Guildhall CHAMBERS

Newsletter

COMMERCIAL NEWS SPRING 2010

EDITORIAL

Welcome to the Spring Commercial Newsletter. If you have not visited Chambers recently you will not have had the benefit of seeing the fruits of our refurbishment and extension programme at 5 to 11 Broad Street. This comprises substantially larger conference and meeting facilities, a new reception area, a new clerks' room (in the old Hammicks Legal Bookshop), together with increased facilities for barristers and staff. We hope to see you soon.

This issue includes discussion of the thorny issue of incorporation of contractual terms by Hugh Sims. If that vital signature is not obtained, the parties will be thrown back on arguments based on reasonable notice or course of dealing. Hugh discusses a recent discussion of the Bristol Mercantile Court on the latter test. The banks have had a fortunate escape from the clutches of the bank charges litigation, thanks to the decision of the Supreme Court in *Office of Fair Trading v Abbey National*. Nevertheless the Consumer Credit Act litigation industry shows no signs of abating, and recent test cases are expertly described by Ross Fentem. At the same time, the Consumer Credit Act faces another overhaul in mid-2010 to implement the Consumer Credit Directive, which Lucy Walker provides an update on. Last, but not least, Malcolm Warner considers recent shenanigans in respect of exit provisions in partnership deeds.

If you have any queries about this Newsletter or the Guildhall Commercial Team please do not hesitate to contact me, or Dan Cuthbertson, the Team Clerk.

Gerard McMeel

IN THIS ISSUE

COMMERCIAL LAW UPDATE
CONTRACT TERMS AND INCORPORATION:

Course of dealing and borderline cases

It is trite law that standard contractual terms may be incorporated into a contract through a "course of dealing". What is not so easy to see or to say is when, in fact, the parties trading relationship becomes sufficiently established so that it can be said there has been a sufficient course of dealing for the rule to apply.

One or two trades will clearly not be enough (though that is not to say standard terms may not be incorporated in those circumstances; they may be incorporated other than through a course of dealing). On the other hand, double figures, depending on the period in question, tends to suggest you are past the line, and the rule is likely to apply. But how about four, or five, within a six month or one year period? This "grey area" came before the Bristol Mercantile Court for consideration in *Capes (Hatherden) Ltd v Western Arable Services Limited* [2009] EWHC 3065 (QB) QBD (Merc) (Bristol) (Judge Havelock-Allan QC).

The facts in *Capes (Hatherden) Ltd v Western Arable Services Limited*

The claimant, a farming company, issued proceedings for debts and/or damages arising from two contracts for sale of malting barley to the defendant, a grain trader. The defendant issued an application to stay the proceedings under section 9 of the Arbitration Act 1996 which, if applicable, requires the Court to stay proceedings in favour of contractually agreed arbitration. The grounds for the stay application were that the defendant's contract notes, issued shortly after the key terms of the contract had been agreed orally over the telephone, incorporated reference to certain industry standard terms (AIC Contract No 1/04 for grains and pulses, the "AIC" being the Agricultural Industries Confederation Limited), and those terms contained an arbitration clause. Accordingly the issue for the Court was whether there had been a sufficient course of trading such that, in relation to the two contracts in issue, the AIC standard terms applied. The parties had entered into four contracts before the two contracts in issue, the last one being 5 months before the first of the two contracts in question. In each contract the same procedure was followed: an oral agreement as regards the key terms, following by a confirmatory contract note containing reference to the AIC standard terms. The claimant's managing director, who was a party to the telephone conversations, gave evidence confirming he was unaware of the reference to the AIC standard terms, which was in relatively small print at the foot of the contract notes, and that in any event he did not know who the AIC was or where he could find the terms, though he accepted that he did subsequently find the terms on the AIC website after the dispute had arisen.

The test for incorporation is of course an objective one: what did each party, by his or her words and conduct, lead the other party to believe were the liabilities he was accepting, and the concomitant rights he was granting?

The judge, conducted an illuminating review of the authorities, including *McCutcheon v McBrayne, Hardwick Game Farm, Hollier v Ramble Motors, British Crane Hire Corporation, SIAT* and *Circle Freight*. He concluded that the facts were right on the borderline. He considered that if there had been evidence to show that the AIC standard terms were the usual terms used by all grain merchants in their trading with grain suppliers, or that the claimant's managing director knew that such terms, containing an arbitration clause, were often used, then there would have been a sufficient course of dealing on the facts of the case. However, there was no such evidence before the Court. As a result, he did not consider that the limited course of dealing (four or five trades) between the parties was sufficient to justify the conclusion that an objective bystander would state that the parties had reached a common understanding that the AIC standard terms would apply.

Comment

The decision in *Capes (Hatherden) Ltd* provides a useful illustration of how the Courts will decide borderline course of trading cases. Spotting borderline course of trading cases tends to be a numbers game initially. However when a borderline course of trading case is spotted, determining which side of the borderline the case falls is unlikely to be determined simply by the number of previous trades. Other factors relating to the contractual setting, or "matrix of fact", from which the contract is formed, are more likely to be determinative.

It is clear from *Capes (Hatherden) Ltd* that important factors to consider in borderline cases, in addition to the number of previous trades, are as follows:

- whether the number of previous trades followed a consistent pattern;
- the period of time over which those trades occurred, and the gaps between them;
- whether the subject matter of the trades was the same;
- whether the standard terms were clearly notified or not;
- whether the terms in question were usual in the industry (albeit not "customary", so as to become an implied term through custom);
- whether the parties in question were aware that the terms, or similar terms, were often used in the industry.

Hugh Sims

Hugh was instructed to act on behalf of the claimant in *Capes (Hatherden) Ltd*.

Through the consumer credit looking-glass

Away from the courts, 2009 may have been an atrocious year for the banks, yet in front of the senior judiciary they notched up a number of notable successes. Most widely-reported was *Office of Fair Trading v Abbey National plc* [2009] 3 WLR 1215, in which the Supreme Court effectively called time on the "bank charges reclaim" litigation clogging the county courts. Less well-publicised was a series of cases handed down, one every month, in October, November and December 2009 in which the courts cast a critical eye over many of the arguments raised by debtors against creditors in the current slew of litigation under the Consumer Credit Act 1974 ("the CCA"). In all three cases, the debtors' principal contentions were roundly dismissed. This article will summarise the key elements of each case in turn.

McGuffick v Royal Bank of Scotland plc [2009] EWHC 2386 (Comm), 6 October 2009

McGuffick concerned a loan entered into in October 2005. In February 2009, Mr McGuffick's solicitors made a request for a copy of his agreement, as well as statutory statement of account, under s.77 of the CCA. S.77 provides that the bank should provide a copy of the agreement and the statement of account within 12 working days, and that during any period of default it is not entitled to *"enforce"* the agreement: s.77(4)(a).

The bank failed to respond by the deadline. It had received hundreds of such requests from solicitors and claims management companies ("CMCs"). Eventually in May it found and served a copy of the agreement. It forgot to provide a signed statement of account. However, it continued to threaten that Mr McGuffick's details would be passed to credit reference agencies ("CRAs"). Mr McGuffick then issued proceedings for among other things a declaration that, because the bank had not complied with s.77, his obligations under the agreement were suspended, and for injunctive relief, restraining the bank from notifying CRAs of default during the period of non-compliance.

Cleverly, as it turned out, the bank chose not to rectify its omission in failing to serve a statement of account under s.77, so that the case could come on as a test case before Flaux J. The key issue that fell to be decided was the meaning of *"enforce"* in s.77(4)(a) of the CCA.

To lay the groundwork, Flaux J held that the effect of s.77 is not to extinguish the debtor's obligations during a period of non-compliance. He remains liable, say, to make instalment payments and if he fails to do so a debt will accrue due. The bank's mirror-image rights remain in existence during a period of non-compliance but are statutorily "unenforceable".

What, then, is "enforcement"? Mr McGuffick argued that any coercive action by the bank to compel or secure performance of his prima facie obligations under the loan was "enforcement", including reporting to CRAs. However, he conceded that among other things none of the following constituted "enforcement": issuing a default notice, threatening legal action or instructing a third party to recover a debt. Flaux J thought the concession rightly made: *"at most these activities are steps preparatory to subsequent enforcement"* [80]. Further, even the bringing of proceedings does not amount to enforcement, because otherwise the bank could not apply to court for an enforcement order under s.127(1) of the CCA: *Rankine v American Express Service Europe Ltd* [2009] CCLR 3.

Once that concession was made, and approved, it was inevitable that the debtor was going to face an uphill struggle in persuading the court that reporting to CRAs was unlawful "enforcement". Unsurprisingly, Flaux J held that the bank was not debarred from reporting the state of Mr McGuffick's account to CRAs during the period of non-compliance. Neither would the bank be debarred from demanding payment from Mr McGuffick: after all, he remained obliged to pay. So, even if reporting his debt to CRAs was indeed an attempt to coerce him to pay the debt, the bank remained entitled to do so.

What does amount to enforcing the agreement, then? The answer is narrow: obtaining a court order, or seeking to enforce it (for instance by way of a charging order).

Mr McGuffick, as well as the OFT in its guidance on s.77, had got it wrong. The decision may have surprised some consumer advisors, but it followed from the various concessions made by the debtor. Once it is understood why those concessions were rightly made – that steps merely preparatory to enforcement were not enforcement – the weakness of Mr McGuffick's case is obvious. The Court of Appeal dismissed Mr McGuffick's application for permission to appeal on 16th February 2010.

Southern Pacific Personal Loans Ltd v Walker [2009] EWCA Civ 1218, 12 November 2009

This was a very different sort of case, turning on a technical argument that the lender had wrongly stated the "total credit" in the agreement. The creditor is required by s.61 of the CCA to state correctly the "amount of credit" in the credit agreement, failing which the agreement is unenforceable unless an order under s.127 can be obtained. For agreements concluded before 6th April 2007 (when s.127 was amended), no enforcement order under s.127 may be made if prescribed terms, such as the "total credit", are incorrect or omitted.

In *Walker*, a loan, secured by a second charge, had been made in March 2005. The debtors had applied for a loan of £17,500, referred to in the agreement as both the "Loan" and the "Amount of Credit". However, an additional payment was required from them of £875, described as a "Broker Administration Fee". Payment of the £875 fee was deferred for the same period as, and on the same interest terms as, the principal loan. The fee was not described as "credit", but as part of the "Total Amount Financed": not a statutory wording.

"High street banks notched up a number of notable successes in front of the senior judiciary."

The Walkers fell into arrears, and possession proceedings followed. Their defence was that the agreement was unenforceable because the £875 fee should have been included in the "credit" on the face of the agreement. Like many such arguments, it was far from attractive, as if successful the Walkers would gain the windfall of over £40,000 (including payments already made) and the clearance of the second charge. But at first instance before HHJ Halbert QC in the Chester County Court, it succeeded. Judge Halbert was much influenced by the payment of interest on the £875, finding that interest on a mere "charge for credit" was not permitted by s.9(4) of the CCA.

The Court of Appeal disagreed. S.9(4) was of no assistance, because it expressly permitted that payment of a charge for credit could be deferred, but was silent on the question of whether interest could be paid on the charge. Interest was not even a necessary feature or indicator of credit: [34]. The judge should have looked at the purpose of the borrowing, and established whether the broker's fee was part of the borrowing itself, or only part of the cost to the Walkers of the borrowing. It was, concluded Mummery LJ, only part of the cost of borrowing.

Judge Halbert can be forgiven for having got this wrong.[1] The dividing line between "credit" and "total charge for credit" is difficult, and at times impossible, to draw. Before *Walker*, many advisors would have assumed that interest was, if not necessary to, then at least an indicium of credit: now, it is clear, that would be mistaken. It is probably not even right to take it into account as a relevant factor in drawing the line. The Court of Appeal's approach reveals a certain documentary fundamentalism,[2] which at [40] turned into circularity: the agreement was clear on its face; it did not describe the fee as credit; so it was wrong to argue that the fee was credit. Although *Walker* will provide banks' representatives with another strong weapon in the CCA bulk litigation, the analytical approach to defining "credit" and "charge for credit" remains unclear.

Carey v HSBC plc [2009] EWHC 3417 (QB), 23 December 2009

Carey is the most important, and certainly the most lengthy, of the three decisions. With the north-western courts clogged by hundreds of debtors' claims issued out of Manchester, Chester and Salford, HHJ Waksman QC selected a tranche of lead cases and transferred them to the Mercantile Court so as to give a binding ruling to manage the bulk litigation.

In most of the cases, allegations were raised that the lender has failed to provide the information required by s.78 of the CCA (which for present purposes is the same as that required by s.77). Among the most important issues considered by Judge Waksman were:

- What must a creditor provide when asked for a "copy" of agreement under s.78?
- Will the s.78 duty be satisfied by providing a reconstituted copy or must the creditor provide a photocopy of the original agreement?
- Must the document be such as would comply (if signed) with the Consumer Credit (Agreements) Regulations 1983 ("the Regulations")?
- If agreement has been varied by the creditor under a contractual power, does the creditor comply by providing only a copy of the current terms?
- Does breach of s.78 give rise of itself to an unfair relationship under s.140A?

The debtors, and the CMCs underpinning them, came off badly in what might be thought to have been a series of artificial claims. In a scrupulous judgment, most of the principal contentions made by the debtors (and a few of the more extreme positions taken by the banks) were rejected.

Firstly, the "copy" required by s.78 could be reconstituted from information held by the creditor as to the terms and nature of agreement from sources other than the agreement itself. The purpose of s.78 is not to prove that the agreement complied with s.61 when made (and so to provide ammunition for claims that it was unenforceable), but to provide information about the agreement. The copy should however contain both the name and address of the debtor as it was at time of execution (although creditors can provide that information from whatever records they have).

Further, when complying with s.78, creditors need not provide a document which in form would comply with the Regulations. The reconstituted information may be contained in a number of documents. However, if the agreement has been varied, the creditor must nevertheless provide a copy of the original agreement and its terms, as well as any variations to it. It would not be good enough for the creditor to provide only the most up-to-date variation, even if by doing so that would be sufficient information to allow the debtor to understand his current obligations.

Unsurprisingly, the debtor cannot legitimately allege that there is an unfair relationship under s.140A (under which the court has a wide range of powers if it finds that the relationship between creditor and debtor arising out of the terms of an agreement is "unfair" to the debtor) only on the basis that there has been a breach of s.78 does not give rise to an unfair relationship under. S.140A is very fact-sensitive, but s.78 provides its own (limited) penalty: the creditor may not "enforce" agreement during the period of non-compliance.

Of the three decisions, *Carey* is the one that most rewards careful reading. The whiff of opportunism surrounding the claims was not allowed to get in the way of a thoughtful judgment. Judge Waksman dealt with a raft of issues in addition to those set out above, and for practitioners running or defending debtors' claims under s.78, the proper approach to those claims has to a large extent been clarified.

Conclusion

So far, the spate of CMC-driven litigation has not met with much judicial favour. Nevertheless, the flurry of judicial activity shows little sign of abating. The bulk "payment protection insurance" litigation will be one of the next in the firing-line, and it is anticipated that the High Court may rule on a number of test cases this year. *Carey* may yet go to appeal. The Court of Appeal is likely to rule soon on whether the de minimis principle applies to the calculation of the total charge for credit in a fixed-sum agreement. And at the time of writing, the Supreme Court is considering an application for permission to appeal by the mortgagor in *SPML v Heath*, which raises among other things the fierce disagreement between Francis Bennion and Professor Roy Goode over the meaning of the "multiple agreement" provision of s.18 of the CCA.

Ross Fentem

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1 And not only for his innovative means of dealing with rogue mobile phone ring-tones in his court: the writer has in the past been obliged to pay £50 to the Barristers' Benevolent Association as a penalty for the unwanted rendition of a popular R'n'B melody.

2 For another recent, but far more clearly expressed, instance, see *Southern Pacific Mortgage Ltd v Heath* [2009] EWCA Civ 1135 on multiple agreements under s.18 of the CCA

OFT guidance on information requests made under s.77, s.78 and s.79 CCA

In recent years, one of the largest growth areas under the Consumer Credit Act 1974, as amended, ("CCA") has been the explosion in litigation relating to unenforceable CCA regulated credit agreements. Often encouraged by claims management companies, borrowers have sought to exploit perceived loopholes in the CCA to avoid repaying thousands of pounds worth of debt accrued under CCA regulated personal loan and credit card agreements. A frequently used tactic has been to rely on the provisions of s.77 and s.78 CCA which state that a creditor cannot enforce a regulated credit agreement whilst he is in default of the obligation, under those sections, to provide the borrower with a true copy of their credit agreement upon request.

Following the judgments in *McGuffick* and *Carey*, which Ross Fentem has analysed in this Newsletter, the Office of Fair Trading ("OFT") has published a consultation paper, (OFT 1175con) on its draft guidance on s.77, s.78 and s.79 CCA. The consultation sets out the OFT's understanding of these sections following the recent Court decisions and also sets out the OFT's views of relevant practices which the OFT would consider unfair under s.25 CCA – the "fitness" test.

The OFT in fact made representations and submitted draft guidance to assist the Court in *McGuffick* and *Carey*. The draft guidance contained in the consultation has been revised to acknowledge the judgments in those cases.

The guidance addresses amongst other things, who is entitled to make an information request; to whom the request should be submitted and in the case of assigned debts, who should respond; how the copy agreement should be constituted; and the timeframe within which a copy agreement should be dispatched to the borrower. The guidance also considers the applicable sanctions for non-compliance, including what is meant by "enforcement".

Importantly, the OFT's guidance expands on the enforcement issues discussed in *McGuffick* and considers the wider impact of failure by the creditor to respond to an information request. Significantly, the OFT concludes that if a creditor threatened court action against a borrower knowing that judgment could not be obtained due to the creditor's default in complying with s.77, s.78 or s.79 CCA, then in the OFT's view this would be oppressive and an unfair commercial practice under the Consumer Protection from Unfair Commercial Practices Regulations 2008.

The OFT confirms that improper business practices will also impact upon a creditor's CCA licence and could result in the imposition of formal requirements. The OFT has expressed particular concern about creditors misleading borrowers into making payments when the creditor knows that the agreement is unenforceable due to failure to comply with an information request.

The consultation is open for responses until 21st April 2010.

Consumer Credit Directive

Preparations for implementation of the Consumer Credit Directive, ("CCD") continue apace. Towards the end of December 2009, the Government published its response to its earlier consultations on the proposals for implementation and draft regulations in relation to the CCD.

The primary concern of the credit industry is however, the extremely short time frame for implementation. The CCD must be transposed into English law by 10th June 2010, but it is likely to be March before final form regulations are available for scrutiny. Parliamentary Counsel is currently working on the regulations and the February 2010 CCD bulletin released by the Department for Business, Innovation and Skills, ("BIS") has confirmed that further drafting amendments will be made to the regulations.

The result is that the credit industry will have a bare three months in which to scrutinise and implement the final regulations, which is understandably causing grave concern. However, by way of solution, BIS has confirmed that there will be an extended transitional period following transposition to allow the industry extra time to comply with the new regime. Further detail is awaited, but the current indication is that businesses will have until February 2011 before full compliance with the CCD is required.

Lucy Walker

Cunning plans to expel partners

An entertaining phenomena appears to becoming prevalent at the moment whereby partners procure that a bright new shiny partnership deed is signed up to (with absolutely wizard expulsion clauses) and then promptly seek to expel a partner relying on breaches predating the deed. Solicitors acting seem to believe this is entirely right and proper. Not surprisingly the partner so ousted feels somewhat hard done by – after all the old deed may have had no expulsion provision in it at all.

Does this work? The short answer is no.

The fundamental error is a failure to appreciate that the principle of freedom to contract is modified as regards partners.

It is perfectly true that underlying all partnerships is a contractual relationship (*Hurst v Bryk* [2002] 1 AC 185), and normally parties entering into a contractual relationship can look to their own interests and as long as they do not induce the contract by a misrepresentation and it is not tainted in some other way the parties become bound to their engagement for its full terms for better or worse.

The reason why partnership contracts are different is because parties negotiating to enter a partnership, or (so the argument goes) to revise the terms of an existing one, owe a duty of good faith to each other (see *Lindley and Bankes on Partnership* 18th edn, § 16-06). It will be appreciated that commonly the new deed will create a new contractual relationship with new terms with the old contract determining.

The practical effect of this duty is, on the authorities, that all the parties to such a negotiation have to disclose to the other parties all matters which are material for the other to know. Further materiality is assessed not on the basis of the subjective views of the party who might make the disclosure but – by parity of reasoning with insurance law – whether its disclosure would have a material effect on the decisions of the parties to whom the disclosure might have been made. It is obviously highly material to a partner to know that the moment he signs the new deed his partners plan to expel him from the new partnership contract he has entered into. You may think I am being over-dramatic but in recent cases crossing my desk the time delay between signing and notice to start the expulsion process has varied between a couple of hours and a couple of weeks.

So how should the "expelled" partner react? This raises some very case specific questions but the obvious choices are to renounce the new deed or accept it – and the latter course, counter-intuitively, has significant potential attractions as I shall seek to outline.

By putting forward the provisions of a new deed in a partnership context, as above, where there is a duty of good faith, there is in fact an implicit representation that there are no reasons justifying an expulsion extant at the present time (see *Conlon v Simms* [2007] 3 All ER 802). As readers will appreciate if one has detrimental reliance on such a representation an estoppel should arise which will prevent the representor seeking to call any evidence which is inconsistent with the representation. It will normally be straightforward to show detriment and there is a presumption as to reliance in many circumstances. Thus in practice the other partners will have served an expulsion notice but be estopped from calling any evidence of pre-deed breaches. So the expulsion notice will be bad, the parties serving it may be held to be in breach of contract (contrast *Hurst v Bryk* above), the solicitors advising the body of partners may be negligent and, most attractive of all, the slate is wiped clean for the "expelled" partner i.e. he remains a partner under the new deed and all his past derelictions cannot be raised against him again in the future.

For those interested in an example of duplicitous partners there is the well known case of *Blisset v Daniel* (1853) 10 Hare 493, 68 ER 1022, where one partner said to the others "its me or Blisset" in a partnership where its true value was not shown in its accounts. Faced with this ultimatum the other partners capitulated and agreed to expel Blisset. However they needed the accounts signed off by Blisset first. So that was organised with Blisset being wholly ignorant of the axe which was to fall and fall it did just after he had signed. The Court was scandalized by this breach of good faith not least because if Blisset had known of the plot he would never have signed the accounts.

There are certain morals to be drawn from the above!

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