Supreme Court

New South Wales

Case Name:	Oak Capital Mortgage Fund Limited v Dlakic
Medium Neutral Citation:	[2019] NSWSC 1538
Hearing Date(s):	2-4 September 2019
Decision Date:	7 November 2019
Jurisdiction:	Common Law
Before:	Fullerton J
Decision:	1. Judgment for the plaintiff. 2. An order for possession of the property known as XX, Randwick in the State of New South Wales. 3. Leave to enter judgment forthwith. 4. Leave to apply for a writ of possession forthwith. 5. The Court notes the plaintiff's undertaking signed by Kathryn Lauren Brann, solicitor, a full copy of which in annexed to the copy of the judgment retained in the Court file. 6. The defendants to pay the plaintiff's costs.
Catchwords:	MORTGAGES AND SECURITIES — mortgages — duties, rights and remedies of mortgagee – default on mortgage – whether mortgagee entitled to possession of land – leave granted to issue writ of execution CONTRACTS —cross-claim — general contractual principles — harsh, unconscionable or oppressive contracts and statutory remedies – whether higher interest rate under loan agreement amounted to a contractual penalty – whether contract unjust for purposes of s 9(1) of the Contracts Review Act– no relief granted
Legislation Cited:	Contracts Review Act 1980 (NSW) Real Property Act 1900 (NSW)

Cases Cited:	ACES Sogutlu Holdings Pty Ltd (in liq) v Commonwealth Bank of Australia (2014) 89 NSWLR 209; [2014] NSWCA 402 Andrews v Australia and New Zealand Banking Group Ltd (2012) 247 CLR 205; [2012] HCA 30 Arab Bank Australia Ltd v Sayde Developments Pty Ltd (2016) 23 NSWLR 231; [2016] NSWCA 328 Bank of Western Australia Ltd v Tannous [2010] NSWSC 1319 Elkofairi v Permanent Trustee Co Ltd [2002] NSWCA 413 Jones v Dunkel (1959) 101 CLR 298; [1959] HCA 8 King Investment Solutions Pty Limited v Hussain (2005) 64 NSWLR 441; [2005] NSWSC 1076 Kowalczuk v Accom Finance (2008) 77 NSWLR 205; [2008] NSWCA 343 Paciocco v Australia & New Zealand Banking Group Ltd (2016) 258 CLR 525; [2016] HCA 28 Perpetual Trustee Co Ltd v Khoshaba [2006] NSWCA 41 Provident Capital Ltd v Papa (2013) 84 NSWLR 231; [2013] NSWCA 36 Qantas Airways v Cameron (1996) FCR 246; [1996] FCA 349 Quantum Asset Management Pty Ltd v Love Properties (WA) Pty Ltd [2017] WASC 167 West v AGC (Advances) Ltd (1986) NSWLR 610
Category:	Principal judgment
Parties:	Oak Capital Mortgage Fund Limited (Plaintiff) Kasim Dlakic (First Defendant) Hamida Dlakic (Second Defendant)
Representation:	Counsel: AW Smith / E Keynes (Plaintiff) J Cohen (Defendants) Solicitors: Summer Lawyers (Plaintiff) MJ Woods & Co Solicitors (Defendants)
File Number(s):	2018/263201
Publication Restriction:	Nil

JUDGMENT

1 **HER HONOUR**: By an amended statement of claim filed in accordance with orders made by Davies J on 26 February 2019, Oak Capital Mortgage Fund Ltd (the plaintiff) seeks an order for possession of land at XX, Randwick (the Randwick Property). Consequential orders for leave to issue a writ of possession and costs assessed on an indemnity basis are also sought. No money order is sought.

2 Kasim Dlakic and his wife Hamida Dlakic (the first and second defendants) are the registered proprietors of the Randwick Property which they hold as joint tenants. They have been the registered proprietors of the Randwick Property since 1989. It is their primary residence.

3 The plaintiff claims an entitlement to an order for possession of the Randwick Property (and consequential orders) by enforcing a guarantee and indemnity dated 28 December 2017 provided by each of the defendants in respect of a loan advanced by the plaintiff to Beachview Australia Pty Ltd (Beachview) in the amount of $1,193,594. The guarantees and indemnities were secured by a registered mortgage granted by each of the defendants against the Randwick Property. The mortgage incorporated two schedules executed by the first and second defendants as directors of Beachview which had the effect of incorporating into the mortgage Beachview's obligations as borrower under the loan agreement with the plaintiff.

4 As at 28 December 2017, the first and second defendants were the directors and beneficial shareholders of Beachview. They were appointed as directors of the company on 13 November 2017. They ceased to be directors on 18 November 2018.

5 Upon settlement of the loan to Beachview, two registered mortgages over the Randwick Property to AMP Bank Limited (AMP) and Peter and Eve Vince in the total amount of $1,030,737.52 were discharged. A caveat lodged by a commercial debtor (Commlend Securities Pty Ltd) for "security fees" in the amount of $69,284.55 was also withdrawn. Of the balance of loan monies, $59,441 was paid to the plaintiff. This represented six months of prepaid

interest. The remaining $8,537 was paid into the first defendant's bank account.

6 Pursuant to Schedule A to the mortgage, Beachview was obliged to make monthly interest payments of 9.9% over the term of the loan (being 12 months). Interest was also to be paid on the 28th day of each consecutive month, commensurate with the commencement date of the loan by 28 December 2017. A higher interest rate of 19.5% applied in the event of an act of default. A failure to make interest payments as required under the mortgage was a specified event of default.

7 Beachview failed to make the first monthly interest payment due and payable under the mortgage on 28 June 2018 (the first six months of interest having been prepaid on settlement) and has made no repayments at any time since.

8 On 5 July 2018, the plaintiff issued a letter of demand to Beachview and to each of the defendants as guarantors. No effort was made on the part of Beachview or the defendants to remedy the default. Neither Beachview nor the defendants contacted the plaintiff to address the issue of default or to challenge the validity of the default notice.

The proceedings and the pleadings

9 On 27 August 2018, the plaintiff commenced proceedings against the defendants as guarantors of Beachview's loan obligations by filing a statement of claim. On 4 October 2018 default judgment was entered in favour of the plaintiff.

10 On 29 November 2018, the defendants successfully moved to have the default judgment set aside.

11 In the further amended defence filed on 22 March 2019 (which, as with the amended statement of claim, was filed in accordance with orders made by Davies J), the defendants deny any liability to the plaintiff and deny the plaintiff has an enforceable mortgage over the Randwick Property. They also maintain that the default notice issued on 5 July 2018 was invalid because interest was not due and payable by Beachview until six months after settlement monies were paid. Since settlement of the loan occurred on 16 February 2018, it is the

defendants' contention that interest was not due and payable until 16 August 2018 and, accordingly, the plaintiff was not entitled to call on the guarantee or to seek an order for possession of the Randwick Property. The defendants also contend that the loan to Beachview is unenforceable because the interest rate provided for in the event of default is a penalty provision and contrary to law.

12 Finally, in answer to the whole of the plaintiff's claim, the defendants contend that "the loan, guarantees and mortgage" were unfair and unjust within the meaning of s 9 of the *Contracts Review Act 1980* (NSW) and that they should be set aside pursuant to s 7 the Act.

13 The same relief is sought in the cross-claim filed by the first and second defendants. In the cross-claim the relief under the *Contracts Review Act* is further particularised as follows:

> 13. The loan and mortgage were against the public interest because:
>
> (i) The Defendants had demonstrated an inability to reasonably protect their own interest;
>
> (ii) The security was the sole residence of the Defendants;
>
> (iii) The Plaintiff was content to lend on the strength of the security alone;
>
> (iv) In making the loan and taking the mortgage the Plaintiff participated in a system which involved the lending of funds to borrowers (including the first and second defendant) with no capacity to repay other than through the forced sale of her residence or through equally unjust refinancing;
>
> (v) The Plaintiff was willing to lend on the value of the security and was indifferent to the purpose of the loan.
>
> 14. There was material inequality in the bargaining power of the cross-claimants and the plaintiff.
>
> 15. The Plaintiff did not reasonably believe that the cross-claimants had adequate comprehension of the obligations they were undertaking.
>
> 16. The provisions of the agreement pursuant to which the loan was advanced were not the subject of negotiation between the parties at the time it was entered into.
>
> 17 It was not reasonably practicable for the cross-claimants to negotiate for the alteration of, or to reject, any provisions of the agreement pursuant to which the loan was advanced.
>
> 18. The consequence of non-compliance with all or any of the provisions of the mortgage was to entitle the Plaintiff to possession of the cross-claimant's only substantial asset being their home.

19. The consequence of compliance with the provisions of the mortgage and the loan it secures was to require the cross-claimant at the end of the term of the loan to either:

(i) Obtain new finance and incur further application, establishment, broking, legal, valuation and other fees; or

(ii) Sell their home at the end of the term of the loan to repay the principal.

20. At the time of entering into the loan contract and mortgage the Plaintiff knew or could have ascertained that the cross-claimants could not pay in accordance with its terms or not without substantial hardship.

21. The provisions of the loan contract and mortgage and their legal and practical effect were not properly explained to the cross-claimants.

22. By reason of speaking poor English the cross-claimants were unable to understand the various provisions of the contractual and mortgage material presented to them nor the effect of those provisions.

23. There was substantial disparity between the literacy of the parties.

24. The mortgage and loan documents were not adequately intelligible.

14 On the first day of the hearing the defendants' counsel sought leave to further amend the defence by claiming an entitlement to equitable relief on the basis that it would be unconscionable to allow the plaintiff's claim where the plaintiff took advantage of its grossly superior bargaining position viz the defendants and their known "disabilities". Leave was granted to further amend the defence to allow a claim for equitable relief on terms that the particulars of the plaintiff's unconscionable conduct were limited to those pleaded in support of the claim for relief under the *Contracts Review Act* at paragraphs 16(a)-(m) of the filed defence (paragraph (l) was withdrawn and paragraph (h) not agitated at the hearing), namely:

(a) There is a clear inequality between the parties in education, language, and knowledge of the transaction.

(b) The provisions of the loan were not subjected to any negotiations.

(c) The loan was not a genuine commercial loan.

(d) The loan was secured against the residential property of the defendants

whom were both pensioners, illiterate and had a limited understanding of English.

(e) The plaintiff knew or ought to have that the defendants had no means to repay the loan.

(f) The plaintiffs knew or ought to have known the loan was being used to refinance a loan secured against the property located at XX, Randwick and accordingly took advantage of the defendants [sic] grossly inferior bargaining position.

(g) The plaintiffs knew or ought to have known the defendants were facing the imminent prospect of having their home repossessed at the time and as such,

the loan contained harsh and opportunistic terms: a high interest rate of 9% (in relation to what was a loan to prevent a residential property from being repossessed); an extortionate rate of 19.5% pa interest in the event of any "default"; and excessive fees

(i) The plaintiff knew or ought to have known the company set up by the defendants had no assets and was not a genuine trading company.

(j) The plaintiff knew or should have known that the defendants were illiterate in the English language.

(k) The defendants given their language problems, lack of financial education and financial position, the defendant's lack of competent legal representation.

(m) The defendants plead that having regard to the public interest the loan was unjust within the meaning of s 9 of the *Contracts Review Act 1980*.

15 In the plaintiff's defence to the cross-claim, including the claim for relief under the *Contracts Review Act,* the plaintiff put in issue the defendants' illiteracy and incapacity to understand English, together with the assertion that there was a "material inequality in their bargaining power", including that "the defendants" had no capacity "to repay the loan" and that it "knew" that Beachview "had no assets" is put in issue. The plaintiff/cross-defendant asserts it had the reasonable belief that the first and second defendants/cross-claimants had adequate comprehension of their obligations under the indemnities and guarantees entered into by each of them to secure Beachview's obligations as borrower under the loan agreement.

16 The plaintiff relies upon a "Guarantor Advice Declaration", executed by each of the first and second defendants/cross-claimants and furnished by their solicitor as part of the loan documents provided to the plaintiff's solicitor in which the defendants individually declared an understanding of the terms of the mortgage; their legal and financial liability under the mortgage; that they had obtained independent legal advice prior to executing the mortgage and that they understood that the provision of the mortgage would have a direct financial impact upon them in the event of Beachview's default under the loan agreement. The plaintiff/cross-defendant also relied upon Australian Legal Practitioner's Certificates executed by the defendants' solicitor, Mr Peter Nagle, on 28 December 2017 and 9 January 2018, also forwarded to the plaintiff's solicitor, in which he certified that he had explained the terms, nature and effect

of the guarantees that were to be entered into by each of the first and second defendants/cross-claimants, and that he satisfied himself that they understood the financial risks that were entailed in executing the guarantees. Mr Nagle gave evidence for the plaintiff.

17 The plaintiff/cross-defendant also contends that since the loan was advanced to Beachview as borrower, it was under no obligation as lender to assess whether the first and second defendants were "suitable borrowers".

18 The plaintiff/cross-defendant also contends that were the loan not advanced to Beachview, and were Beachview not to have made those funds available to meet the defendants' obligations under a Deed of Settlement with AMP as first registered mortgagee, the first and second defendants/cross-claimants would have remained liable to AMP for amounts owing to it, entitling AMP to enforce the default terms under the Deed of Settlement, inclusive of an order for possession of the Randwick Property.

The AMP mortgage/The AMP Deed of Settlement

19 On 29 June 2010, the defendants executed a mortgage over the Randwick Property in favour of AMP securing a loan to the defendants for "refinance of owner occupied property and other non-real estate investments". The principal loan of $880,000 was recorded on the mortgage. On the same date AMP drew a cheque in the amount of $685,290 made payable to the defendants and their sons, Amil and Edin.

20 On 5 August 2015, AMP issued a notice of default pursuant to s 57(2)B of the *Real Property Act 1900* (NSW) for arrears of interest in the amount of $20,089.76. The defendants failed to comply with the default notice and on 10 November 2015 AMP commenced proceedings seeking an order for possession of the Randwick Property. Those proceedings were settled on terms reflected in a Deed of Settlement, under which the defendants agreed to pay AMP the sum of $1,005,737.52 by 6 December 2017 in exchange for AMP agreeing to discontinue the proceedings. The Deed also provided that in the event that the terms of settlement were breached, AMP was entitled to apply to reinstate the proceedings with a view to obtaining a money judgment against the defendants and an order for possession of the Randwick Property.

The Commlend caveat

21 On 20 December 2017, Commlend Securities Pty Ltd (Commlend) registered a caveat on the title of the Randwick Property. The particulars of the interest of Commlend are described as "an equitable charge pursuant to charging provisions within the executed term sheet securing the fees of the caveator" created by virtue of an interim instrument styled as a "Term Sheet" dated 12 November 2017 between Commlend, Beachview and the defendants.

The identity of "Beachview" as borrower

22 Beachview was first registered on 22 June 2016 as a company limited by shares. According to the Australian Securities and Investments Commission (ASIC), the company's status as at the date of the hearing in September 2019 was "Deregistered". ASIC records also reveal the defendants were appointed as directors of the company on 13 November 2017 after their son, Amil Dlakic, ceased to be a director effective the same date.

The loan application

23 On 21 November 2017, the defendants signed a Finance Application Form issued by the plaintiff. The first defendant signed in his capacity as director of Beachview. The second defendant signed in her capacity as director/secretary of the company. In the same capacity they both signed a declaration to the effect that the loan funds, if advanced, would be applied wholly or predominantly for business and/or for investment purposes, namely "refinance".

24 The loan application was forwarded to the plaintiff's Business Development Manager from solicitors in Queensland. There is no evidence as to why Queensland solicitors were acting on behalf of Beachview whose business address is nominated as "c/ Entertaining Taxes Accountants Pty Ltd, 2/28 Bayswater Road Potts Point New South Wales" (the same entity being nominated as the accountant for Beachview), or any direct evidence as to the circumstances in which the defendants signed the application on Beachview's behalf. It would appear that John Hancock, a mortgage broker, was involved in the approach to the plaintiff as a commercial lender.

25 The Queensland solicitors had no further involvement in the matter beyond furnishing by email the completed Finance Application Form on Beachview's behalf, together with a number of what were described in the solicitor's covering letter as "supporting documents". Those documents included:

(1) Photocopies of the passport and drivers licence of the first and second defendants;

(2) An email dated 8 November 2017 from Mr Cromb, a senior associate with HWL Ebsworth, to Mr Andrew Wily, a director of Armstrong Wily Chartered Accountants, confirming that the first and second defendants intended to meet their obligations under Terms of Settlement and Release with AMP by 4pm on 6 December 2017 by payment of the settlement sum of $1,005.737.52 to be made by bank cheque payable to AMP. (It is clear this information was provided as a result of the defendants nominating the Randwick Property in the Finance Application Form as an asset subject to mortgage and under the general heading of "Solvency Inquiries" answering "yes" to a question as to whether arrangement was in place with a creditor to payout a current debt.);

(3) A letter dated 13 November 2017 from Entertaining Taxes Accountants addressed to Commlend Securities Re: Beachview Australia Ltd which reads as follows:

> To Commlend Securities
>
> To Whom It May Concern;
>
> I am the financial accountant for Beachview Australia Pty Ltd. I wish to verify that Beachview Australia Pty Ltd is borrowing the amount of $1,200,000 to pay out the investment loan with AMP Bank Ltd and the additional funds will be used to renovate the property at XX Randwick NSW for a future sale…

26 Finally, it should be noted that the solicitor's letter drew attention to a designated field in the Loan Application Form which concerned how the borrower intends to repay the loan, in which the solicitor emphasised that the "Sale of the Security" after loan funds were directed to the AMP settlement.

The formal letter of offer

27 On 29 November 2017, the plaintiff issued a formal offer of loan funding to Beachview for a loan term of 12 calendar months. The first and second defendants were named as guarantors of that loan.

28 The letter of offer provided that pre interest, capitalised for six months, was payable under the loan agreement after which interest and fees were to be paid monthly in advance. As noted earlier at [6], a higher and lower interest

rate was specified respectively, 9.9% per annum (payable in advance for the term of the loan) and 19.5% per annum, with the plaintiff having the right to charge interest at the higher rate in the event of an act of default.

29 The offer provided, inter-alia, that the purpose of the loan is “Refinance and Property Renovations”; the security for the loan was a first mortgage over the Randwick Property (and a registered charge over Beachview). In the field headed “Loan Takeout Method”, provision was made for copies of any documentation detailing how Beachview intended to repay the loan. None was provided or sought before settlement of the loan.

30 In the field entitled “Special Conditions and Requirements” the plaintiff specified that “proof of income be provided (three months trading statements, payslips, etc)” and in an additional field, entitled “Other Conditions”, the loan was said to be subject to the plaintiff receiving:

> satisfactory credit reports on the company and each of you together with all other information in the amount set out in this letter was subsequently requested…

31 Other than the supporting documents attached to the solicitor’s letter forwarding the Application for Loan Finance, and the emphasis in the covering letter that it was intended that the Randwick Property would be sold at the end of the loan term, there was no evidence adduced in proceedings bearing on the credit status of Beachview as borrower, or the credit status of the first and second defendants as guarantors of the loan and registered proprietors of the Randwick Property provided as security supporting their guarantee. Additionally, no evidence was adduced to suggest that information concerning the issue of the credit status of Beachview or the defendants as guarantors was sought by the plaintiff or provided by the first and second defendants before settlement of the loan.

32 The plaintiff’s counsel submitted that the fact there was no evidence to suggest that the plaintiff initiated any credit enquiries does not allow for the inference to be drawn that no enquiries were made. In addition, counsel submitted that the plaintiff was entitled to proceed on the understanding, as represented by the Queensland solicitors, that the loan monies were to be put on settlement to discharge the defendants’ obligations under the AMP Deed of Settlement after

which “the security” (being the Randwick Property) would be sold to facilitate the discharge of Beachview’s obligations as borrower within the 12-month loan term or on expiration of the term.

33 Counsel for the first and second defendants placed particular reliance on this feature of the arrangements under which the loan was advanced to support his submission that it was a classic form of “asset lending”, in the sense that despite the formal terms upon which the formal letter of offer issued, the plaintiff had no interest in making any assessment of the capacity of Beachview to meet its obligations as borrower, or of the capacity of the first and second defendants to guarantee Beachview’s obligations to make monthly instalments of interest during the last six months of the loan term. It was submitted that the plaintiff’s only interest was in the value of the security which, in the likely event of default, would entitle it to immediately move to realise all outstanding fees and charges under the loan agreement by seeking to recover the principal and an order for possession over the Randwick Property.

34 The characterisation of the contractual arrangements as one of “asset lending” and, for that reason, liable to be set aside as “unjust, harsh and unconscionable” under the *Contracts Review Act* or under the general law, was addressed in final submissions.

35 The first and second defendants initialled each page of the letter of offer as “Borrower and Guarantor”. In executing that part of the document entitled “Acceptance of the Loan Facility Offer” the first and second defendants, in their capacity as directors of Beachview as borrower, confirmed acceptance of the offer of finance (and that they had fully read and understood the terms of the loan facility) and, on their own behalf as guarantors of Beachview’s loan obligations, their understanding that they were guaranteeing Beachview’s obligations as borrower secured against the Randwick Property.

The role of the broker

36 Ashtons Commercial Finance Pty Ltd is nominated on the Finance Application Form in the field entitled “Your Broker”. This was the only field requiring a further signature from the first and second defendants confirming that the broker was their agent and does not represent the plaintiff in any capacity.

Further provision was made for the broker's fees to be paid on settlement unless other arrangements were made.

37 The evidence in the proceedings identified Mr Hancock as the mortgage broker. He was apparently connected, in some way, with Ashtons Commercial Finance Pty Ltd not revealed in the evidence.

38 The first and second defendants gave evidence that Mr Hancock introduced them to the plaintiff. Mr Nagle, their solicitor, also gave evidence that he was introduced to the defendants by Mr Hancock and that Mr Hancock was present during each of his conferences with them in the course of which he rendered advice as to the legal nature, force and effect of the various loan documents they executed on behalf of Beachview, and the various documents they executed as guarantors of Beachview's obligations under the loan. Mr Nagle attributed to Mr Hancock an explanation for why Beachview was the borrower of the funds which were to be committed to discharging the AMP mortgage over the Randwick Property under the AMP Deed of Settlement. Mr Hancock did not give evidence in the proceedings.

39 The plaintiff invited the Court to draw an inference, adverse to the defendants, in accordance with the principle in *Jones v Dunkel* (1959) 101 CLR 298; [1959] HCA 8 that Mr Hancock's evidence would not have assisted them in their defence to the plaintiff's claim; in particular, that his evidence would not have supported their claim to be unaware of the reason Beachview was borrowing funds to discharge the AMP mortgage; that they were not adequately advised or aware of the consequences of guaranteeing Beachview's performance of its obligations as borrower under the loan agreement; that the plaintiff would be entitled to seek an order for possession of the Randwick Property in the event of Beachview's failure to meet its obligation under the loan agreement, including by failing to make monthly interest repayments after the six months of pre-paid interest had been exhausted.

The evidence of witnesses called in the proceedings

40 The following affidavits were read:

For the plaintiff:

- Mr Peter Nagle (solicitor) affirmed 8 April 2019;
- Ms Elisabeth McGready (solicitor) affirmed 9 April 2019;
- Ms Kathryn Brann affirmed 2 November 2018;
- Ms Kathryn Brann affirmed 10 April 2019;
- Ms Kathryn Brann affirmed 31 August 2019;
- Ms Yasmin Hijazi affirmed 22 May 2019;
- Ms Yasmin Hijazi affirmed 31 August 2019;
- Ms Yasmin Hijazi affirmed 2 September 2019 (affidavit of service).

For the defendants:

- Ms Kasim Dlakic affirmed 14 November 2018;
- Ms Kasim Dlakic 21 November 2018;
- Ms Hamida Dlakic affirmed 14 November 2018;
- Ms Hamida Dlakic affirmed 21 November 2018.

Mr Nagle's evidence

41 Mr Nagle was required to attend for cross-examination.

42 He was first admitted as a solicitor of the Supreme Court in 1979 and was admitted to the Bar in 1981. He did not remain in practice full-time having been elected as a member of the Legislative Assembly of the NSW Parliament in 1988, a seat which he held until 2001. He was a university lecturer in the school of business law and taxation from 2001 until 2007 and in 2017 recommenced practice as a solicitor with PJG Solicitors under the supervision of Patrick Gentle. Given the time that had elapsed since he was first admitted as a solicitor, he was not able to practise on an unrestricted practising certificate.

43 In about September or October 2017, at a social function at the house of a friend, Mr Nagle was introduced to Amil Dlakic, the defendants' son, who told him about a court proceeding in which he was a party involving AMP (this would appear to refer to the proceedings brought by AMP against his parents as mortgagors of the Randwick Property). Mr Nagle gave evidence that Amil Dlakic asked if he would meet with Mr Hancock, a financial advisor, and his parents to "discuss the case".

44 Mr Nagle gave evidence that a meeting was convened in a conference room at the John Maddison Tower. He said that at that meeting, although he was acting as a solicitor, he did not provide the defendants with any legal advice. He spent an hour talking with the first and second defendants generally "about the nature of the proceedings in which they were involved with AMP".

45 In December 2017, he was approached by Mr Hancock who requested that he provide the defendants with independent legal advice associated with a mortgage in which they proposed to enter as guarantors of a loan. He agreed and a meeting was convened at the Royal Exhibition Hotel in Sydney, where Mr Nagle was staying in order to be closer to health care providers due to a heart condition from which he was suffering. He was ordinarily a resident in Kandos in the Central Tablelands of New South Wales.

46 The first meeting at the Hotel was convened on 28 December 2017. Mr Hancock was present (in Mr Nagle's evidence, in his capacity as a financial adviser) with both defendants. He said he was provided with a copy of the mortgage documents which he read. He said he went through each document "very slowly and explained what each page of the document meant". He went on to say:

> I spent time explaining to them what the consequences of failing to comply with the mortgage would be, including the risk that the property the subject of the mortgage would be repossessed and they would lose it. I also advised them that it was important that they understood that if they could not make the payments owing under the mortgage they risked losing their house.

47 Mr Nagle gave evidence that he was aware of the currency of the proceedings in which the defendants were involved with AMP and was concerned to ensure that they understood everything that was explained to them. He said, "I did not want to end up in Court like the AMP Bank".

48 Mr Nagle said the conversation with the defendants was conducted over two hours and in English. He said:

> They spoke to me in English and to my observation understood what I was saying. I observed them to nod and ask questions that satisfied me that they understood what I was explaining to them.

49 He said of the matters discussed the defendants were informed that part of the interest owing under the loan would be paid in advance and that the loan was

to be advanced in favour of Beachview but secured over the Randwick Property.

50 Mr Nagle identified the Identity Documents (within the loan documents), being the first and second defendants' passports and drivers licences certified by him as true copies. He said he explained why it was necessary that this information was provided in support of the loan application. He also identified the full complement of the loan documents which were executed by the defendants in his presence at that meeting, including the following:

(1) The mortgage which was dated, attested and executed by each of the defendants on behalf of Beachview as debtor/mortgagor and on their own behalf as guarantors/debtors under the mortgage. The mortgage included in Schedule A to the mortgage included the following:

(a) The identity of the borrower as Beachview with the same entity as debtor together with the names of each of the defendants as debtors with provision for the "debtors" to pay a minimum of six months' interest calculated on the principal ($1,193,594) over the course of the loan;

(b) The commencement date of the loan was specified as 28 December 2017 with the final repayment date being 12 months from that date;

(c) The defendants were each identified by name as guarantors with the Randwick Property as the security under the guarantee;

(d) The higher and lower interest rates payable under the loan were 19.5% per annum and 9.95% per annum respectively.

(2) Schedule B to the mortgage sets out various fees due and payable either prior to the entry into the mortgage or the advance of the principal amount or in some cases on demand. I note specific provision is made for a brokerage fee to be paid on entry into the mortgage in the amount of $19,694.

(3) A document headed "Cheque Directions" executed by each of the defendants on behalf of Beachview provided for the payment of a brokerage fee to Ashtons Commercial Finance together with other fees payable on advance which resulted in a surplus of loan funds in the amount of $1,090,000. I note that retained interest in the amount of $59,494 was assessed referable to the lower rate of interest.

(4) A Debtor's Advice Declaration executed by each of the defendants and witnessed by Mr Nagle in their capacity as company officers of Beachview in which they agreed to enter into the mortgage on behalf of Beachview, acknowledging in so doing that they understood their financial and legal liabilities under the mortgage; that the mortgage had been freely and voluntarily executed without pressure or undue

influence from any third party and after obtaining advice from an independent Australian legal practitioner as to the legal effect of the mortgage. Each of the defendants acknowledged that they considered and understood that the provision of the mortgage would have a financial impact on them in the event that the mortgage is enforced by the lender.

(5) Mr Nagle also executed an Australian Legal Practitioner's Certificate which was forwarded to the plaintiff's solicitor as part of the loan document in which he certified that he had explained to each of the defendants the nature and effect of the mortgage and its legal effect and terms, and that each of the defendants had informed him that he or she had both read and understood the effect of the mortgage and its terms and the financial risks to each of them by signing the mortgage. He also certified that the various loan documents were executed by each of the defendants, whether as company directors of Beachview as borrower or on their own behalf as guarantors in his presence and witnessed by him.

(6) Finally, the loan documents included a minute of a meeting of Beachview where its directors (being the first and second defendants) resolved that the mortgage (which was tabled at the meeting) would be executed in support of an advance for the "purpose of refinance" being "in the best interests and for the benefit of the debtor (Beachview), its shareholders and creditors". In addition, each of the first and second defendants as directors of Beachview were authorised by resolution that "any excess funds of [sic] the loan from said lender be paid into the personal bank account of 'Kasim Dlakic' at Bankwest Randwick". I note that the last resolution is in Mr Nagle's handwriting and initialled by him and each of the first and second defendants.

51 Mr Nagle gave evidence that after the defendants had executed the mortgage and related documents, he retained them in his possession and emailed them to the plaintiff's lawyers on 2 January 2018 via his private email.

52 On 3 January 2018, he spoke with Elisabeth McGready, solicitor, who advised that the plaintiff would not accept the executed documents unless they were forwarded from the office of the solicitor for the borrowers. Mr Nagle provided the email address of PJG Solicitors.

53 Ms McGready sent an email to that address attaching a second set of mortgage documents for re-execution by the first and second defendants.

54 On receipt, Mr Nagle convened another meeting with Mr Hancock and the first and second defendants at the Royal Exhibition Hotel on 9 January 2018 at which the same loan documents summarised above were re-executed by the first and second defendants. The commencement date of the loan was not

amended. It remained 28 December 2017. These documents were reforwarded to Ms McGready.

55 There was a further delay in arrangements to settle the loan (and consequently the discharge of the AMP mortgage and the removal of the caveat) because of what the plaintiff's solicitors considered was the inadequacy of the certificates of identification and certification of them. Those matters were ultimately addressed by Mr Nagle by forwarding substitute certificates and documents to the plaintiff's lawyers under cover of a letter on PJG Solicitors letterhead of 12 January 2018. In that letter, he confirmed that he acted for the first and second defendants and that he knew them personally. He also confirmed the two occasions on which he explained to the defendants the mortgage documents and the company meeting resolution. He nominated the timing of those meetings, with the first meeting extending from 6:12pm to 7:21pm and the second meeting 11:12am to 12:04pm. As to the second meeting he said:

> On the second occasion I spent between 11:12 AM and 12:04 PM in explaining in detail the mortgage documents, company meeting resolution and so they both fully understood the extent of what they were entering into and the consequences if they breach the terms of the mortgage and the consequences of the power of attorney that they executed.

56 Mr Nagle was cross-examined by counsel for the first and second defendants. Although, he agreed that it was apparent to him that the spoken English of the first and second defendants was "not particularly good", he had no difficulty communicating with them in English. He said he had no difficulty understanding what they were saying and they did not alert him to any difficulty they had understanding him. He confirmed he had an appreciation that they were both in receipt of a pension but made no enquiries as to whether they had been in employment prior to qualifying for a pension.

57 He said he made enquiries as to whether they had the means to meet their loan obligations under the mortgage they were guaranteeing as to which he gave the following evidence:

> I asked them, and I made it quite clear to them, that if they didn't pay off this loan, that they could lose their property, and their response to that was 'Amil will win his case against Mr Johnson and therefore we will be able to pay the loan'

58 He confirmed that it was his understanding that neither the first nor second defendants had any personal capacity to make the loan repayments and that they were reliant upon their son being successful in some current or pending litigation with Mr Johnson. When it was suggested to him that he failed to advise them as to the risks that entailed, he said:

> I couldn't give that advice, because I wasn't sure about what Amil Dlakic's case was all about, although I knew it was about, a case against a solicitor, Mr Johnson. But the, there was a component in the loan agreement, as I explained to them, that the upfront interest was to be paid, I think, until the end of September last year, but if they didn't pay the loan each month after that, they more likely than not would lose their property.

59 Mr Nagle confirmed his understanding that it was the plaintiff's lawyers who required that the loan be advanced through a corporate vehicle. He said he gave no advice to the defendants as to the potential impact of that requirement on their exposure as guarantors of the loan as his instructions were limited to explaining the loan documents that they had provided to him. He said that those documents encompassed a loan to Beachview with a personal guarantee from each of the defendants secured against their home in the event of the company's default. He said his advice was limited to the implications of those arrangements. He said he enquired of the defendants as to their relationship with Beachview and it was in that context that Mr Hancock informed him, in the presence of the defendants, that their financial situation was such that it was necessary that Beachview be interposed as borrower. That was further elaborated in the following exchange:

> Q. Were you told anything else about the company, Beachview Pty Ltd?
>
> A. Yes, one of the other reasons that this loan was created was that the, excuse me, that the Dlakics, Kasim and Humeda, were about to lose the property anyway from another action being taken by another lender against them, and they wanted to save their house. And they wanted to live in their house and as I understand it, from both Amil and from his mum and dad, who are really good people, I might say; and his mum and dad, was that the only way it could be saved is Amil had to win his case against Johnson. Other than that, they would either lose their house there and then in December, or alternatively that the, they would lose their house if they didn't pay their loan from Summers Lawyers.

60 He said that Mr Hancock was present at the meeting with the first and second defendants at their insistence as their financial adviser. He said he made no enquiries of them or Mr Hancock as to whether Beachview was able to repay

the loan because he had already been informed that they believed their son would “win his case” and that the loan would be repaid from the proceeds of the litigation. He said that state of affairs concerned him but gave the following evidence:

> …but I did explain to them in great detail, because I had that concern about what happens if he doesn't, the consequences about him not winning his case or not winning it in time, to what would happen to their property; and I explained it to them in detail, on three separate occasions.

61 He went on to say in that context:

> Q. It was your understanding that the only basis that the loan would be repaid in six months' time was that if Amil Dlakic won his case. Is that correct?
>
> A. That is what I was told. And that's why I told them about the consequences that if he didn't win the case, what was going to happen. And here he is, we're here now, because that's what happened.
>
> HER HONOUR
>
> Q. Was it your understanding that when you raised that concern, it being a highly contingent set of circumstances, that your clients understood that there was that contingency, namely that if Amil didn't win his case, the likelihood would be their home would be repossessed?
>
> A. Yes, your Honour. And that's what I told them.

62 Mr Nagle made it clear that when Mr Hancock told him that Beachview was being utilised because of the first and second defendants’ financial circumstances, he understood it was not limited to them being in receipt of the age pension but because of their indebtedness to AMP.

63 When it was suggested to him in cross-examination that he could not have explained the loan documents to either the first or second defendants without the aid of an interpreter he disagreed. He said that Schedule A to the mortgage, in particular, was explained to them in detail. The following question and answer followed:

> Q. What I'm suggesting to you is that you could not be satisfied that they understood what you meant on that occasion, on both occasions that you met with them?
>
> A. Well, sir, with the greatest respect is that they did. And I explained to them what the, I made clear, pay the thing on time. If not, you're going to be paying a higher interest rate if you don't pay it on time.

64 When it was further suggested to him that he did not advise his clients as to their obligations to make payments by a particular date he disagreed.

Mr Dlakic's evidence

65 Mr Dlakic affirmed two affidavits dated 14 November 2018 and 21 November 2018 and was cross-examined. He recalled the circumstances of the loan from AMP and the subsequent default. He agreed he "remember[ed] well" the proceedings commenced by AMP seeking possession of the Randwick Property and he was aware that if AMP was not paid "the money" it was owed (that is, the $1.05 million the subject of the Terms of Settlement), AMP would take possession of his home.

66 It was in this context that Mr Dlakic was first introduced to Mr Hancock. He said he first met Mr Hancock after being introduced to him by his son, Amil, although later in his evidence he said that the introduction was made by Mr Nagle. In either event, the introduction was made in circumstances where Mr Dlakic was looking for a means of repaying the debt owed to AMP, and he had been told that Mr Hancock could help him arrange a loan from a third-party lender.

67 It was around this time that Mr Dlakic had a meeting with Mr Hancock and Mr Nagle. Mr Dlakic met Mr Nagle and Mr Hancock by pre-arrangement at the Royal Exhibition Hotel in Surry Hills at the end of 2017 to seek advice about a potential loan from the plaintiff. It appears that Mr Dlakic brought the loan documentation to this meeting with Mr Nagle but it is not entirely clear how the documents came to be in his possession.

68 Mr Dlakic gave evidence that at the meeting at the Royal Exhibition Hotel, it was Mr Nagle who had mentioned that Amil was going to win some litigation and that this would enable the first and second defendants to repay the loan to the plaintiff. This is in direct conflict with Mr Nagle's evidence.

69 In terms of his awareness of his obligations under the loan, Mr Dlakic acknowledged that Mr Hancock had told him that the loan would need to be repaid within 12 months and he was aware that some of the loan finance would be "kept" to pay for interest.

70 Mr Dlakic agreed that Mr Hancock told him that interest would be charged at 9.95% per annum but he could not recall Mr Hancock explaining the default interest rate of 19.5% per annum. During cross-examination, Mr Dlakic said,

when taken to a page of the mortgage which he accepted carried his signature, that he never noticed the default interest rate noted on that page. He said:

> I really had no chance, I really had no chance to have a look into it and I had no time for it as well, he just told me there will be 9% interest, that's all I remember.

71 Mr Dlakic initially acknowledged that when he signed the loan documentation he understood that if he did not repay the loan to the plaintiff, he might lose his house. However, he said that he was also told by Mr Nagle that if he had trouble making the repayments on time he would receive "some kind of extension". He later gave evidence, when asked again if he understood that he would lose his home if he could not repay the loan to the plaintiff, that he "could not recall the situation that I may lose my house" and that he was told he would be granted an extension if he had trouble repaying the loan. I note there is no mention of any "extension" in the evidence of Mr Nagle. It was not put to him in cross-examination that he had suggested there would be any extension of the time within which the loan was to be repaid.

72 Mr Dlakic gave evidence that it was "possible" that Mr Hancock had given him the plaintiff's formal letter of offer for mortgage loan, which he confirmed carried his signature. He subsequently said that he could not recall being provided the document by Mr Hancock.

73 Mr Dlakic confirmed during cross-examination that his signature or initials appear on each page of the loan documentation which comprises the formal letter of offer for mortgage loan from the plaintiff, the mortgage, Schedule A and B to the mortgage, the Cheque Directions, the Debtor's Advice Declaration, the Guarantor's Advice Declaration, the Mortgage Common Provisions and the minutes of meeting and resolution of directors of Beachview, where it was resolved that the mortgage would be executed. However, he gave evidence that he did not know what he was signing:

> And we signed something, I don't know what we signed. Because, because, everybody said, 'Sign, don't worry. Save the house, don't worry. Don't worry'. That's what happened.

Mrs Dlakic's evidence

74 Mrs Dlakic affirmed two affidavits dated 14 November 2018 and 21 November 2018. Her evidence, whilst more equivocal than that of Mr Dlakic as to her

state of knowledge or understanding of her dealings with Mr Hancock and Mr Nagle, largely accorded with his account of events. Mrs Dlakic also recalled the loan to AMP Bank and that if the loan was not repaid, AMP would take possession of the Randwick Property. Mrs Dlakic also recalled the proceedings that were eventually commenced by AMP and that those proceedings settled on terms such that if AMP was not paid the settlement sum, AMP would take possession of the Randwick Property.

75 Mrs Dlakic gave evidence that she came to know Mr Hancock through their son, Amil, and that Mr Hancock told them that he would help them raise money to repay AMP.

76 Mrs Dlakic recalled that she went to see Mr Nagle for advice about the loan from the plaintiff, which she understood was to be used to repay AMP. Mrs Dlakic could not recall the substance of what was said during the meeting. She thought that she was meeting Mr Nagle to "sign some documents" but said, "I really could not recall what he asked us. Or what he told us". During cross-examination, Mrs Dlakic agreed that Mr Nagle had told her that if she could not repay the amounts owing under the loan, the plaintiff may take possession of the Randwick Property. A few questions later, she said that she could not recall Mr Nagle telling her this.

77 Whilst she claimed her recollection of the meeting was poor, one of the few things she did recall clearly was that, consistent with the evidence of her husband, no mention was made of the default interest rate. Mrs Dlakic was aware at the time of signing the loan documentation that the interest rate was 9.95% per annum as this was brought to her attention by Mr Hancock. She said, however, that neither Mr Hancock nor Mr Nagle mentioned the default interest rate.

78 Mrs Dlakic verified her signature on the Debtor's Advice Declaration annexed to the mortgage documents but she could not recall whether Mr Nagle explained her obligations as guarantor of the loan prior to signing it.

79 Mrs Dlakic gave evidence that at the time of executing the loan documents she did not understand what a mortgage was. She said:

> We took some kind of a loan, we didn't know what mortgage was. We could not understand what mortgage was back then.

80 When Mrs Dlakic was shown the Finance Application Form, she acknowledged that her signature was on the document. However, she said that Mr Hancock never explained the terms of that document to her.

81 Mrs Dlakic was shown the formal letter of offer for mortgage loan and confirmed that it was her signature on that page. She gave evidence that she understood at the time of signing that document that the purpose of that document was to arrange a loan from the plaintiff. However, when asked further about this letter of offer, she said,

> I don't think I read it. Even if I was able to read, I wouldn't be able to understand.

82 In a similar fashion to Mr Dlakic, whilst accepting that it was her signature on various loan documents, Mrs Dlakic claimed no understanding of what she was signing:

> We were signing everything but never really had a look into it what we were signing and that's true. We were always in hurry, hurry and always half an hour just for signatures.

83 She agreed that Mr Hancock told her at the time of signing the loan documentation that the loan would need to be repaid. When asked if Mr Hancock also told her that the plaintiff may seek possession of her home if the loan was not repaid, she replied, "No, because [Mr Hancock] said he will give us extension time". She repeated this later in her cross-examination.

The issues that crystallised in the defendants' final submissions

84 Although it was only faintly pressed in final submissions, the defendants' counsel did not abandon that aspect of the filed defence which asserted that the relief the plaintiff seeks should be refused because the default notice was not validly issued. Neither did he abandon the related assertion that the higher interest rate of 19.5% which was applied to the assessment of interest in the default notice is a penalty and contrary to law.

85 Since both issues involve a construction of particular clauses of the mortgage, I propose to deal with them at the outset. If there is merit in either of them and the plaintiff's claim is defeated for that reason, it will be unnecessary to

consider whether they have made out their claim for statutory relief under the *Contracts Review Act* or equitable relief.

Validity of the s 57 notice

86 As outlined at [50(1)] above, the commencement date of the loan was 28 December 2017. Despite commencing on that date, the loan monies were not advanced to Beachview until 15 February 2018. Although the delay was not fully explained in the evidence, in addition to the issue of the inadequacy of the certificates of identification, as identified at [55] above, there appears to have been some delay in Beachview providing cheque directions.

87 As noted at [50] above, a condition of the loan, as set out in Schedule A to the mortgage, was that six months' interest would be deducted from the principal sum advanced and applied on settlement as payment of interest as and from the commencement date of the loan. The plaintiff submitted that monthly interest was therefore due and payable by Beachview on and from 28 June 2018. Interest was not paid by Beachview on or by that date or thereafter.

88 On 5 July 2018, the plaintiff issued a notice of default under s 57(2)(b) of the *Real Property Act*. In the notice, the default was described as a failure to make a payment which was due on 28 June 2018. The notice required payment of that amount within 31 days of the date of the notice. Neither Beachview nor the defendants complied with the notice. Proceedings were thereafter commenced by the plaintiff. In their filed defence the defendants admit that no payments of interest were made. They gave no evidence to explain Beachview's failure to pay or any evidence to explain their failure to meet Beachview's obligations under the guarantees.

89 The defendants assert that the s 57(2)(b) notice issued by the plaintiff was "of no effect". Specifically, their cross-claim filed on 22 March 2019 states:

> Interest was not payable under the agreement, until six months after the settlement money was paid, which would be on about 16 August 2018. As such, the default notice issued by the plaintiff was of no effect.

90 It would appear that this pleading is premised on an asserted failure by the plaintiff to comply with the requirements of s 57(2)(b) of the *Real Property Act*; specifically, that the notice was issued prematurely, since on the construction of the loan agreement favoured by the defendants' counsel, interest was not

due and payable until six months from the date of payment of the settlement money (being "on or about 16 August 2018") and, accordingly, Beachview was not in default until that date. Counsel for the defendants did not direct the Court to any provisions within the loan agreement which would support that construction.

91 I regard the date of default as being 28 June 2018. In coming to that decision, I note that the plaintiff tendered, without objection, a letter sent by their solicitor to Mr Nagle on 2 February 2018 to the effect that pending receipt of the defendants' direction to pay on the drawdown of the loan that he should remind his clients that "interest is accruing on the loan facility *from 28 December 2017 in accordance with the terms of the loan agreement*". It was not put to Mr Nagle in cross-examination that he failed to bring this to the defendants' attention.

92 Further still, the plaintiff submitted, and I accept, that the operation of s 57 of the *Real Property Act* is not engaged in relation to a claim for an order for possession. As noted in *ACES Sogutlu Holdings Pty Ltd (in liq) v Commonwealth Bank of Australia* (2014) 89 NSWLR 209; [2014] NSWCA 402 (Leeming JA, Beazley P and Macfarlan JA agreeing):

> [102] Section 57(2)(b) qualifies the exercise of the power of sale conferred under s 58. A mortgagee's power to take possession is distinct from the power of sale. In the case of a mortgage of land held under Torrens title, where a mortgage is merely a charge on the land, the right to possession is statutory, and found in s 60 (for the much less straightforward position in the case of old system title, see Lord Selborne's judgment in *Heath v Pugh* (1881) 6 QBD 345 at 359–360).
>
> [103] The statutory power to take possession, to which s 60 is directed, is not subject to the service of a notice under s 57(2)(b). That has often been held at first instance (for example, *Commonwealth Bank of Australia v Comserv (No 1181) Pty Ltd* (1988) NSW ConvR 55–402 at 57,709 (Rogers CJ Comm Div) and *Natwest Markets Australia Ltd v Mannix* (1995) NSW ConvR 55–743 at 55,747 (Rolfe J)). It has been stated by this court by Sheller JA (with whom Priestley and Meagher JJA agreed), in *Long Leys Co Pty Ltd v Silkdale Pty Ltd* (1991) 5 BPR 11,512 at 11,517 (obiter) and held by Hill, Tamberlin and Sundberg JJ in *Abram v Bank of New Zealand* [1996] FCA 1650 at [37]. It should be regarded as settled law.

93 On that approach it is unnecessary to determine the validity (or otherwise) of the notice under s 57(2)(b) since it offers no impediment to the relief sought by the plaintiff. The pleading does not advance the defendants' case.

Contractual penalty

94 As noted at [50(1)(d)] above, there are two rates of interest expressly provided for under the loan agreement incorporated into the mortgage, namely the "Lower Rate of Interest" of 9.95% per annum and the "Higher Rate of Interest" which is 19.5% per annum. As to the operation of these rates of interest, clause 5.3 of the mortgage common provisions provides:

> The Interest to be paid by the Debtor shall at all times be the Higher Interest Amount unless the Lender notifies the Debtor that the Lower Interest Amount is payable by the Debtor for any Interest Period.

95 Clause 5.4 of that same document stipulates:

> The Lender may notify the Debtor that a Lower Interest Amount is to be paid for any Interest Period and upon the Lender giving that notice the Interest to be paid for that Interest Period shall be that Lower Interest Amount.

96 Schedule A to the mortgage qualifies the operation of these two provisions through the imposition of a special condition. That special condition reads as follows:

> The Lender notifies the Debtor that Clause 5.4 applies whilst ever an Event of Default has ***not*** occurred (in the Lender's sole and absolute discretion) whereas clause 5.3 applies at all other times. (Emphasis added.)

97 The defendants submitted that the Higher Interest Rate charged under the loan agreement amounted to a contractual penalty and was therefore unlawful. For the reasons that follow, I reject that submission.

98 The High Court in *Andrews v Australia and New Zealand Banking Group Ltd* (2012) 247 CLR 205; [2012] HCA 30 defined a penalty as follows (French CJ, Gummow, Crennan, Kiefel and Bell JJ):

> [10] In general terms, a stipulation prima facie imposes a penalty on a party ("the first party") if, as a matter of substance, it is collateral (or accessory) to a primary stipulation in favour of a second party and this collateral stipulation, upon the failure of the primary stipulation, imposes upon the first party an additional detriment, the penalty, to the benefit of the second party. In that sense, the collateral or accessory stipulation is described as being in the nature of a security for and *in terrorem* of the satisfaction of the primary stipulation. If compensation can be made to the second party for the prejudice suffered by failure of the primary stipulation, the collateral stipulation and the penalty are enforced only to the extent of that compensation. The first party is relieved to that degree from liability to satisfy the collateral stipulation.

99 More recently, in the case of *Paciocco v Australia & New Zealand Banking Group Ltd* (2016) 258 CLR 525; [2016] HCA 28, the High Court clarified that

the two essential qualities of a penalty are “threat” and “punishment”. As noted by Kiefel J (as her Honour then was):

> [17] A sum stipulated to be paid on default, which amounted to a threat to the person obliged to pay it if the principal obligation was not performed, bore the character of a penalty, as did a sum stipulated to be paid which could not be accounted for other than as a punishment for default.

100 It follows from these authorities that a contractual clause will prima facie amount to a penalty where it imposes an additional or different contractual liability that arises upon the non-observance of a primary contractual obligation.

101 In *Quantum Asset Management Pty Ltd v Love Properties (WA) Pty Ltd* [2017] WASC 167 Banks-Smith J summarised the principles relating to the penalty doctrine. Her Honour noted:

> [63] In both *Andrews v Australia and New Zealand Banking Group Ltd* and *Paciocco v Australia and New Zealand Banking Group Ltd*, the complaint was that fees charged by the bank were penalties. The High Court endorsed the continued relevance of *Dunlop Pneumatic Tyre Co Ltd v New Garage Motor Co Ltd*. The High Court had previously said in *Ringrow Pty Ltd v BP Australia Pty Ltd* that *Dunlop* continued to express the law to be applied to penalties in Australia.
>
> [64] The following can be drawn from the authorities:
>
> (a) the question whether a sum stipulated is a penalty or liquidated damages (that is, a genuine pre-estimate) is to be judged as at the time of the making of the contract;
>
> (b) the party seeking to be absolved of the liability imposed by the stipulation bears the onus of proving that the stipulation constitutes an unenforceable penalty
>
> (c) the critical issue is whether the sum agreed was commensurate with the interest protected by the bargain;
>
> (d) the nature of the interest sought to be protected is relevant. The sum agreed may be intended to protect an interest that is different from, and greater than, an interest in compensation for loss caused directly by the breach. It may be intangible and unquantifiable. This is consistent with Lord Dunedin's statement in Dunlop that, 'the essence of liquidated damages is a genuine pre-estimate of damage'. The reference to 'damage' as distinct from 'damages' is significant;
>
> (e) an interest may be of a business or financial nature;
>
> (f) a sum that is merely disproportionate to the loss suffered does not qualify as a penalty. The penalty must be 'extravagant, exorbitant or unconscionable' and 'out of all proportion' to the interest of the party which it is the purpose of the provision to protect;
>
> (g) the distinction between liquidated damages and a penalty, whilst useful, is not a limiting rule and does not mean that if no pre-estimate

> is made at the time the contract was entered into, the sum agreed will be a penalty;
>
> (h) nor does it mean that a sum that reflects or attempts to reflect other types of loss or damage beyond those caused directly will be a penalty;
>
> (i) it may be that a reliable pre-estimate is not possible or that damage caused by default is of such an uncertain nature that it cannot accurately be estimated or proved. In such a case a stipulated payment agreed by the parties may well be the true bargain and not a penalty;
>
> (j) where pre-estimation of loss is difficult, precision may not be called for, bearing in mind the question is whether the stipulation is 'out of all proportion' to the interest said to be damaged by default;
>
> (k) the court will not lightly interfere with the bargain struck between the parties. The court requires good reason to attract judicial intervention to set aside the bargains upon which parties of full capacity have agreed. That is why the law on penalties is expressed as an exceptional rule and descriptors such as 'extravagant' and 'out of all proportion' are used in its application;
>
> (l) the ultimate question in determining whether a stipulation is a penalty, is whether it is intended only to punish the defaulting party. Framed another way - does the innocent party's interest in the observance of the principal contractual obligation explain the agreed stipulation as having a purpose other than punishment;
>
> (m) the conventional application of the doctrine of penalties arises when a stipulated sum is made payable by upon breach. However, the rule as to penalties is not limited to cases arising out of breach of contract; and
>
> (n) whether a clause is a penalty invites attention to the proper construction of that clause, and the contract as a whole, but it is not solely a matter of contractual construction. The court is not limited to considering the terms of the contract and any background factual matrix evidence that would be admissible for the purposes of contractual construction. (footnotes omitted)

102 As noted above, the defendants as the parties seeking to be absolved of the liability imposed by the contractual stipulation as to interest, bear the onus of proving that the stipulation amounts to a penalty (see also *Paciocco* at [167]).

103 I am not persuaded that the defendants have discharged that burden. In support of the submission that the Higher Interest Rate amounted to a contractual penalty, counsel for the defendants referred to *Andrews* but without elaboration. That case does not advance the defendants' case in any meaningful way. *Andrews* concerned an appeal from a Federal Court decision, in which the Federal Court found that a number of fees charged by ANZ were incapable of being characterised as a penalty as they were not payable upon a

breach of contract. The High Court in *Andrews* unanimously overturned that decision, finding that the rule of penalties is not limited to breaches of contract. As expressed by McDougall J at [73] in *Arab Bank Australia Ltd v Sayde Developments Pty Ltd* (2016) 23 NSWLR 231*;* [2016] NSWCA 328, "the real point of the decision in *Andrews* was to identify that the equitable jurisdiction to relieve against penalties remained alive and well". That proposition bears little significance to the defendants' case.

104 Beyond the asserted reliance upon *Andrews*, nothing further was advanced by the defendants' counsel. No evidence was led to address whether the interest rate was commensurate with the interest protected by the bargain. In order to make such an assessment, I would require evidence of the value of the interest the plaintiff sought to protect through the imposition of the impugned provision and there was no evidence adduced permitting that assessment to be made.

105 Further, the defendants have failed to demonstrate that the Higher Interest Rate was inserted into the loan agreement as a "threat" or for the purpose of "punishing" Beachview as a borrower in default (see *Paciocco* at [17]). Equally, nothing has been proffered to support the proposition that the Higher Interest Rate of 19.5% per annum is "extravagant and unconscionable" (see *Paciocco* at [51]).

106 In any event, it would appear that the interest rate model incorporated in the loan agreement is outside the purview of the penalty doctrine. Under the agreement, the default or Higher Interest Rate was the standard rate applicable under the loan and the Lower Interest Rate only applied if notice was given by the plaintiff, with notice deemed to have been given where there was no default. Accordingly, in a technical sense, the differential interest structure does not operate to penalise the borrower for breach but rather provides for a "concessional" lower rate whilst ever there has been no default. As noted in *Kowalczuk v Accom Finance* (2008) 77 NSWLR 205; [2008] NSWCA 343 (Campbell JA, Hodgson and McColl JJA agreeing):

> [162] …There is a conventional view that a properly drafted mortgage containing higher and lower rates does not attract the law of penalties at all. That is because the law of penalties strikes down those provisions of a contract that state the consequences that will flow when there is a breach of contract, if those consequences are not a genuine pre-estimate of the damage

> likely to be suffered in consequence of that breach. If the mortgage is drafted so that the borrower agrees to pay a particular rate of interest, but the lender agrees to accept a lower rate of interest in full satisfaction of the borrower's obligation to pay interest at that particular rate provided that the lower rate of interest is paid timeously (and, sometimes, provided that there is no breach of any other provision of the mortgage) that provision is not one that states the consequences of a breach of contract, and hence the law of penalties does not apply to it.

107 Further, as noted by counsel for the plaintiff, a clause similar to that contained in the mortgage and memorandum was the subject of consideration by Campbell J (as his Honour then was) in the decision of *King Investment Solutions Pty Limited v Hussain* (2005) 64 NSWLR 441; [2005] NSWSC 1076. His Honour held that such a clause fell outside the ambit of the doctrine:

> [138] One requirement for a provision in a contract being a penalty is that it states a consequence which is agreed to follow from breach of one of the provisions of the contract. The structure of the interest clause in the present case is not like that. Rather, the interest clause in the contract involves a promise by the mortgagors to pay interest at 118.8%, and a promise by the mortgagee that, if the mortgagors pay the interest on time, or no more than 7 days late, the mortgage will accept interest at 60%. *A clause structured in that way is not regarded as a penalty.* (Emphasis added.)

108 The submission that the Higher Interest Rate amounted to an unlawful contractual penalty is rejected.

The claim for statutory relief under the Contracts Review Act

109 Although the defendants seek relief on the basis of both unconscionability under the general law and "unjustness" under the *Contracts Review Act* (the Act), the parties proceeded on the basis that I would deal with the question of statutory relief first, it being accepted that the jurisdiction under the Act is wider than equitable principles of unconscionability.

110 In this case, however, there was little, in any practical sense, to differentiate the claim for statutory relief from the claim for equitable relief. It is clear that the assertion that the plaintiff's conduct as lender was unconscionable because it knew or ought to have known of the defendants' special disadvantage and, for that reason, that their conduct as lender was without regard for conscience or irreconcilable with what is morally right or reasonable (see *Qantas Airways v Cameron* (1996) FCR 246; [1996] FCA 349) is referenced to particulars that are no different from the particulars pleaded in support of the claim under the *Contracts Review Act*.

111 As a preliminary argument, the plaintiff submitted that the operation of ss 7(1) and 19(1) of the *Contracts Review Act* precludes the defendants from seeking the relief pleaded in the cross-claim, namely an order "setting aside" the mortgage loan and guarantees where the loan with Beachview as borrower (signed by the defendants as officers of that company) is incorporated into the registered mortgage by the express inclusion of Schedules A and B (see earlier at [50]). Those sections provide:

> **7 Principal relief**
>
> (1) Where the Court finds a contract or a provision of a contract to have been unjust in the circumstances relating to the contract at the time it was made, the Court may, if it considers it just to do so, and for the purpose of avoiding as far as practicable an unjust consequence or result, do any one or more of the following:
>
> > (a) it may decide to refuse to enforce any or all of the provisions of the contract,
> >
> > (b) it may make an order declaring the contract void, in whole or in part,
> >
> > (c) it may make an order varying, in whole or in part, any provision of the contract,
> >
> > (d) it may, in relation to a land instrument, make an order for or with respect to requiring the execution of an instrument that:
> >
> > (i) varies, or has the effect of varying, the provisions of the land instrument, or
> >
> > (ii) terminates or otherwise affects, or has the effect of terminating or otherwise affecting, the operation or effect of the land instrument.
>
> …
>
> **19 Orders affecting land**
>
> (1) An order made under section 7(1)(b) or (c) has no effect in relation to a contract so far as the contract is constituted by a land instrument that is registered under the *Real Property Act 1900*.

112 The plaintiff submitted that because the registered mortgage and incorporated documents are "land instruments" as defined in s 4 of the Act, namely "an instrument that transfers title to land, creates an estate or interest in land or is a dealing within the meaning of the *Real Property Act"*, and because s 19(1) provides that an order under s 7(1)(b) declaring a contract void in whole or in part or under s 7(1)(c) varying any provision of the contract whether, in whole or in part, has no effect in relation to a contract insofar as it is constituted by a land instrument that is registered under the *Real Property Act*, the only relief to

which the plaintiffs may be entitled under the cross-claim is under s 7(1)(a) or (d) of the *Contracts Review Act*, namely:

> (a) [the Court] may decide to refuse to enforce any or all of the provisions of the contract,
>
> …
>
> (d) [the Court] may, in relation to a land instrument, make an order for or with respect to requiring the execution of an instrument that:
>
> (i) varies, or has the effect of varying, the provisions of the land instrument, or
>
> (ii) terminates or otherwise affects, or has the effect of terminating or otherwise affecting, the operation or effect of the land instrument.

113 As I understand the position, counsel for the defendant acknowledged the force of the analysis proffered by the plaintiff's counsel but submitted that since relief under ss 7(1)(a) and (d) remains available, even on the plaintiff's analysis, it would be open to the Court to "set aside" that part of the loan contract incorporated into the mortgage which provided for interest calculated at 9.9% per annum (the Lower Rate of Interest) and at 19.5% per annum (the Higher Rate of Interest) over a loan term of 12 months as "unconscionable, harsh or oppressive", in circumstances where it must have been clear to the plaintiff that the defendants had no capacity to meet monthly interest payments howsoever calculated, with the contract expressly providing for interest over half of the loan term to be prepaid at the time of contract.

114 Although counsel for the defendants did not abandon the relief sought in the cross-claim, when he was pressed to identify what was encompassed in his oral submissions "as a fair and more realistic result" of the litigation, he submitted that the plaintiff's relief should be confined to an order for possession of the Randwick Property but on terms denying it any entitlement to recover any interest on the unpaid principal.

115 That relief, as with the primary relief sought, remains subject to the defendants satisfying the court of their entitlement to statutory relief under the Act or relief under the general law.

116 For the reasons which follow, the defendants have failed to make good that claim.

The Contracts Review Act – general principles

117 The operation of the *Contracts Review Act* and the scope of the statutory relief to which a party may be entitled where the Court is satisfied that the contract under challenge is unjust "in the circumstances relating to the time at which it was made" (s 7 of the Act) by reason of it being "unconscionable, harsh or oppressive" (s 4 of the Act) – sometimes referred to as the "tautological trinity" – has been the subject of considerable authority from which the following principles can be divined.

118 The evaluative task in which the Court is involved in examining both the terms of the contract and the context in which it was entered into, focuses essentially on whether the contract operates "unjustly" towards the weaker contracting party. The matters to which the court is obliged to have regard in undertaking that evaluation in the first stage of the evaluative exercise provided for in s 9(2) of the Act are illustrative of that focus. It is also necessary when considering the question of "unjustness" for the Court to have regard to the public interest (s 9(1)). That is said to involve discretionary considerations that come into play only where it is "just to do so and for the purpose of avoiding, as far as practicable, an unjust consequence or result" (see *Perpetual Trustee Co Ltd v Khoshaba* [2006] NSWCA 41 at [109] cited in *Bank of Western Australia Ltd v Tannous* [2010] NSWSC 1319 at [33] per Davies J). One of the considerations in the exercise of that discretion is the extent of any benefit obtained by the party who claims relief from the consequences of an unjust contract.

119 It was accepted in final submissions that the statutory relief the defendants seek would not to be withheld simply because the loan funds advanced by the plaintiff were directed to the discharge of the mortgage to AMP over the Randwick Property and the discharge of the second registered mortgage and the withdrawal of the caveat. However, there being no evidence adduced by the defendants that their pre-existing liability to AMP as lender was unenforceable or unjust, in whole or in part (similarly, where their liability to the second registered mortgagee or caveator was not challenged is unenforceable or unjust), any relief in these proceedings to which they may be otherwise entitled would need to accommodate an order for repayment to the plaintiff of the sums directed to third parties on settlement of the loan.

120 That was explained by Davies J in *Tannous* in the following passage:

> [43] Where there is an issue about the unjustness of a contract or mortgage paid out by an incoming mortgagee who is the Plaintiff in proceedings, the issue is not determined by joining that prior mortgagee as a party to the proceedings. Rather, the issue is determined in the context of the discretionary order at the second stage of the *Contracts Review Act* proceedings. That is so, because the issue forms part of the controversy between the Plaintiff and the Defendants. The justiciable issue is what order should be made in circumstances where the contract made between the Plaintiff and the Defendants is held to be unjust. There is no justiciable issue between the Defendants and the mortgagee/lender whose contract has been completed and whose mortgage has been discharged.

121 The same result would necessarily follow in the event that I were persuaded that the transactions into which the defendants entered were unconscionable under the general law and should be set aside for that reason. That is, an order setting aside the transactions as unconscionable would need to be made conditional upon repayment to the plaintiff the value of the benefit the defendants obtained by the discharge of their obligations to AMP, and their obligations to the second registered mortgagee and the caveator (see *Elkofairi v Permanent Trustee Co Ltd* [2002] NSWCA 413).

122 Although the parties did not address detailed submissions as to how considerations of public interest were engaged on the evidence adduced in these proceedings, I propose to take into account the strong public interest in holding parties to their contractual obligations in circumstances where it can be shown that a contract was freely entered into, however ill-advised it might appear in retrospect or how ill-advised it may have appeared to an objective commercial observer at the time of contract, in particular, the weaker contracting party was in receipt of legal advice before entering into the contract. The situation might have been otherwise in this case were there evidence that the plaintiff was aware that the legal and/or financial advice provided to the defendants was deficient or defective or that it ought to be aware of that state of affairs. It might also have been otherwise were the plaintiff aware that the defendants, as guarantors of the loan to Beachview, were labouring under some particular disadvantage, or that they had been prevailed upon by interests associated with Beachview or by a third party to the contract to their disadvantage. The evidence in these proceedings was to the contrary.

123 I am unable to resolve on the evidence whether the plaintiff insisted on the interposition of Beachview as borrower or whether that arrangement was offered by Mr Hancock in his capacity as broker or financial advisor. In either event, in the absence of any evidence adduced by the defendants from Mr Hancock, I am prepared to draw the inference that his evidence would not have assisted them in support of their claim that they failed to appreciate the significance of the interposition of Beachview as the corporate borrower and their added exposure as guarantors of Beachview's liability, or their ignorance of the legal consequences of entering into a loan agreement with the plaintiff as directors of Beachview.

124 In this case, in meeting the defendants' claim for statutory relief from what was said to be a harsh and unjust contract, the plaintiff emphasised that the large compendium of executed loan documents forwarded by the defendants' solicitor, Mr Nagle, to the plaintiff's solicitors on 12 January 2018, were the subject of legal advice as to their legal force and effect; a state of affairs which was both certified on the various loan documents which were executed in Mr Nagle's presence and witnessed by him, and reflected in the Australian Legal Practitioner's Certificate which he completed and included with that material. The plaintiff also relied upon Mr Nagle's evidence that in the course of successive conferences with the defendants at which Mr Hancock was present as their broker or financial advisor, he had no difficulty understanding what they were saying and they did not alert him to any difficulty they had in understanding him.

125 I was invited by the defendants' counsel to reject Mr Nagle's evidence. I was urged to make my own assessment of the capacity of each of the defendants to both speak and understand English referable to the way in which they gave evidence in the proceedings and to conclude that Mr Nagle's assessment of their capacity must be fundamentally flawed. There was no suggestion that I should disbelieve him, but rather that he simply failed to apprehend that his clients had an entirely inadequate understanding of English to understand their contractual obligations. Having made that determination I was invited to find that the defendants had no real comprehension of their obligations in

guaranteeing Beachview's obligations under the loan, or any capacity to appreciate the risk of mortgaging their asset.

126 I am unable to accept that submission. The defendants' knowledge or appreciation of the transactions in which they were engaged with the plaintiff as a commercial lender has to be understood against the background of their position as borrowers viz another commercial lender being AMP Ltd and, as importantly, their knowledge of the consequences of failing to meet their obligations to repay loan monies advanced on commercial terms where that advance was secured by registered mortgage against their sole residence. While their command of English was imperfect, I am left in no doubt that they well understood from the advice they were given by Mr Nagle that in obtaining a loan from the plaintiff to meet their obligations to AMP and secure some added time within which their son could provide them with sufficient funds to pay back the loan to enable the plaintiff to enable them to keep their house. They were taking a risk that they would lose their home if interest was not paid in time. The fact that they did not appear to critically assess the risks involved in contracting in that way is not to be sheeted home to the plaintiff. The *Contracts Review Act* is not intended to protect contracting parties from the consequences of poor financial decisions, or to relieve them of their contractual obligations, otherwise in circumstances where the Court is satisfied that the contract was unjust at the time it was entered into.

127 Furthermore, and despite the pressure under which the defendants were operating at the time of contract, with the date of settlement with AMP pending and the inevitability of losing the Randwick Property being their sole residence in the event that they were unable to meet their obligations under the AMP Deed of Settlement, I am not satisfied they were acting under any special position of disadvantage of which the plaintiff was aware or of which it ought to have been aware. In fact, their evidence allows for a positive finding that they were well aware at all times that if the loan to the plaintiff were not discharged there was every real possibility they would lose their home, a risk they were prepared to take on faith that their son would discharge the loan from the proceeds of successful litigation to which he was a party. There is no evidence as to whether they sought or obtained any advice from those representing their

son as to the prospects of the litigation generating a payout sufficient to discharge the loan. There is evidence (which is not contradicted) that they were informed by Mr Nagle of the risks of re-encumbering the Randwick Property contingent upon the success of their son's litigation but that they determined to take the risk that they might lose their home despite that advice.

Conclusion

128 I am not satisfied that the operation of the contract or the manner in which it was made renders either the contract or any of its provisions unjust in all the circumstances. In particular, I am not satisfied that the defendants were operating under any substantial incapacity at the time of entering into the arrangements with the plaintiff, either as directors of Beachview or as guarantors of that loan, such that their capacity to appreciate and assess the risks entailed in getting a fresh mortgage over the Randwick Property was in any sense compromised.

129 Neither do I regard the contractual terms, including the terms that provided for a differential interest rate as unjust; the consequences of the contract unjust or its effects unjust. These considerations have been described as informing the issue of substantive injustice.

130 Finally, I am not satisfied the contract is unjust because of any unfairness in the plaintiff's methods or the processes as a commercial lender in which the contract was made. This has been described as procedural injustice (see *West v AGC (Advances) Ltd* (1986) NSWLR 610 at 620). The plaintiff was entitled to proceed on the basis articulated in the formal letter of offer that the relatively short-term loan to Beachview was in order to facilitate discharge of a pre-existing liability to those associated with the company with a view to the security offered under the newly created first mortgage ultimately being sold to discharge the loan. Considerations of public interest do not necessitate the imposition of a burden of enquiry on a commercial lender to enquire into a corporate borrower's ability to service the loan, in particular where the lender is satisfied that individuals who are prepared to guarantee a company's liability by the provision of security, including over residential premises, are in receipt of

legal advice (see *Provident Capital Ltd v Papa* (2013) 84 NSWLR 231; [2013] NSWCA 36).

Orders

131 I make the following orders:

(1) Judgment for the plaintiff.

(2) An order for possession of the property known as XX, Randwick in the State of New South Wales.

(3) Leave to enter judgment forthwith.

(4) Leave to apply for a writ of possession forthwith.

(5) The Court notes the plaintiff's undertaking signed by Kathryn Lauren Brann, solicitor, a full copy of which in annexed to the copy of the judgment retained in the Court file.

(6) The defendants to pay the plaintiff's costs.

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