

## Asset Financing and Leasing

# e-bulletin

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As Autumn 2009 progresses there is at least some optimism that the economy is not getting any worse! There are even expectations in some quarters that in the Spring 2010 things will start even to improve. One hopes that the green shoots will be as visible and as welcome as the daffodils in February.

Overall, liquidity is still scarce and banks can still be choosy about deals. Leasing is one financing activity within the banks and it has to fight for the limited amount of liquidity that is available. For brokers the market is even tighter as fewer funders are prepared to take deals from them. However, the break up of some of the state controlled banks may also allow new entrants to the leasing market.

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### Mid ticket leases can be subject to the Unfair Contract Terms Act 1977

It is recognised that small ticket lessor terms and conditions are subject to the "reasonableness" test in the Unfair Contract Terms Act 1977. A court has recently found that a mid ticket lessor's lease terms can be subject to the test.

The situation in Lobster Group Limited -v- Heidelberg Graphic Equipment Limited and Close Asset Finance Limited [2009] EWHC 1919 (Technology and Construction Court) was a classic triangular arrangement where Lobster arranged for the provision of a Heidelberg printing press and finance with CAF. The contractual position will be familiar, a hire agreement between Lobster and CAF, a warranty agreement between Lobster and Heidelberg and a service agreement between the same. The judge, Ramsey J, gave a detailed analysis of the contractual situation and examined each of the contracts to see whether they were reasonable in the circumstances.

For lessors, an important point was a comment that the judge made as follows:- "[Lobster] relied on [Heidelberg] and not on CAF in relation to whether the press was fit for the particular purpose for which [Lobster] were hiring it from CAF. Equally, given the involvement of [Lobster] and [Heidelberg]... I consider that it would have been unreasonable for [Lobster] to rely on the skill and judgement of CAF."

So, the relevant skill and judgement in the supply of the goods is usually not going to be that of the lessor. The protection that the clauses in most standard leases give regarding the exclusion of skill and judgement is still given some efficacy by the courts.

However, other exclusion provisions in the CAF contract terms and conditions were not acceptable to the judge in this case. In the lease it was stated that the letting of the press was made without any term, condition, warranty or stipulation, written or oral, express or implied, whether by statute or otherwise. This was not acceptable to the judge. Neither was the exclusion of liability "in contract or tort or otherwise for any loss or damage suffered by [Lobster] whether or not caused by the negligence of CAF".

As the judge decided that there was an obligation to provide a press of satisfactory quality so CAF were liable for the main defect in the press which was one of "image fit". CAF are liable to pay damages to Lobster in the sum of £14,543.52. This was after the judge gave in an examination of the loss and the division of costs to rectify the problem that Lobster experienced.

CAF were, however, able to claim their termination sum due under the hire agreement. Lobster had stopped paying the rentals but the defect they complained of was not one that amounted to a repudiatory breach of the hire agreement by CAF. The hire agreement had the common clause that required continued payment of rentals even if the quote is unserviceable. The action by Lobster in stopping payment allowed CAF to terminate the hire agreement and claim their termination payment.

So, what can a lessor do? They should review their terms and conditions and, if required, include a clause that states the lessee has arranged with the original supplier/vendor of the goods to provide all warranties and repairs that may be required in relation to the goods. This might not provide immunity from quality

issues but does give the customer some protection with respect to the supplier and gives them the benefits of obligations to repair that the supplier has given. These are, in the end, however, only as good as the supplier itself. The court was favourable to excluding Lobster's claim for loss of profit, so it carefully drafted clause excluding consequential losses can be reasonable.

Clauses which exclude lessor liability are not viewed favourably but those which define the terms upon which the parties conduct their business are more likely to be acceptable. If the parties agree how they will each accept risks in the equipment then that would be acceptable. There is, therefore, the risk and reward argument with regard to whether or not something is reasonable and whether risks are divided by parties in accordance with their respective expertise and roles in the asset finance process. So if the lessor agrees to accept liability for the equipment then the customer should expect to pay higher lease rentals; and also the opposite situation should be acceptable to the courts such that the customer has agreed with the lessor that the rentals are lower due to the customer having assumed more risk in the equipment not working properly. These would probably be viewed as reasonable and provide the required protection.

In the end, this case does represent an extension of application into a larger ticket leasing sector than previously, but lessors should always have been aware of these kinds of risks when putting together their standard lease terms and conditions.

## Two different views of how changes in the contractual relationship may affect the related security

Two cases show how in certain circumstances the security given by a person or a third party may cover changes in a contract.

The first case (and, more recent in time) is the case of *Bank of Scotland Plc -v- Constantine Makris and Ben O'Sullivan* which was decided on 15 May 2009 by Judge David Donaldson QC. The two Defendants, along with a third partner, wished to open a new bar in Milton Keynes and arranged for bank finance, including overdraft facilities; and the bank required various securities from them. One of the securities was an unsecured, all monies, guarantee from the Defendants. Due to certain issues concerned with the other parts of the security (particularly a guarantee from the third partner secured by a legal charge over his house, which house was not owned by the third partner but by the third partner and his mother), the overdraft facility was reduced. The bank then took action after the failure of the bar to recover the debt. They claimed monies under the guarantee but the Defendants claimed that the guarantee had been discharged as a result of the reduction in the original overdraft facility due to the change in the facilities. This was rejected by the court. One of the guarantors had, in fact, signed the second facility letter and so could not challenge on that basis. As the guarantee was for all liabilities rather than a specific liability, the court had no difficulty in finding that the guarantee applied to the reduced overdraft. Had the guarantee been drawn up in such a fashion that it could apply to only a specific facility, then the change in the facility would have probably had the effect of discharging the liability under the guarantee. For asset financiers, this could be an issue when trying to ensure that their facilities come within existing bank guarantees, particularly if the leasing company is a subsidiary of a bank.

The all monies issue was also considered in a slightly different context in the second case of *ING Lease (UK) Limited -v- Harwood* [2007] EW HC 2292 (QB). In this particular part of the litigation concerning the guarantee given by Mr Harwood, the guarantor had signed a written guarantee under which "in consideration of" ING providing finance for Mr Harwood's companies, Mr Harwood guaranteed the due payment of "all monies, obligations and liabilities whether

actual or contingent, now or hereafter due, owing or incurred to ING". One of Mr Harwood's companies incurred debts to another finance company, which finance company assigned those rights to ING. The question before the court, therefore, was whether the assigned debts actually came within the ambit of the ING guarantee.

The court, Michael Harvey QC sitting as a deputy judge, held that the ING claim failed. The court has to ascertain the presumed intention of the parties at the time of giving the guarantee, especially in an "all monies" clause - and whether that is in a guarantee or a mortgage. The guarantee did not include assigned debts unassociated with those original mutual relations between the bank and the guarantor.

The judge gave some interesting reasons for that decision and commented on various other cases on these issues, particularly some from Australia. The judge looked at various provisions within the guarantee regarding the facilities that ING made to the company. The proper construction of the guarantee was that it only applied to the facilities made available by ING to the named companies. Whilst the Australian cases deal more with the situation of a security over land, the judge quoted approvingly from the decision. The construction of 'all monies' clauses in guarantees and other security is to be considered in the light of the commercial purposes within which they were intended to serve.

The need for wording in the guarantee should therefore be considered to ensure that the guarantee will apply even if there is a change in the facility or if there is an assigned debt to the bank. So, the guarantee should be drafted as widely as possible to ensure that what is in the contemplation of the parties as to the extent of the guarantee can also be as wide as possible.

## Characteristics of a regulated consumer hire agreement

The essence of hire that is required for a consumer hire agreement for the purposes of the Consumer Credit Act 1974 is that the hirer acquires the use and possession of goods from the owner of the goods in return for a rent, whether that rent is payable in cash or in kind. It does not apply to gratuitous bailments.

In the case TRM Copy Centres (UK) Limited -v- Lanwall Services Limited [2008] EWCA CIV 382 the House of Lords has decided that a consumer hire agreement for the purposes of section 15 of the Consumer Credit Act 1974 requires a bailment under which the person who has possession of the chattels agrees to pay for the use of it in cash or in kind during his possession. The case itself was a dispute between rival providers of photocopiers in retailers' premises for use by customers in the shops. The form of the agreement by which the copiers were installed in the shops were held not to be consumer hire agreements for the purposes of the Act as there was no rental payable by the retailer to the provider of the copiers.

## Is a higher APR an unfair relationship?

The existence of a higher APR is not of itself indicative of an unfair relationship for the purposes of the Consumer Credit Act.

Judge Burn in the Bromley County Court gave judgment that has decided that a high APR in connection with a "log book loan" was not, of itself, an unfair relationship. The case involved a loan for that amount of money but payable by 55 instalments. The APR was 384.4%. The loan was secured by a bill of sale over the customer's car. The loan account fell into arrears and the vehicle was sold. The lender sued for the balance owing of nearly three times the original amount of the loan. The borrower claimed the agreement constituted an unfair relationship under section 140 of the Consumer Credit Act 1974. This section replaced the old provisions of section 138 of the CCA relating to extortionate credit bargains. The old section had a number of factors that the court could take into account in deciding what is extortionate, but no such factors are in the new unfair relationship provisions. The court, therefore, looks to the relationship between the parties to decide whether or not the relationship is in fact unfair. In this particular instance, the relationship was not unfair for four reasons:-

- 1 the interest rate was high but the risk to the lender was also high;
- 2 the loan was to be repaid over a short period and this was at a competitive interest rate;
- 3 the entitlement to recover the vehicle without a court order was harsh but the borrower was advised and given opportunities to prevent the recovery of the vehicle;
- 4 the lender's procedures in setting up the loan were reasonable and they encouraged the borrower to come to an arrangement rather than lose the car. These indicated that there was not an unfair relationship. However, the court did go on to look at the way in which the agreement had been enforced and some concession was given back to the borrower for the fact that the vehicle had been sold without the keys and logbook.

## The cost of providing a "free" car must be made clear

There is another case in the continuing saga of what can be claimed if a car is provided whilst the Claimant's car is being repaired due to an accident involving the Defendant. The rules regarding spot rate prevail.

In the combined cases of Copley -v- Lawn and Maden -v- Haller [2009] EWCA CIV 580 (17 June 2009), the Court of Appeal held that it is reasonable for a claimant to reject or ignore an offer from a Defendant (or his insurers) which does not set out the clear cost of the hire of the replacement car to the Defendant for the purpose of enabling the Claimant to make a realistic comparison with the cost that he is incurring or about to incur on the supply of the replacement car. Then, if the Claimant does unreasonably reject or ignore the Defendant's offer, the Claimant can recover at least the cost which the Defendant can show he would reasonably have incurred. The Claimant does not forfeit all his damages claims. The general rule that the Claimant can recover the spot rate or market rate for his loss of use of his car is upheld by the Court of Appeal. However, if the Defendant can show that on the facts of the particular case that a car could have been provided even more cheaply than the "spot" or market rate then he will be able to show that the Claimant has not mitigated his claim.

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## **Enforcement of CCA Regulated Agreements in Scotland**

A recent change to the Sheriff Court rules in Scotland requires the inclusion of a copy of the regulated agreement to be attached to the writ.

In Scotland, the initial court in which a regulated consumer hire or consumer credit agreement will be enforced is the Sheriff Court (in England and Wales, it is the County Court). There has been a recent change to the rules which require that the "initial writ" (this being the initial document commencing the enforcement proceedings in the court) requires that the agreement exists and requires details of that agreement to be included. It also requires a copy of the regulated agreements to be attached to the writ. This is a change that did not require any public or any other consultation as it is merely a change in the rules of procedure in the relevant court. However, it will doubtless cause leasing and other finance companies a great deal of difficulty if they do not have the original document. There is also some disparity in the rules with the requirements of the CCA and the Consumer Credit (Cancellation Notices and Copies of Documents) Regulations 1983 which only requires a "true copy" which may exclude any signature box or signature on date of signature. Further guidance will be issued by the Sheriff Court Rules Council shortly.

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## **Company Directors Guide**

Morton Fraser has produced a printed colour booklet on being a director of a private company. It has a foreword from David Watt at the Institute of Directors, Scotland. The guide is available electronically on our website at:- [www.morton-fraser.com/includes/html/getFileData.php?id=8270](http://www.morton-fraser.com/includes/html/getFileData.php?id=8270)