GOUGH SQUARE CHAMBERS' CONSUMER CREDIT COLUMN: NOVEMBER 2019

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In the November 2019 column, James Ross considers the issue of credit broker commissions in the light of the recent judgment in *Wood v Commercial First Business Ltd (in liquidation) [2019] EWHC 2205*.

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THE WORST-KEPT SECRET IN CONSUMER CREDIT

Borrowers and lenders are often introduced by credit intermediaries called brokers. Such brokers are almost universally paid commissions by the lenders to whom they introduce business. Sometimes such payments are not disclosed to borrowers and are described as "secret commissions" or bribes. Sometimes the existence, but not the amount of such payments, is disclosed and they are described as "half secret". It can be difficult to define the legal obligations owed by the broker to the borrower and/or the lender in these various scenarios. That difficulty has increased with the decision in *Wood v Commercial First Business Ltd (in liquidation) [2019] EWHC 2205*, the transcript of which has recently become available.

Is a credit broker the agent of the borrower or the lender?

Although a credit broker is often described as the borrower's "agent", a broker in the consumer credit context is rarely a "full-blooded" agent in the sense of being able to alter the borrower's legal relationship with the lender, for example by signing the credit agreement on behalf of the borrower. Similarly, although a broker will usually have an existing relationship with a number of lenders, often allowing the broker access to underwriting criteria and even a stock of physical forms, the broker will not in any real sense act as "agent" on behalf of the lenders it deals with. In *Plevin v Paragon Personal Finance Ltd and another [2014] UKSC 61*, it was held that the broker did not act as the agent "on behalf of" the lender for the purposes of the unfair relationships provisions in sections 140A-D of the Consumer Credit Act 1974 (CCA). The court went on to find that the broker actually acted as the agent of the borrower, to the extent that the broker performed the function, however defectively, of advising the borrower on the suitability of the product. However, it is submitted that the court was not suggesting that the broker was the borrower's "full-blooded" agent in the sense that the borrower would be legally responsible for the broker's acts or omissions.

Usually, a broker is a mere intermediary or conduit with the borrower's authority only to pass on the borrower's details and completed application documentation to the lender. The broker may provide further services, such as advising the borrower on the most suitable loan product and/or lender in the market or within a more limited panel. Where such advice is given to a borrower, the broker will usually have an obligation to take reasonable care to ensure the suitability of that advice, but will not thereby become the borrower's "agent" other than in a very general sense.

Does a credit broker owe fiduciary duties to the borrower?

The key area in which confusion has arisen in recent years relates to fiduciary duties owed by brokers to borrowers. A fiduciary is someone who has undertaken to act for, or on behalf, of another in a particular matter in circumstances which give rise to a relationship of trust and confidence. The distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to the single-minded loyalty of their fiduciary (see, for example, *Bristol and West Building Society v Mothew [1998]* Ch 1 at 18). It is not sufficient that a person may be described as an "agent" or has given advice to the other party. Instead, the court must meticulously examine the facts in each case to determine whether there has been a "crossing of the line" such that the agent or advisor is not merely required to act with reasonable care and skill, but owes the special duties that arise when a principal is entitled to expect that a fiduciary will act in the principal's interests to the exclusion of the fiduciary's own interests. The correct approach is to determine whether a fiduciary duty has arisen and only then to consider whether there has been a breach of the duty (see *Lloyds Bank plc v Bundy [1975] 1 QB 326*).

Wood v Commercial First

In *Wood v Commercial First Business Ltd*, the broker's terms stated:

> "We [the broker] may receive fees from lenders with whom we place mortgages. Before you take out a mortgage, we will tell you the amount of the fee in writing. If the fee is less than £250, we will confirm that we will receive up to this amount. If the fee is £250 or more, we will tell you the exact amount."

There was no evidence at trial that the broker subsequently informed the borrower of the amount of any fee it would receive from the lender. The judge therefore concluded that the broker had made an implied representation that no commission had been paid, such that the commission was entirely secret (para 135). The judge then went on to state that, having found that the relevant payments were secret commissions, there was no need to consider whether the broker owed any fiduciary duty or whether there had been a breach of that duty (para 142).

It is submitted that this approach is incorrect. The payment of a secret commission only has legal relevance if the recipient is a fiduciary. As explained in the *Bundy* case, the correct approach is first to give meticulous consideration to all the facts to determine whether there is a fiduciary duty, and only then to consider whether has been a breach of that duty (such as receipt of a secret commission).

With respect, the decision in the *Wood* case is difficult to follow. If it is based on the suggestion that the borrower was entitled to receive impartial advice from the broker, surely the question of whether the subsequent commission payment was secret or not is irrelevant, since by that time the advice had been given and relied upon by the borrower. The real criticism (if any) to be levelled at the broker is that it had already entered into an arrangement under which lenders had agreed to make future commission payments under certain circumstances, thereby giving rise to an inherent conflict of interest in the broker's role. But that is not something of which the borrower could complain. She was informed that such commission payments might be made but proceeded with the transaction regardless. The fact that the broker had existing relationships with lenders was presumably the very reason she approached the broker in the first place.

The judge went on to make the following finding at paragraph 130(8):

> "I also find that those cases which suggest that where there is upfront disclosure to the principal of the fact that the agent is to receive a fee from a third party, the principal cannot expect the undivided loyalty of the agent such that no fiduciary relationship can exist (Pickup and Vernon and, to a certain extent, the county court case of Sealey and Winfield) are, with respect, wrong. As stated above, this puts the cart before the horse. The correct analysis, so it seems to me, is not that such disclosure of the proposed payment to the agent by the third party negates the existence of a fiduciary relationship – instead, it merely prevents there being a breach of any underlying fiduciary relationship."

For the reasons set out above, it is the judgment in the *Wood* case that puts the cart before the horse. If there is upfront disclosure to the principal of the fact that the agent is to receive a fee from a third party, this should be of

central - even decisive - importance when considering whether the principal was entitled to expect that the agent will act in the principal's interests to the exclusion of the agent's own interests. Where a borrower approaches a broker in an industry where the universal practice is that lenders will pay broker commissions, and the broker discloses this upfront, why should the borrower later be entitled to claim that the broker has somehow been disloyal merely because the amount of commission was not later disclosed?

In light of the clear conflict between the decisions in *Commercial First Business Ltd v Pickup & Vernon* [2017] CTLC 1 and *Commercial First v Wood*, it is to be hoped that the Court of Appeal will have the opportunity to resolve this issue sooner rather than later.

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