Supreme Court

New South Wales

Case Name:	Bellas v Powers
Medium Neutral Citation:	[2023] NSWSC 1198
Hearing Date(s):	27 July 2023
Decision Date:	10 October 2023
Jurisdiction:	Equity
Before:	Robb J
Decision:	See [95] – [100]
Catchwords:	CONTRACTS — penalties — where facility agreement provided for “Discounted Rate” where no event of default occurs or is subsisting and higher “Standard Rate” on event of default — whether imposition of “Standard Rate” unenforceable as a penalty CIVIL PROCEDURE — separate determination of questions
Legislation Cited:	Competition and Consumer Act 2010 (Cth), Sch 2 – Australian Consumer Law Contracts Review Act 1980 (NSW) Uniform Civil Procedure Rules 2005 (NSW), r 28.2
Cases Cited:	Aquamore Credit Equity Pty Ltd v Hung; First on First Development Pty Ltd v Aquamore Credit Equity Pty Ltd [2021] NSWSC 1681 Arab Bank Australia Ltd v Sayde Developments Pty Ltd (2016) 93 NSWLR 231; [2016] NSWCA 328 Australia Capital Financial Management Pty Ltd v Lindfield Developments Pty Ltd; Guan v Lindfield Developments Pty Ltd [2017] NSWCA 99; (2017) 18 BPR 36,683 Bay Bon Investments Pty Ltd v Selvarajah [2008] NSWSC 1251

	Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd [1915] AC 79 Guardian Mortgages Pty Ltd v Miller [2004] NSWSC 1236; (2004) 12 BPR 22,833 HomeSec Finance Express Pty Ltd v Richardson [2012] NSWSC 1375 Hung v Aquamore Credit Equity Pty Ltd [2022] NSWCA 272 Kellas-Sharpe v PSAL Ltd [2013] 2 Qd R 233; [2012] QCA 371 Robophone Facilities Ltd v Blank [1966] 1 WLR 1428 First Cash Flow Solutions Pty Ltd v Saad [2023] NSWSC 686 Yarra Capital Group Pty Ltd v Sklash Pty Ltd [2006] VSCA 109
Category:	Principal judgment
Parties:	Theo Bellas (First Plaintiff) Artos Espresso Pty Ltd (Second Plaintiff) Tommy Wayne Powers (First Defendant) Rosemary Ann Powers (Second Defendant) Peter Karbone (Third Defendant) Bosilka Stojcevska (Fourth Defendant) Berna Karadag (Fifth Defendant/Interested Party) Haluk Karadag (Sixth Defendant/Interested Party)
Representation:	Counsel: J E O'Sullivan (Plaintiffs) V Bedrossian SC (First and Second Defendants) J Rodgers (Fifth and Sixth Defendants/Interested Parties) Solicitors: Gells Lawyers (Plaintiffs) Independent Legal (First and Second Defendants) Di Lizio & Associates (Third and Fourth Defendants) Kardos Scanlan (Fifth and Sixth Defendants/Interested Parties)
File Number(s):	2022/00161334
Publication Restriction:	Nil

JUDGMENT

1 The plaintiffs in these proceedings are Theo Bellas and Artos Espresso Pty Ltd (Artos). The plaintiffs are parties to a Facility Agreement dated 2 September 2021 in which Artos is described as the "Borrower" and Mr Bellas as the "Guarantor".

2 The first defendant, Tommy Wayne Powers, is described in the Facility Agreement as the "Financier". Rosemary Ann Powers is also described as the "Financier" in the Facility Agreement. Those parties were the first and second defendants to the proceedings at the time the plaintiffs' summons was filed. The plaintiffs filed an amended summons on 6 July 2022, which deleted Ms Powers as a party. The reason why that happened is not known or material to the issues the subject of these reasons for judgment. I note that counsel at the hearing announced his appearance for the first and second defendants and that he referred to "the Powers" in his written submissions. The statement of the number of defendants treats Ms Powers as remaining as a defendant. Notwithstanding the confusion, I will also refer to the Powers. The Powers were described in the Facility Agreement as trustees for the Paecu No 1 Trust Super Fund (the Trust). The status of the Powers as trustees is also not material.

3 It will be convenient from time to time to refer to Mr Bellas as the Guarantor, Artos as the Borrower and the Powers as the Financier, because the reasons largely consist of a discussion of relevant terms of the Facility Agreement in which the parties are described using those terms.

4 The amended summons joined two additional defendants, being the third defendant, Peter Karbone, and the fourth defendant, Bosilka Stojcevska.

5 The hearing took place on 27 July 2023. The issues that were before the Court for determination were as set out in "Schedule 1 – Separate Questions" to order 2 made by Lindsay J on 31 March 2023 under rule 28.2 of the Uniform Civil Procedure Rules 2005 (NSW) (the separate questions order). I will explain the substance of the separate questions below. The record of proceedings for the separate questions order recorded that counsel appeared on that date for the Powers.

6 The record of proceedings also recorded that a solicitor appeared for the third and fourth defendants.

7 Additionally, the record of proceedings recorded that counsel appeared for Berna and Haluk Karadag, who were described as "Proposed Fifth and Sixth Defendants". When the separate questions were listed for hearing by the Registrar on 4 April 2023, the Registrar made an order that the plaintiffs and the third to sixth defendants were to file their written submissions by a specified date. That order suggests that the proposed fifth and sixth defendants had already been made parties, but I have not found an order to that effect on the Court's file. They are described as "interested parties" on JusticeLink.

Amended summons

8 The relief claimed by the plaintiffs in their amended summons included the following prayer 1:

> 1. A declaration that:
>
> a. Item 7 of the "Facility Overview";
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> b. the definition of "Standard Rate" in clause 1.1;
>
> c. clause 5.1;
>
> d. sub-clause 5.3(c);
>
> e. sub-clause 7.1(b) and (c);
>
> f. clause 7.2; and
>
> g. sub-clause 7.3(c)
>
> (together, "**the Penalty Clauses**") of the "Facility Agreement" executed on or about 31 August 2021 between the First and Second Defendants as trustees for the [Trust] as financier, the First Plaintiff as obligor/guarantor and the Second Plaintiff as obligor/borrower ("**Facility Agreement**") are void and unenforceable for being a penalty.

9 Prayers 2 and 3 of the amended summons claimed relief under ss 21, 237 and 243 of the *Australian Consumer Law* (being Schedule 2 to the Competition and Consumer Act 2010 (Cth)) for orders the effect of which would have been that what were described as the Penalty Clauses in prayer 1 were void and unenforceable.

10 In order to understand what has happened with the balance of the prayers for relief in the amended summons, it is necessary to consider Recital A of the Facility Agreement, which provides:

> A. The Borrower and the Guarantor have requested the Financier to provide the Facility to the Borrower for the purpose of assisting with the refinance of the Leichhardt Property and the purchase of the Five Dock Property.

11 The Security for the Borrower's obligations to the Financier under the Facility Agreement, as set out in Item 11 in the Facility Overview at the beginning of the agreement, included first registered real property mortgages granted by the Guarantor over properties owned by him that were called the Leichhardt Property and the Five Dock Property.

12 Prayers 4 to 7 of the amended summons sought declarations that the real property mortgages that were registered against the titles to the two properties did not secure any amount owing under the Facility Agreement, together with orders enforcing the Guarantor's rights of redemption in respect of those properties.

13 Prayer 8 sought an order that an account be taken of all monies received by the Financier on the sale of real estate owned by the Borrower.

Separate questions

14 Having set out definitions of the Facility Agreement and the Leichhardt and Five Dock Properties and Mortgages, Schedule 1 provided:

> 1. Does/did the Five Dock Mortgage operate as security against the Five Dock Property and in favour of the First and Second Defendants in respect of the obligations of the Second Plaintiff under the Facility Agreement?
>
> 2. Does/did the Leichhardt Mortgage operate as security against the Leichhardt Property and in favour of the First and Second Defendants in respect of the obligations of the Second Plaintiff under the Facility Agreement?
>
> 3. Does the imposition by the Facility Agreement of the Standard Rate (as defined in cl 1.1 of the Facility Agreement) operate as a penalty, such that the terms of the Facility Agreement that purport to impose that interest obligation are void and unenforceable?
>
> 4. If the answer to Question 3 above is "No", are the Plaintiffs entitled to the relief under the *Australian Consumer Law* as sought in prayers 2 and 3 of the Amended Summons? If so, what relief?
>
> 5. In light of the answers given to Questions 1 to 4 above, what amount, if anything, remains owing by the First Plaintiff, as guarantor, and the Second Plaintiff, as borrower, to the First and Second Defendants and the repayment of which remains secured against the proceeds of sale of the Leichhardt Property? If nothing remains owing and secured, have the First and Second Defendants been overpaid, such that they are required to reimburse funds to the Second Plaintiff and, if so, how much is required to be reimbursed?

6. Which party or parties should bear the costs of the determination of these separate questions and, if the answers to the separate questions conclude the involvement of the First and Second Defendants in these proceedings, who should bear the First and Second Defendants' costs of the proceedings and upon what basis of assessment?

The hearing

15 The plaintiffs abandoned the claims in prayers 2 and 3 of their amended summons at the hearing, on the basis that they could only succeed in achieving the outcome sought by the first three prayers if they were successful in their claim based upon the doctrine of penalties, which is the basis of prayer 1.

16 The Powers did not challenge the right of the plaintiffs to abandon these prayers, and accordingly separate question 4 is no longer required to be answered.

17 At the hearing, counsel for the plaintiffs also advised the Court that the plaintiffs no longer thought that it was necessary for them to pursue the relief in prayers 4 to 7 of the amended summons. As I understood counsel, that was because the plaintiffs accepted that, even if the registered mortgages were ineffective to secure any debts, Mr Powers was entitled to an equitable charge, and the properties had already been sold and the proceeds of sale either applied in reduction of the debt claimed by the Powers or secured so that they would be available to whichever party demonstrated the better claim to the proceeds.

18 If prayers 4 to 7 of the amended summons are effectively abandoned by the plaintiffs, separate questions 1 and 2 will no longer be required to be answered.

19 Counsel for Mr Powers resisted the Court taking the course advocated by the plaintiffs and not dealing with the claims in prayers 4 to 7 (and accordingly separate questions 1 and 2). As I understand it, that position was taken because of the possibility that the other defendants may have had a claim of proprietary interests in the properties or their proceeds of sale. Counsel wanted the Court to decide the issue of whether the registered mortgages were effective to secure amounts owing to the Powers under the Facility Agreement, to neutralise the possibility that the other defendants may revive the issue in the future.

20 Counsel for the plaintiffs responded by informing the Court that the plaintiffs formally withdrew prayers 4 to 7 inclusive of the amended summons.

21 The issue is complicated because the matter that was listed for hearing was the determination of the separate questions in these proceedings, but two other related proceedings were also listed for directions; being proceedings No 2021/257925 and proceedings No 2022/353496. The Karadags are the plaintiffs in the first of those proceedings, but the Powers are not parties to them. The Powers are the plaintiffs in the second of those proceedings and Mr Bellas is the defendant. I made the necessary directions in the two other proceedings and adjourned them.

22 As I understand it, the proceedings commenced by the Karadags have a relationship to the present proceedings, because if the plaintiffs fail (because they fail in their claim that relevant terms of the Facility Agreement are void and unenforceable because they constitute a penalty), there will be no fund available to satisfy any relief that the Karadags may succeed in obtaining in the proceedings commenced by them. I have not investigated the relationship between the proceedings commenced by the Powers and these proceedings, as that is not an issue relevant to the determination of the separate questions.

23 The only residual relevance of the two other proceedings being before the Court is that, as I understand it, all of the parties who could possibly have an interest in challenging the Powers' priority in respect of their mortgages or charges over the Leichhardt and Five Dock properties (or their proceeds of sale) happened to be represented in Court on the morning of 27 July 2023.

24 As I have noted above, on 4 April 2023, the Registrar ordered all parties to these proceedings who had an interest contrary to the interests of the Powers to file and serve their written submissions. Only the present plaintiffs did so.

25 I record that, at the beginning of the hearing on 27 July 2023, I invited all parties other than the plaintiffs and the Powers who wished to make any submissions on the separate questions to remain in court and they would be given the opportunity to make their submissions. The legal representative of the third defendant in the proceedings commenced by the Karadags excused

himself, and the legal representatives of the other parties remained in court but did not make any submissions.

26 I have set out this somewhat complicated background, because it is necessary for the Court to decide whether it should formally answer separate questions 1 and 2.

27 The position is that the Court has already formally noted that the plaintiffs have withdrawn prayers 4 to 7 inclusive of the amended summons. Consequently, the basis of separate questions 1 and 2 has also been withdrawn. The Powers have taken no formal step to reintroduce those issues into the proceedings. The plaintiffs and the Powers have provided written submissions in respect of separate questions 1 and 2, but counsel for the plaintiffs did not address those questions in oral submissions. As the proceedings came before the Court as separate questions, the Court has not been informed by any party in sufficient detail of the relationship between all of the proceedings and the answers to separate questions 1 and 2. Furthermore, the Court was informed that the parties interested in the separate questions had agreed that the issues would be determined upon the basis of an agreed bundle of documents (subject to limited further documentary exhibits). I have only had regard to the agreed evidence or further evidence tendered without objection. It would not be appropriate for the Court to act on its own investigation of the relationship between the various proceedings without giving the parties an opportunity to be heard on the issue.

28 In these circumstances, I am of the view that it will not be appropriate for the Court to formally answer separate questions 1 and 2. I record that all of the parties to the order made by the Registrar on 4 April 2023, and all the parties who were represented in Court on 27 July 2023, had full opportunity to contest the position adopted by the Powers in opposition to prayers 4 to 7 of the amended summons (as reflected in separate questions 1 and 2) but they did not do so.

29 I will now turn to address separate question 3 concerning whether relevant terms of the Facility Agreement constitute a penalty.

The Facility Agreement

30 As noted above, on 2 September 2021, Mr and Mrs Powers as trustees for the Trust (and called the Financier), entered into a Facility Agreement with Artos, as Borrower, and Mr Bellas, as Guarantor.

31 Clause 1.1 contained a definition of "Obligors" as meaning the Borrower and the Guarantor.

32 By clause 2.1(a), the Financier agreed to make available to the Borrower the Facility. "Facility" was defined in clause 1.1 as meaning "the finance facility up to the Facility Limit as detailed in this Facility Agreement". The "Facility Limit" was defined in the same clause as $3,000,000.00. Clause 2.1(b) recorded that the Financier proposed "to make available to the Borrower, the Facility in a fully drawn advance up to the Net Available Amount". The "Net Available Amount" was defined in clause 1.1 as meaning "the Facility Limit less Initial Costs". "Initial Costs" was defined in the same clause as meaning the costs set out in clause 17.1. That clause listed as Initial Costs an Approval Fee, Broker Fees, and Establishment Fee and Legal Fees, and provided that the total of the Initial Costs may be withheld from the first Drawdown.

33 Clause 6.1 obliged the Borrower to pay the Money Owing under or in connection with the Finance Documents on or prior to the Termination Date. "Money Owing" was defined in clause 1.1 as meaning the Principal Outstanding plus all other debts and monetary liabilities of the Obligors under or in connection with the Finance Documents and in any capacity. "Termination Date" was defined in clause 1.1 as meaning "the date 60 days after the Interest Commencement Date or such later date as agreed to by the Financier." The "Interest Commencement Date" was defined in the same clause as being the earlier date of a number of different events including "the Drawdown Date".

34 Thus, the purpose of the Facility Agreement was to make a short term loan for two months. It is nonetheless significant that the Termination Date may have been extended by agreement between the parties.

35 The "Purpose of Facility" was expressed in clause 2.2 to be that of assisting with the refinance of the Leichhardt Property and the purchase of the Five Dock Property.

36 Clause 5 provided for the calculation and payment of interest in the following terms:

> **5. Calculation and payment of interest**
>
> **5.1 Interest period**
>
> The Borrower shall pay to the Financier interest at the Standard Rate on the Termination Date provided that if no Event of Default has occurred or remains subsisting, then the Financier shall accept the payment of interest for the Term calculated at the Discounted Rate. Any difference between interest charged at the Standard Rate pursuant to clause 7.1 and the Interest Paid In Advance will be added to the Money Owing.
>
> **5.2 Calculation**
>
> Interest is calculated from the Interest Commencement Date to the date of full and final repayment of the Money Owing and:
>
> (a) accrues on a daily basis;
>
> (b) will be paid in accordance with clause 5.3.
>
> **5.3 Payment**
>
> (a) The Interest Paid in Advance must be paid on the Drawdown Date and will be retained by the Financier on account;
>
> (b) The Borrower authorises and instructs the Financier to pay from the amount available to be advanced under the Facility, any amount required to meet the Borrower's obligations pursuant to clauses 5.2 and 5.3.
>
> (c) Without derogating from the fact that the failure to pay interest will be an Event of Default, any interest which accrues on any part of the Facility that is not paid, either pursuant to clause 5.2(a) or otherwise will be capitalised monthly.
>
> (d) Any Interest Paid in Advance will not be refundable in the event that the Money Owing is repaid prior to the Termination Date, pursuant to clause 6.2.

37 The Financier was, under clause 5.1, required to accept interest at the Discounted Rate for the "Term" if the provision was satisfied. "Term" was defined in clause 1.1 as meaning "the period between the Interest Commencement Date and the Termination Date". That factor is significant for the purposes of the Powers' submissions, as will be seen below.

38 The "Standard Rate" was defined in clause 1.1 as meaning the rate shown at Item 6 (an error for Item 7). "Items" were defined as items in the Facility Overview, which was a table at the beginning of the Facility Agreement. The Standard Rate was specified as being 9.75% per 30 days. On a similar basis, the "Discounted Rate" was specified as being 1.75% per 30 days.

39 “Interest Paid In Advance” was defined in clause 1.1 as meaning “60 days interest calculated at the Discounted Rate on the Facility Limit, being the amount of $105,000.00, which is payable on the Drawdown Date and held on account by the Lender as part payment of the Interest amount to be calculated in accordance with clause 5”.

40 Thus, if the Facility Agreement was performed by the Borrower in accordance with its terms, interest of $105,000.00, being at the Discounted Rate, would be retained by the Financier on the Drawdown Date on account of the obligation of the Borrower to pay 60 days’ interest on the Termination Date. In the absence of the occurrence of an Event of Default, the Financier would be obliged to accept the interest held on account as having satisfied the Borrower’s interest obligation (notwithstanding its nominal calculation at the higher Standard Rate).

41 On the other hand, if an Event of Default occurred within the 60 day period, the Borrower would become liable on the Termination Date to pay 60 days’ Interest at the Standard Rate. The Borrower would therefore be required to pay, in addition to the Interest Paid In Advance that had been retained by the Financier, the difference between that amount and the Interest calculated at the Standard Rate. As that difference would then be added to the Money Owing as at the Termination Date, the difference would be capitalised.

42 As will be explained below, it is of significance that clause 5.1 clearly was triggered by the fact of no Event of Default having occurred or being subsisting. It was not triggered only if the Borrower was in default, meaning in breach of a contractual stipulation in the Facility Agreement; such as most likely a failure to make a payment required by the agreement. The situation in this case may therefore be contrasted with that in *Kellas-Sharpe v PSAL Ltd* [2013] 2 Qd R 233; [2012] QCA 371, where Gotterson JA (with whom McMurdo P agreed) held, at [52]-[53], that on the proper construction of the equivalent term to clause 5.1 in that case, the entitlement of the lender to interest at the default rate depended upon the borrower being in default, in the sense of being in breach of contract “the obvious example of which is a failure to pay monies in accordance with the terms of the Loan Agreement.”

43 Clause 7 dealt with Default Interest in the following terms:

7. Default Interest

7.1 Default Interest

(a) The Borrower must pay interest on the Money Owing for the period from (and including) the date on which an Event of Default occurs until (and including) the date on which the Event of Default is remedied to the satisfaction of the Financier.

(b) Interest payable under clause 7.1(a) accrues at the Standard Rate until the Event of Default is remedied to the satisfaction of the Financier (acting reasonably), at which point it will revert to the Discounted Rate.

(c) Any interest calculated at the Standard Rate and which has not been paid, may at the option of the Financier be capitalised monthly and added to the Money Owing.

7.2 Further Interest

If a liability under this agreement becomes merged in a judgment or order or exists after any winding up of the Borrower, the Borrower, as an independent obligation, must pay interest on the amount of that liability from the date the liability becomes payable both before and after the judgment, order or winding up until it is paid, at the Standard Rate.

7.3 Accrual of default interest

Interest payable under this clause 7:

(a) accrues daily; and

(b) is calculated on the basis of:

(i) the actual number of days on which interest has accrued; and

(ii) a 365 day year; and

(c) may be capitalised at monthly intervals to the extent that it has not been repaid.

7.4 Obligation to pay unaffected

Nothing in this clause affects the Borrower's obligation to pay each amount which is due and payable under this agreement on the date on which it falls due for payment.

44 An Event of Default could in principle occur within the 60 day period after the Interest Commencement Date or after the end of that period. Note that, as "Termination Date" was defined in terms that the period could be extended by the Financier, an Event of Default might occur after the end of the 60 day period when the Borrower was not already in default by having failed to repay on the Termination Date, provided that date had been extended by the Financier.

45 Clause 7.1(a) would appear to have the effect that, if an Event of Default occurred before the Termination Date, interest would be calculated at the

Standard Rate until the Event of Default was remedied to the satisfaction of the Financier, but only from the date of occurrence of the Event of Default. Interest would only be payable at the Discounted Rate for the period before the Event of Default. That result would appear to be inconsistent with the ordinary meaning of clause 5.1, which seems to have the result that, if an Event of Default occurred at some time during the Term or subsisted at the Termination Date, the Borrower would have to pay interest at the Standard Rate for the whole of the Term, even in respect of any period before the occurrence of the Event of Default.

46 The wording of clauses 5.1 and 7.1 therefore gives rise to a possible inconsistency. Meagher JA, sitting at first instance, recorded this apparent inconsistency between materially identical terms in the Facility Agreement that his Honour considered in *Aquamore Credit Equity Pty Ltd v Hung; First on First Development Pty Ltd v Aquamore Credit Equity Pty Ltd* [2021] NSWSC 1681 (*Aquamore*). In that case, which involved a Facility Agreement that was in material respects almost identical to the Facility Agreement in this case, one of the issues was whether the terms that governed the obligations of the Borrower on the occurrence of an Event of Default constituted a penalty. I will consider in more detail below his Honour's reasons for answering that question in the affirmative. His Honour's decision was upheld by the Court of Appeal in *Hung v Aquamore Credit Equity Pty Ltd* [2022] NSWCA 272, in response to grounds for appeal that did not challenge his Honour's judgment on the penalty issue.

47 As I understand his Honour's reasons, he resolved the apparent inconsistency by construing the relevant terms as having the effect that what is called the Standard Rate in the present Facility Agreement would only apply for periods when an Event of Default was subsisting. The subsistence of an Event of Default at the Termination Date would not have the effect (inconsistently with the express wording of clause 7.1) that retrospectively the Standard Rate would become payable for periods when no Event of Default subsisted. On that basis, Meagher JA held that one of the borrower's penalty arguments in that case failed. I respectfully agree with the construction of the materially identical provisions adopted by Meagher JA.

48 Returning to the effect of clause 7 of the Facility Agreement, if an Event of Default were to occur before the Termination Date, whether extended by the Financier or not, interest would become payable at the Standard Rate during the period between the occurrence and the remediation of the Event of Default to the satisfaction of the Financier. The interest so calculated would, if not paid by the Borrower, be capitalised monthly under clause 7.1(c) and added to the Money Owing. That state of affairs would continue until the repayment by the Borrower of all of the Money Owing.

49 "Events of Default" are stipulated in clause 11.1. Sixteen events are stated. Two of the events involve breaches of the Facility Agreement; namely (b) the failure by an Obligor to make payments when due under the Finance Documents; and (c) the failure by an Obligor to comply with any obligation or undertaking under a Finance Document, and not remedying the breach where remediable for 5 days after notice from the Financier, or the Obligor becoming aware of the failure to comply. Some Events of Default involve conduct on the part of the Obligors that might be considered wrongful, but would not be a breach of the Facility Agreement, such as (d) uncorrected misrepresentations. Other Events of Default might occur because of circumstances beyond the control of the Obligors, such as (e) an Obligor becoming involved in litigious or other proceedings that have a Material Adverse Effect, or (k) any property of an Obligor becoming subject to compulsory acquisition. Clause 11.1(n) provided that it would be an Event of Default if any event occurred or existed which, in the reasonable opinion of the Financier, had or was likely to have a Material Adverse Effect (the latter term being defined in clause 1.1).

50 By clause 11.2(a), the Financier was obliged to allow the Borrower 5 business days to remedy a Curable Default (which was defined in clause 1.1 as meaning "an Event of Default where the Financier is legally obliged to allow a period of time for the Event of Default to be remedied"). Clause 11.2(b) empowered the Financier, on the occurrence of an Event of Default, to cancel the Facility, declare that the Money Owing was immediately due and payable, and to enforce its rights under any Security. Clause 11.2(c) thereupon obliged the Borrower to immediately repay the Money Owing.

51 Clause 11.5 provided for a fee called the “Default Management Fee”. “Manager” was defined in clause 1.1 as being Credit Connect Pty Ltd (Credit Connect). The effect of clause 11.5 was that whilst an Event of Default subsisted the Manager would be the Financier’s agent in the provision of services to manage and rectify the Event of Default. The Borrower acknowledged that the Manager was entitled to be paid a Default Management Fee at the rate of $360.00 per hour (ex GST) for those services, which was to be paid by the Borrower. The Borrower acknowledged that the fee was a reasonable estimate of the likely management fees incurred by the Manager.

52 The effect of this provision was that the Financier was unlikely to be out of pocket, whenever an Event of Default occurred that was capable of being remedied, for the cost of the Manager’s services to remedy the Event of Default.

53 Clause 16.1 provided for an indemnity for the Financier in the following terms:

> **16. Indemnities**
>
> **16.1 Indemnity**
>
> (a) Each Obligor indemnifies the Financier against any loss the Financier incurs or is liable for in connection with:
>
> (i) the occurrence of any Default;
>
> (ii) the Financier exercising its powers consequent upon or arising out of the occurrence of any Default
>
> …
>
> (b) The indemnity in clause 16.1(a), includes the amount determined by the Financier as being incurred by reason of the liquidation or re-employment of deposits or other funds acquired or contracted for by the Financier to fund or maintain the Facility.

54 The effect of this indemnity was that, if any Event of Default occurred during the term of the Facility, the Obligors would be liable to indemnify the Financier, both against any loss incurred in connection with the Default, but also in connection with the Financier exercising its powers consequent upon the Default (including losses incurred by reason of the liquidation or re-employment of deposits or other funds).

55 One consequence of the relationship between clause 7.1 making the interest payable being calculated at the Standard Rate during the subsistence of any

Event of Default and the identification of the Events of Default in clause 11.1, was that the higher rate of interest would be payable by the Borrower during the period of any Event of Default, irrespective of the nature and amount of the loss that the Financier might suffer as a result of the event occurring, and even in cases where no loss might be suffered.

56 The effective interest rate for periods when the Borrower was not in default (in the sense that no Event of Default had occurred) would be the Discounted Rate of 1.75% per 30 days, which I calculate as about 21.30% per annum. This is a figure calculated on the basis that no interest would be capitalised because of the absence of any default

57 The Standard Rate of 9.75% per 30 days, or 118.6% per annum, was nominally more than 550% of the Discounted Rate. But clause 7.1(c) would have the effect that the Standard Interest of 9.75% per 30 days would, if not actually paid by the Borrower, be capitalised every month. Consequently, interest would accrue after the Event of Default over the first year at an effective rate of approximately 200% per annum , would accrue at an effective rate of greater than 600% per annum during the second year, and so on exponentially.

58 At the hearing, the Powers tendered a Financier's Certificate signed by a representative of Credit Connect pursuant to clause 20.5 of the Facility Agreement, which provided that a certificate "signed on behalf of the Financier in relation to any amount, calculation, interest rate or other matter under the Finance Documents is conclusive and binding on each Obligor, except in the case of manifest error": Exhibit D1. The Powers did not suggest that the purported conclusiveness of the certificate precluded the plaintiffs' penalty claim.

59 The certificate commenced with a debt of $3,000,000 owed on 1 September 2021, and allowed for a repayment on 22 March 2022 of $2,948,211.14 from the proceeds of sale of the Five Dock Property. On the basis of interest at the Standard Rate of 9.75% per 30 days being compounded monthly, the total amount of the debt claimed by the Powers as of 19 July 2023 was $7,803,142.59 (even after the 22 March 2022 repayment).

Legal principles

60 The legal principles that govern the circumstances in which a provision of a contract will be treated as a penalty, and so be void and unenforceable, are not without difficulty. They have been stated succinctly in a number of recent authorities, and I consider that it is not conducive to clarity for each individual trial judge to restate the principles in his or her own terms.

61 I consider that the principles were correctly stated by McDougall J (with the agreement of Gleeson JA) in *Arab Bank Australia Ltd v Sayde Developments Pty Ltd* (2016) 93 NSWLR 231; [2016] NSWCA 328 at [69]-[76], as follows (the reference to "*Dunlop*" being to the decision of the House of Lords in *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* [1915] AC 79):

> [69] The law relating to contractual penalties has been considered by the High Court of Australia in three recent cases:
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> (1) *Ringrow Pty Ltd v BP Australia Pty Ltd* (2005) 224 CLR 656; [2005] HCA 71
>
> (2) *Andrews v Australia and New Zealand Banking Group Ltd* (2012) 247 CLR 205; [2012] HCA 30, and
>
> (3) *Paciocco v Australia and New Zealand Banking Group Ltd* (2016) 90 ALJR 835; [2016] HCA 28.
>
> [70] Counsel's submissions ranged far beyond those cases. However, in my view, the disposition of this appeal need not go so far.
>
> [71] In *Ringrow*, the Court (Gleeson CJ, Gummow, Kirby, Hayne, Callinan and Heydon JJ) accepted at [12] that Lord Dunedin's speech in *Dunlop* set out "the principles governing the identification, proof and consequences of penalties in contractual stipulations", and that the decision in *Dunlop* "continues to express the law applicable in this country".
>
> [72] The relevant aspect of Lord Dunedin's speech (*Dunlop* at 86–87) reads as follows:
>
> > "2. The essence of a penalty is a payment of money stipulated as in terrorem of the offending party; the essence of liquidated damages is a genuine covenanted pre-estimate of damage …
> >
> > 3. The question whether a sum stipulated is penalty or liquidated damages is a question of construction to be decided upon the terms and inherent circumstances of each particular contract, judged of as at the time of the making of the contract, not as at the time of the breach …
> >
> > 4. To assist this task of construction various tests have been suggested, which if applicable to the case under consideration may prove helpful, or even conclusive. Such are:

(a) It will be held to be penalty if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach …

(b) It will be held to be a penalty if the breach consists only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid …

(c) There is a presumption (but no more) that it is penalty when 'a single lump sum is made payable by way of compensation, on the occurrence of one or more or all of several events, some of which may occasion serious and others but trifling damage'."

[73] In *Andrews*, the Court (French CJ, Gummow, Crennan, Kiefel and Bell JJ) referred to *Dunlop* at [69] and following. Nothing that their Honours there said cast any doubt on the position stated in *Ringrow*, to the effect that the principles identified by Lord Dunedin expressed the legal position in this country. That is perhaps not surprising, because the real point of the decision in *Andrews* was to identify that the equitable jurisdiction to relieve against penalties remained alive and well. It followed, in the Court's view, that the penalty doctrine was not only applicable in the case of breach of contract. Since the present case involves a stipulation operative on breach of contract, that aspect of the decision in *Andrews* is of no significance.

[74] I turn to the decision in *Paciocco*. In that case, the High Court held by majority (French CJ, Kiefel, Gageler and Keane JJ) that a late payment fee imposed by the respondent bank on its credit card customers was not a penalty. Their Honours gave separate reasons: Kiefel J (with whom French CJ agreed on this point), Gageler J and Keane J. The majority judgments paid close attention to the reasoning of Lord Dunedin in *Dunlop*. The following propositions emerge from the majority decision:

(1) Lord Dunedin's propositions were not "rules of law", but "distillations of principle": at [143] (Gageler J); compare at [32] (Kiefel J) and at [260] (Keane J).

(2) The essence of a penalty is that it is a collateral stipulation, the (or a predominant) purpose of which is to punish the borrower for breach, and thus to compel performance: at [29] (Kiefel J); at [127], [159], [166] (Gageler J); at [254], [259], [273] (Keane J).

(3) One way of testing whether the impugned stipulation is penal — intended to punish — is to inquire whether the sum that it stipulates to be payable on breach (as I have indicated, the equitable origins and continuing equitable operation of the principle have no present relevance) is to ask whether the stipulated sum is extravagant or out of all proportion to, or unconscionable in comparison with, the maximum amount of damage that might be anticipated to follow from the breach: at [29], [54] (Kiefel J); at [158]-[162] (Gageler J); at [221] (Keane J).

(4) "Damage" in this sense is not limited to damages recoverable upon breach of contract, but may extend to damage, or losses, caused by the impairment of other legitimate commercial interests that were intended to be protected by the stipulation: at [33], [42]-[47] (Kiefel J); at [145], [160][162] (Gageler J); at [216], [283] (Keane J).

(5) The analysis is to be made at the time, and taking into account the circumstances applicable, when the contract was made; not at the time of

> breach; the analysis is prospective, not retrospective (or as is said in some judgments, is *ex ante*, not *ex post*): at [62] (Kiefel J); at [169] (Gageler J).
>
> (6) Mere disproportion between the stipulated sum and the possible damage is not enough to indicate "penalty"; the disproportion must be such that it is unconscionable for the lender to rely on the stipulation: at [54] (Kiefel J), at [164] (Gageler J); at [221], [240], [279] (Keane J).
>
> [75] There are two remaining relevant points to be derived from the decision in *Paciocco*. The first is that the onus of proving that a contractual stipulation amounts to a penalty rests with the person asserting it. As Gageler J said in *Paciocco* at [167]:
>
> > "[167]…The customers bore the evidentiary and persuasive onus throughout that inquiry."
>
> [76] The second point relates to the "presumption" identified by Lord Dunedin in *Dunlop* at his point 4(c). That presumption is the subject of the first ground stated in the notice of contention. As Keane J said in *Paciocco* at [265], that presumption is "a weak one". Further, as Gageler J said at [168], the invariable nature of the penalty compared to the amount overdue or the length of delay, although it cannot be ignored, is "only weakly indicative of the character of the late payment fee as a punishment".

62 In relation to the "presumption" to which his Honour referred at [76] (which was a reference back to par 4(c) of Lord Dunedin's speech set out at [72]), McDougall J added at [100]:

> [100] I turn to the notice of contention. The first ground relies on Lord Dunedin's presumption (expressed in his Lordship's point 4(c) in *Dunlop*). That is the "weak" presumption to which Gageler and Keane JJ referred in *Paciocco*. If there were no other evidence, the presumption might be of some value. However, where there is evidence, the characterisation of the stipulation should be considered by reference to that evidence.

63 There is thus a "weak presumption" that it is a penalty when the one sum is made payable by way of compensation on the occurrence of one or more or all of several events, some of which may cause serious loss, but others trifling or no loss. That is a principle that is likely to apply in cases such as the present, where the collateral stipulation takes effect on the occurrence of any one of a substantial number of Events of Default, many of which by their nature are likely to have no or only trivial consequences. It may be that little evidence is required to rebut the presumption that the objective purpose of the collateral stipulation as at the date of the contract is to punish the borrower for permitting the Event of Default to occur, but if no evidence in rebuttal is proffered by the party seeking to enforce the collateral stipulation, the circumstances as a whole may justify the Court in finding that the collateral stipulation is a penalty. In this way, a burden of adducing evidence may fall upon the party seeking to enforce

the contract, even though the overall burden of establishing that the relevant provision is a penalty lies upon the party seeking to establish its invalidity.

64 In *Yarra Capital Group Pty Ltd v Sklash Pty Ltd* [2006] VSCA 109 (*Yarra Capital*), Chernov JA (with the agreement of Warren CJ) noted with apparent approval that in *Robophone Facilities Ltd v Blank* [1966] 1 WLR 1428 at 1447, Diplock LJ had said that, although the onus of showing that a stipulation is a penalty lies upon the party who is sued upon it, the terms of the clause may be sufficient to give rise to the inference that it is a penalty.

65 *Bay Bon Investments Pty Ltd v Selvarajah* [2008] NSWSC 1251 was a case in which the defendant called no evidence. White J (as his Honour then was) made the following observation concerning the evidentiary onus on the issue of whether a particular provision was a penalty:

> [51] Whilst I accept that the onus is on the defendant to show that the provision is a penalty, it appears to me that once some evidence is adduced which may be sufficient to satisfy that onus, there is an evidentiary onus on the plaintiff to explain the nature of its business, the rates at which it is able to lend, and how, when the contracts were entered into, it would have been anticipated that the moneys would be re-deployed on repayment of the loans. This information was entirely in the plaintiff's camp. Evidence is to be weighed according to the power of a party to produce it. Where facts are peculiar within the knowledge of one party, comparatively slight evidence may be sufficient to discharge the onus of proof lying on the opposite party (*Parker v Paton* (1941) 41 SR (NSW) 237 at 243; *Hampton Court Ltd v Crooks* (1957) 97 CLR 367 at 371–2; *Apollo Shower Screens Pty Ltd v Building and Construction Industry Long Service Payments Corporation* (1985) 1 NSWLR 561 at 564–5; *Krstic v Brindley* [2006] NSWSC 1414 at [26]).

66 As I have said previously in *First Cash Flow Solutions Pty Ltd v Saad* [2023] NSWSC 686

> [56] There may be cases, of which I think the present is one, where the plaintiff must tender the contract upon which it sues in order to make out its case, and the contract itself is then evidence that is capable of establishing a sufficient basis for the Court to find that a particular term is a penalty so as to cast an evidentiary burden on the plaintiff to call evidence to explain why it is not.

67 Consequently, although the burden of proving that a contractual provision is a penalty always remains on the party who makes that claim, which in the context of a loan agreement will generally be the borrower, the lender will need to tender the contract to prove the debt claimed, and the terms of the contract will constitute evidence that may cause an evidentiary onus to shift to the creditor. As the interests that the challenged provision is intended to protect will

be the interests of the creditor, and as the information relevant to the need for the creditor to be able to rely upon the provision to protect those interests may be solely within the creditor's province, the failure of the creditor to lead evidence beyond the contract may have the effect that the presumption operates, notwithstanding its weakness.

68 The Facility Agreement in this case does not impose upon the Borrower a contractual obligation to ensure that Events of Default do not occur. The collateral stipulation, in the form of the imposition of interest calculated at the Standard Rate, engages if an Event of Default occurs, whether or not that occurrence constituted a breach of contract by the Borrower. Such was the case with the Facility Agreement considered by Meagher JA in *Aquamore*, in respect of which his Honour said at [122]-[123]:

> [122] There is no express contractual promise on the part of the Borrower to perform the condition that there be no Events of Default, however two of those events (cll 11.1(b) and (c)) consist of breaches of monetary and non-monetary obligations arising under one or more of the Finance Documents. With few exceptions, the remaining "events" are not in terms breaches of any of those agreements. Some of the occurrences constituting or giving rise to an Event of Default may have been avoidable by the Borrower. Others will not necessarily involve any acts or omissions over which the Borrower has direct control. Some may be capable of being "remedied". Others may not.
>
> [123] In *Andrews* the Court held that the primary stipulation to which the penalty doctrine applies may be the occurrence or non-occurrence of an event which is neither a breach of contract nor an event which it is the responsibility or obligation of the party subjected to the penalty to avoid (at [12], [45], [46], [67]. See also *Paciocco v Australia & New Zealand Banking Group Ltd* (2016) 258 CLR 525; [2016] HCA 28 at [118] , [119] (per Gageler J), [253] (per Keane J)). Accordingly the penalty doctrine applies to cl 7.1 notwithstanding that there may not be any express contractual promise by the Borrower to perform the condition that there be no Event of Default. That is because "a penalty conditioned on failure of a condition is [treated as] in substance equivalent to a promise that the condition will be satisfied" (per Brereton J in *Integral Home Loans Pty Ltd v Interstar Wholesale Finance Pty Ltd* (2007) 2 BFRA 23 at 53–54; [2007] NSWSC 592 , approved in *Andrews* at [67]).

69 In *Australia Capital Financial Management Pty Ltd v Lindfield Developments Pty Ltd; Guan v Lindfield Developments Pty Ltd* [2017] NSWCA 99; (2017) 18 BPR 36,683 (*Guan v Lindfield Developments Pty Ltd*), Ward JA (as her Honour then was) explained the different approaches adopted by the High Court to the test as to when a collateral stipulation is a penalty (with the agreement of McColl and Gleeson JJA) at [367], in the following terms:

> [367] The different approaches of the High Court to this question in *Paciocco (HCA)* may be summarised as follows. Kiefel J (as her Honour then was), with whom French CJ agreed (at [2]), identified (at [29]) the test as being "whether a provision for the payment of a sum of money on default is out of all proportion to the interests of the party which it is the purpose of the provision to protect" and noted that this interest "may be of a business or financial nature". Gageler J framed the enquiry (at [166]) in terms of whether the impugned stipulation "is properly characterised as having no purpose other than to punish", stating that this compelled "a more tailored" enquiry than the legitimate interest approach adopted in *Cavendish*. His Honour expressly noted (at [166]) that this was not to say that the differently framed enquiries "might not lead to the same result". Keane J stated (at [270]) that "the question to be addressed in order to distinguish a penalty from a provision protective of a legitimate interest" was "whether the sum or remedy stipulated as a consequence of a breach of contract is exorbitant or unconscionable when regard is had to the innocent party's interest in the performance of the contract". Nettle J, though in dissent as to the application of the relevant principles, took a broadly similar approach to that of Keane J. His Honour said (at [319]) that "the *Andrews* and *Cavendish* formulations accord with *Dunlop*" and viewed (at [322]) the matter as turning on whether the case was a straightforward case in which the *Dunlop* tests would be perfectly adequate to resolve the issues on appeal, or whether the case "should be seen as one of the more complex types of cases referred to in *Cavendish* which necessitate considerations beyond a comparison of the agreed sum and the amount of recoverable damages". His Honour concluded (at [334]) that there was "no reason why the matter should not be determined in accordance with the *Dunlop* tests" and proceeded on that basis.

70 Her Honour then, at [368], explained the approach that the Court should take to the issue in determining whether a collateral provision is a penalty, as follows:

> [368] With that in mind, it is necessary, first, to identify the interests which are sought to be protected by the impugned stipulation; and, second, to ask whether the impugned stipulation was a stipulation collateral or accessory to another stipulation (the primary stipulation) which imposed an additional detriment upon SXG to the benefit of Linfield in the sense that (consistently with Andrews) it was in the nature of a security for and in terrorem of the satisfaction of the primary stipulation in a manner that (consistently with *Paciocco (HCA)* and *Cavendish*) was out of all proportion to the interests of Linfield intended to be protected by the primary stipulation.

Is the imposition of the Standard Rate a penalty in this case?

71 I find that the terms of the Facility Agreement which imposed the Standard Rate on the Borrower in this case are a penalty, by parity of reasoning with the approach adopted by Meagher JA in *Aquamore*, in respect of which I consider that the material terms of the two Facility Agreements have the same effect, and the general circumstances of the two cases warrant the same conclusions being reached in each. I have not followed his Honour's decision in the sense that I have treated it as a precedent; rather, I respectfully consider that his

Honour's reasons were correct in the determination of the case before him, and that those reasons apply with equal validity to the case that I am required to decide.

72 The only real difference between the terms of the Facility Agreement in the two cases and the other material circumstances is that in *Aquamore* the lower rate of interest was 2.5% per month and the higher rate 5% per month, each compounding monthly, while in the present case the respective rates are 1.75% per 30 days and 9.75% per 30 days, also compounding monthly. Consequently, the effect of the disparity between the interest rate applicable in the absence of the occurrence of an Event of Default and that which applies upon such an occurrence, in determining what I might call the exorbitance of the difference, is magnified considerably.

73 Starting with Ward JA's proposition that the Court should first identify the interests which are sought to be protected by the impugned provision, the only interests suggested by the Powers in the present case is their interests as lenders to earn the greatest amount of interest on their loan funds that was sustainable in the market in which they operated, which was the market for relatively high risk short-term loans on the security of a mortgage over real property. The same was the case in *Aquamore*. This is not a case, such as was considered by Ward JA in *Guan v Lindfield Developments Pty Ltd*, where the party seeking to enforce the collateral stipulation had a commercial interest in the opportunity to develop land and share in the profits of a development, in circumstances where it had already invested considerable funds and effort.

74 There was no objective evidence in this case of the interest rates obtainable by creditors in the market for short-term loans secured by a mortgage over real property. It is a reasonable inference that the personal covenants of Artos, as the Borrower, and Mr Bellas, as the Guarantor, to repay the Money Owing were risky, but the fact that the Advance was secured by a first registered mortgage over the two properties would have significantly diminished the ultimate risk. I am prepared to infer that the Discounted Rate, being a rate agreed between the parties at arm's length, was consistent with there being a market for the provision of bridging finance for short periods at rates up to that

amount. In *Aquamore*, Meagher JA made that finding in respect of the greater amount of 30% per annum.

75 The "collateral stipulation" in the Facility Agreement that is challenged as being a penalty is clause 7.1, which imposes the Standard Rate of interest during periods of the subsistence of an Event of Default, and the "primary stipulation" upon the failure of which clause 7.1 operates is that no Event of Default should occur during the period in which there is Money Owing: cf *Aquamore* at [121]. In this case, I adopt the same reasoning as did Meagher JA at [122]-[123], which is extracted above at [68].

76 The effect of the subsistence of any Event of Default on the parties to the Facility Agreement must be measured having regard to the fact that clause 11.5 and clause 16.1(a) respectively obliged the Obligors to pay, and entitled the Financier to receive, the fee charged by the Manager in rectifying the Event of Default, and any loss the Financier incurred in connection with the occurrence of the Event of Default. To this relatively extreme extent, the Financier was entitled to be compensated for the consequences of the Event of Default, entirely separately from its entitlement to receive, as additional interest, the difference between the Discounted Rate and the Standard Rate, compounded monthly. That difference could in the circumstances only be justified if the evidence established that, if the Monies Owing had been repaid to the Financier when the Event of Default occurred, the Financier could have loaned that money to a different borrower in the market at an interest rate equivalent to the Standard Rate, capitalised monthly. The evidence does not support such a finding, and, given the relatively extreme disparity between the two interest rates in this case, the proposition that short-term borrowers were available who would borrow at the equivalent rate of the Standard Rate capitalised monthly must be rejected.

77 As Meagher JA reasoned in *Aquamore* at [137], the terms of the Facility Agreement that have been considered above placed the Obligors in substantially the same position they would be in if the Borrower had given a promise to the Financier that there would be no Event of Default during the term of the borrowing. Clause 7.1 imposed the Standard Rate of interest,

capitalised monthly, on the Borrower during the subsistence of any Event of Default, whether serious or otherwise, and irrespective of the fact that the Financier was entitled to be compensated for its actual loss under other terms of the Facility Agreement.

78 The evidence does not support a finding that the occurrence of any particular Event of Default, or even any Event of Default at all, would sufficiently increase the credit risk profiles of the Obligors to justify an increase in the applicable interest rate from the Discounted Rate to the Standard Rate.

79 I conclude, as did Meagher JA in *Aquamore* at [143], that the effect and purpose of clause 7.1 "was to discourage any action or inaction on the part of the Borrower that might result in an Event of Default and did so by the imposition of a sufficiently exorbitant interest rate to have that consequence." While the doubling of the interest rate was considered to be exorbitant in that case, I find that, more so in this case, the increase in the interest rate by a factor of over 4 was exorbitant.

80 I will now turn to a consideration of the submissions made by the Powers as to why the reasoning adopted by Meagher JA in *Aquamore* should not be accepted as justifying the same result in the present case.

81 The Powers submitted (at par 24 of their written submissions) that "the penalty doctrine simply has no application to this Facility Agreement especially insofar as interest obligations have accrued after the expiry of the Term. To the extent that a higher and lower rate were available alternatives *during* the Term, the primary obligation under the Facility Agreement was payment of interest at the Standard Rate, thus excluding the application of the penalty doctrine" (emphasis in original). This conclusion was said to follow from the proposition that the real "primary obligation" imposed upon the Borrower in respect of the payment of interest was the obligation to pay the Standard Rate.

82 I respond by noting that the terms of the Facility Agreement considered in *Aquamore* were materially the same as the Facility Agreement in the present case, including, in respect of clause 5.2 in that case (being the equivalent of clause 5.1 in the present case), providing that "the Financier shall accept the payment of interest *for the Term*…" Insofar as the Powers' submission is based

upon clause 5.1 providing a special interest rate regime for the Term, the fact is that the relevant provisions were the same in both cases. Thus, the Powers do not in reality seek to distinguish *Aquamore*, they seek to persuade this Court that the reasoning applied by Meagher JA was wrong.

83 I do not accept this submission. Lord Dunedin's proposition 3 in *Dunlop* requires the Court to decide whether the impugned provision is a penalty "upon the terms and inherent circumstances of each particular contract, judged of as at the time of the making of the contract, not as at the time of the breach…" Looking forward in time from the date of the Facility Agreement, the Term contemplated was 60 days, but the Termination Date could be extended by the Financier (as happened in *Aquamore*). Although clause 5.1 contemplated that the Financier would accept interest calculated at the Discounted Rate in the absence of a subsisting Event of Default, notwithstanding the nominal obligation to pay interest at the Standard Rate on the Termination Date, for the reasons given above, clause 7.1 had the effect that interest would only be payable at the Standard Rate for periods during which an Event of Default subsisted. An Event of Default could occur within the Term, whatever that period might be. The fact is that the contractual regime that would have the effect that the Borrower only had to pay interest at the Discounted Rate would be terminated on the occurrence of any Event of Default within the Term, leading to the obligation on the Borrower to pay the Standard Rate. It is not true to say, as do the Powers, that there is really only one rate of interest, because once the Termination Date has been reached, the Facility Agreement can only continue if there has been a default in payment of the Monies Owing. That in those circumstances only the Standard Rate will be payable does not mean that there is only one rate of interest under the Facility Agreement.

84 The Powers based a submission on the fact that, in *Aquamore*, clause 5.2 of the Facility Agreement required the Financier to accept the Lower Rate "if no Event of Default has occurred *and* is subsisting", while clause 5.1 of the Facility Agreement in the present case only has the same result "if no Event of Default has occurred *or* remains subsisting". In the former case, it seems clear that the Borrower would only lose the right to require the Financier to accept interest for the period of the Term calculated at the Lower Rate, if any Event of Default that

had occurred had continued to subsist up to the Termination Date. The mere occurrence of the Event of Default would not be sufficient to cause the Borrower to lose this advantage. The reason for the use of the word "or" in clause 5.1 of the Facility Agreement is unclear. If "or" is given its literal meaning, the advantage would be lost if an Event of Default had occurred during the Term, even if it had been remedied by the Termination Date. If that were intended, the expression "or remains subsisting" would add nothing to the effect of the provision. I am inclined to think that the better construction is to read "or" as if it meant "and". Whether or not that is correct, in my view, the difference in wording between the two provisions could only change the trigger for the imposition of the interest obligation at the Standard Rate. Clause 5.1 of the Facility Agreement in this case would be more onerous, because interest at the Standard Rate would be payable even if the Event of Default had been remedied by the Termination Date. I doubt the relevance of the difference in wording to the determination of whether clause 7.1 is a penalty. The Powers' submissions do not explain why the difference matters, and I conclude that the difference does not in any material way.

85 The Powers submitted that no submission was made to Meagher JA that pointed out that the loan documentation in *Aquamore* did not provide for any lower rate of interest to apply during the post-Term period of time. That may be true, but it is irrelevant, as the submission depends upon the validity of the submission, which I have rejected, that the Court should treat the Standard Rate as the primary obligation of the Borrower.

86 Next, the Powers submitted that the defendants had provided no evidentiary basis for a submission that interest at 9.75% per 30 days was extravagant, having regard to the increase in the credit risk of the Obligors following the occurrence of any Event of Default. This submission ignores the effect of Lord Dunedin's presumption that has been considered above. It also ignores the fact that the interest payable is compounded monthly.

87 Finally, the Powers submitted that, given the short term nature of the Facility, the submissions made by the plaintiffs based upon the annuitisation of the

Standard Rate unfairly exaggerated the true burden of the Standard Rate provision at the time that the Facility Agreement was entered into.

88 The Powers relied upon *Yarra Capital Group* at [15]. The facts of that case were somewhat unusual, as were the procedural circumstances. Both the borrower and lender were engaged in moneylending businesses that involved making short-term loans, in circumstances of significant risk and at unusually high rates of interest. One party made a number of separate loans to the other repayable in two months. The first party charged a fee that would be the only consideration received if the borrower repaid the loan at the end of the two months. The agreements provided for the payment of a fixed amount for each day that the loan or any part of it was outstanding. In respect of one loan of $100,000, the fixed fee was $20,000, and the amount payable each day was $328.50. The borrower did not repay some of the loans on the agreed dates, but did make substantial repayments. The creditor commenced proceedings to recover the unpaid amounts, and obtained an order for summary judgment from the Master. A judge declined to reverse the Master's decision, and the borrower appealed to the Court of Appeal.

89 The Court of Appeal dismissed the appeal. Chernov JA said (with the agreement of Warren CJ):

> [15] In my view, however, this argument is misconceived in as much as it essentially disregards the relevant terms of the contract and its intended operation at the time of its making, which include the following. First, each of the six loans was made for a very short term, as is apparent from Sch B, and cl 10 of the deeds that makes time the essence of the contract. It follows from this that, at the time of the making of the loans, the parties must have contemplated that they would be repaid in full within a relatively short time. Hence, the notion that the default amount can operate at a rate of interest that is hundreds of per cent, as was argued by the appellants, is an unrealistic reflection of what the parties relevantly contemplated at the time of the agreement. I also consider that, given the short term nature of the loans, the annualisation of the default amount expressed as a percentage of a loan that was to last only a few months, unfairly exaggerates the true burden of the default provision. The second relevant circumstance to bear in mind in considering whether the default amount is a penalty is that the loans were essentially unsecured. Hence, one would expect that the amount charged for the loans would be substantial. Next, the extent of the loss that was likely to be suffered by the respondent if the appellants breached their obligations under the deeds can be gleaned from the amount of the fee that it charged in respect of the loans as it appears in Sch B. This shows that, absent default by the borrower, the respondent's expected earnings averaged out, broadly, at about $175 per day and there is nothing in the material that suggests that this did not

> reflect, in general terms, the minimum loss that the respondent was likely to suffer by reason of the appellants' breach of contract.

90 The argument that his Honour described as misconceived was to the effect that, if the agreed daily payments were annualised, in the sense of determining the equivalent annual interest rate, that rate was so high as to justify a finding that it was not a genuine pre-estimate of damage, and that it was "apparent that the agreed sum is so extravagant, when compared with the greatest loss the respondent was likely to suffer by reason of the appellants' default, that it plainly amounts to a penalty": see [14].

91 There are, in my view, material differences between the circumstances of that case and the present, and also with those of *Aquamore*. The daily payment only fell due upon a failure to repay the loan. The obligation did not arise on the occurrence of any one of multiple events of default, many of which may have been beyond the control of the debtor, and which may not have caused any loss to the lender. The loans were unsecured, save for personal guarantees. Both parties were experienced in the business of short-term moneylending. The loans were apparently made to provide short-term capital for the borrower's moneylending business, and there was a real expectation between the parties that the loans would be repaid within a couple of months. The majority of the Court of Appeal found that the daily rate was a genuine agreed amount of compensation for delays in repayment, in the context where it would have been difficult for the lender to prove actual probable loss by evidence.

92 Ashley JA, in dissent, would have set aside the order for summary judgment only on the basis of permitting the borrower to litigate the penalty issue. A persuasive point made by his Honour was that, as the daily payment was required irrespective of how much of the debt had been repaid, there may be force in the argument that the annualised notional rate of interest might be so high as to justify a finding by the Court that the impugned term was extravagant and unconscionable in the circumstances.

93 I am not persuaded that the conclusions reached by the majority in the circumstances of that case justify the Court in this case in applying a different line of reasoning than did Meagher JA in *Aquamore*.

94 Finally, the Powers relied upon two further cases in support of the proposition that there have been multiple examples where highly experienced judicial officers have accepted and left undisturbed interest rates in the vicinity of, or even higher than, those applicable under the Facility Agreement. In one case, *HomeSec Finance Express Pty Ltd v Richardson* [2012] NSWSC 1375, Button J did not find that a rate of interest of 12% per month was either unjust or unconscionable. In *Guardian Mortgages Pty Ltd v Miller* [2004] NSWSC 1236; (2004) 12 BPR 22,833, Wood CJ at CL did not find that a rate of interest of 14.5% per month was either unjust or unconscionable. That may be true, but the issue in each case was not whether a contractual provision was a penalty. In each case, the issue was whether the interest term was unjust or unconscionable under the *Contracts Review Act 1980* (NSW), or other statutory grounds for reviewing conduct found to be unconscionable. In the former case, Button J noted that the contract in question permitted the lender to capitalise unpaid interest at the high rate specified in the contract, but that the lender had not sued the borrower on the basis that unpaid interest had been capitalised. Though his Honour accepted that the amount claimed was not unconscionable, he found that a claim on the basis of capitalised interest would have been unconscionable. The issues the subject of these cases were far removed from the present, and the judgments do not persuade me that clause 7.1 of the Facility Agreement should not be found to be a penalty in this case.

95 Accordingly, I find that Question 3 of the separate questions should be answered in the affirmative.

96 Question 5 of the separate questions requires the Court to determine the amount of the debt owed by the plaintiffs to the Powers on the basis that the terms of the Facility Agreement that require the Obligors to pay the Financier interest calculated at the Standard Rate are void and unenforceable.

97 At par 46 of their submissions, the plaintiffs set out a table in which they purport to calculate the amount of the interest that they were liable to pay to the Powers up to 27 July 2023 as being $397,039.86. I am not sure whether there is any contest about this amount, given the Court's ruling on the penalty issue.

I will invite the parties to confer on the issue and submit to my Associate short minutes of order to give effect to these reasons. The draft short minutes of order should include any case management orders that may be appropriate for the future conduct of these proceedings.

98 As to question 6, concerning the costs of the determination of the separate questions, the parties agree that the Court should give them an opportunity to provide submissions, in the light of the reasons for judgment. That will be an appropriate course, given that the plaintiffs abandoned at the hearing the issues that supported a number of the separate questions.

99 In the circumstances, the parties should provide written submissions on the costs issue to my Associate at the same time as they provide the short minutes of order.

100 It will be convenient if the parties could do so within 14 days of the publication of these reasons.

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