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6 December 2011

Insurance Law Case Note

The credibility gap and the gullibility fill: *Perpetual Trustee Company Ltd v Milanex Pty Ltd (in liq)* [2011] NSWCA 367 – Mortgage brokers

In the recent case of ***Perpetual Trustee Company Ltd v Milanex Pty Ltd (in liq)*** the NSW Court of Appeal rejected a mortgage broker's claim that a lender's knowledge of discrepancies in a prospective borrower's personal circumstances meant that the lender had not relied upon the mortgage broker's misrepresentations in making the loan.

In doing so, the Court provided further guidance on the often vexed question of the extent to which a party must prove reliance in order to succeed on a claim of actionable misrepresentation.

The claim

In November 2005 Alexander Kotevski (**the borrower**) was a retired builder whose only source of income was an aged person's pension paid by Centrelink. Through a friend in the Slavic community, the borrower was encouraged to take out a loan secured by a mortgage over his home repayable over 30 years. At the time, the borrower was 74 years old.

The loan was brokered by Milanex Pty Ltd (**Milanex**), a mortgage broker that referred business to Good Home Loans Pty Ltd (**GHL**). GHL was responsible for preparing and forwarding the borrower's completed loan application to Calibre Financial Services Pty Ltd (**Calibre**) pursuant to a "Mortgage Origination and Management Agreement" (**MOMA**). Calibre acted as agent for the lender, Perpetual Trustee Company Ltd (**Perpetual**), and submitted the loan application to Perpetual for its approval.

In January 2006 Perpetual accepted the loan application and advanced the borrower $221,935 (**loan**) secured by a registered mortgage over the borrower's home. The borrower made some repayments towards the loan but then defaulted. At the end of 2007 Perpetual took steps to enforce the mortgage. In defence, the borrower sought relief under the *Contracts Review Act 1980* (NSW) (**CRA**) on the basis that the loan agreement was unjust.

Perpetual cross-claimed against Milanex alleging that it had misled Perpetual about the borrower's personal circumstances in connection with the loan application. Perpetual claimed damages against Milanex under section 52 of the *Trade Practices Act 1974* (Cth) and section 42 of the *Fair Trading Act 1987* (NSW).

At first instance

The trial judge found at first instance that the borrower, who had very little formal education and could not read or write English, had been unduly pressured into the loan agreement by his friend. What was more, the borrower had received no benefit from the loan which appeared to have been arranged solely for, and to the benefit of, the borrower's friend. The trial judge found that, while the borrower had received independent legal advice in relation to the loan, the solicitor who had provided that advice could not have been satisfied that the borrower fully understood the loan agreement or had entered into it voluntarily. The trial judge noted that while neither Perpetual nor GHL, Perpetual's agent, connived with Milanex or with the borrower's solicitor in pressuring the borrower into entering the loan agreement, they should have been alerted to discrepancies on the loan application to make further enquiries into the borrower's personal circumstances. Not the least of these discrepancies was the unlikely ability of a 76 year old pensioner to repay a 30 year loan[1].

Not surprisingly, the trial judge upheld the borrower's defence that the loan agreement was unjust and declared the agreement void pursuant to section 7 of the CRA. As the mortgage over the borrower's property was registered, the trial judge also made orders to facilitate the removal of the mortgage from the registrar.

In relation to Perpetual's cross-claim against Milanex, the trial judge found that while Milanex had engaged in misleading and deceptive conduct by representing to Perpetual that the borrower had signed the loan documents, Perpetual's/GHL's reliance on that conduct was not causative of Perpetual's loss. This was because, in the trial judge's view at [301][2]:

[1] Asset lending

[2] *Perpetual Trustee Company Ltd v Alexander Kotevski* [2009] NSWSC 1228

> "[GHL's employee] *conceded that if she had reali*[s]*ed that the application was made on behalf of a 74 year old pensioner, she would not have approved it. Yet she knew he was seventy four years old and she knew, or should have known, from her own enquiries that he was an aged pensioner … The intervening cause of loss was the conduct of GHL and to a lesser extent* [Perpetual's solicitor]" (emphasis added).

On that basis, the trial judge dismissed Perpetual's cross-claim against Milanex. Perpetual appealed.

The appeal

Perpetual challenged the finding by the trial judge that Perpetual's reliance on Milanex's conduct did not cause it loss. Macfarlan JA (with whom Campbell JA agreed and Young JA agreed in the result) considered that GHL's evidence at trial indicated that while GHL did not rely solely on Milanex's representations about the borrower in the loan application, it relied on them in part[3]. His Honour referred to Wilson J's remark in *Gould v Vaggelas* [1985] HCA 75 that "[*t*]*he representation need not be the sole inducement. It is sufficient so long as it plays some part even if only a minor part in contributing to the formation of the contract*".

For that reason, Macfarlan JA considered that it was not to the point that, had GHL been more astute, it might have discovered the falsity of some of Milanex's representations about the borrower's personal circumstances. The fact that GHL had sought to verify some of the information provided to it by Milanex did not mean that GHL had not also relied on Milanex's representations. In cases of this kind his Honour considered that the correct approach was identified in *I & L Securities v HTW Valuers (Brisbane) Pty Ltd* [2002] HCA 41 where Gaudron, Gummow and Hayne JJ observed at [58] that:

> "[T]*o show that, if either of two events had not occurred, a loss which has been suffered would not have been suffered, does not demonstrate that one rather than the other event was the cause of the loss, any more than it demonstrates that neither was a cause of that loss …* [T]*he fact is that both did happen and both contributed to the decision to make the loan*" (original emphasis).

In those circumstances, it was enough that GHL had relied on Milanex's representations in part in making the loan, notwithstanding that GHL had also been careless. Further, as the loan had proven irrecoverable, Perpetual had established its loss.

Milanex sought to advance an alternative argument that Perpetual had failed to mitigate its loss by not enforcing a right provided to it under the MOMA between GHL and Calibre. Clause 12.1(e) of the MOMA provided, among other things, that GHL warranted to Calibre and "*the Mortgagee*" (which, in this case, was Perpetual) that "*the relevant Loan Purchase Request has been fully investigated by* [GHL] *in accordance with the Operations manual*".

It was accepted on appeal that GHL had failed to comply with the operations manual and that such a failure entitled Perpetual to force GHL to take over the mortgage. However, Milanex's contention that Perpetual had failed to mitigate its loss in this way or at all was not pleaded in its defence to Perpetual's cross-claim and was only raised in Milanex's closing written submissions at first instance. Not surprisingly, the Court of Appeal considered that there was prejudice to Perpetual if Milanex were to raise the issue on appeal and Milanex was not permitted to do so. Nevertheless, Macfarlan JA noted that, quite apart from the prejudice to Perpetual had Milanex been permitted to raise this issue, the declaration that the loan agreement was void at first instance (which was not challenged on appeal) and the consequent removal of the mortgage from the register meant that there had not been a mortgage for GHL to purchase at any relevant time.

Proportionate liability

On the borrower's cross-claim against his solicitor at first instance, judgment was entered against the solicitor by consent for $105,000 plus costs on the first day of the trial. Milanex contended on appeal that Perpetual's cross-claim against Milanex was an apportionable claim pursuant to Part 4 of the *Civil Liability Act 2002* (NSW) and that the borrower's solicitor was a concurrent wrongdoer.

In support of that contention, Milanex relied upon some of the allegations in the borrower's cross-claim against the solicitor. These were to the effect that the solicitor had given the borrower independent legal advice about the mortgage and was satisfied that the borrower had voluntarily signed the loan and mortgage. The basis for these allegations consisted of documents containing declarations to this effect signed by the borrower, one of which was witnessed by the solicitor. Perpetual gave evidence that this document was a material factor in it granting the loan. On that basis the court upheld Milanex's contention that the solicitor was a concurrent wrongdoer and apportioned liability to Milanex at 65% and to the solicitor at 35% (Young JA dissented on this and apportioned liability to the solicitor at 25%).

[3] It was not disputed that GHL was acting as Perpetual's agent for the purpose of the loan transaction.

Assessment of Perpetual's loss

At first instance, a declaration was made by the trial judge that the borrower hold the judgment sum received from the solicitor on trust for Perpetual. On appeal, the court recognised that this sum was in effect a payment by the solicitor towards discharging his responsibility for Perpetual's loss.

As Perpetual's principal loss was agreed at $189,623, this meant that the judgment sum held on trust for Perpetual (which, after the borrower's solicitor/client costs, equated to $81,014) exceeded the amount of the solicitor's liability apportioned at 35% (which equated to $66,368 before interest). Ordinarily, that would mean that the amount to which Perpetual was entitled on its judgment against Milanex would have to be reduced to ensure that Perpetual did not obtain double recovery. However, in this case, Milanex did not submit that the excess amount received from the solicitor exceeded the interest that Perpetual was otherwise entitled to.

Milanex sought to account for this omission by arguing that Perpetual's damages could not be finally assessed until the borrower's solicitor/client costs had been assessed which had been deducted from the amount held on trust for Perpetual. The court rejected this submission on the basis that, should any deduction for the borrower's solicitor/client costs have to be reimbursed, that would be an amount that Milanex might be able to point to in support of a partial satisfaction of the judgment against it. However, that prospect was no reason for the court deferring assessment of Perpetual's damages.

Comment

As this case shows, it will not be enough for a party whose conduct is alleged to have induced another party to make a loan or to give a mortgage to show that that party should have known of the true position or have availed itself of the opportunity to make further enquiries into it. It will be enough if the representation has played some part, even if a minor part, in the party acting as it did and suffering loss as a result.

The case is also a reminder for lawyers to plead all available defences and to quantify any loss or set-off to a claim at an early stage in the proceedings. Courts will not permit substantial points raised in submissions and in the absence of evidence to deprive an opposing party of a right to contest an issue at trial or to obtain a benefit of the litigation like having its damages assessed at judgment.

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