



Neutral Citation Number: [2008] EWHC 2325 (Comm)

Case No: 2007-1186

**IN THE HIGH COURT OF JUSTICE**  
**QUEEN'S BENCH DIVISION**  
**COMMERCIAL COURT**

Royal Courts of Justice  
Strand, London, WC2A 2LL

Date: 08/10/2008

**Before:**

**MR JUSTICE ANDREW SMITH**

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**Between :**

**The Office of Fair Trading**  
**- and -**  
**Abbey National PLC and others**

**Claimant**

**Defendants**

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**Jonathan Crow QC, Jemima Stratford, Richard Coleman and Sarah Love**  
(instructed by the Office of Fair Trading) for the Office of Fair Trading

**Ali Malek QC and Richard Brent**  
(instructed by Ashurst LLP) for Abbey National plc.

**Iain Milligan QC and Simon Atrill**  
(instructed by Simmons and Simmons) for Barclays Bank plc.

**Richard Salter QC and Adam Kramer**  
(instructed by Addleshaw Goddard LLP) for Clydesdale Bank plc.

**Robin Dicker QC and James McClelland**  
(instructed by Allen & Overy LLP) for HBOS plc.

**Richard Snowden QC, Daniel Toledano and Patrick Goodall**  
(instructed by Freshfields Bruckhaus Deringer LLP) for HSBC Bank plc.

**Bankim Thanki QC, Richard Handyside and James Duffy**  
(instructed by Lovells LLP) for Lloyds TSB Bank plc.

**Sonia Tolaney**  
(instructed by Slaughter and May) for Nationwide Building Society

**Laurence Rabinowitz QC and David Blayney**

(instructed by Linklaters LLP) for The Royal Bank of Scotland Group plc.

Hearing dates: 7, 8 and 9 July 2008

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**Approved Judgment**

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

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MR. JUSTICE ANDREW SMITH

**Mr. Justice Andrew Smith :**

1. In my judgment in this action dated 24 April 2008, [2008] EWHC 875 (Comm) (my “April judgment”), in particular at paras 295 to 331, I considered the common law relating to penalties, and I made a declaration in an order dated 12 June 2008 that certain Relevant Terms giving rise to Relevant Charges are not penalty clauses at common law. (In this judgment, I use the same abbreviated terms as before.) For reasons that I explained in paras 36 to 38, the April judgment and the order were concerned only with some of the terms currently used by the Banks. However, as had been anticipated, my reasoning applied to other current and to historical terms, and in light of my judgment the OFT has accepted that many other Relevant Terms are not capable of being penal, leaving in dispute a relatively small number of terms used by seven of the Banks (those other than Nationwide).
2. The Banks seek declarations that Relevant Terms and Relevant Charges are “not capable of amounting to” penalties at common law. The questions before me about the controversial terms are those that I identified at paragraph 298 of my April judgment, namely (i) whether the term is truly of contractual effect (and not, for example, merely exhortatory or advisory); (ii) if it is of contractual effect, whether it imposes an obligation or prohibition on the customer (rather than, for example, stipulating a condition precedent to an obligation on the bank); and (iii) if it does impose a contractual obligation or prohibition upon the customer, whether a Relevant Charge is payable upon breach of it. There is no dispute between the OFT and the Banks that otherwise a term is not capable of being penal. The Banks submitted that the terms in issue did not meet one or more of these requirements, and that I should accordingly declare that they are not capable of being penal. They do not invite me to consider whether, if these conditions are met, the amounts levied were extravagant or unconscionable and more than a genuine pre-estimate of loss; and that was left for consideration, if necessary, on another occasion.
3. The OFT has not sought permission to appeal against my April judgment in respect of common law penalties, and no party sought to re-open any questions that I decided in that judgment. I should, however, record that the Banks did not repeat two arguments that I had rejected, namely their contention of waiver (see paras 325 to 327 of my April judgment) and their argument that the 1999 Regulations displace the common law on penalties (see paras 328 to 331). However, they reserved their position about these contentions upon any appeal. RBSG also reserved its position in relation to another argument that I rejected in my April judgment when considering the application of the 1999 Regulations to Relevant Charges, namely whether the Relevant Charges are the price, or part of the price, for services provided by the Bank, although for my part I find it more difficult to understand how this might affect the question of common law penalties.
4. The court has a discretionary jurisdiction under CPR 40.20 to make binding declarations, and will exercise it to grant declarations as to the parties’ rights or as to the existence of facts or a principle of law, where the rights, facts or principles have been established to its satisfaction. As a matter of practice, the court is cautious about

making declarations on the basis of admissions or concessions: see, for example, Wallersteiner v Moir, [1974] 1 WLR 991 at p.1029 and 1030, applying Williams v Powell, [1894] WN 141. Moreover, as a general rule it is desirable to hear from all persons whose rights might be affected by a declaration: see Zamir & Woolf, The Declaratory Judgment (3<sup>rd</sup> Edition) at para 6.001. The declarations sought by the Banks might affect the rights of their customers whose current accounts are governed by Relevant Terms, and no customer appeared before me.

5. I must therefore exercise some caution before making the declarations sought by the Banks, and I accept the OFT's submission that I should not do so if there is a realistic possibility that further factual investigation might affect the position. That said, I also accept the Banks' contention that in large part the questions before me are of contractual construction that I can properly determine without further factual investigation or evidence.
6. There are particular reasons in this case that the court should be the more willing to exercise its declaratory jurisdiction. First, as I explained in my April judgment, one of the purposes of this action is to facilitate the expeditious, fair and orderly management of cases brought by individual customers in county courts, and the declarations are sought to that end. Secondly, the OFT has examined the Relevant Terms, drawn to my attention any which it considers might arguably be penal and made submissions in support of that view. It might be said that it has played the part of a representative bank customer. Moreover, the FSA (who was party to the Litigation Agreements to which I referred in my April judgment) was represented by counsel at the hearing before me and would, no doubt, have raised any concerns that it has. In my judgment the OFT has identified all of the Relevant Terms that might arguably be penal, and all its admissions and concessions have been properly made.
7. In the circumstances of this case, I consider that I should be prepared to make declarations such as the Banks seek provided I am satisfied of the legal position about whether the term is capable of being penal in its contractual context. I must be satisfied among other things that the provisions of the contract in question can be identified with sufficient certainty for a declaration to be properly and usefully made about whether its terms are capable of being penal. Of course, in any particular case a customer might have made his individual arrangements with his bank that varied or displaced those terms, but this consideration does not, I think, mean that it is necessarily inappropriate to make a declaration as to whether a contract on a bank's standard terms was capable of being penal in respect of particular provisions.

#### Provisions about the customer overdrawing on his account

8. I shall not repeat what I have previously said about the law of penalties. However, before considering the individual controversial terms, I should say something about two matters of some general application to what I have to decide.
9. First, as I put it in paras 64 and 66 of my April judgment, "Prima facie a customer is not in breach of his contract with his bank if he gives instructions to make a payment

without having the necessary funds or facility to cover the payment (whether at the time when the instructions are given by the customer or when they are received by the bank or both). He is taken to be requesting overdraft facilities .... The contractual position between bank and customer is not affected by the customer using a cheque guarantee card provided by the bank to support a payment made to a third party. The effect of its use is simply that the bank, through the agency of the customer, undertakes to the third party (not strictly by way of guarantee) that it will not dishonour the cheque on presentation for want of funds in the account...". I add that when a bank provides a debit card to a customer, it does not agree to provide the customer with credit: it is simply providing a convenient payment mechanism: see Goode, Consumer Law and Practice, Vol 1, Part 1C, para 24.84.

10. This is particularly relevant when considering the meaning and effect of statements in the Banks' documentation that a customer is not to overdraw his account without or in excess of a facility agreed in advance. In principle the parties could agree that the customer will be in breach of contract if he allows his account to become overdrawn. (As I explained in paras 325 to 327 of my April judgment, it would depend upon the facts of the particular case whether the customer would have a defence such as waiver or acquiescence.) Whether the parties have so agreed depends upon the wording of the particular contract between the Bank and the customer. However, I see force in the argument that it is unlikely that a bank and a current account customer would provide in their contract that the customer should be in breach of contract whenever the account became overdrawn, given that typically this will happen when upon his instruction his bank chooses to make a payment that it was not obliged to make.
11. The OFT recognises this: it submits that the intention and effect of such provisions is not that the customer is in breach of contract if the account in fact goes into overdraft. They are to be understood to provide that the customer is not to give his bank a Relevant Instruction, that is to say an instruction to make a payment for which the bank does not hold the necessary funds and has not agreed a facility when it comes to be processed. Mr J Crow QC, who represents the OFT, accepted that this interpretation often involves some departure from the contractual wording but argued that it reflects the substance of the agreement that the parties intended to make.
12. I accept the OFT's submission that in deciding whether a term is of contractual effect and if so whether its effect is to impose a prohibition on the customer, I should consider the substance of the arrangements between the bank and the customer. In considering whether a provision is of truly contractual effect, it might, as the OFT submits, be relevant that it is set out in a leaflet or other document which expressly states that it is of contractual effect or which contains provisions which are, or some of which are, obviously contractual. I also accept that typically a term capable of giving rise to a penalty will be in normative or prescriptive language, and will make the obligation or prohibition clear to the customer. However, the test for determining the meaning and effect of a written provision is to ask what its words in their context would convey to a reasonable man. As will be apparent when I consider the individual terms that are in issue, the OFT invites an interpretation of these provisions that involves a significant departure from their literal wording, and that to my mind is

not justified in order to identify what the words would convey as a matter of their natural and ordinary meaning.

13. I should mention some of the implications of the OFT's interpretation. First, as Mr Crow acknowledges, it would mean that a customer would be in breach of such a term if he (or another authorised signatory on the account) gave a Relevant Instruction that his bank declined to honour, notwithstanding that the account never in fact became overdrawn. Thus, a breach by the customer might result in him incurring either an Unpaid Item Charge if the Relevant Instruction was not honoured or another kind of Relevant Charge if it was.
14. Secondly, an account might become overdrawn otherwise than as a result of a Relevant Instruction: for example, because of interest or charges debited to the account. The OFT's interpretation of the prohibition against the account becoming overdrawn would have to be expanded to accommodate this.
15. Thirdly, Mr Crow accepted that a customer would not be in breach of a provision of this kind if he (or another authorised signatory on the account) drew and delivered a cheque which was not then covered by funds in his account provided that he knew that they would be there by the time that the cheque was presented and processed. Mr Crow submitted that what matters is whether there are the necessary funds or a facility at the time when the cheque comes to be processed. The timing of this is, of course, not in the control of the customer, but depends upon when the payee pays the cheque into his account.

#### Provisions about cheque guarantee cards

16. The second general matter that I refer to before turning to specific controversial provisions concerns whether Relevant Charges are payable upon a breach. I referred to this question in my April judgment, but my conclusions there did not depend upon it except in the relatively straightforward case of the Barclays' terms where the fact that the customer might have supported a cheque with his cheque guarantee card in breach of contract made no difference to the charges levied: see paras 308 to 312.
17. In Jervis v Harris, [1996] Ch 195 (to which I referred at para 299 of my April judgment) the Court of Appeal considered a term in a lease obliging a tenant to do repairs and providing that if he did not do so, the landlord might carry them out and recover from the tenant the costs and expenses incurred. Unsurprisingly, it was held that the money was payable not upon the breach but because the landlord decided to do the repairs himself and upon him doing them, notwithstanding that the tenant's breach was, of course, necessarily a part of the sequence of events whereby the money came to be payable. It was argued that similarly here the Banks' terms and conditions could not be penal because no breach on the part of a customer would be sufficiently closely connected with him incurring a Relevant Charge. In particular, this argument was raised in relation to terms that the customer was not to use a cheque guarantee card without having adequate funds or a facility to cover payment of the cheque. It was contended that a Guaranteed Paid Item Charge is payable upon

the overdraft being provided rather than upon the customer's breach. It can immediately be seen that in these circumstances the bank is committed to paying the cheque and in this respect (at least) its position is different from that of the landlord in Jervis v Harris, who was under no obligation to carry out repairs to the leased property.

18. The fact that a penalty is a sum payable upon breach does not mean that the law against penalties has no application whenever the wrongdoer receives some advantage from his wrongdoing, whether from and at the expense of the other party or otherwise, at least (and this is sufficient for present purposes) if the benefit to the wrongdoer and the corresponding expense to the other party is inherent in or intimately related to the wrongdoing, as when it involves the customer using a cheque guarantee card without the requisite funds or facility and thereby obtaining an overdraft. The payment levied for creating the overdraft would still be naturally referable to the breach: that, to my mind, would be the natural perception by the parties to the contract and the normal characterisation of the payment by the reasonable man. I would add that because the payment would be seen as referable to a breach, it might act in terrorem to deter breach, a fundamental characteristic of a penalty.
19. Nor do I consider that the law of penalties applies only if the wrongdoing is a necessary and sufficient cause of the charge being payable. The contract need not provide that the penalty is payable whenever the term is broken in order for it to be payable upon breach. Some banks allow customers a "buffer" so that charges are not levied if customers overdraw by a small amount, or do not levy a charge upon the first occasion that customers overdraw, or limit the number of charges levied in a month or other period. The fact that a payment is levied only if the breach is committed in particular circumstances or if other conditions are satisfied does not in itself mean that it is not paid on breach. Thus, a bank's terms might prohibit the customer from using his cheque guarantee card and provide for a Guaranteed Paid Item Charge, but allow the customer a "buffer". The Guaranteed Paid Item Charge imposed where the customer is not protected by the "buffer" might still be penal. (If the customer used his card when its use is prohibited but he was protected by the "buffer", it would depend upon the particular contract whether the bank would, in principle, be entitled to unliquidated damages, often nominal damages, or the provision of a "buffer" impliedly excluded this.)
20. Further, a sum can be penal if it is payable upon events that may or may not be a breach of contract if in fact it becomes payable upon a breach. Although the law on this question has caused some difficulty (see Chitty on Contracts (2004) 29th ed., vol 2 para 38-314), the better view, it seems to me, is that "where a sum is contractually payable on the happening of a number of events, including a breach of contract by the payer, the sum is capable of being a penalty when the circumstances giving rise to payment are the breach of contract, but not when the circumstances giving rise to payment are otherwise": Lewison, *The Interpretation of Contracts*, (2007) 3<sup>rd</sup> Ed para 16.04 p.598, and see Cooden Engineering Co Ltd v Stanford, [1953] 1 QB 86.

21. I make one further introductory observation. As I explained in para 323 of my April judgment, the application of the principle of construing contra proferentem means in these circumstances that, in the event of ambiguity or other uncertainty, the contract between a bank and its customer is to be construed so as to avoid customers being under a contractual obligation or prohibition, and to that extent therefore against a provision giving rise to a penalty. However, my decision has not depended upon the application of this principle in the case of any of the provisions that I consider in this judgment.
22. I come therefore to the provisions of the Banks' documentation which the OFT submits include Relevant Terms or provide for Relevant Charges that might be penal, or at least where the position is too uncertain for it to be appropriate to make a declaration.

### Abbey

23. The OFT submits that the "Terms and Conditions" in Abbey's leaflet dated January 2007 governing its current account ("Abbey's January 2007 conditions") include two provisions that are capable of being penal.
24. First, condition 6 of Abbey's January 2007 conditions was headed "Overdrafts", and condition 6.3 provided as follows:

"An unauthorised overdraft occurs if without our agreement you overdraw your Account or exceed the limit of an overdraft which we have agreed. If you overdraw your Account when we have not given you an overdraft you are in breach of these Conditions and must immediately pay sufficient money into your Account to put it into credit, taking account of any interest and charges you will have incurred. Similarly, if you exceed the limit of an overdraft which we have given you, you must immediately pay sufficient money into your Account to bring yourself within your overdraft limit."

Condition 6.4 provided that:

"If you have an unauthorised overdraft, you will be charged as set out in our Tariff of Charges or specified to you and these may include fees for transactions we are unable to process due to lack of available funds on your Account."

The relevant tariff provided for Unpaid Item Charges, Paid Item Charges and Overdraft Excess Charges.

25. The OFT submits that this condition provided that a customer was in breach of condition 6.3 if he issued a Relevant Instruction, that is to say an instruction for a payment that was not covered by funds in the account or an arranged facility, although it acknowledges that this involves some departure from the literal wording

- of the condition. Abbey accepts that condition 6.3 is of contractual effect, and submits that it obliges a customer who overdraws his account without or in excess of a facility immediately to pay funds into the account to redress the position. Abbey argues that condition 6.3 does not prohibit the customer from giving a Relevant Instruction, and that an account will be overdrawn only if it opts to pay upon a Relevant Instruction. Accordingly, it is said, the condition applies only if a Relevant Instruction is honoured, and then there is an obligation immediately to pay into the account sufficient funds to bring it into credit or within the limit of any overdraft facility on the account. A failure to comply with that obligation would be a contractual breach, but since it does not give rise to any Relevant Charge, condition 6.3 is not capable of being penal.
26. On the face of it, Abbey's submission too is inconsistent with the literal wording of condition 6.3. The second sentence specifically refers to the customer being in breach of the conditions if he overdraws his account, not if he fails immediately to repay any overdrawn amount; and the third sentence contemplates that the position will be "similar" if the customer exceeds an arranged overdraft limit.
27. Thus, both the OFT and Abbey invite an interpretation of condition 6.3 that requires some departure from its wording. The OFT submits that the references to the customer going overdrawn or exceeding an agreed overdraft are to be interpreted as references to him giving an instruction which would have that effect if Abbey made the payment requested. Abbey submits that the reference to the customer being in breach of the conditions refers not to what would be categorised as a breach as a matter of legal analysis, but to a condition triggering an obligation upon the customer to redress the unauthorised overdraft on his account. I prefer Abbey's construction of the condition. Although the lawyer would realise that the customer was not in contractual breach because of an unauthorised overdraft per se and might therefore consider the wording of condition 6.3 misleading, I do not consider that this interpretation unduly strains the language as it would ordinarily be understood. The condition is directed to making it clear that the customer who overdraws is operating the account in a way which the agreement does not contemplate and this puts him under an immediate obligation to take corrective action. The second sentence of condition 6.3 is to be read as a whole and the first part of it is, to my mind, naturally interpreted as simply providing a justification for the obligation specified in the second part.
28. I therefore accept Abbey's contention that condition 6.3 imposed a contractual obligation upon the customer to bring his account into credit or, as the case might be, within an agreed overdraft limit, if he overdrew because Abbey honoured a Relevant Instruction or for any other reason. However, if the customer was in breach of that obligation, it did not result in a Relevant Charge being levied: the analysis is similar to that under the Nationwide terms that I considered at paras 316 to 318 of my April judgment. It follows, in my judgment, that condition 6.3 is not capable of being penal.

29. Condition 16 of the “Terms and Conditions” in Abbey’s January 2007 conditions was headed “Using your cards” and sub-condition 16.3 was headed “Guaranteeing cheques”. It provided:
- “a) Your card may enable you to guarantee cheques. If so, you may use it in the UK, Gibraltar, Isle of Man or Channel Islands to guarantee payment of a personal cheque up to the limit of the card. The person you pay the cheque to must write your card number on the cheque. You cannot cash more than one guaranteed cheque a day. The guarantee is governed by the rules of the Cheque Card Scheme, details of which are available on request.
  - b) You must not use your card to guarantee a cheque for more than the available funds on your Account.
  - c) We may debit a guaranteed cheque to your Account even if it contains legal or technical irregularities.”
30. Abbey accepts that condition 16.3b was of contractual effect and that it imposed a contractual prohibition upon the customer relating to the use of a card. It operated as a prohibition against using the card to support a cheque for more than was in the account or covered by an overdraft facility when the cheque was processed.
31. The tariff of charges that applied to Abbey’s current accounts provided for payment of a Paid Item Charge of £30 “for each item we pay which results in an unauthorised overdraft or while you have an unauthorised overdraft” and an Overdraft Excess Charge of £20. It did not provide for a separate Guaranteed Paid Item Charge.
32. Abbey therefore submits that there is no penal consequence of breach of the prohibition in condition 16.3b because, while Abbey levied a Paid Item Charge, it did not levy a distinct Guaranteed Paid Item Charge; and thus it did not levy a charge or impose a payment by reason of the cheque card being used to guarantee a cheque. A breach of the prohibition upon use of a card might lead to the account incurring a Paid Item Charge because the guaranteed instruction is paid, but then the charge was not levied upon the card being used contrary to the prohibition. The use of the card is simply part of the history that leads to the Paid Item Charge being incurred. In short, Abbey submits that the position is indistinguishable from that which I considered in respect of Barclays’ terms at paras 308 to 312 of my April judgment.
33. The OFT submits that a factual investigation is required in order to assess Abbey’s argument, and that I should not make a declaration that condition 16.3b is not capable of being penal. I am unable to accept this: the question is one of interpretation of the relevant contractual provisions and for the reasons that Abbey advanced, I consider that condition 16.3b is not capable of being penal.
34. The other terms and conditions of Abbey that the OFT submits might include penal provisions relate to its Instant Plus account and took effect on 3 May 2005 (“Abbey’s

- May 2005 conditions”). The leaflet setting out these conditions stated in its introduction that they “(a) set out the contract between you and us; (b) explain our obligations to you, and your obligations to us...”.
35. Abbey’s May 2005 conditions included at condition 13.3b a similar provision to condition 16.3b of Abbey’s January 2007 conditions. Condition 24 was headed “Overdrafts” and it provided at condition 24.2:
- “An unauthorised overdraft occurs if without our agreement you overdraw your account. If you overdraw your account when we have not been given an overdraft you are in breach of these Conditions and must immediately pay sufficient money into your account to put it into credit, taking account of any interest and charges you will have incurred.”
36. In fact, Abbey did not issue cheque books to its customers with an Instant Plus account, and it submits that therefore no customer could be in breach of condition 13.3b. Furthermore, Abbey levied no Paid Item Charge, Guaranteed Paid Item Charge or Overdraft Excess Charge upon customers with an Instant Plus account. The only Relevant Charge was an Unpaid Item Charge.
37. I accept Abbey’s statement of its practice as to the operation of these accounts. As it seems to me, the question of Relevant Charges being penal could arise only if for some reason a customer had been permitted to operate an Instant Plus account in a way that Abbey did not contemplate and that was contrary to its practice. This leads to the question whether it is appropriate to make a declaration about Abbey’s May 2005 conditions. In light of representations that I received after making a draft judgment available to the parties, I shall invite further submissions about this.
38. It is agreed that Abbey’s January 2007 conditions (and its May 2005 conditions) are representative of other conditions used by Abbey between 2001 and September 2007 and the order that I make should reflect this.

### Barclays

39. The OFT submits that Condition 7 of the General Conditions of Barclays’ Terms and Conditions of May 2002 (“Barclays’ May 2002 conditions”) might be capable of being penal in effect. Barclays’ May 2002 conditions were introduced by a statement under the heading “Customer agreement” that:

“This agreement

- applies if you have an account with Barclays in the United Kingdom;
  - explains our obligations to you and your obligations to us;
- and

- applies to our key products and services provided to you in the United Kingdom.”

Condition 7 of the General Conditions was headed “Borrowing from us” and provided as follows:

“7.1 You must keep your account(s) in credit unless we agree an overdraft with you ...

7.3 If you

overdraw without agreeing an overdraft with us; or

exceed an agreed overdraft limit;

we may ask you to make an immediate payment into your account and we may charge our unauthorised interest rate and fees in the amount of the overdraft or excess until either it has been repaid or we have agreed an overdraft or an increased limit.”

40. Barclays’ May 2002 conditions provided at condition 9.4 for charges to be levied:

“To compensate us for the additional costs we have to pay if you break this agreement we will charge the standard charges set out in our tariff and the amount of any other losses and reasonable costs which we incur as a result of your breach of this agreement. These include, but are not limited to, the cost of tracing you, notifying you of the breach, communicating with you about the breach and enforcing payment of any amount due to us.”

Thus, the conditions contemplated that charges would be made upon the customer being in breach of his contract with the Bank.

41. The Relevant Charges that Barclays set out in the tariff and referred to in condition 9.4 were an Unpaid Item Charge and what was called from July 2002 a “Paid Referral Fee”. A Paid Referral Fee was charged, as I understand it, when the account went into unauthorised overdraft in any month and also whenever an unauthorised overdraft increased: thus, it did not exactly reflect a typical Paid Item Charge as described in para 6 of my April judgment (being charged by reference to days when an unauthorised overdraft was incurred or increased, rather than by reference to the number of Relevant Instructions that were honoured) or a typical Overdraft Excess Charge. The Bank allowed a “buffer” before a Paid Referral Fee was levied.
42. The OFT submits that condition 7.1 obliged the customer to keep his account in credit and that this obligation and the provisions for payments upon breach of condition 7.1 were reasonably capable of being penal. Barclays accepts that condition 7 was part

of its contract with its customer, but says that condition 7.1 did not impose any contractual obligation upon the customer: that at most it defined the circumstances in which Barclays was under a contractual obligation to pay in accordance with the customer's instructions. Mr Iain Milligan QC submits on behalf of Barclays that condition 7.3 did not provide for the consequences of the customer being in breach of a contractual obligation, but for the consequences of Barclays honouring the customer's instructions with the result that the account was not in credit, namely that Barclays might require that the account be put into credit and might charge fees and interest at the rate for unauthorised overdrafts. He argues that this condition is materially similar to the condition 8.2 in Clydesdale's current terms that, as I concluded in my April judgment (at paras 313 and 314), does not impose upon customers any contractual obligation or prohibition but at most defines the limits of customers' rights to give instructions to the Bank that the Bank must pay.

43. I agree with that submission. Accordingly, I reject the OFT's argument that the conditions applied when the customer issued a Relevant Instruction whether or not it was honoured. To my mind, the natural interpretation of condition 7.3 of Barclays' May 2002 conditions is that it is concerned only with when Barclays honoured a Relevant Instruction, and has no application if Barclays did not pay in accordance with it. This is clear from the wording of the condition and it is reinforced by the heading "Borrowing from us".
44. The OFT sought to distinguish Barclays' May 2002 conditions from the Clydesdale terms. It says that Barclays' conditions 7.1 and 7.3 can the more readily be seen to impose an obligation on the customer because they are expressed in terms of what "you", i.e. the customer, must do, whereas Clydesdale's conditions are expressed in the passive voice, "Your account must always be kept in credit unless you have agreed an overdraft facility with us...". I cannot attach this significance to the active voice of the verb.
45. I therefore do not consider that the Barclays' May 2002 conditions are capable of being penal. This conclusion is supported by a further argument made by Mr Milligan: that in its leaflet, "Our bank charges explained", Barclays did not indicate that a customer acted in breach of contract if he overdraw upon his account without arranging a facility in advance. Barclays said this:

"We would prefer you to ask for an overdraft before you need to use it. However, if you have not agreed or increased a limit with us in advance and go overdrawn or exceed your limit, you will be charged interest at the unauthorised rate. Any payment which causes this excess will be paid at the Bank's discretion ... Please note that we will charge a £20 paid referral fee when the balance of your account goes beyond your agreed limit or account buffer, if you have no agreed limit..."

This is consistent with the conclusion that I have reached, and it is proper to take account of the leaflet when interpreting the May 2002 conditions. The conditions

provided that the contract between the Bank and its customer was contained in, inter alia, the “additional conditions”, and these included the conditions in the leaflet: see paras 156 and 157 of my April judgment.

46. Having reached this conclusion, it is not necessary to consider an alternative argument advanced by Barclays, but I mention it briefly. Barclays contends that, even if condition 7 prohibited the customer from allowing his account to become overdrawn, no Relevant Charge was payable upon breach of that prohibition. Mr Milligan adduced two arguments in support of this contention. First, because under Barclays’ May 2002 conditions the customer was given a “buffer” and charges were levied only if the overdraft exceeded it, it was argued that a breach of the prohibition would not necessarily result in the Relevant Charge being levied. As I have said, in my judgment a charge can be penal without it being payable whenever there is a breach of the contract. Secondly, Mr Milligan submitted that condition 7 is not penal because the Relevant Charges would still be incurred even if the contract did not prohibit the customer from overdrawing: it was said that the charges were not incurred upon the breach because they would still have been payable if the provision that the customer was in breach if he overdraw on his account were deleted from the contract. This does not, I think, show that, in the contract as it was written, no Relevant Charge is imposed upon a breach, and I am not persuaded by this alternative argument.
47. The OFT submits that there are provisions in the terms published in 2003 for Woolwich’s Openplan accounts (the “Woolwich Openplan 2003 conditions”) that are capable of being penal. The Woolwich Openplan 2003 conditions were in a leaflet entitled “terms and conditions” and containing “general terms and conditions” and specific terms and conditions relating to different kinds of accounts. Condition 7 of the “current account terms and conditions” was headed “Current Account Reserve”, and the expression “Current Account Reserve” was defined as “an overdraft”. Condition 7 provided as follows:

“7.1 We reserve the right to decline any request from you to borrow using a Current Account Reserve. ...

7.5 Our prior agreement must be obtained before you exceed your Current Account Reserve limit.

7.6 We may decide not to pay a cheque or other item or refuse authorisation for a Card transaction if it would cause the available balance on your Account to be exceeded. ...

7.8 If we pay a cheque or other item issued by you and as a result you exceed the available balance on your Account, this does not mean that we have agreed a Current Account Reserve, or an increase to your agreed Current Account Reserve limit. You must pay us sufficient money to cover the amount of the cheque or other item without delay.

7.9 You must not use your Card to borrow from us unless a Current Account Reserve has been agreed separately...”

48. Condition 13.2 provided that the Bank might “levy reasonable transaction and service charges ... including but not limited to fees in respect of a Current Account Reserve...”. The Relevant Charges set out in the applicable tariff were an Unpaid Item Charge and a Guaranteed Paid Item Charge, both of which were described as being in respect of “administrative costs”, and also an Overdraft Excess Charge.
49. Mr Milligan submits that condition 7.5 did not prohibit the customer from giving a Relevant Instruction (as the OFT contends), but identified the circumstances in which he had a right to exceed his authorised overdraft limit (or Current Account Reserve limit). This, he argues, is clear once it is recognised that condition 7.5 must be read in its context, that is to say together with conditions 7.6 and 7.8. I agree with that submission: this construction seems to me to be in accordance with the natural and ordinary meaning of condition 7 read as a whole. It would strain the language of condition 7.5 to interpret it as prohibiting the customer from issuing a Relevant Instruction, and there is no good reason to impose that strained interpretation upon it.
50. This leads to the question how condition 7.9 is to be interpreted. The “Card” to which condition 7.9 referred was defined as “an ATM card and debit card and where so stated on the card a cheque guarantee card”. Thus, use of the card did not always mean that the Bank was obliged to honour the Relevant Instruction: it would have to do so only if the card was used as a cheque guarantee card or if the debit card was used above a retailer’s “floor limit”. Nevertheless, if condition 7.9 were to be construed in isolation from the rest of condition 7, then I would, I think, see force in the OFT’s contention that it imposed a contractual prohibition upon the customer, so as to provide that he was in breach of his contract with the Bank if he used the card without the necessary funds to make the payment in question and without an agreed facility. However, I am persuaded by Mr Milligan’s submission that it is important that condition 7.9 is to be construed as part of condition 7, and alongside condition 7.5; and that it is understood to have a similar effect to condition 7.5. For this reason, I reject the submission that condition 7.9 imposed a contractual prohibition on the customer.
51. Having reached these conclusions, I do not need to consider Mr Milligan’s further argument that, even if conditions 7.5 and 7.9 imposed contractual prohibitions, no Relevant Charge was levied upon breach.
52. Finally, as far as Barclays is concerned, I come to the “Banking and Savings Conditions” which were issued in 2003 for Woolwich’s current accounts (“Woolwich’s 2003 Banking and Saving Conditions”). These were introduced with the words, “These Conditions are the contract which you will have with us. They explain your obligations to us and our obligations to you...”. Part 4 was headed “Overdrafts” and condition 4.1 provided as follows,

“You should always keep your Account in credit and we will require immediate payment of any unauthorised overdraft. We may allow you to go overdrawn if we have already agreed an overdraft with you or we allow a Payment Transaction which results in your Account going overdrawn. We will write to you to confirm the amount and the terms of an overdraft.”

The expression “Payment Transaction” was defined and meant a withdrawal from the account by any instruction.

53. Part 5 was headed “Charges”. It provided that Barclays might make a charge for Payment Transactions and services, and that

“If you have gone overdrawn on your Account without our permission or breach any of these Conditions ... we reserve the right to charge you for any costs incurred ... in the recovery of your Account Documents, the cost of the overdrawn balance, reasonable costs and fees paid by us in tracing you and recovering the overdrawn balance.”

54. The tariff relevant to the Woolwich’s 2003 Banking and Saving Conditions provided for an Unpaid Item Charge and a Guaranteed Paid Item Charge (again described as administrative charges), and for an Overdraft Excess Charge.
55. Barclays’ argument in respect of this condition is similar to that about condition 7 of Barclays’ May 2002 conditions, and for similar reasons I accept it.
56. It is agreed that Barclays’ May 2002 conditions, the Woolwich Openplan 2003 conditions and the Woolwich’s Banking and Saving 2003 Conditions are representative of other conditions used by Barclays between 2001 and 2007.

#### Clydesdale

57. The OFT submits that there are provisions in the Terms and Conditions published in 2000 to apply to Yorkshire Bank’s current accounts (the “Yorkshire 2000 conditions”) that might be penal. Condition 2 was headed “Operation of the Account”. Condition 2.9 explained what was meant by “uncleared cheques”, that is to say cheques paid into the account in respect of which funds had not yet been collected, and condition 2.10 provided,

“You should not withdraw against these uncleared cheques unless we give you permission. If you do draw against them, debit interest may be payable even though your statement may show your Account is in credit.”

58. Condition 3 was headed “Overdraft” and provided as follows:

“3.1 You must obtain our agreement before you overdraw your Account.

3.2 If we decide to make payments from the Account, or pay cheques which are guaranteed by your cheque guarantee card when there are insufficient funds available, then any overdraft created is classed as unauthorised. This is also the case when you exceed any overdraft limit. See also 4.4 below.

3.3 If you draw cheques, authorise or make payments without sufficient money available in your Account, taking account of any overdraft limit and allowing for uncleared cheques, we may return the payments and make a charge for doing so.

3.4 In accordance with normal banking practice, all overdrafts are payable on demand.”

Condition 4.1 provided, “Charges and interest applicable to the Account are published in the form of tariffs....”. Condition 4.4 (to which condition 3.2 referred) provided that, “If your Account has an unauthorised overdraft, then additional charges may be levied which will be debited to your Account on the day on which the overdraft is created”.

59. The relevant tariff provided for Unpaid Item Charges, a Guaranteed Paid Item Charge (and also a Debit card abuse charge for Switch transactions that would have been returned by the Bank had they not been guaranteed), and an Overdraft Excess Charge. The Bank allowed a “buffer” which protected the customer when the amount of overdrawn was small.
60. The OFT submits that the effect of conditions 2.10 and 3.1 might be penal. The Bank submits that these conditions were not of contractual effect but only advised or informed the customer of his rights; that they did not in any event impose any contractual obligation on the customer; and that no Relevant Charge was imposed if the customer did not observe the conditions.
61. The Yorkshire 2000 conditions certainly included statements that were simply informative: for example, condition 5 that was headed “Good Banking”. Condition 2 itself contained both contractual terms and mere information. (An example of the latter is condition 2.15: “Cheques made payable from your account which are 6 months or more old may be returned unpaid”.) Mr Richard Salter QC, who represents Clydesdale, submits that condition 2.10 was one of a series of conditions that explained to the customer how the account worked. I agree with that submission. There would have been no good reason for the Bank to place specific restrictions upon the customer overdrawn his account that applied after he had paid into his account cheques that had not been cleared, but that did not apply when he overdrawn in other circumstances. The real question as far as the Yorkshire 2000 conditions

are concerned is whether condition 3.1 imposed a general contractual prohibition against overdrawing and if so whether a Relevant Charge was levied upon breach.

62. I reject the OFT's submission that condition 3.1 contained a contractual prohibition. It seems to me that, as Mr Salter submits, there is really no significant difference between this condition and condition 8.2 of Clydesdale's current terms and conditions, and that the thrust of the reasoning at paras 313 to 314 of my April judgment is applicable to condition 3.1. As with the Barclays' May 2002 conditions, I reject the OFT's suggestion that the impact, or natural meaning, of condition 3.1 is different because condition 8.2 is expressed in the passive voice ("Your account must be kept in credit..."). I consider that condition 3.1 is naturally understood as stating the limits upon the customer's rights and therefore upon the Bank's obligations to pay upon his instructions.
63. Mr Salter also submitted that no Relevant Charge would be payable upon a breach of condition 3.1 because a breach was not a necessary and sufficient condition of any Relevant Charge being levied. As I have explained, I reject the submission that a charge cannot be a penalty unless a breach is a necessary and sufficient condition of the charge being payable. However, in view of my other conclusions about conditions 2.10 and 3.1, I say no more about Mr Salter's arguments that none of Clydesdale's Relevant Charges would be payable upon breach.
64. The terms and conditions of Yorkshire Bank for current account customers in October 2003 are not materially different from the Yorkshire 2000 conditions, and for similar reasons I do not consider them to be capable of being penal.
65. I understand that since the July hearing Clydesdale have drawn to the attention of the OFT other terms that the OFT either accept are not capable of being penal or are not distinguishable from the Yorkshire 2000 conditions. I shall invite further submissions from the OFT and Clydesdale about whether I should make any declaration about them.

## HBOS

66. The terms (the "HBOS Easycash 2007 conditions") that are now used for HBOS's basic account, which it calls its Easycash account, are set out in a leaflet dated March 2007. It explains on page 2 under the heading "Account features" that it is "a straightforward account and is ideal if you don't need an account with an overdraft, a cheque book or a cheque guarantee card". On the next page, the leaflet states, "there is no authorised overdraft facility". On page 5, under the heading "Charges and interest for unauthorised overdrafts", it states, "There is no overdraft facility on Easycash accounts. If you are aged 18 and over and have an unarranged overdraft, we will charge you interest and make charges for failed Direct Debits and standing orders which may apply...". HBOS levies an Unpaid Item Charge on this account but no other Relevant Charges.

67. The leaflet sets out “Easycash conditions”, which are said to “explain how your account works. These conditions also tell you about the main services we may let you use on your account...”. Thus, the leaflet presents the conditions as having, at least in part, an explanatory purpose.
68. Condition 15 is headed, “Overdrawn accounts”. It reads:
- “15.1 You must not allow your account to go overdrawn. If any transaction does make your account go overdrawn, this does not mean that we have agreed to allow you to have an overdraft.
- 15.2 If your account goes overdrawn we will charge you interest at the rate or rates of interest we set. You must also immediately pay us the amount that you are overdrawn (and any charges) so you are no longer overdrawn. ...
- 15.7 We may make charges in connection with any overdraft on your account under conditions 16.1, 16.2, 16.3 and 16.4.”

The conditions that are referred to in condition 15.7 provide that HBOS may make charges “on your account and for services or facilities we make available to you”; that the current charges are shown in the leaflet; and that HBOS may change the charges. The leaflet shows an Unpaid Item Charge for customers who are aged over 18 of £39 per item (subject to a maximum of 3 items per day), and, as I have said, no Paid Item Charge or other Relevant Charge.

69. The OFT argues that condition 15 is in a part of the leaflet that describes itself as setting out “Conditions”, and is expressed in terms of what the customer “must” do: that is to say, that it is directed to the customer and uses language at least consistent with a contractual obligation. Thus, the OFT submits that in substance the condition puts the customer under a contractual obligation not to issue any instructions which, when they come to be processed, are not covered by funds in the account.
70. The OFT acknowledges that elsewhere in the HBOS Easycash 2007 conditions the expression “you must” is used simply to inform the customer how to operate his account without creating any contractual obligation. For example, the customer is told that if, having reported his card lost or stolen, he finds it, “you must cut it into two pieces...”. However, the OFT points out that in condition 15.2 the expression “you must immediately pay us the amount that you are overdrawn...” places an obligation on the customer, and it submits that in condition 15.1 the expression “you must not....” should be given similar effect.
71. It is important to recognise that the Easycash account is a basic account and as such is an account upon which overdraft facilities are not provided. Considered against that background, in my judgment condition 15 defines the limits of the customer’s right to have instructions honoured and makes clear the limits of the facilities that HBOS

provides on the account. This is consistent with and reflected in condition 15.2 that requires that if an account becomes overdrawn the overdrawn must immediately be repaid, and the fact that the only Relevant Charge is an Unpaid Item Charge. Moreover, even if condition 15 placed a contractual prohibition upon the customer, I would not interpret it as applying when the customer gave a Relevant Instruction that was dishonoured and would not conclude that any Relevant Charge was payable on its breach. The HBOS Easycash 2007 conditions are in my judgment incapable of being penal.

72. HBOS' earlier leaflets for its Easycash account dated April 2003, November 2004 and January 2006 contained provisions that were materially similar, and I conclude that their provisions too are not capable of being penal.

73. Conditions that historically applied to Halifax Bank Accounts and Cardcash accounts were set out in HBOS' leaflets dated November 2001 (the "Halifax 2001 Conditions"), Cardcash accounts being of the nature of basic accounts and allowing no overdraft or other credit facilities. The leaflets had on their cover "Special conditions, Bank account conditions". It was stated under the heading "Welcome to the Halifax" that the conditions "explain how your account works"; and that the charges and interest were set out in a separate leaflet.

74. Condition 12 in the Halifax 2001 Conditions was headed, "How do you use a card to guarantee a cheque?" It provided:

“12.1 If your card has a cheque guarantee sign on it, we will always pay a cheque you write for no more than the amount shown on the cheque guarantee sign on the card, if the person that you make the cheque out to complies with the Association for Payment Clearing Services Rules of the UK Domestic Cheque Guarantee Card Scheme...”

12.2 You must not use your card to guarantee a cheque if the amount of the cheque is more than you have in your account (taking account of any agreed overdraft and the amount of any withdrawal which we still have to take out of your account)”.

75. Condition 18 was headed "Overdrafts". It provided:

“18.1 If you have a Cardcash account you must not allow your account to go overdrawn. If you have a Halifax Current Account then unless we agree that you can do so, you must not use your account or allow anyone else to use it if this would make your account go overdrawn or over your overdraft limit....”

18.4 If without our agreement:

- your account goes overdrawn; or

- you go over your overdraft limit,

we will charge you interest on the amount of your overdraft, including any agreed overdraft, at the rate or rates we set. You must also immediately pay us the amount that you are overdrawn (and any charges) so that you are no longer overdrawn or bring the overdraft back within your agreed overdraft limit....

18.9 If we have:

asked you to pay any money you owe us on your account; or

got a court judgment for you to pay any money you owe us on your account,

then, for as long as your account is overdrawn, you will have to pay interest ... and any charges on your overdraft. ...

18.12 We may make charges in connection with any overdraft on your account under condition 19.1 or 19.2.

18.13 We may also make charges in connection with any overdraft on your account under condition 19.3 or 19.4.”.

76. Condition 19.1 provided that HBOS could make charges “on your account and for services or facilities we make available to you”, and continued, “Please ask us for a copy of the current charges (including those for basic account services) which apply to Halifax Current Accounts and Cardcash accounts”. Condition 19 went on to provide that the Bank could change the charges.
77. HBOS produced leaflets setting out its account charges and interest rates. Until April 2003 they provided for an Unpaid Item Charge and an Overdraft Excess Charge subject to a “buffer”. From 28 April 2003 HBOS removed the “buffer” and also introduced a Paid Item Charge. It never had a Guaranteed Paid Item Charge distinct from the Paid Item Charge.
78. The OFT submits that conditions 12.2 and 18.1 might be capable of being penal.
79. HBOS accepts that condition 12.2 was of contractual effect and that it imposed a contractual prohibition on the customer. It submits that because it levied no Guaranteed Paid Item Charge distinct from the Paid Item Charge, no Relevant Charge was imposed upon breach of condition 12.2 and therefore it is not capable of being penal. I accept that submission. I consider that the reasons that I held in my April judgment (at paras 308 to 312) that condition 12.2 of Barclays’ card conditions is not capable of being penal apply equally to condition 12.2.

80. HBOS disputes that condition 18.1 imposed a contractual prohibition on the customer. I also agree with that submission. The first sentence, it seems to me, like condition 15.1 of the HBOS Easycash 2007 conditions, defined the limits of the customer's right to have his instructions honoured by the Bank. I consider that the second sentence is naturally to be understood to have a similar effect to the first sentence, and therefore, as I interpret the provision, it too defined the customer's rights.
81. I therefore conclude that the Halifax 2001 Conditions are not capable of being penal. HBOS' conditions issued for Halifax Bank Accounts and Cardcash accounts in July 2003, November 2004, February 2005, May 2005, June 2006 October 2006 and February 2007 are materially similar to the Halifax 2001 Conditions, and similarly I conclude that they are not capable of being penal.
82. HBOS also applied for a declaration in respect of the terms governing its Intelligent Finance accounts (to which I referred at para 38 of my April judgment). However, in the course of the hearing, it became apparent that there was not sufficient material before the court to deal satisfactorily with them. I adjourned that application, giving the parties liberty to restore it.

### HSBC

83. HSBC issued a leaflet entitled "Personal Banking, terms and conditions" in July 2001 that applied to the Bank's current accounts and contained what I shall call the "HSBC 2001 current account conditions". The leaflet stated, "These terms and conditions are a contract between you and us". Condition 5 of Section 1 was headed "Clearing credits and cheques". Condition 5.2 was headed "Credits you receive" and condition 5.2.1 read as follows:

"We determine whether a cheque has "cleared" in order to:

- decide whether to allow you to withdraw the money, and
- calculate any interest that should be paid, either by us to you or by you to us, and
- most importantly, confirm whether a cheque has been paid.

A cheque can still be returned unpaid later even if we have decided to allow you to withdraw the money ... Please ensure that you understand what happens when a cheque is returned unpaid later as set out below. If you do not understand, please ask us to explain."

The condition then set out various details about clearing procedures and continued, “You should not write a cheque unless you have cleared funds in your account from which such cheque can be met”.

84. Condition 7 was headed “Borrowing from us”, and read, “Provided you are 18 years of age or over, borrowing can be arranged either by overdraft on your Bank Account subject to the terms below, or by a separate loan ..” It continued, at condition 7.1:

“You should always keep your Bank Account in credit unless we have agreed an overdraft with you. We understand that occasionally you may accidentally overdraw your account by a small amount without an agreed limit. If we allow this to happen, we will not charge you our applicable fee for overdrafts not agreed in advance as long as your Bank Account is not more than £50 overdrawn. Customers under the age of 18 must always keep their bank account in credit. ”

Condition 7.4 provided, “You must not go over any overdraft limit that is agreed with us unless you get our agreement first”. Condition 7.7 provided that HSBC might “decide not to pay a cheque or other item or to allow a card transaction if it would make your account go overdrawn or, for Bank Accounts, it would go overdrawn without an agreed overdraft limit or over any agreed overdraft limit. This would include standing orders, Direct Debits or bill payments which you had previously instructed us to make or Switch transactions you have made. If this happens, we may charge our fee for returned items”. Condition 7.9 provided that, if HSBC decided to pay upon a Relevant Instruction and this resulted in an overdraft or an overdraft in excess of an agreed limit, “this does not mean that we have agreed an overdraft or an increased limit”. Condition 7.10 provided for interest to be charged on overdrafts, and condition 7.11 provided, “As well as charging interest under 7.10, we may also charge our applicable fee for overdrafts not agreed in advance for any statement period when your Bank Account is overdrawn without an agreed overdraft or goes over any agreed overdraft limit, whether for one day or more, to cover our management and administration costs (see the relevant price list).”

85. Condition 9.2 was headed “Your card and your account”, and dealt with the customer’s use of a bank card. Condition 9.2.2 provided, “You must not use your debit card to borrow from us on your Bank Account unless you are 18 and over and an overdraft has been agreed separately”. Condition 9.2 and subsequent conditions contained other provisions about what the customer “must not” do: for example, condition 9.2.4 provided, “You must not use your card after the end of the month when it expires as stated on your card...”.
86. The tariff for the HSBC 2001 current account conditions provided for an Overdraft Excess Charge, an Unpaid Item Charge and a charge in respect of guaranteed cheques and Switch transactions. This was similar to a Guaranteed Paid Item Charge, but was not levied for each item but was initially a “£30 flat fee” and then levied on the basis of a charge of £30 per item “after the initial advice”.

87. The OFT submits that conditions 5.2.1, 7.1, 7.4 and 9.2.2 are capable of being penal. It argues that, when condition 5.2.1 stated that, “You should not write a cheque unless you have cleared funds in your account from which such cheque can be met”, it created a contractual prohibition and the customer was in breach of contract if he contravened it. However, to my mind that does not take proper account of the context of the sentence. It was part of an explanation about how the Bank dealt with cheques paid to the credit of the account. I interpret it as advisory and not as creating a contractual prohibition.
88. HSBC accepts that conditions 7.1 and 7.4 were of contractual effect in that they set out the limits upon the customer’s rights to have the Bank honour his instructions. It disputes that the expressions about what the customer “should” or “must” do evince an intention that he should be under a contractual prohibition, and that the customer was in breach of contract if he gave a Relevant Instruction (or gave a Relevant Instruction that the Bank decided to honour). Accordingly, the Bank submits that these conditions were similar in their effect to condition 8.2 of Clydesdale’s current terms that I considered at paras 313 and 314 of my April judgment. I agree with this submission. As with other terms to which I have referred, I am not persuaded by the OFT’s submission that, because, unlike Clydesdale’s condition 8.2, HSBC’s conditions 7.1 and 7.4 are not expressed in the passive voice, they should be given a different interpretation.
89. HSBC submits that condition 9.2.2 did not evince an intention to create a contractual prohibition on the customer about using a debit card to borrow from the Bank because the condition was directed towards actual borrowing and not to attempts to borrow with the card: that is to say, it was directed to what could come about only with the Bank’s consent. Again, I accept HSBC’s submission. The wording of the clause was not apt to cover an attempt to use the card to overdraw the account, and to my mind the natural interpretation of the condition is that it explained to customers their rights as account holders.
90. I therefore do not need to consider HSBC’s further argument that if any of these conditions imposed a contractual prohibition, no Relevant Charge was payable upon breach of it.
91. The version of the Personal Banking terms and conditions issued in September 2002 (the “HSBC 2002 current account conditions”) contained provisions similar to those at conditions 5.2.1, 7.1 and 9.2.2 of the HSBC 2001 current account conditions. Condition 7.4 was slightly differently worded: “You should always stay within an agreed overdraft limit unless you get our agreement to increase this first”.
92. I come to the version of the Personal Banking terms and conditions issued in August 2005 and applicable to current accounts (the “HSBC 2005 current account conditions”). Condition 5.1.1 stated, “... You must only write a cheque if there are cleared funds in the account, or an agreed overdraft to cover it”. Condition 5.2.1 provided that if the customer drew against uncleared cheques which are subsequently

returned unpaid “we may charge interest (if applicable) and/or our applicable fee for overdrafts not agreed in advance”.

93. Condition 7 was headed “Borrowing from us”. Condition 7.3 stated, “You must keep your Bank Account and saving account(s) in credit unless we have agreed an overdraft”, and condition 7.4 provided, “We will give you a letter setting out the terms of any agreed overdraft. You must stay within the agreed limit.” Condition 7.11, headed “Unauthorised overdrafts”, said:

“As well as charging interest ... we may also charge our applicable fee for reviewing unauthorised overdrafts each time your Bank Account or savings account goes overdrawn, or further overdrawn, without an agreed overdraft. We may also charge this fee when your Bank Account goes over, or further over, any agreed overdraft limit.”

Condition 7.16 provided:

“We may not pay a cheque or other item or allow a card transaction, if it would make your account go overdrawn or over any agreed overdraft limit. We may charge you for this. If we do pay the cheque, other item or card transaction and your account goes overdrawn or over any agreed overdraft limit, this does not mean that we have agreed an overdraft or increased limit. You must immediately pay enough into your account to cover the overdrawn amount or the amount that is over your overdraft limit, or contact us to discuss the matter.”

Paragraph 7.17 provided that the Bank might charge fees as well as interest if it paid a cheque guaranteed by a Maestro debit card or a Maestro transaction and the account went overdrawn or over an agreed overdraft limit as a result.

94. Condition 9 concerned cards and condition 9.2.2 provided, “You must not use your debit card to borrow from us on any account without an agreed overdraft”.
95. The tariff for the HSBC 2005 current account conditions provides for a Paid Item Charge, a Guaranteed Paid Item Charge and an Unpaid Item Charge.
96. I do not consider the differences between the HSBC 2001 current account conditions and the 2002 and 2005 versions significant for present purposes. I consider that the 2002 and 2005 versions are not capable of being penal.
97. The “principal” terms and conditions dated July 2001 that HSBC used for its First Direct customers (the “First Direct 2001 conditions”) were introduced as follows:

“Banking with First Direct is designed to take the hassle out of your financial life, by giving you, the individual, control of your money when it suits you, letting you get on with what’s

next. There needs, naturally, to be some ground rules, so that we both know where we stand. These are for your protection as well as ours. ”

They went on to state that the First Direct 2001 conditions “are the contract between you and us”.

98. The First Direct 2001 conditions provided at condition 3.5 that if the account went overdrawn or if an overdraft was increased because an item was returned unpaid, fees might be charged.
99. Condition 4 was about cards that could be used in ATMs, as debit cards to pay for goods and services at retailers or over the internet or through other electronic media and as cheque guarantee cards. Condition 4.5.2 provided that:

“You must not use your card to borrow from us unless an overdraft has been agreed separately. ... Unauthorised overdrafts will be charged interest at our Unauthorised Overdraft Interest Rate. We will also charge our usual fees for unauthorised overdrafts. ”
100. Condition 5 was headed “Borrowing From Us” and condition 5.1.1 provided, “You should always keep your Cheque Account or Bank Account in credit, unless we have agreed an overdraft with you...”. Condition 5.1.3 provided, “You should not exceed any agreed overdraft limit unless you get our agreement first”. Condition 5.1.6 provided that if the Bank paid in accordance with a Relevant Instruction and the account went into overdraft or exceeded an overdraft limit, “this does not mean that we have agreed an overdraft, or an increase to your agreed limit”. Condition 5.1.7 provided that if the account went into unauthorised overdraft, then interest would be charged and “an Overdraft Fee for any statement month when the balance on your account exceeds your limit, whether for one day or more, and an Excess Overdraft Fee for any day where there are subsequent increases in the excess or re-occurrence of an excess during the statement month”. It went on to say that the overdraft fees were published in the Bank’s Interest Rates and Charges Leaflet and on its website. The tariff leaflet provided for charges by way of an Overdraft Excess Charge and something akin to a Paid Item Charge, and also for an Unpaid Item Charge.
101. The OFT submits that conditions 4.5.2, 5.1.1 and 5.1.3 are capable of being penal, but I reject that submission. Condition 4.5.2 is not distinguishable from condition 9.2.2 of the HSBC 2001 current account conditions, and conditions 5.1.1 and 5.1.3 are not distinguishable from conditions 7.1 and 7.4 of the HSBC 2001 current account conditions.
102. The Account terms and conditions that HSBC used for its First Direct customers and that were dated January 2006 stated that they were “the contract between you and us”. They had a provision similar to condition 4.5.2 of the July 2001 terms and conditions. They provided in the Special Conditions at condition 4.5.1 under the heading

- “Cheques” as follows: “You may only write a cheque on a Cheque Account or a Bank Account and only then if there are cleared funds in the account or an agreed overdraft to cover it”. The condition went on to explain the timing of clearing procedures.
103. Condition 5.3 was headed “Your Card and Your Account”. Condition 5.3.1 provided that, “You must not use your card to borrow from us unless an overdraft has been agreed separately .... Unauthorised overdrafts will be charged interest at our unauthorised overdraft interest rate. We will also charge our usual fees for unauthorised overdrafts”.
  104. Condition 6 of the Special Conditions was headed “Borrowing from us” and condition 6.1 provided: “You may borrow from us on your Cheque Account or Bank Account if we have agreed an overdraft facility with you. You must stay within the agreed overdraft limit. If we have not agreed an overdraft facility with you, you must keep your Cheque Account or Bank Account in credit.” Condition 6.7 provided, “We may not pay a cheque or other item or allow a card transaction, if it would make any account go overdrawn or go over an agreed overdraft limit. We may charge you for this.” Condition 6.9 was in similar terms to condition 5.1.7 of the First Direct 2001 conditions. Condition 6.10 said that the Bank would continue to charge the unauthorised overdraft interest rate and other charges until an overdraft was agreed or the cleared balance on the account was in credit or within any agreed overdraft limit.
  105. As with the First Direct 2001 conditions, the relevant tariff provided an Overdraft Excess Charge, for something similar to a Paid Item Charge and for an Unpaid Item Charge.
  106. The First Direct terms and conditions dated February 2007 are materially similar to the 2006 version.
  107. I consider that, like the First Direct 2001 conditions, the 2006 and 2007 versions are materially similar to the HSBC 2001 current account conditions, and therefore I consider them incapable of being penal.
  108. It is agreed that the conditions that I have considered are representative of other conditions used by HSBC in 2001 and thereafter, and the order that I make should reflect this.

#### Lloyds TSB

109. As I explained in my April judgment (at para 240), before November 2007 Lloyds TSB did not have full written terms for its current account services. However, it issued leaflets that set out “Terms and Conditions” for current account customers who had a bank card governing use of the card. The last version was called “for the journey” and was issued in March 2007, and I shall call the terms the “Lloyds TSB 2007 card conditions”. Earlier versions of the leaflets containing similar terms (as far as is material) were issued in March 2001, October 2004 and October 2006.

110. The cards to which the Lloyds TSB 2007 card conditions applied were of three kinds: Cashpoint cards that only allowed the customer to withdraw cash from ATMs; debit cards that allowed both cash withdrawals at ATMs and use as a debit card to pay retailers; and cards that could be used as cheque guarantee cards as well as a debit card and for ATM withdrawals. The leaflets used the language of contract: for example, condition 1 was headed "Definition of some Words used in this Agreement".
111. Condition 6 of the Lloyds TSB 2007 card conditions was headed "Your Cheque Guarantee", and condition 6.5 provided, "You must not write a Guaranteed Cheque which exceeds the amount in your Account or the limit of any overdraft we have agreed with you". This was one of a number of provisions about how the customer was to use his card: for example, condition 6.2 provided, "You must sign and date the cheque in the presence of the payee and make sure that the payee (not you) writes the Card number on the back of the cheque"; and condition 6.4 provided, "You must not write more than one cheque guaranteed by us in any one Transaction".
112. Condition 9 was headed "Your Account". Condition 9.1 provided, "We provide you with your Card so that you can operate your Account more conveniently. The Card itself does not give you an automatic overdraft or any other form of credit. We will be entitled, under the terms of the Account, to charge interest at our standard rate for unauthorised overdrafts and to debit that interest and any resulting bank charges from your Account". Condition 9.2 provided, "If you do use your Card to create an overdraft we have not agreed or to exceed an agreed overdraft limit, you will have broken the terms of the Account and you must repay the unagreed amount immediately". Condition 9.4 read, "We may deduct from your Account any charges payable as specified in our published tariff of charges. We may change the tariff at any time but we will send you a copy of the new tariff before any changes take effect and you can get a copy of the latest tariff from any of our branches".
113. Relevant tariffs of charges were published in a series of leaflets: no fewer than 16 versions of it were published between July 2001 and June 2007. I was also referred to some pages printed from Lloyds TSB's website which set out charges, but condition 9.4 referred to a tariff that was published in the form of a copy that could be obtained from branches. I am not in a position to determine on the evidence before me whether information on the website is of any, and if so what, contractual significance; and I shall say nothing more about it.
114. The leaflets were not concerned only with charges relating to use of a Card. The wording of the leaflets differed from time to time, but I can sufficiently explain the position by referring to the version that was current between December 2006 and June 2007. Under the heading "If you go overdrawn without agreeing this with us first", it stated this: "We will ... charge you a fee for any borrowing not agreed with us in advance. These charges are shown in the table below, and will be charged to your account monthly". The table set out an "Overdraft Excess Fee" and an Unpaid Item Charge (called a "Returned item fee"). Of the Overdraft Excess Fee, the table stated "We charge this when you go overdrawn and don't have an overdraft, or if you

- go overdrawn above an agreed overdraft limit. We will charge this fee again on each day we make a payment for you that increases your overdraft”. Thus, like the Barclays’ Paid Referral Fee, the Overdraft Excess Fee did not exactly reflect a typical Paid Item Charge or a typical Overdraft Excess Charge as described in para 6 of my April judgment. The table stated of the “Returned item fee”, “You’ll be charged this fee whenever there is not enough money in your account to make a payment such as a direct debit, cheque or standing order”. Despite this, I understand from the name “Returned item fee” that this charge was not made whenever the Bank received a Relevant Instruction but when it declined to pay a Relevant Instruction.
115. Until August 2006 the customer had the benefit of a “buffer” so that he was not charged an Overdraft Excess Fee unless he overdraw his account (or exceeded an agreed overdraft limit on it) by more than £10. Further, from April 2002 the Bank did not charge the Overdraft Excess Fee if the customer had not overdrawn his account (or overdrawn it in excess of an agreed limit) in the previous 12 months. It also placed a limit on the number of Overdraft Excess Fees that it charged a customer in any month.
  116. Lloyds TSB did not levy a Guaranteed Paid Item Charge or any other charge that related specifically to the use of a card. Nor was there ever a charge that related directly to the Bank honouring a Relevant Instruction (although this might trigger an Overdraft Excess Fee either because it took the account into overdraft or over an overdraft limit or because it increased an unauthorised overdraft).
  117. The OFT submits that conditions 6.5 and 9.2 might be capable of being penal. Lloyds TSB accepts that these conditions imposed contractual prohibitions on its customers. This is clear from the terminology used in condition 9.2, and, while taken in isolation the effect of condition 6.5 might be less clear, reading the conditions as a whole I agree with Lloyds TSB’s concession. Lloyds TSB disputes, however, that any Relevant Charge was made upon breach.
  118. As I interpret conditions 6.5 and 9.2, they meant that the customer was in breach of his contract with the Bank only when his account became overdrawn without or in excess of an agreed overdraft. I do not accept that the customer was in breach of either condition or any provision of Lloyds TSB’s 2007 card conditions when he gave a Relevant Instruction that was not honoured. More specifically, I do not consider that a customer would have been in breach of condition 9.2 if he sought to use his card but the Bank did not allow him to do so because his account would have gone into an overdraft without or beyond an agreed facility. The customer would not in these circumstances “use [his] Card to create an overdraft [the Bank had] not agreed or to exceed an agreed overdraft limit” within the meaning of condition 9.2. Accordingly, Lloyds TSB’s Returned item fee was not payable upon a breach of either condition and could not have operated as a penalty.
  119. This leads to the question whether, if the customer contravened condition 6.5 by writing a guaranteed cheque that was honoured or condition 9.2 by use of his card and the account went into unauthorised overdraft because the Bank made the mandated

payment or allowed a withdrawal, any Overdraft Excess Fee payable upon the resulting overdraft became payable upon the breach so as potentially to engage the legal principles applicable to penalties. In support of his submission that no Relevant Charge is payable on a breach of Lloyds TSB's 2007 card conditions, Mr Bankim Thanki QC, who represents the Bank, submits that the same charge would be incurred if Lloyds TSB chose to pay a Relevant Instruction when no card had been used. That is indeed contemplated by the leaflets setting out the charges imposed by Lloyds TSB, and was not questioned by the OFT. If the contract between Lloyds TSB and its customers is assumed to incorporate a right for the Bank to levy charges as set out in the leaflets, then I would accept the submission that Relevant Charges were not imposed upon breach of the Lloyds TSB 2007 card conditions: the position would be like that discussed in paras 308 to 312 of the April judgment in relation to condition 12.1 of Barclays' Card conditions. However, because at the relevant time the contracts between Lloyds TSB and its customers were not incorporated in written form, I am not at present persuaded that I should make a declaration in general terms on the assumption that the contracts between the Bank and its current account customers provided that the Bank was entitled to levy all the charges set out in the Bank's leaflets. Moreover, before making a declaration in these circumstances I should wish to hear submissions about the decision of Mr Justice Morgan in The Office of Fair Trading v Foxtons Limited, [2008] EWHC 1662 (Ch), which was decided after the hearing before me. I shall therefore invite further submissions from the OFT and Lloyds TSB.

## RBSG

120. In June 2001 RBSG issued a version of its "Terms and Conditions for NatWest Personal Current Accounts" (the "NatWest June 2001 conditions"). The introductory words stated that they gave the customer "important information about your NatWest Account and card", and the first paragraph, against the side-note "Our Dealings with You", said that "The information on these pages (and the further instructions and conditions) are the terms of the contract between you and NatWest". They said against the side-note "Fees":

"Full details of our fees, and when they may be applied, are given in 'Personal current account fees – a straightforward guide'. You will get a copy of this in your new account opening pack. We will send further information whenever there are changes giving you reasonable notice of the changes. The main details are also printed on the back of all personal account bank statements."

121. Under the "Terms and Conditions for NatWest Servicecards, Cashcards & First Reserve Cashcards", there was a provision against the side-note "Using your Card" in these terms:

"You must only use your Card in accordance with these Conditions of Use and any operating instructions including the

User Guide which we or our agents give you at any time. Such instructions form part of the contract between you and the Bank ... You must not use your Card to go overdrawn on your Account unless we have previously agreed this with you. If you do go overdrawn without our agreement, you will be liable to pay interest for each day you are overdrawn on the total amount of the unauthorised borrowing together with our normal account charges. Full details of the interest and charges can be obtained from any branch of the Bank or from the reverse of your Account statement ...”

122. The relevant tariff leaflet provided for:

- i) an Unpaid Item Charge;
- ii) a Guaranteed Paid Item Charge, which was stated in these terms: “Card Misuse: If you use your NatWest Servicecard, Cashcard or cheque guarantee card when there is not enough money in your account”; and a fee of £25 per item was stated;
- iii) a Paid Item Charge of £25 for each day (up to a limit of £75 in a charging period); and
- iv) an Overdraft Excess Charge of £14 for each charging period.

Until about November 2001 the Bank gave similar information about these charges on the reverse of NatWest’s personal current account bank statements, but it then abandoned this practice.

123. RBSG accepts that the statement “You must not use your Card to go overdrawn on your Account unless we have previously agreed this with you” was a provision of the contract between the Bank and its customer, and that it stipulated something that the customer was not to do under its terms. However, RBSG submits that it did not mean that the customer was under a binding obligation not to use his card or that, if he did so, he was in breach of contract. The purpose of the prohibition, it is submitted, was only to make clear to the customer that he did not have the Bank’s authority to use his card “to go overdrawn” on his account without the prior agreement of the Bank and “to discourage him from doing so”.

124. As things stand, I am not persuaded by this submission, notwithstanding the similarities between this statement in the NatWest June 2001 conditions and condition 9.2.2 of the HSBC 2001 current account conditions. Indeed, I sent to the parties a draft of this judgment in which I rejected the submission. I have, however, received a note from those representing RBSG in which they indicate a wish to make further submissions in light of my conclusions about other Relevant Terms and in particular the HSBC 2001 current account conditions. Without precluding the OFT or, indeed, other parties from arguing that it would be wrong to consider further submissions, I consider on reflection that I should not finally determine the position

about the NatWest June 2001 conditions in this judgment, and that I should, at least, reserve the possibility of inviting further assistance from counsel about them in light of this judgment.

125. The Bank had generally similar provisions in its NatWest Personal Banking Terms and Conditions issued in October 2004 (the “NatWest October 2004 conditions”), and in its Royal Bank of Scotland Terms and Conditions for Personal Customers issued in June 2005 (the “RBS June 2005 conditions”). Both sets of conditions included provisions that, “You (and any additional cardholder) must not use the card if to do so would overdraw the account without our prior agreement, or would increase any borrowing on the account to more than we have agreed”. Similar arguments apply to these provisions as to the NatWest June 2001 conditions, and therefore I make no determination about them in this judgment.
126. In July 2003 RBSG issued a leaflet for the use of its NatWest customers called, “A guide to Personal Current Account fees” (the “NatWest July 2003 leaflet”), and the OFT submits that this provision, under the heading “Fees for overdrafts you have not arranged”, is capable of being penal:

“You must always have an agreed overdraft or Credit Zone Overdraft before you spend or withdraw any amounts that may cause your account to go overdrawn. If you exceed your arranged overdraft facility, or if you go overdrawn without prior arrangement you will be charged.”

(As I understand it, a Credit Zone Overdraft was simply an arranged facility to overdraw.) The document then referred to an Excess Overdraft Charge called a “£20 Unarranged Borrowing Fee”, an Unpaid Item Charge called an “Unpaid Fee”, a Guaranteed Paid Item Charge under the heading “Card Misuse”, and a Paid Item Charge under the heading “Paid Referral”.

127. The NatWest July 2003 leaflet was on its face a “Guide” for customers rather than a document setting out contractual terms and conditions. The OFT submits, however, that the sentence of the leaflet that I have set out is capable of being penal provided that it was of contractual effect.
128. I do not consider that it would be right to make a declaration about the effect of this statement without satisfactory information about the terms of the contract that is said to have incorporated it. The OFT told me that the terms and conditions that incorporated the NatWest July 2003 leaflet was a version of them that was issued by RBSG in February 2003. There is a version of the NatWest Current Account Terms and conditions in the papers before me that appears to have been produced or printed in February 2003 but that version states that the terms and conditions “apply from 7 October 2002”. I do not consider that the contractual position regarding the NatWest July 2003 leaflet is sufficiently clear to make any declaration about its effect and whether its provisions are capable of being penal.

129. As matters stand, I am not prepared to make a declaration about the NatWest July 2003 leaflet. If RBSG or the OFT so wish, I shall allow this part of the application too to be restored for further consideration.
130. Although some reference is made in the papers before me to RBSG's Graduate and Student Accounts, I did not hear specific oral submissions about them. Again I shall allow RBSG and the OFT to make separate submissions about them if either wishes to do so.

### Conclusions

131. As far as the terms in issue between the OFT and the Banks are concerned:
  - i) Barclays, Clydesdale and HSBC are entitled to declarations, and I invite submissions about their exact wording.
  - ii) I shall consider the position with regard to Abbey's May 2005 conditions in light of further submissions, but otherwise Abbey is entitled to a declaration.
  - iii) HBOS is entitled to a declaration except in respect of its Intelligent Finance accounts.
  - iv) I invite further submissions from Lloyds TSB and the OFT as to whether I should make any declaration in favour of Lloyds TSB and if so what its terms should be.
  - v) As things stand, I am not satisfied that I should make any declaration in favour of RBSG, but shall seek further assistance from counsel about its application.
132. I also invite further submissions about what declarations I should make about the terms that the OFT does not contend are or might be penal and about what declarations I should make to give effect to this judgment.