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Gough Square Chambers' consumer credit column: May 2021

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Status: **Published on 26-May-2021** | Jurisdiction: **United Kingdom**

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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 May 2021 column, Ruth Bala considers the impact of the recent decision in *Wood v Commercial First Business Ltd and Others and Business Mortgage Finance 4 plc v Pengelly [2021] EWCA Civ 471*. The case concerns the issue of broker "secret commissions".

Broker secret commission post-Wood and Pengelly

The Court of Appeal has recently handed down judgment in *Wood v Commercial First Business Ltd and Others and Business Mortgage Finance 4 plc v Pengelly [2021] EWCA Civ 471*, on the issue of broker "secret commissions". This was another significant loss for the credit industry. David Richards LJ gave the lead judgment (with which the others agreed).

This column analyses the impact of the decision, which is summarised in Legal update, Loan agreements rescinded after brokers' failure to disclose amount of commission (Court of Appeal).

Whether half or fully secret

The classification of a broker commission case as "half secret" (where the fact of commission has been disclosed to the borrower, but not the amount) or "fully secret" has consequences for remedies; it arguably also affects the test for liability.

In both *Wood* and *Pengelly*, the broker's terms and conditions notified the mortgagors that the broker "may" receive fees from creditors with whom it placed mortgages. If the terms had stopped here, then these would have been "half secret" cases (with the wording resembling that in *Hurstanger Limited v Wilson [2007] 1 WLR 2351*). However, the terms went on to promise that in the event commission was paid, the mortgagors would receive notification of the amount. Given the finding of fact that no such notification was received, the court correctly categorised these as fully secret cases.

Cases without broker fee

Cases where the borrowers do not themselves pay any broker fee were not referred to by the Court of Appeal, but they fall within a special category that deserves its own treatment. In my view these should be "half secret" cases, irrespective of whether the terms disclose the fact of commission. The borrower must be taken to understand that the broker will not be working for free and therefore has constructive knowledge of the lender's payment of commission.

Fully secret cases: requisite duty owed by broker

In *Wood and Pengelly*, the Court of Appeal definitively rejected the need for the broker to owe the borrower a fiduciary duty. This is not especially controversial in the context of fully secret cases. In my previous column on the topic, I referred to Slade LJ's three stage test in *Industries and General Mortgage Co Ltd v Lewis [1949] 2 All ER 573* as authority that the claimant need only prove that the broker was his agent (and not necessarily his fiduciary). This is because the claimant is able to rely on the common law causes of action for "money had and received" and fraud, without needing to call upon the equitable cause of action for breach of fiduciary duty.

Post-*Wood and Pengelly*, rather than applying Slade LJ's three stage test, the court should pose the single question formulated by Richards LJ, namely:

- Was the broker under a duty to provide information or advice on an impartial or disinterested basis?

(*Wood and Pengelly* at [48] and [92]).

There is no change in the law on remedies: if the test is satisfied then the borrower is entitled to rescission as of right, subject to his making counter-restitution (at [101]).

Cases where test might be unsatisfied

The width of Richards LJ's test clearly encompasses information-only sales. Not only was the broker in *Wood and Pengelly* acting on an information-only basis, but it had only been engaged to provide information in respect of a single product - the most restricted level of service. As such, there will be few instances where Richards LJ's test is not satisfied.

Examples worthy of litigation are where:

- No broker fee is paid by the borrower.
- The broker has a very detached role (for example, involving no oral conversation with the borrower).
- The broker is tied to a single product/lender.
- The broker's terms and conditions entitle it to make a random selection from its panel of lenders (the Court of Appeal relied at [113] on the fact that in *Wood and Pengelly* the broker's selection from its panel of lenders was not random).

Half secret cases: requisite duty owed by broker

The really interesting question is whether Richards LJ's test should also be applied in "half secret" cases. Those acting for borrowers will stress that Richards LJ at no point qualifies his test by suggesting that it only applied to "fully secret" cases. Nonetheless, *Wood and Pengelly* were "fully secret" cases and so the leading authority on "half secret" cases remains *Hurstanger*, where Tuckey LJ said at [39]:

> "Is there a half-way house between the situation where there has been sufficient disclosure to negate secrecy, but nevertheless the principal's informed consent has not been obtained? Logically I can see no objection to this. Where there has only been partial or inadequate disclosure but it is sufficient to negate secrecy, it would be unfair to visit the agent and any third party involved with a finding of fraud and the other consequences to which I have referred, or, conversely, to acquit them altogether for their involvement in what would still be breach of fiduciary duty unless informed consent had been obtained."

The other Court of Appeal "half secret" cases are *McWilliam v Norton Finance (UK) Limited t/a Norton Finance in liquidation [2015] CTLC 60*, where Tomlinson LJ opened his judgment with the remark, "This appeal raises the question whether a credit broker ... owed to its consumer clients ... a fiduciary duty" and *Medsted Associates Ltd v Canaccord Genuity Wealth (International) Ltd [2019] EWCA Civ 83*, where Longmore LJ said (at [29]) "The question, for present purposes, is whether that relationship was a fiduciary one".

In *Wood and Pengelly*, Richards LJ appears to accept, reluctantly, that *Hurstanger* is binding authority that a fiduciary duty is required in "half secret" cases. When considering *McWilliam and Medsted Associates*, he acknowledges that, applying *Hurstanger*, a fiduciary relationship was necessary for the borrowers to succeed because those were "half secret" cases (at [84] and [88]).

When considering *Commercial First Business Ltd v Pickup and Vernon [2017] CTLC 1* (a High Court "half secret" case), Richards LJ said it was wrongly decided because the broker's involvement "was sufficient to impose a fiduciary duty on the broker, in the limited sense in which that term is used in that context" (at [125]). The "limited sense" remark reflects Richards LJ's preference for ditching the concept of fiduciary duty altogether, in both fully and secret commission cases. Nonetheless, anything said about "half secret" cases in *Wood and Pengelly* is obiter and the *Hurstanger* line of cases survives.

Equally, Richards LJ's unhelpful comment about any term disclosing the fact of commission needing to be expressly drawn to the borrower's attention (at [120]) is obiter and purports to introduce an additional requirement into half-secret cases that does not derive from the *Hurstanger* line of cases.

It has been widely assumed that the Court of Appeal's judgment in *Wood and Pengelly* sounds the death knell for creditors defending broker commission claims. However, the impact of the judgment will be diluted if it can be properly confined to fully-secret cases.

Gough Square Chambers' consumer credit columns

For previous consumer credit columns written by barristers at Gough Square Chambers, see Practice note, Gough Square Chambers' consumer credit column.