

Specialist Debt Advice Service

Spotlight

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Cars on Hire Purchase (HP) in Bankruptcy

This month's Spotlight discusses how cars on Hire Purchase (HP) might be viewed in bankruptcy by the Official Receiver and what a debtor may need to consider before applying for bankruptcy.

Insolvency termination clause

Most HP and conditional sale agreements include an 'insolvency termination clause' under which the finance company may terminate the agreement if the borrower goes bankrupt, gets a debt relief order, or enters an individual voluntary arrangement. This is subject to the restriction at s90(1) Consumer Credit Act 1974 that a court order is required where one third or more of the total purchase price has been paid.

Usually, the finance company will not take action under this clause if there are no arrears and the borrower continues to make contractual payments. However, this should be checked with the finance company in advance. If the finance company is minded to terminate the agreement, they may, as an alternative, agree to the agreement being transferred into an acceptable third party's name, so this is something that might be explored.

Is the car an asset?

The finance company retains ownership of a car under an HP agreement until all the payments, including any optional purchase fee, have been paid. Where the value of the car, less selling costs, would be enough to settle the outstanding finance and leave a surplus, the Official Receiver would consider selling the car and settling the finance agreement to raise monies for the bankruptcy estate. In practice, because of the speed at which the value of a car deteriorates, there will not often be a surplus after a car is sold and the finance repaid.

Is the car an exempt asset?

Amongst the items that may be exempted from a bankruptcy estate are motor vehicles that are necessary for the personal use of the bankrupt in their employment, business or vocation, in seeking employment and/or where the vehicle is necessary to meet a basic domestic need of the bankrupt and their family.

However, following the Court of Appeal decision in *Mikki v Duncan* [2016] [EWCA Civ 1312](#) it would not be possible for the client to claim their benefit in the agreement as an exempt asset. This is because the court held that an interest in an agreement cannot be an exempt asset as defined by s283(2) Insolvency Act 1986:

“(a) such tools, books, vehicles and other items of equipment as are necessary to the bankrupt for use personally by him in his employment, business or vocation;

(b) such clothing, bedding, furniture, household equipment and provisions as are necessary for satisfying the basic domestic needs of the bankrupt and his family.”

Therefore, the question of whether a car is an ‘exempt asset’ is not, directly relevant where it is subject to an HP or conditional sale agreement. The car is not the asset of the bankrupt and their interest in the agreement is not capable, in law, of being exempt.

Will the Official Receiver allow the client to keep the car?

If the HP agreement offers no value to the bankruptcy estate, the Official Receiver is likely to disclaim it.

Third party payments

The Official Receiver is unlikely to object to a third-party making payments to the agreement should this be possible.

Income payment agreement or order (IPA/O)

Unless a bankrupt has 'benefit only' income, the Official Receiver will wish to consider the possibility of making an IPA/O.

IPA/Os are provided for by [s310 and 310A Insolvency Act 1986](#) and the relevant procedures are set out from [Rule 10.108 The Insolvency \(England and Wales\) Rules 2016](#). They will normally last for a period of three years, so will continue beyond discharge. S310(2) of the Act provides that:

“The court shall not make an income payments order the effect of which would be to reduce the income of the bankruptbelow what appears to the court to be necessary for meeting the reasonable domestic needs of the bankrupt and his family.”

So, the question becomes one of whether the ongoing HP repayments, along with the other expenses involved in running the car, are a 'reasonable domestic expense'. Clearly, each case will turn on its own merits and there will inevitably be a good deal of subjectivity involved. There is no specific guidance to Official Receivers as to when car HP payments and related expenses should be allowed but Insolvency Service guidance, generally, is that: “An assessment should be made as to whether the expenditure claimed is realistic, relevant and appropriate to the bankrupt's circumstances.” The Standard Financial Statement is used as the basis for this discussion.

The word “necessary” in s310 is instructive – the Official Receiver is likely to consider whether the use of taxis and/or public transport would be a viable alternative and cost less? A client will need to be prepared to argue that use of a car is not just convenient – it is **necessary** – and the HP and other car expenses are, therefore, a necessary domestic expense.

Where it is not possible to come to an agreement, the Official Receiver may apply to court for an IPO. Insolvency Service guidance to Official Receivers is to always try to come an agreement first, and Official Receivers are generally reluctant to apply to court – there is additional cost and work involved and unless the bankrupt is being clearly unrealistic there is no certainty of outcome. In practice, this means there is likely to be some scope for negotiation regarding the amount of any IPA or whether one is put in place at all.

After-acquired asset

You should consider whether the effect of a third-party, or your client making payments to the agreement would be to create an after acquired asset before discharge, which could then be pursued by the Official Receiver.

Insolvency Service guidance to Official Receivers

The Insolvency Service guidance to Official Receivers (which has replaced the Technical Manual) on dealing with motor vehicles can be found at [Chapter 27](#) of their guidance and the guidance on income payment agreements and orders can be found at [Chapter 35](#). This information is currently available on the 'What do they Know' website but is expected to be published as part of GOV.UK in January 2021.