

## FIDUCIARY DUTIES AND SECRET COMMISSIONS

### CIVIL WATCH – PRACTICE NOTE

***As part of Goldsmith Chambers' Civil Watch series, Dilan Deeljur, the Deputy Head of the Civil Team, provides a useful insight into fiduciary duties and secret commissions by studying the case of Wood v Commercial First Business Limited and Business Mortgage Finance 4 Plc v Pengelly [2021] EWCA Civ 471.***



### INTRODUCTION

1. Do you need to establish a fiduciary duty between a broker and borrower where the broker has taken a fully secret commission? This was the question posed to the Court of Appeal in *Wood v Commercial First Business Limited and Business Mortgage Finance 4 Plc v Pengelly* [2021] EWCA Civ 471. The answer is no!
2. “Where an “agent” providing advice, information or recommendations has received or been offered, a bribe or secret commission, the question that the court should ask and focus on is: did the “agent” owe a duty to be impartial and to give disinterested advice, information or recommendations?”

David Richards LJ in *Wood v CFBL* [2021] EWCA Civ 471 at para 102.

### THE BACKGROUND

3. Liability for the return of secret commissions paid by lenders to credit brokers has been the subject of a recent, comprehensive judgment of the Court of Appeal in *Wood*.
4. Both *Wood* and *Pengelly* were based on the similar set of facts and a similar relationship. Both involved a borrower, using a broker to obtain a secured loan from a commercial lender. And importantly, in both cases, the broker received a percentage commission payment from the lender which was not clearly disclosed to the borrower. (Note below the difference between fully secret and half secret commissions). In November 2018 the lender entered liquidation and was dissolved in December 2019 with the loans being securitised and assigned to third-parties.
5. The borrowers (*Wood* and *Pengelly*) defaulted on repayments and claimed for rescission of the loan agreements and the accompanying mortgages on the basis of the broker’s fully secret commission. In *Wood*, Mrs Wood issued proceedings to set aside the loan agreement after enforcement proceedings had been taken against her and possession orders made. Mr James Pickering (sitting as a Deputy

Judge of the High Court) found at first instance in her favour and rescinded the mortgage. The assignees appealed.

6. In *Pengelly*, at first instance HHJ Carr dismissed Mr Pengelly's defence and counterclaim and gave the assignee mortgagee liberty to enforce its possession order. Mr Justice Marcus Smith allowed Mr Pengelly's appeal on the point of rescission. Again, the assignee appealed this decision.
7. The two High Court judges differed significantly on the question as to whether a fiduciary relationship was a pre-requisite to the principles concerning secret commissions or bribes being engaged as against the lender. Mr Pickering found that no such duty was necessary. Marcus Smith J held that such a duty was needed

#### THE COURT OF APPEAL DECISION – FIDUCIARY RELATIONSHIP

8. If a "fiduciary relationship" is needed as a pre-requisite for remedies in respect of bribes or secret commissions the inherent risk is either that civil remedies which should be available will be denied because there is not a fiduciary relationship, or that the term "fiduciary relationship" will be applied so widely as virtually to deprive it of content (see paragraph 46 of the Judgment).
9. That means that questioning whether there is a fiduciary relationship as a precondition for civil liability in respect of bribes or secret commissions cases is an unnecessarily elaborate, and perhaps inaccurate, question (see para 48).
10. It is the content of the duty, not the label attached to it, that matters, which is in accordance with the authorities as well as with principle (para 50). The Court acknowledged that in a significant number of authorities, particularly recently, the liability of the payer and recipient of the bribe or secret commission was in terms of a "fiduciary duty" and an accessory liability for the payer. However, such references were only in a "wide" and "very loose sense" (paras 73, 79 and 83).
11. In a case of a 'half-secret commission' (for example where the existence of a commission is disclosed but not the amount thereof) the Court of Appeal in *Hurstanger Ltd v Wilson and Anthr* [2007] 1 WLR 2351 made clear that it is necessary to establish a fiduciary relationship (see para 128 of that judgement).

#### THE TEST

12. If there is no need for the payee to be in a 'fiduciary relationship' with the borrower the question becomes less complex. The payee will be "*someone with a role in the decision-making process in relation to the transaction in question e.g. as agent, or otherwise someone who is in a position to influence or affect the decision taken by the principal*" (see para 51 of Wood).
13. As stated above the question then becomes: *did the "agent" owe a duty to be impartial and to give disinterested advice, information or recommendations?*" (para

102) or should the agent have been honest and impartial. That question is to be framed by reference to the terms of engagement (para 47). But that does not necessarily need the court to conduct a complex analysis on a 'fiduciary duty of loyalty', which previous authorities espoused. The Court of Appeal explicitly cautioned against over complication.

#### WHAT HAPPENED IN WOOD THEN?

14. It followed in Wood that the broker, on the basis of their terms and conditions, did owe the requisite duties on the facts to engage the law applicable to secret commissions. The broker was under a duty to make a disinterested selection of mortgage product to put to its client in each case. To the extent that it was necessary, the Judges below were also correct to hold that the broker owed a fiduciary duty of loyalty to Mrs Wood and Mr Pengelly (para 110).
15. In a situation where the broker only put forward a single product for the client's consideration (the so called "information-only sale"), it was the broker and not the client, who had access to a panel of lenders and the broker undertook to work from that panel to provide the "appropriate" product to meet the client's individual circumstances and needs. This necessarily involved judgment and choice on the part of the broker. Moreover, under the terms and conditions the Broker had express authority to negotiate with lenders and could thereby seek to improve the terms available to the client (para 113).
16. Wood reverses the High Court authority of HHJ Raynor in *Commercial First Business Ltd v Pickup and Vernon* [2017] CTL 1 (here the Court had dismissed the 'half secret' commission claim on the basis that no fiduciary duty was owed as there could be no expectation of "undivided loyalty" and the broker was a mere introducer) was wrongly decided (para 126).

#### WAS IT HALF SECRET OR FULLY SECRET?

17. Half secret is where the existence of commission is disclosed but not the amount of commission, fully secret is where the borrower is not told about the existence of commission at all. The broker's terms and conditions were identical for Mrs Wood and Mr Pengelly. They stated that the broker "may" receive fees from creditors with whom it placed mortgages. The terms went on to say:

*"Before you take out a mortgage, we will tell you the amount of the fee in writing. If the fee is less than £250, we will confirm that we will receive up to this amount. If the fee is £250 or more, we will tell you the exact amount."*

18. The Court found that the broker's failure to make any disclosure in accordance with the terms and conditions (both stating that they did not receive any such notifications) in these cases meant that Mrs Wood and Mr Pengelly were entitled to proceed on the basis that no commission was being paid (para 119). Therefore on both cases this was a case of "fully secret" commission.

## REMEDY

19. As this was a full secret commission, the principal was entitled to have the relevant contract rescinded as of right at his or her election (para 61). Therefore rescission of a transaction with the third party was available as of right in cases of bribes or secret commissions, subject to making counter-restitution (para 101).

## COMMENT

20. In theory this decision means it is very difficult for a broker to prove he or she did not owe their customer a duty to provide information and advice impartially, which will in turn expose both the broker and the lender to the applicable civil remedies. But close attention will need to be paid to the terms and conditions between a borrower and broker in order to establish whether a full secret or half secret commission, and on the duty owed. Although the Court of Appeal at no point qualifies the test by suggesting that it only applied to ‘fully secret cases’, Wood and Pengelly were both fully secret commissions. That may or may not mean *Hurstanger* remains the authority on half-secret cases.

21. While the test for the requisite duty owed by a broker has been simplified, the remedy of rescission it should be noted for practical purposes is subject to counter-restitution. Borrowers should seek to establish in evidence a differential in what the broker did offer (as a result of his secret commission or bribe) and what he did actually offer. The test clearly encompasses information-only sales and so it is wide.

**DILAN DEELJUR**  
**GOLDSMITH CHAMBERS**  
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