



FINANCIERS DEPOSITING FUNDS DIRECTLY WITH SUPPLIERS BEWARE!

BY ASHLEY GOOBANKO

Two recent court cases have highlighted the need for financiers, that are in the business of financing the purchase of chattels, to protect themselves from the risks associated with directly depositing funds into suppliers' accounts (as opposed to borrowers' accounts).

Judgments handed down this year from the Queensland District Court and the New South Wales Supreme Court are a warning to financiers that these types of deposits may be unrecoverable if they do not take precautions under certain circumstances.

The cases tell a story of fraudulent invoices and nonexistent equipment causing financiers to make direct deposits with suppliers. They also reveal how the Courts can conclude that these deposits are unrecoverable, primarily where the supplier has no notice of the source or the purpose of the funds.

QLD CASE: FINANCIER LOSES \$66,762

In the Queensland District Court case the borrower, Platinum Store Pty Ltd ("Platinum Store"), applied to BOQ Equipment Finance Ltd ("BOQEF") for a loan to purchase two motor vehicles. Platinum Store provided the financier with two invoices for the purchase. After conducting due diligence enquiries and relying on the details in the invoice, BOQEF agreed to enter into two chattel mortgage agreements and deposited \$118,008.95 directly in to the account of the supplier of the motor vehicles, Visposin Pty Ltd ("Visposin").

Platinum Store made several mortgage repayments to BOQEF but eventually defaulted. BOQEF subsequently discovered that the invoices were fraudulent and that the motor vehicles did not exist. It commenced court proceedings against Visposin and its director, Paul Norris, to recover the funds. It claimed that Visposin and Norris were unjustly enriched in the sum of \$118,008.95 and that the deposit made to Visposin was a mistake. The financier also claimed that the monies were deemed to be held on trust by Visposin for the purpose of purchasing the two motor vehicles, a purpose which ultimately failed.

The Court accepted that the funds had been deposited by mistake and that BOQEF had established an entitlement to restitution. However, the Court also accepted that Visposin had a defence that protected it from returning a majority of the deposit.

Visposin and Norris claimed that they were led to believe that BOQEF's deposit was a business loan for Norris's son. The son, it was claimed, had convinced Norris that he did not have his own bank account and he needed Visposin's account to receive the deposit. Norris gave the majority of the funds deposited by BOQEF to his son.

The Court found that Visposin was not given notice of any mistake or irregularity regarding the deposit. It also found that Visposin, as agent for Norris's son, acted in good faith, having no notice of the irregularity. These findings helped the Court to conclude that a trust was not formed and Visposin was entitled to the defence of change of position. This protected Visposin from returning to BOQEF the portion of the deposit that was given to Norris's son.

BOQEF lost \$66,762 from a deposit of \$118,008 and the Court ordered Visposin to return what remained of the original deposit.

¹ BOQ Equipment Finance Ltd v Visposin Pty Ltd & Anor [2011] QDC 266

² Australian Financial Services and Leasing Pty Ltd v Hills Industry Ltd [2011] NSWSC 267

continued overleaf

BRISBANE / SYDNEY / MELBOURNE / SURFERS PARADISE / MOOLOOLABA

In This Issue

FINANCIERS DEPOSITING FUNDS DIRECTLY WITH SUPPLIERS BEWARE!

Page 1

PPS REGISTER: GOVERNMENT INDICATES JANUARY 30 COMMENCEMENT IS STILL POSSIBLE

Page 2

REVERSE MORTGAGES – FURTHER ENHANCEMENTS

Page 3

NEW SOUTH WALES' NEW IDENTIFICATION REQUIREMENTS FOR MORTGAGEES

Page 4

Level 2, 200 Adelaide Street Brisbane Qld 4000
Phone 07 3228 5333 Facsimile 07 3221 8500

Level 9, 68 Pitt Street Sydney NSW 2000
Phone 02 9239 9400 Facsimile 02 9239 9499

Level 2, 535 Bourke Street Melbourne VIC 3000
Phone 03 8622 2700 Facsimile 03 8622 2722

P O Box 2794, Nerang BC Qld 4211
Phone 07 3228 5386 Facsimile 07 5574 7722

24 Walan Street Mooloolaba Qld 4557
Phone 07 5457 9800 Facsimile 07 5478 2696

E-mail us at macgill@macgillivrays.com.au
Phone us on 1300 369 581



FINANCIERS DEPOSITING FUNDS DIRECTLY WITH SUPPLIERS BEWARE!

NSW CASE: FINANCIER LOSES \$198,000

The NSW decision involved a set of similar circumstances. In this case two companies (TCP and TCP2) approached Australian Financial Services for a loan to purchase some equipment for their business. The companies gave Australian Financial Services invoices that were purported to be from three separate suppliers. Australian Financial Services agreed to be the financier and, relying on the invoices, made direct deposits with the three suppliers.

Australian Financial Services eventually discovered that the invoices were fraudulent and the equipment did not exist. It contacted the suppliers requesting the deposits to be returned. However, the suppliers refused to return the deposits. Australian Financial Services commenced legal action, claiming the suppliers were unjustly enriched.

The suppliers, like Visposin in the Queensland case, claimed a defence of change of position. The Court found that one of the suppliers, Bosch Security Systems, was entitled to this defence.

Bosch claimed that when it received the funds from Australian Financial Services, it was not aware of the financier's reason for the deposit. The TCP companies, at that time, owed a debt to Bosch and they were ordered, by way of a court judgment, to repay it. Bosch claimed it had mistakenly accepted the deposit as payment for this debt and, in doing so, relinquished its legal rights to recover the debt.

Australian Financial Services argued that at the time the funds were deposited, a constructive trust was created and the funds were solely to be used for the purpose of purchasing the equipment specified in the invoices. As Bosch failed to use the funds in accordance with the purpose, Australian Financial Services argued that Bosch was in breach of trust. It claimed that Bosch did or ought to have known the purpose of the deposit. Reasons for this included Australian Financial Services:

1. calling Bosch on the same day the payment was made;
2. informing Bosch of the deposit; and
3. quoting Bosch the fraudulent invoice numbers.

However, the Court held that Bosch did not have the requisite knowledge to know the true intention of the deposit and concluded that a trust was not created. The Court determined that Bosch's defence of a change of position protected it from returning the deposit to the financier. The deposit was unrecoverable and Australian Financial Services lost \$198,000.

RECOMMENDATIONS

These cases highlight the need for financiers to take added precautions when entering into a chattel mortgage or similar agreement that involves the direct deposit of funds into a supplier's account. If necessary, lending protocols relating to these types of deposits should be revised to ensure that adequate notice is provided to the prospective supplier of the purpose of the funds. If such precautions are taken, financiers that find themselves in similar circumstances to those outlined in the above cases may limit a supplier's ability to claim a defence of change of position and possibly increase the chances of exposing fraudulent activity prior to settlement.

MacGillivrays is experienced with assisting financiers and can recommend prudent precautions that can assist in addressing these types of risks.

MacGillivrays have written more on this topic in "Chattel Financiers Careful Who You Pay" published in Banking in Brief issue 26.



BY ASHLEY GOOBANKO

PPS REGISTER:

GOVERNMENT INDICATES JANUARY 30 COMMENCEMENT IS STILL POSSIBLE



The Federal Government has recently reported to a Senate Committee that a commencement date of 30 January 2012 for the personal property security reforms is still anticipated.¹ However, a recent Federal Bill (Personal Property Securities Amendment (Registration Commencement) Bill 2011) if made law, will allow the Attorney-General to determine a new start date for the PPS register beyond February 2012. The Bill has passed the House of Representatives and at the time of writing a Parliamentary Committee has recommended it should also be passed by the Senate.

The Government faces a complex task to create the registry. It involves the migration of data from a number of different databases nationwide. It is possible that issues could arise that could delay the planned commencement. Queensland legislation has also been made recently (Personal Property Securities (Ancillary Provisions) (Postponement) Regulation 2011) due to delays in the register's start date.

Despite this the Government appears confident that the registry will be available as planned but, by proposing laws that allow for a commencement date later than February 2012 suggests that nothing should be taken for granted.

MacGillivrays will be conducting a client seminar to assist with understanding the Act and the operation of the new register.

To register your interest in the seminar, please email marketing@macgillivrays.com.au

¹Legal and Constitutional Affairs Legislation Committee, Senate, *Personal Property Securities Amendment (Registration Commencement) Bill 2011 [provisions]* (2011)



BY GREG YOUNG

REVERSE MORTGAGES – FURTHER ENHANCEMENTS

THE GOVERNMENT FORESHADOWED THAT IN PHASE 2 OF THE CONSUMER CREDIT LAW REFORMS ONE OF THE FIRST MATTERS IT WOULD LOOK AT WOULD BE ENHANCEMENT TO THE REGULATION OF REVERSE MORTGAGES.

By December the Senate Economics Committee report to the Federal Parliament on the Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011, should be made available. This Bill proposes to make changes to the National Consumer Credit Code that will affect businesses that provide a range of credit products, including reverse mortgages. Minister Shorten, when introducing the Bill to Parliament, expressed the government's intention to protect senior Australians that access the equity in their homes through a reverse mortgage. The Bill, if passed, will regulate the market by introducing a range of laws that include disclosure requirements that lenders and brokers must abide by. The draft laws also provide remedies for consumers that experience loss or damage due to credit providers breaching their disclosure requirements. The Bill, if passed, will implement many of the changes previously proposed or discussed by Government. The Bill;

- Defines what a reverse mortgage is.
- Introduces specific responsible lending conduct obligations in relation to reverse mortgages.
- Requires use of an ASIC approved website to generate projections and other information.
- Introduces a reverse mortgage information statement and prescribes the circumstances in which it must be used and where it must be displayed.
- Protects non-owner occupants of properties which are subject to a reverse mortgage.

- Introduces specific disclosure requirements if the reverse mortgage limits the rights of non-owner occupants.
- Requires lenders to record non owner occupants of reverse mortgaged properties.
- Prohibits certain events from being regarded as events of default under a reverse mortgage.
- Proposes that the regulations may require independent legal advice to be given before entering into a reverse mortgage.
- Imposes additional requirements on lenders before seeking to enforce a reverse mortgage.
- Prohibits negative equity.
- Enables borrowers to end a reverse mortgage if the amount owing exceeds the market value.
- Inserts provisions for determining market value in accordance with regulations (if any) and circumstances in which a shortfall on sale may be pursued (such as fraud or misrepresentation by the borrower).

The Bill still has to pass both Houses of Parliament so there are opportunities for amendments to be made, but we suggest the framework for these reforms is now set. As with other changes being made to the National Credit Code, the contents of the regulations will be of paramount importance.

We will keep you informed as matters develop.



BY RICHARD WILLIAMS



NEW SOUTH WALES' NEW IDENTIFICATION REQUIREMENTS FOR MORTGAGEES

The New South Wales' *Real Property Amendment Regulation 2011* is now law. The regulation details the identification steps the Government requires mortgagees to take to confirm the identity of mortgagors. In our bulletins, April 2010 and December 2010, we commented on the proposals relating to this law.

The significant changes between these regulations and the earlier proposals are:

- the provision for lenders to rely on certified copies of identification documents;
- the recognition that a lender need not personally interview the mortgagee; and
- the provision of an alternative identification route, being compliance with the Anti-Money Laundering and Counter Terrorism Financing Rules (AML/CTF Rules).

THE AML/CTF RULES

The provision deems a lender to have satisfied the identification requirements if the lender

"has complied with the Anti-Money Laundering and Counter-Terrorism Financing Rules under the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 of the Commonwealth in relation to the mortgage." [my emphasis]

"in relation to the mortgage" may have more significance than it first appears. The AML/CTF rules have no provisions in them relating to mortgages. AML/CTF does not deal with identification of mortgagors, it deals with the identification of parties to financial transactions. It would be unconstitutional for the Federal Government to pass AML/CTF Rules relating to identification of mortgagors of land in a State.

Most of the time a lender will automatically identify the person signing a mortgage under their AML/CTF rules because the person is the borrower or a director of the borrower (e.g. a company loan). The provision above applies to this class of person so a lender's normal AML/CTF procedures should satisfy the requirements.

GUARANTORS AND ATTORNEYS

However there are a small number of people who sign mortgages and who a lender may not be required by AML/CTF to identify. These are:

- guarantors who the lender has no obligation to identify under AML/CTF because there is no relevant relationship; and
- some attorneys under a power of attorney in a similar position.

We sought clarification from the draftsman of the new regulation and were advised that the draftsman had not contemplated mainstream lenders taking mortgages from guarantors. This means that it is uncertain whether the provision will apply in circumstances where the guarantor has no relevant relationship with the lender.

Until the law is clarified in relation to these people we recommend that lenders should use the identification procedures in the regulations to identify them.

CERTIFIED DOCUMENTS

The other significant change from the draft versions of the regulations is the provision allowing a lender to rely on certified copies of documents.

This change also has its limitations. It allows a lender to rely upon *"a copy of a document ... certified as a true copy of the original only by a person authorised to take and receive statutory declarations under section 21 of the Oaths Act 1900."* [my emphasis] This means the following people.

"Registrar-General, a Deputy Registrar-General or any justice of the peace, notary public, commissioner of the court for taking affidavits, Australian legal practitioner ..., or other person by law authorised to administer an oath,"

Please note, with the exception of an Australian Legal Practitioner, notary public or other person authorised by law to administer an oath, the people mentioned in the section are appointed under NSW law. Their counterparts outside NSW have no power to certify these documents unless the laws of the relevant State give that power.

For example, Bank Managers, Pharmacists, and Registered Conveyancers can not certify documents for the purpose of these provisions. In Queensland only Judges and Australian Legal Practitioners (Solicitors, Barristers and notaries public) can certify these documents for the purpose of the NSW regulations.

WHAT DO YOU NEED TO DO NOW?

Unless you intend to personally identify each borrower and guarantor, using the method described in our December 2010 bulletin, Lenders will need to rely on either their AML/CTF identification procedures, or certified documentary evidence (usually being a copy of a driver's licence or passport).

AML/CTF

If you chose the AML/CTF route, you should revise your AML/CTF procedures for identifying parties to your transaction documents so that they are consistent with the requirements of the AML/CTF Rules, particularly with regard to Rule 4.

CERTIFIED COPIES OF DOCUMENTS

If you are going to rely upon certified documentary evidence for identification of mortgagors, implement procedures to make sure that the documents are certified by the appropriate people. The KISS approach (keep it simple ...) is to make sure that certified documents are only certified by Australian Legal Practitioners.

DOCUMENT RETENTION

You will also need to implement procedures to ensure that you keep evidence of the relevant identification and all documents relating to it for at least seven (7) years after the mortgage is registered. If registration is delayed for any reason, this could be much longer than 7 years after you close your file. It may be prudent to file the relevant paperwork with the securities for the loan to ensure that this requirement is observed.

We are happy to assist you with your compliance requirements. Please contact our Banking Services Team on 1300 369 581 or gordonp@macgillivrays.com.au

PLEASE NOTE: This newsletter is not legal advice and our comments are of a general nature only. This document is not to be relied on as substitution for proper detailed advice. If you would like to be removed from, or added to our mailing or emailing list, contact Kandice Buckle on (07) 3228 5333 or macgill@macgillivrays.com.au



BY GORDON PERKINS