

Gough Square Chambers' consumer credit column: August 2020

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

In the August 2020 column, Sabrina Goodchild considers the recent judgment in *Kerrigan v Elevate Credit International Ltd* [2020] EWHC 2169 (Comm). In *Kerrigan*, the High Court clarified that, in a case concerning payday lending, the court will apply different tests for causation as between claims for breach of statutory duty and claims alleging the existence of an unfair relationship under the Consumer Credit Act 1974 (CCA).

Causation in the context of unaffordable payday loans

Introduction

In *Kerrigan v Elevate Credit International Ltd* [2020] EWHC 2169 (Comm), the High Court clarified that, in a case concerning payday lending, the court will apply different tests for causation as between claims for breach of statutory duty and claims alleging the existence of an unfair relationship.

Kerrigan v Elevate Credit International Ltd

In March 2020, HHJ Worster heard a payday lending test case on alleged non-compliance by the lender with its creditworthiness assessment obligations in the context of repeat lending. The borrowing of high-cost short-term credit (HCSTC) by the 12 sample claimants spanned three creditworthiness regimes between 2014 and 2018 (section 55B of the Consumer Credit Act 1974 (CCA), the Consumer Credit sourcebook (CONC), and CONC following the introduction of the HCSTC price cap). It resulted in claims for:

- Breach of statutory duty under section 138D of the Financial Services and Markets Act 2000 (FSMA).
- An order under section 140B of the CCA on the basis that the relationship between the lender and the borrower was unfair to the borrower.

- Negligence in making lending decisions resulting in psychiatric injury to the borrower.

The judgment is wide-ranging and deals with a number of issues including:

- Whether the creditworthiness requirements were breached.
- Causation and loss under the section 138D FSMA claim.
- Whether there exists a duty to take reasonable care in undertaking creditworthiness assessments not to cause psychiatric injury.
- Whether an unfair relationship can be established.

Of particular interest is the view the court expressed on the requirements for causation, both under a claim for breach of statutory duty and under the unfair relationship provisions, in the specific context of payday loans.

Decision on causation

Breach of statutory duty

Having identified systematic breaches of CONC 5, principally by the lender's failure to take into account patterns of repeat borrowing in the course of conducting a creditworthiness assessment, on its face, a claim under section 138D(2) of FSMA for breach of statutory duty arises if the lending was post 1 April 2014. However, that is not the end of the story. Section 138D(2) provides:

"A contravention by an authorised person of a rule made by the FCA is actionable at the suit of a private person **who suffers loss as a result of the contravention**, subject to the defences and other incidents applying to actions for breach of statutory duty" [emphasis added].

The judge found that the usual requirements of causation apply, meaning that a claimant has to prove that any loss suffered was caused both in fact and law by the CONC contravention. In other words, the loss must arise "because the creditworthiness assessment undertaken failed to consider the potential for that loan to have an adverse impact on that borrower's financial situation" [50].

Although causation will need to be determined on a case by case, loan by loan basis, in the context of HCSTC, a number of important general principles were identified by the judge:

- A loan made following a non-compliant creditworthiness assessment may not adversely affect a borrower's financial situation. It may in fact, if proved on the facts, assist the borrower by providing short term finance to deal with a short-term financial crisis [135].
- The loss (that is, the interest) may have been incurred in any event. To establish the same, consideration needs to be given to the following two questions:
 - on the balance of probabilities, if the lender refused an application because it had a CONC compliant creditworthiness assessment, would the applicant have applied to another HCSTC lender? On the sample evidence before the judge, he found that the borrowers would.
 - what percentage of other HCSTC lenders would have lent? This consideration is required to assess the chance that the third-party alternative lender would have acted in such a manner as would have avoided the harm to the claimant. The starting point is to presume that the other HCSTC lenders comply with CONC. The case of *Wright v Cambridge Medical Group* [2011] EWCA Civ 669 was distinguished. This is because, even if the other lenders have a CONC compliant process, they may come to an unimpeachable decision to lend (for example, they may never have lent to that borrower before, so repeat lending is not a relevant consideration) and so the loss would still be incurred.
- The claimant is then left with a claim for loss discounted by the chance that further lenders would grant them a loan in circumstances that did not give rise to another CONC claim. This discount is applicable in the peculiar context of repeat lending breaches. It is in this particular context that the decision of the third-party creditor to lend on the same facts is unlikely to be a breach.

The judge did not specify how the quantification of the chance is to be approached in the circumstances of individual claims. However, his remarks at [201] and [217] about the claimants struggling on causation in their FSMA claims, indicate that the discount is likely to be substantial.

- Once causation is established for one loan, it is a "relatively easy matter" for the borrower to establish causation on the same basis in relation to subsequent loans. This is unless it can be shown that the pattern of borrowing has ended, for example by a lapse of time [132].

The judge further identified the question of whether dishonesty in relation to income and expenditure when making an application intervenes to break the chain of causation. The judge queried whether it mattered that the dishonesty pre-dates the lender's breach of CONC and the loss incurred.

Unfair relationship

In contrast to the position under a claim for breach of statutory duty, the judge clarified that the usual requirements of causation do not strictly apply in a claim alleging the existence of an unfair relationship. Instead, "[t]he court is to have regard to all the relevant circumstances when determining whether the relationship is unfair, and the same sort of approach applies when considering what relief is required to remedy that unfairness" [214].

As with claims barred by limitation, the fact that all necessary elements of a separate claim cannot be proved (for example, causation in the context of a breach of statutory duty claim), is not a bar to proceeding under an unfair relationship claim. This is because the only question there is whether the relationship is unfair. However, the judgment indicates that there may still be some discount to reflect the fact that the claimant would simply have obtained a loan elsewhere, if that is considered fair. The court held (at [216]) that if the relationship is unfair, it is likely "some" relief will be granted to remedy that, noting that here one of the significant distinctions between the FSMA and "unfair relationship" claims becomes apparent. Further, the judge said (at [217]) that "that particular difficulty" (establishing causation of loss) "does not arise (at least not as acutely) in a claim under section 140A".

The judge appeared to see merit in the argument (although conceded that this view was formed without the benefit of argument from counsel) that there should be a "tipping point" approach, such that the fact that the claimants did not benefit from the safeguard of a compliant creditworthiness assessment is sufficient to render the relationship unfair and justify some relief. The path to successfully establishing an unfair relationship

is likely to be smoother than to a claim for breach of statutory duty, with the judge commenting that “the unfair relationship claim [is] a more attractive vehicle for these claims”.

Comment

This case offers important High Court guidance on how basic causal principles apply to complex factual matrices. It is already being relied upon by creditors in the different context of payment protection insurance (PPI) commission non-disclosure trials, where there are currently fierce disputes raging in the county courts about the proper role of a “causal” approach to granting relief under section 140B of the CCA.

However, unfortunately, due to the administration of the lender while awaiting judgment, this test case is not as comprehensive as might have been hoped. None

of the general principles outlined by the judge have been applied to any of the 12 sample claimants and so the detail of how such claims will be determined, particularly in relation to causation and quantum, remains unresolved. This is particularly problematic given the limited value of each individual case.

Further payday lending litigation is listed before the same judge later this year, and it may be that there is a further judgment applying these high-level principles to the facts.

Gough Square Chambers' consumer credit columns

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