

Claims for Possession of Land Following Mortgage Default - A Rising Tide

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This article provides a brief overview of aspects of the contemporary mortgage market in Australia, together with a short examination of court processes which operate in New South Wales where litigation is commenced following mortgage default.

The Possession List

Home ownership has been an aspiration of many Australians for decades. For most, it is necessary to take out a mortgage to purchase a home. For many, a mortgage commitment will place considerable strain upon family and personal finances. In a range of circumstances, this strain may translate into mortgage default and the institution of court proceedings by the lender seeking, amongst other things, possession of the land secured by the mortgage.

Where proceedings of this type are commenced in this State, they are placed in the Possession List in the Common Law Division of the Supreme Court. Numerically, this is the largest list in the court and the level of filings in the Possession List has increased in recent years.

During 2005, there were 4,873 cases lodged in the Possession List, a 59 per cent increase over the number lodged in 2004.¹ During 2006, there were 5,368 matters commenced in the Possession List, a 10 per cent increase over 2005.²

A 2008 snapshot

The 2006 Australian Census confirms an increase in the level of mortgaged home ownership. In 2006, 33 per cent of occupied private dwellings were fully owned, 32 per cent were being purchased and 27 per cent were being rented. The biggest change since the 1996 Census has been the rise in the proportion of dwellings being purchased, up from 25 per cent. This has been countered by a decline in outright home ownership, down from 41 per cent. In 2006, the median monthly housing loan repayment of the 2,448,212 occupied private dwellings being purchased was \$1,300, up from \$780 (\$1,011 in 2006 dollars) since 1996. In 2006, New South Wales had the highest median monthly loan repayments of all the States and Territories (\$1,517).³

Mortgage lending practices in Australia

There has been a shift in mortgage-lending practices in Australia in recent years as past conservative lending practices have given way to a looser approach.⁴

According to the Australian Prudential Regulation Authority (APRA), since 2001, lenders outside the authorised-deposit taking institutions (ADI) sector began to offer loans written with considerably less than the normally required documentation and checking of income and serviceability (products usually referred to as "*low-doc*" loans). As this market expanded, ADIs responded by offering similar products. There was an increasing tendency for ADIs to offer loans which had originated from mortgage brokers and other third-party channels. In some cases, ADIs accepted assessments done by those who had referred the borrower to them (without ADIs themselves verifying the borrower information). Greater emphasis was placed on the security underlying the loan rather than the ability of the borrower to repay the loan.⁵

A 2003 report commissioned by the Australian Securities and Investments Commission pointed to an increasing use of mortgage brokers with associated problems including poor advice, inadequate disclosure of fees and commissions by some brokers, inconsistent documentation from brokers, uncertainty about the nature and price of the service, fraudulent activity such as manipulating loan applications (in a small number of cases) and a need for clarity as to whether brokers were acting for consumers or were really agents for lenders.⁶ Some legislative reform concerning mortgage brokers has occurred in New South Wales.⁷ National legislation concerning finance and mortgage brokers has been foreshadowed, with draft legislation prepared in New South Wales receiving the support of all States and Territories and the Commonwealth's Office of Regulatory Review. An exposure draft of the Finance Broking Bill 2007 was released on 28 November 2007 for comment.⁸

Following a short-term inquiry, the House of Representatives Standing Committee on Economics, Finance and Public Administration issued a report on 17 September 2007 into home-loan lending practices and the processes used to deal with people in financial difficulty.⁹ The Committee recommended that the Australian Bureau of Statistics collect and publish annual data on housing repossessions, that the Commonwealth Government regulate credit products and advice (including regulation of mortgage brokers and non-bank lenders) and that reforms be made to the External Dispute Resolution (EDR) system.¹⁰

Classes of mortgage lenders

In broad terms, Australian mortgage lenders fall into three groups.

The first group comprises lenders within the APRA-supervised ADI sector including banks, building societies and credit unions. ASIC administers the Australian Financial Services (AFS) licensing system, a requirement of which is that AFS licensees must be a member of an ASIC-approved EDR scheme. These include the Banking and Financial Services Ombudsman (BFSO) and the Credit Ombudsman

Service.¹¹ Banks have adopted the Code of Banking Practice, a voluntary code of conduct which sets standards of good banking practice.¹² The activities of the BFSO include monitoring of compliance with the Code of Banking Practice and obligations under the Uniform Consumer Credit Code concerning customers in financial difficulty.¹³ Credit unions and building societies also have a code of practice.¹⁴

There is a large number of non-ADI lenders whose products and services vary considerably. Some compete in the mainstream home loan market, offering prime and low-doc products using similar lending practices to ADIs.¹⁵

The second group of lenders comprises a range of non-ADI lenders not operating in the same way as traditional banks by raising funds from retail deposits. As a result, they are not supervised by APRA and less detail is known about their operation.¹⁶

Members of the Mortgage and Finance Association of Australia, which include some non-ADI lenders and mortgage brokers, are required to comply with the code of that Association.¹⁷

The third group of lenders comprises other non-ADI lenders, sometimes called sub-prime¹⁸ or nonconforming lenders.¹⁹ The concept of sub-prime, non-conforming or adverse credit lending is well known in Australia and in other countries, including the United States of America where a collapse in the sub-prime market has had detrimental international consequences.²⁰

Sub-prime loans in Australia represent about one per cent of the stock of total mortgages, compared to around 15 per cent in the USA, and arrears on Australian loans are considerably less than those on US sub-prime loans.²¹ Further points of contrast are that Australian non-conforming loans have lower loan-to-valuation ratios (around 75 per cent) than US sub-prime loans (around 95 per cent) and US "teaser" (low introductory) interest rates are not a feature of Australian nonconforming loans.²²

Non-conforming lending involves borrowers (typically with poor credit or payment histories) who would be denied loans by mainstream lenders. It is a specialist industry sector pursued by unregulated lenders.²³ Around 60 per cent of the value of non-conforming loans involves refinancing or consolidation of other debts.²⁴ A small segment within the non-conforming sector is said to engage in predatory lending.²⁵

Proceedings in the Possession List

The vast majority of matters in the Possession List (over 95 per cent) are undefended.

Lenders who obtain judgment for possession of land do not always choose to obtain a writ of possession or, if they do, to execute it. Frequently, negotiations take place between the parties which lead to refinancing of the loan (to discharge the existing mortgage) or sale of the property with the lender and borrower co-operating for this purpose to maximise the sale price.

Unless an arrangement is reached between the lender and the borrower, however, the lender may proceed to obtain default judgment and a writ of possession may issue, by leave of the court. A writ of possession, if obtained, will be executed by the Sheriff and the lender will take possession of the property.

A small proportion of matters in the Possession List are defended. Defences (and grounds for refusal of relief) which are relied upon include relief under the *Contracts Review Act* 1980,²⁶ claims of unconscionable conduct or misleading or deceptive conduct under the *Trade Practices Act* 1974 (Cth) and/or *Fair Trading Act* 1987 on the part of the lender, mortgage brokers and others,²⁷ relief under the Consumer Credit Code (NSW),²⁸ failure to comply with requirements of the *Farm Debt Mediation Act* 1994²⁹ and, sometimes, claims of fraudulent conduct, including forgery.³⁰

High interest rates are a common feature of mortgages with non-conforming lenders. The existence of a high interest rate may not, of itself, render the contract unjust.³¹ It has been observed, in this context, that bad bargains are not necessarily unconscionable bargains or illustrative of unconscionable conduct.³² Default interest provisions have been held to be unenforceable as a penalty.³³

A significant number of defended matters in the Possession List spring from the non-conforming loan market. Many defended matters involve complex litigation in which guarantors, mortgage brokers, solicitors, accountants and others are joined as parties.

Stay applications

A substantial part of the court's work in Possession List matters involves applications by defendants for a stay of execution of a writ of possession. Commonly, this is the first point at which the defendant will become actively involved in the litigation.

A broad range of factors may be taken into account in the exercise of discretion to grant a stay of execution of a writ of possession.³⁴ The most common circumstances in which a stay is sought by a defendant include:

- a. where the defendant is attempting to refinance and to discharge the mortgage³⁵
- b. where the defendant is attempting to sell the property³⁶
- c. where the defendant asserts that an arguable defence to the proceedings exists and wishes to be let in to defend the proceedings³⁷
- d. where a delay in execution of the writ is sought on hardship grounds.³⁸

A practical difficulty may confront a defendant wishing to sell the property in a falling market. The sale may not discharge the outstanding level of indebtedness on the property, with the defendant left to satisfy the outstanding sum personally.³⁹

An avenue being used increasingly by mortgagors, in an attempt to extricate themselves from mortgage difficulties, is application for early release of superannuation benefits. APRA administers legislation that permits the early release of superannuation under specified "*compassionate grounds*". APRA must be satisfied that an application meets the criteria for early release of superannuation, but the final decision lies with the trustee of the relevant superannuation fund.⁴⁰ Superannuation benefits may be released to enable a person to make a payment to prevent foreclosure of a mortgage on the person's principal place of residence or to prevent exercise by the mortgagee of an express or statutory power of sale over that residence.⁴¹ In 2006, APRA approved 13,871 applications for the release of \$135 million, compared with 10,459 applications for the release of \$77 million in 2005.⁴²

Defendants who seek to refinance for the purpose of discharging an existing mortgage may be tempted to borrow from the extreme end of the non-conforming market. Perceived short-term benefits of this step may be outweighed by the long-term disadvantages. The Consumer Credit Legal Centre (NSW) advises borrowers in financial difficulty against refinancing through a "*lender of last resort*".⁴³

If the defendant fails to obtain alternative finance and the plaintiff proceeds to take possession of the property and exercise power of sale, then additional enforcement and legal costs generated by a series of stay applications and deferred appointments to execute the writ of possession usually will be passed on to the defendant.⁴⁴

All of this emphasises the need for advice at an early point in the proceedings to allow a sensible assessment by a defendant of the available options.

Court processes

In 2006, a Possession List Users Group was formed to assist consultation between legal representatives appearing in Possession List matters, including plaintiffs 'solicitors and representatives of the Legal Aid Commission of New South Wales and the Consumer Credit Legal Centre (NSW), and officers of the court. Through the Users Group, a number of proposals have been made to improve court processes to assist parties in this class of proceedings.

A simplified short-form Statement of Claim for uncomplicated possession claims has been introduced,⁴⁵ with clear prompts to the borrower concerning the desirability of obtaining early legal advice (including free advice through LawAccess NSW),⁴⁶ the availability of interpreter services and possible consequences of the litigation.

Clearer procedures have been developed for the hearing and determination of stay applications.

Endnotes

- * Possession List Judge, Common Law Division, Supreme Court of New South Wales.
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 11. *op cit* n 9, para 5.15-5.19.
 12. *"Code of Banking Practice"* at <http://www.bankers.asn.au/Default.aspx?ArticleID=446>, accessed 10/12/2007.
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 14. *op cit* n 9, para 5.27.
 15. *op cit* n 9, para 2.35.
 16. *op cit* n 9, para 2.34.
 17. *op cit* n 9, para 5.28.

18. *Volpes v Permanent Custodians Ltd* [2005] NSWSC 111 at [2]; *Volpes v Permanent Custodians Ltd* [2005] NSWSC 827 at [4]; *Permanent Mortgages Pty Ltd v Cook* [2006] NSWSC 1104 at [37]; *Manufacturers House Pty Ltd v Ashington No 147 Pty Ltd* [2005] NSWSC 767 at [51].
19. *Liberty Financial Pty Ltd v Scott* (No 4) (2005) 11 VR 629 at [8], [27].
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24. op cit n 9, para 2.37.
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28. *Permanent Mortgages Pty Ltd v Cook* [2006] NSWSC 1104 at [45]ff; *Cook v Permanent Mortgages Pty Ltd* [2007] NSWCA 219; *Permanent Custodians Ltd v Upston* [2007] NSWSC 223; *Benjamin v Ashikian* [2007] NSWSC 735; *Hamafam Pty Ltd v Saadullah* [2007] NSWSC 818 at [15]-[32].
29. *Craigie v Champion Mortgage Services Pty Ltd* [2007] NSWCA 15.
30. *Chen v Song* [2005] NSWSC 19; *Chandra v Perpetual Trustees Victoria Ltd* [2007] NSWSC 694; *Sabah Yazgi v Permanent Custodians Ltd* [2007] NSWCA 240.
31. *King Mortgages v Satchithanatham* [2006] op cit n 26, at [146].
32. *Accom Finance Pty Ltd v Mars Pty Ltd* [2007] NSWSC 726 at [54]; *Kowalczyk v Accom Finance Pty Ltd* [2007] NSWCA 225 (stay pending appeal).
33. *Guardian Mortgages Pty Ltd v Miller* [2004] NSWSC 1236 at [110]; *Capital Securitisation Ltd v Jammal* [2007] NSWSC 1073 at [97]-[99]; cf *King Investment Solutions v Hussain* [2005] NSWSC 1076 at [136]-[138].
34. *GE Personal Finance Pty Ltd v Smith* [2006] NSWConv R 156-164; [2006] NSWSC 889 at [9]-[30].
35. ibid at [16]-[19]; *National Australia Bank Ltd v Convy* [2007] NSWSC 1039.
36. *GE Personal Finance Pty Ltd v Smith* op cit n 34, at [20].
37. ibid at [15]; *Balanced Securities Ltd v Oberlechner* [2007] NSWSC 80 at [19]-[20]; *Hamafam Pty Ltd v Saadullah* [2007] NSWSC 818 at [6]-[7].
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