An tOmbudsman Seirbhísí Airgeadais agus Pinsean
Financial Services and Pensions Ombudsman

Decision Ref:	2021-0279
Sector:	Banking
Product / Service:	Business Bank account
Conduct(s) complained of:	Fees & charges applied
Outcome:	Upheld

LEGALLY BINDING DECISION
OF THE FINANCIAL SERVICES AND PENSIONS OMBUDSMAN

The Complainant is a private limited company and this complaint is brought on its behalf by its directors. The Complainant restructured existing loan facilities pursuant to a Letter of Offer dated **23 June 2010**. These facilities were restructured again pursuant to a Letter of Offer dated **29 February 2012**. The Complainant defaulted in its repayment obligations and surcharge interest was applied to the loan account by the Provider. The Complainant disputes the Provider's entitlement to charge surcharge interest in respect of these facilities.

For the purpose of setting out the position of each party to this complaint, it is important to note that the parties have separately indicated that the submissions made in the course of a linked complaint, connected to the parties, apply equally to this complaint.

The Complainant's Case

The Complainant states that the Provider applied surcharge interest to a loan account totalling €50,880.10 including compounding. An *Interest Audit Finding* dated **25 April 2018** prepared by the Complainant's representative has also been furnished. The Complainant argues that the Provider is now refusing to refund the surcharge interest despite numerous legal rulings on the charging of this type of interest.

In a letter dated **17 January 2019**, the Complainant's representative has referred to three High Court decisions: ***ACC Bank plc v Friends First Managed Pensions Funds Limited*** [2012] IEHC 435; ***AIB plc v Fahy*** [2014] IEHC 244; and ***Sheehan v Breccia*** [2016] IEHC 67, stating that all three deal with the issue of surcharge interest.

It is also pointed out that in the course of correspondence with the Provider, the Complainant's representative asked whether the surcharge interest rate applied to the loan was negotiated with the Complainant and was a genuine pre-estimate of probable loss or a generic rate.

Referring to the Provider's response letter dated **5 February 2018**, it is submitted the Provider *clearly states* that the surcharge interest rate (of 0.75% per month, or 9% per annum) was *'never open to or subject to negotiation by the Company and apply to all loan facilities provided by the Bank'.* It is further submitted this confirms the interest rate applied to the loan was a generic interest rate and a penalty, and was therefore, unenforceable.

In a letter dated **7 March 2019**, the Complainant's representative explains that it sought to identify whether the surcharge interest applied to the loan met three criteria, as set out in the various judgments, stating:

1. The interest rate applied was not negotiated with the Complainant;

2. The surcharge rate applied (9% per annum) was a generic rate contained in the terms and conditions; and

3. The surcharge interest rate did not represent a genuine pre-estimate of loss arising from default.

It is submitted that the Provider has failed to show the interest rate applied was a genuine pre-estimate of probable loss, and that it was negotiated with the Complainant and not a generic rate.

In resolution of this complaint, the Complainant wants a refund of the surcharge interest applied to the loan and reimbursement for all professional costs and expenses incurred in resolving this issue. In particular, paragraph 127 of the decision of Haughton J in ***Breccia*** has been cited as summarising the crux of this complaint.

The Provider's Case

The Provider wrote to this Office on **19 February 2019** requesting that it decline to investigate this complaint pursuant to ***section 52(1)(f)*** of the ***Financial Services and Pensions Ombudsman Act 2017*** (the **Act**) on the basis that the subject matter was of such a degree of complexity, the courts were a more appropriate forum to determine the dispute. The Complainant disagreed with the Provider's position on the matter as outlined in its letter of **7 March 2018**.

By letter dated **27 March 2019**, the Provider addressed the matters arising in this complaint under three separate headings: (i) *Accord and Satisfaction*; (ii) *Limitations Periods*; and (iii) *Specific Issues Raised by the Complainant*.

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Accord and Satisfaction

The Provider submits the legal principal of accord and satisfaction applies to this complaint as the Complainant and associated parties entered a Debt Settlement Agreement with the Provider dated **20 March 2015**, (the **DSA**). The DSA confirmed the terms whereby the Provider would settle and forbear in relation to all of the parties' combined debt obligations and liabilities, and they agreed *'… in consideration of the mutual agreements set out below (and for good and valuable consideration, the receipt of which is acknowledged by each of the Parties) …'.*

In my Preliminary Decision I stated:

…Subsequent to the execution of the DSA, a Receiver appointed by the Provider disposed of most of the secured assets,…

The Provider, in a post Preliminary Decision submission, states that it "*made the majority of Receiver appointments over its Secured Assets in November 2013, so the Receiver appointments occurred prior to execution of DSA rather than subsequent to same".* [the Provider's emphasis added]

As there was a surplus remaining upon the completion of this process, a variation of the DSA was mutually agreed between the Provider and the Complainant whereby in consideration for the payment of €300,000, two properties with a value of approximately €2 million were returned to the Complainant. Additionally, the Provider did not require the disposal for two other properties and also released a mortgage over a principal private residence.

The Provider refers to a definition of accord and satisfaction in ***Chitty on Contract*** (Volume 1 – General Principles, 32nd ed., 2015), as *"… the purchase of a release from an obligation whether arising under contract or tort by means of any valuable consideration, not being the actual performance of the obligation itself …."* It is submitted the *accord* in this instance equates with the agreement between the parties, the DSA, and the obligations to be complied with by each party, whereby the Complainant's obligations to the Provider are discharged. The *satisfaction* is the consideration or acts of each party to be observed and performed, so as to make the agreement operative. The Provider states this legal premise relies on a decision of ***British Russian Gazette and Trade Outlook Limited v Associated Newspapers Limited*** (1933). The Provider submits that although the release (the Provider's forbearance/settlement) is in a form normally ineffective to discharge a contract and which is executionary on one side only, it will operate as a discharge if the other party (the Provider) agrees to accept some other or additional consideration in return for the right which it abandons.

Chitty states that once a valid compromise has been reached, on mutually acceptable terms, *'… it is open to the party against whom the claim is made to avoid the compromise on the ground that the claim was in fact invalid, provided that the claim was made in good faith and was reasonably believed to be valid by the party asserting it.'*

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It is further noted by ***Chitty*** that in order to establish a valid compromise *'… it must be shown that there had been an agreement (accord) which is complete and certain in its terms, and that consideration (satisfaction) has been given or promised in return for the actual forbearance to pursue the claim. It is a good defence to an action for breach of contract to show that the cause of action has been validly compromised.'*

The Provider submits that as stated in ***British Russian Gazette***, where there is a clear and unconditional discharge, abandonment or release of a claim by one party (the Provider) in return for the promised performance by the other party (the Complainant) of a series of acts, that original claim can never be revived.

Chitty states that *'… the claimant [the Provider] will agree to accept the other party's promise of performance in satisfaction of his claim. The original claim is then discharged from the date of the agreement [the DSA] and cannot be revived.'*

It is stated that it is not open to the Complainant, having fully compromised and settled all debt obligations to the Provider, to seek to re-open the Provider's claim and argue or dispute certain terms and provision of the Provider's claim which cannot be revived.

The Provider also refers to a passage in **Foskett*, The Law and Practice of Compromise***, (2nd ed, 1985) *'… Generally speaking a compromise agreement will discharge all original claims and counterclaims unless its express content provides for their revival in the event of breach.'* It is submitted that it is evident from the DSA that its terms do not envisage that either party can reopen or initiate any further dispute in relation to the matters compromised and agreed in the DSA, which include and refer to the repayment of the debt due by the Complainant as referenced in Schedule 1 - Part 1, the Facility Letter; Part 2 (the Guarantees); and Part 3, the Schedule of Liabilities.

Limitation Periods

The Provider refers to ***section 51*** of the Act and the time limits for making a complaint pursuant to ***section 44(1)(a)***. It is stated that the Offer Letter is dated **29 February 2012** and this letter contains, as a term in the bespoke appendix drafted specifically for the Complainant, reference at clause 8, to the Provider's entitlement to charge surcharge interest where *"… any amount (is) not paid by the Borrower to the Bank by its due date."* Within a very short period of the loan being drawn down, the Complainant defaulted on the express repayment obligations, thus triggering the application of surcharge interest. Accordingly, the Complainant and its advisors were aware and on notice of the existence of the surcharge interest provisions prior to and certainly on the date of the Offer Letter which was negotiated, agreed and signed in excess of 6 years ago, thus being *"… 6 years from the date of the conduct giving rise to the complaint."*

Alternatively, the Complainant became aware or reasonably should have been aware of the application of surcharge interest when same was first charged as of **May 2012** and at various stages thereafter until the DSA was entered into.

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The Provider remarks that at no stage during the period **May 2012** to late **2014** did the Complainant raise any issue or concern with respect to the application or payment of surcharge interest, even though the Complainant *"… became aware, or ought reasonably to have become aware, of the conduct giving rise to the complaint … during this period."*

Further to this, the Provider states that when Complainant entered the DSA, details of the various liabilities would have been brought to its attention, as well as details of interest payable and accrued, including surcharge interest would have been brought to its attentions as part of the negotiations and discussions in advance of execution of the DSA. Specifically, details of the relevant liabilities were set out in Schedule 1, Part 3 and no issues were raised as to the quantum or calculation of these amounts.

At no point prior to the negotiation or execution of the DSA or immediately thereafter did the Complainant raise any issue with the inclusion of surcharge interest as part of the liabilities due to the Provider.

The Provider also submits that there are no reasonable grounds to allow a period of greater than either 6 years or 3 years for the making of this complaint, and it would be unjust and inequitable to do so.

Specific Issues Raised by the Complainant

The Provider submits there are legal complexities to this complaint, and solely relying on High Court and Court of Appeal decisions does not take into account the factual matrix which applied to each individual case and whether relevant terms/provisions in one set of circumstances actually apply or are relevant to this particular complaint. It is stated that the Provider was contractually entitled to apply its surcharge interest rate provisions during **2012** until late **2014** given that the ***Friends First*** decision was not raised at that time, and the ***Breccia*** decision was not determined at that stage. The Provider also draws a number of distinctions between the present complaint and a Legally Binding Published Decision of this Office referenced by the Complainant's representative.

The Provider's letter of **27 March 2018** was followed by an extensive exchange of submissions between the parties.

Jurisdiction

The Provider has advanced two principal grounds as to why this Office does not have jurisdiction to investigate this complaint. First, owing to the complexity of the subject matter, it argues that the courts are the more appropriate forum for determining this complaint. Secondly, it argues that the complaint has not been made within the time limits prescribed by the Act.

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Section 50(2) of the Act states that where a question arises as to whether this Office has jurisdiction to investigate a complaint, *"… the question shall be determined by the Ombudsman whose decision shall be final."*

Dealing with the first point raised by the Provider, ***section 52(1)(f)*** of the Act states that this Office ***may*** decline to investigate a complaint if:

> *"the subject matter of the complaint is of such a degree of complexity that the courts are a more appropriate forum."*

While extensive and detailed submissions have been furnished by both parties, the Provider has not identified what it is about this particular complaint that renders its subject matter *of such a degree of complexity* that it should not be investigated by this Office.

However, having considered the subject matter of this complaint and the parties' submissions, I am not satisfied this complaint has any particular degree of complexity which would require this Office to decline to investigate it pursuant to ***section 52(1)(f)*** of the Act. Therefore, I determine that this Office has jurisdiction to investigate this complaint.

The second point raised in relation to jurisdiction by the Provider is one as to time limits. The time limits for the making of complaints to this Office are set out in ***section 51*** of the Act. The Complainant claims that surcharge interest was wrongfully applied to the loan account the subject of this complaint between **22 August 2011** and **23 November 2014**. However, a complaint was not made to this Office until **1 May 2018**.

During the relevant period, two loan agreements were entered into. The first in **June 2010** and the second in **February 2012**. The facilities restructured on foot of each Letter of Offer were effectively to be repaid within 12 months. In light of the term/duration of each facility, they do not constitute a *long term financial service* within the meaning of the Act. Accordingly, the time limit contained in ***section 51(1)*** of the Act applies, meaning that the complaint must be made not later than 6 years from the date of the conduct giving rise to the complaint. However, ***section 51(5)*** of the Act is also of relevance to a determination as to whether this complaint was made within the appropriate time limit. ***Section 51(5)*** states:

> *"For the purposes of subsections (1) and (2)-*
>
> *(a) conduct that is of a continuing nature is taken to have occurred at the time when it stopped and conduct that consists of a series of acts or omissions is taken to have occurred when the last of those acts or omissions occurred, …"*

Both facilities were in respect of the same loan account number and one was a restructure of the other.

In my Preliminary Decision I stated:

> *…the Interest Audit Findings document prepared by the Complainant's representative shows that surcharge interest was applied up to* ***September 2017****.*

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> *Further to this, in a letter to this Office dated **21 April 2020**, the Complainant's representative explains that surcharge interest was being applied to the loan account up to the date **April 2020**. None of this has been disputed by the Provider.*

However, the Provider has in its post Preliminary Decision submission detailed that "*Surcharge Interest was only charged/applied to the Account between 21 May 2012 and 24 November 2014 (the "**SI Charge Period**")".*

Taking into consideration the Letters of Offer and the Complainant's evidence showing the continued and essentially uninterrupted charging of surcharge interest, I am satisfied the conduct complained of comes within the meaning of ***section 51(5)***. Therefore, I am not satisfied the time limit prescribed by ***section 51(1)*** for the making of a complaint has expired. Accordingly, I am satisfied this complaint has been made within the appropriate time limit.

The Complaint for Adjudication

The complaint is that the Provider wrongfully applied surcharged interest to the Complainant's loan account between **22 August 2011** and **23 November 2014**.

Decision

During the investigation of this complaint by this Office, the Provider was requested to supply its written response to the complaint and to supply all relevant documents and information. The Provider responded in writing to the complaint and supplied a number of items in evidence. The Complainant was given the opportunity to see the Provider's response and the evidence supplied by the Provider. A full exchange of documentation and evidence took place between the parties.

In arriving at my Legally Binding Decision, I have carefully considered the evidence and submissions put forward by the parties to the complaint.

Having reviewed and considered the submissions made by the parties to this complaint, I am satisfied that the submissions and evidence furnished did not disclose a conflict of fact such as would require the holding of an Oral Hearing to resolve any such conflict. I am also satisfied that the submissions and evidence furnished were sufficient to enable a Legally Binding Decision to be made in this complaint without the necessity for holding an Oral Hearing.

A Preliminary Decision was issued to the parties on 3 June 2021, outlining my preliminary determination in relation to the complaint. The parties were advised on that date, that certain limited submissions could then be made within a period of 15 working days, and in the absence of such submissions from either or both of the parties, within that period, a Legally Binding Decision would be issued to the parties, on the same terms as the Preliminary Decision, in order to conclude the matter.

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Following the issue of my Preliminary Decision, both parties made further submissions to this Office, copies of which were exchanged between the parties.

Having considered the parties' additional submissions and all submissions and evidence furnished by both parties to this Office, I set out below my final determination.

The Provider has also in its post Preliminary Decision submission, detailed in response to my statement "*Taking into consideration the Letters of Offer and the Complainant's evidence showing the continued and essentially uninterrupted charging of surcharge interest, I am satisfied the conduct complained of comes within the meaning of* ***section 51(5)"***.The Provider has submitted in its post Preliminary Decision submission that the "*SI Charge Period does not represent "continued and essentially uninterrupted charging of Surcharge Interest"".* Having considered all the evidence and post Preliminary Decision submissions, it would appear that "*interest continued to be charged by* [the Provider], *on the surcharge interest that was applied, on an ongoing basis"* until the loan account was closed.

The Loan Facilities

The Company entered into a loan agreement with the Provider pursuant to a Letter of Offer dated **23 June 2010** (the **First Letter of Offer** or the **First Facility**). Two amounts were advanced on foot of this facility: €3,894,519 and £649,312. The purposes of the advances were to restructure existing facilities. The First Facility was *replaced and superseded* by a Letter of Offer dated **29 February 2012** (the **Second Letter of Offer** or the **Second Facility**). Two amounts were advanced on foot of this facility: €3,938,763.46 and £652,883.13. The purposes of these advances were to restructure existing facilities. In each Letter of Offer, the indicative interest rate was stated as 5.82%.

Dispute over Surcharge Interest

The Complainant's representative wrote to the Provider on **1 December 2017**, taking issue with the application of surcharge interest to the Complainant's loan account. The Provider responded on **12 January 2018** as follows:

> *"… Pursuant to the issue and acceptance of the 2012 Offer Letter by the Company, Statements in respect of the Account post-restructure disclose an Interest underpayment by the Company in March 2012; and no further Interest payments appear to have been made by the Company to the Account until November 2012 – this is in clear breach of the repayment terms and obligations set out in the 2012 Offer Letter which, per clause 12 (i) and (iii) of the terms and conditions in the appendix, are deemed Events of Default.*

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Furthermore, per clause 8A (i) and (iii) of the terms and conditions in the appendix to the 2012 Offer Letter, the Bank was contractually entitled to seek an additional Interest charge from the Company as the stated rate of 0.75% per month (by way of Interest Surcharges) upon the happening of the stated events…

To the extent that the Company failed, with almost immediate effect, to discharge its contractual obligations and make the agreed Interest payments as set out in the 2012 Offer Letter, despite having contracted and agreed to such arrangements …; then, such failure to repay the agree Interest amounts was deemed an Event of Default … entitled the Bank to charge the said Interest Surcharges. …"

The Surcharge Interest Clause

The First Letter of Offer does not reference the surcharge interest provisions. However, the Second Letter of Offer under the section *Interest Rate*, states:

"… Surcharge interest will continue to be charged in accordance with Clause 8 of the Terms and Conditions in respect of the above facilities. …"

Clause 8 of the Terms and Conditions for both facilities is essentially identical and provides for the charging of surcharge interest. Clause 8 states as follows:

*"**8. Interest Surcharges***

8A. Interest Surcharges Rates and amounts on which Interest Surcharges will be charged

An additional interest charge at the rate of 0.75% per month or part of a month (i.e. 9% per annum) subject to a minimum of €2.54 per month will be paid by the Borrower on the following amounts:

(i) any amount not paid by the Borrower to the Bank by its due date.

(ii) any amount not repaid on the Bank's demand where such demand is made in the case of an Overdraft facility or other facility repayable on demand;

(iii) any outstandings which become repayable by the Borrower to the Bank following the occurrence of an Event of Default pursuant to Clause 12 of these Terms and Conditions;
and

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(iv) the amount of any overdrawn balance which has not been authorised by the Bank's prior agreement or any overdrawn balance which is in excess of the overdraft limit authorised by the Bank's prior agreement.

8B. Periods of Accrual of Interest Surcharge

The additional interest charge provided for above shall accrue:

(i) in the case of any sum not paid by the Borrower on its due date, from such date until the relevant sum if paid in full;

(ii) in the case of any sum repayable by the Borrower on the Bank's demand (and whether such sum is outstanding by way of Overdraft or otherwise), from the date of such demand until the relevant sum is repaid in full;

(iii) in the case of any outstandings which have become repayable by the Borrower to the Bank pursuant to Clause 12 of these Terms and Conditions (Events of Default), from the date from which such outstandings become payable or repayable to the Bank pursuant to Clause 12 of these Terms and Conditions until such outstandings are repaid or discharged in full;

(iv) in the case of any unauthorised Overdraft balance or any excess over an authorised Overdraft balance, from the date such authorised Overdraft balance or excess occurs until it is repaid in full; and

(v) in all cases both before and after judgment as appropriate.

8C. Surcharge Interest – Additional

The Borrower shall discharge interest due to the Bank at the rate relevant to the amounts owing by the Borrower to the Bank in addition to any amount of additional interest as provided for in this Clause 8.

8D. When and How Surcharge Interest is Payable

The additional interest charges provided for in this Clause 8 shall be payable by the Borrower to the Bank at the same time and in the same manner as the relevant interest charge, currently quarterly. Such additional interest shall be charged to the Borrower's account or accounts with the Bank.

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8E. Liquidated Damages

Any such additional interest charge as is provided for in this Clause 8 is intended to constitute liquidated damages to the Bank including compensation for its increased administrative and related general costs occasioned by:

(i) the Borrower's default in payment of any amount when due including when such amount becomes due on the Bank's demand; and or

(ii) the Borrower causing any unauthorised Overdraft or any unauthorised excess over an authorised Overdraft limit to occur; and or

(iii) the Borrower otherwise defaulting in respect of the Borrower's obligations to the Bank.

8F. Change in Interest Surcharges

The rate or minimum amount of additional interest charge provided for in Clause 8A above may at any time and from time to time be changed by the Bank at its absolute discretion, subject to approval by the relevant Regulatory Authority.

In the event of any such change or alteration occurring during the continuance of a facility, the Bank will give the Borrower a minimum of 30 days prior notice that such change or alteration is to take place.

Notice under the Clause 8F may be given by the Bank to the Borrower by any means the Bank considers reasonable."

The Law on Surcharge Interest Clauses

According to **Breslin and Corcoran** in ***Banking Law*** (4th ed., Round Hall, 2019, para. 8-037), *"A clause is a loan agreement to the effect that the amount of interest payable upon a default by the borrower is automatically increased, may be unenforceable if, properly construed, it is a penalty."*

The leading Irish authority is the Supreme Court decision in ***Pat O'Donnell & Co Ltd v Truck and Machinery Sales Ltd*** [1998] 4 IR 191, which discussed the distinction between a permissible genuine pre-estimate of damage and an impermissible sum in excess of any actual damage that would possibly or probably arise from a breach.

In ***ACC Bank Plc v Friends First Management Pension Funds Ltd*** [2012] IEHC 435, the question of whether default interest in a loan contract was a penalty was considered by Finlay Geoghegan J. On the evidence, each sides' expert agreed that where a facility goes into default, it would be re-categorised as impaired.

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This classification had cost implications for the lending bank because it would need to set aside an increased level of capital for the anticipated loss. It appears also to have been agreed that the actual cost to the bank would vary according to the nature of the default. Finlay Geoghegan J concluded that the surcharge interest of 6% per annum could not be considered a reasonable pre-estimate of loss. The application of surcharge interest trebled the margin on the facility, and almost doubled the applicable interest rate, and the entire surcharge rate was triggered even if one interest payment fell into arrears. This was not, therefore, akin to the minimal 1% additional interest found to be acceptable and enforceable in the UK decision of ***Lordsvale Finance Plc v Bank of Zambia*** [1996] QB 752.

At paragraph 79 of her judgment, Finlay Geoghegan J expressed the basic rule, as endorsed in ***Pat O'Donnell***, as requiring the court to determine whether or not the additional sum payable is a genuine pre-estimate of the probable loss by reason of the breach. The court should determine whether the predominant contractual function of the provision was to deter a party from breaking the contract or to compensate the innocent party for breach, by comparing the amount that would be payable on breach with the loss that might be sustained if a breach occurred.

In ***AIB v Fahy*** [2014] IEHC 244, O'Malley J accepted that *"a bank is entitled in principle to charge surcharge interest where a borrower is in default"* but held the surcharge interest rate of 12% to be a penalty where a bank offered no evidence as to the basis for its calculation so it could not be seen as a genuine pre-estimate of loss.

Most recently, in ***Sheehan v Breccia*** [2018] IECA 286, the clause under scrutiny before the Court of Appeal provided for a 4% per annum uplift in interest payments. Expert banking evidence was led in the High Court to show that while it was not possible to accurately predict the level of loss that would be incurred on default, banks are likely to incur additional risk and administrative costs when a loan goes into default. The default or surcharge rate was almost double that of the normal interest rate applying under the loan.

The creditor, a co-shareholder in the underlying business, argued that where a precise pre-estimate of damage was impossible and the provision was commercially justifiable, the bargain made between the parties should be respected provided the surcharge was not extravagant or unconscionable. This approach was rejected by the Court of Appeal who indicated that only the Supreme Court could reconsider principles as to whether a surcharge interest clause is or is not a penalty.

Speaking on behalf of the Court of Appeal, Finlay Geoghegan J noted (at paragraph 22) in essence that:

1. The onus of establishing that a clause is a penalty rests on the party alleging this.

2. The question of whether a clause is penal must be assessed at the time the agreement was entered not at the date of breach.

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3. While there is a reluctance on the part of the courts to interfere with the terms of a contract agreed between two parties of equal bargaining power, the willingness to do so in relation to a clause which is determined to be a penalty is an exception to the general rule.

Finlay Geoghegan J held (at paragraph 40) that the question for the court to determine was *"whether or not the additional sum payable is a genuine agreement for the payment of liquidated damaged."* This question then turns on whether or not the additional sum payable represents a genuine pre-estimate of the probable loss to the innocent party by reason of the potential breaches of contract to which the clause applies. The judge accepted that latitude ought to be applied where there is a difficulty in a pre-estimate of the damage suffered where there is probable variation in what loss and damage will in fact be suffered.

As a result, Finlay Geoghegan J held (at paragraph 44) that the question could be phrased as a determination of whether *"the clause is a genuine attempt by the parties to estimate in advance the loss which will result from the breach."* (Emphasis added).

Finlay Geoghegan J concluded that the 4% surcharge interest clause in question was not a genuine attempt to agree upon liquidated damages or estimate the loss which the original lender might suffer by reason of a relevant default. In reaching this conclusion, the judge noted that the clause was contained in the bank's general terms and conditions. Accordingly, it could not have been a genuine advance estimate of the bank's loss arising on a breach of the specific loan agreement between the bank and the borrowers. It was further noted that expert evidence established that the probable loss depends on an interplay between the amount outstanding at the time of default, the value of the security ultimately realised, and the cost in time or effort in achieving these outcomes. Finlay Geoghegan J further accepted that the experts were in agreement that the pre-estimate of probable loss in the event of default formed part of the analysis which the bank did prior to determining the general interest rate to be applied to the facility.

Analysis

The Debt Settlement Agreement

The main point raised by the Provider in response to the Complainant's claim that surcharge interest was wrongfully applied to the loan account is premised on the principle of *Accord and Satisfaction*, in that the DSA entered into in **March 2015**, which is a compromise agreement, precludes the Complainant from now raising the issue of surcharge interest.

The DSA is between the *Obligors* and the Provider. The Company is not included in the definition of *Obligor* or *Party/Parties* as defined in the DSA. In additions to this, clause 9.3 states *"This Agreement shall not become effective or otherwise bind any party unless and until it has been duly executed for and on behalf of all Parties."*

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Although the DSA was executed by individuals who are the directors of the Complainant, there is no evidence to show the DSA was executed by these individuals in their capacity as directors of the Complainant or by/on behalf of the Complainant. Execution of the DSA appears to have been by the *Obligors* in their personal capacity. As such, it has not been established that the Complainant was a party to or bound by the DSA.

The Provider's reliance on the DSA is also weakened by Recital F contained on the first page of the DSA and would seem to run contrary to the Provider's submission outlined above. Recital F states:

> *"F. A table setting out the liabilities of the Obligors and [the Complainant] to the Bank and to [a related entity] is attached at schedule 1 part 3 to this Agreement* ***for illustrative purposes only****. …"* [My emphasis]

Therefore, it is arguable that the inclusion of the Second Letter of Offer in the relevant schedule is for illustrative purposes only and is not capable of binding, or compromising any obligations of, the Complainant.

In light of these matters, I do not accept that the DSA binds the Complainant, nor am I satisfied it precludes the Complainant from making a complaint in respect of the charging of surcharge interest.

Surcharge Interest Clause

Applying the legal principles outlined above, I accept the Complainant bears the burden of establishing that clause 8 is a penalty. In support of its position, the Complainant has referred to case law, the fact clause 8 was not individually negotiated or discussed in respect of either facility at the time they were entered into and it constitutes a generic term. The view is also expressed by the Complainant's representative (which is a financial services firm engaged in advising clients whether, for example, they have been subject to penalty interest rates) that clause 8 is not a genuine pre-estimate of loss.

The question as to whether clause 8 is a penalty is to be assessed at the time the agreement was entered into. The Provider has not made any submission or proffered any evidence to assist this Office in assessing the rationale for including a 9% annual surcharge interest rate at the time each of the facilities were entered into.

The question of whether the agreement provides for the repayment of liquidated damages normally falls to be decided by determining whether the clause is construed as a genuine pre-estimate of loss. Little assistance can be gleaned from the wording of clause 8 in particular clause 8E which simply states *"… Clause 8 is intended to constitute liquidated damages to the Bank including compensation for its increased administrative and related general costs …"* I do not consider this is sufficient to render clause 8 a liquidated damages clause as opposed to a penalty. The real question is whether the clause can be considered as a genuine pre-estimate of loss.

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However, the Provider has not made any submission or furnished any evidence in relation to an advance estimate of the costs or losses that might be occasioned on foot of the Complainant's default. Further to this, the Provider has not identified the factors, if any, that were considered by it when determining that a 9% surcharge interest rate was appropriate to the Complainant as an individual borrower to compensate for whatever costs might arise in the event of default.

It is recognised that latitude ought to be applied when there is a difficulty in a pre-estimate of the damage suffered where there is probable variation in what loss and damage will in fact be suffered. Equally, it cannot be denied that there is a difficulty or likely to be difficulty associated with estimating the probable damage that will be suffered by a lender should a borrower default on a loan facility. This is because probable damage depends on an interplay between regulatory capital requirements, the amount outstanding at the time of default, the extent of the breach, the value of any security ultimately realised, and the cost in time and effort in remedying the default position.

I would also accept the observations by ***Breslin and Corcoran*** (at paragraph 8-044) that *"[a] default interest rate addresses the borrower's impaired credit, the true cost of which is normally impossible to quantify precisely."* Therefore, while latitude should be applied, I would expect some form of explanation from the Provider, who set the rate in clause 8, for its rationale in attributing a 9% surcharge interest rate to the Complainant's facilities. As the matter is phrased in ***Breccia***, there is no evidence before me of *"a genuine attempt of the parties to estimate in advance the loss which will result from the breach."*

The fact a surcharge interest provision is contained in the general terms and conditions of both facilities tends to show that clause 8 could not have been a genuine advance estimate of the Provider's loss arising from a breach of the relevant facility or that it was individually negotiated. The Provider's letter of **5 February 2018**, would support this position:

> *"… Please note that Bank surcharge interest provisions were never open to or subject to negotiation by the Company and apply to all loan facilities provided by the Bank to customers, without exception.*
>
> *To the extent that the provisions contained in the appendix to the 2012 Offer Letter set out standard provisions/obligations, then the Bank is not obliged, nor is intended that we justify or explain the application of the said surcharge interest provisions, which are deemed contractual terms and obligations of the agreement entered into between the Bank and the Company, as signed off by both parties to the 2012 Offer Letter. …"*

There was no reference to surcharge interest in the First Letter of Offer, and while there was a brief reference to clause 8 in the section Letter of Offer, it simply explained the continued application of clause 8 to the restructured facility. I do not consider the reference to clause 8 in the Second Letter of Offer is sufficient to constitute a genuine attempt to estimate in advance the likely damage arising from a breach.

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While the courts had the benefit of expert evidence in the cases referred to above as to whether the clauses in question were penalties, no such evidence has been tendered by the parties to this complaint. However, I believe that I am entitled to have regard to the nature of the evidence required by the courts and tendered by the parties to those cases, to assist me in my consideration of this complaint.

The surcharge interest rate contained in clause 8 is 9%. This is squarely within the range of surcharge interest rates that have been struck down by the courts and almost 4% higher than the interest rate applicable to the Complainant's facilities.

Accordingly, I am satisfied it has been established that clause 8 is a penalty. Moreover, the Provider has not advanced any submissions or evidence to show otherwise. Therefore, on the basis of the relevant legal principles and the foregoing analysis, I am not satisfied clause 8 as contained in the terms and conditions of both Letters of Offer can properly be described as providing for the payment of liquidated damages following default. Rather, clause 8 is designed to deter a breach of contract. Hence, it is more properly described as a penalty as there is no evidence of an attempt by the Provider to estimate in advance, the losses that would result from the Complainant's default under either facility.

Therefore, I am not satisfied the Provider was entitled to apply surcharge interest to the Complainant's loan facilities pursuant to clause 8 and any interest applied to the facilities pursuant to clause 8 was wrong and should not have occurred.

The Complainant maintains that surcharge interest was applied to the loan from **22 August 2011** to **23 November 2014**. This period covers the facilities extended on foot of both Letters of Offer. In my Preliminary Decision, I had stated that the Provider appears to accept that surcharge interest was applied from **May 2012** to **November 2014**. However, no comment is made in respect of the period prior to **May 2012**. Equally, it is not disputed that surcharge interest was applied to the loan for the period claimed by the Complainant. However, it is not clear whether or, if so, on what basis, surcharge interest would have been applied to the Complainant's loan prior to **March 2012**, this being the point when default in the interest repayment occurred.

I had also stated that I noted from the Provider's letter of **12 January 2018** that the Complainant defaulted on its interest repayment obligation in **March 2012**. However, the fact the Second Letter of Offer states that *"Surcharge interest will continue to be charged in accordance with Clause 8 of the Terms and Conditions in respect of the above facilities …"* would tend to suggest that surcharge interest was being applied to the loan prior to the date of the Second Letter of Offer, being **29 February 2012**.

The Provider has, in its post Preliminary Decision submission in response to the above, sought to reassure the Complainant company and this Office that "*Surcharge Interest was not applied to the Complainants' Account at any stage prior to May 2012, save for the SI Charge Period*". The Provider reiterates that "*Surcharge Interest was only charged/applied to the Account between 21 May 2012 and 24 November 2014 (the "**SI Charge Period**")".*

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By letter dated **9 April 2020**, the Provider offered *"… a full refund in the amount of* ***€50,880.10*** *(representing the total amount claimed by the Complainant). …"* The Provider's willingness to refund the amount claimed by the Complainant is welcome. However, it is not entirely clear when surcharge interest was first applied to the Complainant's loan account. Further to this, the Complainant's representative indicated to this Office in a letter dated **21 April 2020** that surcharge interest continued to be applied by the Provider. As outlined earlier, I am not satisfied the Provider was entitled to charge surcharge interest pursuant to either Letter of Offer. This also means that the Provider was not entitled to continue to charge surcharge interest on the loan. Accordingly, any such interest should be refunded to the Complainant.

Therefore, I uphold this complaint and direct that the Provider refund all surcharge interest and also pay a sum of €5,000 in compensation to the Complainant.

Conclusion

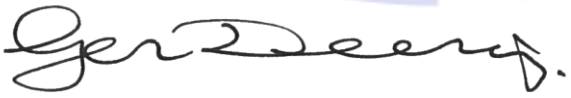
My Decision is that this complaint is upheld, pursuant to ***Section 60(1)*** of the ***Financial Services and Pensions Ombudsman Act 2017***, on the grounds prescribed in ***Section 60(2)(a), (b) and (g)*** *as its conduct was contrary to law, unreasonable and improper.*

I direct pursuant to ***Section 60(4)*** of the ***Financial Services and Pensions Ombudsman Act 2017,*** that the Respondent Provider refund all surcharge interest and also pay a sum of €5,000 in compensation to the Complainant to an account of the Complainant's choosing, within a period of 35 days of the nomination of account details by the Complainant to the Provider.

I also direct that interest is to be paid by the Provider on the said compensatory payment, at the rate referred to in ***Section 22*** of the ***Courts Act 1981***, if the amount is not paid to the said account, within that period.

The Provider is also required to comply with ***Section 60(8)(b)*** of the ***Financial Services and Pensions Ombudsman Act 2017.***

The above Decision is legally binding on the parties, subject only to an appeal to the High Court not later than 35 days after the date of notification of this Decision.



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FINANCIAL SERVICES AND PENSIONS OMBUDSMAN

19 August 2021

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Pursuant to *Section 62* of the *Financial Services and Pensions Ombudsman Act 2017*, the Financial Services and Pensions Ombudsman will publish legally binding decisions in relation to complaints concerning financial service providers in such a manner that—

(a) ensures that—

(i) a complainant shall not be identified by name, address or otherwise,

(ii) a provider shall not be identified by name or address, and

(b) ensures compliance with the Data Protection Regulation and the Data Protection Act 2018.