

New South Wales
Court of Appeal

CITATION:	**Perpetual Trustee Company Limited v Albert and Rose Khoshaba [2006] NSWCA 41**
HEARING DATE(S):	6 December 2005
JUDGMENT DATE:	20 March 2006
JUDGMENT OF:	Spigelman CJ at 1; Handley JA at 99; Basten JA at 105
DECISION:	1 Grant leave to appeal; 2 Direct the Appellant to file a Notice of Appeal within 14 days hereof; 3 Appeal dismissed; 4 The Appellant to pay the Respondents' costs.

CATCHWORDS:	CONTRACTS – Unjust contracts – Determination that a contract "unjust" – Appellate review – Nature of decision appealed from – Conclusion that "unjust" – Whether discretionary – Whether reviewable – Discussion – Contracts Review Act 1980, s7. - CONTRACTS – Unjust contracts – When contract "unjust" – Courts to apply contemporary standards of what is "unjust" – Court cannot be constrained by other decisions as if they were rules – Relevant circumstances – Where money borrowed for investment – Purpose of the loan– Lender's indifference to purpose of loan– Lender's failure to adhere to its own lending guidelines.
LEGISLATION CITED:	Contracts Review Act 1980: ss 7, 9 Unfair Contract Terms Act 1977 (UK) Unfair Terms in Contract Regulations 1999 (UK)

CASES CITED:	Antonovic v Volker (1986) 7 NSWLR 151 Baltic Shipping Co v Dillon (1991) 22 NSWLR 1 Beneficial Finance Corp Limited v Karavas (1991) 23 NSWLR 256 Blackburn v Allianz Australia Insurance Ltd (2004) 61 NSWLR 632 Buck v Bavone (1976) 135 CLR 110 Buller v Black (2003) 56 NSWLR 425 Coal & Allied Operations Pty Ltd v AIRC (2000) 203 CLR 194 Commercial Bank of Australia Limited v Amadio (1983) 151 CLR 447 Crowe v Commonwealth Bank of Australia [2005] NSWCA 41 CSR Ltd v Della Maddalena [2006] HCA 1 Dinsdale v The Queen (2000) 202 CLR 321 Director General of Fair Trading v First National Bank plc [2002] 1 AC 481 Elders Rural Finance Ltd v Smith (1996) 41 NSWLR 296 Elkofairi v Permanent Trustee Co Ltd (2003) 11 BPR 20,841 Esanda Finance Corp Ltd v Tong (1997) 41 NSWLR 482 Figliuzzi v Yonan [2005] NSWCA 290 Fleming v The Queen (1998) 197 CLR 250 Fox v Percy (2003) 214 CLR 118 George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd [1983] 2 AC 803 House v The King (1936) 55 CLR 499 Karl Suleman Enterprizes Pty Ltd (in liq) v Babanour (2004) 49 ACSR 612 Minister for Immigration and Ethnic Affairs v Wu Shan Liang (1996) 185 CLR 259 Minister for Immigration and Multicultural Affairs v Eshetu (1999) 197 CLR 611 Mulligan v Coffs Harbour City Council (2006) 221 ALR 764 Murphy v Overton Investments Pty Ltd [2002] FCAFC 129 Nguyen v Taylor (1992) 27 NSWLR 48 Norbis v Norbis (1986) 161 CLR 513 Permanent Trustee Australia Co Ltd v FAI General Insurance Co Ltd (2001) 50 NSWLR 679 Permanent Trustee Australia Co Ltd v FAI General Insurance Co Ltd (2003) 214 CLR 514 Roy Morgan Research Centre Pty Ltd v State Revenue (Vict) (2001) 207 CLR 72 Russo v Aiello (2003) 215 CLR 643 SH Lock (Australia) Ltd v Kennedy (1988) 12 NSWLR 482 Singer v Berghouse (1994) 181 CLR 201 St Clair v Petricevic (1988) ASC 55-688 St George Bank Ltd v Trimarchi [2004] NSWCA 120 Warren v Coombes (1979) 142 CLR 531 Weiss v The Queen (2005) 80 ALJR 444 West v AGC (Advances) Ltd (1986) 5 NSWLR 610 Wyong Shire Council v Shirt (1980) 146 CLR 40

PARTIES:	Perpetual Trustee Company Limited (Appellant) Albert and Rose Khoshaba (Respondents)
FILE NUMBER(S):	**CA** 40390/2005
COUNSEL:	M Cashion SC, J White (Appellant) M B J Lee (Respondents)
SOLICITORS:	Gadens Lawyers (Appellant) Marsden's Law Group (Respondents)

LOWER COURT JURISDICTION:	District Court
LOWER COURT FILE NUMBER(S):	3639/2003
LOWER COURT JUDICIAL OFFICER:	Rolfe DCJ

IN THE SUPREME COURT
OF NEW SOUTH WALES
COURT OF APPEAL

CA
40390/05

SPIGELMAN
CJ
HANDLEY
JA
BASTEN JA

Monday 20
March 2006

PERPETUAL TRUSTEE COMPANY LIMITED v Albert and Rose KHOSHABA

The Respondents are pensioners and members of the Assyrian community in Sydney. In late 2000 the Respondents became aware that many members of the Assyrian community were investing in a trolley-collecting business operated by Karl Suleman Enterprizes Pty Ltd ("KSE"). The business operated as a pyramid investment scheme. After meeting with persons associated with KSE, the Respondents decided to invest.

They were referred by KSE to Combined Home Loans Pty Ltd ("CHL"). CHL submitted a loan

application to Australian Mortgage Wholesalers Pty Ltd ("AMW"), whose role it was to assess the application on the Appellant's behalf in accordance with specified Guidelines.

The loan application, initially submitted in Mr Khoshaba's name alone, was deficient in several respects. It falsely described Mr Khoshaba as being employed and earning a salary of $43,000. The trial judge found that Mr Khoshaba had no knowledge that this information had been submitted to the lender. Furthermore, that part of the application that inquired as to the purpose of the loan was left unanswered. After it had been submitted, the loan application was amended to include Mrs Khoshaba as a joint applicant. The trial judge found that her signature on the form had been forged.

Pursuant to the guidelines, AMW was required to verify the employment and income position of the applicants. The Guidelines also required that full details of the purpose of the loan be given. In neither respect were the Guidelines followed.

In February 2001 the Appellant, as trustee for a securitised mortgage programme, lent the Respondents $120,000 and took a mortgage over their family home (the 'Loan Agreement'). The Respondents forwarded $100,000 of these monies to their daughter, who invested them in KSE (the 'Investment Agreement').

The trial judge found that the Appellant had no knowledge of the Investment Agreement, and that it had no involvement in falsifying the loan application.

KSE collapsed, with the Respondents owing the Appellant $87,572. The Respondents sought relief from the Loan Agreement pursuant to the *Contracts Review Act* 1980 (the "Act"). The trial judge found the Loan Agreement to be unjust for two principal reasons:

· The Appellant's failure, contrary to prudent lending practice, to follow its own lending guidelines in assessing the Respondents' loan application; and

· The Appellant's failure to recommend to the Respondents that they receive independent legal or accounting advice.

The trial judge granted relief, reducing the Respondents' debt to the Appellant to $29,803.57.

HELD

The Appellate Role

Per Spigelman CJ, Handley and Basten JJA agreeing
1. The trial judge erred by considering the Appellant's failure to follow the Guidelines by reference to prudent lending practice. This was not how the case was run. [56], [104], [120]

Per Handley and Basten JJA, Spigelman CJ discussing but not deciding

2. An appellate court undertaking an appeal by rehearing of a determination under s7 of the Act should adopt the following approach:

a. The facts found by a judge sitting without a jury should be reviewed in accordance with the principles identified in *Fox v Percy* (2003) 214 CLR 118. [100], [106]

b. A finding that a contract is unjust should be reviewed in accordance with the principles identified in *Warren v Coombes* (1979) 142 CLR 531. [40], [100], [107]
Singer v Berghouse (1994) 181 CLR 201; *Coal & Allied Operations Pty Ltd v AIRC* (2000) 203 CLR 194 considered.
Norbis v Norbis (1986) 161 CLR 513; *Buck v Bavone* (1976) 135 CLR 110; *Minister for Immigration and Ethnic Affairs v Wu Shan Liang* (1996) 185 CLR 259; *Minister for Immigration and Multicultural Affairs v Eshetu* (1999) 197 CLR 611; *Murphy v Overton Investments Pty Ltd* [2002] FCAFC 129; *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd* [1983] 2 AC 803; *Director General of Fair Trading v*

First National Bank plc [2002] 1 AC 481 referred to.
c. The discretion to award relief should be reviewed in accordance with the principles identified in *House v The King* (1936) 55 CLR 499. [100], [109]

Unjustness

3. When Parliament adopts general standards such as "justness", Parliament intends courts to apply contemporary community standards about what is just. Such standards may vary over time. [64], [104], [105]
West v AGC (Advances) Ltd (1986) 5 NSWLR 610; *Elkofairi v Permanent Trustee Co Ltd* [2002] NSWCA 413 referred to.

4. The purpose for which a loan is obtained is a relevant circumstance within the meaning of s7 of the Act. [70], [104], [122]
West v AGC (Advances) Ltd (1986) 5 NSWLR 610 explained.

5. Where the Court has to apply a standard as general as what it "unjust", it cannot be confined by decisions in other cases as if they were rules. [73], [104], [105]
West v AGC (Advances) Ltd (1986) 5 NSWLR 610; *Crowe v Commonwealth Bank of Australia* [2005] NSWCA 41; *Baltic Shipping Co v Dillon* (1991) 22 NSWLR 1 referred to.

6. The fact that the lender was willing to lend on the value of the security alone, and was indifferent to the purpose of the loan, is entitled to significant weight in the determination of unjustness. [82], [92], [104], [126]
Elkofairi v Permanent Trustee Co Ltd [2002] applied.

7. In a tripartite situation, failure to recommend that a person seek advice is not entitled to significant weight when the advice is relevant to that part of the transaction which does not involve the rights and obligations or interests of the person against whom relief is sought. [90], [104], [105]
West v AGC (Advances) Ltd (1986) 5 NSWLR 610 considered.

Per Handley JA

8. The knowledge of AMW, including its knowledge that the Guidelines had not been complied with, was for legal purposes the knowledge of the Appellant. [103]
Permanent Trustee Australia Co Ltd v FAI General Insurance Co Ltd (2001) 50 NSWLR 679 applied.

Per Basten JA

9. When considering the relevance of a failure to ensure that a lender receives independent advice, it is in error to look for a duty imposed under general law to ensure such a result. A contract may be unjust without there being any breach of a general law duty. [127]
Elders Rural Finance v Smith (1996) 41 NSWLR 296 followed.

10. Where the security is the sole residence of the borrower, and the borrower has been content to lend on the strength of that security alone, there is a public interest in treating contracts as unjust in circumstances where the borrower has demonstrated an inability reasonably to protect their own interests. [128]

Per Spigelman CJ, Handley and Basten JJA agreeing

Relief

11. The Appellant was not innocent of the cause of the unjustness. Relief should be granted. [96], [104], [105]
Beneficial Finance Corp Ltd v Karavas (1991) 23 NSWLR 256; *Nguyen v Taylor* (1992) 27 NSWLR 48 distinguished.

ORDERS

1. Grant leave to appeal.

2. Direct the Appellant to file a Notice of Appeal within 14 days hereof.

3. Appeal dismissed.

4. The Appellant to pay the Respondents' costs.

IN THE SUPREME COURT
OF NEW SOUTH WALES
COURT OF APPEAL

CA 40390/05

SPIGELMAN CJ
HANDLEY JA
BASTEN JA

Monday 20 March 2006

PERPETUAL TRUSTEE COMPANY LIMITED v Albert and Rose KHOSHABA

Judgment

1 **SPIGELMAN CJ:** This is an application for leave to appeal and, if granted, an appeal from the judgment of Rolfe DCJ in the District Court of New South Wales, in which his Honour made orders pursuant to s7 of the *Contracts Review Act* 1980.

2 The issues that arise in this case are of some complexity. Notwithstanding that the amount involved is not large, the issues that have arisen may have significant implications for lending practices. Leave to appeal should be granted.

Background Facts

3 In February 2001 the Appellant entered into a Loan Agreement with Mr and Mrs Khoshaba ("the Respondents") pursuant to which the Appellant advanced the sum of $120,000, receiving $116.872.50 net of brokerage and fees. As security for the loan the Appellant took a first registered mortgage over the residence of the Respondents. The bulk of the monies in the amount of $100,000 was advanced to the Respondents' daughter and by her to Karl Suleman Enterprizes Pty Ltd ("KSE") under an Investment Agreement. Under that agreement a fortnightly sum, originally $2,500 later increased to $5,000, was either transferred by, or paid at the direction of, the Respondents' daughter into the bank account of the Respondents.

4 The Investment Agreement purported to constitute an investment in a shopping trolley collection business. It had the structure of pyramid selling scheme. Eventually the scheme collapsed, leaving the Respondents without the expected flow of revenue and a debt to the Appellant. (See *Karl Suleman Enterprizes Pty Ltd (in liq) v Babanour* (2004) 49 ACSR 612.)

5 On the calculations presented to the Court, which calculations are not in issue in this appeal, the Respondents received a "total benefit" under the loan agreement of $81,103.39: being the addition of $16,103.39 not invested with RSE and $65,000 paid to the Respondents pursuant to the Investment Agreement.

6 At the time of the hearing before Rolfe DCJ the Respondents had repaid $51,299.82 to the Appellant. Accordingly, the difference between the total benefit received and the amount repaid was $29,803.57. The debt, with accumulated interest, was calculated in the amount of $87,572.38. The effect of Rolfe DCJ's judgment was to reduce the debt to the amount of $29,803.57, being the balance of the "total benefit" received by the Respondents and not repaid by them.

7 Rolfe DCJ determined that the financial arrangements, including the original investment, were made by the Respondents and their daughter as part of a family arrangement. His Honour found that the three members of the family approached the matter as a single economic unit, and that it made no difference to them who the borrowers or investors would be. (Judgment p36.) There is no appeal from his Honour's finding in this respect. Nor is there a notice of contention suggesting that anything turns on the different contractual rights and obligations of the respective family members.

8 The loan was taken up for the primary purpose of making the investment. There is no suggestion that the Appellant or anyone acting on its behalf played any role in inducing the Opponent to enter into the Investment Agreement. Nor was there any suggestion that the Appellant or anyone acting on its behalf had any information about the investment proposed or its risks and possible returns.

9 The basic steps involved in the Loan Agreement and the associated Mortgage were as follows:

· The Appellant entered into the Loan Agreement as trustee for a securitised mortgage program. This program was managed by RESIMAC Limited ("RESIMAC").

· RESIMAC in turn entered into a Mortgage Origination and Management Deed ("MOMD") with Australian Mortgage Wholesalers Pty Limited ("AMW").

· It was AMW's role under the MOMD to assess loans on behalf of RESIMAC.

· About 40 brokers would submit loan applications to AMW. AMW would propose borrowers to RESIMAC.

· In this instance, the broker who prepared and submitted the Respondents' loan application to AMW was Combined Home Loans Pty Limited ("CHL"). The loan application was submitted twice.

· On the first occasion it was submitted under cover of a facsimile dated 17 January 2001 from Beneficial Lending & Investments ("BLI"), a company related to CHL. Mr Khoshaba was the only loan applicant. Mr Khoshaba was, falsely, shown to have an occupation and an income of $43,000 pa.

· When the loan application was submitted for a second time (by facsimile dated 25 January 2001), Mrs Khoshaba was shown as a second loan applicant. The application form attributed no occupation or income to Mrs Khoshaba. A credit check carried out by AMW showed that Mrs Khoshaba was in receipt of social security benefits.

· Pursuant to the terms of the MOMD, AMW had to satisfy itself as to the correctness of the information contained in the loan application by carrying out certain steps in compliance with RESIMAC's internal lending guidelines (the "Guidelines").

10 The steps taken by the Respondents with respect to the investment and loan were as follows.

11 On his Honours findings:

· A long time friend of Mr Khoshaba, Mr Ubert Rashed, recommended investment in interests associated with Mr Karl Suleman. Mr Rashed informed Mr Khoshaba that he had invested $100,000 and was earning $2,500 per fortnight from that investment.

· Mr Khoshaba visited Mr Suleman, and was referred to Mr Suleman's accountant, a Mr El-Gamal.

· Mr Khoshaba visited Mr El-Gamal in November 2000, and was then referred to Mr Victor Abdelkodous, whom he met in the company of Mr Rashed and Mr Khoshaba's daughter, Tilda, in January 2001. Mr Khoshaba informed Mr Abdelkodous that Mr Khoshaba was a pensioner, and Mr Abdelkodous responded that he would "fix it" so that the investment could proceed.

· At a subsequent family meeting, which included the Respondents' children Tommy and Tilda, the Respondents decided to invest with Mr Suleman.

· Mr Khoshaba subsequently met again with Mr Abdelkodous, again in the company of his friend, Mr Rashed. At that time, Mr Abdelkodous informed Mr Khoshaba that he could obtain a loan for $120,000, of which $100,000 would be invested with Mr Suleman. Mr Khoshaba signed a loan application, which he did not read, for an amount of $120,000.

· The loan application was sent by Mr Abdelkodous to AMW On 17 January 2001.

· The application included a signed confirmation of Mr Khoshaba's employment by the principal of "Rascid Couriers", verifying Mr Khoshaba's income of $43,000 per year. The trial judge found that this document was false. Mr Khoshaba denied any knowledge that such information would be or had been submitted to the lender, and the trial judge accepted that denial.

· On 25 January 2001, the loan application was varied by the addition of Mrs Rose Khoshaba as an applicant. Mrs Khoshaba denied that she signed the loan application. The trial judge found that her signature on the document was a forgery.

· In February 2001, the Respondents signed the Loan Agreement and mortgage, which settled on 15 February 2001.

· On 19 February 2001, Tilda Khoshaba signed the investment agreement with KSE, in her name alone. However, Tilda Khoshaba's evidence was that the investment was a family investment. The trial judge accepted that the Khoshabas regarded themselves as "one economic unit" for the purpose of the investment.

12 The evidence also showed:

· Mr Khoshaba became aware of KSE from discussions amongst the Assyrian community at his Church.

· Mr Khoshaba was subsequently impressed by the Bishop's exhortations to invest with Mr Suleman.

· Mrs Khoshaba was also aware, in July-August 2000, that a lot of people in the Assyrian community were talking about investments they had made with Mr Suleman, from which they were making a lot of income.

13 There was no suggestion in the evidence that any person for whose conduct the Appellant could be said to be responsible played any role in, or obtained any advantage from, the Opponent's investment with KSE.

14 Rolfe DCJ made the following findings of fact about the personal background of the Respondents:

· They came to Australia in 1971.

· In 1978 they purchased the residence which became the subject of the mortgage.

· Mrs Khoshaba had not worked for more than 30 years and Mr Khoshaba had been retired for some time. Both were pensioners.

· The Respondents were members of the Sydney Assyrian community. In that community there was a considerable amount of discussion about the investment scheme operated by KSE, being a pyramid scheme in which investments were made in a shopping trolley collection service business.

· The Respondents had discussions with other members of the community, including Mr Karl Suleman himself, about making an investment.

· They were referred to AMW by the finance broker who lodged a loan application with AMW on their behalf.

15 There were a number of factual disputes as to the communication between Mr Tadros of AMW and the Respondents. These factual disputes were resolved in favour of the Respondents. There is no appeal from these findings. As noted above, the loan application in fact suggested that Mr Khoshaba was in employment. Insofar as false statements had been made on behalf of the Respondents, which included a false statement of income of Mr Khoshaba and a forged signature of Mrs Khoshaba, his Honour exonerated the Respondents from any knowledge or involvement in their making.

16 His Honour rejected the evidence of Mr Tadros of AMW that he had had communication with the Respondents, and had taken other steps in accordance with the Guidelines. He found that he had concocted false records of such communications and steps.

17 His Honour found on the facts that the Appellant, through Mr Tadros of AMW, should have been aware of matters which rendered the Loan Agreement unjust and that AMW had sufficient notice to demand that steps be taken to ensure that the Respondents knew what they were doing. His Honour found that if AMW or RESIMAC had discovered the fact that the Respondents were in fact pensioners, the loan would never have been made.

The Trial Judge's Reasons

18 His Honour referred to two elements which appear to have been decisive in reaching the conclusion that the Loan Agreement and related mortgage was unjust. These two elements were:

> (i) The Appellant's loan assessment Guidelines were not followed in assessing the Respondents' loan application and
>
> (ii) The Appellant did not recommend to the Respondents that they receive independent legal or accounting advice.

19 On the Guidelines issue, his Honour said:

> "AMW simply failed to perform its critical role in the assessment process. That is to say, in performing its assessment role on behalf of the defendant's manager, RESIMAC, AMW departed from the prudent lending practices contained in the RESIMAC guidelines. The reason why the failure to adhere to the guidelines was critical was because the failure to make proper inquiries of the plaintiffs and to verify their circumstances and Mr Khoshaba's employment position made it possible for the transaction to go ahead. There is no way the transaction would have gone ahead if RESIMAC's guidelines had been adhered to. This is what makes the Loan Agreement unjust.
> The RESIMAC guidelines recognise that the system of securitised loans is rife with the possibility of fraud or misrepresentation. They are obviously designed to prevent a fraud occurring. This is beneficial from both RESIMAC's point of view and that of a potential borrower. Fraud occurred in this case because the guidelines were not followed. In particular, the following

examples of the failure to follow the guidelines are pertinent:

(i) Contrary to paragraph 6.2, the Khoshabas were not 'acceptable employment types', because Mr Tadros knew Mrs Khoshaba was in fact a pensioner.

(ii) Contrary to paragraphs 6.3, 6.4 and 6.5, the Khoshabas employment and income position and circumstance were not adequately verified.

(iii) Contrary to paragraph 8.0(1)(d) and (e), the loan submission submitted to RESIMAC did not include sufficient evidence of the Khoshabas' employment or income.

(iv) Contrary to paragraph 8.0(1)(a), the loan submission submitted to RESIMAC did not include 'full details of the loan purpose'.

(v) Contrary to paragraph 15.3, there was a failure to comply with the 'absolutely imperative' requirement that originator managers provided a full and correct disclosure of the intended loan facility; insufficient steps were taken to ensure that no misleading statements were made in connection with the loan.

(vi) Contrary to paragraph 10.6, insufficient steps were taken to ensure documents were unaltered or properly executed.

(vii) Contrary to paragraph 15.10, AMW was not 'especially vigilant' with regard to the loan that was originated by BLI.

(viii) Contrary to paragraph 3.16, the plaintiffs should only have been included as borrowers if it could have been demonstrated, which it was not, that they were to receive a direct financial benefit from the transaction.

In other words, if AMW had done its job, it would have been plain to AMW that the Khoshabas were the putative victims of a fraud and the loan would never have proceeded. I am therefore comfortably satisfied that the failure of AMW to perform its task in a manner demanded of it by the RESIMAC guidelines renders the Loan Agreement an unjust contract.

It follows, as a matter of logic, that the Mortgage is therefore an unjust contract as well." (40-42)

20 I interpolate to note, notwithstanding that his Honour said on two occasions that the contract was "unjust" because of a failure to adhere to the Guidelines, counsel for the Respondents did not seek to uphold the reasoning on that basis. He submitted that the Court should understand his Honour to have reached the conclusion of 'unjustness' on the full range of relevant factors, but that he had given particular weight to the two matters that were dealt with at length.

21 As to the independent advice issue, his Honour said:

"In addition to the foregoing, but as a separate finding, I am comfortably satisfied that the defendant, through RESIMAC and AMW, should have ensured that in the circumstances the plaintiffs were given the opportunity of obtaining independent legal or accounting advice. I have no doubt that any solicitor or accountant advising the Khoshabas would have discovered that something was very odd about the Loan Application being approved for two pensioners and would have had serious doubts about Karl Suleman's investment scheme. Obviously, if the defendant had required the giving of independent advice, as I am satisfied that it should have, no injustice would have arisen, as any competent professional would have advised against the entry into the transaction.

It is no excuse for the defendant to suggest that it was unaware of there being any improper behaviour and it was unaware of any disability relating to the Khoshabas. In this regard the plaintiffs submit that through AMW the defendant did 'know' in the relevant legal sense. The plaintiffs submit that the Court must consider as part of its determination concerning the unjustness of the Loan Agreement and Mortgage whether the defendant had knowledge of such facts as ought to have raised in its mind the possibility that the plaintiffs had not been in a position to make a judgment as to their interest in a properly informed manner. I accept the plaintiffs' written submissions in chief on this issue which are set out in paras 21-33 of counsel's written submissions. Given the fact that the plaintiffs were

pensioners and that the loan application submitted to RESIMAC did not include sufficient evidence of the plaintiffs' employment or income, or full details of the loan purpose, this was a case which called out for simple inquiry of the plaintiffs as to whether or not they had been independently advised. In the absence of that inquiry by Mr Tadros, or anyone else on behalf of the defendant, I am satisfied that the Loan Agreement and Mortgage are unjust because of the circumstances that existed at the time the Loan Agreement and Mortgage were executed." (42-44)

22 Of the Respondents' contentions in pars [21]-[33], which his Honour adopted by reference, the most significant are:

"21. As Mr Tadros said:

Q. It would have been a good idea for people to get independent advice in circumstances such as this, in issue in this case.

A. I believe so, yes.

22. The lack of proper inquiry or requiring independent advice is another factor demonstrating why this contract was unjust. The advice should have been substantive; in addition to an explanation of the terms of the transaction, it was necessary that the advice include advice on whether the transaction is in the interests of the weaker party in the circumstances; in other words, whether the weaker party should proceed with the transaction.

23. The extent of the risk which is being undertaken cannot be ascertained merely from the terms of the contractual documentation: it is necessary to consider it in the context of the totality of the Khoshabas' circumstances and the context of the circumstances in which the contracts arose; this would have included the financial soundness of the proposal part of which was the patently absurd investment proposition.

24. It is no answer to this case to say it was all somebody else's fault. Any absolute rules are inconsistent with an assessment of unjustness that is determined by a statutory charge to take account of the public interests and all the circumstances of the case (sec 9(1)) and other specified factors (sec 9(2)).

25. Obviously enough, as with the lending guidelines referred to above, relief is not able to be obtained just because a Bank or other financial institution does not require independent advice be obtained. This must be so: it cannot be argued that it demonstrates unjustness for someone who understands a loan contract or mortgage and the attendant risks to be deprived of the opportunity of having explained what he already understands. Notwithstanding this, there must be circumstances, such as here, where independent advice was clearly appropriate and its absence ensured the unjustness pregnant in the transaction was not salved.

26. The lack of independent advice is but one of the factors to be considered. Without limiting the generality of the factors to be taken into account, independent advice is one of the specified sec 9(2) factors to which the Court is required to pay regard. In certain circumstances its absence is determinative if a finding is made, as the Khoshabas' submissions urge, that there was no real understanding of the underlying transaction.

...

28. The defendant cannot excuse this behaviour by suggesting it did not 'know' of any improper behaviour or any disability of the Khoshabas. Indeed, by reason of the behaviour of AMW, the primary submission of the Khoshabas is that the defendant did 'know' in the relevant legal sense.

...

31. The Court must consider, as part of the unjustness calculus whether the defendant had knowledge of such facts as ought to have been raised in its mind [sic] the possibility that the applicants for relief had not been in a position to make a judgment as to their interests in a properly informed manner."

23 It is possible to read his Honour's words: "In addition to the foregoing, but as a separate finding ..." as implying that his Honour concluded that the contract was not just on *each* of two *alternative* bases. The word "finding" is not, however, a word that necessarily suggests that. The Respondents did not submit that the Court should proceed on that basis. The two issues became inextricably interwoven when his Honour

proceeded to consider the independent advice point on the basis that *both* applicants for the loan were pensioners. This is something which the Appellant would only have known if the Guidelines had been followed. It is, accordingly, unnecessary to identify appellable error in the *House v The King* sense with respect to his Honour's analysis of the independent advice issue.

24 As quoted above, his Honour expressly accepted pars [22] and [26] of the Respondent's submissions which, I repeat, state:

> "22. The lack of proper inquiry or requiring independent advice is another factor demonstrating why this contract was unjust."
> "26. The lack of independent advice is but one of the factors to be considered …"

25 These references are inconsistent with any suggestion that the independent advice was, of itself, sufficient to lead to a conclusion that the contract was unjust.

26 The Respondents' submissions in this Court proceeded on the basis that his Honour's finding of 'unjustness' was based on the full range of relevant factors. They did not suggest that his Honour's reasons should be understood as expounding two alternative bases for this conclusion. Accordingly, the concluding sentence of this passage of his Honour's reasons quoted above - that the contract was unjust - should be understood in the same way as his Honour's similar references when dealing with the Guidelines issue.

27 The Appellant submitted that this Court should treat these two elements as the only factors which his Honour took into account. This submission should be rejected. His findings must be understood, as the Respondents submitted, in the context of the other matters about which his Honour made findings and which are pertinent to what Mason P has called "the unjustness calculus" (*St George Bank Ltd v Trimarchi* [2004] NSWCA 120 at [36]). I have set out above the relevant findings in the section headed Background Facts.

28 It is also pertinent to note his Honour's earlier factual finding:

> "I have no doubt that if either of the Khoshabas had been spoken to by someone from AMW or RESIMAC about their circumstances and their employment position, that the Khoshabas would have unhesitatingly told the truth. Had such inquiries been made, then obviously the loan would never have been made to the plaintiffs."

29 His Honour also accepted the submission on behalf of the Respondents that the Appellant had constructive knowledge of facts which should have raised in the minds of persons acting on its behalf a realisation that the Respondents were not in a position to make a judgment as to their interests in a properly informed manner. Picking up the reference to "a simple inquiry" in the judgment of Deane J in *Commercial Bank of Australia Limited v Amadio* (1983) 151 CLR 447 at 479, Rolfe DCJ concluded:

> "Given the fact that the plaintiffs were pensioners and that the Loan Application submitted to RESIMAC did not include sufficient evidence of the plaintiff's employment or income, or full details of the loan purpose, this was a case which called out for simple inquiry of the plaintiffs as to whether or not they had been independently advised."

The Appellate Role

30 Section 7(1) relevantly provides:

> "(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 the following …"

31 Different views have been expressed as to the appropriate test for appellate intervention with a first instance finding under s7(1) of the Act that a contract was unjust. Some have taken the view that the appeal court must find appellable error in accordance with the well-known test in *House v The King* (1936) 55 CLR 499 at 505. Others have taken the view that the formulation of the judgment for which s7(1) calls is not the exercise of a discretion, although an appellate court would exercise restraint before interfering with a finding of fact of this evaluative character. The different views are set out in *Murphy v Overton Investments Pty Ltd* [2002] FCAFC 129 at [104]-[109].

32 The contemporary jurisprudence of the High Court emphasises that the starting point for the determination of such issues must be a careful analysis of the text of the statute establishing the right to appeal. (See, e.g. *Fleming v The Queen* (1998) 197 CLR 250 at [7]-[12]; *Dinsdale v The Queen* (2000) 202 CLR 321 at [20]-[22], [57]-[58]; *Coal & Allied Operations Pty Ltd v AIRC* (2000) 203 CLR 194 at [5]-[19]; *Roy Morgan Research Centre Pty Ltd v State Revenue (Vict)* (2001) 207 CLR 72 at [9]-[12], [46]-[51]; *Fox v Percy* (2003) 214 CLR 118 at [21]-[23]; *Weiss v The Queen* (2005) 80 ALJR 444 at [9]-[11], [31]-[40]; *CSR Ltd v*

Della Maddalena [2006] HCA 1 at [13]-[19].)

33 The issue is not always easy to determine. In the United Kingdom there are two different regimes in which the court has to determine the "reasonableness" or "fairness" of a contractual provision. The House of Lords has determined that the *Unfair Contract Terms Act* 1977, concerning exemption clauses, involves a discretion. (*George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd*[1983] 2 AC 803.) However, the *Unfair Terms in Contract Regulations* 1999, it appears, does not. (*Director General of Fair Trading v First National Bank plc* [2002] 1 AC 481.) This is so even though the similarity between the two tests has been described as "profound". (*Chitty on Contracts* (28th Ed. 1999) at [15-050].)

34 The structure of s7(1) involves a two-stage inquiry: first, was the contract unjust; secondly what, if any, orders should be made. The second stage is clearly discretionary. The first stage may more accurately be described as a judgment. (On this distinction in administrative law see: Francis Bennion "Distinguishing Judgment and Discretion" [2000] *Public Law* 368; Bennion "Judgment and Discretion Revisited: Pedantry or Substance" [2005] *Public Law* 707.)

35 The word "discretion" is often deployed loosely in legal discourse. (See *Norbis v Norbis* (1986) 161 CLR 513 at 518; *Coal & Allied v AIRC* supra at [19].) It is sometimes suggested that any decisions involving a value judgment on which reasonable minds may differ is a discretionary judgment (e.g. *Norbis v Norbis* supra at 518, 540; *Russo v Aiello* (2003) 215 CLR 643 at [27]). This reasoning supports the Respondents' contention. However, the contrary view has also been strongly advanced. (See *Buller v Black* (2003) 56 NSWLR 425 at [37]-[38], [96]; *Blackburn v Allianz Australia Insurance Ltd* (2004) 61 NSWLR 632 at 634 [2]-[4]; *Figliuzzi v Yonan* [2005] NSWCA 290 at [31]-[36], [67]-[68].)

36 The High Court decisions in *Singer v Berghouse* (1994) 181 CLR 201 at 210-212 and *Coal & Allied v AIRC* supra at [19]-[21], on different legislation also appear to support the conclusion that the s7(1) decision is discretionary. Of course each statutory scheme must be considered separately. The statutes considered in *Singer v Berghouse* and *Coal & Allied v AIRC* also involved a two stage process. In each case the first stage involved a judicial evaluation, by the application of a broadly stated standard to particular facts, and the second stage involved judicial selection from a range of options.

37 However, in *Singer v Berghouse* supra the majority judgment emphasised at 210-211 that, notwithstanding the evaluative character of the first stage it remained a finding of fact. In *Coal & Allied v AIRC* supra at [2], the majority judgment referred to the degree of subjectivity involved in making the first stage judgment and said that it could be "described as a discretionary decision" albeit "in a broad sense".

38 That what is involved in the first stage of s7(1) of the Act under consideration is a finding of fact is suggested by the text:

· Note s7(1) states: "… the Court *finds* a contract … to have been unjust."

· Subsections 9(1) and (4) use the language of fact when they state: "In determining whether a contract … *is* unjust …"

39 This contrasts with other language, e.g. a requirement that the Court must be "satisfied" of the relevant matter, as was the case in *Norbis v Norbis, Singer v Berghouse* (208) and *Coal & Allied v AIRC* (199). Such a statutory provision can be accurately described as conferring "a very wide discretion". (See *Buck v Bavone* (1976) 135 CLR 110 at 119.)

40 Where, as here, the first statutory step is clearly a finding of fact, albeit one involving a broadly based value judgment, it may be that the Court should invoke the principles reflected in *Warren v Coombes* (1979) 142 CLR 531 rather than in *House v The King*. Nevertheless, in most cases it is unlikely that the different tests will lead to different results.

41 It is not necessary to resolve this issue as, in my opinion, the trial judge has committed an appellable error.

The Guidelines Ground

42 Mr M Cashion SC, who appeared for the Appellants, accepted that the fact of departure from the guidelines was a relevant consideration in the determination of 'justness'. He submitted that such departure was not, of itself, entitled to significant, let alone determinative weight. I agree with that submission, at least in a case where the departure from the Guidelines is not evidence of departure from prudent lending practice or, as Mason P expressed it in *St George Bank Ltd v Trimarchi* [2004] NSWCA 120 at [44], "normal and appropriate lending practice".

43 As quoted above, his Honour identified the failure to comply with the RESIMAC guidelines as one of two matters which he emphasised when concluding that contract was unjust. In the course of that reasoning his Honour referred to "the prudent lending practices contained in the RESIMAC guidelines". His Honour said, as quoted above, that the guidelines were "designed to prevent a fraud occurring". His Honour added "this is

beneficial from both RESIMAC's point of view and that of the potential borrower".

44 The Appellant submits that his Honour's findings, particularly his reference to "prudent lending practice", departed in a material way from the case run at trial.

45 The Appellant submits that no case was propounded that failure to comply with "prudent lending practice" was an element in the evaluation. It asserts that the case advanced relied, and relied only, on the mere fact of departure from the Appellant's Guidelines.

46 In its Statement of Claim the Respondents, as plaintiffs below, particularised a range of respects in which it was said that the Loan Agreement and the Mortgage were said to be unjust contracts within the meaning of the Act. At the commencement of the trial they sought to amend those particulars by adding a particular (h) as follows:

> "The loan was made otherwise than in accordance with prudent lending practice."

47 The proposed amendment was objected to on the grounds that it changed the nature of the case and would require the Appellant to adduce additional evidence on, inter alia, what "prudent lenders" would do and specifically refer to the need to adduce expert evidence.

48 Specifically Mr J Simpkins SC, who appeared for the Appellant at trial, said:

> "But for the first time we are being required, if this amendment is permitted, to seek to justify what we do or didn't do by reference to the practices of other prudent lenders." (9/11/04 T14 lines 45-48)

He reiterated his understanding of the purport of the amendment when he said:

> "So the second basis of objection is that … whether my client conformed to prudent lending practice …" (9/11/04 T15 lines 34-36)

49 The particular in this form was withdrawn (T 9/11/04 at pp12-16). A new particular (h) was added which simply stated:

> "The loan was made otherwise than in accordance with the RESIMAC Prime Mortgage Programme Guidelines in that: …"

50 Mr Simpkins SC had also objected on the basis of insufficient particularisation. The new particular (h) identified a range of paragraphs (i) through to (xii), specifying each of the paragraphs of the Guidelines said not to have been complied with.

51 Mr M B Lee who appeared for the Appellant both at trial and this Court, when putting the detailed amendments before the trial judge, said:

> "Lee: … In respect of paragraph (h) I abandoned the very general words and sought to set out with specificity the particular … paragraphs … of the RESIMAC Prime Mortgage Programme Guidelines that we say were not complied with in relation to this loan … So this is not a general reference to prudent lending guidelines, this is entirely focused on what is in the RESIMAC Prime Mortgage.
> His Honour: It's subjective rather than objective.
> Lee: Yes." (10/11/04 T2 lines 34-48)

52 In my opinion, the case did not proceed on the basis that one of the particulars of the injustice was a failure on the part of the Appellant to observe prudent lending practice, represented by the Guidelines. Rather it was the Appellants mere failure to comply with its own Guidelines that was the element to be inserted in the evaluation.

53 Mr Lee submitted that a fair reading of his Opening, particularly his reliance on *Trimarchi*, and of his cross-examination of Mr Tadros from AMW, indicated that the case as it developed during the course of the trial was such as to make clear that the Respondents did contend that a breach of the RESIMAC Guidelines amounted to a breach of prudent lending practice. If so, this represented a substantial change in the nature of the case. He observed that no objection was taken to references to "prudent lending practices" in the written submission. I am reluctant to accept that so significant a change in the case occurred impliedly, when it had been expressly abjured at the time the pleadings were amended.

54 No particular part of the Opening is relied on. I am unable to discern anything sufficiently specific. The relevant reference to *Trimarchi* at [44] occurred at a time when Mr Lee was contending for particular (h) in its original form and before it was withdrawn (See 9/4/04 T13 lines 11-20). The cross-examination on departures from the Guidelines did identify reasons for the existence of the guidelines which were capable of establishing that compliance was "prudent". However, it was also pertinent to establishing the fact and extent of departure.

55 This was not sufficient to permit the Respondents to rely, by a process of implication, on a particular which

had been abandoned. In my opinion, nothing occurred which would justify reading the actual particular (h) as if it meant the same as the originally proposed particular (h).

56 In my opinion, his Honour erred in relying on the Guidelines as constituting prudent lending practice. This was not how the case was run.

57 The Appellant also submitted that there was no evidence that the Guidelines constituted prudent lending practice. I would not have accepted that submission. Their very existence, and the evidence of the Mr Tadros, could have sufficed. However, in view of the conclusion to which I have come above, it is unnecessary to elaborate.

58 Whatever the appropriate approach to appellate intervention, the Appellant had made out its case in this regard. His Honour should not have determined the case on the basis that the Appellant's failure to follow the Guidelines was a departure from prudent lending practice.

Was the Contract Unjust?

59 In another case, it would be appropriate to remit the matter for redetermination. However, the amount involved in this dispute is not large. The legal costs are already a substantial proportion of the amount in dispute. It would be a travesty to order a new trial. The parties asked this Court to determine the matter. It should do so.

60 An important feature of this case is that no criticism has been directed to the terms and conditions of the loan and mortgage entered into between the parties. Nor has it been suggested that the Appellant received any advantage, direct or indirect, from the transaction other than that specified in the loan agreement itself. What is said to be unjust is the fact that the Appellant agreed to give a loan to the Respondents at their request in circumstances, not known to the Appellant, that funds advanced would be used for a dubious investment.

61 Another important aspect of this case are the credit findings by his Honour in favour of the Respondent, particularly his finding that the Respondents were unaware of the false information in the application and the finding that Mr Tadros did not undertake the various checking tasks which he asserted had occurred. These findings were not challenged.

62 It is also pertinent to note that the Appellant did not make any submission that his Honour erred in approaching the issue of 'justness' from the perspective of the two Respondents. Nor did it submit that this Court should not adopt the same perspective. As I have noted above, his Honour made a finding that the loan and the investment had been entered into by the whole family unit, including the Respondents' daughter. She had a reasonable income and had originally proposed herself as the borrower for that reason. His Honour did not appear to apply his finding about a single family unit, in the evaluation of 'justness'. This Court was not asked to do so or to find that his Honour erred in doing so.

63 In many respects this case, in its basic structure, is similar to that considered by this Court in *West v AGC (Advances) Ltd* (1986) 5 NSWLR 610 where the Court held, by majority, that the contract was not "unjust". The Appellant in this case relies on a number of steps in the reasoning in *West* in support of its contention that the contract in the present case should not be found to be "unjust".

64 Of course each case must depend upon its own facts. Furthermore, *West* is now 20 years old. When the Parliament adopts so general, and inherently variable, a standard as that of 'justness', Parliament intends for courts to apply contemporary community standards about what is just. Such standards may vary over time, particularly over a period of two decades.

65 There have been observations in this Court that the standards may have changed from those applied in 1986 in *West.* (See *Elkofairi v Permanent Trustee Co Ltd* [2002] NSWCA 413; (2003) 11 BPR 20,841 at [79].)

66 The Appellant relied on the distinction drawn by McHugh JA in *West* at 621 between the contract and the overall transaction, relevantly the loan and the investment of the funds. On the basis of that distinction the Appellant submitted (T p22 cf T 31) that the investment agreement was not part of the "circumstances relating to the contract" within s7(1). In my opinion this submission should be rejected.

67 Nothing McHugh JA said in *West* suggests that the purpose for which a loan is obtained is not one of the relevant "circumstances". His Honour was drawing attention to the fact that the ultimate focal point of consideration under s7(1) must be the contract sought to be set aside or varied.

68 In my opinion, the purpose for which a loan is advanced is a relevant circumstance. This is confirmed by s9(2)(l) which includes, amongst the matters to which a court shall have regard in determining whether a contract is unjust: "The commercial or other setting, *purpose* and effect of the contract."

69 The purpose of a loan is a concern of a lender, because it is usually a material consideration in

determining whether the particular lender is able to service and repay the loan. The Appellant's own Guidelines confirm the relevance of this matter, both in identifying the requirement that the purpose be specified and in the structure of the Guidelines themselves. In detail not necessary to be set out, the Guidelines specify quite distinct criteria, including different maximum amounts of loans, for different kinds of purposes to which the loans will be applied.

70 Accordingly, the purpose of the loan is a relevant circumstance relating to the contract within the meaning of s7 of the Act.

71 The Appellant also relied on the following observations of McHugh JA in *West*:

> "If a contract or one of its relevant provisions is neither unfair nor unreasonable so far as the applicant is concerned, it is difficult to see how the existence of inequality in bargaining power or lack of independent advice, for example, can render the contract or a provision of the contract unjust.
> …
> If a defendant has not been engaged in conduct depriving the claimant of a real or informed choice to enter into a contract and the terms of the contract are reasonable as between the parties, I do not see how that contract can be considered unjust simply because it was not in the interests of the claimant to make the contract or because she had no independent advice." (621)

72 His Honour referred to a distinction between a contract which was "unfair" and one that was "unjust" and said:

> "… A contract will not be unjust as against a party unless the contract or one of its provisions is the product of unfair conduct on his part either in the terms which he has imposed or in the means which he has employed to make the contract." (622)

(And see *Crowe v Commonwealth Bank of Australia* [2005] NSWCA 41 at [75]-[77].)

73 His Honour's reasoning is instructive. It was, however, directed to the issues in that case. Where the Court has to apply a standard as general as what is "unjust", it cannot be confined by such reasons as if they were rules. I do not understand McHugh JA to have put forward these observations as rules. Rather, the observations are to be understood, correctly, as identifying relevant considerations entitled to significant weight.

74 The same can be said of the observation of Gleeson CJ, on which the Appellant relied in *Baltic Shipping Co v Dillon* (1991) 22 NSWLR 1 at 9, that:

> "… the general policy of the law is that people should honour their contract. That policy forms part of our idea of what is just."

75 In any event, the Appellant did engage in relevant conduct – by way of the failure to observe its own Guidelines and to recommend independent advice – which makes the particular reasoning in *West* not directly applicable.

76 Plainly, the conduct, whether by act or omission, of the party resisting a finding of unjustness under the Act is highly relevant, and will often be determinative. However, the scope of relevant circumstances is not confined to what the person resisting an order under s7(1) did or did not do and knew or ought to have known. The critical phrase in s7(1) – "the circumstances relating to the contract at the time it was made" – cannot be so limited. Section 9(1) provides that when determining unjustness "the court shall have regard to the public interest and to all the circumstances of the case". Furthermore, s9(2)(l) includes, as I have noted, amongst the relevant circumstances "the commercial or other setting, purpose and effect of the contract".

77 In the present case, the Appellant submitted, correctly in my opinion, that the fact that the Appellant had no involvement of any kind in the investment was entitled to significant weight in its favour.

78 The Appellant's submissions as to how this Court determine the issue of 'unjustness', against the background of uncontested factual findings, focused on the two particulars which Rolfe DCJ had emphasised: failure to comply with the Guidelines and failure to recommend independent advice. With respect to the first of these I set aside, for the reasons discussed above, any use of the Guidelines as an indication of prudent lending practice.

79 The Appellant submitted that the failure to observe its own Guidelines was not entitled to substantial, let alone determinative, weight. The Appellant accepted that the failure was a relevant consideration. However, it submitted that the Guidelines were designed for the purpose of protecting the lender, not the borrower. Their purpose was to enable the Appellant to assess and minimise its own risk.

80 This proposition can be accepted, but it does not lead to the conclusion, urged on the Court by the Appellant, that the failure is entitled to minimum weight when determining what is just in all the

circumstances. The benefit to the borrower from a proper risk assessment may be indirect, because unintended, but that does not mean that it cannot, in appropriate circumstances, be entitled to significant weight in the determination of unjustness. It is clear from the list of factors contained in s9(2) and (3) of the Act, that a substantial purpose of the legislative scheme is to protect persons who are not able to look after themselves.

81 Rolfe DCJ's finding of fact, which is not challenged, that if the Guidelines had been observed the Appellant would never have advanced the loan to the Respondents was justified. The finding does not go only to causation. It is a factor entitled to be taken into account and given weight in the determination of unjustness.

82 I have set out above in the extract from his Honour's findings on the Guidelines issue each of the respects in which the Appellant failed to observe its own Guidelines. Of these failures the most significant, in my opinion, is the fact that the section of the standard form application about the purpose of the loan was left blank. This indicates that, as in *Elkofairi* supra at [79], the Appellant "was content to lend on the value of the security". In my opinion, that approach is entitled to significant weight in the determination of unjustness. (I note that nothing like this occurred in *West* where the purpose of the loan was known.)

83 On the information actually available to the Appellant, a husband and wife – one with a $43,000 per annum income and the other a pensioner – borrowed $120,000 for, as far as the Appellant cared to know, immediate expenditure. Enforcing a security against the personal residence of such borrowers should not be treated as if it were the first resort. That is what, on paper, the Appellant can be described as having done.

84 This conclusion is reinforced by the Appellant's concomitant failure to verify or follow up, in the way identified by Rolfe DCJ, other details in the loan application. I do not suggest that the matter can be approached, as his Honour appeared to do, on the basis that the Appellant should be fixed with the knowledge it would or may have acquired if the Guidelines had been observed. However, the other failures, such as not verifying employment and income and not ensuring documents were properly executed, reinforce the conclusion that the Appellant was prepared to act on the basis of adequate security alone.

85 Where the security is the family home of a low income earner and a pensioner, this posture on the part of a lender is entitled to significant weight against the lender in the determination of unjustness.

86 With respect to the independent advice issue, McHugh JA left open a significant relevant matter in *West,* when he said:

> "A nice question would arise as to whether a contract which did no more than make reasonable provision for the protection of the lender was nevertheless unjust because the lender had not insisted that the borrower get independent advice whether she should borrow money from it. That is, the question would be whether the conduct of the lender was unfair in its dealing with the borrower so as to make the contract unjust. An affirmative finding of an unjust contract in those circumstances would seem to imply that the lender owed a duty to the borrower to ensure that she used the borrowed money wisely or, at all events was able to repay the instalments." (629)

87 With respect to the independent advice issue, the Appellant submitted:

· No aspect of the loan agreement or the mortgage required independent advice.

· The decision to invest was made independently of the Appellant on the basis of an evaluation of the investment by the Respondents.

· There was no evidence, nor was it part of the Respondents' case, that AMW was associated with or was in any way connected with KSE.

· Neither AMW, nor the Appellant knew anything about the proposed investment and, in particular, about the terms of the Investment Agreement, its risks and returns. The Respondents' knowledge of the investment was greater than the Appellant's.

· There was no inequality between the lender and borrower in terms of understanding the risks associated with using proceeds from the Investment Agreement to repay the loan.

· The fact that a lender has knowledge that one of two loan applicants for a joint loan is a pensioner, is not a circumstance that calls for a lender to recommend independent legal or accounting advice. The Appellant submitted that it did not know that Mr Khoshaba was in receipt of a pension or that the income attributed to him in the loan application was false. Whilst the Appellant is taken to have been on notice that Mrs Khoshaba was in receipt of a pension, the loan application did not attribute any income to Mrs Khoshaba and, therefore, in terms of the lender's credit assessment, Mrs Khoshaba was not material.

· Whether or not a loan application contains sufficient evidence of income is a matter for a lender to decide, it being a commercial decision for the lender. It is not a matter that calls for a lender to recommend independent legal or accounting advice.

· The mere fact that a loan application does not disclose the purpose of the loan, is not a circumstance that warrants an inquiry by the lender as to whether the borrowers had received independent legal or financial advice.

88 I have set out above, the reasons of Rolfe DCJ on the independent advice issue. His Honour did not expressly indicate what were the circumstances which ought to have led the Appellant to ensure that the Respondents obtain "independent legal or account advice". He expressed himself in the language of causation when he concluded that such advice "would have discovered that something was very odd" about a loan being approved for two pensioners and would have had serious doubts about KSE investment scheme, leading to advice that the Appellants should not have entered the transaction. In the passage I have quoted above, his Honour concluded that the contract was unjust because of the failure to inquire whether the Respondents had obtained independent advice.

89 The reference to "independent advice" in s9(2)(h) of the Act and in the case law, is a reference to advice "independent" of the party to the contract seeking to resist an order under s7 of the Act. No such advice was relevant, in the circumstances of this case, with respect to the loan agreement and mortgage sought to be set aside. The relevant advice was with respect to the investment agreement and whether the parties should borrow anything at all.

90 In a tripartite situation such as this, I do not believe that a failure to recommend that a person obtain advice is entitled to significant weight when the advice is relevant to that part of the transaction which does not involve the rights and obligations or interests of the person who is said to have failed to make the recommendation. Even pensioners must take responsibility for their own actions.

91 On the facts of the present case, it appears clear that the overwhelming enthusiasm of their compatriots in the Assyrian community was the primary motivating factor in the Respondent's wish to obtain the loan. I doubt that any recommendation by the prospective lender would have had any effect.

92 The conflicting considerations are finely balanced. Had the Appellant or its representatives made any inquiries about the purpose of the loan I would have allowed the appeal. I do not mean to suggest that the Appellant had to determine that the proposed investment was reasonable and capable of servicing the loan. It is the indifference, suggesting that the Appellant was content to proceed on the basis of enforcing the security, which I find determinative.

93 The Appellant submitted that this Court should re-exercise the discretion and, in the circumstances, refuse to grant relief under the Act. The Appellant submitted that it was generally unsound to grant relief under s7 where the party against whom relief is claimed was both innocent and ignorant of the circumstances giving rise to that injustice.

94 The Appellant relied on a number of authorities including the judgment of Meagher JA in *Beneficial Finance Corp Limited v Karavas* (1991) 23 NSWLR 256 at 277 where his Honour said:

> "There is jurisdiction under the Act to make orders in favour of a party to a contract who proves that at the date of the contract he suffers from a relevant disability even though the other party to the contract is unaware of that disability, although in general it would be unsound to exercise the jurisdiction in those circumstances. … The reason for that view is that it is hardly just to deprive an innocent person of valuable property, of which contractual rights are a species. Nevertheless such a jurisdiction undoubtedly exists."

95 To similar effect were the observations of Sheller JA in *Nguyen v Taylor* (1992) 27 NSWLR 48 where his Honour said, after referring to the reasoning of Meagher JA in *Karavas*:

> "The question of the unjustness of the contract is to be determined in the circumstances relating to the contract at the time it was made and, in this case, without regard to the ignorance or innocence of the appellant. However when coming to determine how the discretion should be exercised the court, in my opinion, is entitled to have regard to additional circumstances and importantly for the purposes of the present case the ignorance and innocence of the appellants … in the context that it was the respondent's agent who misled him."

96 I do not doubt the existence of the discretion. It falls to be exercised afresh in this Court. In my opinion the Appellant cannot be regarded as an innocent party of the kind referred to in the authorities. Again I place particular reliance on the indifference of the Appellant and its representatives to the purpose of the loan, indicating that it was content to proceed on the basis enforcing the security. This is not a case for the exercise of the discretion to refuse relief.

97 It was not submitted that his Honour's orders should be varied if this Court reached this conclusion. In such

a case it would be appropriate, if requested, for the Court to ensure that a person in the position of the Appellant would be subrogated to any rights the Respondents had against third parties. Quite probably such rights are regarded as of little value and that may explain why no submission was made in this respect.

98 The orders I propose are:

1 Grant leave to appeal.

2 Direct the Appellant to file a Notice of Appeal within 14 days hereof.

3 Appeal dismissed.

4 The Appellant to pay the Respondents' costs.

99 **HANDLEY JA**: In this appeal I have had the benefit of reading the reasons for judgment of the Chief Justice and Basten JA in draft form. I agree that a case under the Contracts Review Act involves a three stage process – the making of findings of primary fact where these are disputed, the formation of an evaluative judgment as to whether or not the contract is unjust, and why, and then, if necessary, the exercise of the Court's discretionary power to grant relief and determine its extent.

100 The first stage may involve credit findings, and the drawing of inferences which attract the usual standards of appellate review, the second involves a drawing of inferences and the application of an indeterminate legal standard which, as to fact is subject to review in accordance with *Warren v Coombs* (1979) 142 CLR 531, and as to law is open to full review. The exercise of the Judge's discretion on the nature and extent of relief is subject to review in accordance with the principles in *House v The King* (1936) 55 CLR 499.

101 I agree with Basten JA that the phrase "the unjustness calculus" is not helpful because it suggests, wrongly, that the exercise is mechanistic whereas in my view it is, within broad legal limits, impressionistic and evaluative.

102 The appellant was a trustee for Resimac Ltd which managed a securitised mortgage programme. Resimac employed Australia Mortgage Wholesalers Pty Ltd (AMW) as its agent to assess loan applications on its behalf and pass on to Resimac approved applications for its acceptance. However it is clear from the evidence of Mr Tadros of AMW that Resimac relied on AMW to ensure that applications fell within its guidelines and were otherwise appropriate for acceptance. One of the duties of AMW as agent of Resimac was to satisfy itself that the information on the loan application was correct and to approve or reject applications in accordance with Resimac's guidelines.

103 In cases such as this the he legal rights of the principal are governed by the acts and state of mind of the agent as if they were its own: *Permanent Trustee Australia Co Ltd v FAI General Insurance Co Ltd* (2001) 50 NSWLR 679, 693-98, not affected on this point by the decision of the High Court (2003) 214 CLR 514. Accordingly the knowledge of AMW, including its knowledge that Resimac's guidelines had not been complied with, was for legal purposes the knowledge of Resimac, and the appellant as trustee for Resimac can be in no better position.

104 Subject to the above I agree with the Chief Justice and the orders he proposes.

105 **BASTEN JA**: I gratefully accept the explanation of the issues in this appeal, as set out by the Chief Justice, with whose reasons I agree, subject to what follows.

Nature of appeal

106 In considering an application for relief under s 7 of the *Contracts Review Act* 1980 (NSW) the Court must undertake a three stage process although, of course, the steps need not be taken in a particular order or necessarily identified as separate steps. The first step is to make findings of primary fact as to the circumstances revealed in the evidence. In undertaking an appeal by way of rehearing, from a trial judge sitting without a jury, this Court should approach a review of the facts in accordance with the principles identified in *Fox v Percy* (2003) 214 CLR 118. In this case, there was no fresh or further evidence to be considered.

107 The second step in the process is a finding that a contract or a provision of a contract is "unjust". This, as the Chief Justice notes at [38], is variously described in s 7(1) as a finding and in s 9(1) and (4) as a determination. On either description, the Court is not exercising a discretionary power, but making an evaluative judgment as to the whether the facts as found satisfy a statutory description which in turn engages a discretionary power. The determination that a pre-condition or criterion for the exercise of the power is met, may properly be equated with the drawing of an inference and is therefore reviewable in accordance with the principles established in *Warren v Combes* (1979) 142 CLR 531 at 551-552 (Gibbs ACJ,

Jacobs and Murphy JJ).

108 In *Buck v Bavone* (1976) 135 CLR 110 at 118-119, Gibbs J considered the extent to which a court could review the decision of an administrative authority which was required to be "satisfied" of the existence of certain matters specified in the statute. As his Honour noted (at 118) such a state of satisfaction must be properly formed and will be set aside if formed "arbitrarily or capriciously": see also *Minister for Immigration and Ethnic Affairs v Wu Shan Liang* (1996) 185 CLR 259 at 274–276 (Brennan CJ, Toohey, McHugh and Gummow JJ) and *Minister for Immigration and Multicultural Affairs v Eshetu* (1999) 197 CLR 611 at [131]-[137] (Gummow J). As noted by Gibbs J in *Buck v Bavone* at 119, the possibility of demonstrating error is likely to depend upon whether the statutory criterion is narrowly defined, or whether it admits of matters of "opinion or policy or taste". Section 9(2) requires a court to take in to account, in determining whether a contract is unjust, a set of matters, some of which are defined with reasonable precision, but others of which are not. In the latter category may be found the requirement that the Court shall have regard to "the public interest" and to the circumstances of the case, including the consequences or results which may arise from compliance with any or all of the provisions of the contract: s 9(1).

109 The third step involves the exercise of the power to grant relief which may, but need not, follow from the conclusion that a contract or a provision thereof is unjust. That is truly a discretionary power to be exercised if the Court "considers it just to do so, and for the purpose of avoiding as far as practicable an unjust consequence or result": s 7(1). The exercise of the power will be reviewable only in accordance with the principles established in *House v The King* (1936) 55 CLR 499 at 504-505.

110 As the Chief Justice notes, there is authority which would support differing approaches to these questions in different statutory circumstances, but the trend of authority in this Court in relation to similar provisions is consistent with this approach: see [35]-[37] above. In the context of this Act, the question has been adverted to on a number of occasions, without a definitive result being achieved: see *Antonovic v Volker* (1986) 7 NSWLR 151; *SH Lock (Australia) Ltd v Kennedy* (1988) 12 NSWLR 482 and *Beneficial Finance Corporation Ltd v Karavas* (1991) 23 NSWLR 256. The principles set out above are consistent with those adopted by Samuels JA in *Antonovic* (at 154-155, Kirby P agreeing) and reiterated by his Honour in *Karavas* (at 270E), in the following terms:

> "To my mind the finding that a contract is unjust is no more discretionary in character than a finding that an act or omission was negligent, a conclusion about which different minds may also take different views. But the fact that it may be difficult to determine a factual conclusion does not mean that it is to be perceived as inhabiting an area in which the fullest rein is to be given to the predilections of individual judges without the wholesome restraint of uniformity which the attentions of an appellate court is designed to provide."

111 In *Antonovic*, giving the matter a slightly different flavour, Samuels JA expressed himself "reluctant too readily to attribute to determinations of this kind the comparative immunity from review conferred upon those decisions which are treated as exercises of judicial discretion": at p 155.

The section 9 considerations

112 The considerations identified in s 9 are matters to which a court shall, to the extent that they are relevant, have regard. In judicial review terms, they would be described as mandatory considerations. They involve factors which may tend in different directions in a particular case or may simply be inapplicable. However, I do not, with respect, find it helpful to refer to them as part of "the unjustness calculus". This phrase appears to reflect a label adopted in relation to the exercise required of a court in determining whether there is negligence or not in a tort case, derived from *Wyong Shire Council v Shirt* (1980) 146 CLR 40 at 47, known as the "Shirt calculus". As was said by Gleeson CJ and Kirby J in *Mulligan v Coffs Harbour City Council* (2006) 221 ALR 764 at [2], the use of the word "calculus" is unfortunate, because it tends to misdescribe the process to be engaged in as a method of calculation. In mathematical terms, it has a precise meaning, as in reference to differential calculus, which gives it a flavour far distant from the exercise required to be undertaken under ss 7 and 9 of the *Contracts Review Act.*

113 One danger of identifying the exercise as some form of calculation is that it may lead, subconsciously, to an approach whereby the power is thought to be engaged when at least one criterion is satisfied and should be exercised when a reasonable number of criteria are satisfied. That approach would be incorrect. The exercise requires an assessment of the relevant circumstances in relation to a broad concept of unjustness.

114 The term "unjust" is defined in s 4 to include "unconscionable, harsh or oppressive", a definition which is clearly intended to give the term an expansive meaning but which does little to define the boundaries. As was noted almost 20 years ago by McHugh JA in *West v AGC (Advances) Ltd* (1986) 5 NSWLR 610 at 621A, in language which has been repeated on many occasions thereafter:

> "The *Contracts Review Act* 1980 is revolutionary legislation whose evident purpose is to overcome the common law's failure to provide a

> comprehensive doctrinal framework to deal with 'unjust' contracts."

115 That is not to say that the Court is launched on an uncharted sea with no navigational guides, but rather that constraints which would preclude intervention according to established principles of legal or equitable doctrine, may not be decisive under the Act. Thus, while equity provides relief against the unconscientious conduct of the defendant, the Act may permit relief in circumstances where the conscience of the defendant is not affected. Similarly, a contract, or a provision thereof, may be unjust in circumstances where there was no pre-existing duty owed by, say, a lender to a borrower to act in a particular way.

116 There are passages in the judgment of McHugh JA in *West*, including those set out by the Chief Justice at [71] above, which may support a contrary view. However, as his Honour also stated in *West* at 620F:

> "Under s 7(1) a contract may be unjust in the circumstances existing when it was made because of the way it operates in relation to the claimant or because of the way in which it was made or both. Thus a contractual provision may be unjust simply because it imposes an unreasonable burden on the claimant when it was not reasonably necessary for the protection of the legitimate interests of the party seeking to enforce the provision: c.f. s 9(2)(d)."

117 An issue of central importance in this case is the weight which should be given to the lack of awareness of the lender with respect to the circumstances of the borrowers. Thus, for example, if the borrowers were labouring under a disability which rendered them not reasonably able to protect their interests, for the purposes of s 9(2)(e), that fact may not be known to the other party. In *Karavas* (at 277C), Meagher JA stated:

> "There is jurisdiction under the Act to make orders in favour of a party to a contract who proves that at the date of the contract he suffers from a relevant disability even though the other party to the contract is unaware of that disability, although in general it would be unsound to exercise the jurisdiction in those circumstances.
>
> ...
>
> The reason for the view is that it is hardly just to deprive an innocent person of valuable property of which contractual rights are a species. Nevertheless, such a jurisdiction undoubtedly exists. In the present case, for example, it is made quite clear from s 9(2)(i) of the Act that relief may be granted if a finding is made that a party to a contract did not understand 'the provisions and their effect' of a contract."

118 In *St Clair v Petricevic* (1988) ASC ¶55-688 a vendor sought to set aside a contract of sale of land at a price which had been significantly lower than the asking price. The vendor's home encroached on a right-of-way which benefited the prospective purchasers. They made an offer for the land, combined with a threat to assert their rights over the right-of-way and demolish the encroaching property if it were not accepted. At the time the vendor agreed to the sale she was distressed and agitated, having learned that she suffered from a serious illness. Hope JA (with whom Clarke JA agreed) stated at p 58,207:

> "Her ability to be resolute in the face of the threat which [the purchasers' agent] made, and to continue with the negotiations, must, in my opinion, have been significantly affected. ... Furthermore, it is not relevant to the question whether the contract should be found to be unjust by reason of the defendant's health that the plaintiffs did not know of it and did not try to take advantage of it. In this regard it is the position of the defendant that is to be considered."

This Court set aside an order for specific performance made in favour of the purchaser and set aside the contract of sale.

119 Reading *St Clair* and *Karavas* together, the true position may be that a claimant can establish the unjustness of a contract by reliance on factors of which the other party was ignorant when the contract was entered into, but that such ignorance may be relevant in determining whether to grant relief. The fact that the power may be engaged by circumstances which were not known to the other party at the time the contract was made is well-established: see, eg, *St George Bank Ltd v Trimarchi* [2004] NSWCA 120 at [36], Mason P, Sheller JA and Cripps AJA agreeing.

Application of principles

120 As explained by the Chief Justice, the trial judge was in error in his treatment of the internal lending guidelines, in a manner which was material to the conclusion which he reached. Accordingly, it is necessary to determine whether, on the correct approach, a different result should follow.

121 Further, it is necessary to consider whether the failure of the lender to require that the borrowers

received independent financial advice in relation to the proposed business transaction for which the loan was sought, was a material consideration.

122 While it is true, as McHugh JA stated in *West* at p 621E, that the Act "regulates contracts not investments", nevertheless, the transaction or investment which constitutes the purpose for which the loan is obtained may be relevant in a number of respects. One possibility is that the lender played some part in the investment decision: see *Elders Rural Finance Ltd v Smith* (1996) 41 NSWLR 296 at 309F-G (Handley JA). That is not this case, but the investment decision may be relevant in other respects. Thus, as noted above, s 9(1) requires that the Court have regard to all the circumstances of the case including the consequences which may arise in the event of compliance or non-compliance with, or a contravention of, the contract. Where there is a security, the fact that failure to meet a repayment instalment may lead to sale of the security, is therefore a relevant consideration.

123 Further, s 9(2)(d) requires consideration of whether the terms of the contract are reasonably necessary for the protection of the interests of the lender. Thus, in *Elkofairi v Permanent Trustee Co Ltd* [2002] NSWCA 413, this Court held that a contract was unjust by reason of a combination of two circumstances, namely that the borrower was in a position of special disadvantage (although unbeknownst to the lender) and, secondly, that the lender was "content to lend on the value of the security only", knowing that the borrower had no income or other assets, with the result that it was likely that the borrower would lose her home: see [53] and [79], Beazley JA, Santow JA and Campbell AJA agreeing. The Court held that the loan contract was unjust, perhaps by reference both to the interests of the borrower and also in the public interest.

124 In the present case, the trial judge found that the agent of the lender, Mr Tadros, had not made any inquiries as to the purpose of the loan or the income of the borrowers. The loan application stated, falsely, that the husband was in employment and had an income for $43,000 per year. The loan repayments of approximately $10,000 per year fell, broadly speaking, within the relevant guideline. However, in the absence of any attempt to verify the accuracy of the figure, the lender should be taken not to have relied upon the ability of the borrowers to make instalment repayments on time, in accordance with the terms of the contract.

125 Where the loan was intended for investment purposes, rather than expenditure on consumable items, it was at least arguable that the loan would be self-funding. Again, however, the failure of the lender to inquire as to the purpose of the loan indicates that no reliance was placed on that possibility.

126 In these circumstances, the question of independent advice was not considered by the lender, because it was content to lend money which would be immediately dissipated. If the loan be unjust, it must be because the lender approached the matter on that basis, and not because the borrowers believed a particular investment was likely to be profitable, a belief which professional advice would have debunked. The fact that there was such a false belief, which may have been induced by unfair pressure or unfair tactics exerted by a person independent of the lender, would itself be a material factor if it were shown that the agent of the lender had knowledge of that fact: s 9(2)(j)(iii). The reason that the agent of the lender had no such knowledge was because he made no inquiries as to the purpose of the loan. The trial judge found that, had inquiries been made of the borrowers, they would have answered them honestly. These circumstances do not mean that constructive knowledge should be imputed to the lender, but the circumstances are relevant to a consideration of whether the loan contract and security may be unjust, in part, because no such inquiry was made.

127 The issue with respect to an ill-advised investment was discussed, hypothetically, by McHugh JA in *West* (see the passage set out at [86] above) in terms of whether the lender in such circumstances acts "unfairly" in relation to the borrowers and, whether "the lender owed a duty to the borrower to ensure that she used the borrowed money wisely". In relation to the first limb of this approach, his Honour appears to have assumed that these circumstances might only give rise to a form of procedural unfairness. It is at least arguable that the contract may be unjust in a substantive sense. In relation to the second limb of the test, it would, in my view, be an error to look for a duty imposed under the general law to ensure such a result. A contract may be unjust without there being any breach of a general law duty: see Mahoney P in *Elders Rural Finance Ltd v Smith* (supra) 41 NSWLR at 299B.

128 To engage in pure asset lending, namely to lend money 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, is to engage in a potentially fruitless enterprise, simply because there is no risk of loss. At least where the security is the sole residence of the borrower, there is a public interest in treating such contracts as unjust, at least in circumstances where the borrowers can be said to have demonstrated an inability reasonably to protect their own interests, for the purposes of, for example, s 9(2)(e) or (f). That does not mean that the Act will permit intervention merely where the borrower has been foolish, gullible or greedy. Something more is required: see *Esanda Finance Corp Ltd v Tong* (1997) 41 NSWLR 482 at 491 (Handley JA) cited with approval in *Elkofairi* (supra) at [77] by Beazley JA.

129 The trial judge found, and it does not appear to have been in dispute, that the borrowers were both born in Iran and were educated and married there. English was their second language. They were members of Sydney's Assyrian community when the loan was made. Mr Khoshaba had no education beyond Year 11 in Iran and had worked in that country as a foreman at a Volvo factory. When he arrived in Australia in September 1971, he did not speak English. He obtained work at a cable-making factory in Liverpool. It appears that he had no business experience or property or investments, either in Iran or in Australia.

130 The background of Mrs Khoshaba was similar. She had worked as a typist in Iran and in a clothing factory, as a sewing machine operator, in Australia. She had also worked as a packer at a pharmaceutical company in Australia. She did not know the names of her employers and can have worked only briefly in Australia, as in her affidavit sworn in March 2004, she said she had not worked "for over 30 years". Both were pensioners, presumably in receipt of an age pension as a couple.

131 These disadvantages were to some extent offset by the fact that they received advice from their Australian educated daughter, but his Honour found that both the parents and the daughter were naive, apparently in relation to financial matters. These circumstances would probably not have justified a finding that the borrowers were under a special disadvantage or disability, for the purposes of equitable principles of unconscionable dealing, but in my view they are sufficient to satisfy the requirements of the particular public interest identified above, in concluding that asset lending may be unjust.

132 Accordingly, I agree with the conclusion reached by the Chief Justice and the orders he proposes.

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