

Banks beware - a new take on late payment fees

Litigation Update

On 5 February 2014, the Federal Court of Australia handed down its much anticipated decision in *Paciocco v Australia and New Zealand Banking Group Limited (ANZ)* [2014] FCA 35 (*Paciocco*). The decision in *Paciocco* - finding that certain late payment fees charged by ANZ to its customers were penalties and therefore unenforceable - is another important development in the law concerning penalties in the finance and banking industry.

The Federal Court in *Paciocco* reinforced the take home 'penalty' principles identified by the High Court in *Andrews v Australia and New Zealand Banking Group Ltd* (2012) 247 CLR 205 (*Andrews*), and the decision will have major repercussions for banks and other financial institutions who charge their customers with standard late payment fees of \$20 or more.

Facts

Paciocco was a representative action brought by a number of ANZ customers who held various accounts with the bank.

The contractual terms for each of the accounts included terms that entitled ANZ to charge the following fees:

- honour;
- dishonour;
- non-payment;
- overlimit; and
- late payment,

(collectively defined by the Federal Court as the 'Exception Fee Provisions').

The key question which the Federal Court considered was whether the exception fees charged by ANZ, pursuant to the Exception Fee Provisions, constituted 'penalties' at common law and in equity.

Who does this affect?

- Banks.
- Bank customers.
- Other financiers or credit providers seeking to impose 'late payment fees' or comparable charges on potential customers.

Article Highlights

- *Paciocco* alleged that two categories of bank fees constituted penalties, being:
 - (i) late payment fees, and
 - (ii) honour, overlimit, dishonour and non-payment fees.
- The Federal Court determined that late payment fees of \$20 - \$35 are a penalty, and therefore unenforceable.
- Fees imposed for an amount over and above the financial prejudice sustained by the financier, and those fees which are considered to be collateral to a primary stipulation in favour of the financier, are likely to be a 'penalty'.



Key considerations and guidelines

In determining whether a fee is a penalty at common law, Justice Gordon confirmed that the principles set out in *Dunlop Pneumatic Tyre Company Limited v New Garage and Motor Company Limited* [1915] AC 79 (*Dunlop*) (confirmed in *Ringrow Pty Ltd v BP Australia Pty Ltd* (2005) 224 CLR 656) remain applicable. In *Dunlop*, the approach adopted by the Court was to pose the following questions in relation to the relevant fee:

- a. Is the sum extravagant and unconscionable compared with the greatest loss that could conceivably be proved to have followed from the breach? If so, then the fee will be deemed a penalty.
- b. Does the breach consist only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid? If so, then the fees will be held to be a penalty.
- c. Is a single lump sum made payable by way of compensation on the occurrence of one or more or all of several events, some of which may occasion serious and other but trifling damage? If so, then there is a presumption (but no more) that the fee is a penalty.

As to whether a fee is a penalty in equity, Justice Gordon found that the question must be framed by reference to the decision in *Andrews*, which emphasised that the fee must operate in the nature of a security for, and as an effective threat for, the satisfaction of the primary stipulation before it could be considered a penalty.

In applying the range of principles derived from *Dunlop*, *Andrews* and *AMEV-UDC Finance Limited v Austin* (1986) 162 CLR 170, Justice Gordon asked the following questions in respect of each Exception Fee:

1. What are the terms and inherent circumstances of each particular contract, judged at the time of the making of the contract?
2. What is the event or transaction upon which the bank imposed the fee?
3. Is the fee payable upon the customer breaching his contractual obligations?
4. Is the fee an additional detriment in the nature of a security for, and as an effective threat for, the satisfaction of the customer's contractual obligations?
5. Is the fee extravagant and unconscionable in amount or it is a genuine pre-estimate of damage?
6. What extent (if any) did the fee exceed the quantum of loss and damage which ANZ actually sustained as a result of the customer breaching his contractual obligations?

Contact



Victoria Butler
PARTNER

t: +61 8 9426 6694
e: vbutler@jacmac.com.au



Paul Mac
SPECIAL COUNSEL

t: +61 8 9426 6715
e: pmac@jacmac.com.au



Anna White
ASSOCIATE

t: +61 8 9426 6796
e: awhite@jacmac.com.au

Nour Kirk
SOLICITOR

t: +61 8 9426 6679
e: nkirk@jacmac.com.au



The decision

The Federal Court ruled that the Exception Fees fell into two broad categories: (i) late payment fees; and (ii) honour, overlimit, dishonour and non-payment fees.

In relation to the first category of Exception Fees, the Federal Court found that the late payment fees constituted a penalty at common law and equity as the liability to pay the late payment fee was contingent upon a breach of contract, and further or alternatively was collateral (or accessory) to a primary stipulation (to make a payment by a particular date) in favour of ANZ.

The Federal Court ruled that the second category of Exception Fees did not constitute a penalty because the consumer's liability to pay each of those Exception Fees was not collateral (or accessory) to a primary stipulation in favour of ANZ. The Federal Court went on to say that the *'liability to pay each arose as a result of, and in exchange for, something more than and different from what had been agreed in the primary stipulation. They were not penal in nature.'*

Unlike late payment fees, honour, overlimit, dishonour and non-payment fees did not arise because of, or involve, a breach of contract. The liability to pay arose from a request by the customer for an advance or loan from ANZ, which ANZ had the discretion to approve (resulting in an honour or overlimit fee) or decline (resulting in a dishonour fee) pursuant to the provisions of the customer's contract.

Commentary

Banks should carefully consider the amount charged for late payment fees. The law will operate so as to ensure that the only money the bank will be entitled to recover from customers, who fail to meet their minimum monthly repayment on debts owed, is a sum which compensates the bank for the financial prejudice occasioned by the actual failure to pay on time.

Disclaimer: This publication is intended to provide general information only and should not be relied upon as legal advice. If you require legal advice on a matter please contact us.

Contact Us

t +61 8 9426 6611 f +61 8 9321 2002 e jacmac@jacmac.com.au

a Level 25, 140 St Georges Terrace, Perth, Western Australia 6000
GPO Box M971, Perth, Western Australia 6843

www.jacmac.com.au