CURRENT ASPECTS OF UNSECURED LENDING
LIABILITY OF LENDERS

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I started off my paper on this subject by saying that nobody likes banks. Well that is certainly universally true amongst judges. Banks start off one down. It is almost entirely true for the rest of the community. That has not been much of a problem legally until relatively recently. As I said in my paper there has been all kinds of remedies which you can produce in difficult cases - i.e in fraud, duress and all that sort of thing, but they have only been used in really hard cases and nobody would have been surprised.

In the United Kingdom we had a string of cases which were very worrying. It started with the Bundy case which I have mentioned in my paper where Lord Denning, "bless his heart", in an effort to do what the courts have a nasty tendency to do nowadays (which is to do justice), said he found many reasons why some guarantors should be let off the hook. He pronounced a series of theories which sounded very attractive to the consumer protection lobby, but made businessmen, bankers and lawyers extremely agitated because essentially he said that inequality of bargaining power meant that you have to presume undue influence.

In my experience the last thing a banker wants is equality of bargaining power. To suggest that where there is inequality of bargaining power that means undue influence exists, automatically makes life practically impossible. There was a lot of other talk in Bundy about the special relationship which goes further than what we had expected in terms of relationship between a bank and its customers.

There have been a succession of cases since which have brought the law back to something more approaching sanity on the subject. But what they have all indicated is that the courts are much readier nowadays in England to look at the banker/customer relationship and say: bankers are not any longer people who simply take your money and hand it back when you ask for it; if they lend money it is because a customer comes in and ask for some money and they hand it over to you, you sign a receipt and that is it!

The courts are inclined to say that there is much more to the relationship and they are justified in saying. If you look at the television advertising in London you realise very quickly that the banks will do the most amazing things for customers at virtually no cost. It comes as a slight surprise to them when you tell them that it is just a debtor/creditor relationship and they are not your financial advisers and so on.

So we have a little bit of a conflict going on. We though we were in dead trouble with the Bundy case. That has been fought back but we are all waiting for the next time the courts flex their muscles on this.

In the meantime I discovered through some diligent research that all the American cases on the subject reach the same results. It is all a kind of consumer protection. They have expressed their views in various ways. A lot of it comes down to what they call "economic duress". This can be redefined in various ways. One Californian judge said that what this was all about was the courts enforcing certain minimal standards of business conduct. There is a school of thought which says that all standards of business conduct are minimal but I presume we here have something else in mind.

But this makes the blood run cold as well because in England, and I think in all the Commonwealth countries, we do not expect the judges to enforce or not enforce transactions in accordance with whether they think they are in accordance with good business practice or not. That is certainly not the case in Scandinavia where the judges will not give you a remedy on an event of default if they think it is not in accordance with good business practice. It comes as a nasty shock. That is not the case in France where the judges have a very wide discretion indeed as to whether to enforce something. But it is the case in the Commonwealth countries. We expect the judges to have a look at the documents, if there has not been any fraud or duress or whatever in the conventional sense, then to enforce it and we have seen a tendency in the United States to question that approach.

The thing that comes out in the cases in the United States more than anything else is that if the banks get so close that they are exercising some kind of control then they start to get into trouble. It is questionable of course as to what you mean by control. But most of the control that arises, arises in difficult situations, in workout situations, when life starts getting tough. Now that is the very time when the banker wants to exercise some degree of control. He is prepared, subject to his financial ratios and so on, to let the borrower carry on while things seem in order. But when things become difficult he wants to step in. He wants to appoint directors, he wants to be very closely involved in the day to day management, because basically he wants his money back. Very often he acts in the interests of other creditors as well.

But what the US courts have been inclined to say is: "Look, if you are involving yourself in the affairs of the company to this extent, you must accept responsibility for what goes wrong. You can't have it all ways". The English courts have not extended their doctrines like that on control yet but what we have got is some statutory law now in England which really reflects the same sort of idea. We have a new Insolvency Act which, we are trying to digest, which creates a new kind of wrong. This really does mean that people who get involved in the control of the company in the period leading up to liquidation can find themselves having to contribute to the assets. In other words they have to underwrite the thing. Basically it is aimed at directors and similar persons. We also have a definition of shadow director which can extend to anybody who tells the directors what to do. That of course is exactly what banks, in a workout situation, have to do if they are to rescue the company. We are waiting to see what is going to happen.

It could be that this will frighten some banks into not getting involved so closely in workouts. I think that would be unfortunate on the whole because my impression has been that the business community has benefited overall by the willingness of banks (maybe for selfish motives, but I am not sure that matters) to go in, lend a hand in rescuing the thing and getting their money back through creating an on-going company.

I am not asking you to do anything, answer anything or whatever else, I am just putting you on notice that there are movements in England and the United States which do give one pause a bit as to quite where things are going. The judges are more willing to interfere. The legislators are also more willing to interfere with banks getting really close to their customers. These developments make one a bit uneasy.