NZLR.

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IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CP.147/86

[redacted]

1774

IN THE MATTER of the Credit Contracts Act 1981

A N D

IN THE MATTER of Memorandum of Mortgage No. 550205/5 (Canterbury Land Registry)

BETWEEN: EMUS HOLDINGS (AUCKLAND) LIMITED a duly incorporated company having its registered office at Papatoetoe and carrying on business as an Investment Company

Plaintiff

A N D: PAUL ERNEST PITHER of Christchurch, Horticulturist, a n d BARBARA PITHER of Christchurch, Housewife

First Defendants

AND GULF MORTGAGE COMPANY LIMITED a duly incorporated company having its registered office at Auckland an carrying on business as a Finance Company

Second Defendant

Hearing: 24 October 1986

Judgment: 20 November 1986

Counsel: C F Foote for Plaintiff
N A Till for First Defendants
G V Hubble for Second Defendant (abides decision of the Court, given leave to withdraw)

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JUDGMENT OF HENRY, J.

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In this action the Plaintiff seeks rectification of the terms of a certain memorandum of mortgage and also

relief under s.31 or alternatively s.32 of the Credit Contracts Act 1981 from the consequences flowing from a failure to comply with the disclosure provisions of that Act.

The First Defendants are the registered proprietors of a property situated at Belfast, Christchurch. In late 1984 they entered into negotiations with Mr R W Boyd, a mortgage broker and governing director of the Second Defendant, concerning an advance of money to be secured by way of mortgage over the property. These negotiations culminated in an arrangement recorded in a letter dated 29 May 1985. Earlier that same month Mr Boyd had telephoned a representative of the Plaintiff with a view to negotiating the sale of the proposed mortgage, the Plaintiff being an investment company which as part of its business operations purchased mortgages at a discounted figure. The negotiations between the Plaintiff and the Second Defendant were concluded on or about 28 May 1985. The First Defendants duly executed a memorandum of mortgage on 5 June 1985 securing repayment of a principal sum of $100,000.00 due on 7 June 1987. Registration of the mortgage was effected on 11 June 1985. Settlement as between the First Defendants and the Second Defendant then took place with the appropriate transfer of mortgage being executed on 17 June and registered on 27 June. The terms of the mortgage called for payment of interest quarterly on the 7th days of June, September, December and March, at a stipulated interest rate of 16%, with a penalty interest rate being fixed at 20%.

The memorandum of mortgage incorrectly records the interest commencement date as being 7 June 1987 (the date for repayment of the principal) instead of 7 June 1985, but nothing presently turns on that admitted error. No reduction of the principal sum is called for during the term of the advance.

Consequent upon a failure by the First Defendants to make payment of the interest instalments, a notice under s.92 of the Property Law Act 1952 was served on them, following which proceedings were initiated to effect a mortgagee's sale of the property. These resulted in a challenge being made to the validity of the intended exercise of the power of sale because the original loan transaction did not comply with the disclosure provisions of the Credit Contracts Act 1981. The initial complaint was that although the mortgage called for quarterly payments of interest, the disclosure notice detailed monthly payments. As a result, on 14 October 1985 amended disclosure forms were sent to the First Defendants detailing quarterly payments of interest. Following subsequent correspondence between the respective solicitors a further amended disclosure notice was sent to the First Defendants on 30 January 1986, this time in response to a claim that the finance rate was substantially incorrect. Three main issues arise, which I will now consider.

Rectification:

The rectification sought is in respect of the provision of the mortgage which requires interest to be paid quarterly. On behalf of the Plaintiff, it was contended that the true agreement as between the First Defendants and the Second Defendant was that interest was to be paid monthly, not quarterly. The legal principles to be applied are not in dispute, it being accepted that the inquiry is as to the common intention of the parties down to the time of execution of the written instrument (Dundee Farm Ltd v Bambury Holdings Ltd [1978] 1 NZLR 647). It was also common ground that the fact of the mortgage being transferred did not here affect the Plaintiff's right to seek rectification.

Mr Boyd, governing director of the Second Defendant, deposed to the effect that the negotiations with the First Defendants had proceeded on the basis of interest being payable monthly. That this was so, is supported by the documentation leading up to the execution of the mortgage which can be summarised in the following manner :

9 May: Letter from Mr Boyd to Mr D J Davies, director and secretary of the Plaintiff, which refers to "interest only per calendar month".

28 May: Letter from Mr Boyd to Mr Davies as to revised interest rate, again stating "interest only per calendar month".

28 May: Letter from Mr Boyd to Plaintiff's solicitors advising particulars of mortgage with "interest only per calendar month".

29 May: Memorandum signed by First Defendants recording terms of proposed mortgage, interest "payable monthly".

29 May: Letter of instructions from Mr Boyd to his solicitors to prepare mortgage documents "interest only per calendar month".

5 June: Memorandum of disclosure requirements, signed by First Defendants noting monthly payments of interest.

5 June: Bank Authority Automatic Payment signed by First Defendants requiring monthly payments of "1st mortgage interest"

The only written reference to interest being payable quarterly is to be found in the memorandum of mortgage itself. A legal employee, Claire Brown, gave evidence of having prepared and typed that document from Mr Boyd's letter of instructions of 29 May. She explained that the majority of mortgage documents she was concerned with related to the solicitors' nominee company which always contained provisions for quarterly payments of interest, and

accordingly an insertion of that provision in the present instance was probably due to inadvertence on her part. I can see no other explanation for what has occurred, and I am satisfied that at all relevant times it was the intention of the parties to the mortgage that the interest payable on the loan was to be payable monthly. This inference I think is inescapable when regard is had to the circumstances and the documentation leading up to the execution of the mortgage, particularly in the absence of any competing allegation or suggestion from either of the First Defendants.

It remains then to consider whether an order for rectification should now be made. In exercising the discretion, the following relevant factors need to be considered. First, any order for rectification would be effective as from the date of execution of the instrument, namely 5 June 1985, thus putting the First Defendants in a different breach situation from that which has pertained up until now. Second, the Plaintiff itself proceeded on the basis of the express terms of the mortgage in that it gave an amended disclosure notice on 14 October specifying quarterly payments of interest. This stand was repeated in the second amended disclosure notice dated 30 January 1986. Third, the plea for rectification was not advanced until the filing of the amended statement of claim on 22 July 1986, the action having been instituted on 27 February 1986. Fourth, no substantial need for rectification is evident.

No prejudice or detriment of any sort to the Plaintiff emerges, and the loan has now only a comparatively short time to run until maturity.

Looked at overall, I do not think it an appropriate case to exercise the discretionary remedy and accordingly an order for rectification will not issue.

Non-disclosure of finance rate:

Section 21 (1) (a) requires initial disclosure to contain all the information, statements and other matters specified in the Second Schedule. One of the specified matters is the finance rate, which is itself defined in s.6. The finance rate disclosed in the initial disclosure document here was 25.5%, which it is now common ground was incorrect. The finance rate involved in this transaction is 28.8%, substantially outside the tolerance of .25% permitted by s.6 (1) (a). The disclosure requirements of the Act were therefore contravened.

Relief under s.31:

Section 31 of the Credit Contracts Act 1981 provides :

> "31. Relief for inadvertent non-disclosure:
> Sections 24 to 28 of this Act shall not apply in respect of a failure to make initial disclosure, modification disclosure, continuing disclosure, or request disclosure of a controlled credit contract or modification contract (as the case may be ) if the creditor shows that -

(a) The failure was due to inadvertence or to events outside the control of the creditor; and

(b) Disclosure was made as soon as reasonably practicable after the failure was discovered by the creditor or brought to his notice; and

(c) Where disclosure documents relating to the contract state as the finance rate of the contract a rate that is less than the correct finance rate, the creditor has reduced the finance rate of the contract to the rate diclosed in those documents; and

(d) The creditor has compensated or offered to compensate the debtor under the contract for any prejudice caused the debtor by the failure."

Section 24 prohibits enforcement of a credit contract or of any security given pursuant to it before the required disclosure is made. Section 25 provides a penalty for failure to make initial disclosure under which the debtor's liability to pay an amount equal to "the specified amount" is extinguished. It is common ground that in the present case, that amount is the total cost of credit amounting to $50,218.92. Sections 26 to 28 have no present application.

To obtain relief under s.31 a creditor must establish each of the four matters there detailed. If he does, then total relief from the effects of ss.24 to 28 must follow, no element of discretion arising. I will refer to each of the subsections.

(a) On the evidence I am not satisfied that the failure to disclose the correct finance rate was due either to inadvertence or to events outside the control of the creditor.

In my view the term "creditor" although defined in s.2 as including a transferee, must refer in this context to the original creditor whose obligation it was to make the disclosure. The present plaintiff did not become a "creditor" until such time as the transfer of mortgage was completed, which was after initial disclosure was required to be made, and its rights (and obligations) as a creditor did not commence until that time. The only direct evidence as to inadvertence was from the legal employee, Claire Brown, who typed in the now admittedly incorrect finance rate figure of 25.5%. She was unable to explain why she had put in that figure and assumed, but I think only because subsequently she had been so told, that it was a mistake. No evidence was given as to her actual instructions, nor as to who had made the calculation which she was instructed to put in. The evidence is quite equivocal, and even when taken in conjunction with the preliminary documentation, which contains mention of a finance rate of or about 29%, does not satisfy me that the 25.5% figure was inadvertent. All that is established is that it is an incorrect figure for the finance rate of this particular transaction, and that is insufficient to bring the case within s.31 (a).

(b) Disclosure of the correct finance rate was not made until the second amended notice was sent on 30 January 1986. Plaintiff's solicitors had been alerted to the real possibility of error on 1 November 1985, and

by 12 November they were in possession of an actuarial report showing a figure of 29%. In my judgment the delay is too great to allow a finding that correct diclosure was made as soon as reasonably practicable.

(c) An appropriate reduction was made.

(d) An effective offer to compensate was made. Some criticism was levelled at the form of the offer to compensate, but the principal letter concerned, dated 30 January 1986, is in my view expressed in clear and unequivocal terms and complies with the provisions of s.31 (d).

Because two of the four pre-requisites have not been established, it follows that the Plaintiff is not entitled to the relief sought under s.31.

Relief under s.32:

Section 32 provides :

"32. Power of the Court to reduce penalty:

(1) The Court may, on the application of a creditor under a credit contract, order -

(a) That any of sections 24 to 28 of this Act shall not apply in respect of a credit contract, or modification contract, or any class or classes of such contracts; or

(b) That any amount for which liability has been extinguished pursuant to any of those sections be reduced to an amount specified by the Court.

(2) In deciding whether to make such an order, the Court shall have regard to the following matters :

(a) Whether the creditor is a financier:

(b) The extent of, and the reasons for, the non-disclosure:

(c) The extent to which a debtor or guarantor has been prejudiced by the non-disclosure:

(d) Such other matters as the Court thinks fit.

(3) Any order under this section may be made on such terms and conditions as the Court thinks fit."

Relief under this section is discretionary. The philosophy behind the penalty provisions for non-disclosure clearly is to make the Act self-policing and to encourage compliance with its terms, and there is little point in enacting legislation of this kind, designed as it is primarily for the protection of the ordinary consumer, if there are no real "teeth" to ensure the intended protection is real. The long title of the Act speaks of ensuring that all terms of contracts are disclosed to debtors and of ensuring that the cost of credit is disclosed on a uniform basis in order to prevent deception and to encourage competition. In the light of that sort of background it is clear why a monetary penalty such as is provided by s.25 has been enacted. The legislation, however, has also recognized that there may be circumstances where relief from those consequences should be given. Section 31 excuses, with appropriate safeguards for the debtor, simple inadvertency.

Otherwise the starting point is that s.25 is to take effect, and s.32 will only fall to be applied in circumstances where the general intent and purpose of the legislation can still be maintained and implemented without derogation by the giving of relief from what are to be regarded as the prima facie consequences. It follows, I think, that there must be substantive reasons for departing from the stipulated penal provisions.

Because of the special nature of the Act little assistance is to be gained from dicta relating to other legislative enactments. The only positive guidance to the exercise of the Court's discretion is to be found in paragraphs (a) (b) and (c) of subsection (2), to which regard must be had.

To consider whether reasons for reducing the penalty are established, I turn to the relevant matters.

(a) Whether the creditor is a financier:

The Plaintiff is a financier, as also is the Second Defendant, the original creditor. The importance of this factor is self-evident. A financier is a person who, in general terms, is in the business of financing. Such a person is expected to be fully aware of the statutory requirements, and to ensure important matters such as disclosure of the finance rate are properly covered by the statutory documentation.

The finance rate is a matter of particular significance, because it is that which most readily advises the debtor of what his contract really means in respect of what his borrowing is costing him. It also enables and indeed encourages "shopping around", thus promoting the desirable concept of competition. Care and accurancy are required, and a financier must know the risk is real if correct disclosure is not made.

(b) The extent of, and the reasons for, non-disclosure:

The extent of the non-disclosure or error in respect of the finance rate here is of substance, being one of over 3%. On the other hand it must be borne in mind that there had been reference to the finance rate during the course of negotiations with a figure of 29% featuring, so to that extent the error is less significant than it may otherwise have been. The reasons for this non-disclosure are not clear, and there is no real explanation as to how it came about. At best for the Plaintiff, it can be inferred that there was no intentional attempt to mislead or to defeat the purposes of the Act. The other discrepancies as to frequency and commencement date of interest payments are here of minor significance.

(c) Prejudice to the debtor:

No evidence was adduced to establish that any prejudice has resulted.

Although the First Defendants were in financial difficulty and required the finance as a matter of some urgency, there is nothing to indicate advantage was taken of this aspect, nor that they were diverted from carrying out a search for alternative and cheaper finance. Accordingly I find there has in fact been no prejudice.

(d) Other relevant matters:

The contract is quite ordinary and in usual terms, without any severe conditions adverse to the debtors, although the total cost of credit is quite high with a substantial discount factor of some $18,219.00. The First Defendants have not made any payments of interest, and made no challenge to their expressed liabilty under the mortgage until steps for enforcement were taken. It is obvious they would benefit very substantially overall if s.25 is to operate without adjustment. Another factor is that the Plaintiff has not itself been directly responsible for the non-disclosure, being a transferee in good faith.

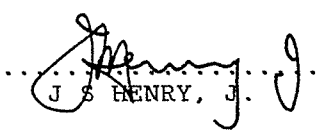
Taking all matters into consideration, I have reached the view that it would here be an appropriate case to give the Plaintiff relief, the extent of which can only be a balancing exercise to try and achieve overall fairness within the context and intendment of the Act.

Under s.25 the amount which falls to be extinguished from the liability of the First Defendants under the original contract is agreed as being $50,218.92. The Plaintiff's attempt to bring itself within the s.31 relief provisions has in my view already resulted in an effective reduction of the finance rate and of the liability of the First Defendants from which it cannot now resile. The quarterly payments of interest have been reduced from $4000.00 to $3186.04, an effective total reduction of $6511.68 over the two year term of the loan, and that must be taken into account. The First Defendants have had the use of the loan and subject to the consequences of any default by them the continuing use of it for the agreed term. The Plaintiff has taken steps to regularise the documentation. Looking at it overall, and giving due weight to those matters specified in s.32 and also to what I believe is the policy of the legislation, I have reached the conclusion that the liability of the First Defendants under the original terms of the contract should be reduced by a total of $15,000.00, this representing where I feel the present case comes within the possible penalty spectrum which lies between nil (s.31) and $50,218.92 (s.25).

Accordingly there will be an order reducing the amount for which the liability of the First Defendants has been extinguished pursuant to s.25 of the Act from $50,218.92 to the sum of $15,000.00, leaving the First Defendants still liable for the balance of $35,218.92.

It would seem that the reduced penalty will take effect at the end of the term of the loan pursuant to s.29, thus leaving the First Defendants under an existing liability to pay the reduced interest instalments meantime.

Costs are reserved, but I indicate without having heard argument that it may be appropriate in all the circumstances for no order to be made.



J S HENRY, J.

Solicitors:

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