

The complaint

Mr H has complained about The Royal Bank of Scotland Plc (RBS) using redress from a mis-sold payment protection insurance (PPI) policy to repay a debt, on the basis that the debt was written off in a sequestration.

What happened

Mr H, in his capacity as a sole trader, had a PPI policy on his RBS business overdraft. Mr H went through a sequestration, so his overdraft debt was written off, and a portion of the arrears remained unpaid. In total, around £200,000 of debt was left unpaid to RBS.

Mr H later complained about the sale of the PPI. RBS agreed it had been mis-sold and offered to redress this. This came to about £6,000. They explained that if Mr H had been subject to insolvency, they would pay the redress to the relevant account first – the redress was first subject to the clearance of any arrears.

Mr H accepted this offer, and RBS set off the PPI compensation – using it to clear some of the £200,000 or so of arrears that went unpaid in the sequestration.

Mr H complained. His representative argued that the redress was due to Mr H directly, as he'd been discharged from the sequestration years ago, therefore there were no arrears to set off against.

Our adjudicator looked into things independently and thought RBS had acted fairly in setting off the redress. Mr H disagreed with the adjudicator's opinion, so the complaint's been passed to me to decide.

What I've decided – and why

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

I should first explain that our service was set up by Parliament to resolve cases informally, based on what is fair and reasonable. Of course, we take into account the relevant law, regulations, and good industry practice to help us come to our conclusions. But the overarching principle is fairness. Indeed, I am able to depart from the law where I find that fairness demands I do so.

So I have taken into account the legal arguments from Mr H's representative, and I am grateful that he set them out clearly. But the crux of my decision is based on what's fair – which takes into account the law, but is not exclusively based on it.

In terms of the legal position, I acknowledge the representative's argument that on the discharge of the sequestration, Mr H was discharged of all his debts and obligations.

With that said, I also note that when someone's estate is sequestrated, their assets are vested – i.e. transferred to – a trustee for the benefit of their creditors. For Mr H, this would have included his right to redress for the mis-sold PPI, which formed an asset that was transferred to his trustee. It was property in the sequestration. That it was only discovered afterwards doesn't change that.

It is possible for Mr H's discharged trustee to apply to the court to be re-appointed, so that he can either distribute the compensation among Mr H's creditors or – more likely – adjudicate a reformulated claim by RBS which includes a "balancing of accounts in bankruptcy". The principle of balancing of accounts in bankruptcy would allow RBS to set off any debts against the bankrupt's claim.

I don't know what a court might do in Mr H's case – it's possible it may decide to effectively undo his discharge, or it's possible it may decide not to do so. But the point is that I don't agree the compensation is necessarily payable to Mr H directly. It's possible it could be paid to the trustee to distribute amongst the creditors, or kept by RBS to reduce the amount that was left unpaid.

But even if I accept the legal arguments of Mr H's representative, as I said before I must apply an overarching test of what is fair and reasonable in the circumstances of the case. And I think it's fair for RBS to use Mr H's PPI redress to reduce the money left unpaid when he was discharged from the sequestration.

When two parties owe each other money, it seems only fair that they each pay what they owe. While RBS owed Mr H about £6,000 for mis-selling PPI, Mr H left unpaid arrears of about £200,000 that he'd owed to RBS from the same period in the same capacity. So it seems both fair and practical to use one debt to reduce the other.

I'll put it another way. Let's imagine a situation where Mr H owed someone money, and they also owed him a much larger amount of money. I don't think Mr H would feel it was fair if the other person never repaid their debt to Mr H, but Mr H was still forced to repay his debt to them – even if that other person had since been insolvent.

And while of course I accept that Mr H was discharged from his sequestration, it did not mean that the underlying debt got repaid to RBS. And the amount left outstanding after the sequestration was very significant, and far larger than the PPI redress.

I have also taken into account that Mr H's sequestration ended some years ago, and that there are arguments to be made about the time that's passed. But then his PPI redress comes from premiums which were charged even longer ago than that. So if I were to find that RBS were dealing with money owed from too long ago, I'd surely have to fairly say that Mr H was *also* pursuing money owed from too long ago.

Another key point is that when a PPI policy has been mis-sold, we tell businesses to put their customers in the financial position they'd be in now had the policy never been sold – as far as it's possible to do that. Here, had Mr H's overdraft PPI not been sold, then he would not have an extra £6,000 or so now. Instead, his debt would've most likely been about £6,000 smaller going into the sequestration as the PPI premiums would never have been added to his overdraft balance. So it makes the most sense to use the PPI redress to reduce Mr H's unpaid debt in line with what it would've most likely looked like without PPI. Doing so more effectively puts Mr H in the financial position he would've been in but for the PPI.

Further, the PPI premiums would have been charged to Mr H's overdraft, meaning a portion of them would have most likely been written off in the sequestration. Because of the time that's passed, statements are no longer available to show how many premiums were or were not left unpaid. But it means there were most likely premiums that Mr H never actually paid for with his own money – instead, they were added onto the balance and later written off. And it certainly wouldn't seem fair for RBS to have to give Mr H a "refund" of any premiums which by all accounts he never paid in the first place.

Lastly, thinking about what *should* have happened, ideally Mr H's trustee should have pursued the PPI claim before discharging him. While the trustee may not have known about the potential claim at the time, it was nonetheless erroneous to overlook an asset – it was supposed to have been either passed to RBS to set off against or otherwise distributed amongst all of Mr H's creditors. It was not supposed to have been paid to Mr H directly. So again, had things happened as they should have in that sense, Mr H still would not have received the PPI redress directly.

So while I know that this will come as a disappointment for Mr H, and while it is not my intention to disappoint him, I don't think I can fairly tell RBS to pay the PPI redress to him directly when there was a much larger debt left outstanding from the same period in the same capacity.

My final decision

For the reasons I've explained, I think The Royal Bank of Scotland Plc settled Mr H's PPI claim in a fair way. I make no further award.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mr H to accept or reject my decision before 20 March 2023.

Adam Charles
Ombudsman