

Legislation to regulate unfair contract terms in the Bailiwick

Update prepared by Gordon Dawes and Iona Mitchell (Guernsey).

This Update provides a summary of new legislation which will regulate the use of unfair contract terms in the consumer credit and home finance space in Guernsey.

The Lending, Credit and Finance (Bailiwick of Guernsey) Law, 2022 creates a new statutory framework for the protection of retail customers who make use of consumer credit and the provision of home finance. In this Update, the third in the series, we consider the provisions relating to unfair contract terms.

Introduction

The **Lending, Credit and Finance (Bailiwick of Guernsey) Law, 2022** (the **LCF Law**) will regulate the credit and finance sector, in order to protect consumers who make use of services relating to consumer credit. Firms offering or intermediating such services in or from within the Bailiwick, or Bailiwick bodies doing so anywhere in the world, will need to be licensed and regulated by the Guernsey Financial Services Commission (the **Commission**).

The protections will arise in the context of, or with a view to a 'regulated agreement' for the provision of credit. For an overview of what this means, refer to our Update on Part II of the LCF Law, which regulates credit and consumer business, [here](#).

A commencement ordinance, expected to be approved imminently, provides that the LCF Law will come into force in two parts: initially on **1 January 2023** to enable licence applications and **on 1 July 2023** when the LCF Law will be fully operational.

Unfair contract terms

The LCF Law gives the Commission the power to make Rules in respect of consumer protection in connection with business regulated by the LCF Law, including making Rules in respect of unfair contract terms and conditions and unfair practices.

On 21 July 2022 the Commission released the **draft Lending, Credit and Finance Rules and Guidance, 2022** together with a **Consultation Paper** which closed on 15 September 2022. It is anticipated that the final Rules and Guidance will be published by **31 December 2022**.

Part 6 of the Rules effectively prohibits the use of unfair agreement terms in regulated agreements between customers and credit providers and all agreements to provide ancillary services in connection with regulated agreements.

The fairness test

When considering whether a term is unfair, the Commission will apply a test of fairness and transparency. The approach to fairness is similar to that taken in the UK in respect of the Consumer Rights Act 2015. A term will be unfair if, contrary to the requirements of good faith, it causes significant imbalance in the parties' rights and obligations, to the detriment of the customer or client.

The Guidance to the relevant Rule provides more detail as to the fairness test, which has three elements:

- **Significant imbalance.** This is concerned with whether a term is '*so weighted in favour of the business that it tilts the rights and obligations significantly in its favour*', eg if imposing a disadvantageous burden on the customer. A contract may be considered balanced if both parties enjoy rights of equal extent and value, taking into account the nature of the agreement.
- **Customer detriment.** A finding of unfairness does not require proof that a term has already caused actual harm. The fairness assessment is concerned with rights and duties and its focus is on potential, not actual, outcomes.
- **Good faith.** This relates to the substance of terms as well as the way that they are expressed. It is based on the general principle of 'fair and open dealing', where terms are expressed fully, clearly, and legibly, and with due respect for the customer's interests.

Transparency

In considering unfair contract terms, in addition to the fairness test the Commission will also consider transparency, which is about the agreement being in plain, understandable language and legible. Documentation should be drafted so as to put customers in a position where they can make a balanced and informed decision whether or not to enter into an agreement.

Case law applicable in the UK considering the fairness test and transparency will likely be persuasive in Guernsey given that a similar approach is used.

Automatically unfair terms

There are some terms that are automatically considered unfair and must not be used:

- terms which exclude or restrict a business' liability arising from a breach of customer rights provided by law
- terms which relieve a business from providing services with reasonable skill and care
- terms that the Commission deems to be unfair.

The Commission retains discretion as to which terms it deems to be unfair. Schedule 5 to the Rules introduces a list of 20 terms that are not automatically unfair but, in most circumstances, would be considered to be unfair. This non-exhaustive list is drawn from the long list of terms utilised in a similar way in the UK and includes:

- terms which require the customer to pay a disproportionately high compensation for failing to fulfil their obligations under the agreement
- terms which enable the business to alter the terms of the agreement, unilaterally and without a valid reason, which is specified in the agreement
- terms which oblige the customer to fulfil their commitments where the business does not perform their obligations.

Many of the terms listed in Schedule 5 are terms which lack an element of reciprocity; where the business is either permitted or required to do something but equivalent rights and obligations do not apply to the customer.

The Guidance states that there are certain circumstances where a term in this list, which would otherwise be considered unfair, would be permissible. The Guidance provides as an example any changes to the interest rate to reflect the base rate. However the Commission would expect the customer to be notified immediately. The Guidance does not indicate whether a failure to do so would render such a term unfair.

What happens if a term is unfair?

The Rules state that automatically unfair terms will be unenforceable. This means that consumers will be able to proceed as if the unfair terms do not apply and rely upon this in any proceedings brought by or against them.

The Rules also provide that businesses must not enforce unfair terms and customers must be provided with redress in cases where unfair terms have been enforced and must be returned to the position they would have been in had the unfair terms been voided.

The Commission as the regulator of relevant businesses under the LCF Law has the usual supervisory powers in relation to licensees, including to issue directions requiring the directed business to do or not do any thing and to take decisions. As with the other regulatory laws, the Commission's exercise of these powers is subject to a right of appeal to the Royal Court.

What's next?

As stated above, it is anticipated that the final Rules will be published by the end of this year. We expect that there will be some changes around the unfair terms provisions, largely to align more closely with the UK. A large number of Guernsey consumer lenders are already UK regulated and therefore closer alignment with the UK would be beneficial.

The provisions concerning unfair terms only apply to regulated agreements between customers and credit providers and agreements to provide ancillary services in connection with regulated agreements. Since Guernsey does not currently have any equivalent to the UK's Consumer Rights Act 2015 or its predecessor the Unfair Contract Terms Act 1977, contracts outside of this scope will continue to be free from unfair contract terms regulation. In addition, Guernsey remains without any sale of goods legislation.

It is noteworthy that the States of Guernsey even as far back as 16 February 2016 debated and resolved to direct the preparation of general consumer protection legislation, but supervening events took priority and no draft legislation has been released.

More recently, in *Smith v Carey Olsen (Guernsey) LLP* 2020 GRC 062; 2020 GLR 236 Bailiff McMahon declined to develop the common law of Guernsey along the lines of the unfair contract terms legislation in the UK on the basis that the States of Deliberation had resolved to direct the preparation of such legislation. The proper course was to await the enactment of that legislation and the Court should not in the meantime be tempted to fill the gap.

It remains to be seen whether legislation regulating this area more widely will follow, perhaps modelled on the LCF Law.

Watch this space.

Contacts



Christopher Edwards
Partner | Advocate
Mourant Ozannes (Guernsey) LLP
+44 1481 739 320
christopher.edwards@mourant.com



Frances Watson
Partner | Advocate
Mourant Ozannes (Guernsey) LLP
+44 1481 739 331
frances.watson@mourant.com



Gordon Dawes
Partner | Advocate
Mourant Ozannes (Guernsey) LLP
+44 1481 723 466
gordon.dawes@mourant.com



Helen Wyatt
Partner | Advocate
Mourant Ozannes (Guernsey) LLP
+44 1481 731 408
helen.wyatt@mourant.com



John Lewis
Partner | Advocate
Mourant Ozannes (Guernsey) LLP
+44 1481 731 505
john.lewis@mourant.com



Sally Rochester
Director
Mourant Consulting, Guernsey
+44 1481 731 508
sally.rochester@mourant.com

This update is only intended to give a summary and general overview of the subject matter. It is not intended to be comprehensive and does not constitute, and should not be taken to be, legal advice. If you would like legal advice or further information on any issue raised by this update, please get in touch with one of your usual contacts. You can find out more about us, and access our legal and regulatory notices at [mourant.com](https://www.mourant.com). © 2022 MOURANT OZANNES ALL RIGHTS RESERVED