UNCONSCIONABLE CONDUCT AND SECTION 52 OF THE TRADE PRACTICES ACT (AND FAIR TRADING ACT PROVISIONS) IN RELATION TO BANKING TRANSACTIONS

MARK SNEDDON

Lecturer - Faculty of Law
Monash University, Melbourne

My paper is in the nature of a commentary. Some have said that commentators are akin to appellate judges in that they too have a proclivity to ride in and shoot the wounded, that being the principal speaker. This commentator takes the view that if a judge needs to be equipped with the superior moral attainment of humility to speak to a group of banking lawyers, a fortiori an academic who comes to commentate on a paper by a judge addressed to the same group of lawyers. Therefore let me thank Justice Spender on your behalf for an excellent paper and limit myself to making a few comments partly by way of amplification and partly by way of qualification of the judge's remarks.

In the judge's paper he outlined the distinction between procedural unconscionability and substantive unconscionability. This distinction, made originally by academic lawyers has since been picked up by Mr Justice McHugh in the New South Wales Court of Appeal. Procedural unconscionability refers to unfairness in the bargaining process and the method of making the contract. Substantive unconscionability refers to the unfair substantive terms of the contract or the unjust effects of the contract or the transaction.

The judge in his paper said quite rightly that the equitable doctrine of unconscionability has to do exclusively with procedural unconscionability - that is the process of entering into the transaction. The equitable doctrine as laid down in Blomley v. Ryan and expanded in Commercial Bank of Australia v. Amadio has two limbs - one is that one party be at a special disadvantage to another and secondly that the party who has the upper hand as it were make some unconscientious use of that special advantage. Amadio is a classic example of that.

Let me add one caveat to this proposition that procedural unconscionability relates to the inception of the transaction - that is the discussion or the bargaining leading up to the making of the bargain. This caveat stems not from the classic equitable doctrine of unconscionability as laid down in Blomley v. Ryan and Amadio but from the recent High Court decision in Waltons Stores

v. Maher. Waltons Stores is a case of equitable estoppel. Different judges use different terms to describe the estoppel but I will use equitable estoppel as a compendium. I think Waltons Stores stands for the proposition that unconscionable behaviour is now adopted as a unifying basis for the imposition of equitable estoppel.

It seems to me quite conceivable that a bank may run into equitable estoppel problems because of its unconscionable behaviour both in the course of making the contract, that is in the pre-contractual negotiations and so on and also during the life of the contract. If that is so, that is going to be somewhat different to the classic doctrine of unconscionability which looks essentially to the pre-contractual negotiations.

In Waltons Stores the High Court held that an equitable estoppel may arise in relation to a non-contractual, voluntary representation by a bank or in relation to an assumption or expectation held by the other party, which the bank induced or failed to disabuse the other party of and on which the other party has relied and acted to its detriment. That situation raises what in Justice Brennan's terms is called an equity and the equity will compel the bank to adhere to the representation or assumption which it failed to disabuse the other party of or induced or otherwise will compel the bank to do what is necessary to avoid the detriment to the party.

For example, during the life of a guarantee a surety may agree to the release of certain security put up by a co-surety on the basis of an erroneous assumption that further advances to the principal debtor were subject to a limit, or in fact that no further advances were to be made. Now the bank knowing of this assumption, knowing that it is incorrect, refrains from correcting it. Further advances are made and the surety is called upon to make good an amount exceeding the assumed limit. An equity may then be raised in the surety against the bank to be satisfied by restricting the surety's liability to the amount of the incorrectly assumed limit. Thus under Waltons Stores unconscionable conduct which founds relief in the form of equitable estoppel may affect the transaction through its life and not just at its inception.

The second point that I want to make about unconscionability in the context of equitable estoppel as found in Waltons Stores v. Maher relates to the suggested solution of urging upon the other party to the transaction the gaining of independent legal advice. The judge has made a fine analysis of the judgments in Amadio and come to the conclusion that the dicta there suggested the relationship of special disadvantage, which is necessary for the classic equitable doctrine, may be constituted merely by an inequality in bargaining power, and a lack of relevant knowledge or information on the part of the party other than the bank. The unconscientious taking advantage, which is the other limb of the doctrine, may consist merely in the bank proceeding with the

transaction when it ought to have been aware that the other party has not received accurate and adequate advice. Thus if the bank proceeds while being aware that the other party lacked relevant information or a proper understanding of an important aspect of the transaction, then this may be enough to have the transaction set aside.

To escape the consequences of that problem which has arisen because the High Court has taken such a generous view towards the weaker party, the judge has suggested that the banks urge upon their mortgagors and guarantors the obtaining of independent legal advice and he has quoted the various cases from the United Kingdom which suggest that if getting that advice is urged on the other party then whether they in fact get that advice or not, the bank is protected. The mere urging of the advice is all that is necessary. If the other party declines to get the advice or for whatever reason still proceeds with the transaction having obtained the advice, then the bank has covered itself and is not going to be subject to the classic equitable doctrine of unconscionability.

I think that is right in relation to the classic equitable doctrine provided a real opportunity to obtain the advice is provided. I am not at all sure that it is right in relation to the operation of the doctrine of equitable estoppel. If the other party takes advice and is not disabused of an erroneous assumption which it was under - the advice is inadequate in other words - and the bank knows that the other party still labours under the wrong assumption even after taking the advice, and the bank does not then correct the assumption, then an equitable estoppel may still arise. After all, in the Waltons Stores case itself it will be remembered that Mr Maher was independently advised all along by his solicitors, but both he and his solicitors were led by Waltons and its solicitors to believe that leases would be exchanged. That was the relevant assumption that was erroneous and which was encouraged or at least which Waltons did not disabuse Maher and his solicitors of.

Independent advice then may be inadequate or independent advisers may also fall prey to misrepresentations or wrong assumptions and an equitable estoppel may still then arise based on the bank proceeding with the transaction knowing that the erroneous expectation or assumption has not been corrected. So I merely make the point that to urge on the other party to get independent advice may well save the bank's bacon in relation to the classic doctrine of unconscionability, but it is not a sure fire protection in the area of equitable estoppel which is created by an unconscionable act on the part of the bank.

Let me turn then to the area of substantive unconscionability, that is contracts with unfair terms and unfair effects. Relief from such unconscionability must be found in statute and not in the equitable doctrines and the classic statute that we have in this country at the moment is of course the Contracts Review Act

1980 (NSW). Section 7 provides that where the court finds a contract or provisions of a contract to have been unjust in the circumstances relating to the contract at the time it was made then the court may provide relief. Now that phrase "unjust in the circumstances relating to the contract at the time it was made" would seem on its fact to refer to procedural unconscionability - that is unconscionability in the transaction leading up to the making of the contract. But in fact that has been interpreted as embracing both substantive and procedural unconscionability. So, for example, Mr Justice McHugh in West v. AGC (Advances) Ltd ((1986) 5 NSWLR at p.620) was able to say that a contract may be unjust under the Contracts Review Act because its terms, consequences or effects are unjust. This is substantive injustice. Or a contract may be unjust because of the unfairness of the methods used to make it. That is procedural injustice. Most unjust contracts will be the product of both procedural and substantive injustice.

It seems to me that lawyers outside New South Wales are not able to breathe freely just because we do not have the benefit or the burden of the Contracts Review Act in our jurisdictions. It seems a similar process which reads those words in the Contracts Review Act as applying to substantive unconscionability as well as procedural unconscionability can be applied to s.52A of the Trade Practices Act and its Fair Trading Act clones. That is to say they can be read to proscribe not only conduct in making a contract but conduct being the performance of or the enforcement of the rights and duties imposed by the contract - the actual terms of the contract and the execution of it. See particularly paragraph (2)(b) of s.52A but note the exception in sub-s.3 which relates specifically to the bringing of legal proceedings and arbitration. In other words s.52A and the Fair Trading Acts will go, or could be construed to go to substantive as well as procedural unconscionability.

It is said that we do not have to worry terribly much about s.52A in relation to banks for two reasons. One is that it has a limitation built in, in sub-s.(5), that it only applies to services ordinarily acquired for personal, domestic or household use or consumption. Presumably in the context of banks we are talking then about personal loans, housing loans for principal residences and the like. The second suggested limitation is that the cost barrier to consumers of running a Federal Court action over what may be a proportionately small sum is going to deter a lot of cases from coming on. I think that both are true limitations.

Under the Fair Trading Acts however, the courts which have been vested with jurisdiction are not the superior courts in the various jurisdictions. For example, in Victoria the County Court has been vested with jurisdiction. That reduces to some extent, although it obviously does not eliminate, the cost disincentive to bringing an action. In any event we have already seen under the Contracts Review Act, which is also limited to non-commercial

contracts, cases of banking unconscionability brought by "consumers".

One such case is Westpac Banking Corporation v. Sugden. In that case four provisions of Westpac's standard form of guarantee were held to be unjust in the circumstances of the case. They were not adequately explained to the guarantors, the guarantors were not urged to get independent advice and the provisions were held not to be reasonably necessary to protect the legitimate interests of the bank in the case.

No relief was granted in that case because on the facts no unjust consequence or result had flowed from those provisions. But there was at least one provision there, which made the certificate in the bank conclusive evidence in relation to the amount of moneys outstanding, where the judge felt that it was quite possible that unjust consequences might have flowed and he would have given relief. So on the basis of that case and my speculation as to the interpretation of the Fair Tracing Act provisions, I think it is quite feasible that a number of provisions in the various banks' standard form contracts are likely to be considered and held up to scrutiny to see whether they are unjust or unconscionable in terms of s.52A and the Fair Trading Act equivalents.

That leads of course to the process which the judge has described of banks reviewing their standard form documentation.

In summary then, if I might just pick up on his Honour's closing remarks, both the legislatures and the courts are now requiring a higher standard of commercial ethics by virtue of broad brush tests of unfairness and unconscionability. Self-interest has been found wanting as the sole motivator of business conduct. Judicially these requirements are finding expression in the law of unconscionability, equitable estoppel, undue influence, relief from forfeiture, and constructive trusts. The courts seem unhappy with the standard of commercial morality currently prevailing and are requiring business and institutions to lift their game.

No simple rules as to how to cover oneself are going to work. It seems to me that we are not in an area of strict and complete legalism and simple answers, but in an area of flexible equity. And a general increase in standards of care (or caring even) for the other party, in prudence and in honesty, in lieu of sharp or sloppy practice is what the courts seem to be seeking. Certainly it is what the legislatures seem to be seeking, and it is that which is needed.

I have no clever advice as to how banks may go about this other than to say that all the things that they seem to be doing at the moment are correct in terms of reviewing their procedures, their manuals and their standard form documentation and so on. Simple answers such as adopting a straight forward rule of encouraging

the other party to get independent legal advice will certainly go some way towards getting banks out of the difficulties they are encountering. But because the courts and legislatures are seeking an increase in the standards of commercial conduct generally, particularly in relation to consumers, a set of bright line rules and simple solutions will not provide a panacea.