

The protection of consumers in credit contracts

Vella v Permanent Mortgages Pty Ltd [2008] NSWSC 505

By Lucinda Wilson

Throughout Australia, legislation exists to protect consumer interests in credit contracts. This article gives an overview of how such codes and acts are applied in the context of fraudulent credit contracts. Specifically, do these codes and acts provide recourse for litigants, who were not in truth a party to the contract, because of a fraud exercised against them?

On 28 May 2008, Young CJ in Eq handed down a voluminous decision in *Vella v Permanent Mortgages Pty Ltd*¹ (*Vella*). His Honour considered, among other things, whether the *Consumer Credit (New South Wales) Act 1995* (NSW) and the *Contracts Review Act 1980* (NSW) can be applied by the courts to assist a defrauded individual.

The plaintiff, Mr Vella, had a business partner with whom he had a joint bank account. The business partner arranged for two loan agreements and mortgages to be executed in the plaintiff's name. The mortgages were registered and, later, monies were paid into the joint bank account under the loan agreements secured by the mortgages. In total, about \$2.5 million was paid into the joint bank account, most of which was removed from the account by the business partner using forged cheques in his favour.

His Honour held that the mortgages and loan agreements were all forged.²

AN INTRODUCTION TO THE CONSUMER CREDIT ACTS IN AUSTRALIA

Each state and territory of Australia has legislation and associated regulations that regulate the provision of consumer credit. The basis of most of this legislation is the *Consumer Credit Code* (the Code) set out in the Appendix to the *Consumer Credit (Queensland) Act 1994*. For example, the Code is incorporated into:

1. NSW law, by s5 of the *Consumer Credit (New South Wales) Act 1995*,
2. Queensland law, by s4 of the *Consumer Credit (Queensland) Act 1994*;
3. Tasmanian law, by s4 of the *Consumer Credit (Tasmania) Act 1996*;
4. Northern Territory law, by s4 *Consumer Credit (Northern Territory) Act 1995*;
5. Australian Capital Territory law, by s4 of the *Consumer Credit Act 1995* (ACT);
6. Western Australian law, by s5 of the *Consumer Credit (Western Australia) Act 1996*;

7. South Australian law, by s5 of the *Consumer Credit (South Australia) Act 1995*; and
8. Victorian law, by s5 of the *Consumer Credit (Victoria) Act 1995*.

The Code came into operation on 1 November 1996. Its purpose has been described as the protection of debtors: *Agussol v Australian Finance Direct Ltd*.³

By virtue of s6(1) of the Code, each of the Consumer Credit Acts listed above applies to the provision of credit (and to the credit contract and related matters) if, when the credit contract is entered into, or (in the case of pre-contractual obligations), is proposed to be entered into:

- (a) the debtor is a natural person ordinarily resident in this jurisdiction or a strata corporation formed in this jurisdiction; and
- (b) the credit is provided or intended to be provided wholly or predominantly for personal, domestic or household purposes; and
- (c) a charge is or may be made for providing the credit; and
- (d) the credit provider provides the credit in the course of a business of providing credit or as part of or incidentally to any other business of the credit provider.⁴

The most contentious of these four criteria is (b), the purpose for which the credit is provided or intended to be provided (the second criterion). The controversy and competing authorities on this criterion are referred to in *Bahadori v Permanent Mortgages*⁵ (*Bahadori*). Young CJ in Eq turned his mind to the second criterion in *Vella*, but made no reference to *Bahadori*.

Section 8 of the Code sets out the criteria that determine whether the Code applies to a specific mortgage. If it does, that mortgage is not enforceable unless signed by the mortgagor.⁵ This section of the Code operates as a statutory exception to indefeasibility.⁶

If the debtor in a credit contract claims that the Code applies to his or her credit contract, s11(1) of the Code presumes that it does.

However, if the debtor declares that the credit is not to be provided for personal, domestic or household purposes, by a declaration that is substantially in the form required by the regulations, the Code will not apply to that credit contract.⁷

If the credit contract is a forgery, it is most likely that any declaration under s11 of the Code will also be a forgery.⁸ Therefore, as was held in *Vella*,⁹ if the declaration was not in truth signed by the debtor, it is not a declaration for the purpose of s11 of the Code.

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Young CJ in *Eq* also held that, in the circumstances in *Vella*, where the credit-provider (or any relevant person who obtained the declaration from the debtor such as a finance broker) failed to make appropriate enquiries about the purpose of the credit, the s11 declaration cannot overturn the presumption that the Code applies. Subsection 11(3) makes a declaration ineffective for the purposes of s11 if the credit-provider (or relevant person) knew, or had reason to believe, at the time the declaration was made, that the credit was in fact to be applied wholly or predominantly for personal, domestic or household purposes.

Returning to the interpretation of the second criterion in s6 of the Code, Young CJ in *Eq* observed that the 'legislation does not expressly indicate whether the purpose is to be considered subjectively or objectively or by a combination of subjective and objective considerations'.¹⁰ His Honour considered s6 in the context of s11, and the 'beneficial purpose of the legislation'.¹¹ In this context, his Honour held that the question for the court is the use to which the funds are put, or are intended to be put, and in making this enquiry the court may consider the purpose for which the money was used when the credit was provided.¹²

As to the use to which the credit was actually put, Harrison J has said that:

'[f]actors which occur after the transaction was entered into, should not in my view, be considered. As a matter of statutory construction, to read these words and give them their ordinary and natural meaning, the section requires that the intended purpose of the legislation be discerned from the time the contract is entered into, or proposed to be entered into.'¹³

It is, with respect, difficult to see why a credit-provider ought be bound by the Code if the intended use of the credit was not said to be personal, but when the debtor received the funds, s/he decided to use them for a personal purpose. Justice Harrison's comments on this point seem to be logical in the circumstances, and are to be contrasted to the findings in *Jonsson v Arkway Pty Ltd*,¹⁴ which were cited in *Vella*.¹⁵

In considering the second criterion in *Vella*, Young CJ in *Eq* held that the debtor to be considered is the named debtor in the forged credit contract, being Mr Vella, and that in the circumstances of a forged credit contract, the defrauded debtor 'had no purpose at all in respect of the provision of the advances of the mortgagees'.¹⁶ It appears that it is on this basis that the debtor had no purpose for the credit, that the Code was held not to apply where the credit contract was a forgery.¹⁷

In obiter, the following have been considered purposes of credit that represent personal use:

1. refinancing or consolidation of private debts;¹⁸
2. short-term bridging finance;¹⁹
3. acquisition of personal assets;²⁰ and
4. providing a home for the borrower's parents as beneficiaries under a family trust.²¹

It seems his Honour also considered the identification of a particular business as the intended destination of the credit, and identification of the income earning activity to which the credit was intended to be used, in correspondence about

the credit contract, as relevant to the purpose of the credit.²²

In conclusion, the Code is an imperfect device to protect defrauded individuals who are fraudulently named as debtors in credit contracts.

THE CONTRACTS REVIEW ACT

In NSW, the *Contracts Review Act 1980* provides a mechanism of judicial review of certain contracts and to grant relief in respect of harsh, oppressive, unconscionable or unjust contracts.

If the court finds that a contract is unjust in the circumstances relating to the contract at the time it was made, it may grant certain relief.²³ Young CJ in *Eq* seemed to accept in *Vella* that mortgages in NSW are deemed to be contracts by force of the *Real Property Act 1900*.²⁴ In any event, the *Contracts Review Act* may be applied by a court to give relief in relation to a mortgage.²⁵

Section 6(2) of the *Contracts Review Act* again makes the purpose of the contract a necessary consideration before the court may apply the Act in favour of a defrauded individual. That section provides:

'A person may not be granted relief under this Act in relation to a contract so far as the contract was entered into in the course of or for the purpose of a trade, business or profession carried on by the person or proposed to be carried on by the person, other than a farming undertaking ... carried on by the person or proposed to be carried on by the person wholly or principally in New South Wales.'

In deciding the application of the *Contracts Review Act*, Young CJ in *Eq* stated '[f]or the reasons set out when I was considering the Consumer Credit Code, on the evidence the purpose of the contract was commercial'.²⁶ His Honour therefore concluded that s6(2) prevented application of the *Contracts Review Act* to Mr Vella.

It is difficult to see how these two findings follow. In fact, when considering the Code, his Honour held that the debtor to be considered, the defrauded individual, had *no purpose* in the contract to which the Code is said to apply. 'No purpose' does not equate to a commercial purpose, and it would therefore seem to me, with respect, that s6(2) of the *Contracts Review Act* would be no bar to the application of that Act.

It is also difficult to imagine a contract that would be more unjust than one alleged to have been executed by a named debtor, when in actual fact the debtor is a defrauded individual.

Notes: 1 [2008] NSWSC 505. 2 *Vella* at [10]. 3 [2004] ASC 155-066. 4 (1997) 69 NSWLR 49 at 57. 5 s38(1) and (4). 6 *Vella* at [331]. 7 Section 11(2) and (4) of the Code. 8 See *Vella* at [350]. 9 *Ibid*, at [341] and [352]. 10 *Ibid*, at [342]. 11 *Ibid*, at [342]. 12 *Ibid*, at [342]. 13 *Bahadori*, at 60. 14 (2003) 58 NSWLR 451. 15 *Vella* at [342]. 16 *Ibid*, at [343]. 17 *Ibid*, at [356]. 18 *Ibid*, at [345]. 19 *Ibid*, at [346]. 20 *Ibid*, at [347]. 21 *Jonsson*, at 456. 22 *Vella*, at [348]. 23 Section 7 of the *Contracts Review Act*. 24 *Vella* at [357]. See also definition of mortgage as a 'personal contract' in Butt, P. *Butterworths Australian Legal Dictionary*, LexisNexis, 1997, at 763. 25 *Contracts Review Act* s8, sched 1 (1)(a) and (4)(a). 26 *Vella*, at [353].

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