Consumer protection--statutory wording and contractual effect

19/05/2015

Financial Services analysis: What rights do consumers get when a lender uses documentation compliant with the Consumer Credit Act 1974 (CCA 1974) for loans outside the scope of the Act? David Bowden comments on the submissions made to the Court of Appeal in the expedited Northern Rock appeal.

Original news

Northern Rock Asset Management Plc (NRAM) v Jeffrey McAdam & Ann Hartley A3/2015/0150

What is the background to this case?

NRAM, previously known as Northern Rock Plc, is the successor company to which Northern Rock Building Society transferred its business in 1997. This lender got into financial difficulties from August 2007 onwards. On 17 February 2008 it was taken into public ownership and is now indirectly wholly owned by HM Treasury. Since nationalisation it has not undertaken any new lending, but holds a substantial book of historic residential mortgages dating back before nationalisation. NRAM has to administer this secured lending book.

Under CCA 1974, s 77A there is the requirement to send periodic statements to borrowers. These s 77A statements have to contain certain prescribed information. If they do not, then interest is not chargeable during a period of default. The s 77A statements NRAM had historically sent were not compliant. NRAM had compensated borrowers whose lending was clearly within the scope of CCA 1974 because the loan was for less than £25,000. NRAM had another large group of 41,000 borrowers who had used its 'Together' mortgage to borrow sums above this limit, typically £30,000. NRAM disputed any compensation obligation to this group because it said CCA 1974 did not apply to them.

The only deficiency with the s 77A statements are they did not state the original amount of credit provided (as required), but the borrowers would have known how much they had borrowed so nothing was being concealed from them. The borrowers have not suffered any loss as a result of this minor omission.

There had been three schools of thought in relation to using documentation compliant with CCA 1974 for lending which was outside the scope of CCA 1974:

- the lending was not CCA 1974 regulated at all because of CCA 1974, s 8. CCA 1974 cannot therefore apply to cover situations which are explicitly outside its scope. Before 6 April 2008 this provided that a consumer credit agreement was only regulated by CCA 1974 where it was within the then financial limit of £25,000 or less
- if the documentation used Form 12 or 14 of the Consumer Credit (Agreements) Regulations 1983, SI 1983/153, Sch 2, a consumer only received connected lender liability rights under CCA 1974, s 75--if it used Form 6 a consumer also only received cancellation rights
- a consumer was contracted into, as far as possible, the totality of the CCA's protections

NRAM brought a claim under the Civil Procedure Rules 1998, SI 1998/3132 Pt 8 to determine if CCA 1974 applied to this group. Two of its customers were joined in the action as defendants. NRAM agreed to pay the legal costs of both parties. In a reserved judgment of Mr Justice Burton handed down in the Commercial Court on 10 December 2014 (see *NRAM plc v McAdam and another* [2014] EWHC 4174 (Comm), [2015] 2 All ER 340) following a two-day hearing on 18/19 November 2014, the lender finally got a ruling on this issue. The judge went for the third of these formulations. Any remediation paid will have to be paid by UK taxpayers as a whole to these NRAM customers. The judgment below estimates that the remediation bill will be £258m.

NRAM appealed to the Court of Appeal. The appeal was expedited and heard over two days on 28/29 April 2015 by Longmore, Richards and Gloster LJJ. Judgment was reserved and is expected before the end of term in July 2015. The lender is seeking to persuade the Court of Appeal that the first formulation is correct.

There were eight appeal grounds but this was condensed into three issues for the court with one additional smaller issue added by the respondent borrowers.

What is the significance of this case?

If NRAM loses its appeal, it estimates that the compensation bill (which will be paid by UK taxpayers as a whole) will be £258m with a continuing remediation bill of £2m a month while the technical defaults continue. It has never been alleged, let alone proved, that any of these borrowers have suffered any loss by virtue of having been sent statements which were not technically compliant with CCA 1974, s 77A.

The s 77A requirements were added when the provisions in the Consumer Credit Act 2006, s 6 (CCA 2006) came into force on 1 October 2008. It would add salt to the wound if NRAM has to pay remediation because the majority of this customer class took out their loans before these new rights came into force or were contemplated.

The impact of the ruling in this case could be wider than just these legacy NRAM loans. There is a tranche of business-to-business lending which has been written by lenders using CCA 1974-regulated documentation. This has included lending over £25,000 or any lending to limited companies. Some lending documentation says that if the customer is a limited company or the lending is over the CCA 1974-regulated financial limit, then references to CCA 1974 are not to apply. This means a customer has to read the documentation carefully to establish if the agreement is CCA 1974-regulated or not.

If the parties had treated the loan 'as if' it were a CCA 1974-regulated agreement, then it would be unenforceable because the lender had not sent out statements under CCA 1974, s 77A. This issue was not thought about when CCA 2006 was passed. Nowhere does it say that monies have to be paid back by a lender. If the judgment below is correct, this would mean the borrowers would be unjustly enriched at the lender's expense.

The legal remedy is unjust enrichment--but has NRAM been unjustly enriched in any way? The customers agreed to repay their loans. This is not an unjust enrichment of the creditor.

What were the issues the Court of Appeal was asked to address?

Although there were eight grounds of appeal, the skeleton arguments condensed this into these three issues:

- Did the statutory wording have contractual effect?
- If it did, what was its proper meaning and effect?
- If it did not, was it nonetheless capable of giving rise to an estoppel or implied term?

What does the appellant lender say?

NRAM's oral submissions lasted nearly seven hours.

Re London Scottish Finance (in administration) [2013] EWHC 4047 (Ch), [2013] All ER (D) 199 (Dec) held that if the customers had paid under an irredeemably unenforceable agreement, then these sums could be repaid but this was an 'unfair relationship' issue. In *Office of Fair Trading v Abbey National* [2008] EWHC 2325 (Comm), [2009] 1 All ER (Comm) 717 there is scant support for automatic repayment or quasi-restitution. This flies in the face of the no further sanctions in CCA 1974, s 170(1) which says:

> 'A breach of any requirement made (otherwise than by any court) by or under this Act shall incur no civil or criminal sanction as being such a breach, except to the extent (if any) expressly provided by of under this Act.'

Breaches of CCA 1974 could be taken into account by the Office of Fair Trading under its licensing regime or the Financial Conduct Authority (FCA) under its permission regime. Although CCA 1974, s 77A can, in practice, create unenforceability, it is not irredeemable because a creditor can rectify defects by sending out proper notices.

There are two leading encyclopaedias on consumer credit law. The first is *Goode: Consumer Credit Law and Practice*, and the other is the *Encyclopaedia of Consumer Credit Law* now edited by Professor Eva Lomnicka.

Much was made at the appeal hearing of the volte face by the present editors of *Goode*. Before the first instance hearing, the commentary in *Goode* appeared to support the first or second constructions and that most beneficial to the lender. However, after the decision of Burton J was handed down, that commentary was changed to support the third construction least favourable to the lender.

The *Guest & Lloyd* analysis of Professor Lomnicka had not changed because of this case--see para 2-009:

> 'It is suggested that the parties cannot, by agreement, confer jurisdiction on the court to make enforcement orders under s 127 and hence that all the provisions (eg s 65) that might result in an application under that section cannot by agreement be rendered applicable to non-regulated agreements. Alternatively given that the court has no statutory jurisdiction to enforce such agreements (the relevant provisions being confined to "regulated agreements" as defined), the parties cannot be regarded as having agreed that their agreements are unenforceable except on an order of the court, given that the court does not have statutory jurisdiction to enforce them.'

What is the position if the borrowers claimed that NRAM had warranted to them by using CCA 1974-regulated documentation that the lending was regulated by CCA 1974? To this NRAM said that on the whole these claims would be time-barred because the agreements are more than six years old now.

What do the borrowers say?

While the skeleton arguments were of similar length at 25 pages, the borrowers' oral submissions were much shorter at three hours in length. It was noticeable that the borrowers had no convincing answer to NRAM's point about CCA 1974, s 170.

In relation to the three issues, the borrowers had this to say:

- issue 1--clearly 'yes' because a court cannot disregard statements as inapplicable to the particular agreement
- issue 2--you assess what a reasonable person who was appraised of the relevant background would have understood
- issue 3--the case for an implied term is irresistible because of needs of business efficacy

Additionally, the borrowers had a short fourth issue as to whether there was an assumption or representation that the agreement was CCA 1974-regulated. The borrowers emphasised that the scope of the appeal was narrow being limited only to CCA 1974, s 77A.

Does authority on landlord and tenant law have any bearing on this case?

Five volumes of authorities were produced for the Court of Appeal. These included not just relevant extracts from CCA 1974 but also ten sets of regulations made under it, 28 cases and five academic authorities.

The judgment below relies heavily on a number of appellate cases in the field of landlord and tenant law. It is doubtful whether these have quite the wide scope that the trial judge found. Burton J found himself bound by a prior Court of Appeal decision in *Daejan Properties v Mahoney* (1995) 28 HLR 498, [1995] 2 EGLR 75. This case concerned whether a tenancy remained a protected tenancy under the Rent Act 1977 (RA 1977) when it had been transferred. Here the court held that the landlords by their representation, on which the defendant and her mother relied, had estopped themselves from denying that the defendant and her mother would be treated as joint tenants and so as joint statutory tenants, since a statutory tenancy was the only tenancy in existence at the time.

More favourable is the Court of Appeal decision in *Tomlin v Reid* 185 EG 913. Here, in another RA 1977 case, the landlord's agent gave a tenant the assurance that when he moved to certain new premises he would have the protection of the Rent Restriction Act. The tenant, acting in reliance upon this assurance, moved to these premises. The Court of Appeal held that:

- the Rent Act 1957, s 11(2) meant the tenant was not entitled to statutory protection
- there was no contract that the premises should be treated by the landlord as though they were controlled premises, and even if there were such a contract, it would be invalid, and
- there was no estoppel against the landlord since the agent's representation was one of law

In the Court of Appeal, NRAM submitted that the CCA 1974 regime was different to that applying to Rent Act tenancies. NRAM pointed out that under CCA 1974 a consumer under a regulated agreement was given a right to apply to a court for a time order under CCA 1974, s 129, and the court had powers to make an enforcement order on terms under CCA 1974, s 127 if the agreement was improperly executed because the requirements of CCA 1974, s 65 and regulations made under it had not been complied with. Other attempts were also made at distinguishing *Daejan* on its facts.

What interventions did the judges make? What points seem to be troubling them?

The judges were initially frustrated in not being able to see a statement which was compliant with CCA 1974, s 77A so that they could compare any deficiencies for themselves. The appellant's counsel was asked if compliant statements had now been issued on a 'without prejudice' basis but was told not. There were a series of declarations on the loan application that a borrower had to make. These included not only that the information the borrower provided was correct but also that an unsecured loan was not regulated by the FCA. Lady Justice Gloster thought this was a funny thing for a borrower to be declaring.

However, Gloster LJ was clear that even if CCA 1974 was contractually incorporated, it would be impossible to require a court to extend its jurisdiction to make an enforcement order (under CCA 1974, s 127) or a time order (under CCA 1974, s 129) to agreements which were not in fact CCA 1974-regulated.

The panel was troubled as to what a reasonable consumer would understand from the NRAM documentation. Richards LJ intervened that 'statements are simply statements under the CCA'. Longmore LJ was more frank saying that 'before I read the papers in this case I wouldn't have had the slightest idea'.

Gloster LJ wondered whether, if borrowers had known the true position, and it was important to them to have the suite of CCA 1974 rights, they would have wanted to borrow less than £25,000. She was taken by the pre-NRAM analysis in *Goode* where it states that 'taken to its logical conclusion,' the only relevant rights are the right of withdrawal and the right of early settlement. She felt, however, that this text (since changed substantially since the first instance decision was handed down) was not altogether on NRAM's side.

Longmore LJ intervened to comment that to any reasonable consumer or person, the words NRAM used in its documentation 'would be of contractual effect'.

What should lawyers do next?

The appeal was expedited. At the end of the hearing Longmore LJ gave no indication as to when judgment will appear. Whichever way this appeal is determined, the losing party will have to consider whether to pursue a final appeal to the Supreme Court.

Meanwhile, where there are CCA 1974, s 77A claims, these should be put on hold pending the ruling in this case.

Finally, the law could be changed to put this matter beyond doubt. As the CCA 1974, s 77A issue arises from CCA 2006, the Department for Business, Innovation and Skills has the power to lay a statutory instrument modifying any Act or subordinate legislation as it thinks fit (CCA 2006, s 68).

The views expressed by our Legal Analysis interviewees are not necessarily those of the proprietorThe views expressed by our Legal Analysis interviewees are not necessarily those of the proprietor.