

IN THE HIGH COURT OF JUSTICE
QUEENS BENCH DIVISION
COMMERCIAL COURT

BETWEEN:

THE OFFICE OF FAIR TRADING

Claimant

-and-

- (1) ABBEY NATIONAL PLC
(2) BARCLAYS BANK PLC
(3) CLYDESDALE BANK PLC
(4) HBOS PLC
(5) HSBC BANK PLC
(6) LLOYDS TSB BANK PLC
(7) NATIONWIDE BUILDING SOCIETY
(8) THE ROYAL BANK OF SCOTLAND GROUP PLC



Defendants

**THE OFFICE OF FAIR TRADING'S
JOINT REPLY AND DEFENCE TO COUNTERCLAIMS**

REPLY

- 1 Each of the defendants ("the banks") in its defence and counterclaim makes certain allegations that, despite some variations in the way in which they are put, appear in substance to be common to all or, in the case of some allegations, most of the banks. The common allegations cover the substance of each of the cases advanced by the banks. The claimant ("the OFT") replies to them in this joint reply. Individual replies for each bank are contained in the schedules hereto, as follows:

- 1.1 Schedule 1: Abbey National plc
 - 1.2 Schedule 2: Barclays Bank plc
 - 1.3 Schedule 3: Clydesdale Bank plc
 - 1.4 Schedule 4: HBOS plc
 - 1.5 Schedule 5: HSBC Bank plc
 - 1.6 Schedule 6: Lloyds TSB Bank plc
 - 1.7 Schedule 7: Nationwide Building Society
 - 1.8 Schedule 8: The Royal Bank of Scotland Group plc.
- 2 It is the banks that assert that the Unfair Terms in Consumer Contracts Regulations 1999 (“the Regulations”) do not apply to the Relevant Terms (as defined below) by reason of the alleged exclusion contained in Regulation 6(2). The OFT advances the allegations in this reply without prejudice to the burden of proof, which is on the banks. Alternatively, whether Regulation 6(2) excludes the Relevant Terms from any assessment of fairness is a question on which neither party has the burden of proof, and is for the assessment of the court.
- 3 In this reply:
- 3.1 references to a numbered regulation are references to the numbered regulations contained in the Regulations;

- 3.2 references to the current terms and conditions are references to the current terms and conditions of the banks' respective Current Account Contracts (as defined in paragraph 4 below);
- 3.3 references to the historical terms and conditions are references to the sample of historical terms and conditions of the banks' respective Current Account Contracts; and
- 3.4 for the sake of simplicity, the OFT uses only the present tense when describing the content and effect of the Relevant Terms (whilst acknowledging that some of the Relevant Terms are no longer current).

I. THE OPERATION OF CURRENT ACCOUNT CONTRACTS

Current Account Contracts

- 4 All of the banks provide a current account for their consumer customers pursuant to contracts that incorporate (it is be assumed, for the purposes of these proceedings) the banks' standard form terms and conditions. A contract incorporating such standard form terms and conditions is called "the Current Account Contract" in this reply. (The OFT makes no admissions as to whether and how standard form terms and conditions have been incorporated in the case of any particular contract between a bank and a customer, or as to any steps taken by the banks to draw their customers' attention to the charges that are the subject of these proceedings.)
- 5 The Current Account Contracts have the following characteristic features that, as further pleaded in section II below, are the main subject matter of the Current Account Contracts for the purposes of the Regulations:
- 5.1 The customer grants the bank a loan, repayable on demand, that the bank credits to the current account.

- 5.2 The customer may deposit cash, cheques and other payments (and thereby increase the amount of the loan credited to the account).
- 5.3 In so far as the account is in credit, the customer has the right to withdraw money (and thereby reduce the loan).
- 5.4 In so far as the account is in credit, the customer has the right to instruct the bank to make payment to third parties (and thereby reduce the loan).
- 6 The banks offer their customers a range of further optional services, including overdraft facilities, under certain Current Account Contracts. Such further services are not, however, necessary for the operation of a current account, which can work without them. Moreover:
- 6.1 Overdraft facilities are not offered as part of all current accounts provided by the banks to their customers. For example, Abbey National plc operates a “Basic Account” which provides the services referred to paragraph 5 above, but under which overdraft facilities are not available.
- 6.2 An overdraft facility is usually provided only on the customer’s express request. The banks take into account the customer’s financial standing, among other things, when considering such requests. The banks can, and do, refuse such requests.
- 7 Further, the main reason why customers open current accounts is so that they can receive the services described in paragraph 5 above.

Available funds, sufficient funds and insufficient funds

- 8 At various points in this reply, the OFT refers to a current account having “available funds”, “sufficient funds”, or “insufficient funds” for a payment or withdrawal:

8.1 “Available funds” means the funds at the disposal of the customer for payment or withdrawal at the time that such payment or withdrawal is processed by the bank, taking into account:

- (a) any cleared funds in the account;
- (b) plus any overdraft facility;
- (c) plus any other funds that the bank may put at the customer’s disposal, such as credit balances from cheques that have not cleared;
- (d) less any payments that, though they have not been debited, the bank may deduct from the available funds because the bank considers that they are or soon will be due for payment (for example, the bank may set aside funds to cover a debit card payment that has been automatically authorised).

8.2 Some instructions for payment or withdrawal are processed almost instantly, when they are instructed, such as cash withdrawals from ATM machines, transactions conducted over the counter and immediate online transfers. For such transactions, the available funds are reckoned when the customer attempts the transaction. Other transactions, such as cheques, direct debits and standing orders, are typically processed in batches in the early hours of the morning. The available funds for these transactions are reckoned as at the end of the previous day.

8.3 A customer has “insufficient funds” at the time that a payment or withdrawal is processed where the amount of the available funds is less than, and “sufficient funds” where the amount of the available funds is equal to or more than, what is necessary to meet a payment or withdrawal instructed by him.

Overdraft facilities

- 9 Where a bank grants an overdraft facility, it expressly agrees with its customer that he may have credit on his current account up to a specified limit. The bank must have the funds available for the customer, whether or not he draws down the facility, and, for this reason, may charge a fee.

Temporary loans

- 10 Where a customer instructs a bank to make a withdrawal or payment (whether to the bank or a third party) for which he has insufficient funds in his account, the bank is not obliged to honour the instruction (except in the case of guaranteed cheques or any other payment method where the bank is contractually bound to a third party to meet the payment). The bank may nonetheless honour the instruction and grant the customer a temporary loan of the amount necessary to cover the payment or withdrawal (a “temporary loan”). The temporary loan is debited to the customer’s account.

- 11 A temporary loan also arises under the Current Account Contracts when the customer’s account goes into overdraft (without any overdraft facility), or beyond any agreed overdraft limit, by reason of any of the following:

- 11.1 the bank levying a Relevant Charge (as defined in paragraph 20 below);
- 11.2 the bank charging other fees;
- 11.3 the bank charging interest; or
- 11.4 a previous credit being reversed (such as when a cheque that has been paid into a customer’s account is returned unpaid).

Authorisation limits

- 12 Each of the banks sets internal limits (referred to as “authorisation limits” in this reply, but also known by other names, such as pencil limits and shadow limits) on each customer’s current account for the purposes of determining whether or not to honour an instruction for payment or withdrawal. Authorisation limits may vary according to the method of payment involved, but are typically structured in the following ways.
 - 12.1 There may be a debit balance limit within which an instruction for payment or withdrawal is automatically met, provided that it would not cause the limit to be exceeded, and above which the instruction is automatically refused.
 - 12.2 Alternatively, there may be a debit balance limit within which an instruction for payment or withdrawal is automatically met, provided that it would not cause the limit to be exceeded, and above which the instruction is referred for further consideration by a person or an automated process to determine whether to honour or refuse the instruction. There may be a further, higher limit above which instructions are automatically refused.
- 13 The banks usually set authorisation limits when the current account is opened. The limits are based on an assessment of the customer’s creditworthiness and may be revised from time to time.

Buffers

- 14 Where a customer has insufficient funds for a payment or withdrawal that he has instructed, some of the banks provide a temporary loan without levying a charge if the amount required to meet the payment or withdrawal is within certain predefined, low limits. The limit within which a charge is not levied is often referred to as a “buffer”. Different buffers may apply to the various Relevant Charges (as defined in paragraph 20 below). Some of the current and

historical terms and condition disclose the buffers to the customers. Others do not.

The banks' systems for dealing with customers' instructions

- 15 A bank providing current account services must have systems and processes (“Payment Systems and Processes”) for determining whether to comply with customers’ instructions for payment and withdrawal.
- 16 As more fully particularised in Annex A hereto:
 - 16.1 All instructions involve, at some stage, a programmed automated assessment of the instruction.
 - 16.2 The assessment and execution or refusal (as the case may be) of some instructions may be entirely automated.
 - 16.3 Some instructions involve manual handling (notably, cheques).
 - 16.4 Comparatively few instructions involve someone within the bank exercising a discretion, when the instruction is received, to honour or refuse the instruction.
 - 16.5 Some instructions involve a combination of one or more of the above.
- 17 The resources required to deal with a particular instruction for payment or withdrawal for which the customer has insufficient funds may not be greater than those required to deal with a particular instruction for which the customer has sufficient funds. The actual resources required will depend on the circumstances, including:
 - 17.1 the method of instruction that the customer has used;

- 17.2 the authorisation limit or limits that the bank has set on the account; and
- 17.3 the amount of the shortfall in the available funds relative to the authorisation limit or limits that the bank has set on the customer's account.

The charges levied if the customer has insufficient funds

- 18 The banks have the right to amend their standard form terms and conditions at any time on giving notice. Each of the banks in recent years has changed from time to time the characterisation and description of the charges levied when a customer instructs a payment out of, or withdrawal from, his current account that, if honoured, would result in his account going overdrawn (without any overdraft facility) or above a previously agreed overdraft limit.
- 19 However, the true nature of such charges and the circumstances in which they are levied have not materially changed during the period for which the banks have supplied the current and historical terms and charges.
- 20 All of the banks' terms and conditions provide for charges ("the Relevant Charges") to be made where instructions for payments and withdrawals are received, or interest or charges or fees are levied, for which the customer has insufficient funds. The charges, which are referred to in paragraph 10 of the amended particulars of claim, are given various names by the banks but in substance comprise four basic types, some or all of which are charged by all the banks, as follows:
- 20.1 Unpaid Item Charge;
- 20.2 Paid Item Charge;
- 20.3 Overdraft Excess Charge; and

20.4 Guaranteed Paid Item Charge.

Unpaid Item Charge

21 This is a charge that is levied when the customer gives an instruction for payment or, in some cases at least, withdrawal, that the bank declines to honour because the customer does not have sufficient funds in his account.

22 Annex B hereto sets out:

22.1 the Unpaid Item Charge payable under each bank's current terms and conditions for its main current account(s); and

22.2 the extent to which the banks' current terms and conditions, or any explanatory document provided to customers, identify the methods of payments that may or may not give rise to the charge.

23 Some of the Unpaid Item Charges are subject to limits (often called "caps") on the number of charges that will be levied within a specified period. In some cases, the caps are disclosed to the customer. In others, they are not.

Paid Item Charge

24 This is a charge that is levied when the customer gives an instruction for payment or, in some cases at least, withdrawal, for which he has insufficient funds in his account and which the bank honours. (Where the payment has been made by a method of payment that is guaranteed, and that the bank is therefore obliged to honour, some of the banks levy a different charge, as explained in paragraph 32 below.) Some Paid Item Charges may also be subject to disclosed or undisclosed caps during a specified period. They may also be subject to disclosed or undisclosed buffers.

- 25 Not all of the banks' current terms and conditions distinguish between an Unpaid Item Charge and a Paid Item Charge. For example, Abbey National charges what it calls an "Instant Overdraft Request Fee", which is payable whether the temporary loan is granted or not. However, the OFT in this reply treats such a fee as an Unpaid Item Charge where the customer's instruction for payment or withdrawal is not honoured, and a Paid Item Charge where it is honoured.
- 26 Annex C hereto sets out the Paid Item Charges payable under each bank's current terms and conditions for its main current account(s).

Overdraft Excess Charge

27 This is a charge that is levied if, during a specified period (typically a day or a month):

27.1 an account is and/or goes overdrawn (and there is no overdraft facility), or

27.2 the debit balance is and/or goes above the limit on an existing overdraft facility

and in both cases, irrespective of the reason why the excess has occurred.

28 Where the specified period is daily, the Overdraft Excess Charge may be subject to a cap on the number of charges per month.

29 Disclosed or undisclosed buffers may apply to these charges.

30 In the case of banks that levy both Paid Item Charges and Overdraft Excess Charges, one instruction for payment or withdrawal may result in both charges being levied.

- 31 Annex D hereto sets out the Overdraft Excess Charges payable under each bank's current terms and conditions for its main current account(s).

Guaranteed Paid Item Charge

- 32 Where a bank honours, in accordance with the guarantee, a cheque issued in conjunction with a cheque guarantee card (or, in the case of some banks, a debit card payment made under a guaranteed debit payment system) for which the customer does not have sufficient funds:

32.1 some banks under their current terms and conditions levy a Paid Item Charge (and do not distinguish between guaranteed payments and other methods of payment); and

32.2 some banks under their current terms and conditions levy a distinct charge, which the OFT will here call a "Guaranteed Paid Item Charge". These charges may also be subject to disclosed or undisclosed buffers.

- 33 Annex E hereto sets out the Guaranteed Paid Item Charges payable under each bank's current terms and conditions for its main current account(s).

II. THE APPLICATION OF THE REGULATIONS TO THE RELEVANT TERMS

- 34 For the reasons particularised in paragraphs 35 to 75 below, the terms ("the Relevant Terms") that impose the Relevant Charges (which are referred to in the agreed Annexes to the amended particulars of claim):

34.1 are not in plain intelligible language; and/or

34.2 do not relate to the definition of, and/or are not, the main subject matter of the contract for the purposes of Regulation 6(2)(a); and

34.3 do not relate to the adequacy of the price or remuneration of any goods or services supplied in exchange, for the purposes of Regulation 6(2)(b).

Unpaid Item Charges and the Relevant Terms that provide for them

Regulation 6(2)(a)

35 The rights under and/or features of the Current Account Contract set out in paragraph 5 above are fundamental to any Current Account Contract.

36 Consumers and the banks would consider each of those rights and/or features to be necessary aspects of a Current Account Contract.

37 By contrast:

37.1 The Unpaid Item Charge is levied only in certain specific and contingent circumstances that may never arise in a particular Current Account Contract.

37.2 The circumstances that trigger an Unpaid Item Charge arise outside the ordinary course of the operation of the current account and/or are aberrant.

37.3 On the proper construction of Regulation 6(2)(a), the main subject matter of a contract is goods and/or services and not the price or remuneration for such goods and/or services: the Unpaid Item Charge is neither goods nor a service (still less the main goods or service).

37.4 A Current Account Contract can work without an Unpaid Item Charge.

38 In the premises:

- 38.1 the main subject matter of the Current Account Contract is as set out in paragraph 5 above;
- 38.2 the Unpaid Item Charges and the Relevant Terms that provide for them do not relate to the definition of, and are not, the main subject matter of the Current Account Contracts but rather are incidental and/or subsidiary terms; and
- 38.3 it is denied that Regulation 6(2)(a) excludes the Unpaid Item Charges and the Relevant Terms that provide for them from an assessment of fairness.

Regulation 6(2)(b)

- 39 On the proper construction of Regulation 6(2)(b), “services” are services that are, or form part of, the main subject matter of the contract.
- 40 All instructions, whether or not they are covered by sufficient funds in the customer’s account, are processed by the banks’ Payment Systems and Processes. Such acts as the banks perform prior to a refusal to carry out an instruction for payment or withdrawal are acts required to be done in preparation for honouring or, if there are insufficient funds, refusing the customer’s instruction, and are not in themselves services that the bank supplies to the customer.
- 41 Further or alternatively, such acts as the banks perform prior to a refusal to carry out an instruction for payment or withdrawal and/or the refusal itself and/or any related action that the bank may take following such refusal:
- 41.1 are not a benefit that the customer receives or enjoys; and/or
- 41.2 are of no appreciable value to the customer; and/or

41.3 are performed for the benefit of the bank not the customer; and/or

41.4 are not the main subject matter of the contract.

42 In the premises:

42.1 the banks do not provide any service, within the meaning of Regulation 6(2)(b), in exchange for the Unpaid Item Charges;

42.2 it is denied that the Relevant Terms that provide for the Unpaid Item Charges relate to the adequacy of the price or remuneration, as against goods or services supplied in exchange; and

42.3 it is denied that Regulation 6(2)(b) excludes the Unpaid Items Charges and the Relevant Terms that provide for them from an assessment of fairness.

Paid Item Charges and the Relevant Terms that provide for them

Regulation 6(2)(a)

43 The OFT repeats paragraphs 35 and 36 above.

44 By contrast:

44.1 The Paid Item Charge is levied only in certain specific and contingent circumstances that may never arise in a particular Current Account Contract.

44.2 The circumstances that trigger a Paid Item Charge arise outside the ordinary course of the operation of the current account and/or are exceptional and/or aberrant. Further, the banks that levy this charge consider, or ought to consider, this to be the case.

- (a) In some cases this is expressly stated or reflected in the banks' respective current terms and conditions. For example, Nationwide Building Society provides that membership will be withdrawn if the customer goes overdrawn without agreement or exceeds an agreed overdraft limit (clause 1). In the past, the exceptional nature of the circumstances giving rise to the Paid Item Charges has been expressly stated and/or reflected in all of the banks' terms and conditions.
- (b) The payee (referred to in this paragraph as "the creditor") in most payment instructions is a creditor of the customer, or someone from whom the customer obtains goods and/or services and/or a pecuniary advantage in exchange for the payment. In the case of such payees, no payment instruction giving rise to a Relevant Charge and/or a temporary loan could lawfully arise except in cases where the customer has made an error, which may be for the reasons pleaded in paragraph 72 below, as to his available funds:
- (i) In the case of cheques and payments by debit card, the tendering of a cheque or debit card for payment constitutes a representation to the creditor that the customer has available funds and/or that the payment will be met. A customer may not lawfully issue a cheque, or present a debit card, to pay a creditor, and/or to obtain goods, services or pecuniary advantage, if he knows that he will have insufficient funds, or doubts that he will have sufficient funds, when the payment is processed in the ordinary course.
- (ii) Payment by standing order, direct debits and any other method of instructing payment are liable to involve representations by the customer to the creditor as to his intention to ensure that the payments are covered by sufficient funds in his account, and the creditor assumes and/or expects and/or requires that to be the case.

- (iii) Further, in many instances the customer undertakes to the creditor that he will be paid pursuant to the contractual method of payment.
- (iv) Cases where there are insufficient funds to meet a payment to a creditor should therefore only arise where there has been an error on the part of the customer.
- (v) Instructions by a customer for withdrawals for which there are insufficient funds likewise may also arise where there has been an error on the part of the customer.

44.3 The Paid Item Charge is neither goods nor a service (still less the main goods or service): paragraph 37.3 above is repeated (the necessary changes having been made).

44.4 A Current Account Contract can work without a Paid Item Charge.

45 Further or alternatively, the Paid Item Charges, both standing alone and when applied in conjunction with other Relevant Charges (and interest), can, and often will, result in the customer obtaining credit on uneconomic terms and/or paying charges that are disproportionate to the amount of credit and/or the period for which it is extended. Terms in a consumer contract that can operate in this way are presumptively not the main subject matter of the contract for the purposes of Regulation 6(2)(a).

46 In the premises:

46.1 the Paid Item Charges and the Relevant Terms that provide for them do not relate to the definition of, and are not, the main subject matter of the Current Account Contracts but rather are incidental and/or subsidiary terms; and

46.2 it is denied that Regulation 6(2)(a) excludes the Paid Item Charges and the Relevant Terms that provide for them from an assessment of fairness.

Regulation 6(2)(b)

47 In so far as the banks contend or specify in their terms and conditions that the Paid Item Charge is the price or remuneration for the alleged service of “considering whether to grant an overdraft”:

47.1 such acts as the banks perform when considering whether to grant an overdraft are acts done in preparation for honouring or refusing the customer’s instruction, and are not in themselves services that the bank supplies to the customer;

47.2 further or alternatively, the alleged service:

- (a) is not a benefit that the customer receives or enjoys; and/or
- (b) is of no appreciable value to the customer; and/or
- (c) is performed for the benefit of the bank not the customer; and/or
- (d) is not main subject matter of the contract; and/or
- (e) should not, for the purposes of the Regulations, be regarded as a service for the reasons set out in paragraph 44.2 above.

47.3 in the premises, the alleged service is not a service within the meaning of Regulation 6(2)(b).

48 In so far as the banks contend or specify in their terms and conditions that the Paid Item Charge is supplied in exchange for providing the temporary loan:

- 48.1 the temporary loan is not the main subject matter of the contract: paragraph 39 above is repeated;
- 48.2 in the premises, the temporary loan is not a “service” within the meaning of Regulation 6(2)(b).
- 49 If, which is denied, the temporary loan and/or considering whether to grant a temporary loan are services within the meaning of Regulation 6(2)(b), the OFT contends as follows.
- 49.1 Each bank charges its customers interest on temporary loans.
- 49.2 The interest payable increases in proportion to the amount of the temporary loan and the length of time for which it is made, whereas the Paid Item Charges are charged at a flat rate irrespective of the amount and, in some cases, the duration, of the temporary loan.
- 49.3 In the premises, the main term as to price or remuneration for a temporary loan is the term that provides for the payment of interest.
- 49.4 The Relevant Terms providing for Paid Item Charges are, at most, incidental and/or subsidiary terms as to price or remuneration and fall outside Regulation 6(2)(b).
- 49.5 In the premises, it is denied that the Paid Item Charges are the price or remuneration, within the meaning of Regulation 6(2)(b), of the service.
- 50 In the premises, it is denied that:
- 50.1 the Relevant Terms that provide for the Paid Item Charges relate to the adequacy of the price or remuneration, as against the goods or services supplied in exchange; and

50.2 Regulation 6(2)(b) excludes the Paid Item Charges and the Relevant Terms that provide for them from an assessment of fairness.

Overdraft Excess Charges and the Relevant Terms that provide for them

Regulation 6(2)(a)

51 The OFT repeats paragraphs 35 and 36 above.

52 By contrast:

52.1 The Overdraft Excess Charge is levied only in certain specific and contingent circumstances that may never arise in a particular Current Account Contract.

52.2 In so far as this charge is triggered by the same circumstances that trigger a Paid Item Charge, it arises outside the ordinary course of the operation of the current account and/or is exceptional and/or aberrant, and the banks that levy this charge consider, or ought to consider, that to be the case, for the reasons pleaded in paragraph 44.2 above.

52.3 The Overdraft Excess Charge is neither goods nor a service (still less the main goods or service): paragraph 37.3 above is repeated (the necessary changes having been made).

52.4 A Current Account Contract can work without an Overdraft Excess Charge.

53 Further or alternatively, the Overdraft Excess Charges, both standing alone and when applied in conjunction with other Relevant Charges (and interest), can, and often will, result in the customer obtaining credit on uneconomic terms and/or paying charges that are disproportionate to the amount of credit obtained and/or the period for which it is obtained. Terms in a consumer

contract that can operate in this way are presumptively not the main subject matter of the contract for the purposes of Regulation 6(2)(a).

54 In the premises:

54.1 the Overdraft Excess Charges and the Relevant Terms that provide for them do not relate to the definition of, and are not, the main subject matter of the Current Account Contracts but rather are incidental and/or subsidiary terms; and

54.2 it is denied that Regulation 6(2)(a) excludes the Overdraft Excess Charges and the Relevant Terms that provide for them from an assessment of fairness.

Regulation 6(2)(b)

55 In so far as the banks contend or specify in their terms and conditions that the Overdraft Excess Charge is supplied in exchange for the alleged service of “considering whether to grant an overdraft”, paragraph 47 above is repeated.

56 In so far as the banks contend or specify in their terms and conditions that the temporary loan is supplied in exchange for the Overdraft Excess Charge, paragraph 48 above is repeated.

57 Further or alternatively, if, which is denied, considering whether to grant an overdraft and/or granting an overdraft are services within the meaning of Regulation 6(2)(b), it is denied that such services are supplied in exchange for the Overdraft Excess Charge. The Overdraft Excess Charges are levied periodically because a certain state of affairs exists during the relevant period, namely that the customer’s account is and/or goes overdrawn (and there is no overdraft facility), or the debit balance is and/or goes above the limit on an existing overdraft facility. They are not in exchange for any service.

- 58 If, which is denied, considering whether to grant a temporary loan and/or the temporary loan are services, and if, which is denied, the temporary loan is supplied in exchange for the Overdraft Excess Charge.
- 58.1 Such charges are not the “price” or “remuneration”, within the meaning of Regulation 6(2)(b) of the 1999 Regulations, of the services represented by the act of considering whether to grant an overdraft and/or the overdraft itself.
- 58.2 Paragraphs 49.1 and 49.2 above are repeated.
- 58.3 Most of the banks generally also charge one or more other Relevant Charges in the respect of the event that triggers the Overdraft Excess Charge.
- 58.4 In the premises, the main term as to price or remuneration for a temporary loan is the term that provides for the payment of interest.
- 58.5 The terms that provide for the Overdraft Excess Charges are, at most, incidental and/or subsidiary terms as to price or remuneration and fall outside Regulation 6(2)(b).
- 59 In the premises, it is denied that:
- 59.1 the Relevant Terms that provide for the Overdraft Excess Charges relate to the adequacy of the price or remuneration, as against the goods or services supplied in exchange; and
- 59.2 Regulation 6(2)(b) excludes the Overdraft Excess Charges and the Relevant Terms that provide for them from an assessment of fairness.

Guaranteed Paid Item Charges and the Relevant Terms that provide for them

Regulation 6(2)(a)

- 60 The OFT repeats paragraphs 35 and 36 above.
- 61 By contrast:
- 61.1 The Guaranteed Paid Item Charge is levied only in certain specific and contingent circumstances that may never arise in a particular Current Account Contract.
- 61.2 The circumstances that trigger a Guaranteed Paid Item Charge arise outside the ordinary course of the operation of the current account and/or are exceptional and/or aberrant (and/or under most current and historical terms and conditions that levy such charges give rise to a breach of contract, as further pleaded in paragraph 87 below). Further, the banks that levy this charge consider, or ought to consider, this to be the case. Paragraph 44.2 above is repeated.
- 61.3 The Guaranteed Paid Item Charge is neither goods nor a service (still less the main goods or service): paragraph 37.3 above is repeated (the necessary changes having been made).
- 61.4 A Current Account Contract can work without a Guaranteed Paid Item Charge.
- 62 Further or alternatively, the Guaranteed Paid Item Charges, both standing alone and when applied in conjunction with other Relevant Charges (and interest), can, and often will, result in the customer obtaining credit on uneconomic terms and/or paying charges that are disproportionate to the amount of credit obtained and/or the period for which it is obtained. Terms in

a consumer contract that can operate in this way are presumptively not the main subject matter of the contract for the purposes of Regulation 6(2)(a).

63 In the premises:

63.1 the Guaranteed Paid Item Charges and the Relevant Terms that provide for them do not relate to the definition of, and are not, the main subject matter of the contract but rather are incidental and/or subsidiary terms; and

63.2 it is denied that Regulation 6(2)(a) excludes the Guaranteed Paid Item Charges and the Relevant Terms that provide for them from an assessment of fairness.

Regulation 6(2)(b)

64 In so far as the banks contend or specify in their terms and conditions that the alleged service of “considering whether to grant an overdraft” is supplied in exchange for the Guaranteed Paid Item Charge, paragraph 47 above is repeated.

65 In so far as the banks contend or specify in their terms and conditions that the temporary loan is supplied in exchange for the Guaranteed Paid Item Charge, paragraph 48 above is repeated.

66 If, which is denied, the granting of a temporary loan is a service within the meaning of Regulation 6(2)(b), the Guaranteed Paid Item Charges are not the price or remuneration, within the meaning of Regulation 6(2)(b), for which such service is supplied in exchange. Paragraph 49 above is repeated.

67 In the premises, it is denied that:

67.1 the Relevant Terms that provide for the Guaranteed Paid Item Charges relate to the adequacy of the price or remuneration, as against the goods or services supplied in exchange; and

67.2 Regulation 6(2)(b) excludes the Guaranteed Paid Item Charges and the Relevant Terms that provide for them from an assessment of fairness.

The banks' allegations that the Relevant Charges are the price or remuneration, or an "integral part of the price", or part of an "integrated pricing structure", for a "package of services"/ "integrated bundle of services"

68 As to the allegations made by the banks that the Relevant Charges are the price or remuneration, or an "integral part of the price", or part of an "integrated pricing structure", for a "package of services" (also described by The Royal Bank of Scotland Group plc as an "integrated bundle of banking services" and by Lloyds TSB bank plc as "the range of banking services"):

68.1 The Relevant Charges are levied specifically for the events and circumstances that give rise to them.

68.2 The banks' respective terms and conditions and explanatory documents specifically relate to the Relevant Charges to these events and circumstances.

68.3 Further, a customer who does not incur any Relevant Charges is nonetheless entitled to use, alternatively the banks make available to him, the "package of services"/"integrated bundle of banking services" available under the Current Account Contract.

68.4 The price of the various services provided under a Current Account Contract are not "integrated" in any sense relevant to the Regulations.

68.5 The services provided under a Current Account Contract are not “packaged”, “integrated” or “bundled” in any sense relevant to the Regulations.

68.6 If, which is denied, services provided under the Current Account Contracts and/or the price of or the remuneration for such services are “packaged”, “integrated”, or “bundled”, this does not affect the analysis of the question whether the Relevant Terms are excluded from an assessment of fairness by reason of Regulation 6(2)(a) and/or (b).

68.7 In the premises, these allegations, and their relevance, are denied.

The OFT’s response to the argument advanced by certain banks based on an alleged discrete contract

69 As to the allegations made by some of the banks to the effect that (1) a new and specific contract (“the Discrete Contract”) comes into being between a customer and a bank each time that a customer gives a payment or withdrawal instruction for which there are insufficient funds; (2) that under the Discrete Contract, in return for the bank considering the customer’s instruction and/or (as the case may be) granting or declining the customer the temporary loan, the customer agrees to pay the bank’s charges for these services; and (3) that the various charges are the main subject matter of the Discrete Contract, and/or relate to the adequacy of the price or remuneration for a service supplied in exchange under such contract:

69.1 The banks and their respective customers agree in the Current Account Contracts their respective rights and obligations in the event that the customer instructs a payment or requests a withdrawal for which the customer does not have sufficient funds in his account. The alleged Discrete Contract is unnecessary, is not intended by the parties (on an objective assessment of their intentions, including having regard to the

facts and circumstances pleaded in paragraph 44.2 above) and is not to be implied.

69.2 Further or alternatively, save in the cases where the customer issues a cheque guaranteed by a cheque guarantee card or uses a debit card in circumstances where the bank is contractually bound to accede to the payment request, the alleged Discrete Contract is not supported by consideration from the banks as they retain a complete discretion whether to consider the customer's request or not, and whether to accede to the request or not.

69.3 In the premises, it is denied that the Discrete Contract comes into being each time that a customer gives a payment or withdrawal instruction for which there are insufficient funds in his account.

69.4 If, which is denied, each such instruction does give rise to and/or is the subject of a discrete contract, nonetheless the relevant contract, for the purposes of Regulation 6(2)(a), is the Current Account Contract, to which any Discrete Contract is merely ancillary.

69.5 If, which is denied, each such instruction does give rise to and/or is the subject of the Discrete Contract, and if, which is denied, such contract is the relevant contract for the purposes of Regulation 6(2)(a), then the OFT contends as follows.

Regulation 6(2)(a)

- (a) The main subject matter of the Discrete Contract is:
 - (i) the customer's request for a temporary loan, or
 - (ii) the bank's consideration of the customer's request; or

- (iii) where a temporary loan is not granted, the refusal of the temporary loan; or
 - (iv) where a temporary loan is granted, the temporary loan.
- (b) The Relevant Charges:
 - (i) are not goods or services: paragraph 37.3 above is repeated; and/or
 - (ii) are incidental and/or subsidiary terms of the Discrete Contract.
- (c) In the premises, it denied that:
 - (i) the Relevant Terms and the Relevant Charges relate to the definition, or are, the main subject matter of the alleged Discrete Contract; and
 - (ii) on the premise that the question is to be considered in relation to the Discrete Contract, that Regulation 6(2)(a) excludes the Relevant Terms and the Relevant Charges from an assessment of fairness.

Regulation 6(2)(b)

- (d) On the premise that the question is to be considered in relation to the alleged Discrete Contract, it is denied that Regulation 6(2)(b) excludes the Relevant Terms and the Relevant Charges from an assessment of fairness. The OFT relies on the same facts and matters that are pleaded in paragraphs 39 to 42, 47 to 50, 55 to 59 and 64 to 67 above in relation to each of the Relevant Charges.

- (e) Further or alternatively, Regulation 6(2)(b) is concerned with assessments, alternatively terms, that relate to the adequacy of the price or remuneration, as against the goods or services supplied in exchange under a single contract. In the premises, if the customers are charged pursuant to a Discrete Contract, it is denied that the charges can be characterised for the purposes of Regulation 6(2)(b) as the price or remuneration for a wider “integrated” “package of services” supplied under another contract.

Plain intelligible language

70 Some of the Relevant Terms:

70.1 are not clear and/or transparent; and/or

70.2 do not provide the consumer with a fair opportunity to understand how they will apply; and/or

70.3 are liable to mislead the consumer; and

70.4 in the premises, are not in plain intelligible language.

71 Full particulars of these allegations are contained in Annex F hereto. However, there are three common objections to the ways in which certain of the Relevant Terms in the banks’ current terms and conditions are expressed and explained. The second and third objections do not apply to Nationwide’s Relevant Terms.

First Objection

72 The ways in which the Relevant Terms apply is not made sufficiently clear to consumers:

- 72.1 Some of the terms and conditions do not make clear precisely what type of payment or withdrawal instruction by the customer or other event (such as previously imposed Relevant Charges, other bank charges, and interest) will trigger a Relevant Charge.
- 72.2 Neither the terms and conditions nor any of the explanatory documents give any or sufficient information concerning the criteria by which the banks decide whether or not to honour an instruction for which the customer has insufficient funds.
- 72.3 Neither the terms and conditions nor any explanatory documents explain the order in which the banks process transactions where several payments instructions are pending for consideration. In particular, as standing orders, direct debits, cheques and certain other types of payment are typically processed in batches overnight, the order in which instructions are processed may affect which, if any, of them are honoured and/or the type and number of the Relevant Charges that are levied.
- 72.4 In all the circumstances, the Relevant Terms (standing alone and/or read in the context of the other terms and conditions and/or in the context of other explanatory documents) do not enable the customer to know with reasonable confidence, in common situations where he makes or contemplates making a payment or withdrawal:
- (a) whether such an instruction would be met, or would probably be met;
 - (b) when the available funds for meeting a payment or withdrawal are reckoned;
 - (c) whether such an instruction would attract, or would probably attract, a Relevant Charge or Charges and, if so:

- (i) the type of Relevant Charge or Charges;
 - (ii) the number of such charges; and
- (d) when the Relevant Charges will be, or probably will be, levied.

Second Objection

73 The Relevant Terms of some of the banks are liable to give the customer the impression that there is nothing wrong with paying for goods and services, or with obtaining property, services or pecuniary advantages, by making payments for which he has insufficient funds in his account, whereas in fact:

- (a) a customer who, knowing or suspecting that he will not have sufficient funds in his account when the payment is processed in the ordinary course, pays for, or seeks to pay for, goods or services, and/or obtains property, services or pecuniary advantages, using a cheque or other method of payment, risks committing a criminal offence; and
- (b) a customer who uses a method of payment stipulated by a contract between him and the payee without having sufficient funds in his account when the payment is processed to cover the payment risks incurring civil liability to the payee if the bank does not honour the payment instruction.

74 In support of the allegation made in the last preceding paragraph, the OFT contends that the Relevant Terms in the current terms and conditions of certain banks, in so far as they purport to levy charges for “requests” and “services”, use language that appears to treat such conduct as acceptable or proper:

74.1 The characterisation of all payment instructions for which there are insufficient funds as mere “requests” for overdrafts is liable to convey to consumers the false impression that:

- (a) that such requests are similar to requests for an overdraft facility, save only that they are “informal”, and
- (b) that making such requests is a perfectly permissible conduct, even if it involves, for example, issuing cheques for which the customer knows or suspects he has insufficient funds, and thereby obtaining and/or paying for, or purporting to pay for, property, services or pecuniary advantages;

74.2 The characterisation of the bank’s response to such “requests” as a “service” of “considering whether to meet such request” and/or of refusing or granting the loan (as the case may be), and any similar characterisation:

- (a) is liable to reinforce the false impression referred to in paragraph 74.1 above;
- (b) further or alternatively, is in itself misleading because:
 - (i) “considering whether to meet the request” is not a service, and it is inappropriate to so describe it;
 - (ii) there is no or very little consideration of the payment or withdrawal instruction where it falls outside of the authorisation limit; and
 - (iii) where the payment or withdrawal instruction is within the authorisation limit, in most cases it is automatically met.

Third Objection

75 Many of the banks use the same terms (for example, “overdraft”, “overdraft facility”, “overdraft service”, etc) to describe both overdraft facilities and temporary loans. This is liable to mislead consumers because it implicitly equates two very different things:

75.1 an agreed credit facility that allows the customer to borrow up to a specified limit for a period of time; and

75.2 a temporary loan that the banks expect to be repaid straightaway.

The assessment of fairness

76 If, which is denied, the Relevant Terms are in plain intelligible language and relate to the definition of, or are, the main subject matter of the contract, and/or relate to the adequacy of the price or remuneration for the service supplied in exchange, each of the Relevant Terms is nonetheless subject to an assessment of fairness, subject to the limits of Regulation 6(2). The banks’ allegations to the contrary are denied.

77 Contrary to what the banks contend, Regulation 6(2) does not put a particular class of terms beyond the reach of the 1999 Regulations, but rather circumscribes the grounds on which a court may conclude that a particular term is unfair. A conclusion that a term is unfair must not relate to – in effect, have as its supporting reasons an assessment concerning the fairness of – two matters:

77.1 the definition of the main subject matter of the contract; or

77.2 the adequacy of the price or remuneration, as against the goods or services supplied in exchange.

78 Therefore, subject to the limits imposed on the assessment by Regulation 6(2), the Relevant Charges may be assessed for fairness.

79 The OFT has not concluded its investigation into, and any assessment of, the fairness of the Relevant Charges. There is not therefore presently any dispute between the OFT and any of the banks concerning an actual assessment of the fairness of any of the Relevant Charges.

Historical Terms

80 With regard to the historical Relevant Terms:

80.1 the OFT denies that they are in plain intelligible language, for reasons that are substantially the same as those pleaded in paragraph 70 to 75 above and Annex F in respect of the current terms and conditions;

80.2 if, which is denied, they are in plain intelligible language, they are not excluded from an assessment of fairness by reason of Regulation 6(2) (for the reasons that are pleaded in paragraphs 34 to 79 of this reply).

81 However, as appears from the prayer in the OFT's amended particulars of claim, the OFT does not presently seek any declaratory relief in respect of the historical Relevant Terms, save in so far as the banks rely on them in these proceedings. None of the banks have pleaded any significant differences between the current and historical Relevant Terms. Whatever the outcome of the OFT's investigation into the fairness of the Relevant Charges may be, the OFT would not in these proceedings seek an enforcement order concerning historical Relevant Terms. At the trial of the preliminary issues, the OFT will be inviting the court:

81.1 so far as concerns the claim by the OFT, to consider the historical Relevant Terms only as part of the evidence in the case, and in particular for the purpose of demonstrating that certain of the banks have from time to time

amended their terms and conditions in order to recharacterise the Relevant Charges, but that the substance of the Relevant Charges and the Relevant Terms has not materially changed; and

81.2 so far as concerns the claims by the banks, and in particular in relation to their claim for a declaration relating to penalties, to deal with any particular terms relied on by the banks: see further section IV below of this reply and defence to counterclaims.

82 The OFT recognises that a number of cases before the county courts will depend on an assessment of historical Relevant Terms and that a declaration by the court concerning such terms, so far as they are materially different from the current Relevant Terms, may be considered to be in the public interest.

DEFENCE TO COUNTERCLAIMS

III. THE OFT'S RESPONSE TO THE BANKS' COUNTERCLAIMS IN RELATION TO GOOD FAITH

83 Each of the banks seeks declarations that:

83.1 it is a necessary but not a sufficient precondition to the Relevant Terms being shown to be unfair within the meaning of Regulation 5(1) that they be shown to be contrary to the requirement of good faith; and

83.2 that good faith for the purposes of Regulation 5(1) means dealing openly and fairly with the customer: most of the banks say that the relevant time is when the contract is made.

84 As to this counterclaim:

- 84.1 The OFT accepts that it is a necessary but not a sufficient precondition to the Relevant Terms being shown to be unfair within the meaning of Regulation 5(1) that they be shown to be contrary to the requirement of good faith, but has not contended or suggested otherwise.
- 84.2 The banks do not allege that there exists a dispute between the parties in relation to this point, and none exists.
- 84.3 As regards the meaning of “good faith”, the banks invite the court to state in different words what Regulation 5(1) states concerning the requirement of good faith. The banks invite the court in effect to rewrite Regulation 5(1) by replacing one open-textured concept (good faith) with another (fair and opening dealing). Such a declaration would not settle the rights and obligations of litigants, and would not be an appropriate use of the court’s declaratory jurisdiction.
- 85 The OFT will contend, so far as necessary, in relation to the words “contrary to the requirement of good faith” in Regulation 5(1) as follows:
- 85.1 they qualify the words “causes a significant imbalance”;
- 85.2 the significant imbalance caused by the contractual term must be “contrary to good faith” if the term is to be regarded as unfair;
- 85.3 the phrase has both substantive and procedural content and must be interpreted autonomously; and
- 85.4 it is denied that, without reference to any actual facts, it can be stated, or that it is appropriate for the court to declare, that in all cases the requirement of good faith would be satisfied if the banks had dealt with the customers fairly and openly when the contract was made.

86 In the premises:

86.1 the banks' counterclaims for this declaration do not disclose a cause of action; and

86.2 it is denied that the banks are entitled to, or that the court should exercise its discretion to grant, the declaration.

IV. THE OFT'S RESPONSE TO THE BANKS' COUNTERCLAIMS THAT THE RELEVANT TERMS ARE NOT CAPABLE OF AMOUNTING TO PENALTIES AT COMMON LAW

87 Each bank counterclaims for a declaration that its Relevant Terms are not capable of amounting to penalties at common law. As to these counterclaims:

87.1 Where a bank's current or historical terms and conditions on their proper construction provide that the customer shall be in breach of contract if he seeks to initiate a withdrawal or payment for which there are insufficient funds, terms that impose a charge in these circumstances are capable of being penalties at common law if they are not a genuine pre-estimate of the losses occasioned by the breach. The OFT has identified in the following annexes the terms that are capable of being penalties:

- (a) Annex G1 hereto shows those current terms and conditions that impose an obligation not to attempt to go overdrawn; and
- (b) Annex G2 hereto shows those historical terms and conditions that impose an obligation not to attempt to go overdrawn.

87.2 It is therefore denied that the terms referred to above are incapable of being penalties at common law. The claim for a declaration as regards those terms is denied.

- 87.3 It is admitted that Relevant Charges payable where the customer seeks to initiate withdrawal or a payment for which there are insufficient funds in circumstances where the customer's conduct does not amount to a breach of contract, are not capable of amounting to penalties at common law. However, the OFT has not contended or suggested to the contrary.
- 88 Some of the banks allege that, in so far as the customer commits a breach of contract when he instructs a payment or withdrawal for which he does not have sufficient available funds, the breach is waived. As to this:
- 88.1 The banks that make this allegation have not particularised how the waiver arises, but it is in any event denied.
- 88.2 If, which is denied, there is a waiver, it is denied that it is relevant to, alternatively determinative of, the question whether the charges are penalties or not.

BRIAN DOCTOR QC
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RICHARD COLEMAN
SARAH LOVE

I, Winnie Ching for the General Counsel, believe that the facts stated in this Joint Reply and Defence to Counterclaim are true.

 9/11/07

Claim No. 2007 Folio 1186

IN THE HIGH COURT OF JUSTICE

QUEENS BENCH DIVISION
COMMERCIAL COURT

BETWEEN:

THE OFFICE OF FAIR TRADING
Claimant

-and-

- (1) ABBEY NATIONAL PLC**
- (2) BARCLAYS BANK PLC**
- (3) CLYDESDALE BANK PLC**
- (4) HBOS PLC**
- (5) HSBC BANK PLC**
- (6) LLOYDS TSB BANK PLC**
- (7) NATIONWIDE BUILDING SOCIETY**
- (8) THE ROYAL BANK OF SCOTLAND GROUP
PLC**

Defendants

**THE OFFICE OF FAIR TRADING'S
JOINT REPLY AND DEFENCE TO
COUNTERCLAIMS**

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