SUPREME COURT OF QUEENSLAND

CITATION:	*Scholz & Anor v Ace Finance Aust Pty Ltd* [2018] QCA 234
PARTIES:	**JOHN MICHAEL SCHOLZ** **(first appellant)** **JANICE MERLE SCHOLZ** **(second appellant)** **v** **ACE FINANCE AUST PTY LTD** **ACN 101 588 747** (respondent)
FILE NO/S:	Appeal No 3361 of 2018 SC No 9662 of 2016
DIVISION:	Court of Appeal
PROCEEDING:	General Civil Appeal
ORIGINATING COURT:	Supreme Court at Brisbane – [2018] QSC 27
DELIVERED ON:	25 September 2018
DELIVERED AT:	Brisbane
HEARING DATE:	19 July 2018
JUDGES:	Sofronoff P and Gotterson JA and Boddice J
ORDERS:	**Appeal dismissed with costs.**
CATCHWORDS:	CONTRACTS – GENERAL CONTRACTUAL PRINCIPLES – CONSTRUCTION AND INTERPRETATION – IMPLIED TERMS – where the appellants sold development land and took a second mortgage to secure payment of the purchase price – where the respondent lent money to the purchaser and took a first mortgage to secure repayment of the money – where the respondent's rights as first mortgagee were governed by a Deed of Priority – where the purchaser of the land is alleged by the respondent to have defaulted – where the respondent took possession of the land, developed it and sold it, keeping all of the proceeds of sale – where the appellants are attempting to recover a sum of money from the respondent that they allege exceeds the respondent's entitlement under the Deed of Priority – where the appellants pleaded, by way of Reply, that the respondent's entitlement was limited by an implied term in the Deed of Priority to interest, fees, charges, costs and expenses that were 'reasonable' and were 'reasonably incurred' – where the agreement between the respondent and purchaser of the land provided a specified interest rate – where the interest, fees, charges, costs and expenses referred to under the Deed of Priority were

those as set out in the agreement between the respondent and purchaser of the land – where an implied term that the interest, fees, charges, costs and expenses incurred by the respondent be reasonable would contradict the express terms of the priority deed – where the respondent was successful in its application to have these pleadings relating to an implied term of reasonableness struck out – whether the learned primary judge was right to strike out the paragraphs of the appellants' reply as unsustainable

Acron Pacific Ltd v Offshore Oil NL (1985) 157 CLR 514; [1985] HCA 63, cited
BP Refinery (Westernport) Pty Ltd v Shire of Hastings (1977) 180 CLR 266; [1977] UKPCHCA 1, discussed
Codelfa Construction Pty Ltd v State Rail Authority (NSW) (1982) 149 CLR 337; [1982] HCA 24, discussed
Finchbourne Ltd v Rodrigues [1976] 3 All ER 581, distinguished
Lister v Romford Ice and Cold Storage Co Ltd [1957] AC 555; [1956] UKHL 6, cited
The Moorcock (1889) 14 PD 64, cited
Victorian Producers Co-operative Co Ltd v Edwards (1993) 62 SASR 415; [1993] SASC 4145, distinguished

COUNSEL: A J Greinke for the appellants
G J P Handran, with I Klevansky, for the respondent

SOLICITORS: TdK Law for the appellants
Hickey Lawyers for the respondent

[1] **SOFRONOFF P:** This appeal concerns a dispute about pleadings.

[2] According to these pleadings, the appellants sold development land to Odna Pty Ltd ('Odna') and took a second mortgage to secure payment of the purchase price. The respondent is a moneylender. It lent money to Odna to develop the same land and took a first mortgage to secure repayment of that money. The respondent's rights as first mortgagee have been limited by a "Deed of Priority" to which the appellants and the respondent are parties, the terms of which have to be considered in due course.

[3] Odna is alleged by the respondent to have defaulted in its obligations to the respondent, who then took possession of the land, finished developing it and sold it. It kept all the proceeds of sale.

[4] The appellants are plaintiffs who are seeking to recover from the respondent-defendant a sum of money that they allege has been withheld from them in excess of the respondent's due entitlement under the Deed of Priority. In the alternative they seek an account. It is convenient to refer to the parties to this appeal as plaintiffs and defendant.

[5] After pleading the contracts of sale and loan between the parties, and the mortgages, the plaintiffs pleaded the effect of clause 3 of the Deed of Priority which established the priority ranking of the two securities. However, as the plaintiffs have admitted in their Reply, that plea was inaccurate and, in fact, clause 3 (and clause 4 which is

also relevant) actually provided as follows, as alleged in paragraph 4(d) of the Defence:

> "(d) The terms of the Deed of Priority relevantly included:
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> (i) (by clause 3 and the Schedule), the Defendant has first priority for money and liabilities secured by the First Mortgage up to the amount of $3,500,000.00 plus interest and all fees, charges costs and expenses whether capitalised or not payable under the Finance & Development Agreement;
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> (ii) (by clause 3 and the Schedule), the Plaintiffs have second priority for money and liabilities secured by the Second Mortgage up to the amount of $2,299,999.00;
>
> (iii) (by clause 3 and the Schedule), the Defendant has third priority for the balance of money and liabilities secured by the First Mortgage;
>
> (iv) (by clause 4), before being applied in accordance with the order of priority provided for in clause 3, the proceeds received from the enforcement of the First Mortgage must be applied in payment of all reasonable costs and expenses incurred by the Defendant in exercise of any power in relation to the Security."

[6] The ultimate plea, upon which the plaintiffs' case rests, is in paragraph 21 of the Statement of Claim:

> "The defendant has received from the proceeds of sale of the Property at least $2,300,000 over and above its first priority entitlement of $3,500,000, interest, fees, charges, costs and expenses, particulars of which cannot be provided until completion of interlocutory steps."

[7] The basis for that allegation does not appear in the Statement of Claim. Instead, although it forms the basis for the plaintiffs' entitlement to the relief claimed, it emerged only in the Reply in the form of paragraphs 7A, 7B, 7C and 7D which are as follows:

> "7A On the proper construction of the Priority Deed, or by way of a term implied as a matter of law, the defendant was only entitled to priority for interest, fees, charges, costs and expenses to the extent that such charges were reasonable, and were reasonably incurred by the defendant.
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> 7B The defendant purported to accrue interest at a rate of 36% per annum, compounded monthly, which interest charge:
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> 7B.1 was unreasonable at this rate, relative to the rate of borrowing available to the defendant, and akin to a penalty;
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> 7B.2 was unreasonably incurred, since Odna was not in default, such that the "Higher Rate" in the Finance & Development Agreement did not apply; and

7B.3 was unreasonably incurred, because the defendant made an election to enter in possession as mortgagee and thereafter continue the development itself, rather than to sell the Property.

7C A reasonable rate of interest would be 12% or alternatively 18% per annum.

7D The defendant purported to charge the following fees, which were unreasonable in amount, and/or were unreasonably incurred, because the defendant made an election to enter in possession as mortgagee and thereafter continue the development itself, rather than to sell the Property:

7D.1 a purported "Establishment Fee" of $96,250.00;

7D.2 a purported "Administration Fee" of 0.25% per month plus GST;

7D.3 a purported "Risk Management Fee" of $627,000.00 plus GST, and

7C.4 a purported "Finance Control Fee" of $125,000 per annum."

[8] The defendant applied to Davis J for orders that, if made, would effectively have determined finally whether or not those pleas could be maintained. His Honour declined to embark upon that course for discretionary reasons that are not challenged by the defendant. Davis J concluded his reasons by saying that it was "obvious that the Amended Reply will need to be further amended, so a more appropriate course may be to strike out paragraphs 7A-7D of the reply, give leave to the plaintiff to amend the amended reply consistently with these reasons, and make directions to advance the case." His Honour heard submissions and, relevantly, ordered that those paragraphs be struck out and that the plaintiffs deliver a further amended reply.

[9] The plaintiffs now appeal from the order striking out paragraphs 7A to 7D of the Amended Reply. The grounds of appeal should be set out:

(a) The primary judge erred in finding that terms to the effect that interest, fees and charges be reasonable or be reasonably incurred were incapable of being implied into the Priority Deed.

(b) The primary judge failed to apply the principles in *BP Refinery (Westernport) Pty Ltd v Shire of Hastings* (1977) 180 CLR 266 and *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234.

(c) The primary judge erred in finding at [68] that there was no room for the implication of such terms in clause 3.1(a) of the Priority Deed.

(d) The primary judge ought to have found that it was arguable that such terms were implied into the Priority Deed, as a matter for the trial judge.

(e) Accordingly, the primary judge erred in striking out paragraphs 7A, 7B, 7C and 7D of the amended reply.

[10] It is important to notice that the disputed paragraphs allege an interpretation of the Priority Deed. The interpretation of the Finance and Development Agreement and mortgage are not in issue.

[11] Clause 3 is the relevant clause in the Priority Deed. The plaintiffs would seek to limit the scope of the words "plus interest and all fees, charges, costs and expenses … payable under the Finance and Development Agreement" by the operation of an implied term that would limit those items to charges that "were reasonable and were reasonably incurred".

[12] The pleading in this respect suffers from several difficulties. First, paragraph 7A alleges that the limitation arises "[o]n the proper construction of the Priority Deed". No argument was directed to his Honour or to this Court to sustain that allegation. It is, in truth, unsustainable for the words of the Deed to provide that the relevant charges are those "payable … under the Finance and Development Agreement", whatever they may be. The Deed could not be clearer that the amount must be calculated according to the terms of that Agreement.

[13] Second, paragraph 7A alleges "a term implied as a matter of law".[1] This appears to be a mistake because the plaintiffs' submissions, both below and on appeal, sought to sustain the plea on the basis that the term was one implied in fact.

[14] Third, if what is really sought to be alleged is a term implied in fact, then no facts have been pleaded to support the conclusion pleaded in paragraph 7A.

[15] Fourth, as his Honour noticed, the expression "akin to a penalty" is vague and uninformative. Is it alleged that the clause imposed a penalty and was, for that reason, void? Or are those words mere pejorative surplusage?

[16] There are other problems that would, themselves, have justified striking out those paragraphs, but they were not argued and it is not necessary to deal with them.[2]

[17] The vital point, which his Honour identified, was that it was simply impossible, consistently with the authorities, to imply a term as a matter of fact that conflicted with the express terms of the Priority Deed which gave priority to the defendant for the "interest etc. ..payable … under the Finance and Development Deed". It merely requires a calculation of the amount so payable pursuant to the terms of the Agreement. An allegation that the defendant was only entitled to priority by way of a reasonable sum would conflict with the express words of the clause.

[18] The plaintiffs cited *The Moorcock*[3] and *BP Refinery (Westernport) Pty Ltd v Commissioner for Railways (NSW)*[4] but these cases support the defendant. The former case was considered by the Privy Council in the latter case, which stands as authority for propositions that are identical to those declared by the High Court in

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1 See eg *Lister v Romford Ice and Cold Storage Co Ltd* [1957] AC 555 at 572-3.

2 eg: if, as paragraph 7B.2 alleges, Odna was not in default, then there is no question of implied terms to be considered. The application of the higher rate was not authorized by the contract. Paragraph 7B.3 does not disclose why entry into possession and subsequent development was unreasonable.

3 (1889) 14 PD 64.

4 (1977) 180 CLR 266.

Codelfa Construction Pty Ltd v State Rail Authority (NSW)[5] and, indeed, Mason J referred expressly to *BP Refinery* in his reasons.[6] All those cases require that, for a term to be implied as a matter of fact, the term must, *inter alia,* be necessary to give business efficacy to the contract "so that no term will be implied if the contract is effective without it" and the implied term must "not contradict any express term of the contract".[7] The plaintiffs' proposed term fails both requirements.

[19] Nor do cases such as *Victorian Producers Co-operative Co Ltd v Edwards*[8] and *Finchbourne Ltd v Rodrigues*[9] support the pleading. Those were cases in which the relevant quantum was not defined as it is in this case. In such cases it is possible, and it may be necessary, to imply a term that the charges must be reasonable. They say nothing about the contract in this appeal.

[20] As Davis J also observed in paragraph [68] of his reasons, whether or not a limitation, based upon reasonableness of the rate of interest and of other charges, might be implied into the Finance and Development Agreement, as distinct from the Deed, is an entirely separate question and one that the plaintiffs have so far not addressed. So too is the question whether the interest rate of 36 per cent is a penalty one that has not been raised in connection with the Agreement, although such a plea would have to deal with the decision of the High Court in *Acron Pacific Ltd v Offshore Oil NL*[10] and other such cases. It is open to them to address those questions and, if so advised, to raise a plea in relation to them.

[21] However, in my respectful opinion, Davis J was right to strike out these paragraphs as unsustainable.

[22] For these reasons I would dismiss the appeal with costs.

[23] **GOTTERSON JA:** I agree with the orders proposed by Sofronoff P and with the reasons given by his Honour.

[24] **BODDICE J:** I agree with Sofronoff P.

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5 (1982) 149 CLR 337.
6 *supra*, at 347, referring to the passage that now appears in 180 CLR at 283.
7 *ibid*.
8 (1993) 62 SASR 415.
9 [1976] 3 All ER 581.
10 (1985) 157 CLR 514