FEES? NOT SO SIMPLE: *ANDREWS AND ORS V AUSTRALIA NEW ZEALAND BANKING GROUP LTD* [2012] HCA 30 (6 SEPTEMBER 2012)

LUDMILLA K ROBINSON[*]

I INTRODUCTION

On 22 September 2010 the appellants commenced representative proceedings in the Federal Court of Australia against the Australia New Zealand Banking Group ('ANZ') pursuant to Part IV of the *Federal Court of Australia Act* 1976 (Cth). There were approximately 38,000 group members. John Andrews, Angelo Saliba and Geoffrey Field were the 'head' applicants, or representatives, for the group members. Their claim was based upon the premise that certain 'fees' charged by the ANZ are not, in effect, fees at all, but penalties imposed upon the Bank's customers and, as such, are void or unenforceable pursuant to the doctrine of penalties. As a consequence, the appellants further claimed restitution for money had and received or, in the alternative, damages.

At first instance, Gordon J held that the majority of the fees charged by the ANZ could not be characterised as penalties because the penalty doctrine cold only be invoked when the impost arose from a breach of contract or where there was no responsibility or obligation upon the appellants to avoid the events which triggered the imposition of the fees.

The appellants appealed against this finding to the High Court, which allowed the appeal with costs, determining that the penalty doctrine could be applied where there was no breach of contract or occurrence of an 'uncontrolled' event. The High Court remitted the matter to the Full Court of the Federal Court for determination as to whether the ANZ fees were penalties within the parameters discussed in its judgment.

In addition to the proceedings under consideration, six similar proceedings were commenced in the Federal Court against other

[*] BA (Hons) (JCU), Dip Ed (UNE), Dip Law (JAB), PhD (JCU), SJD (UTS), Barrister and Lecturer in Law at the University of Western Sydney.

Australian financial institutions, including the other major banks, bringing the total of represented litigants to approximately 170,000 and the total value of the claims in excess of $223 million.

Apart from the significance of the number of litigants involved in the representative actions, the ultimate effect of the High Court's decision and the subsequent findings of the Full Court of the Federal Court in this matter upon banking and finance practice, bank/client relations and financial institution profitability, cannot be overstated.[1]

II BACKGROUND: THE FEDERAL COURT PROCEEDINGS

The Federal Court proceedings were commenced in the Victorian Registry of the Federal Court[2] and claimed relief against:

> fees identified as honour, dishonour, and non-payment fees charged by the ANZ in respect of various retail deposit accounts and business deposit accounts, and fees identified as over limit and late payment fees charged by the ANZ in respect of consumer credit card accounts and commercial credit card accounts. [3]

Although the initial pleadings filed by the applicants contained a number of grounds upon which their claim was based, including unconscionable conduct on the part of the ANZ[4] and the use by the Bank of 'unfair' terms[5] in its contracts and which were accordingly 'unjust' transactions,[6] the principal emphasis of their claim was for:

1. declarations that the disputed 'fees' were void or unenforceable as penalties; and
2. the repayment of all or part of the disputed fees by way of restitution for money had and received or damages.

In addition, separate questions were presented to the court for resolution. These questions included the issues of:

1. whether the fees were payable by the applicants upon breach of contractual obligations and, or in the alternative,

[1] The practical effect of the decision will be discussed in the Conclusion to this Note.

[2] *Andrews v Australia New Zealand Banking Group Ltd* (2011) 288 ALR 611.

[3] *Andrews v Australia New Zealand Banking Group Ltd* [2012] HCA 30 (6 September 2012), [19].

[4] In contravention of the *Australian Securities and Investments Commission Act 2001* (Cth) and the *Fair Trading Act* 1999 (Vic) ('FTA').

[5] Pursuant to ss 32W and 32Y FTA.

[6] Pursuant to the *Consumer Credit (Victoria) Code.*

2. whether the applicants had a responsibility to ensure that the circumstances giving rise to the fees did not occur.

As pointed out on appeal by the High Court in its judgment: 'If there was an affirmative answer to either of the alternative questions, it was then asked whether the fees were capable of being characterised as a penalty by reason of that fact.'[7]

What had been conceded by the ANZ, and was therefore not in issue, was the fact that the disputed fees were not based upon an estimate by the Bank of the damage it would suffer should a breach of the Bank's requirements occur. It was therefore accepted by the parties and consequently by the court, that the fees charged were disproportionately high in relation to the costs incurred and the resultant loss suffered by the Bank.

Gordon J, the primary judge, found that a late payment fee was payable on breach of contract and, as such, could be characterised as a penalty and was therefore void. In respect of the other fees, however, her Honour found that the charges were not imposed as a result of any breach of contract, nor did the applicants have a responsibility to avoid the occurrence of any event which would give rise to the imposition of the fees. Thus, these fees could not be brought within the ambit of the penalty doctrine. In arriving at this decision, her Honour followed the reasoning *Interstar Wholesale Finance Pty ltd v Integral Home Loans Pty Ltd* [8] ('*Interstar*').

On 21 December 2011, the applicants filed an Application for Leave to Appeal in the Federal Court against part of the orders made by Gordon J. In January 2012, application was made by the applicants to have the Leave Application and the Appeal itself, if Leave were granted, removed to the High Court. On 11 May, the High Court granted the Application.

III PROCEEDINGS IN THE HIGH COURT OF AUSTRALIA

A *Grounds for the Appeal*

The appellants appealed to the High Court to set aside the findings, set out in orders 1 and 2 and as handed down by Gordon J in the primary proceedings on 13 December 2011:

[7] Ibid [20].

[8] [2008] NSWCA 310; (2008) 257 ALR 292.

1. that the honour, dishonour, non-payment and over limit fees were not charged by the ANZ upon breach of contract by its customers; and
2. that the customers had no responsibility or obligation to avoid the occurrence of events upon which these fees were charged, and

accordingly, the fees could not be characterised as penalties.

The effect of Gordon J's decision was to limit the application of the penalty doctrine to those instances where the fee was imposed as a result of:

- breach of contract, or
- the occurrence of an event which the appellants had no obligation or responsibility to control (i.e. an uncontrolled event).

It could be argued this limitation of the penalty doctrine puts a 'block' upon equitable relief by confining it solely to the remediation of injustices arising from the enforcement of contractual rights.[9]

In the grounds for their appeal, the appellants pleaded that:

1. 'the fees in question were imposed upon or in default of the occurrence of stipulated events but were out of all proportion to the loss or damage which might have been sustained by the ANZ by reason of the occurrence of those events;'[10]
2. the fees were charged for a service with no content, and
3. 'despite the form of the dishonour fee, with the provision of further accommodation by the ANZ to the customer, in substance it is a disguised penalty.'[11]

The appellants also sought to challenge various statements from *Interstar*[12] relied upon by Gordon J in her judgment.

Further, in her judgment Gordon J also raised the issue as to whether the ANZ requirement to pay the fees was not:

> a security for performance by the customer of its obligations to the ANZ, or whether the fees were charged by the ANZ, as specified in pre-existing arrangements with the customer, and ANZ respectively, for the further accommodation provided to the customer by its

[9] See part C below.

[10] *Andrews* [2012] HCA 30 (6 September 2012), [27].

[11] Ibid [28].

[12] *Interstar* [2008] NSWCA 310; (2008) 257 ALR 292.

> authorising payments upon instructions by the customer upon which the ANZ otherwise was not obliged to act, or upon refusal of accommodation.[13]

However, the Court decided that such 'live issues' of this nature 'is entirely a matter upon further trial,'[14] and therefore, pursued the question no further.

Thus, in formulating their joint decision regarding the application of the penalty doctrine, French CJ, Gummow, Crennan, Keifel and Bell JJ, addressed (*inter alia*) the following issues:

1. the genesis, nature, scope and effect of the penalty doctrine;
2. the *Interstar* decision;
3. the various meanings of the term 'condition' in bonds and contracts; and
4. the common law action of assumpsit.

B *The Penalty Doctrine*

A penalty is a 'punishment' imposed for non-compliance with a term or condition of an agreement which demands from the party in breach 'an additional or different liability'[15] from the requirement set out in the original term or condition. Thus, a penalty will arise in the following circumstances:

- In an agreement between A and B, there is a stipulation[16] which imposes a liability upon A, such as the repayment of a debt by instalments paid at particular intervals, This is referred to as the primary stipulation.
- Collateral to this primary stipulation is a secondary obligation which comes into effect if, and only if, A breaches the primary

[13] *Andrews* [2012] HCA 30 (6 September 2012), [79].

[14] Ibid [83].

[15] Ibid [9].

[16] The High Court chose to use the term 'stipulation' in reference to the clauses in which the fees were prescribed, rather than the words 'term,' 'obligation' or 'condition' because it better reflected 'the origin of the penal obligation or condition, as known today, in the stipulation (*stipulatio*) in Roman law at a period where stipulations for the payment of money were alone valid,' ibid [37]. The utility of the word 'stipulation' in attempting to clarify the nature of a penalty, in preference to the more common appellations is questionable. It is arguable that the mere derivation of a word from a Latin (or Greek) source does little to elucidate the concept it encapsulates. Indeed, it might also be argued that the opposite effect is the most common outcome of detailed etymological discussion.

stipulation. For example, if A fails to make the required repayment instalment on time.

- The collateral stipulation imposes a detrimental condition upon A, such as the payment of an additional impost, but confers a benefit upon B.[17]
- As a result, the collateral stipulation may be regarded as being in the nature of a security for the proper performance by A of the primary stipulation.[18]
- Thus, provided that B can be compensated for any detriment occasioned by A's failure to observe the primary stipulation, A is required to provide compensation, but only to the extent of the damage suffered by B.
- However, if the compensation prescribed by the collateral stipulation exceeds the loss and/or damage suffered by B, the impost will be characterised as a penalty.

It is important, however, to note the following:

- A penalty cannot be imposed if B cannot be compensated financially for the loss or damage caused by A's default. 'It is the availability of financial compensation which generates the "equity" upon which the court intervenes; without it the parties are left to their legal rights and obligations.'[19]
- The primary stipulation may relate to the occurrence of an event unrelated to the obligation imposed upon A to make a payment or repayment.[20]
- Nor is it necessary for the collateral stipulation to require A to make a money payment to B in order to be characterised as a penalty. The stipulation which requires A to transfer to B some other type of property may also be a penalty, if the compensation imposed exceeds the quantum of loss or damage suffered by B.[21]

Thus, the character of a penalty will be accorded to a stipulation which requires A to provide compensation to B in excess of any loss or damage suffered by B as a result of A's failure to fulfill a primary obligation.

[17] Ibid [10].

[18] Ibid. Here the High Court cites both *Rolfe v Peterson* (1722) 2 Bro PC 436, 442; 1 ER 1048, 1052 and *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* [1915] AC 79, 86.

[19] Ibid [11].

[20] Ibid [12].

[21] Ibid [13].

The penalty doctrine developed in equity[22] to provide relief against insistence by one party upon their legal rights, when such insistence would result in an unfair or unconscionable outcome for the other party. Indeed, 'the relief afforded by equity against penalties and forfeitures and unconscionable insistence upon legal rights generally brings into focus the antithetical attitude of equity and the common law.'[23] However, as pointed out by Priestly J in *Austin v United Dominions Corporation Ltd*,[24] in the nineteenth century 'the courts showed a restlessness with their longstanding duty to relieve against penalties.'[25] His Honour went on to suggest that this restlessness was the outcome of the rise of the concept of freedom of contract which in turn resulted in incorporation of the penalty doctrine into the common law.[26] He also noted that 'the operation of that law was clarified by the recognition of the distinction between a penalty and a genuine pre-estimate of liquidated damages.'[27]

It is highly arguable that Priestly J's implied acceptance of the proposition that an equitable doctrine had, in fact, been 'incorporated' into the common law is a manifestation of the so-called 'fusion fallacy.'[28] Indeed, the High Court in *Andrews* was at pains to distinguish between the concept of a penalty, on the one hand and on the other, a pre-estimate of liquidated damages,[29] thereby prefiguring their criticism[30] of the New South Wales Court of Appeal statement in *Interstar* that 'the modern rule against penalties is a rule of law, not equity.'[31]

Not only did the High Court reaffirm that the penalty doctrine was one of equity, but it unambiguously rejected the ANZ contention that the scope of the doctrine was limited to instances of breach of contract.[32] Moreover, the penalty doctrine was not applied exclusively to compensation for breaches of contract, but could be triggered by the

[22] The genesis of the doctrine is uncertain, but it was certainly extant in its modern form in Chancery during the Chancellorship of Lord Nottingham (1673-1682). See R Meagher, D Heydon and M Leeming, *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies* (LexisNexis Butterworths, 4th ed, 2002) 577 [18-010].

[23] Ibid.

[24] [1984] 2 NSWLR 612.

[25] Ibid 626.

[26] Ibid.

[27] Ibid.

[28] Discussed briefly in Part 4 below.

[29] *Andrews* [2012] HCA 30 (6 September 2012), [15].

[30] Ibid [31]–[32].

[31] *Interstar* (2008) 257 ALR 292, 320.

[32] *Andrews* [2012] HCA 30 (6 September 2012), [46].

failure of an occurrence of an event[33] which was stipulated in the agreement between the parties but did not, of itself, impose a contractual obligation.[34] The Court cites with approval[35] the statement of Brereton J in *Interstar* at first instance, who states that:

> relief may be granted in cases of penalties for non-performance of a condition, although there is no express contractual promise to perform a condition – apparently on the basis that despite the absence of such an express promise, a penalty conditional on failure of a condition is for these purposes in substance equivalent to a promise that the condition will be satisfied.[36]

This reflects the 'regard paid by equity to substance rather than merely to form,'[37] and is demonstrated by 'the grant of relief in the case of penal bonds for non-performance of a condition which was not the subject of any contractual promise.'[38] Thus, the attempt by the Court of Appeal in *Interstar* to limit the scope of the penalty doctrine to a contractual promise arose from a misunderstanding of the doctrine itself and was therefore erroneous.

C *The Interstar Decision*

The appellant in *Interstar* was a finance company and the respondent, Integral Home Loans Pty Ltd ('IHL') conducted a business as a 'mortgage originator' (aka a mortgage broker). IHL was paid commissions by Interstar pursuant to a series of agreements on any mortgages it introduced to the finance company. These agreements also empowered Interstar to terminate the agreements if 'any one of a range of events'[39] occurred. Not all of the events constituted breaches by IHL, nor were all of the events subject to IHL's control.

At first instance, Brereton J found that the termination clause constituted a penalty provision and was therefore void on the basis that 'the event giving rise to the penalty, as the act or event upon which liability was conditioned, could be the termination of the agreements even if the ground for termination was not a breach

[33] Or, conversely, the actual occurrence of the event.

[34] Ibid [49].

[35] Ibid [67].

[36] *Interstar* [2007] NSWSC 406; (2007) Aust Contracts Reports 90-261, 90,037

[37] *Andrews* [2012] HCA 30 (6 September 2012), [49].

[38] Ibid.

[39] *Interstar* (2008) 257 ALR 292, 320.

thereof.'[40] Thus, because the provision was void, IHL were entitled to continued receipt of the commissions.
The Court of Appeal, however, held that the agreements conferred no accrued rights upon IHL. Moreover, since there was no forfeiture of property upon termination, the provisions of the agreements were neither a means of ensuring compliance with the contracts nor a penalty.[41]

The High Court, however, disagreed with the Court of Appeal in its findings that:

1. Brereton J, at first instance, had erred in 'denying that the [penalty] doctrine had ceased to be one of equity;'[42]
2. that the doctrine was now wholly legal in nature;[43]
3. the application of the doctrine was limited to failures of stipulations which were breaches of contract;[44]
4. the penalty doctrine reflects the public policy 'of keeping parties to their bargains.'[45]

Accordingly, the High Court upheld the appellants' challenge to the *Interstar* decision and went so far as to state that the Court of Appeal had 'misunderstood the scope of the penalty doctrine.'[46]

D *Definition of the term 'condition'*

Further to its discussion of the decision in regard to *Interstar*, the High Court turned its attention to both the definition of the term 'condition' and the consideration of nature of a bond.[47] First, 'like the term "rescission," the term "condition" has several distinct meanings and application.'[48] Second, the nature of the bond is relevant because 'it was here that equity first intervened.'[49] A bond, unlike a simple contract or exchange of promises, is an instrument under seal 'whereby the obligor is bound to the obligee.'[50]

[40] Ibid 319.
[41] Ibid.
[42] *Andrews* [2012] HCA 30 (6 September 2012), [29].
[43] Ibid.
[44] Ibid.
[45] Ibid [31].
[46] Ibid [50].
[47] Ibid [33]–[45].
[48] Ibid [33].
[49] Ibid.
[50] Ibid [34].

In the modern context, a 'condition' is taken to denote 'a vital or material promise, the breach of which will repudiate a contract.'[51] However, the term 'condition' does not have either this denotation or connotation when used in connection with a bond. Rather, the term 'condition' is used to indicate the agreement to perform the condition: it is an 'acknowledgement of indebtedness.'[52]

In the early years of the common law, a bond was used to secure the strict performance of an obligation and was thus, in the nature of a penalty, which could be invoked if a particular condition did, or did not, eventuate. The condition need not be the occurrence of an event, but could also have been an act or omission. In such cases, equity would only intervene if the failure of the condition were compensable. From here, the courts of equity went on 'to extend their jurisdiction to deal with stipulations which were penal provisions in simple contracts. However, it does not follow that this extension was a change in the nature of the jurisdiction.'[53]

Thus, the High Court's carefully argued discussion of the term 'condition' and the nature of a bond served to demonstrate that:

> (a) the first field for the operation of the equitable doctrine concerned the enforcement of bonds, (b) with respect to the bonds, the expressions "obligation" and "condition" are not employed in the same or corresponding sense as appears in dealing with the breach of contractual promises, and (c) it does not follow, as the ANZ would have it, that in a simple contract the only stipulations which engage the penalty doctrine must be those which are contractual promises broken by the promisor.[54]

E *The common law action of assumpsit*

Finally, in its discussion of the issues raised in *Andrews*, and in particular, the decision in *Interstar*, the High Court turned its attention to the apparent confusion between the penalty doctrine and the common law action of assumpsit. Although assumpsit was abolished by the *Judicature Act* 1873 (36 & 37 Vict c 66) ('*Judicature Act*'), the term has survived and is used today to denote an action for damages for breach of a simple contract.

[51] Ibid [35].
[52] Ibid [36].
[53] Ibid [44].
[54] Ibid [45].

In its submissions, and based upon the *Interstar* decision, the ANZ claimed that the scope of the penalty doctrine had been 'restricted to those cases today where, hypothetically, an assumspsit action would have lain at common law in the nineteenth century.'[55]
However, in regard to the *Interstar* decision, the High Court notes that the Court of Appeal: 'rather than acknowledging the concurrent administration in New South Wales (as elsewhere) of law and equity, appears to treat the penalty doctrine as having disappeared from equity by absorption into the common law action of assumpsit. This proposition should be rejected.'[56]

Assumpsit developed in common law courts as a remedy for breaches of agreements not under seal and for which an action for breach of covenant would not lie. It was further 'extended to certain cases where there was no more than an implied undertaking to pay, thus giving rise to the unhappy expression "quasi-contract."'[57] Eighteenth century English statutes regulated the enforcement of bonds and the obligations of a debtor by limiting repayment to the principal, interest and costs.[58] However, these regulations did not prevent the promisee from claiming damages in excess of the amount owed from the promisor, either upon suit or as provided in the bond. Further, the common law courts were constrained by the remedies they could offer to alleviate such excessive claims. For example, the common law courts' 'power to grant injunctions . . . was limited to restraining the repetition or continuation of breaches of contract in respect of which the plaintiff was entitled to bring an action for damages.'[59] Thus, the penalty doctrine was the only means of relief against excessive and unsubstantiated claims based upon contract. Therefore, in conclusion to their discussion on the separate natures of assumpsit and the penalty doctrine, the High Court stated that: '[i]t should be emphasised that, in any event, under the Judicature legislation it is equity not the law that is to prevail. In *Interstar* the Court of Appeal thus had no basis for the proposition that the penalty doctrine is a rule of law not of equity.'[60]

IV *ANDREWS* AND THE FUSION FALLACY

[55] Ibid [62].
[56] Ibid [51].
[57] Ibid [52].
[58] For a detailed discussion of the history of statutory control of the enforcement of bonds see ibid [53]–[61].
[59] Ibid [59].
[60] Ibid [63].

The *Interstar* decision and the unquestioning acceptance at first instance by Gordon J in *Andrews* of the NSW Court of Appeal's pronouncement that the penalty doctrine had become part of the common law are disturbing examples of the persistence of the pernicious and, apparently immortal, 'fusion fallacy.' The fusion fallacy arose in the wake of the *Judicature Act* in the nineteenth century and is the mistaken belief that, as a result of the Act, there was a 'fusion' of the common law and equity into a single system of substantive law. Whilst the Act enabled common law courts to apply equitable remedies, such as injunctions, specific performance, and restitution for money had and received, the enactment was solely procedural in nature. It did not 'fuse' equitable doctrines and remedies with those of the common law and therefore was not substantive.[61] Equity always was and always will be, one hopes, a system of doctrines and remedies which exists independently from the common law.

It is therefore interesting to note that throughout *Andrews* the High Court is at pains to stress the independence of equity from the common law. Further, it is 'consummation devoutly to be wished' that the contemporary perpetuators of the fallacy take note and that the High Court's ratio in *Andrews* proves to be the final word necessary on this topic.

V CONCLUSION

As noted in the Introduction, above, the significance of the decision in *Andrews* cannot be understated. In purely legal terms, the High Court has clarified the principles relating to the application and scope of the penalty doctrine. It is now clear that the doctrine may be invoked in any instance where:

- fees are charged by an institution which are unrelated to a breach of contract; or
- there was no obligation or responsibility on the part of the customer to avoid an occurrence upon which the fees were charged.

The key is whether the fee exceeds the damage suffered by the institution. If so, the fee may be characterised as a penalty. Thus, it is a matter of substance and not form.

[61] For a discussion of the fusion fallacy, see Meagher, Heydon and Leeming, above n 22, 52–54, [2-100]–[2-110]

On that basis, it is arguable that the scope of the penalty doctrine is not limited to finance or banking agreements, but could be extrapolated to any agreement in which a fee (or forfeit in the nature of a fee) is charged by one of the parties for an obligation imposed upon the other. For example, clauses in leases which require the tenant to pay a fee, or forfeit their bond, if, in the opinion of the landlord or agent, the leased premises require some form of rectification on termination of the lease. If the fee or bond exceeds the cost of rectification, it is arguable that the requirement is a penalty and therefore void. Also, by analogy, the principles could apply to the sale of commodities and services, such as electricity and gas.[62]

It is also arguable that, in practical terms and especially if the Full Court of the Federal Court find in favour of the Appellants, the financial consequences for all banks and financial institutions in regard to customer contracts could be incalculable. Not only would there need to be a reimbursement to all customers of all fees charged upon the same terms as those charged by ANZ, but those banking and finance contracts couched in the same terms as the Andrews/ANZ agreements would need to be rectified in accordance with the decision. Moreover, all such future contracts would need to be reviewed and rewritten, so as to avoid the characterisation as penalties.

Irrespective of the eventual decision of the Full Court of the Federal Court in regard to the matters remitted to it by the High Court, *Andrews* has, at the very least, provided possibly unpalatable food for thought for Australia's financial institutions in regard to the fees charged to customers and the hallowed concept of the 'bottom line' of profitability, which is most frequently pursued at the considerable expense of their customers.

[62] See the High Court's discussion of *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* [1915] AC 79, *Andrews* [2012] HCA 30 (6 September 2012), [69]–[77].