The doctrine of penalties

Thomas Prince reports on *Andrews v Australia and New Zealand Banking Group Limited* [2012] HCA 30

The High Court has given new life to the doctrine of penalties, holding that the doctrine is not limited in scope to contractual provisions operating on a breach of contract. This is significant departure from the pre-existing law established by the New South Wales Court of Appeal's decision in *Interstar Wholesale Finance Pty Limited v Integral Home Loans Pty Limited*[1].

Background

The applicants represent a group of approximately 38,000 customers of ANZ who are seeking in proceedings in the Federal Court a declaration that various bank fees charged by ANZ are void or unenforceable as penalties. There are five categories of bank fees in issue, described as honour, dishonour, non-payment, over limit and late payment fees.

At first instance, Gordon J answered a number of separate questions directed to the issue of whether the various fees were payable on a breach of contract and, if so, whether they were capable of being characterised as penalties. Her Honour found that the late payment fees were payable on a breach of contract and therefore were capable of being characterised as penalties. However, her Honour found that the remaining fees were not payable on breach of contract by the customer, and were instead charged as a consequence of a decision by ANZ to afford or to decline the provision of further financial accommodation to the customer. Accordingly, following *Interstar*, Gordon J found that the remaining fees were not capable of being characterised as penalties.

The applicants sought leave to appeal to the full court of the Federal Court from Gordon J's answers to the separate questions, and part of that application was removed directly into the High Court.[2] The High Court (French CJ, Gummow, Crennan, Kiefel and Bell JJ in a joint judgment) granted leave to appeal, set aside part of the answers given, and declared that the fact that the fees were not charged upon breach of contract, and that the customers had no responsibility or obligation to avoid the occurrence of the events upon which the fees were charged, did not render the fees incapable of characterisation as penalties.

Doctrine of penalties not limited to breach of contract

The High Court rejected statements of Mason and Deane JJ in *AMEV-UDC Finance Limited v Austin*[3] that the modern doctrine of penalties is a doctrine of law not equity and that the equitable jurisdiction to relieve against penalties had 'withered on the vine'. Relying on a range of historical materials but, principally, a number of 18th century Chancery cases concerning penal bonds, the court rejected the proposition, propounded in *Interstar* and accepted in England,[4] that the doctrine of penalties is limited in application to contractual provisions operating upon a breach of contract.

The High Court explained that a contractual stipulation is, prima facie, a penalty where it imposes upon one party ('the obligor') an additional detriment to the benefit of the other party ('the obligee') and the stipulation is, in substance, in the nature of a security to the obligee for the satisfaction of another stipulation ('the primary stipulation'). The primary stipulation need not be another contractual obligation of the obligor but may be simply the occurrence or non-occurrence of an event. The detriment imposed upon the failure of the primary stipulation need not be the payment of money, but may include the transfer or use of property to or for the benefit of the obligee.

Conditions of relief against penalty

The High Court emphasised that relief against a penalty is only available if two conditions are satisfied. First, compensation susceptible of evaluation and assessment in money terms must be made to the obligee for the failure of the primary stipulation. Secondly, the value of the benefits to be provided under the penalty must, in the sense described in the established cases such as *Dunlop Pneumatic Tyre Co Limited v New Garage and Motor Co Limited*,[5] be incommensurate with the interest protected by the primary stipulation. Where relief is available, the obligor will be relieved from performance of the penalty only beyond the extent of the compensation payable to the obligee for the failure of the primary stipulation.

A Pyrrhic victory?

The High Court's conclusion that the fees in question were not incapable of characterisation as penalties was a significant win for the applicants. However, in

its reasons the court noted that a further issue was presented as a result of Gordon J's findings that the fees other than the late payment fee were charged for further financial accommodation provided to customers. The court drew attention to, and approved, a line of cases[6] to the effect that a contractual term that on its proper construction merely requires the payment of money or the transfer of property by one party as the price for obtaining additional rights is not a penalty. However, this issue was not directly raised by the separate questions answered by Gordon J and the court indicated that it must await further trial, along with the grounds upon which the applicants submit that the penalty doctrine applies to the bank fees.

Thus, while the case is an important one with respect to the doctrine of penalties it is perhaps also another illustration of the dangers of separate questions.

Endnotes

1. (2008) 257 ALR 292.
2. Pursuant to section 40(2) of the *Judiciary Act 1903* (Cth).
3. (1986) 162 CLR 170 at 191.
4. *Export Credits Guarantee Department v Universal Oil Products Co* [1983] 1 WLR 399 (HL).
5. [1915] AC 79, applied in *Ringrow Pty Limited v BP Australia Pty Limited* (2005) 224 CLR 656.
6. Including *Metro-Goldwyn-Mayer Pty Limited v Greenham* [1966] 2 NSWR 717 (CA).