GOUGH SQUARE CHAMBERS' CONSUMER CREDIT COLUMN: APRIL 2016

James Ross, Ruth Bala, Thomas Samuels and Lee Finch are all specialist consumer credit counsel at Gough Square Chambers. On a regular basis, they share their views with Practical Law Financial Services subscribers on topical developments or key issues relating to consumer credit.

In the April column, Thomas Samuels considers the impact of the replacement of the old extortionate credit bargain test with the unfair relationship provisions at sections 140A-C of the Consumer Credit Act 1974 (CCA).

Thomas Samuels, Gough Square Chambers

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UNFAIR RELATIONSHIPS: A REVIEW

Introduction

The Consumer Credit Act 2006 (CCA 2006) has just had its tenth anniversary, having come into force on 30 March 2006.

Consumer credit legislation was the subject of criticism before the CCA 2006. Indeed, as far back as 2002, the Court of Appeal stated that:

> "Simplification of a part of the law which is intended to protect consumers is surely long overdue so as to make it comprehensible to layman and lawyer alike. At present it is certainly not comprehensible to the former and is scarcely comprehensible to the latter" (*McGinn v Grangewood Securities Ltd [2002] EWCA Civ 522, at [1]*).

However, the CCA 2006 in fact marked the start of a trend in the opposite direction, being the first in a series of major changes over the last decade that have led to the current complex web of regulation. Perhaps its greatest innovation was the replacement of the old extortionate credit bargain test with the unfair relationship provisions at sections 140A-C of the Consumer Credit Act 1974 (CCA). This column considers the impact of that amendment.

Extortionate credit bargain versus unfair relationship

The old extortionate credit bargain test (at section 138 of the CCA) related to the cost of the borrowing, that is whether the parties' bargain was "grossly exorbitant" or "otherwise grossly contravene[d] the ordinary principles of fair dealing." It considered whether the consumer was being taken advantage of in financial terms but did not extend to other potential sources of unfairness. Moreover, the threshold for establishing an extortionate credit bargain was noted to be "a high one" (*Broadwick Financial Services Ltd v Spencer [2002] 1 All ER (Comm) 46*). As a result, there were only very few successful extortionate credit bargain challenges.

The unfair relationship provisions came into force on 6 April 2007 and applied to all new and existing agreements unless they became "completed" (such that no sum was or would become owing) during the 12 month transitional period which followed (schedule 3, paragraphs 14(1)-(3), CCA 2006). Their intended purpose was to give the courts a more flexible tool to redress unfairness in the parties' relationship, as reflected by the language of section 140A(1) of the CCA, which allows the court to consider one or more of the following:

- Any of the terms of the agreement or of any related agreement.
- The way in which the creditor has exercised or enforced any of their rights under the agreement or any related agreement.
- Any other thing done (or not done) by, or on behalf of, the creditor (either before the making of the agreement or any related agreement).

Further, section 140A(2) of the CCA states that the court "shall have regard to all matters it thinks relevant" in assessing the fairness of the relationship.

As was the case under the old extortionate credit bargain test, the unfair relationship provisions apply to "a credit agreement", meaning any agreement entered into between a creditor and an individual or small partnership. Therefore, even if the agreement between the parties might otherwise be exempt under the CCA, for example credit for business purposes, the debtor is able to claim under section 140A. Notable examples include *Paragon Mortgages Ltd v McEwan-Peters [2011] EWHC 2491 (Comm)* where lending of £30 million to support a buy-to-let enterprise was challenged, and *Deutsche Bank (Suisse) SA v Khan [2013] EWHC 482 (Comm)* in which a "quasi-commercial" £50 million facility was alleged to be unfair on its terms.

Scope of the challenge

Consequently, the scope for challenge has become considerably broader, allowing challenges to be made in a variety of situations from the level of interest rates to inappropriate collections activities. As a result of the generous limitation periods that apply to unfair relationship applications (see *Patel v Patel [2009] EWHC 3417 (QB)*) and the reverse burden of proof under section 140B(9) of the CCA, often a claim which might otherwise be doomed in misrepresentation or negligence is arguable under section 140A of the CCA.

The insertion of section 140A into the CCA coincided with the masse of payment protection insurance (PPI) misselling litigation, and it was in that context that the vast majority of unfair relationship claims were made. Most frequently unfair relationship allegations simply replicated the misrepresentation or breach of statutory duty claim in the hope that the reverse burden of proof would be enough to get the debtor's case home.

Indeed, the leading case of *Plevin v Paragon Personal Finance Ltd [2014] 1 WLR 4222*, arose from an allegation of unfairness as a result of the insurance intermediary's failure to disclosure receipt of commission during the sale of PPI. Lord Sumption noted that

> "...the standard of fairness in a debtor-creditor relationship is a matter for the court, on which it must make its own assessment... An altogether wider range of considerations may be relevant... They include the characteristics of the borrower, her sophistication or vulnerability, the facts which she could reasonably be expected to know or assume, the range of choices available to her, and the degree to which the creditor was or should have been aware of these matters" (at [17]).

Impact of unfair relationship provisions

The unfair relationship provisions have led to a shift of focus from exclusively considering "hard" black-letter law to now taking account of "softer" concepts, with lenders incorporating them into their processes and procedures. For example, pre-unfair relationships, a lender needed only to consider whether a statement might be misleading or whether the documentation conformed to the legislative requirements. Now, however, fairness is a central concept that must be borne in mind throughout the parties' relationship. As illustrated by *Plevin*, compliance by a lender with its legal obligations may not be enough to defend an unfair relationship application.

Indeed, some of these softer legal concepts have now been incorporated into the FCA's rules in its Consumer Credit sourcebook (CONC). For example, CONC 2.2.3R prevents a firm using a name that might mislead customers as to the nature of the business: the brand-name "EZ Sunshine Loans" for an aggressive sub-prime lender is unlikely to be appropriate, although it falls foul of no traditional hard-edged legal duty. Equally, CONC 7.3.9R prohibits a firm

from refusing to negotiate with a customer in default who is developing a repayment plan. Certainly, pre-unfair relationships, a firm would have been well within its rights to take immediate legal action against a customer in default; any possible comeback would have been by way of an adverse costs order at the conclusion of litigation. However, the unfair relationship provisions have changed the regulatory view of such enforcement, so that now breach of CONC 7.3.9R constitutes a breach of statutory duty (as per section 138D of the Financial Services and Markets Act 2000 (FSMA)).

In short, the unfair relationship provisions have led to a sea-change in the way in which lenders think – or should think – about their interactions with customers.

The future

That said, the influence of the unfair relationship provisions may now be on the wane. The Mortgage Credit Directive (*2014/17/EU*) (MCD) regime came into force on 21 March 2016 and, with it, the majority of new second-charge loans move from regulation under the CCA to regulation under the mortgage regime (embodied within the FCA's amended Mortgages and Home Finance Conduct of Business sourcebook (MCOB)). The consequence is that unfair relationship challenges will no longer be available in relation to secured lending.

Concerns were raised during the consultation process for the implementation of the MCD but were dismissed:

> "On the unfair relationships test, the Treasury decided to switch off the CCA (including the unfair relationships provisions) for second-charge mortgages, and we consider that MCOB 13 provides adequate and appropriate protections for customers in payment difficulties" (FCA policy statement 15/9, at [59]).

Given the scope of the unfair relationship provisions, in particular the reverse burdens of proof and advantageous limitation periods, it might be thought that the FCA's response fell somewhat short.

Challenges to the parties' relationship in the context of second-charge lending has been a key battleground for unfair relationship applications (for example, *Swift Advances plc v Okokenu [2015] CTLC 302*). However, for such business written after 21 March 2016, the unfair relationship route of challenge will no longer exist. This change considerably blunts the force of the provisions, with the result that those lending on security may now breathe a little easier. More fundamentally, it may signal the beginning of the end for the CCA 2006's most fundamental innovation.