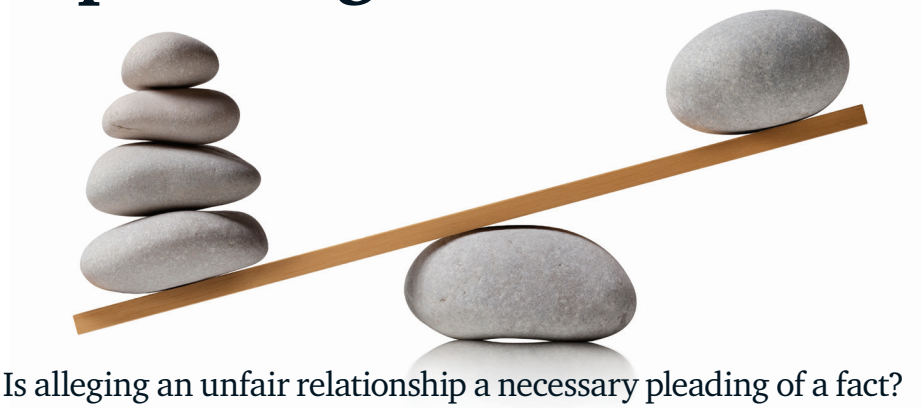
Unfair relationships & pleadings of fact



Is alleging an unfair relationship a necessary pleading of a fact? Fred Philpott examines a recent judgment of the High Court

IN BRIEF

▶ In *Goldhill Finance Ltd v Smyth*, a borrower lost her house on a pleading point because in the county court there was no specific allegation of an unfair relationship, despite fairness having been raised in her original statement.

In what may be seen by some as an unsatisfactory case, a county court judge ruled that the unfair relationship provisions of the Consumer Credit Act 1974 (CCA 1974) only applied if the agreement was regulated. He therefore did not consider the unfair relationship provisions because he was not asked to do so. The case went to appeal in the High Court (*Goldhill Finance Ltd v Smyth* [2023] EWHC 362 (KB)).

The background

The case involved a bridging loan over six months with interest at 2% per month simple but on default 5% per month compound. The borrower had signed declarations which had the effect (if true, which they were not) of the agreement being unregulated. It is an important part of the consumer credit regime that the unfair relationship provisions in s 140A-C, CCA 1974 apply even if (with one exception) the agreement is unregulated if it is with an individual, as was the position in respect of extortionate credit bargains before the Consumer Credit Act 2006. That this was not the basis of the county court decision was the result of the borrower being a litigant in person at the outset, her counsel being instructed at the last minute, and the lender taking a pleading point. The facts and procedural history of the case are of obvious importance in understanding how the result came about.

The facts

Ms Smyth lived in a residential property with her two young children. She had a first mortgage and took the six-month bridging loan for the sum of £50,000 with six months' interest rolled up being £16,978. This was in September 2018 and at the trial the total outstanding was said to be about £250,000 (this was in June 2021); at the time of the appeal (November 2022), it was approximately £740,000.

The proceedings

In response to a standard form claim for possession, Ms Smyth filled in a response form for mortgaged residential premises (form N11M). In response to the question: 'Do you want the court to consider whether or not the terms of your original loan agreement are fair?', she replied 'Yes'. However, for some reason, this question is said to be answered only if the loan was a regulated consumer credit agreement.

She attached a statement (which the High Court judge agreed formed part of the 'defence') which said: 'I would ask the court to examine if the terms of the loan were fair.'

Moving forward, the High Court held that this did not raise the issue of unfair relationships, for the reasons I will set out below.

The lender's reply to the defence was that the borrower had signed a declaration that she would not have the benefit of the protection and remedies under the Financial Services and Markets Act 2000 or CCA 1974 if this were a regulated agreement under those Acts. The reply made no reference to the caveat to that declaration that this would not oust the unfair relationships provisions. The declaration was that the loan was for business purposes and that the borrower would not be using more than 40% of the property as a residence for her or her family.

On a factual basis, there is no doubt that Ms Smyth was using and intended to use the property as a residence for her and her children. It was accepted at trial that there was no evidence to support the case that the lender knew or suspected that the declaration was untrue. It is, perhaps, unfortunate that, leaving the case under consideration aside, a number of lenders who are not authorised are using such declarations in order to lend money to people desperate for funds and who will sign anything. On appeal to the High Court, it was not challenged that the declaration was effective and therefore the agreement was unregulated.

There was an initial hearing which recited the issues, including the 'fairness of the agreement'. Again, this was held on appeal not to raise the unfair relationship provisions.

There was another hearing and a case summary drafted by counsel for the lender, which included: 'If the loan is regulated, then were the terms fair?'. A position statement drafted by counsel for Ms Smyth alleged that 5% was 'extortionate and grossly exceeds the principles of fair dealing' (one sees here an echo of the test for an extortionate credit bargain under the former provisions replaced by the unfair relationship provisions).

The position statement expressly said that the unfair relationship provisions apply, but this was held to be insufficient because the position statement was not a pleading.

When counsel for the lender read this, he made the point that the pleadings did not refer to an unfair relationship, and that any application to amend the pleadings would be resisted. There was no application.

The county court trial

Judge Gerald in the county court said that the issue was whether the agreement was regulated, and if so, were the interest rates reasonable. Neither counsel took issue with this, and the judge concluded that the agreement was not a regulated mortgage contract within CCA 1974 and therefore it was 'not necessary to consider the fairness or otherwise of terms'. He expressly said: 'the agreement was not a regulated mortgage contract and therefore falls outwith the provisions of [CCA 1974] and can be enforced free of statutory restrictions.'

The appeal

Other counsel were instructed on behalf of Ms Smyth on the appeal to the King's Bench Division. The issue was that of unfair relationships (with an additional point alleging penalty).

Mr Justice Soole did not accept that the form and the statement expressly or by implication raised an unfair relationship allegation. The terms were said to be unfair, not the relationship, although it was accepted that s 140A(1)(a), CCA 1974 refers to terms.

The judge continued by finding that:

- the case summary 'put beyond doubt that the issue of fairness did not arise for consideration if the loan were held to be regulated' (it is assumed that the word should have been 'unregulated');
- the judge's so-called error of law in referring to 'outwith' the statutory provisions was only on the basis of the agreed issues. It was not accepted that counsel for the lender should have intervened because that statement by the judge was made in the context of the pleaded case;
- the issue of unfair relationship was therefore a new point which could not now be taken on appeal; and
- as to penalty, the judge need not of his own motion have raised the point (if a term is a penalty, then it is on the basis that the term is contrary to public policy which a court may raise of its own motion). Notwithstanding *Cavendish Square Holding BV v Talal El Makdessi* [2015] UKSC 67, it is more than arguable that an uplift from 2% per month simple to 5% per month compound is a penalty. Interest rates in 2018 were almost nominal. Contrast the extortionate credit bargain case of *Ketley (A) Ltd v Scott* [1981] ICR 241 which upheld a rate of 48% per annum on a bridging loan when the bank rate was 10%.

The result is that, unless further appealed, Ms Smyth and her children will lose their home because of a secured debt for what must be now in excess of £0.75m on a loan of £50,000. They will do so because in the court below there is no specific allegation of an unfair relationship, despite fairness having been raised in Ms Smyth's original statement with her response form.

Pleading points

Issues regarding pleadings are a useful judicial tool. The importance attached to them may be dependent upon the merits or otherwise of any particular case. Over the years there has been a distinction between a judge's response on a pleading point being to say 'Mr X, it is not pleaded', or 'Miss Y you are not taking a pleading point are you?' The latter often said with some distaste.

Numerous cases have considered the importance of pleading. Most recently, *National Highways Ltd v Hubble* in Manchester County Court (13 January 2023) (at paras [70] to [75]) dealt with motor vehicles damaging highway furniture. The judge in that case referred extensively to the authorities on pleadings, including *Charles Russell Speechlys LLP v Beneficial House (Birmingham) Regeneration LLP* [2021] EWHC 3458 (QB) which cited in particular the case of *Boake Allen Ltd & others v HMRC* [2006] EWCA Civ 25 where Lord Justice Mummery said: 'While it is good sense not to be pernickety about pleadings, the basic requirement that material facts should be pleaded is there for a good reason.' One can contrast the case under consideration with the approach by counsel (para [211]) in *Boston Trust Company Ltd and another v Szerelmey Ltd and others* [2023] EWHC 308 (Ch), where it was said that 'he was taking no pleading point' and the matter should be tackled on its merits.

Is alleging an unfair relationship a necessary pleading of a fact? Undoubtedly it should be raised (see *Carey v HSBC Bank plc* [2009] EWHC 3417 (QB)). But is it essential to use the expression 'unfair relationship'?

Conclusion

The result came about because Ms Smyth was acting in person for much of the time; her counsel was instructed very late and the judge was (obviously unintentionally) led into concluding that, if unregulated, the unfair relationship provisions do not apply. NLJ

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