Neutral Citation [2014] IEHC 244

THE HIGH COURT

Record no. 2011/618S

Between/

ALLIED IRISH BANKS PLC.

PLAINTIFF

AND

SIOBHAN FAHY

DEFENDANT

Judgment of Ms. Justice Iseult O'Malley delivered the 2nd May, 2014.

Introduction

1. In this case the plaintiff seeks liberty to enter final judgment in the sum of approximately €1.6m on foot of a loan of €1.3m made to the defendant on the 30th June, 2006. The defendant, who is a solicitor, makes the case that in her dealings with the plaintiff in relation to this loan she was a consumer and that the terms of the Consumer Credit Act, 1995 were not complied with. As a separate issue she contends that certain sums included in the overall figure represent surcharge interest which, she says, is not recoverable in her case.

2. The plaintiff says that it was a commercial loan to which the Act did not apply. It also contends that any surcharge interest charged was justified by reference to the terms and conditions of the loan.

Summary of facts

3. Before dealing with the circumstances of the 2006 loan, it is necessary to set out something of the previous history between the parties.

4. Prior to 2006 the defendant had banked with the plaintiff for some time and had taken out a number of loans. Her relationship manager from 2003 until 2008 was a Ms. Carmel Hayes, who dealt with both her personal and business banking. In late 2004 or early 2005 the defendant also brought the banking business of her practice to the plaintiff.

5. Apart from the ordinary business of her practice (principally litigation and conveyancing), the defendant had also, in 2004, established a business called Home Law Direct. This involved the franchising of a fixed-price conveyancing service to other solicitors. Franchisees paid a stipulated sum to join and also paid 10% of their conveyancing fees plus €600 per month to a separate company called Home Law Direct Marketing Ireland.

6. Separately, the defendant was the beneficial owner of two property development companies called Trezglen Holdings Limited ("Trezglen") and SPF Corporate International Limited ("SPF").

7. In 2005 the defendant had four mortgages on her family home in County Limerick, with a total outstanding balance of about €643,000. Ms. Hayes has said that she believes that about €275,000 of the sums thus borrowed and secured on the home had been related to business and property investment. This was denied by the defendant, who says that the "vast majority" of the money related to personal spending. Neither side has produced any documentation relating to these mortgages. The defendant paid interest on the loans at the bank's normal home loan rate.

8. In June of that year she entered into an agreement to borrow the sum of €950,000 from the plaintiff. According to the plaintiff, it was understood that the purposes of the loan was to clear the four mortgages and to invest the remainder in the expansion of Home Law Direct.

9. The defendant does not accept that it was intended that any substantial portion of this loan was to be used for business purposes. Her evidence is that, in addition to clearing the mortgages, she required €270,000 to repay loans from family members, made in connection with the completion of a purchase of lands in Ballysimon, Co. Limerick. She asserts that she had spent about €40,000 on Home Law Direct and that, because of its business model, it did not require much more capital. She says that the bank was aware of this and of the necessity to repay the family loans.

10. The period of the loan was agreed to be 15 years. Monthly repayments were €5,686. The cost of the credit was €73,501.60. The security was the assignment of various insurance policies and legal charges over the offices of the defendant's practice and an investment property owned by the defendant in Castletroy, Limerick. The defendant's home was not part of the security.

11. At the request of the defendant, the loan account was to be set off against her client account. So long as there were sufficient funds in the client account to cover the loan- i.e. €950,000- the interest on the loan account would be 1 per cent. If the funds in the client account fell below that figure, the interest rate on the loan would be 1 per cent of whatever figure was to the credit of that account, with the rate on the difference rising to the bank's Prime rate plus 1.5 per cent.

12. In applying for this facility on behalf of the defendant, her bookkeeper described what was being sought as a commercial loan, secured against the office building. The purpose of the loan was to clear the current liabilities on the defendant's home, stated to be approximately €650,000

> *"and the balance for Siobhan & Homelawdirect project."*

13. The letter also says that if it would be quicker to process the additional €300,000 first, and leave the mortgage as it was for the time being, that option would be preferred.

14. In making the agreement the plaintiff decided to treat the defendant as a consumer within the meaning of the Consumer Credit Act, 1995. The agreement is clearly drawn up as a consumer contract, with provision for an optional 10- day "cooling off' period. Ms. Hayes's evidence is that this approach was taken because home mortgages were being cleared and she did not want "any ambiguity around it later on."

15. This loan was drawn down on the 27th July, 2005. On the same day €643,000 was applied to clearing the defendant's home loans and the sum of €307,193.65 was lodged to the Home Law Direct account. However, a payment of €270,000 was then immediately made out of the latter account to Denis McDwyer & Co., a solicitor's firm. According to the defendant, this represented the repayment of the family loans relating to the purchase of the lands at Ballysimon. The remaining sum of just under €40,000 was left in the Home Law Direct account for "ongoing administration costs".

16. The defendant says that this was effectively a personal loan and that is the reason why she was treated as a consumer.

17. Payments were made by the defendant in accordance with the terms of this Joan agreement and the balance had been reduced to €900,000 before the next relevant development.

The 2006 facility
18. On the 28th March, 2006 the defendant's accountants wrote to Ms. Hayes, advising her that the defendant intended to liquidate Trezglen and SPF. For this purpose it would be necessary to put the companies in funds in the amount of €400,000 to repay sums owed by the defendant to SPF and to deal with capital gains tax liabilities. It was anticipated that this would eventually result in a distribution of €200,000 to the defendant.

19. It was not suggested by the plaintiff that the €200,000 was to be used to repay any part of the loan but Ms. Hayes says that she believed that this money would be reinvested in the defendant's business. She accepts, however, that she was not told that by the defendant. Mr. Kieran O'Regan, the Head of Business Banking at the time, has said in evidence that he believes that he did have a meeting with the defendant in June, 2006. On the basis of his notes of the meeting he says that he was told that the €200,000 would go into Home Law Direct. The defendant's evidence is that she was not present at such a meeting. She denies having represented to anyone from the bank that the money would be put into the franchise. She says that she received approximately €247,000 from the liquidation, that this was paid into her personal account and that she used it to discharge her personal income tax.

20. The defendant also sought an alteration in the terms of the 2005 loan, to interest-only for a period of one year. This was agreed.

21. An alteration was also proposed in relation to the security for the loan, with the Castletroy investment property being removed and replaced by the lands in Ballysimon. The plaintiff says that this proposal came from the defendant. She denies this and says that she queried the necessity for it, but was told that she would not get the loan unless she agreed.

22. A letter of sanction for a facility of €1.3m (being the sum of €900,000 outstanding on the 2005 loan plus the €400,000 now requested) issued and was signed by Ms. Hayes and the defendant on the 30th June, 2006. The document states the purpose of the loan as being

> *"Reimbursement of funds owed to SPF Corporate Int and subsequent reinvestment into Home Law Direct Franchise."*

23. The defendant says that she did not take issue with this because she never saw the letter and indeed she claims that she was not given an opportunity to read it. She signed it because she would not otherwise get the loan.

24. A similar arrangement as described above was put in place regarding the defendant's client account, which was now required to have a minimum of €1.3m in it to set off against the loan funds.

25. The rate of interest was provided for as follows:

> *"1% set off against funds on client's current account no 18130088 and in the event of there being insufficient funds in same the Banks Prime rate varying, plus 1.500% per annum, will apply currently 4.875% per annum."*

26. The monthly repayments were stated to be as follows:

> *"Interest only payments of EUR 1,084 pm to be provided year one with capital & interest repayments of EUR 8,294 pm thereafter over remaining 14 years assuming sufficient funds in Solicitor's clients account for duration of loan."*

27. Ms. Hayes has said that the defendant was not treated as a consumer in relation to this loan because she believed it to be a business facility. She did not refer to the home loans because they had been cleared. However she accepts that the outstanding €900,000 of the 2005 loan was encompassed in the new facility.

28. The defendant contends that the original €950,000 was effectively included in this loan, and that since a large proportion of that sum had been for the purpose of clearing home mortgages, it was incorrect to treat the later facility as being purely business-related. She further states that she had never intended to use the loan for investment in Home Law Direct, since its business model entailed very little in the way of expenditure. She does say that she may have told the plaintiff that Home Law Direct had a "short term need" for about €40,000 or €50,000, and there might have been a "vague mention" of putting in this amount after the tax arising from the liquidations had been paid.

29. The loan was, in the first sentence of the letter of sanction, expressed to be subject to the Bank's General Terms and Conditions governing business lending, as set out in a booklet dated March 2006. The relevant part of this booklet is the section dealing with the calculation of interest. Under the heading "Surcharge Interest" it reads as follows:

> *"Unscheduled or unauthorised borrowings by a Customer oblige the Bank to arrange impromptu funding in the money market and generate additional administrative activities. This gives rise to costs, expenses and risk to the Bank which are covered by the application of surcharge interest. Surcharge interest, in addition to the interest applicable to the facility, will be charged:*
>
> > *(i) where the balance (or the net aggregate balance) on any account(s) exceeds the relevant limit or an account is overdrawn without a sanctioned limit ("excess balances'}; and*

(ii) where any residual debit balance remains unpaid after the Bank has demanded payment or after the expiry of the review date or the repayment period of a facility, without the Bank's agreement to extend or renew the facility ("residual balances').

30. The booklet states that the surcharge rate of interest is subject to change from time to time. Changes are to be notified by publication in at least one national newspaper and information regarding the rate is at all times available in the bank.

31. Mr. O'Regan, the head of the business banking section, says that surcharge interest is calculated automatically once a customer is outside his or her loan agreement. In a set-off situation, where the credit funds were less than the amount of the loan that would attract higher interest "and possibly a surcharge."

32. Ms. Hayes has said that a copy of the booklet was furnished to the defendant.

33. On the 30th June, 2006, the day the letter of sanction was signed by both parties, Ms. Hayes gave the defendant a draft for €290,000 for SPF. This company had its account in a different bank. The sum of €110,000 was lodged to the account of Trezglen.

34. Ms. Hayes says that the lodgement to Trezglen was made on the defendant's instructions - this is denied by the defendant, who says that for tax reasons she did not want it to happen. No lodgement docket has been produced by the bank. The defendant has said in evidence that she "can only assume" that it was arranged by her accountant and the bank, but she does not know if this was so. She did not make any complaint about it because she did not see the relevant bank statements, being too busy with other matters.

35. The defendant's evidence is that after the liquidations, approximately €180,000 was paid in respect of tax liabilities. About €14,500 of the Trezglen monies and about €32,000 of the SPF monies "came back into the office". Approximately €246,000 "came back" to her. This was lodged in her personal account.

36. The defendant has put into evidence certain internal memoranda obtained by her from the bank under the Data Protection Act. Some of these post-date the loan agreement and contain the views of bank officials and their advisors on the issues between the parties. These do not appear to me to be relevant.

37. There are three pages of memoranda which were presented to the court in booklet form as being three separate items but were on occasion treated in evidence as a single document. It is difficult to contextualise them since there is no apparent beginning or ending, whether they are read singly or cumulatively. They are not dated or paginated, but appear to have been created by Ms. Hayes.

38. The first page states that no accounts were yet available for Home Law Direct but cites management figures for the periods ended July 2005 and July 2006. Projections are given for 2007 and 2008. Notes in relation to the drawings and income of the franchise indicate that the defendant had invested €350,000 of her own funds in it in 2005. There is also reference to the fact that a legal dispute had arisen in relation to the Ballysimon purchase, whereby the defendant

"incurred substantial cost & EUR270k to repay family loan".

39. It seems to me that this document could not have been written in 2005, having regard to the 2006 figures in it. It does not, therefore, support the contention that the purposes of the 2005loan included repayment of the €27,000.

40. The second page is headed "Report and Recommendations". It gives a brief description of the defendant and the Home Law Direct project. Under the heading "Proposal" there is the following passage:

"Client is now seeking a loan facility of 950k over 15 years on a 1% set off against clients funds.

She will utilise 639 of this facility to clear existing home mortgage on her PDH ...

The balance of 311k is required to further fund expansion of the Home LA Direct Franchise and to cover Working Capital pending inflow of client fees.

To date client has spent 70k on this project which was utilised to fund marketing, stationery, consultancy fees and web site set up."

41. I think it is obvious that this was written in contemplation of the 2005 loan.

42. The third page refers to the fact that the bank holds a charge over the office premises and goes on to say that there is an offer of a charge over the Ballysimon lands, which the writer regards as a valuable property. The following quotation comes under the heading "Recommendation":

"Siobhan Fahy to date has spent significant time and money (EUR350k to date) into setting up the Home Law Direct Franchise. As can be seen she has sold the franchise to 11 firms already well spread all over the country and she is currently working on 4 other locations. These franchises have to provide a minimum of EUR 20k pa to Homelaw Direct Ireland. This income stream has only started to come on line since 03/06.

We are dealing here with a woman of substantial legal experience whose initiative is now being recognised as a market leader. She has incurred significant start up costs in Homelaw Direct but the potential is now being recognised ...Ultimately client intends to build the franchise further and sell on the business at some future date.

Client and Accountants have met with Kieran O'Regan & discussed this case indepth. As a result we are supportive of this additional facility..."

43. In my view this document must have been written in 2006.

44. The defendant made payments on foot of the loan until January 2011, when she terminated all relevant standing orders.

Relevant statutory provisions

45. It is common case that if the defendant was in fact acting as a consumer in taking out the 2006 loan, the contract falls foul of the provisions of the Consumer Credit Act, 1995 and the plaintiffs claim must fail. This is because of the mandatory nature of s. 30, which stipulates that a "cooling off' period must be provided. Non-compliance with the section may not be overlooked by the court and results in the contract being unenforceable.

46. Section 2 of the Act (as amended by Part 12 of Schedule 3 of the Central Bank and Financial Services Authority of Ireland Act, 2004) defines the term "consumer" ins. 2 as "*a natural person acting outside the person's business.*"

47. "*Business*" is defined as including "*trade and profession*".

Submissions on the consumer contract issue
48. Counsel for the parties are agreed upon the following propositions - that the court cannot split the loan into constituent elements; that a person may have more than one business, trade or profession and that the defendant bears the burden of establishing that she was a consumer.

49. It is also agreed that the issue to be determined by the court cannot be decided by reference to the security given for the loan or to the applicable interest rate.

50. The plaintiff relies on the authority of *Allied Irish Bank v Higgins* and submits that the loan related, either in its entirety or to a significant extent, to purposes inconsistent with the defendant acting in the capacity of a consumer. If the purpose was mixed, it is submitted in reliance on *Gruber* that it could be treated as a consumer contract only if the commercial aspect was negligible.

51. On behalf of the defendant it is submitted that her business was conveyancing and the Home Law Direct franchise and that in taking out the loan she was acting outside these areas. The purposes of the monies advanced in 2005 were, it is argued, to clear the home loans and to repay family loans. Both of these are described as personal. Since the bank treated her as a consumer for that transaction, she remained a consumer in relation to it. The 2006 loan was, and was treated by the parties as, a top-up to the 2005 facility and she should therefore have continued to be treated as a consumer.

52. The defendant relies on *Standard Bank London v Apostalakis* [2002] C.L.C. 933 as an example of persons entering into a contract for the purposes of profit but nonetheless being held to be acting outside their trade or profession.

Authorities on consumer contracts
53. The leading Irish judgment on the issue as to the applicability of the Act in this context is *Allied Irish Bank Plc v Higgins* [2010] IEHC 219. In that case the defendants had formed a partnership with the intention of acquiring lands for development. The plaintiff had advanced a number of loans to them for this purpose. In resisting an application for summary judgment, the defendants all adduced evidence that they were not professionally involved in the business of property development. They therefore contended that they had an arguable defence by virtue of the provisions of the Act, in that they were acting outside their business when they borrowed the money. The bank said that it was a commercial transaction.

54. Kelly J. noted that the object of the partnership, in buying and developing the lands, was to make a profit. Having regard to the evidence of the defendants he accepted that property investment was not their principal or main business. However, he rejected the proposition that for the purposes of the Act a person could have only one business or trade or profession, outside of which any borrowings must be made as a consumer. He referred to the following definition of a consumer in Council Directive 87/102/EEC, as amended by Council Directive 90/80/EEC:

> *"a natural person who, in transactions covered by this Directive, is acting for purposes which can be regarded as outside his trade or profession",*

noting that it did not materially differ from that in the Act.

55. Having had regard to the fact that s. 18 of the Interpretation Act, 2005 provides that, unless the context otherwise requires, the singular imports the plural, Kelly J went on:

> *"Second, the interpretation urged by these defendants would have the most profound consequences in business and commercial life. It would mean that every person who belonged to a trade or profession and who decided to borrow money to invest it in promoting another business with a view to profit would have to be treated as a consumer under the Act. The legislature could never, in my view, have so intended. If it did it would have said so in clear and unequivocal terms."*

56. The judgment also refers to the decision of the European Court of Justice in *Benincasa v Dentalkit* (Case C-269/95). In that case, a franchising agreement had been entered into for the use of Dentalkit's equipment and trademark in a dental practice. A dispute having arisen, the claimant argued that he had not made the contract in the course of or for the purpose of his trade or profession because it was only in contemplation of such trade or profession.

57. In the course of its judgment the Court, having referred to the Directive definition cited above, said:

> *"As far as the concept of 'consumer' is concerned, the first paragraph of Article 13 of the Convention defines a 'consumer' as a person acting 'for a purpose which can be regarded as being outside his trade or profession'. According to settled case-law, it follows from the wording and the function of that provision that it affects only a private final consumer, not engaged in trade or professional activities.*
>
> *It follows from the foregoing that, in order to determine whether a person has the capacity of a consumer, a concept which must be strictly construed, reference must be made to the position of the person concerned in a particular contract, having regard to the nature and aim of that contract, and not to the subjective situation of the person concerned. As the Advocate General rightly observed in point 38 of his Opinion, the selfsame person may be regarded as a consumer in relation to certain transactions and as an economic operator in relation to others.*
>
> *Consequently, only contracts concluded for the purpose of satisfying an individual's own needs in terms of private consumption come under the provisions designed to protect the consumer as the party deemed to be the weaker party economically. The specific protection sought to be afforded by those provisions is unwarranted in the case of contracts for the purpose of trade or professional activity, even if that activity is only planned for the future, since the fact that*

an activity is in the nature of a future activity does not divest it in any way of its trade or professional character."

58. It is important to note also that Kelly J. considered that, since "the subjective situation of the person concerned" was not the decisive factor, the subjective view of the plaintiff bank, whether right or wrong, was of no relevance.

59. In his conclusions on the issue, Kelly J. said

> *"These defendants acted as partners in a partnership which borrowed money from AIB. They did so with a view to investing in property and its development for profit. In so doing they engaged in business and the Act had no application to them."*

60. *Gruber v BayWa AG* (Case C-464/01) concerned the applicability of the consumer provisions of the Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters 1968. The claimant sought damages for defective tiles used to reroof a building which was used partly as his dwelling house and partly for his farming purposes. The issue was whether he had contracted for goods for a purpose outside his trade or profession, which would entitle him to rely upon special jurisdictional rules.

61. On a reference from the national court, the European Court of Justice held that where a person concluded a contract relating to goods intended for purposes which were in part within and in part outside his trade or profession, he could only rely upon the special rules for the protection of consumers if the "trade or profession" element was so limited as to be negligible. In determining the issue, a court should take into account the content, nature and purpose of the contract and the circumstances in which it was concluded.

62. *Standard Bank London Ltd v Apostolakis* [2002] C.L.C. 933 is a judgment of the English Commercial Court on certain preliminary issues in an application for summary judgment, one of which was whether or not contracts entered into between the parties were consumer judgments. The defendants, a Greek married couple, were a civil engineer and a lawyer. They entered into and agreement with the plaintiff bank whereby the latter was to purchase ECUs on their behalf in exchange for drachmas. Unilateral action by the bank taken on foot of a devaluation of the drachma resulted in litigation in both the Greek and English courts.

63. In holding that the contracts were consumer contracts, Longmore J. ruled that despite the size of the contracts the defendants had been acting outside their trade, business or profession. They were not engaged in the trade of foreign exchange contracts as such, but were simply disposing of income in the hope of making a profit.

64. Longmore J. distinguished *Benincasa* on the basis that the factual situation was very different. He doubted whether the Court of Justice had intended to substitute the words "for the purpose of satisfying an individual's own need in terms of private consumption" for the definition in the Directive.

Discussion on the consumer contract issue

65. The primary issue for determination is the position of the defendant in entering into the loan agreement, having regard to the nature and aims of that agreement.

66. I find that much of the defendant's evidence in relation to the nature and aims of the agreement is unsatisfactory and unsupported by either documentation or, as might be expected, evidence from her financial advisors. To take one example, she disputes the assertion by the plaintiff that she had invested or intended to invest significant sums in Home Law Direct. Where the plaintiff refers to her having spent €350,000, she says that it was €40,000. She has not produced accounts or bank statements to back this up.

67. I do not accept her evidence that she was not given an opportunity to read the letter of sanction. I find it highly unlikely that a person of her legal and business experience would accept such treatment at the hands of a bank with which she was, at the time, doing a lot of business. If in fact she did not read it, I consider that she would nonetheless be bound by her signature.

68. However, I do not consider it necessary to go through the evidence in detail because, in my view, the most important consideration is this: the initial application made on her behalf for this facility was made for what were unquestionably business purposes. The defendant was the full beneficial owner of two property companies. She was engaged in the property business, through them and, it seems, in her own personal capacity- the court is not definitively aware of who the legal purchaser of the Ballysimon lands was. She wished to liquidate the companies and funds were needed to this end.

69. Further, the bank was told in the application that at least some portion of the proceeds would be invested in Home Law Direct.

70. These were business purposes, and in making the application she was acting in the course of business. There has been no suggestion that her accountants were not authorised to put the application in these terms. The funds advanced were, as a matter of fact, paid to the two companies. I note here the defendant's evidence that she did not authorise the payment to Trezglen - again, one would expect some evidence from the persons who dealt with the bank on her behalf in this regard.

71. It is not clear which party proposed that these funds should be advanced by way of a new facility encompassing the existing one. However, whether she asked for, or was offered, the option to transfer her existing loan into the new arrangement, she was in my view still in the position of a person seeking a business facility. She did not cease to act in a business capacity in making the decision to incorporate the old loan. As the Court of Justice said in *Gruber*,

> *"Where a contract simultaneously serves both private and trade or professional needs, it may be possible to determine the proportion of the contract within each category. It is not however possible to deem the customer to be, in that proportion or indeed in any other proportion, both in a weaker position than the supplier and on an equal footing with him in relation to one and the same contract."*

72. The defendant was not in any way disadvantaged by not being treated as a consumer- any rights that she had in that capacity had been fully respected in the 2005 transaction, and she was not taking on any new liabilities in respect of any consumer aspect of the existing loan.

The surcharge interest

73. The plaintiffs claim includes a sum of €94,602.06 by way of surcharge interest. Such interest was levied for four separate quarters between December 2008 to March 2010 at a rate of 12% of the net balance. After March 2010 no surcharge interest was charged.

74. According to the evidence of Ms. Jean Ryan on behalf of the plaintiff,

"The net balance is arrived at by taking the debit balance on the loan account less the credit funds."

75. The "credit funds" in this instance were the monies in the client account. Ms Ryan stated that the interest was calculated on a daily basis and was charged to the loan at the end of the quarter.

76. What appears to have happened is that, at a time after the expiry of the "interest only" period, the level of funds in the client account began to fall below the loan level and the surcharge figure of 12% then came into play. However, at a certain stage a "no surcharge" flag was placed on the account. This appears to have been on foot of representations made by the defendant.

77. Ms Ryan was not in a position to say what the basis for the 12% rate was, simply stating that it was the applicable rate and that surcharge interest was provided for in the general terms and conditions.

Submissions on interest
78. The defendant's complaint is that there is no evidence as to how the rate came to be set at 12%. It is argued that there is therefore no evidence as to whether it was a genuine pre-estimate of the cost to the plaintiff of default on the part of the defendant, and that it should in the circumstances be regarded as an unenforceable penalty. In this respect reliance is placed on the judgment of Finlay Geoghegan J in *ACC Bank v Friends First Managed Pension Funds Limited* [2012] IEHC 4325.

79. The defendant also says that there is no evidence that the plaintiff informed her of the applicability of the rate of 12%, whether by notification in the branch premises or by advertisement in a national newspaper.

80. In *ACC Bank v Friends First*, part of the plaintiff bank's claim depended on a clause in its General Conditions providing that if the borrower defaulted in the payment on the due date of any sum payable under a facility, this would give rise to a liability to pay interest at 0.5% per month above the rate otherwise applicable to the facility. This rate was therefore applicable not just to default in relation to the principal sum, but to any default in relation to interest, costs or charges. The issue was whether this was a penalty, intended as a deterrent against default, or a genuine pre-estimate of loss, within the meaning of the principles established in *Dunlop Pneumatic Tyre Company Ltd v New Garage and Motor Company Ltd* [1915] AC 79.

81. It should be noted that Finlay Geoghegan J. considered that the burden of establishing that the imposition of the surcharge interest was a penalty rested on the defendant.

82. Both parties called expert evidence on the matter. The witnesses were agreed on a number of issues, including the fact that banks were obliged to attach a "probability of default" factor to each loan that they make and that default on a facility carried cost implications for a bank, because of the need to set aside an increased level of capital for the anticipated loss. The plaintiffs expert considered that 6% per annum was a "minimal reflection" of this cost. The defendant's expert, whose evidence was accepted by Finlay Geoghegan J., was that a generic pre-estimate of additional loss, covering all types of default, was not possible. The learned judge stated that she was further influenced by the fact that the charge increased the agreed margin in the facility letter by a factor of three. She therefore held that the charge could not be considered as a genuine pre-estimate of its loss or of the additional costs to the plaintiff of providing capital in the event of default.

83. The plaintiff in the instant case points to the reference in the letter of sanction to the general terms and conditions document and argues that the terms relating to surcharge interest therein form part of the contract. It says that the defendant's account was in default after the expiry of the interest only period of the facility and the entitlement to levy the charge arose because of that default.

Discussion on surcharge interest issue
84. I accept that the onus is on the defendant to establish that the claimed charge amounts to a penalty. I further accept that a bank is entitled in principle to charge surcharge interest where a borrower is in default. However, the borrower is entitled to challenge the bank's evidence as to the basis for the charge with a view to undermining the contention that it is a genuine pre-estimate of loss.

85. In this case the plaintiff has offered no evidence at all as to the basis for the rate of 12%. The contractual terms as set out in the booklet of terms and conditions refer only to the factual situations in which surcharge interest will be charged but give no guidance as to how it will be calculated.

86. Having regard to the fact that the interest rate in the letter of sanction, set out in paragraph 22 above, already made provision for an increase in a situation where the credit funds were insufficient (and thus had already made provision for the increased possibility of impairment of the loan), and having regard to the absence of evidence in relation to the surcharge rate, I do not consider that the level of 12% can be seen as a genuine pre-estimate of loss. It appears to be more in the nature of a penalty and therefore unenforceable.

Conclusion
87. The plaintiff is entitled to judgment in the amount claimed, less any element related to surcharge interest.