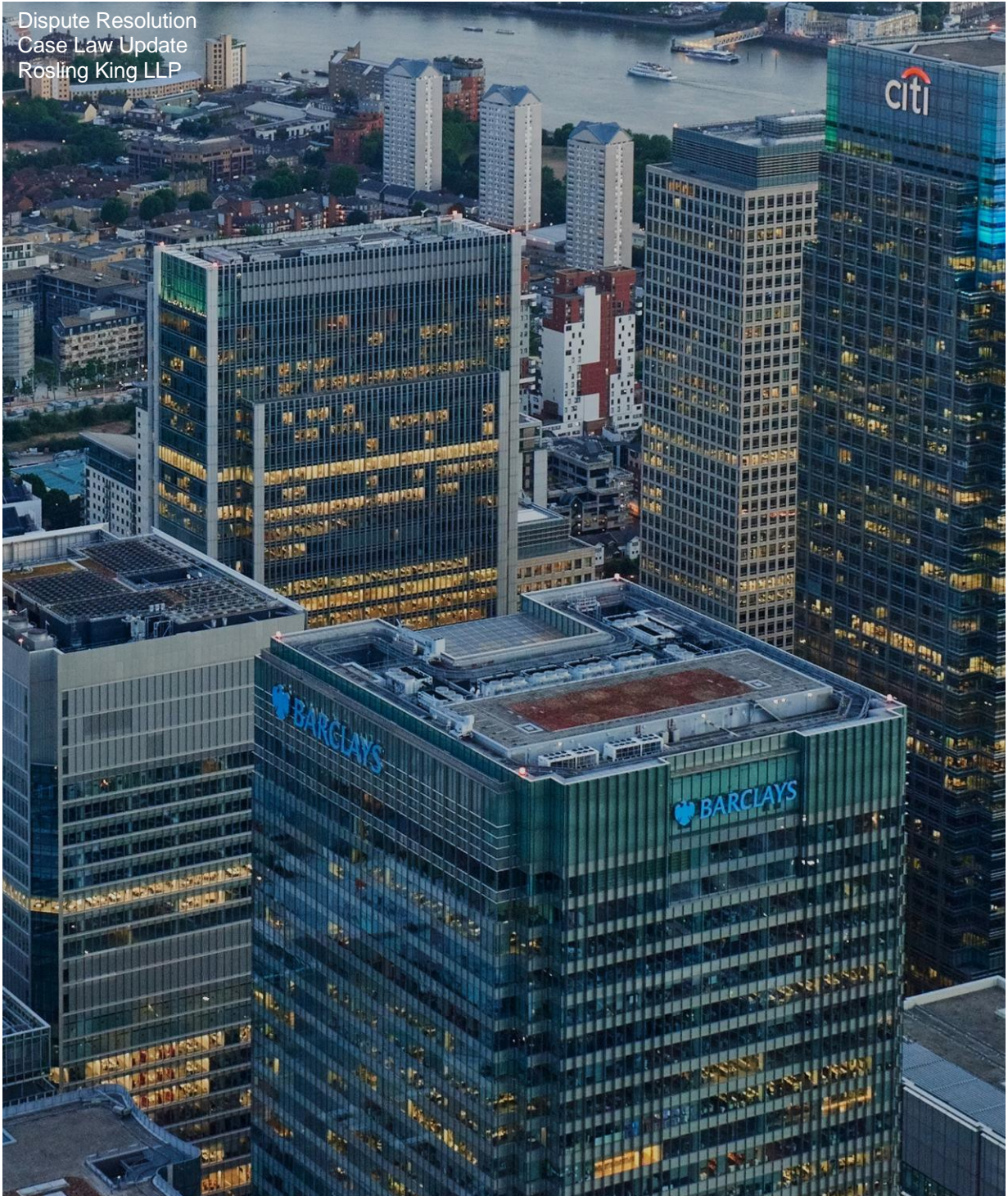


Dispute Resolution
Case Law Update
Rösling King LLP



Background

Mr and Mrs Thomas (the “Claimants”) were partners in an award-winning organic farming business which they had built from scratch. In 2006, the Claimants transferred their borrowing from another bank to Triodos Bank NV (the “Defendant”) because it had a reputation for supporting businesses with strong green credentials. The Claimants entered into two variable rate loan agreements with the Defendant, for £300,000 and £1.15m respectively. In June 2008 the Claimants restructured a sizeable proportion of their borrowing from variable rates to fixed rates. The restructuring was done in two tranches, one at a rate of 6.71% and the other at 7.52% (the “Fixed Rate Loans”). The term of both Fixed Rate Loans was 10 years.

In accordance with clause 2.10 of the Defendant’s terms and conditions, an “early repayment fee” was payable in the event of early redemption. Further, clause 2.11 of the terms and conditions provided that an additional “extra repayment premium” (also referred to as the “redemption penalty”) was payable if a fixed rate loan was repaid early. Prior to agreeing to the switch to fixed rates, Mr Thomas queried whether the maximum likely redemption penalty would be in the region of £10-20,000. The Defendant did not refute or correct him. The Defendant referred to the Business Banking Code (the “BBC”) in its literature and in the letters confirming the fixed interest rate products. The Claimants subsequently found themselves tied to interest rates which were well in excess of the market rate, following a fall in interest rates as a result of the global financial crisis. The Claimants enquired about the redemption penalties in the event that the Fixed Rate Loans were repaid early and discovered that the penalties for early redemption were far greater than the £10-20,000 the Claimants had expected. The Claimants issued proceedings against the Defendant as a result.

The Claim

The Claimants alleged that while it was not possible for the Defendant to predict the fall in interest rates after September 2008, the Defendant should have explained the financial consequences which would result from the Claimants repaying the Fixed Rate Loans before the end of the 10 year term. It was further alleged that the Defendant positively misrepresented the financial consequences that would follow a decision to redeem the loan before the end of the 10 year term.

Decision

HHJ Havelock-Allan QC allowed the Claimants’ claim against the Defendant. Duty of care

It was held that the Defendant owed the Claimants a duty to take reasonable care not to misstate any facts on which the Claimants could be expected to rely. If it was found that some or all of the misrepresentations were made, and that the Claimants

relied on them in deciding to fix the rates, then the Defendant would be liable. In the instant case, it was necessary to consider whether the duty of care which the Defendant owed to the Claimants went than simply a duty not to misstate.

A significant feature of the case was that the Defendant had advertised that it subscribed to the BBC. The Fairness Commitment in the BBC included a promise, directed to the customer, that if the Defendant was asked about a product, it would give the customer a balanced view of the product in plain English, with an explanation of its financial implications. There were no disclaimers, “basis” clauses or exclusions in the terms and conditions which would lead to the conclusion that the Defendant was not willing to assume responsibility for honouring that promise. When the Claimants enquired about fixing the rate on the loans, the Defendant owed them more than a duty not to misstate. The duty of care which the Defendant owed was to explain the financial implications of fixing the rate. It was a duty it owed only in response to the Claimants’ inquiries because that is what the Defendant had signed up to in the BBC. It was not a duty to volunteer information if not asked.

In order to discharge its duty the Defendant was required to provide an explanation, in plain English, of what fixing the interest rate entailed and the consequences of such a decision. Essential components of the explanation were: (1) that the rate could be fixed for a period (whether in months or years, and whether for any minimum or maximum length of time); (2) where the available fixed rates could be found (i.e on the internet); (3) what those rates represented (the forward cost of money); (4) the effective rate that would be payable (i.e. the current swap ask rate for the period of the fixed rate, plus the bank’s margin, if any); and (5) the financial consequences of terminating the fixed rate before the end of the term. Further, the Defendant should have provided an accurate description of how clauses 2.10 and 2.11 operated in the event of early repayment. A worked example was not necessary, but the ingredients of the calculation under each clause should have been made clear in terms which gave a balanced picture.

Breach of the duty of care

The failure of the Defendant to clarify the position when Mr Thomas asked whether the maximum likely redemption penalty was in the region of £10-20,000 gave rise to a misrepresentation which influenced the Claimants’ decision to enter into the first of the Fixed Rate Loans. Simply being asked the question should have alerted the Defendant to the fact that the Claimants did not understand how clause 2.11 of its terms and conditions worked.

Comment

As the Court detailed in its judgment, there are conflicting first instance decisions as to the duties owed by banks when they are providing information about a product, as



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opposed to advice. This case is an interesting decision indicating that banks sometimes owe an “intermediate duty” to explain the product, which is higher than their duty not to mislead or misstate. However, each case will be decided on its own facts and the Defendant’s reference to the BBC in its literature was of particular relevance in this case.