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SUPREME COURT OF VICTORIA

COURT OF APPEAL

S APCI 2019 0085

JAMS 2 PTY LTD (ACN 600 173 117) (and others according to the attached schedule) — Applicants

v

JEFFREY WILLIAM STUBBINGS — Respondent

JUDGES:	BEACH, KYROU and HARGRAVE JJA
WHERE HELD:	MELBOURNE
DATE OF HEARING:	8 May 2020
DATE OF JUDGMENT:	5 August 2020
MEDIUM NEUTRAL CITATION:	[2020] VSCA 200
JUDGMENT APPEALED FROM:	*Jams 2 Pty Ltd v Stubbings (No 3)* [2019] VSC 150 (Robson J); *Jams 2 Pty Ltd v Stubbings (No 4)* [2019] VSC 480 (Robson J)

EQUITY – Unconscionable conduct – Asset-based lending – Wilful blindness – Lending organised by firm of solicitors – Lending secured on borrower's only significant assets – No evidence of ability to repay sought or received – Whether asset-based lending unconscionable – Consideration of unconscionability requires close examination of all the circumstances – Whether lenders put on inquiry – Lenders entitled to rely on certificates of independent legal and financial advice – *Australian Securities and Investments Commission v Kobelt* (2019) 368 ALR 1; (2019) 93 ALJR 743; [2019] HCA 18 considered; *Elkofairi v Permanent Trustee Co Ltd* [2002] NSWCA 413 considered and distinguished; *Tonto Home Loans Australia Pty Ltd v Tavares* [2011] NSWCA 389 considered – Application for leave to appeal granted – Appeal allowed.

APPEARANCES:	Counsel	Solicitors
For the Applicants	Mr D Williams QC with Mr J Mattin	Christopher William Legal
For the Respondent	Mr A Dinelli with Mr A Christopherson	Garlan & Hawthorn Brahe Lawyers

COURT OF APPEAL
459 Lonsdale Street, Melbourne, VIC 3000

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BEACH JA
KYROU JA
HARGRAVE JA:

1 Asset-based lending involves lending on the value of the assets securing the loan, without any consideration of the borrower's ability to repay the loan from their own income or other assets. No credit-risk analysis other than the calculation of the loan amount to security value ratio is undertaken by the lender. Thus, the lender makes the loan 'without regard to the ability of the borrower to repay by instalments under the contract, in the knowledge that adequate security is available in the event of default'.[1]

2 There are numerous cases which have considered whether, in the circumstances of the particular case, asset-based lending constitutes unconscionable conduct in equity or under various statutory provisions which prohibit such conduct. The prevailing view is that the existence of asset-based lending, while a relevant factor in deciding whether a particular loan resulted from unconscionable conduct, is not determinative — because 'all the circumstances' of each case must be considered.[2] For example, there may be irregularities with the loan application which put the lender on notice that further inquiries should be made.[3]

3 This case concerns asset-based lending by the applicants, three clients of a firm of solicitors, to a company owned and controlled by the respondent guarantor, Jeffrey Stubbings. The true purpose of the loan was to enable Stubbings to purchase, in his own name, a property as a home. The loan was secured by a first mortgage over the property, with the three clients being co-tenants of the mortgage in the proportions

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1 *Perpetual Trustees Company v Khoshaba* [2006] NSWCA 41, [128] (Basten JA); *Kowalczuk v Accom Finance Pty Ltd* (2008) 77 NSWLR 205, 227 [96] (Campbell JA) ('*Kowalczuk*').

2 For example, *Kowalczuk* (2008) 77 NSLWR 205, 227–8 [96]–[99]; *Tonto Home Loans Australia Pty Ltd v Tavares* [2011] NSWCA 389, [3], [291]-[293]; *Violet Home Loans Pty Ltd v Schmidt* (2013) 44 VR 202, 219–20 [59]; *Perpetual Trustees Australia Ltd v Schmidt and Violet Home Loans Pty Ltd* [2010] VSC 67, [200], [207] (J Forrest J).

3 Ibid; *Elkofairi v Permanent Trustee Co Ltd* [2002] NSWCA 413, [56] ('*Elkofairi*').

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in which they provided the loan moneys. For convenience, we will sometimes refer to the applicants as 'the first mortgagees'.

4 Interest under the loan was payable monthly in advance. The first month's interest was paid from the loan proceeds, and Stubbings managed to pay the second interest payment. No further payments were made.

5 Thus, within a few months of the loan being settled, the company defaulted in paying interest. The first mortgagees commenced proceedings against Stubbings seeking possession of the property. By his defence and counterclaim, Stubbings alleged (among other things) that the loan, his guarantee and the first mortgage were procured by the unconscionable conduct of the first mortgagees. Stubbings also joined a finance broker, a solicitor and an accountant as third parties, on the basis that they had misled him or breached duties of care in connection with the transaction. The defence and counterclaim was successful at trial,[4] and the trial judge set aside the first mortgage on certain terms. The first mortgagees now seek leave to appeal.

6 As appears below, another client of the solicitors also lent money to the company on second mortgage security over the property. The second mortgagee was not a party to the proceeding, although its position was relevant at trial — both as an aspect of the overall circumstances in which the loan was made by the first mortgagees and with respect to the formulation of the final orders made by the trial judge.

Relevant facts

7 On 30 June 2015, Stubbings owned two houses in Narre Warren, each of which was mortgaged to the Commonwealth Bank. The combined value of the houses was $770,000 and Stubbings had equity of about $530,000. His mortgage payments were

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4 *Jams 2 Pty Ltd v Stubbings (No 3)* [2019] VSC 150 ('Reasons').

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low, only $260–$280 per week. Both of the houses were occupied by members of his family — one of them Stubbings's son. Stubbings did not live in either house. Instead, he lived in rental premises in Boneo, where he worked repairing boats for the owner of that property. However, following a falling out with the owner, Stubbings needed to move. Stubbings did not want to live at one of his Narre Warren properties, because he preferred living on the Mornington Peninsula. In these circumstances, he thought that he could purchase a small property on the Mornington Peninsula using his equity in the two Narre Warren houses as additional security, as he did not have any money to contribute to a deposit.[5]

8 At the time, Stubbings was unemployed and had no regular income. He had occasional income from some work as a handyman changing tap washers, mowing lawns and the like. He had not filed tax returns for some years. He was substantially in arrears with his obligations to pay rates in respect of the two Narre Warren properties, and had entered into an arrangement to pay the outstanding rates over time. Although he may have had some rental income from the two Narre Warren properties, the evidence did not disclose whether that was so or whether any rental income exceeded his mortgage payments.

9 In these circumstances, Stubbings was introduced to Theo Kassinidis by a friend. Mr Kassinidis appears to have been some kind of finance intermediary. Stubbings told Kassinidis that he wanted to buy a property on the Mornington Peninsula, 'of around about $250,000'. Kassinidis prepared a home loan application to the ANZ Bank on behalf of Stubbings. After a few days, Kassinidis informed Stubbings that the application had been declined because Stubbings had no financial records, such as tax returns or financial statements.[6] Kassinidis then said to Stubbings: 'Look, I'll put you onto someone else and they will be able to help you out'.[7] He told Stubbings to expect a call from 'Johnny Tee', a reference to Trayan Tzontzourks — whose

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5 Ibid [8], [105]–[106].

6 Ibid [108].

7 Ibid [109].

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surname is commonly shortened to 'Zourkas'.[8]

10 Stubbings then met Zourkas and spoke with him on a number of occasions. In the first meeting, Stubbings told Zourkas that he believed he had equity of about $400,000 in the two Narre Warren properties and that he 'wanted to buy a little house' to live in. Zourkas responded in terms that 'there would not be a problem going bigger and getting something with land'.[9] On the basis of this first conversation with Zourkas, Stubbings went looking for a house to purchase.[10]

11 Stubbings found a property to suit his purposes — of about five acres with two houses on it — located in Truemans Road, Fingal. Following two further meetings with Zourkas, Stubbings agreed to purchase the Fingal property. At the second meeting, Stubbings told Zourkas about the Fingal property and Zourkas told him to get a section 32 vendor's statement.[11] At the third meeting, Stubbings showed the section 32 statement to Zourkas. The section 32 statement stated the sale price at $900,000. There was then a discussion during which Zourkas told Stubbings that he could borrow enough to pay out the two CBA loans over the Narre Warren properties, purchase the Fingal property, and have about $53,000 surplus loan funds to enable him to pay three months' interest on the loan while he sold the Narre Warren properties, reduced the loan to about $400,000, and then refinance the loans with a bank at lower interest rates.[12] There was no mention of a second mortgage loan at this stage.

12 On 30 June 2015 Stubbings signed a contract to purchase the Fingal property for $900,000, subject to a loan being approved by the National Australia Bank for the

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8 Ibid [109].

9 Ibid [114].

10 Ibid [116].

11 Ibid [118].

12 Ibid [120]–[124], [137]–[138]. There is some confusion in the Reasons as to whether the third meeting occurred before, or after, Stubbings purchased the Fingal property. From the evidence as a whole, however, it appears that the third meeting preceded the purchase of the property, and this was common ground on the appeal.

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whole of the purchase price by 7 July 2015. The contract of sale provided that a deposit of $90,000 was payable by that date, of which $100 had been paid. Settlement was due on 28 August 2015. Stubbings understood that the finance condition meant that he only stood to lose $100 if he could not get finance to proceed with the purchase. That understanding was not legally correct. By general condition 14 of the contract of sale, Stubbings had only an option to terminate the contract if finance was not obtained and he in fact immediately applied for the loan and did everything reasonably required to obtain approval for the loan. There was no evidence that the loan was applied for by 7 July 2015 or of Stubbings exercising his option to terminate the contract of sale. Accordingly, the contract of sale in fact became unconditional and Stubbings was, strictly, liable to pay the balance of the $90,000 deposit and to proceed with the purchase. However, as appears below, the vendor appears to have taken a different view and, in any event, the contract of sale was replaced by a later contract of sale which was renegotiated in the circumstances described below.

13 At some stage in July or early August, Zourkas approached Myer Jeruzalski, a solicitor who specialises in arranging for his clients to lend money on the security of land. Jeruzalski is a partner in the law firm Ajzensztat, Jeruzalski & Co ('AJ Lawyers'). On 10 August 2015, AJ Lawyers arranged to have the two Narre Warren properties and the Fingal property valued for the purposes of mortgage finance. The two Narre Warren properties were valued at $375,000 and $395,000 respectively, and the Fingal property was valued at $820,000, making a total of $1,570,000.

14 The evidence does not disclose who paid for the valuations, and the judge made no finding. Jeruzalski said that no loan would be offered on behalf of his clients without a satisfactory valuation to support the loan being made, and that the proposed borrower would be asked to provide the funds to pay for the valuation. Zourkas suggested in evidence that Stubbings paid for the valuations, but the judge did not accept his evidence unless corroborated. It appears likely, however, that Stubbings — by one means or another — found the money to pay for the valuations

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and that, in this respect, Zourkas's evidence is correct. Stubbings gave no evidence on the matter.

15 By two letters dated 21 August 2015, AJ Lawyers offered, on behalf of their clients, to provide first and second mortgage finance to a company owned by Stubbings, the Victorian Boat Clinic Pty Ltd ('the company'). Each offer was conditional on the loans being guaranteed by Stubbings, who was to provide a first and second mortgage over the two Narre Warren properties and the Fingal property as security for his guarantee.

16 Other conditions of the offers included that:

(1) The company was to grant a charge over its assets, although, as appears below, it had none and had never traded.

(2) The proceeds of the loans were not being used for personal, domestic or household purposes but were being used wholly or predominantly for business purposes or investment (other than in residential property) purposes, so that the National Credit Code[13] ('the Code') did not apply to the loans.

(3) The loans would be for a maximum period of 12 months and a minimum period of six months. If the loans were repaid within the six month period, the company would still be liable for interest for the whole of the six month period; and if repaid after six months, but before the 12 month period of the loan, an interest penalty of one month's interest was payable.

(4) A procuration fee of one per cent plus GST (first mortgage) and five per cent plus GST (second mortgage) was payable to AJ Lawyers on the principal amount of each loan 'in addition to any other procuration fees payable to any other parties'.

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13 *National Consumer Credit Protection Act 2009* (Cth), Sch 1.

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(5) By clauses (y) and (z), the loans were conditional on: (y) the company 'confirming [its] ability to satisfy all of its obligations in respect of the proposed mortgage together with evidence of serviceability'; and (z) 'satisfactory explanation … as to the proposed means of repayment of the proposed loan [being] provided'.

17 The first mortgage loan was for the sum of $1,059,000 at an interest rate of 10 per cent per annum and a default rate of 17 per cent per annum. The second mortgage loan was for $133,500 at an interest rate of 18 per cent per annum and a default interest rate of 25 per cent.

18 It appears that a second mortgage was necessary because the first mortgage amount was limited to two-thirds of the combined valuations of the two Narre Warren properties and the Fingal property. This was consistent with the standard practice of AJ Lawyers in arranging first mortgage loans for their clients. Any loan above that loan-to-security ratio was riskier, and thus a second mortgage at higher rates was required to pay consultancy fees of $27,000 to Zourkas; loan procuration fees and the mortgagees' legal costs totalling $31,500 to AJ Lawyers; the costs and expenses of the purchase of the Fingal property, including stamp duty; and, importantly, the first month's interest under the two mortgages (about $10,000), which was payable in advance. The balance of the loan proceeds was to be paid to Stubbings for the purposes discussed below.

19 Stubbings accepted the offers on 22 August 2015, by signing the two letters on his own behalf and on behalf of the company in the spaces provided. Zourkas brought the offer letters to Stubbings and asked him to sign them at their fourth meeting. At this meeting, Stubbings also signed a 'mandate' at Zourkas's request. The mandate was a pro forma document which was largely completed by Zourkas in handwriting. It contained an agreement by Stubbings to pay Zourkas a consultancy fee of $27,000, even if the loan did not proceed, and that liability was secured by a charge over the

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Narre Warren properties. The trial judge found that the amount of $27,000 was not included in the document when it was signed by Stubbings.[14]

20 At around this time, it appears that the vendor was considering withdrawing from the sale. Stubbings told Zourkas of this and they met at a café in Rosebud. Zourkas suggested that they go and see the vendor, which they did. In the course of the discussions, Zourkas said to the vendor: 'Look, the money is fine. We've just had a couple of complications. We'll make the contract unconditional'. The vendor was apparently happy with that and following further negotiations a price of $815,000 was agreed on an unconditional basis.[15]

21 On 27 August 2015, Stubbings signed a revised contract to purchase the Fingal property. The purchase price was $815,100. The deposit was stated to be $81,510, of which $5,100 was acknowledged as having been paid, with the balance of the deposit and purchase price due at settlement on 28 September 2015. The evidence disclosed, however, that a further $5,000 part payment of the deposit was never paid. Indeed, Stubbings gave evidence he had 'no idea' where the reference to a $5,100 payment came from.

22 By letters dated 16 September 2015 addressed to Stubbings (second mortgage) and 17 September 2015 addressed to the company (first mortgage), AJ Lawyers said they were 'instructed to approve' the two mortgage loans. It appears that at this point, AJ Lawyers had made some inquiries as to the nature of the Fingal property. Jeruzalski gave evidence that he was aware that the property was five acres (and thus 'not a typical residential block'). Under cross-examination, Jeruzalski also admitted that he had known that the Fingal property was zoned 'green wedge', which meant that it could not be used for commercial purposes, and that he had received this information because 'we rang the council'. However, Jeruzalski claimed that 'the accountant' and 'the solicitor' had given him advice that Stubbings

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14 Reasons [133], [290].

15 Ibid [127]–[129].

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'had applications in council and that [Stubbings was] conducting a business there.' Jeruzalski was not pressed further in cross-examination about this evidence.

23 The letters from AJ Lawyers dated 16 and 17 September 2015 enclosed documents for execution by the company and Stubbings to effectuate the two transactions. The documents included certificates of 'Independent Financial Advice (to be signed by an Accountant)' and a certificate of 'Independent Legal Advice'. Although not expressly stated in the first mortgage approval letter, it is clear in context (including from the second mortgage approval letter) that the loan approvals were both conditional on the two certificates being duly signed and returned.

24 The documents also included Disbursement Authorities in respect of the two loans which set out the two procuration fees to be paid from the settlement proceeds to AJ Lawyers and the consultancy fee of $27,000 payable to Zourkas. No mention was made of any fees being paid by AJ Lawyers to either the independent solicitor or accountant who were to sign the two certificates of independent advice which AJ Lawyers had drafted. However, AJ Lawyers later paid the solicitor $1,650 and the accountant $300 from the loan proceeds. As appears below, Stubbings says that he also paid, at Zourkas's direction, cash amounts to the solicitor and the accountant.

25 The two letters enclosing the documents were collected by Zourkas from Jeruzalski, and he gave the letters to Stubbings.[16] Zourkas told Stubbings that he needed to see a solicitor — 'in front of whom he would sign the document[s]'[17] — and an accountant.[18] The solicitor was Con Kiatos and the accountant was Jordan Topalides. According to Stubbings, whose evidence the trial judge preferred to that of Zourkas, Zourkas gave two sealed envelopes to Stubbings on 19 September 2015 — one labelled 'Accountant' and the other labelled 'Solicitor', as well as a business card for Kiatos, which was exhibited in the court book, and a phone number for

16 Ibid [170].

17 Ibid.

18 Ibid [134].

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Topalides. Zourkas told Stubbings to 'take these documents, get them signed and bring them back'.[19] Stubbings said that he did as he was told, that the envelopes were sealed when they were given to him and sealed when he returned them to Zourkas after having signed the documents as described below.

26 All of the documents prepared by Jeruzalski, with the exception of the certificate of independent financial advice, were signed by Stubbings in the presence of Kiatos, before Stubbings met with Topalides. Before setting out the circumstances in which the documents were signed, it is convenient to set out the terms of the certificates of independent legal and accounting advice, and a related acknowledgment signed by Stubbings.

27 The certificate of independent legal advice was addressed to the lenders in respect of the proposed first mortgage loan. Under the heading 'Acknowledgment by Guarantor' is a list of questions to be answered by Stubbings in hand writing. The list of questions and answers is in the following terms:

> 1 Have you received copies of the documents described under the heading 'Security Documents' below? *Yes*
>
> 2 Have you been given an opportunity to read those Security Documents? *Yes*
>
> 3 Have the Security Documents been fully explained to you by your solicitor? *Yes*
>
> 4 Do you understand the effects of the Security Documents and the consequences to you if the Borrower defaults on its obligations to the Lender? *Yes*
>
> 5 In particular, do you understand that if the Borrower fails to pay all of the moneys due to the Borrower to the Lender then the Lender will be entitled to call on you as Guarantor to recover the moneys due to it? *Yes*
>
> 6 Was this Acknowledgement read and signed by you BEFORE you signed the Security Documents? *Yes*[20]

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19 Ibid.

20 Emphasis added.

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28 Each of the answers 'Yes' was written by Kiatos, not Stubbings.[21] Stubbings signed the document under the words:

> I confirm the accuracy of the answers to the above questions and acknowledge that the Lender will be relying on these answers in respect of giving the loan to THE VICTORIAN BOAT CLINIC PTY LTD.
>
> I request the Lender to give this loan to the Borrower.

29 On the same day, 19 September 2015, Stubbings, in his capacity as sole director and secretary, signed an acknowledgment by the company to the first mortgagees that it had obtained independent legal advice before executing the loan documents.

30 Kiatos also signed the certificate of independent legal advice. It appears that he did so in two capacities, one to witness Stubbings's signature, and the other to confirm his 'Certificate by Independent Solicitor' in the following terms:

> Before the Security Documents were executed by the Guarantor/s I explained the contents, nature and effect of them to the Guarantor/s. In particular, I explained and advised on the consequences of default under the relevant Security Documents, including the Lender/Mortgagee's right to sell the property constituting the security. The Guarantors appeared to be aware of and to understand the terms, nature and effect of the Security Documents and their obligations under them. I have made a diary note of the advice and explanation give to the Guarantor/s.[22]

31 The certificate of independent financial advice was signed by Topalides on 19 September 2015. The certificate is addressed to the lenders concerning the loan to the company on the security of a debenture charge over its assets. The certificate states that Topalides, 'being an Accountant, hereby certify as follows':

> 1 I have been instructed by THE VICTORIAN BOAT CLINIC PTY LTD ACN 601 712 172 to explain the financial risks being assumed:-
>
> (a) by executing the security documents in respect of the financial accommodation to be provided by the Lender which security documents are referred to in Item 1 of the Schedule below ('the Security');
>
> (b) by the application of the said financial accommodation for the

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21 Reasons [80].

22 Ibid [83].

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purposes referred to in Item 2 of the Schedule below.

2 Before the Security was executed by the Borrower, I explained the financial risk being assumed by executing the Security and by the application of the aforesaid financial accommodation in the manner stated in Item 2 of the Schedule.

3 To the best of my knowledge and belief and in my opinion the Borrower appears to understand the nature and extent of the financial risk which the Security places and the nature and extent of the financial risk which will be assumed by the application of the aforesaid financial accommodation in the manner stated in Item 2 of the Schedule.

4 I have been engaged by the Borrower in advising and have given this Certificate entirely independently of any other Borrower or Guarantor.

5 The Loan herein is required for business purposes.

DATED the 19th day of September 2015.

[J Topalides]
……..

SCHEDULE

Item 1 — ("the Security") Loan Agreement to secure an advance of $1,059,000 & Debenture Charge

Item 2 — (purpose of borrowings)

(please complete)

Set up & Expand the business
……..

32 The words 'Set up & Expand the business' are in Topalides's handwriting.[23]

33 Also on 19 September 2015, Stubbings signed a deed on his own behalf and on behalf of the company, under which he and the company covenanted with the first mortgagees that, among other things, the purpose of the first mortgage loan was 'for business purposes', 'not for personal, domestic or household purposes', 'not to purchase, renovate or improve residential property for investment purposes', or to 'refinance credit that [had] been provided wholly or predominantly to purchase, renovate or improve residential property for investment purposes'. Although dated

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23 Ibid [194].

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'30 September' in handwriting, the deed was included in the package of documents sent under cover of the 17 September 2015 letter from AJ Lawyers and thus likely to have been signed on 19 September with the date left blank. 30 September 2015 was the date of settlement.

34 There were significant divergences in the evidence given by Stubbings and Kiatos. Matters in dispute included the extent to which Stubbings's financial position was divulged, the nature of the legal advice provided by Kiatos, and whether Stubbings provided $1,500 cash to Kiatos, in addition to the $1,650 which was later paid to Kiatos from the loan proceeds. Kiatos had been joined to the proceeding as a third party, but the claim against him was settled. For this reason, the trial judge did not make any findings with respect to the inconsistent evidence of Stubbings and Kiatos.[24]

35 As to the dealings between Stubbings and the accountant, Jordan Topalides, the evidence was again conflicting. It was agreed that, following referral from Zourkas, Stubbings attended on Topalides, bringing mortgage documentation and the unsigned Certificate of Independent Financial Advice which had been prepared by AJ Lawyers and given to him by Zourkas. Stubbings's evidence was that the meeting was short, approximately 15 minutes, and that he handed Topalides $1,000 in cash in an envelope. Stubbings claimed that Topalides did not make any inquiries as to his income or occupation, and in fact asked no questions at all.

36 Topalides, however, recalled that he went through the loan documentation carefully with Stubbings over two and a half hours. He recalled that Stubbings informed him that the loan was to relocate and expand his existing business of boat repairs.

37 Topalides also said he told Stubbings would need at least $16,000 each month in order to service the loan, and that Stubbings claimed in response that his income

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24 Ibid [185].

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would increase to $20,000 to $25,000 a month after purchasing the Fingal property, which Topalides apparently accepted. Nonetheless, Topalides claimed that he tried to convey to Stubbings that 'it was not a loan that he would recommend to Mr Stubbings'.[25] The trial judge noted the apparent inconsistency of these claims[26] and said it was 'doubtful' that Stubbings claimed he was earning such an income.

38 Topalides denied receiving cash from Stubbings, but admitted receiving a $300 fee from AJ Lawyers after settlement.[27]

39 After noting certain inconsistencies between Topalides' evidence and that of other witnesses, the trial judge found that the evidence 'suggests that his purported recollection of what took place at the meeting may not be reliable';[28] that the evidence also suggested that 'Mr Topalides may have accepted cash from Mr Stubbings';[29] that it was 'doubtful'[30] that Stubbings claimed to Topalides he was earning sufficient income to service the loan; and that Topalides 'did not understand the transaction into which Mr Stubbings was proposing to enter'. These findings led the judge to find that the Certificate of Independent Financial Advice should not have been signed in the circumstances, and that Topalides breached his duty of care to Stubbings in doing so.[31]

40 Settlement of the two loans and the purchase of the Fingal property by Stubbings took place on 30 September 2015. The settlement statement records that the following (rounded) amounts were paid from the loan proceeds on that day, leaving a balance of only $16,360 held on trust by AJ Lawyers for the company and Stubbings:

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25 Ibid [201].

26 Ibid [213].

27 Ibid [210].

28 Ibid [209].

29 Ibid [212].

30 Ibid [334].

31 Ibid [337].

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(1) the purchase price of the Fingal property;

(2) the amount owed to the Commonwealth Bank as mortgagee of the Narre Warren properties;

(3) $10,000 for one month's interest in advance on the first and second mortgages.

(4) $44,000 for stamp duty in respect of the purchase of the Fingal property.

(5) $2,000 for Titles Office registration fees.

(6) $19,300 for AJ Lawyers' procuration fee and legal costs in respect of the first mortgage.

(7) $12,300 in respect of AJ Lawyers' procuration fee and legal costs in respect of the second mortgage.

(8) $27,000 for Mr Zourkas's 'consultancy fee'.

41 Following settlement, the amount of $16,360 was reduced to $6,959 by payments authorised by Stubbings in the following rounded amounts:

(1) $7,450 for unpaid council rates in respect of the Narre Warren properties.

(2) $1,650 to Kiatos for his unpaid fees.

(3) $300 to Topalides for his unpaid fees.[32]

42 Stubbings and his family then moved into the houses on the Fingal property to live. He lived in one house and his son in the other. Although some boat hulls and parts belonging to Stubbings were stored on the property, no business was conducted or ever intended to be conducted with them by either Stubbings or the company.

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[32] The request and authorisation for payment of the legal and accounting fees was by email dated 9 October 2015 from Kiatos to Jeruzalski's conveyancing assistant and copied to Stubbings.

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43 When the second month's interest became due, Stubbings did not have sufficient income to pay it. He sold some assets and managed to make the second interest payment. He was unable to pay the third month's interest and so tried to sell the Narre Warren properties, but this was prevented by a combination of factors including a caveat lodged by a person claiming to be a third mortgagee. In these circumstances, Stubbings and his company defaulted under the terms of the loan agreements.

44 The first mortgagees then brought proceedings in the Trial Division of the Supreme Court seeking possession of the two Narre Warren properties and the Fingal property. A summary judgment application before an associate judge resulted in the first mortgagees obtaining judgment for possession of all three properties.[33] Stubbings appealed against the possession orders, but did not seek a stay pending the hearing and determination of the appeal. Before the appeal could be heard and determined, the first mortgagees took possession of the Narre Warren properties but not the Fingal property. In April 2017 they sold those properties for $392,500 and $466,000 respectively, a total of $858,500. The net sale proceeds of these sales were applied in reduction of the loan account for the first mortgage loan.

45 On appeal, Elliott J held that the associate judge had been wrong to grant summary judgment, and gave Stubbings leave to defend the remainder of the proceeding seeking possession of the Fingal property.[34]

46 At trial, Stubbings defended the proceeding on three principal grounds. First, that the first mortgage was governed by the National Credit Code, and the first mortgagees had breached that Code in a number of respects. As the loan was made to the company, this defence failed.[35] Second, on the basis of false and misleading conduct by Zourkas on behalf of the first mortgagees. This defence failed on the

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33 *Jams 2 Pty Ltd v Stubbings* [2016] VSC 711.

34 *Stubbings v Jams 2 Pty Ltd* (2017) 53 VR 420.

35 Reasons [232]-[246].

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basis that Zourkas was not the agent of the mortgagees but was the agent of the company and Stubbings.[36]

47 Third, Stubbings defended the proceeding on the basis that AJ Lawyers, as agent of the first mortgagees, acted unconscionably by the manner in which the loans were offered, approved and made. In summary, Stubbings contended that the loan constituted 'asset-based lending' in circumstances where AJ Lawyers knew that the first mortgagees would have to rely on the secured properties for repayment, because Jeruzalski knew Stubbings and the company could only contribute $100 towards the purchase of the Fingal property, no evidence had been sought or obtained as to the ability of Stubbings or the company to repay the loan and, notwithstanding that the purported purpose of the loan was to enable the company to 'set up and expand the business', Jeruzalski well knew that the loan funds would not be used for that purpose but were overwhelmingly required to be used for the purpose of acquiring the Fingal property.

48 The trial judge accepted the unconscionable conduct defence and made orders which he considered 'practically just' in all the circumstances. On this basis, the trial judge ordered that the loan agreement and guarantee were 'declared invalid and unenforceable and set aside',[37] the first mortgagees deliver up to Stubbings within 14 days a registrable discharge of the first mortgage,[38] and that Stubbings account to the first mortgagees for the sum of $109,315 on an unsecured basis, with payment stayed for six months.[39]

49 The third party proceedings were resolved in the following ways. First, as noted, the claim against Kiatos was settled. Second, the claim against Topalides was found proved and judgment was entered against him. However, as Stubbings was fully

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36 Ibid [223]-[224].

37 *Jams 2 Pty Ltd & Ors v Stubbings (No 4)* [2019] VSC 480, [46]; Order 2 ('Relief Reasons').

38 Ibid Order 1.

39 Ibid Order 3.

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compensated by the orders made on his successful counterclaim, no damages were awarded. Third, while the judge found that Zourkas had misled Stubbings, he nevertheless dismissed the third party proceeding against him on a narrow pleading point.[40] However, had the claim against Zourkas succeeded, it appears likely that the judge would have nevertheless awarded no damages against him – on the same basis as none were awarded against Topalides. While proportionate liability claims were made between third parties, it appears that no claims for proportionate liability or contribution were raised between the first mortgagees as defendants to counterclaim and the third parties.

50 The first mortgagees seek leave to appeal against the trial judge's unconscionability findings. If they are unsuccessful in challenging those findings, they seek leave to appeal against the form of the final orders, which they contend are against authority and not 'practically just' in the circumstances. As all grounds of appeal are arguable, leave to appeal should be granted. We will thus refer to the grounds of appeal on this basis.

51 We note that Stubbings has not taken any steps to protect himself in the event that the appeal by the first mortgagees is allowed – for example, by a cross-appeal against the trial judge's refusal to award damages against Topalides or his decision to dismiss the third party proceedings against Zourkas. Thus, if the appeal in this case is allowed, Stubbings will be unable to recover his losses from either Topalides or Zourkas in the context of this appeal.

52 Further, we note that Stubbings has not filed a notice of contention. He relies only on, and seeks to support, the trial judge's Reasons — to which we now turn.

Judge's reasons for finding unconscionability

53 After setting out the issues for determination, the trial judge commenced his

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40 Reasons [328].

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reasons with a description of the 'system of lending' usually undertaken by AJ Lawyers in arranging for its clients to make asset-based loans on mortgage security, and which he held was in fact followed in this case, in the following terms:[41]

(1) Jeruzalski's primary practice for about 30 years has been arranging loans for his clients in the manner described.

(2) Jeruzalski is approached by other solicitors, accountants or brokers seeking a loan for a client. For example, Zourkas has introduced many borrowers to him. The introducer assists Jeruzalski in arranging for the loan documentation to be executed by the borrower and in obtaining certificates of independent advice from a solicitor and an accountant to be signed by the borrower, the solicitor and the accountant.[42]

(3) Jeruzalski does not entertain direct approaches for finance. There must be an intermediary, such as another solicitor, finance broker or a consultant such as Zourkas, who first approaches him.[43] On this basis, there is no need for Jeruzalski to meet, and he does not meet, the prospective guarantor or other representative of the borrower company. He only deals with them by correspondence. Any details that Jeruzalski needs to know about the borrower and guarantor are obtained from the intermediary.[44]

(4) Jeruzalski will only arrange for loans on behalf of his clients to be made to companies. The purpose of this is to ensure that the loans are not governed by the Code. He will not allow his clients to make loans governed by the Code.[45]

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41 Ibid [52]–[67].

42 Ibid [56].

43 Ibid [61].

44 Ibid [62].

45 Ibid [57].

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(5) Loans must be secured by a mortgage over real estate, and guarantees from the directors and/or shareholders of the borrower company.[46]

(6) In deciding whether or not to arrange for his clients to lend money, Jeruzalski gives no weight to the ability of the borrower or guarantor to repay the loan, other than from the mortgaged security. Thus, before entertaining making an offer of a loan, a valuation of the proposed security is obtained. Apart from checking to see that the directors or guarantors are not bankrupt, Jeruzalski does not seek any further information about them or their personal or financial circumstances.[47] Jeruzalski makes no credit risk analysis of the ability of the proposed borrower company, or the guarantor or guarantors, to repay the loan or the interest; that is a deliberate decision on his part,[48] and Jeruzalski does not provide his clients with any other information by which they could engage in any credit risk analysis other than considering the loan-to-property value ratio.

(7) Apart from forming the view that, based on the valuation, the proposed security is satisfactory, Jeruzalski does not advise his clients but simply brings the lending opportunity to their attention as 'experienced business people who make their own decision whether to lend or not'.[49] In this case, a representative of each of the first mortgagees gave evidence that they had made their decisions to lend based on the valuations of the Narre Warren properties and the Fingal property alone.[50]

(8) If a client is willing to make the proposed loan, Jeruzalski makes a formal written offer to the borrower and the guarantor on behalf of his client. If the

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46 Ibid [57].

47 Ibid [57].

48 Ibid [58].

49 Ibid [60].

50 Ibid [69].

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offer is accepted, Jeruzalski then prepares all loan and security documents, including the guarantee, together with draft certificates of independent legal and accounting advice to be signed by the borrower, guarantor, a solicitor and an accountant. Jeruzalski gives these documents to the intermediary, such as Zourkas in this case, to deliver to the borrower and guarantor and to obtain the necessary signatures.[51]

54 The trial judge then set out the facts of this particular case, by reference to the terms of the documents and the oral evidence.

55 As to Jeruzalski's involvement, the judge noted Jeruzalski's evidence that, while he never met or spoke with Stubbings,[52] Zourkas told him that the proposed loan was a business loan and the business was mainly concerned with boat repairs.[53]

56 As to whether Jeruzalski knew or suspected that Stubbings had no income when the loans were made to him, the trial judge set out Jeruzalski's evidence in full, in the following terms:

Counsel:	Now, in relation to the allegations that Mr Stubbings has made just this morning, were you aware that he did not have, as he alleged, any income?
Mr Jeruzalski:	Was I aware? *I don't seek income particulars*.
Judge:	Pardon?
Mr Jeruzalski:	I'm aware now.
Judge:	No, at the time you advanced the moneys, were you aware?
Mr Jeruzalski:	*Most – most probably*.
Judge:	*– that he alleges that he had no income?*
Mr Jeruzalski:	*Most probably*.
Judge:	Were you aware of that?

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51 Ibid [63]–[67].

52 Ibid [89].

53 Ibid [88].

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Judge:	Pardon?
Mr Jeruzalski:	*Most probably I was aware of that.*
Judge:	You were?
Mr Jeruzalski:	Yeah.
Judge:	That he had no income?
Mr Jeruzalski:	*Well, I'm lending on the assets.*
Judge:	You may want to get the witness to expand.
Counsel:	Would you please expand on that?
Mr Jeruzalski:	I have here three valuations on the three properties and we were told that, um, he was setting up a business.
Judge:	He was setting up a business?
Mr Jeruzalski:	That's right. He had a — he had — he had a business running before but he wanted to buy this property, so that he could further expand the business. The business was boat repair and so on. Most of the people who come and see — seek funds —
Judge:	But the question was, as I understand it, were you aware that he had income or had asserted to the broker or someone else that he had no income? Were you aware of that at the time?
Mr Jeruzalski:	I just can't remember.
Judge:	You can't remember?
Mr Jeruzalski:	Mmm. *I said most probably I would've been aware he had no income. If he — sorry.*
Counsel:	Is that upon the basis of that it was an asset loan or something that may have been told to you?
Mr Jeruzalski:	*Correct. I'm not looking for income figures.* And a borrower goes away to seek independent accounting advice and legal advice as to whether he can perform and — and honour the obligations under the mortgage. *If he had an income sufficient to service a loan of that amount, he would've gone to a bank*.[54]

57 Further, the trial judge noted Jeruzalski's evidence that he was aware that Stubbings had only paid a $100 deposit on the Fingal property under the contracts of

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54 Ibid [92] (emphasis added).

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sale.[55]

58 The trial judge then set out the details of Stubbings's lack of significant income and his poor financial circumstances (except for his equity in the two Narre Warren properties),[56] that he had no intention of conducting any business on his own or through the company,[57] his dealings with Kassimidis and the introduction to Zourkas,[58] and his dealings with Zourkas.[59]

59 In respect of the dealings between Stubbings and Zourkas, the trial judge made strong adverse credit findings against Zourkas — stating that he was 'not prepared to accept Mr Zourkas's evidence on any relevant issues, unless corroborated';[60] and that he was 'satisfied that Mr Zourkas was not an honest man, but [was] a man prepared to prey upon the weak and the vulnerable like Mr Stubbings'.[61] The result of the trial judge's rejection of Zourkas as a credible witness is that he accepted the evidence of Stubbings that:

(1) Zourkas had told Stubbings, or at least was aware that Stubbings believed at the time of his entry into the loan and mortgage agreements, that there would be $53,000 of the loan funds remaining after the purchase price of the Fingal property had been paid, and that this would allow Stubbings to pay the first two months' interest repayments on the two loans and perform some renovations to the Narre Warren properties to prepare them for sale.[62]

(2) Further, Zourkas had told Stubbings that those two months' interest repayments would demonstrate to a first-tier bank, namely Westpac, that the

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55 Ibid [96].

56 Ibid [98]–[107].

57 Ibid [107].

58 Ibid [108]–[109].

59 Ibid [109].

60 Ibid [180].

61 Ibid [271].

62 Ibid [220](a); [222].

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loans were serviceable and Zourkas would help Stubbings refinance the loans at a lower rate after two months.[63]

(3) At the time that Stubbings signed the 'mandate' document by which Zourkas became entitled to a $27,000 'consultancy fee', the figure of $27,000 in the document had not been filled in. The amount of the fee, and the date of the document, was added in later by Zourkas.[64]

(4) Contrary to Zourkas' claims that Stubbings told him he earned 'five to six thousand dollars a week',[65] Zourkas knew of Stubbings's lack of income and poor financial state.[66]

60 The trial judge then considered the various defences put forward by Stubbings. As to the defence based on false and misleading conduct, while the trial judge accepted that Zourkas had misled Stubbings,[67] the trial judge rejected this defence on the basis that it was not established that Zourkas was acting as the agent of the first mortgagees or AJ Lawyers in connection with the loan.[68] The trial judge found, however, 'that Mr Zourkas was acting as an intermediary or facilitator for AJ Lawyers, who were the agents of the plaintiffs, in facilitating the making of the loan.'[69]

61 As to the defence based on breaches of the Code, the trial judge concluded that the Code did not apply — because the loan was to the company and not to Stubbings personally, whose only role was as a guarantor providing a mortgage to secure the loan to the company.[70] In the course of his reasons for denying the Code defence, the

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63 Ibid [220](b)-(d); [222].

64 Ibid [133], [290].

65 Ibid [162].

66 Ibid [163].

67 Ibid [222].

68 Ibid [223].

69 Ibid [224].

70 Ibid [226]–[246].

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judge stated that there was 'no doubt' that the loan was made to the company and that there was 'no suggestion that the loan was a sham and was in fact made to Mr Stubbings'.[71] This was notwithstanding that all but approximately $6,000 of the loan moneys were expended to or for the benefit of Stubbings in the purchase of the Fingal property and the discharge of the Commonwealth Bank mortgages over the two Narre Warren properties.[72]

62 Next, the judge set out the legal principles which he intended to apply to resolution of the unconscionable conduct defence. He referred to *Commercial Bank of Australia Ltd v Amadio*[73] and the commentary in Meagher, Gummow and Lehane's *Equity: Doctrine & Remedies*[74] for the general equitable principle.[75] The judge referred to the need for the weaker party to be at a special disadvantage and for the stronger party, with sufficient knowledge of that disadvantage, to take unconscientious advantage.[76] As to the requirement that the stronger party have sufficient knowledge of the special disadvantage of the other party, the judge referred to the decision of the New South Wales Court of Appeal in *Elkofairi*[77] in some detail.[78] Although the judge did not refer to *Elkofairi* again, it is clear from the detail in which he considered the case and quoted from it and from his reasoning, that he was influenced by the facts and result in that case in his determination that the first mortgagees, by their agent Jeruzalski, had acted unconscionably. We will return to *Elkofairi*, and the reliance placed upon it by Stubbings, later in these reasons.

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71 Ibid [232].

72 Ibid.

73 (1983) 151 CLR 447.

74 J D Heydon, M J Leeming, P G Turner, '*Meagher, Gummow & Lehane's Equity: Doctrines & Remedies* (LexisNexis Butterworths, 5th ed, 2015) 502 [61-010] ('*Meagher, Gummow & Lehane*').

75 Reasons [254].

76 Ibid [253]–[255].

77 [2002] NSWCA 413.

78 Reasons [274]–[280].

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63 As to statutory unconscionability, the judge referred[79] to the decisions at first instance and on appeal to this Court in *Violet Home Loans Pty Ltd v Schmidt*,[80] the first instance and appeal judgments of this Court in *Director of Consumer Affairs v Scully (No 3)*,[81] and the decision of the New South Wales Court of Appeal in *Tonto Home Loans Australia Pty Ltd v Tavares*.[82] Relevantly, the trial judge accepted the following propositions from these authorities:

(1) Making an asset-based loan does not of itself constitute unconscionable conduct. Something more is required in the circumstances of the particular case.[83]

(2) In order to find statutory unconscionable conduct, it was necessary to establish 'moral obloquy' or 'some moral tainting' in the transaction. This position was based on the law as it then stood.[84]

(3) The assessment of whether or not there has been unconscionable conduct is an 'evaluative judgment' in the context of all the circumstances of the case.[85]

(4) The requirement of moral obloquy or moral taint could be satisfied where, absent deliberate wrongdoing, there was a reckless failure to inquire involving 'wilful blindness'.[86]

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79 Ibid [256]–[262].

80 On appeal: *Violet Home Loans Pty Ltd v Schmidt* (2013) 44 VR 202, 219–20 [59] ('*Violet*'); at first instance: *Perpetual Trustees Australia Ltd v Schmidt and Violet Home Loans Pty Ltd* [2010] VSC 67, [200], [207] (J Forrest J) ('*Schmidt*').

81 [2013] VSCA 292 ('*Scully*').

82 [2011] NSWCA 389 ('*Tonto*').

83 Reasons [259], citing *Schmidt* [2010] VSC 67, [200]; and on appeal *Violet* (2013) 44 VR 202, 211 [32].

84 For example, *Tonto* [2011] NSWCA 389, [291]; *Violet* (2013) 44 VR 202, 219 [58]; *Scully* [2013] VSCA 29, [48]-[51].

85 Reasons [260], citing *Tonto* [2011] NSWCA 389, [291]–[293]; as accepted by this Court in *Violet* (2013) 44 VR 202, 211 [32], and confirmed by the High Court in *Australian Securities and Investments Commission v Kobelt* (2019) 368 ALR 1; (2019) 93 ALJR 743; [2019] HCA 18, 15 [47].

86 Reasons [261], citing *Scully* [2013] VSCA 292, [31]–[32]; approved in *Violet* (2013) 44 VR 202, 219 [58].

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64 The trial judge then summarised Stubbings's unconscionability defence as he understood it. Insofar as remains relevant on appeal, that summary was in the following terms:

> … Mr Stubbings alleges that the lenders entered into the mortgage and loan agreements and conducted the mortgage and loan agreements in the following manner:
>
> (a) Funds were advanced on asset-based lending, being that the lenders would rely on the properties for repayment, and the lenders knew that Mr Stubbings had and would only contribute $100 towards the purchase of the Fingal property.
>
> (b) The lenders had no evidence and did not request any evidence regarding Mr Stubbings' ability to repay, or the capacity of VBC[87] to repay, the loan.
>
> (c) It was the lenders' intention that any amount owing to them would be recovered on the basis of enforcing and selling the properties.
>
> (d) Notwithstanding that the purported purpose of the loan was for VBC to 'set up and expand the business', the lenders were at all times aware that the entire funds and the loan were to be used for the acquisition of property.
>
> ...
>
> (f) The lenders purported to advance money to VBC when the company was inactive and never had traded.
>
> ...
>
> Mr Stubbings alleges that the lenders have engaged in conduct that in all the circumstances is unconscionable pursuant to … s 12CB of the ASIC Act, and is unconscionable at law.[88]

65 For the purposes of the unconscionability defence based in equity, the trial judge found that Stubbings was under a special disadvantage in his dealings with Zourkas and the first mortgagees.[89] This was because Stubbings, like the plaintiff in *Schmidt*,[90] was 'unsophisticated, naïve and had little financial nous', was 'unrealistic in the management of his financial affairs and demonstrated a complete lack of business

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87 Victorian Boat Clinic Pty Ltd. See [15] above.

88 Reasons [248]–[249].

89 Ibid [263]–[272].

90 [2010] VSC 67, [211], cited in Reasons [263]-[4].

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understanding'.[91] In the courtroom, Stubbings was unable to carry out simple calculations and his child-like speech and demeanour satisfied the judge that 'he was precisely the sort of person who needed protection and was vulnerable to being exploited'.[92] The fact that Stubbings entered into the transaction as it was evidenced his vulnerability. As appears below, while relevant, this was not a necessary finding for the purposes of the statutory defences based on the statutory concept of unconscionable conduct.

66 The trial judge then considered whether, in all the circumstances of the case, Jeruzalski had sufficient knowledge about Stubbings and the proposed transaction to make it unconscionable — in equity or under statute — to make the loan without first inquiring as to the ability of the company and Stubbings to make the interest instalments and repay the loan.

67 The trial judge commenced his analysis of whether the conduct of the first mortgagees, including their agent Jeruzalski, constituted unconscionable conduct by setting out seven 'factors' — in substance, conclusions reached by him on the evidence — which he considered to be relevant in determining whether the unconscionable conduct case had been made out:

> First are the deliberate steps taken by AJ Lawyers to ensure that they did not ascertain any information about Mr Stubbings' financial circumstances and his ability to service the loan, particularly in circumstances where they believed that there was a real risk that he may not have had a sufficient income to service the loan.
>
> Second is the knowledge of AJ Lawyers that the loan they were making on behalf of the lenders could cause severe damage to the guarantor if the guarantor was not able to service the loan. In other words, AJ Lawyers knew that the loan could be a dangerous product in the wrong hands and wreak significant damage on the guarantor.
>
> Third is the reliance AJ Lawyers placed on Mr Zourkas to obtain and procure the custom of Mr Stubbings and, consequently, the deliberate steps taken by AJ Lawyers to ensure that they were not informed of the representations and inducements made by Mr Zourkas, or his knowledge of Mr Stubbings'

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91 Reasons [264].

92 Ibid [270].

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mistaken beliefs, in entering into loan transaction.

Fourth are the steps taken by AJ Lawyers to immunise themselves from the taint of any knowledge that might expose them to a claim that they had acted unconscionably in making the loan requested by Mr Stubbings. This included ensuring they did not meet Mr Stubbings or obtain any information about Mr Stubbings, and *using Mr Zourkas as a shield to protect them from any knowledge of Mr Stubbings' special disadvantage*.

Fifth are the false representations made by Mr Zourkas to Mr Stubbings, or at least his knowledge of Mr Stubbings' misunderstandings about the loan as discussed above, and his conduct generally to procure Mr Stubbings' custom for AJ Lawyers.

Sixth is the failure by AJ Lawyers to avail themselves of the contractual right the plaintiffs had to obtain information from the borrower.

Seventh is the system of conduct used by AJ Lawyers to procure and make the loan sought by Mr Stubbings.[93]

68 These 'factors' overlap. Many of them are dependent on the judge's conclusion that the AJ Lawyers' 'system of lending' involved 'a high level of moral obloquy'.[94] The fifth factor includes Zourkas's false representations to Stubbings, or his knowledge concerning Stubbings's misunderstandings — notwithstanding that the judge found that Zourkas was not the agent of AJ Lawyers or the first mortgagees and his conduct could not be attributed to them.[95]

69 The trial judge then considered the conduct of Zourkas, finding that it was clearly unconscionable but was not to be attributed to the first mortgagees because Zourkas was not acting as their agent.[96] However, the trial judge reasoned that this did not make the conduct of Zourkas irrelevant to the unconscionability defence. This was because Zourkas 'carried out a central part of AJ Lawyers' system of conduct in procuring loans on behalf of clients and immunising AJ Lawyers from information about borrowers (such as Mr Stubbings) that may have threatened the enforceability

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93 Ibid [282]–[288] (emphasis added) (citation omitted).

94 Ibid [313].

95 Ibid [223].

96 Ibid [289]–[291].

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of the loan'.[97]

70 The trial judge concluded that the system of lending involved a 'high level of moral obloquy' and was followed in this case; and that the system was designed to 'immunise [AJ Lawyers] and their clients from the risk that their loans may be characterised as unconscionable at law or by statute'.[98] The judge did not, however, accept that the system had the desired effect. His Honour considered that the application of the system towards Stubbings was unconscionable in all the circumstances, because it involved wilful blindness on Jeruzalski's part as to Mr Stubbings's financial and personal circumstances'.[99] This was because Jeruzalski had been put on inquiry but 'knowingly and deliberately shut his eyes to Mr Stubbings's circumstances … to ensure that the loans would go through and that he would earn his fees'.[100] On this basis, the trial judge concluded as follows:

> *… Asset-based lending coupled with the system of conduct adopted by AJ Lawyers, leads me to conclude that they AJ Lawyers must be treated as knowing of Mr Stubbings' personal and financial circumstances*.
>
> I uphold Mr Stubbings' defence that the loan, first mortgage and guarantee were procured by unconscionable conduct. Accordingly, I propose to order that the loan, guarantee, and mortgage be set aside, on condition that Mr Stubbings is not unjustly enriched.[101]

71 In summary, the judge's conclusion was that the asset-based system of lending, combined with the failure to inquire about Stubbings's personal and financial circumstances when Jeruzalski ought to have done so given his knowledge, was unconscionable in all the circumstances.

72 The trial judge's reasons for concluding that AJ Lawyers had been put on inquiry of Stubbings's financial and personal circumstances were varied and overlapping.[102]

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97 Ibid [292].

98 Ibid [293], [299], [313].

99 Ibid [315].

100 Ibid [316].

101 Ibid [316]–[317] (emphasis added).

102 Ibid [293]–[316].

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They may be summarised as follows:

(1) The AJ Lawyers' system of lending was applied to the loans.

(2) AJ Lawyers stood to make substantial procuration and legal fees if the loans proceeded, and Jeruzalski knew that Zourkas had a financial incentive to earn his $27,000 consultancy fee.[103]

(3) Jeruzalski knew that asset-based lending was 'a dangerous product' in the wrong hands, and that the loans were particularly risky for Stubbings as a guarantor – as he stood to lose a substantial part (at least $100,000) of his existing equity in the Narre Warren properties if the company defaulted. For example, his equity would at least be depleted by the wasted amounts paid for fees to Zourkas and AJ Lawyers, and by interest at default rates under the two mortgages while the properties were sold.[104]

(4) Jeruzalski assumed or suspected that Stubbings and the company 'would not have the income to service the loans'.[105]

(5) In those circumstances, Jeruzalski, as a solicitor, had moral and ethical duties 'to satisfy himself that Stubbings was not unreasonably exposing himself to the significant financial risks accompanying the loans'[106] but Jeruzalski nevertheless 'deliberately chose' not to make such inquiries[107] 'because he was concerned that, or suspected that, the answers he may have received would have given him information that could form the basis for setting the loans aside on the grounds of unconscionability, and thus preventing his making the loans on behalf of the lenders'.[108]

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103 Ibid [311].

104 Ibid [299]–[308].

105 Ibid [310].

106 Ibid [309].

107 Ibid [310]–[311].

108 Ibid [312].

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(6) Although the AJ Lawyers' system of lending had the in-built safeguard that borrowers were required to provide certificates of legal and accounting advice, and this was required of the company and Stubbings, 'Jeruzalski must have suspected that Stubbings would be guided by Zourkas as to which solicitor and accountant to approach'.[109] Moreover, as far as Jeruzalski was concerned, the solicitor and accountant would only be paid if the loans went ahead — so there was 'no incentive for them to withhold the certificates'.[110] In these circumstances, the judge said that it was 'perhaps a bridge too far' to characterise Topalides and Kiatos as an independent accountant and independent solicitor.[111]

Grounds of appeal: unconscionability finding

73 There are 18 grounds of appeal. Grounds 1 to 13 seek to attack the trial judge's finding that the first mortgagees, especially by their agent Jeruzalski, acted unconscionably in making the loan on the security of Mr Stubbings's guarantee and mortgages, as follows:

> 1 The learned trial Judge erred at [316] of the Reasons for Judgment in finding that 'Mr Jeruzalski's behaviour constituted unconscionable conduct'.
>
> 2 The learned trial judge erred in finding at [308] that Mr Jeruzalski 'knew that the loans were a risky and dangerous undertaking for Mr Stubbings', when Mr Jeruzalski:
>
> (a) understood that through his company Victorian Boat Clinic Pty Ltd (which was the borrower) Mr Stubbings was operating, and intended to expand at the 6-acre premises being purchased with the loan, a boat repair business;
>
> (b) had ensured that Mr Stubbings had received independent legal and financial advice; and
>
> (c) had been informed that Mr Stubbings proposed to sell his two existing properties within a few months so as to pay out or

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109 Ibid [314].

110 Ibid [314].

111 Ibid [314].

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substantially pay down the loans well in advance of the principal falling due for repayment.

3 The learned trial Judge erred in finding at [309] and [310] that Mr Jeruzalski had a moral duty and ethical obligation to satisfy himself that Mr Stubbings was not unreasonably exposing himself to the significant financial risks accompanying the loans.

4 The learned trial judge erred in finding at [282] that AJ Lawyers took 'deliberate steps … to ensure that they did not ascertain any information about Mr Stubbings' financial circumstances and his ability to service the loan', when:

(a) no such case was pleaded, opened or advanced by the Respondent;

(b) no such proposition was put to Mr Jeruzalski, the principal of AJ Lawyers who had conduct of the loan matter on behalf of the Applicants and who gave evidence at trial;

(c) Mr Jeruzalski's relevant evidence was to the effect that he did not seek information about financial circumstances and serviceability because his clients' lending decisions were based on the sufficiency of the offered security; his evidence was accordingly that the gathering of such information was unnecessary, not that he deliberately avoided obtaining it.

5 The learned trial Judge erred in finding at [312] that:

(a) 'under the system of conduct that AJ Lawyers adopted, Mr Jeruzalski knowingly and deliberately failed to make any inquiries about Mr Stubbings and whether Mr Zourkas had misled him about Mr Stubbings' ability to service the loans, about Mr Stubbings' understanding of the loans, or about Mr Stubbings' financial nous and vulnerability; and

(b) Mr Jeruzalski knowingly and deliberately failed to make those inquiries 'because he was concerned that, or suspected that, the answers he may have received would have given him information that could form the basis for setting the loans aside on the grounds of unconscionability, and thus preventing his making the loans on behalf of the lenders' (see also the finding at [58] that 'I understood from his evidence that he would prefer not to know these things in case his knowledge would in some way undermine his clients' ability to recover their loans' –

in circumstances where:

(a) there was no duty on Mr Jeruzalski to make any such inquiries;

(b) the Respondent did not plead, open or put to Mr Jeruzalski when he gave evidence at trial that he should have made such inquiries, nor that his reason

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for doing so was as so found by his Honour; and

(c) Mr Jeruzalski gave no such evidence.

6 The learned trial judge erred in finding at [313] that 'the system of conduct' that AJ Lawyers adopted in the circumstances demonstrated a high degree of moral obloquy'.

7 The learned trial Judge erred in finding at [313] that Mr Jeruzalski 'gave evidence that, in his eyes, AJ Lawyers' business model immunised them and their clients from the breach of equity to protect the likes of Mr Stubbings', when in fact Mr Jeruzalski gave no such evidence.

8 The learned trial Judge erred in finding at [314] that Mr Jeruzalski's conduct in requiring Mr Stubbings to obtain legal and accounting advice and requiring certificates from a solicitor and an accountant, knowing or suspecting that Mr Stubbings would be guided by Mr Zourkas as to which solicitor and accountant to approach, was 'part of a system of conduct adopted by AJ Lawyers to immunize the firm from knowledge that might threaten the enforceability of the loan', when:

(a) such requirements are reasonable, prudent and common;

(b) had the lenders or their solicitors sought to direct or control Mr Stubbings as to who to approach, then the requirement of independence would be compromised. It was accordingly a matter for Mr Stubbings as to who to approach, including as to whether or not to accept any recommendation by Mr Zourkas;

(c) it was not necessarily the case that the solicitor and accountant would be paid only if the loans went ahead, nor (even if that were so) that the independence of professional persons would thereby be compromised.

9 The learned trial Judge erred in finding at [315] that there was 'wilful blindness' by AJ Lawyers as to Mr Stubbings' financial and personal circumstances, and at [316[[sic] that 'Asset-based lending coupled with the system of conduct adopted by AJ Lawyers, leads me to conclude that AJ Lawyers must be treated as knowing of Mr Stubbings' personal and financial circumstances.'

10 Further or alternatively, the learned trial Judge erred in finding at [317] that the loan, first mortgage and guarantee was 'procured by unconscionable conduct', in circumstances where:

(a) the transaction was introduced to the Applicants by Mr Jeruzalski, to whom it was introduced by Mr Zourkas;

(b) the Applicants did not know, and had no reason to suspect, that either Mr Zourkas or Mr Jeruzalski had behaved unconscionably;

(c) the Applicants did not 'procure' the transaction at all; rather

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they were approached for a loan by a corporate borrower whose director had entered into an unconditional contract to purchase a property and required funds to complete that purchase;

(d) the borrower and mortgagor had received independent legal and financial advice, and had provided certificates to that effect to the Applicants;

(e) the Applicants had no reason to doubt the contents of those certificates;

(f) there was no inequality of bargaining power;

(g) the transaction was, on its face, beneficial to the Respondent given that he had already entered into an unconditional contract to purchase a property, had been unable to obtain bank finance to complete the purchase, and was seeking finance to complete the purchase to avoid the adverse financial consequences of defaulting on the purchase; and

(h) there was nothing about the transaction which would have indicated to the Applicants that Mr Stubbings was, or may have been, under any special disadvantage in entering into the transaction; and of his second Judgment in the premises, there was no moral obloquy on the part of the Applicants.

11 Further or alternatively, the learned trial Judge erred in imputing to the Applicants any unconscionable conduct by, or constructive knowledge of, Mr Jeruzalski of AJ Lawyers where, if Mr Jeruzalski entertained any concern as to Mr Stubbings' ability to service the mortgage, he did not convey any such concern to the Applicants.

12 The learned trial Judge erred in the reasons for Judgment in finding, further or alternatively in placing an emphasis or relevance as to the issue of unconscionability upon his finding, at [10] that Mr Zourkas 'provided [services] to [AJ Lawyers] to assist in making the loan', and at [11] that '[t]he service provided by Mr Zourkas to AJ Lawyers is essential to the way AJ Lawyers conducted its loan business with those introduced by Mr Zourkas, as it avoids AJ Lawyers dealing directly with the borrower and the guarantor, and thus assists in immunising AJ Lawyers from being tainted with any knowledge of the financial and personal circumstances of the guarantor and the borrower', when:

(a) Mr Zourkas did not 'provide' any 'service' to AJ Lawyers, but was merely (in connection with his own business as a broker, and as agent for potential borrowers) one of many sources of introduction of borrowers to client lenders of AJ Lawyers;

(b) no such case was pleaded, opened or pursued by the Respondent at trial; and

(c) no such case was put to Mr Jeruzalski when he gave evidence

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at trial.

13 The learned trial Judge erred at [266] in finding that Mr Stubbings was under a special disadvantage in giving the guarantee and mortgages, in that:

(a) the matters identified by his Honour do not amount to a special disadvantage; further or alternatively

(b) the Applicants were not on notice of such matters.

74 Grounds 14 to 16, and 18 seek to challenge the form of the final orders setting aside the first mortgage on certain conditions. Ground 17 raised an issue about indefeasibility of title, which was abandoned on the hearing of the appeal.

Did the first mortgagees act unconscionably?

Applicable Law: unconscionable conduct in equity

75 The equitable doctrine of unconscionable conduct was summarised by Nettle and Gordon JJ in *Australian Securities and Investments Commission v Kobelt*[112] in the following terms:

> Relief under the doctrine of unconscionable conduct requires that the innocent party was subject to a special disadvantage in dealing with the other party when the transaction was entered into, 'which seriously affect[ed] the ability of the innocent party to make a judgment as to [their] own best interests'; and that the other party unconscientiously took advantage of that special disadvantage. The existence of those circumstances at the time of the transaction is what 'affect[s] the conscience' of the stronger party and renders the enforcement of the transaction, or the taking of the benefit, 'unconscientious' or 'unconscionable'.
>
> It is not possible to identify exhaustively what amounts to a special disadvantage. However, the essence of the relevant weakness is that it 'seriously affects' the innocent party's ability to safeguard their own interests. Relevant matters may include, but are not limited to, 'poverty or need of any kind, sickness, age, sex, infirmity of body or mind, drunkenness, illiteracy or lack of education, lack of assistance or explanation where assistance or explanation is necessary'; as well as 'illness, ignorance, inexperience, impaired faculties, financial need or other circumstances' that affect the innocent or weaker party's ability to protect their own interests. It is not sufficient that the matters give rise only to an inequality of bargaining power.

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112 (2019) 368 ALR 1; (2019) 93 ALJR 743; [2019] HCA 18 ('*Kobelt*').

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A party will have unconscientiously taken advantage of an innocent party when the former knew or ought to have known of the existence and effect of the special disadvantage; or, put another way, when the special disadvantage was sufficiently evident at the time of the transaction to make it unconscientious to procure or accept the assent of the innocent party.

Unconscionable conduct does not require a finding of dishonesty. However, it is not merely concerned with what is 'fair' or 'just'. Unconscionable conduct can include the passive acceptance of a benefit in unconscionable circumstances. And unconscionable conduct can be found even where the innocent party is a willing participant, the question is how that willingness or intention to participate was produced.

As this Court has recognised and restated a number of times, invocation of equitable doctrines, including unconscionable conduct:

> calls for a precise examination of the particular facts, a scrutiny of the exact relations established between the parties and a consideration of the mental capacities, processes and idiosyncrasies of the [weaker party]. Such cases do not depend upon legal categories susceptible of clear definition and giving rise to definite issues of fact readily formulated which, when found, automatically determine the validity of the disposition. ... [']A court of equity takes a more comprehensive view, and looks to every connected circumstance that ought to influence its determination upon the real justice of the case'.[113]

Applicable law: statutory unconscionability

76 Section 12CB of the *Australian Securities and Investments Commission Act 2001* (Cth) ('ASIC Act') provides, in part:

> **Unconscionable conduct in connection with financial services**
>
> (1) A person must not, in trade or commerce, in connection with:
>
> (a) the supply or possible supply of financial services to a person (other than a listed public company); or
>
> (b) the acquisition or possible acquisition of financial services from a person (other than a listed public company);
>
> engage in conduct that is, in all the circumstances, unconscionable.
>
> …
>
> (3) For the purpose of determining whether a person has contravened subsection (1):
>
> (a) the court must not have regard to any circumstances that were

113 Ibid 37–9 [146]–[150] (emphasis added) (citations omitted).

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not reasonably foreseeable at the time of the alleged contravention; and

(b) the court may have regard to conduct engaged in, or circumstances existing, before the commencement of this section.

(4) It is the intention of the Parliament that:

(a) *this section is not limited by the unwritten law* of the States and Territories relating to unconscionable conduct; and

(b) this section is capable of applying to a system of conduct or pattern of behaviour, whether or not a particular individual is identified as having been disadvantaged by the conduct or behaviour; and

(c) in considering whether conduct to which a contract relates is unconscionable, a court's consideration of the contract may include consideration of:

(i) the terms of the contract; and

(ii) the manner in which and the extent to which the contract is carried out; and is not limited to consideration of the circumstances relating to formation of the contract.

…[114]

77 Section 12CC(1) of the ASIC Act provides:

12CC Matters the court may have regard to for the purposes of section 12CB

(1) Without limiting the matters to which the court may have regard for the purpose of determining whether a person (the supplier) has contravened section 12CB in connection with the supply or possible supply of financial services to a person (the service recipient), the court may have regard to:

(a) the relative strengths of the bargaining positions of the supplier and the service recipient; and

(b) whether, as a result of conduct engaged in by the supplier, the service recipient was required to comply with conditions that were not reasonably necessary for the protection of the legitimate interests of the supplier; and

(c) whether the service recipient was able to understand any documents relating to the supply or possible supply of the

114 Emphasis added.

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financial services; and

(d) whether any undue influence or pressure was exerted on, or any unfair tactics were used against, the service recipient or a person acting on behalf of the service recipient by the supplier or a person acting on behalf of the supplier in relation to the supply or possible supply of the financial services; and

(e) the amount for which, and the circumstances under which, the service recipient could have acquired identical or equivalent financial services from a person other than the supplier; and

(f) the extent to which the supplier's conduct towards the service recipient was consistent with the supplier's conduct in similar transactions between the supplier and other like service recipients; and

(g) if the supplier is a corporation—the requirements of any applicable industry code (see subsection (3)); and

(h) the requirements of any other industry code (see subsection (3)), if the service recipient acted on the reasonable belief that the supplier would comply with that code; and

(i) the extent to which the supplier unreasonably failed to disclose to the service recipient:

(i) any intended conduct of the supplier that might affect the interests of the service recipient; and

(ii) any risks to the service recipient arising from the supplier's intended conduct (being risks that the supplier should have foreseen would not be apparent to the service recipient); and

(j) if there is a contract between the supplier and the service recipient for the supply of the financial services:

(i) the extent to which the supplier was willing to negotiate the terms and conditions of the contract with the service recipient; and

(ii) the terms and conditions of the contract; and

(iii) the conduct of the supplier and the service recipient in complying with the terms and conditions of the contract; and

(iv) any conduct that the supplier or the service recipient engaged in, in connection with their commercial relationship, after they entered into the contract; and

(k) without limiting paragraph (j), whether the supplier has a contractual right to vary unilaterally a term or condition of a contract between the supplier and the service recipient for the

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supply of the financial services; and

(l) the extent to which the supplier and the service recipient acted in good faith.

78 Unconscionable conduct under s 12CB(1) of the ASIC Act 'is not limited by the unwritten law',[115] a clear reference to the equitable doctrine of unconscionable conduct. That does not mean that the equitable doctrine ceases to have any relevance as, although the 'statutory conception of unconscionability is more broad-ranging' than the equitable principles, the equitable principles still have a significant part to play in ascribing meaning to the term 'unconscionable' under s 12CB(1).[116]

79 Like equity, s 12CB of the ASIC Act requires a focus on 'all the circumstances' of the case.

80 There have been many decisions which have grappled with the content of the various statutory prohibitions against unconscionable conduct, and whether they set a 'lower bar' than unconscionable conduct in equity. The most recent pronouncements by the High Court are to be found in *Kobelt*, where the Court split four to three on the application of the facts to the relevant principles and did not speak with one voice as to the content of the relevant principles. *Kobelt* was far divorced from the circumstances of this case, involving whether Kobelt's system of providing 'book-up credit' to impoverished and often illiterate and innumerate Aboriginal customers involved unconscionable conduct in contravention of s 12CB(1).

81 Kiefel CJ and Bell J (in the majority) described the exercise to be undertaken as an 'evaluative judgment',[117] to be undertaken on the facts of the specific case at hand, as to whether the conduct in question was 'against conscience'.[118] They determined

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115 Section 12CB(4)(a) of the ASIC Act.

116 *Kobelt* (2019) 368 ALR 1, 37; (2019) 93 ALJR 743; [2019] HCA 18, [144] (Nettle and Gordon JJ), referring to *Paciocco* (2015) 236 FCR 199; 321 ALR 584; [2015] FCAFC 50, [283].

117 Ibid 15 [47].

118 Ibid 15 [48].

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that the book-up system was not unconscionable because it did not involve Kobelt exploiting or otherwise taking advantage of the customers' lack of education or financial acumen, due to the long history of book-up credit in rural and remote indigenous communities.[119] This approach was consistent with Kiefel CJ and Bell J applying the equitable principles. In their Honours' view, that was what was required in the circumstances, because that was what ASIC had contended:

> The first feature is that ASIC's case, below and in this Court, is that unconscionable conduct involves 'the existence of a special [dis]advantage of which someone takes ... [u]nconscientious advantage' and that Mr Kobelt's conduct in supplying credit under his book-up system took unconscientious advantage of the vulnerability of his Anangu customers.[120]

82 Thus, in their Honours' view:

> In the circumstances, the appeal does not provide the occasion to consider any suggestion that statutory unconscionability no longer requires consideration of (i) special disadvantage, or (ii) any taking advantage of that special disadvantage.[121]

83 It can thus be seen that Kiefel CJ and Bell J did not make any pronouncement as to the content of the statutory prohibition against unconscionable conduct in s 12CB(1) of the ASIC Act. They decided the case on the obviously correct basis that, if conduct is unconscionable in equity, it will also be unconscionable under s 12CB(1). Keane J (also in the majority) agreed with Kiefel CJ and Bell J as to the approach to be taken given ASIC's contentions.[122] The remaining four judges did not take such a narrow view of ASIC's case. They considered that the content of the statutory prohibition against unconscionable conduct in s 12CB(1) of the ASIC Act was central to ASIC's case that Kobelt's book-up system contravened that section.

84 Gageler J (in the majority) directly addressed the issue. He stated that, while

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119 Ibid 2 [79].

120 Ibid 15 {48] (citations omitted).

121 Ibid (citation omitted).

122 Ibid 30–3 [117]–[123], especially at [119]: '[ASIC] did not propound a meaning for "unconscionable" different from its ordinary meaning; and so [Mr Kobelt] had no occasion or opportunity to meet such a contention.'

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s 12CA simply imposes an additional 'statutory sanction' on unconscionable conduct in equity,[123] s 12CB 'does something more', as its prohibition is expressed in s 12CB(1) and(4)(a) to be 'not limited by the unwritten law'.[124] In Gageler J's view, the 'correct perspective'[125] is that stated by the Full Court of the Federal Court in *Australian Competition and Consumer Commission v Lux Distributors Pty Ltd*,[126] which he described as follows:

> s 12CB operates to prescribe a normative standard of conduct which the section itself marks out and makes applicable in connection with the supply or possible supply of financial services. The function of a court exercising jurisdiction in a matter arising under the section is to recognise and administer that normative standard of conduct. The court needs to administer that standard in the totality of the circumstances taking account of each of the considerations identified in s 12CC if and to the extent that those considerations are applicable in the circumstances.[127]

85 As the 'normative standard' was expressed in the terminology of courts administering equity, Gageler J stated that the prohibition in s 12CB signifies 'the gravity of the conduct necessary to be found by a court in order to be satisfied of a breach of that standard';[128] and emphasised that 'behaviour is only unconscionable where there is some real and substantial ground based on conscience for preventing a person from relying on what are, in terms of the general law, that person's legal rights'.[129] On this basis, while accepting that unconscionable conduct under s 12CB is 'unconfined to conduct that is remediable on that basis by a court exercising jurisdiction in equity',[130] Gageler J considered that the normative standard in s 12CB does not authorise a court 'to dilute the gravity of the equitable conception of

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123 Ibid 22 [82].

124 Ibid 22-3 [83].

125 Ibid 24 [87].

126 [2013] FCAFC 90, [23], [41] ('*Lux Distributors*').

127 *Kobelt* (2019) 368 ALR 1, 24; (2019) 93 ALJR 743; [2019] HCA 18, [87].

128 Ibid 24 [88].

129 Ibid, quoting from *Burt v Australia & New Zealand Banking Group Ltd* (1994) ATPR (Digest) 46–123 at 53, 598.

130 Ibid 23 [83].

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unconscionable conduct so as to produce a form of equity-lite'.[131] However, contrary to views he had expressed in *Paciocco v Australia & New Zealand Banking Group Ltd*,[132] Gageler J rejected his previous statement, accepting earlier authority,[133] that unconscionable conduct within the meaning of s 12CB required 'a high level of moral obloquy'. On reflection, his Honour considered that such 'arcane terminology does nothing to elucidate the normative standard embedded in the section'.[134]

86 Gageler J summarised the statutory standard to be applied in s 12CB cases as requiring proof in all the circumstances that the conduct in question is 'so far outside societal norms of acceptable commercial behaviour as to warrant condemnation as conduct that is offensive to conscience';[135] noting that for a court to pronounce conduct as unconscionable under s 12CB involves a heavy onus in reaching the conclusion that the conduct is 'offensive to a conscience informed by a sense of what is right and proper according to values which can be recognised by the court to prevail within contemporary Australian society'.[136]

87 Nettle and Gordon JJ (in the minority) also drew attention to s 12CB(4)(a) and stated that unconscionable conduct under s 12CB was not limited by the equitable principles governing unconscionable conduct under the 'unwritten law'.[137] In their Honours' view, reference to the non-exhaustive list of relevant factors in s 12CC, to be considered in all the circumstances of a particular case in order to determine whether conduct is unconscionable under s 12CB(1), 'necessarily implies that the statutory conception of unconscionability is more broad-ranging than that of the unwritten law;' but the unwritten law nevertheless has a significant part to play in

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131 Ibid 24 [90].

132 (2016) 258 CLR 525, 587 [188] ('*Paciocco*').

133 *Attorney-General (NSW) v World Best Holdings Ltd* (2005) 63 NSWLR 557, 583 [121] ('*World Best Holdings*').

134 *Kobelt* (2019) 368 ALR 1, 25; (2019) 368 ALR 1; (2019) 93 ALJR 743; [2019] HCA 18, [91].

135 Ibid 25 [92].

136 Ibid 25 [93].

137 Ibid 37 [144].

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ascribing meaning to the term 'unconscionable' under s 12CB(1).'[138]

88 Nettle and Gordon JJ stated that the non-exhaustive list of factors in s 12CC provides 'express guidance as to the norms and values that are relevant to inform the meaning of unconscionability and its practical application'.[139] These factors, they considered, assisted 'in setting a framework for the values that lie behind the notion of conscience identified in s 12CB'.[140] Later, their Honours said that, in considering whether there has been unconscionable conduct in the particular circumstances of a given case:

> The assessment of whether conduct is unconscionable within the meaning of s 12CB involves the evaluation of facts by reference to the values and norms recognised by the statute, and thus, as it has been said, a normative standard of conscience which is permeated with accepted and acceptable community standards.[141] It is by reference to those generally accepted standards and community values that each matter must be judged.[142]

89 Edelman J (also in the minority) agreed with the reasons of Nettle and Gordon JJ, both as to the statutory standard to be applied and its application to the facts.[143]

90 In our view, putting aside the differing views as to the facts of the case, the issue of principle as to the content of the statutory standard to be applied in assessing whether conduct is, in all the circumstances, unconscionable within the meaning of s 12CB(1) of the ASIC Act is that stated by Gageler, Nettle, Gordon and Edelman JJ. In summary, although only Gageler J was in the majority — and thus the consistent statements of the four judges represent obiter dicta — it is dicta which has obviously

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138 Ibid, referring to the Full Federal Court decision in *Paciocco* (2015) 236 FCR 199, 271 [283].

139 *Kobelt* (2019) 368 ALR 1, 40; (2019) 368 ALR 1; (2019) 93 ALJR 743; [2019] HCA 18, [154], referring to the Full Federal Court decision in *Paciocco* (2015) 236 FCR 199, 270 [279] and 276 [306], and to *Lux Distributors* [2013] FCAFC 90, [23].

140 Ibid, referring to the Full Federal Court decision in *Paciocco* (2015) 236 FCR 199, 272 [285], 276 [304]; and *Commonwealth Bank of Australia v Kojic* (2016) 249 FCR 421, 436 [58] (Allsop CJ), 442 [87] (Edelman J).

141 *Lux Distributors* [2013] FCAFC 90; (2013) ATPR 42-447, at 43,463 [23], cited in *Paciocco* (2015) 236 FCR 199, 275 [298].

142 *Kobelt* (2019) 368 ALR 1, 54; (2019) 368 ALR 1; (2019) 93 ALJR 743; [2019] HCA 18, [234] (citation in original).

143 Ibid 62 [268].

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been seriously considered and should be followed and applied by this Court until the High Court says otherwise.[144] The applicable standard is a normative one involving the evaluation of whether the conduct in question is 'so far outside societal norms of acceptable commercial behaviour as to warrant condemnation as conduct that is offensive to conscience';[145] in the sense that a court should only take the serious step of denouncing conduct as unconscionable when it is satisfied that the conduct is 'offensive to a conscience informed by a sense of what is right and proper according to values which can be recognised by the court to prevail within contemporary Australian society'.[146] The evaluation exercise is informed by the non-exhaustive list of factors in s 12CC.[147]

91 As previously noted, before the decision in *Kobelt*, intermediate appellate authority was to the effect that there could be no statutory unconscionable conduct within the meaning of legislation such as s 12CB unless a 'high level of moral obloquy' or other 'moral taint' was established.[148] Further, before rejecting this terminology, Gageler J himself had accepted it as a governing criterion in *Paciocco*.[149] This was the position when the trial judge decided this case and, as he was required to do, he considered whether the conduct at issue was infected with moral obloquy, and found that it was. In doing so, the judge considered earlier cases concerning allegations of unconscionable conduct where there was asset-based lending. There was no error in that approach. That said, we accept that the effect of *Kobelt* is that the previously accepted arcane terminology of 'moral obloquy' should no longer be used. But the requirement that the conduct in question be 'so far outside societal

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144 *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* (2007) 230 CLR 89, 150; [2007] HCA 22, [134] ('*Farah Constructions*').

145 *Kobelt* (2019) 368 ALR 1, 25; (2019) 93 ALJR 743; [2019] HCA 18, [92] (Gageler J), 54 [234] (Nettle and Gordon JJ), 62 [268] (Edelman J).

146 Ibid 25 [93] (Gageler J), 54 [234] (Nettle and Gordon JJ), 62 [268] (Edelman J).

147 Ibid 24 [87] (Gageler J), 40 [154] (Nettle and Gordon JJ), 62 [268] (Edelman J).

148 For example, *World Best Holdings* (2005) 63 NSWLR 557, 583 [121]; *Scully* [2013] VSCA 292; *Tonto* [2011] NSWCA 389, [293].

149 (2016) 258 CLR 525, 587 [188].

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norms of acceptable commercial behaviour as to warrant condemnation as conduct that is offensive to conscience'[150] should still be understood as requiring an evaluative judgment as to the morality of the allegedly unconscionable behaviour.

92 It follows that, while searching for a differently expressed criterion of liability for unconscionable conduct, the earlier cases concerning unconscionable conduct under statute in the context of asset-based lending continue to be relevant. In substance, the requisite criterion of liability has been rebadged in terms of the normative standard expressed in *Kobelt*.

93 However, it is important to note the statement of this Court in *Schmidt* that:

> little is to be gained by a close factual analysis of the myriad of cases that have considered whether particular conduct was unconscionable. Whilst there are sometimes factual similarities between the cases, inevitably there are differences. Similarly, we do not find it of assistance to consider whether conduct is unconscionable simply because of the type of lending that is involved, for example, asset based lending. Rather, the task requires a more synthesised approach which takes into account all of the facts relevant to the impugned conduct and determines whether, in all the circumstances, that particular conduct is unconscionable.[151]

94 That is not to say, however, that the fact that a loan involves asset-based lending is irrelevant to the inquiry as to whether, in all the circumstances of the case the lending was unconscionable. This is because, of its very nature, asset-based lending carries with it the structural risk that the focus on the loan to security value ratio may overwhelm other relevant circumstances known to the lender which may demonstrate that the borrower is under a special disadvantage or it is otherwise unconscientious to lend on the terms of a particular loan.

First mortgagees' contentions

95 In general, the grounds of appeal contend that the unconscionability finding — both in equity and under statute — was not open on the evidence as a whole and the

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150 *Kobelt* (2019) 368 ALR 1, 25; (2019) 93 ALJR 743; [2019] HCA 18, [92].

151 *Violet* (2013) 44 VR 202, 219 [59]; *Schmidt* [2013] VSCA 56, [59].

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pleaded issues for determination. The first mortgagees contend that 'mere' or 'pure' asset-based lending is not, by itself, unconscionable unless there is something about the particular transaction which, in all the circumstances of the case, makes it so.[152] The first mortgagees contend that the trial judge erred in finding that — because the AJ Lawyers' system of lending involving deliberate abstention from inquiry was applied in this case, notwithstanding Jeruzalski's knowledge of matters which should have put him on inquiry — this case went beyond mere asset-based lending. Specifically, the grounds of appeal contend that particular findings of fact, inferences and conclusions of the judge were erroneous when considered in light of the evidence as a whole.

96 The first mortgagees' contentions involved the following steps.

97 First, the first mortgagees emphasise that there is no evidence that Jeruzalski was told by Stubbings, Zourkas or anyone else that Stubbings had no income, or insufficient income, to service the loans for at least six months, and possibly 12 months, pending the sale of the two Narre Warren properties. The lengthy exchange from Jeruzalski's evidence at Reasons [92], quoted above,[153] when read as a whole discloses only that Jeruzalski assumed that Stubbings had 'no income' in the sense that he could not demonstrate to a bank or other financial institution that he had sufficient income or that he had financial records, including tax returns, to establish that he did. The primary judge in fact held only that Jeruzalski 'suspected that Mr Stubbings would not have the income to service the loans'.[154]

98 Second, the first mortgagees contend that the trial judge erred in his characterisation of the 'system' of lending adopted by AJ Lawyers in its application to Mr Stubbings as involving:

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152 For example, *Kowalczuk* (2008) 77 NSLWR 205, 227–8 [96]–[99]; *Tonto* [2011] NSWCA 389, [3], [291]-[293];*Violet* (2013) 44 VR 202, 219–20 [59]; *Schmidt* [2010] VSC 67, [200], [207] (J Forrest J).

153 At [56] of these reasons.

154 Reasons [310].

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(1) the taking of 'deliberate steps … to ensure that they did not ascertain any information about Mr Stubbings's financial circumstances and his ability to service the loan';[155]

(2) deliberately failing 'to make any inquiries about Mr Stubbings and whether Mr Zourkas had misled [Mr Jeruzalski] about Mr Stubbings's ability to service the loans, about Mr Stubbings's understanding of the loans, or Mr Stubbings's financial nous and vulnerability … because he was concerned that, or suspected that, the answers he may have received would have given him information that could form the basis for setting aside the loans on the grounds of unconscionability, and thus preventing his making the loans on behalf of the lenders';[156]

(3) 'a high level of moral obloquy',[157] because it was designed and viewed by Jeruzalski as 'immunising' his clients 'from a breach of equity to protect the likes of Mr Stubbings';[158]

(4) a requirement for certificates of independent legal and accounting advice in circumstances where Jeruzalski 'suspected that Mr Stubbings would be guided by Mr Zourkas as to which solicitor and accountant to approach … as part of the system of conduct adopted by AJ Lawyers to immunise the firm from knowledge that might threaten the enforceability of the loan'.[159]

The first mortgagees contend that this erroneous characterisation of the system and its application to Stubbings 'infected the judge's approach' to the determination of whether the first mortgagees, through Jeruzalski, had engaged in unconscionable conduct towards Stubbings.

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155 Ibid [282], [312]; appeal ground 4.

156 Ibid [312]; appeal ground 5.

157 Ibid [313]; appeal ground 6.

158 Ibid; appeal ground 7.

159 Ibid [314]; appeal ground 8.

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99 The first mortgagees contend that there is nothing unconscientious about AJ Lawyers' system. The system involved no more than making asset-based loans available on a 'take it or leave it basis' to companies which did not have sufficient income, or financial records to demonstrate sufficient income, to service the loan — particularly where the loan is a short-term loan pending asset sales and refinance. In that regard, they contend that the loans offered by AJ Lawyers fulfil a legitimate demand by persons who, for whatever reason, cannot obtain finance from banks and other lending institutions at lower interest rates and choose to accept 'third tier' loans of the kind offered. In that regard, they rely upon the decision of the High Court in *Paciocco*,[160] where the High Court found that bank fees charged to customers on a 'take it or leave it basis' were not unconscionable.[161] They rely also on *Kobelt*, where the practice of book-up credit, which the customers chose to accept — but which 'would be patently unacceptable conduct elsewhere in modern Australian society' — was held to be not unconscionable in the particular circumstances of the case.[162]

100 The first mortgagees also contend that the system did not involve any deliberate failure to inquire. The system was designed for asset-based lending, where all that the proposed lenders required was that the loan be to a company, so that the Code did not apply, and that there be a valuation acceptable to them. In circumstances where it is obvious that the borrower will be a company which is unable to provide sufficient evidence of income to satisfy a bank of its ability to service the proposed loan, there is nothing unconscionable in only seeking valuation information and thus engaging in pure asset-based lending. As to the fact that the letters of offer included terms that the proposed loans to the company were conditional on the provision of satisfactory evidence of serviceability,[163] the first mortgagees contend that this

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160 (2016) 258 CLR 525.

161 Ibid.

162 *Kobelt* (2019) 368 ALR 1, 29 [110] (Gageler J).

163 Clauses (y) and (z) of the two letters of offer for the first and second mortgages. See [16(5)] above.

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standard condition was for their protection and not to protect the borrower — and assert, on the basis of Jeruzalski's evidence, that the condition appears to have been routinely waived unless there was some special reason to enforce it.

101 Third, the first mortgagees contend that the mere fact that Jeruzalski suspected that Stubbings did not have sufficient income, or evidence of income, to obtain a loan from a bank or other financial institution was not sufficient to put him on inquiry — in the absence of which he was 'wilfully blind' and knowledge of Stubbings's personal and financial circumstances should be attributed to him.[164] They contend that the trial judge erred in holding that Jeruzalski's assumption or suspicion that Stubbings did not have sufficient income to service the loans enlivened a 'moral duty to satisfy himself that Mr Stubbings was not unreasonably exposing himself to the significant financial risks accompanying the loans',[165] particularly where Jeruzalski was a practising solicitor, was erroneous[166] — as was his related finding that Jeruzalski had 'moral and ethical obligations … to obtain information on Mr Stubbings's ability to service the loans' but deliberately chose not to do so.[167] Moreover, they contend that the trial judge was in error when he held that Jeruzalski 'knew that the loans were a risky and dangerous undertaking to Mr Stubbings [because] as a solicitor practising in the area of making loans on behalf of his clients … [h]e would have known that if Mr Stubbings defaulted in payment, then the cost and hardship that the loan agreements would impose on Mr Stubbings would be substantial'.[168]

102 In support of their contention that Jeruzalski had not been put on inquiry as to Stubbings's personal and financial circumstances, the first mortgagees contend that there was no reason for Jeruzalski to think that Stubbings — with the benefit of

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164 Appeal grounds 2, 3, 9, 10 and 11.

165 Reasons [309].

166 Appeal ground 3.

167 Reasons [310].

168 Ibid [308].

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advice from Zourkas, an independent solicitor (Kiatos) and an independent accountant (Topalides) — was not fully aware of the risks and did not have some plan to obtain sufficient money to pay the interest pending sale of the two Narre Warren properties and refinance of the remaining balance of the loans at that time. For example, Stubbings may have had other assets to sell or family resources to call upon to tide him over. Moreover, Stubbings admitted in his evidence that Kiatos had told him that the loans were 'high risk' and that the 'interest is fairly high'. In all the circumstances, the first mortgagees contend that there was nothing irregular or unusual about the asset-based lending in this case, and thus contend that it is distinguishable from other cases where asset-based lending has been held to be unconscionable — such as *Schmidt*[169] and *Elkofairi*.[170]

103 Finally, on wilful blindness issues, appeal ground 11 was explained in oral argument as, perhaps clumsily, contending that, in circumstances of proposed asset-based lending, there was no requirement for Jeruzalski to inform the first mortgagees that he suspected Mr Stubbings did not have sufficient income to service the loans pending the proposed sale of the two Narre Warren properties.

104 Fourth, to the extent that the trial judge's Reasons involved him accepting that the fact Stubbings did not have sufficient income to service the loan meant that it was inevitable that there would be a mortgagee sale — and that Stubbings would thus lose a substantial part of his equity in the Narre Warren properties in payment of procuration fees, consultancy fees, high interest and selling costs — the first mortgagees contend that the judge was in error, as such a scenario was a mere 'backstop' as with every loan on the security of a mortgage. There was nothing about the transaction to indicate that the first mortgagees intended such a result. Rather, they should be taken to have intended that Stubbings would pay interest for at least six months, until the Narre Warren properties were sold, and that the loans

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169 *Violet* (2013) 44 VR 202; *Schmidt* [2010] VSC 67.

170 [2002] NSWCA 413.

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would then be refinanced and they would be paid in full. The first mortgage was simply there to protect them in case Stubbings was unable to realise his plans.

105 Fifth, the first mortgagees challenge the proposition underlying the judge's Reasons that there was no benefit to Stubbings in entering into the loans, because default was inevitable. They emphasise that Stubbings was in a financial predicament of his own making before AJ Lawyers became involved. He had committed to the first contract of sale, which had become unconditional, and after renegotiation of the price he had entered into an unconditional contract of sale under which he had only paid $100 as a deposit (although recorded in the contract as $5,100). He was liable, in any event, for the full amount of the deposit. In these circumstances, not proceeding with the loans would have led to a 'disastrous' result for Stubbings in that he would be liable for the balance of the deposit — $76,410 if the $5,000 is taken into account or $81,410 if it is not — and would still be liable for Zourkas's $27,000 fee under the terms of the mandate.

106 Sixth, the first mortgagees contend that the trial judge was in error in finding that Stubbings was under a special disability in his dealings with the first mortgagees, and that even if he was under such a disability, they did not have sufficient knowledge of any such special disability.[171]

107 Seventh, the first mortgagees contend that the trial judge did not, for the purposes of considering statutory unconscionability under s 12CB(1) of the ASIC Act, give any consideration to the non-exclusive list of factors in s 12CC. When regard is had to those factors, they contend that none of them supports a finding of unconscionability in the circumstances of this case.[172] Specifically, they contend:

(1) There was no inequality of bargaining power between the first mortgagees and Stubbings. He simply chose to enter into the loans on the security of his

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171 Appeal ground 13.

172 Appeal ground 10.

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properties.[173]

(2) There was no allegation or finding that the terms of the loans or the first mortgage were not reasonably necessary for the protection of the first mortgagees' legitimate interests.[174]

(3) There was no suggestion that Stubbings was unable to understand the documents which he executed. It is immaterial that he may have been misled by Zourkas, who was not the agent of the first mortgagees.[175]

(4) There is no evidence of any undue influence, pressure or unfair tactics adopted by the first mortgagees or their agents, AJ Lawyers.[176] Indeed, neither AJ Lawyers nor the first mortgagees 'procured' the loan. They simply responded to an approach by Stubbings, through his agent Zourkas, for finance and offered finance on a take it or leave it basis.

(5) There is no evidence that Stubbings could have obtained a loan at a cheaper rate or on better terms than those which were offered by the first mortgagees.[177]

108 Eighth, the first mortgagees contend that the basis on which the trial judge found unconscionability was not pleaded by Stubbings and was not put to Jeruzalski in cross-examination. In those circumstances, they contend that it was procedurally unfair to find his conduct — and thus the first mortgagees' conduct — unconscionable. In particular, the first mortgagees contend that the judge's findings, based on the system of lending involving moral obloquy and wilful blindness, and that Stubbings was under a special disadvantage, were not pleaded or put.

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173 Section 12CC(a).

174 Section 12CC(b).

175 Section 12CC(c).

176 Section 12CC(d).

177 Section 12CC(e).

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109 Ninth, the first mortgagees contend that the trial judge ought to have exercised greater caution before making the grave finding of 'unconscionable conduct' concerning a transaction which was and is commonplace in the community and provides a valuable service to those who cannot obtain finance from banks or other finance providers. In effect, a 'reverse floodgates argument' was put, namely, that if the trial judge's decision is upheld it will have the effect of putting an end to asset-based 'mortgage lending practices' by solicitors — which have been commonplace and viewed in the community as a legitimate means of obtaining finance for decades, if not longer.

Stubbings's contentions

110 Stubbings contends that no error in the trial judge's reasons has been demonstrated. He emphasises that the question of whether someone has engaged in unconscionable conduct is always a factual question, to be answered having regard to all the circumstances of the particular case, and that the trial judge's decision should be given particular weight where it involves the making of a broad evaluative judgment on the basis of all the circumstances of the case.

111 In essence, Stubbings contends that the case is a simple one. The first mortgagees lent him and his company far beyond their capacity to repay. He was bound to lose the two Narre Warren properties and the Fingal property from the moment the transaction completed because he had no income or other means of servicing the loan, and this would have been obvious to Jeruzalski had he made the inquiries which ought to have been made by him given his knowledge at the time. But these inquiries were not made because, under the AJ Lawyers' system of lending, Jeruzalski was not interested in making any such inquiries for fear of what he might learn. That conduct is properly described as being contrary to the normative standard of acceptable commercial behaviour as stated in *Kobelt*. This is particularly so in circumstances where Jeruzalski, as agent for the first mortgagees, had the contractual power to require that Stubbings and the company provide proof of their

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plans to service and repay the loans as a condition of making them — but chose not to exercise that power notwithstanding facts known to Jeruzalski which called for inquiry.

112 Stubbings places particular reliance on the decision of the New South Wales Court of Appeal in *Elkofairi* and the decision of this Court in *Violet*; each of which he contends supports the general proposition that it is unconscionable to engage in asset-based lending if the circumstances of the case put a lender on inquiry as to whether the borrower has the capacity to service the loan, or to repay the loan other than by a sale of the security property or properties. He contends that the AJ Lawyers' system of lending, as applied in this case, was correctly characterised by the trial judge as involving 'wilful blindness' and thus a high level of moral obloquy — a finding which more than satisfied the normative standard expressed in *Kobelt* for statutory unconscionable conduct.

Analysis

113 It is first necessary to consider whether the authorities relied upon by Stubbings should be applied to the circumstances of this case. As noted, he places principal reliance on the New South Wales Court of Appeal decision in *Elkofairi*,[178] where the leading judgment was delivered by Beazley JA. Mr and Mrs Elkofairi were the joint proprietors of their home in Castle Hill, subject to a mortgage to St George Bank which was in arrears. Mr Elkofairi forged Mrs Elkofairi's signature on a loan application to Aussie Home Loans, seeking a loan sufficient to pay out the St George Bank mortgage and for additional funds of $350,000 for business purposes. The loan application was assessed by another company, Queensland State Home Loans, which recommended approval of the loan to Permanent Trustee Co Ltd as lender. The pro forma loan application form required Mr and Mrs Elkofairi to set out their assets and liabilities and a statement of their income. Mr Elkofairi disclosed that the

178 [2002] NSWCA 413.

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Castle Hill property was worth $1.2 million and that he owned a motor vehicle worth $40,000, but disclosed no other assets. The only liability disclosed was the amount owing to St George Bank. The income section of the form was left blank.

114 Queensland State Home Loans recommended the loan to Permanent Trustees on the basis that there had been an independent valuation and a 'credit check on each loan applicant'. The 'credit check' appears to have been the obtaining of three letters from Mr Elkofairi's accountant in support of the loan application. The letters stated variously that Mr Elkofairi was 'an honest and reliable person', the accountant was 'not aware of any factors which may affect [Mr Elkofairi's] ability to make the repayments or which may cause substantial hardship to [him] to make repayments', and that the accountant knew Mr Elkofairi's income, expenditure and financial position and was of the opinion that Mr Elkofairi would be 'able to repay the loan in accordance with its terms and can do so without hardship'. None of the letters referred to Mrs Elkofairi's position, and the accountant did not purport to act for her or know anything of her financial affairs.

115 In fact, the accountant's letters were erroneous. At the time of making the loan application, Mr and Mrs Elkofairi each owed about $25,000 in tax, had failed to honour a debt reduction arrangement reached with the ATO, they were being pressed to repay the St George Bank mortgage loan, and St George Bank had commenced proceedings for possession of the Castle Hill property.

116 Mrs Elkofairi was obviously under a special disadvantage. She was completely uneducated and could not read or write in either her first language of Arabic or in English. She could not understand spoken English except for a very few simple expressions. Her husband was domineering, non-consultative about family decisions, aggressive and intimidating. She signed documents at his request without him giving her any explanation as to what they were for. She suffered ill-health and was on a disability pension. Although she had obtained an apprehended violence order against her husband at one time, and had lived in a women's refuge for a period of six weeks, she continued to live with her husband because she knew that,

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under the standards applying in her community, she would lose her status with her children if she did not.

117 The loan and mortgage documents were sent by Permanent Trustees' solicitors to Mr and Mrs Elkofairi at the Castle Hill property. The documents included two pro forma documents, namely: (1) an 'Acknowledgement as to not receiving legal advice'; and (2) a 'Schedule One Solicitor's Certificate' which was to be signed if legal advice was received. Mrs Elkofairi signed the documents in the presence of a solicitor. Although the trial judge accepted the solicitor's evidence as credible, on his own evidence the solicitor did not explain to Mr and Mrs Elkofairi that, if the loan was not repaid, the mortgagee could sell the Castle Hill property. Mr and Mrs Elkofairi elected to sign the 'Acknowledgement as to not receiving legal advice', which was in the following terms:

> I acknowledge that:
>
> 1. The Mortgagee has advised me to take independent legal advice before signing the Mortgage, and I have had an opportunity to do so.
>
> 2. I have chosen not to take independent legal advice on the nature and effect of the Mortgage.
>
> 3. I have read and understood the nature and effect of the Mortgage.
>
> 4. I have signed the Mortgage freely and voluntarily.

118 When default was made under the loan, the mortgagee brought proceedings against Mr and Mrs Elkofairi for possession of the Castle Hill property. Mrs Elkofairi denied that the mortgagee was entitled to enforce the mortgage against her on three grounds: (1) the principles stated in *Yerkey v Jones*;[179] (2) unconscionable conduct in equity, relying on *Amadio*;[180] or (3) the *Contracts Review Act 1980* (NSW).

119 The mortgagee was successful at trial. On appeal, it was held that the *Yerkey v Jones* defence was not made out in the circumstances of the case.[181] Beazley JA then

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179 (1939) 63 CLR 649.

180 (1983) 151 CLR 447.

181 *Elkofairi* [2002] NSWCA 413, [38]–[49] (Beazley JA), [87] (Santow JA), [112] (Campbell AJA).

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considered the equitable defence that the mortgage was procured by unconscionable conduct of the mortgagee. There was no issue that Mrs Elkofairi was under a special disadvantage. The issue was whether Mrs Elkofairi's special disadvantage was sufficiently evident to the mortgagee.[182] Beazley JA concluded that in all the circumstances, notwithstanding that the mortgagee and its agents did not have any actual knowledge of Mrs Elkofairi's special disadvantage, the total absence of financial information as to the business purpose of the loan and the fact that no income was stated for either Mr or Mrs Elkofairi:

> should certainly have sounded a warning bell to a lender in respect of any borrowing, let alone a borrowing in the order of three quarters of a million dollars. In addition, there were the added factors that the respondent was aware that the appellant did not have legal advice in respect of the mortgage. Nor did it have any information as to her ability, existing or prospective, to service the loan.[183]

120 Beazley JA continued:

> 56 In my opinion, notwithstanding that the respondent did not have knowledge of the appellant's lack of education and her language and domestic difficulties, her lack of income, in the circumstances of this transaction – that is a large borrowing secured over her only asset, in circumstances where the application form failed to disclose any income for either husband or wife – placed her in a special position of disadvantage. *Though the full extent of that special position of disadvantage was not known to the respondent, nonetheless the absence of any relevant financial information was sufficient to put the respondent on notice of the appellant's lack of capacity to meet the repayment obligations under the mortgage. That left as the only source of repayment the selling of her only asset, as again the respondent must be taken to have known.*
>
> 57 Counsel for the respondent submitted that the respondent did not need to be concerned with the fact that the borrowers, or the appellant at least, had no income. It was sufficient for its purposes that the loan was amply secured. That was a position, according to the respondent, which the respondent was entitled to take. I do not agree. In fact, it demonstrates the unconscientious nature of the transaction and the advantage the respondent took of the appellant's disadvantageous position. *On its own submission, the respondent was only concerned with its ability to recoup any amount outstanding on the loan in circumstances where it must be taken to have known, because on the only information the respondent had, the appellant had no income, that the appellant, who was*

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182 Ibid [51]–[53].

183 Ibid [55].

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> *exposed to liability for the whole of the loan, had no ability to make even the first payment. The unconscientious nature of the transaction was that she was thereby at risk of losing her only asset. That risk was both immediate and real.*
>
> 58 It is no answer that the respondent was content with the transaction because the loan was well secured. Nor is it an answer that the respondent had assurances from Mr Elkofairi's accountants of his ability to repay. Even if it could be said that the respondent was entitled to assume that the husband would bear the liability for the repayments (an assumption which I do not consider is available), the vagueness and unparticularised nature of the accountant's letters were not sufficient, in this case, to entitle the respondent to make the assumption that the lending to the appellant was not unconscientious.
>
> 59 *In my opinion, therefore, it was unconscientious for the respondent to lend a large sum of money to a person with no income with full knowledge that if the repayments under the loan were not met, it could sell that person's only asset.*[184]

121 Stubbings contends that this case is relevantly indistinguishable from *Elkofairi* and, moreover, that *Elkofairi* stands for a general principle that it is unconscionable for a lender to engage in asset-based lending when it knows that the borrower has no income from which to service the loan, or has any reason to doubt the capacity of the borrower to service the loan, unless full inquiries are first made and the lender is satisfied that the borrower will be able to do so.

122 In our view, *Elkofairi* stands for no such general principle. If it does, we would respectfully say that it is clearly wrong; as it would amount to stating a principle of law that asset-based lending is, by itself, unconscionable. As appears above, that is contrary to the weight of other intermediate appellate authority and is inconsistent with the requirement, in both equity and under statute, that the serious finding that someone has acted unconscionably depends upon a close examination of all the facts of the particular case.

123 In our view, Beazley JA was not stating any such general principle but was considering a particular submission in the context of the facts of the case that there was no need for the mortgagee to inquire further because 'it was sufficient for its

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184 Ibid [56]–[59] (emphasis added).

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purposes that the loan was amply secured'. In the context of the facts of *Elkofairi*, that submission was bound to fail — and Beazley JA was right to reject it. But the facts in *Elkofairi* are far divorced from those in this case. Here, Stubbings suffered none of the profound disabilities of Mrs Elkofairi. He was in control of his own affairs and could well speak and read English. He owned other assets, including the two Narre Warren properties. As far as Jeruzalski was aware, Stubbings had received legal advice and signed an 'Acknowledgement by Guarantor' which stated that he understood the loan and mortgage documents and the consequences if there was a default. Moreover, Kiatos had signed a 'Certificate by Independent Solicitor' stating that: 'In particular, I explained and advised [Stubbings] on the consequences of default under the relevant Security Documents, including the Lender/Mortgagee's right to sell the property constituting the security'. The lender in *Elkofairi* did not have the benefit of such acknowledgement or certificate.

124 Stubbings also relies on *Violet*.[185] However, the facts in *Violet* are distinguishable from this case. In that case, the agent of the lender, Violet Home Loans, engaged in unconscionable conduct. Here, the unconscionable conduct of Zourkas is not to be attributed to the first mortgagees, because Zourkas was not their agent. This case is closer to the facts in *Tonto*,[186] where the unconscionable conduct was committed by a loan introducer (Streetwise) which was not the agent of the lender. In those circumstances, the unconscionable conduct of Streetwise was not attributed to the lender.

125 In *Tonto*, a lender engaged a mortgage originator (Tonto) to find and introduce borrowers. In turn, Tonto used a sub-introducer (Streetwise) to find and introduce borrowers to it. The conduct of Streetwise was undoubtedly unconscionable, including by making fraudulent representations to borrowers that they could meet their obligations to repay the loans. Streetwise was not Tonto's agent. Accordingly,

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185 (2013) 44 VR 202.

186 [2011] NSWCA 389.

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its state of mind and conduct could not be attributed to Tonto, or the lender as Tonto's principal.[187] In these circumstances, Allsop P emphasised the need to focus on the actual states of mind and conduct of the persons who were alleged to have acted unconscionably: the lender and Tonto. Neither Tonto nor the lender was aware of Streetwise's offending conduct until after the loans had been made. Nor was there any direct unconscionable conduct by the lenders or Tonto. In these circumstances, Allsop P held that it was not unconscionable for the lender to maintain and enforce the loan transaction.[188] This was notwithstanding criticisms of the lender's and Tonto's conduct, concerning the failure to adhere to their own lending guidelines and the 'structural creation of risk' by using Streetwise as a sub-introducer.[189]

126 We turn to consider AJ Lawyers' system of lending. The trial judge described and characterised AJ Lawyers' system of arranging asset-based loans as agent for its clients as one involving a deliberate intention to neither seek nor receive information as to the personal and financial circumstances of the borrowers; and held that the purpose of the system was to protect (or 'immunise') the lenders from claims that the loans should be set aside as unconscionable. In our view, that is a description of 'pure' or 'mere' asset-based lending. Given the state of the prevailing law — that asset-based lending is not, by itself, unconscionable conduct —[190] especially when combined with the fact that the system of lending included a requirement for certificates of independent legal and accounting advice, the trial judge's general characterisation of this system of asset-based lending as involving moral obloquy or being unconscionable as that term is now understood was in error. We generally accept the first mortgagee's contentions in this respect. The judge's adverse view of the system of lending — in substance an adverse view of asset-based lending as a

187 *Tonto* [2011] NSWCA 389, [287], [288], [291].

188 Ibid [292].

189 Ibid.

190 For example, *Kowalczuk* (2008) 77 NSLWR 205, 227–8 [96]–[99]; *Tonto* [2011] NSWCA 389, [3], [291]-[293]; *Violet* (2013) 44 VR 202, 219–20 [59]; *Schmidt* [2010] VSC 67, [200], [207] (J Forrest J).

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concept — overwhelmed (or as the first mortgagees contend 'infected') his determination of the unconscionability issue.

127 It follows that the real question in this case is whether the trial judge correctly held that Jeruzalski had knowledge of facts which ought to have put him on inquiry as to Stubbings's personal and financial circumstances, including details of the company's assets and business. In considering the trial judge's findings on this issue, we have conducted a 'real review' of the evidence in light of the applicable principles. We accept that an appeal court should not interfere with a judge's findings of primary fact unless they are demonstrated to be wrong by 'incontrovertible facts or uncontested testimony', or they are 'glaringly improbable' or 'contrary to compelling inferences'.[191] There is a distinction with respect to appellate review findings of inferences where: 'in general an appellate court is in as good a position as the trial judge to decide on the proper inference to be drawn from facts which are undisputed or which, having been disputed, are established by the findings of the trial judge'.[192] We are also mindful that 'considerable caution' should be observed in disturbing a trial judge's finding of unconscionable conduct because it represents a judicial conclusion to 'the application to a mass of evidence of a legal standard expressed in broad statutory language'.[193]

128 Although the trial judge did not expressly say so, it is clear from his acceptance that recklessness, in the form of wilful blindness, may constitute unconscionable conduct that the judge had in mind the third category of knowledge from the formulation of Peter Gibson J in *Baden v Société Générale pour Favouriser le Développment du Commerce et de l'Industrie en France SA*,[194] which was in the following

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191 *Robinson Helicopter Company Inc v McDermott* (2016) 331 ALR 550, 558–9 [43].

192 *Lee v Lee* [2019] HCA 28, [55] (citations omitted).

193 *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd* (2003) 214 CLR 51, 86 [82]-[83] (Kirby J); *Australian Competition and Consumer Commission v Samton Holdings Pty Ltd* (2002) 117 FCR 301, 319 [51].

194 [1993] 1 WLR 509, 575-6 [250] ('*Baden*'); approved in *Farah Constructions* (2007) 230 CLR 89, 163–4 [171]–[178].

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terms:

(1) actual knowledge;

(2) wilfully shutting one's eyes to the obvious;

(3) wilfully and recklessly failing to make such inquiries as an honest and reasonable person would make;

(4) knowledge of circumstances which would indicate the facts to an honest and reasonable person; and

(5) knowledge of circumstances which would put an honest and reasonable person on inquiry.

129 In *Farah Constructions*, the High Court accepted that the third *Baden* category of knowledge was a species of 'actual knowledge, as understood both at common law and in equity'.[195] The fourth and fifth *Baden* categories of knowledge represents constructive knowledge.[196]

130 In this case, we are not satisfied that Jeruzalski knew of matters which should have put him on inquiry. He did not wilfully and recklessly fail to make such inquiries as an honest and reasonable lender would make in the circumstances, or at least have knowledge of circumstances which would put an honest and reasonable lender on inquiry. Jeruzalski should not be treated as having actual or constructive knowledge of Stubbings's personal and financial circumstances and the fact that the company had no assets, had never conducted business and did not immediately intend to do so.

131 At the time Jeruzalski approved the loans on 19 September 2015, the matters known to Jeruzalski concerning the ability of Stubbings and the company to service

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195 *Farah Constructions* (2007) 230 CLR 89, 163 [174].

196 Ibid.

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the loans for between six and 12 months pending refinance following a sale of the Narre Warren properties were — putting the case at its highest for Stubbings — as follows:

(1) Jeruzalski assumed that Stubbings and the company had 'no income', in the sense that they did not have sufficient income to service interest under the loans for between six and 12 months.

(2) Jeruzalski knew that Stubbings and the company had paid only a token deposit under the two contracts to purchase the Fingal property — $100 under the first contract (in force when the loan offers were made) and $5,100 under the second contract (in force when the loans were approved). This supported Jeruzalski's assumption that Stubbings and the company had insufficient income to service the loans.

(3) Jeruzalski had been informed by Zourkas that the proceeds of the two loans would be used to both settle the purchase of the Fingal property and to pay out the existing CBA mortgage loans over the two Narre Warren properties; and that Stubbings's plan was to then sell the two Narre Warren properties and then refinance the loans with a bank. Jeruzalski gave evidence that he treated Stubbings's equity in these properties as his deposit on the Fingal property.

(4) From the disbursement authorities prepared by his office at the time the loans were approved, Jeruzalski knew that — after settlement of the Fingal property purchase, repayment of the mortgages over the Narre Warren properties, and the payment of all costs and expenses including loan procuration fees and commissions — the net proceeds of the loans available to Stubbings and the company for any business purposes would be very small in comparison to the amount borrowed.[197]

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[197] In fact, only $16,360 was available, and that decreased to about $7,000 once it was realised that Stubbings had a substantial debt for unpaid rates on the Narre Warren properties, and had

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(5) Jeruzalski had been told by Zourkas that Stubbings and the company intended to conduct a 'business concerned with boat repairs' at the Fingal property.[198]

(6) Jeruzalski knew that he, as agent of the mortgagees, had the right under conditions (y) and (z) of the letters of offer to demand that Stubbings and the company provide 'evidence of serviceability' or evidence of 'proposed means of repayment of the loans' but chose not to exercise that right before approving the loans.

132 If these were the only matters known to Jeruzalski at the time the loans were approved, they may have been sufficient to justify the serious finding that it was unconscionable for him to abstain from inquiry in all the circumstances. But they were not the only matters. Jeruzalski well knew and relied on the fact that, as part of the system of lending, the loan approvals were conditional on the company and Stubbings obtaining independent legal and accounting advice and for the two certificates he had prepared to be signed and returned before the loans were made. Signed certificates were in fact returned to him. In our view, Jeruzalski was entitled to rely on the certificates — both as evidence that Stubbings had consulted a solicitor and an accountant for advice and as to the truth of the matters stated in the certificate. On that basis, Jeruzalski should not be fixed with knowledge of Stubbings' personal and financial circumstances such that default under the loans was inevitable, as the trial judge appears to have found.

133 We conclude that the certificates, especially the accountant's certificate, made it

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not paid the fees of Kiatos and Topalides. These amounts were paid from the settlement proceeds.

198 We note that in cross-examination by Stubbings, Jeruzalski said that he knew that the Fingal property was zoned 'green wedge' — and a permit or exemption was required to conduct a business from it. Jeruzalski said he assumed that such a permission could be obtained and that a business could be conducted from the large shed depicted in photographs of the Fingal property in the valuation. However, Jeruzalski's evidence about the green wedge was not referred to in submissions before the trial judge, is not referred to in the Reasons, and no written or oral submissions were directed to it on appeal.

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reasonable for Jeruzalski to refrain from inquiry as to how the company and Stubbings intended to, or whether they could in fact, service the loans pending refinance following sale of the two Narre Warren properties. In reaching that conclusion, we have been mindful that the judge inferred that:

> Mr Jeruzalski *must have suspected* that Mr Stubbings would be guided by Mr Zourkas as to which solicitor and accountant to approach. *I see this conduct as part of the system* of conduct adopted by AJ Lawyers to immunise the firm from knowledge that might threaten the enforceability of the loan. *As far as Mr Jeruzalski was concerned*, the accountant and the solicitor would only be paid if the loans went ahead. There was no incentive for them to withhold the certificates. If they withheld the certificates, then they would receive nothing for their services. *To characterise them as independent is perhaps a bridge too far*.[199]

134 In our view, those inferential findings, and the 'bridge too far' comment are not supported by the evidence. No basis for the inferred suspicion is given. No basis is given for the inference that the suspected conduct was 'part of the system'. The disbursement authorities enclosed with the two approval letters made no mention of the fees due to Kiatos and Topalides coming from the loan proceeds, and their fees were not deducted at settlement. It was only after settlement that their fees were paid from the $16,360 remaining in the AJ Lawyers trust account – after authorisation from Stubbings.

Conclusion and orders

135 For the reasons given above, we conclude that the appeal against the trial judge's unconscionability finding should be allowed, the trial judge's orders should be set aside, and it should be ordered instead that: (1) there be judgment for the first mortgagees for possession of the Fingal property; and (2) Stubbings's counterclaim be dismissed. In these circumstances, it is unnecessary to consider whether the orders made by the trial judge on the basis of his unconscionability finding were appropriate in all the circumstances and, given the basis of the orders has been

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199 Reasons [314] (emphasis added).

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rejected, we will not do so in any detail.[200] In our view, however, on the basis that there was unconscionable conduct as found by the judge, the judge ought to have fixed the amount payable by Stubbings to the first mortgagees by including Stubbings's liability for the balance of the deposit due by him if he did not complete the purchase of the Fingal property in accordance with the second contract of sale. Practical justice demanded that he account to the first mortgagees for that benefit arising from the first mortgage loan transaction.

136 We will hear the parties as to the form of orders and as to costs.

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200 *Boensch v Pascoe* [2019] HCA 49, [7]–[8], [101].

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SCHEDULE OF PARTIES

JAMS 2 PTY LTD (ACN 600 173 117)	First Applicant
CONTERRA PTY LTD (ACN 078 900 017)	Second Applicant
JANACO PTY LTD (ACN 006 209 105)	Third Applicant
- and -	
JEFFREY WILLIAM STUBBINGS	Respondent

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