Others (Ancillary Relief: Claim Against Assets of Extended Family)* [2005] EWHC 2860 (Fam), [2006] 1 FLR 1263, Nicholas Mostyn QC (then sitting as a deputy High Court judge) commented (at para [36]):

> 'In my opinion, it is essential in every instance where a dispute arises about the ownership of property in ancillary relief proceedings between a spouse and a third party, that the following things should ordinarily happen:
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> (i) The third party should be joined to the proceedings at the earliest opportunity;
> (ii) Directions should be given for the issue to be fully pleaded by points of claim and points of defence;
> (iii) Separate witness statements should be directed in relation to the dispute; and
> (iv) The dispute should be directed to be heard separately as a preliminary issue, before the financial dispute resolution (FDR).'

This passage is universally and correctly cited in support of the proposition that issues of beneficial ownership of property between a spouse and a third party should be determined as a preliminary issue. It is also frequently and incorrectly cited in support of the premise that a creditor's claim for repayment (eg the bank of mum and dad calling in a loan) should follow the same procedure.

This guidance, which relates back to *Tebbutt v Haynes* [1981] 2 All ER 238 and was endorsed by the Court of Appeal in *Edgerton v Edgerton and Zaffirili Shaikh* [2012] EWCA Civ 181, [2012] 2 FLR 273 at para [53], applies only to issues of beneficial ownership between a spouse and a third party. It does not apply to issues of indebtedness, or mandate the joinder of family members who assert that they are creditors of the parties.

Nevertheless, should the creditor be invited to intervene?

The principle underlying the rules on joining a party was considered by Hughes LJ in *Goldstone v Goldstone* [2011] EWCA Civ 39, [2011] 1 FLR 1926 (albeit in reference to CPR Pt 19.2, upon which FPR Pt 9.26B is modelled):

> '… it is desirable to equip a single court with the means of deciding all relevant connected issues within the same proceedings and to avoid a multiplicity of different and potentially conflicting proceedings.'

Accordingly, the court undoubtedly has a discretion to join a third party to resolve preliminary issues other than beneficial ownership, if it is desirable to add the party so the court can resolve all matter in dispute (FPR Pt 9.26B(1)(a)).

However, in exercising this discretion the court must seek to give effect to the overriding objective (FPR Pt 1.2) of enabling the court to deal with cases justly, ie to ensure the case is dealt with expeditiously and fairly, proportionately, with the parties on an equal footing, saving expense and allotting an appropriate share of the court's resources to it (FPR Pt 1.1(2)). Too often, the hearing of a preliminary issue/intervener case departs from several, in some cases, all of these components of the overriding objective.

What then is the alternative?

In many cases, the simple answer is that the creditor can attend court as a witness, either voluntarily (having served a witness statement which complies with FPR PD 22A) or involuntarily, by witness summons (FPR Pt 24.2).

The court can then assess as part of a final hearing the alleged debt as one of the statutory criteria at s 25(2)(b) of the Matrimonial Causes Act 1973 ('… the financial . . . obligations and responsibilities which each of the parties to the marriage has or is likely to have in the foreseeable future'). Having heard the evidence of the

parties and the alleged creditor tested, the court should be in a position to reach findings of fact on the relevant issues, which are generally factual:

(a) Was the money advanced by way of gift or loan?

(b) If the money was loaned, what are the terms of the loan, and

(c) Most controversially, was this a 'soft loan'?

Soft loans

In *Jacobellis v Ohio* 378 US 184, US Supreme Court Justice Peter Stewart declined to precisely define the subject matter of the suit (in that case, hardcore pornography) but commented 'I know it when I see it'. It is similarly difficult to nail down a precise definition of what is a 'soft loan'. In *M v B (Ancillary Proceedings: Lump Sum)* [1998] 1 FLR 53, permission to appeal had been allowed by Ward LJ on the trial judge's failure to distinguish '… hard debts, such as her debt to the bank and soft debts, such as her borrowings from her mother and her brother' (p 59), although the categories are hardly mutually exclusive. A parent may choose to invest in a child's property, and secure that interest by way of charge registered at the Land Registry. In such circumstances, it is difficult to see how a court would regard such a loan as 'soft'.

Perhaps a better definition of 'soft loan' can be found in *W v W (Financial Remedies: Confiscation Order)* [2012] EWHC 2469, [2013] 2 FLR 359 per Ryder J (as he then was) at para [28] '… They are soft debts in the sense that provided the W does not "fall out" with any of the principals then they will wait for their monies to be returned'.

The court's powers

As practitioners will be aware, under the Matrimonial Causes Act 1973 the court has no power to adjust the amount owed or assign the burden of the debt. Debts are commonly dealt with through undertakings (eg the undertaking to use best endeavours

to release one party from his mortgage covenants – although see paras 50 and 55 of the draft Financial Remedy Omnibus for the contrary view that a party can be ordered to use her best endeavours).

Where a creditor appears as a witness and the court is satisfied that debt is now repayable, the court has no power to make an order in the creditor's favour (unless he is joined as a party: see *Burton v Burton* [1986] 2 FLR 419). However, the court can in most cases deal with the issue indirectly, eg making a lump sum order in one party's favour upon his undertaking to repay the amount of the loan to the creditor.

It is right to say that this solution is not a perfect one. It means that the issue of an outstanding debt will not be resolved by the FDR, and it assumes there are sufficient matrimonial assets to cover the debt. However, in most cases this will be preferable to involving the parties and creditor in a full-blown intervener claim. Furthermore, while the FDR would take place with the issue unresolved, it is a rare case which does not involve some sort of factual dispute which the FDR judge will have to navigate around, eg earning capacity, income and housing need. Nevertheless a pragmatic solution is generally available. Where the contentious issue is debt, it is suggested that an interested creditor might be invited to attend the FDR in person with the court making *TL v ML* case management directions only where settlement is impossible.

In what circumstances should a creditor intervene?

There are admittedly cases where it is both desirable (FPR Pt 9.26B) and in compliance with the overriding objective (FPR Pt 1.1) that a creditor is joined and all parties plead their cases towards a preliminary hearing, although it is suggested that these will be few in number. These will generally involve a debt sufficiently large to warrant the outlay of costs but also may involve significant legal issues. As with issues of beneficial interest, in determining the existence and 'hardness' of a debt owed to a joined third party, the court applies the general common law and does not perform a discretionary exercise. As Hughes LJ (as he then was) noted in *Goldstone v Goldstone* [2011] EWCA Civ 39, [2011] 1 FLR 1926 at para [66]: 'It is salutary for family practitioners to keep the distinction clearly in mind.'

Where a loan is properly documented, or otherwise can be proven to the court's satisfaction it will assist a spouse little to assert that it would be 'unfair' to honour its terms. Rather, the question may be: is the loan document fraudulent or is it otherwise a sham. As the President of the Family Division has underlined in *A v A* [2007] EWHC 99, [2007] 2 FLR 467 at para [21] (then as Munby J):

> '. . . what it is important to appreciate (and too often, I fear, is not appreciated at least in this division) is that the relevant legal principles which have to be applied are precisely the same in this division as in the other two divisions. There is not one law of "sham" in the Chancery Division and another law of "sham" in the Family Division. There is only one law of "sham", to be applied equally in all three Divisions of the High Court.'

The court's powers in such circumstances

Where a creditor is joined as an intervener, and the court is satisfied on the balance of probabilities that a debt should be repaid, the court can enter judgment. It can proceed to order how the debt is repaid and consider what (if any) interest is owing. The court does not have the power of adjusting the amount of the debt (there is no civil equivalent to a property adjustment order) and, since the court's TOLATA jurisdiction is not exercised in respect of a debt, it is doubtful if the court should proceed to make declarations in respect of the debt.

Conclusion

Pulling the threads together, in most cases it should not be necessary to join the bank of mum and dad:

(1) *TL v ML* is not authority for the proposition that a creditor such as a family member should be joined as an intervener for the hearing of a preliminary issue.

(2) In most cases where a family member purports to call in a debt, can attend court as a witness, and the court can deal with the alleged debt indirectly (ie included within a lump sum paid to one of the parties upon their undertaking to pay the creditor). While this is not a perfect solution, and may involve the issue being 'live' at the FDR, it avoids the often ruinous cost of an intervention.

(3) The court has a discretion to join an intervener in respect of an issue other than beneficial ownership of a property, however it is suggested this should be exercised sparingly.

(4) Bearing in mind the costs and delay of a third party intervening, the requirements of FPR Pt 9.26B (5) should not be overlooked. The rules require that a prospective intervener should make a Pt 18 application, supported by evidence. The possibility of a party being joined without an application (FPR Pt 9.26B(4)) should be the exception rather than the rule.