

Position Statement Issue 3

30 June 2011

Stay on Execution Default Judgment Orders

This Position Statement describes how we deal with complaints where a borrower seeks a stay of the lender's execution of default judgment orders.

While we cannot interfere with or overturn default judgment orders, we have identified instances where the Credit Ombudsman Service Limited (COSL) may determine that execution of the orders may be stayed.

In preparing this Position Statement, we have considered relevant law, applicable industry codes of practice, good industry practice, and fairness.

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1. Introduction

- 1.1 If a borrower defaults on his or her loan obligations, the lender is entitled to recover the debt by enforcing the security supporting the loan. Where the security is over real property, the lender may seek court orders granting possession of the security property.
- 1.2 If the borrower does not take an essential step within the time required by court rules (for example, failing to file a defence), the lender may obtain default judgment for possession of the security property.
- 1.3 Default judgments may also be obtained in relation to loans that are unsecured, and loans secured by property other than real property, but these are less common.
- 1.4 COSL's jurisdiction in this area is not limited to default judgments that relate to loans secured by real property, and COSL will apply the same general principles when considering a request for a stay of a default judgment regardless of the type of loan involved, or the nature of any security taken for the loan.
- 1.5 However, this Position Statement does focus particularly on issues associated with stays of default judgments on loans which are secured by residential properties because:
 - (a) we expect that the majority of the work that COSL will do in this area, at least in the foreseeable future, will relate to loans of this type;
 - (b) the security is typically the borrower's family home and, not surprisingly, borrowers tend to be willing to go to significantly greater lengths to avoid the sale of their homes, than they are to avoid enforcement of security over other types of property given as security. It is appropriate that we recognise this by giving borrowers in this position as much guidance as reasonably possible so they not only have realistic expectations about the role that COSL can play, but are also in a position to make the most effective use of the services we are able to offer;
 - (c) the issues which arise in connection with the enforcement of security over residential properties tend to be the more complex ones, and we hope that guidance of any kind in relation to these complex issues will be of particular value to borrowers.
- 1.6 Borrowers who want a stay of execution of a default judgment in relation to other types of loans or loans with other kinds of security can expect that COSL will apply the same general principles that we apply in relation to loans secured by residential property. This is to ensure that outcomes are achieved which recognise the practical differences between different kinds of loan products and different types of security, but which nevertheless reflect the consistent application of underlying principles. We may issue additional guidance in future, including in relation to loans secured by property other than residential property or other types of loans, if it becomes apparent that there is a need for it.
- 1.7 A borrower may have reasons for seeking a delay (or 'stay') of execution of the default judgment – for example, because they consider it is in the interests of all parties that they sell the security property themselves, or they wish to challenge the validity of the judgment.
- 1.8 Courts have broad powers to vary or set aside default judgments or to grant stays of execution. The courts will exercise their powers appropriately, and in the interests of justice.
- 1.9 Although the court has wide powers to grant stays of default judgments and can do so whenever it considers appropriate on a borrower's application, there are certain circumstances where the courts have been more willing to grant a stay of a default judgment. For example, where the borrower:
 - (a) can demonstrate that it is likely they can sell the security property themselves within a reasonable time;

- (b) can establish that they expect, in the very near future, to be able to refinance the loan which is the subject of the default judgment;
- (c) can show that they are suffering from personal (as distinct from financial) hardship¹ and need a reasonable time to organise their affairs; or
- (d) has reasonable grounds to apply to have the default judgment set aside altogether, for example:
 - (i) the orders made in the judgment appear to be irregular², or
 - (ii) the judgment was obtained in contravention of a legal requirement³, or
 - (iii) there is a substantive defence⁴ available to the lender's claim, and the borrower can show that they will apply to set the default judgment aside, but needs more time to prepare their case.

1.10 Despite the fact that borrowers are able to apply to the court to stay execution of a default judgment, we have observed that often they do not exercise their right. The precise reasons are not clear, but are likely to include that borrowers:

- (a) are not aware that they can apply for a stay;
- (b) are not legally represented;
- (c) may not be able to afford the cost involved in seeking a stay; or
- (d) may be located in a remote or rural area and face practical difficulties in bringing matters to court.

- 1 This is distinct from an application to vary a credit contract on grounds of financial hardship (which is not possible after judgment - *Permanent Custodians Limited v Carolyn Joy Upston* [2007] NSWSC 223).
- 2 Irregular default judgment orders are those that are not consistent with the relevant court rules. Other circumstances that render default judgment orders irregular include those that are signed:
 - too soon (*Anlaby v Praetorius* (1888) 20 QBD 764 (CA));
 - for too much (*Hughes v Justin* [1894] 1 QB 667 (CA));
 - in breach of good faith (*Daly v Silley* [1960] VR 353); or
 - without evidence that no defence has been delivered by the borrower (*Dibeek Holdings Pty Ltd v Notarus* (1998) 143 FLR 132).
- 3 For example:
 - a contravention of COSL Rules (for example: contravention of COSL Rule 18 relating to financial hardship applications); or
 - a contravention of professional obligations such as the Mortgage and Finance Association of Australia (MFAA) Code of Practice or the Mutual Banking Code of Practice; or
 - a defective statutory notice.
- 4 Substantive defences to possession include:
 - relief under the Contracts Review Act 1980 (where applicable) or the National Consumer Credit Protection Act 2009 - [*Perpetual Trustee Co Ltd v Khoshaba* [2006] NSWCA 41; *Permanent Mortgages Pty Ltd v Cook* [2006] NSWSC 1104; *Cook v Permanent Mortgages Pty Ltd* [2007] NSWCA 219; *Permanent Custodians v Upston* [2007] NSWSC 223; *Benjamin v Ashikian* [2007] NSWSC 735; *Hamapham Pty Ltd v Saadullah* [2007] NSWSC 818];
 - claims of unconscionable conduct or misleading conduct under the Australian Securities and Investments Commission Act 2001 on the part of the lender or mortgage broker - [*No Fuss Finance Pty Ltd v Miller* [2006] NSWSC 630];
 - failure to comply with procedural requirements such as those arising pursuant to the Farm Debt Mediation Act 1994 (NSW) - [*Craigie v Champion Mortgage Services Pty Ltd* [2007] NSWCA 15]; and
 - claims of fraudulent conduct, including forgery - [*Chen v Song* [2005] NSWSC 19; *Chandra v Perpetual Trustees Victoria Ltd* [2007] NSWSC 694; *Sabah Yazgi v Permanent Custodians Ltd* [2007] NSWCA 240].

- 1.11** Given the relative certainty of the way in which courts will grant stays of enforcement in the situations set out in paragraph 1.8, COSL will exercise its jurisdiction in those specific situations with the aim of achieving the same result (or a comparable result) to that which a borrower could reasonably be certain of achieving if they applied to the court. Other than the situations set out in paragraph 1.8, we do not regard there to be sufficient certainty or consistency nor an adequate framework of established legal principles, for COSL to determine complaints relating to stays of execution.
- 1.12** This Position Statement provides guidance as to how, and in what circumstances, COSL may consider and determine complaints from borrowers seeking stays of execution.
- 1.13** A borrower who seeks a stay of execution should request their lender to stay the execution first and explain the reason(s) for their request. If the borrower and the lender are unable to reach agreement and the circumstances fall within the scope of COSL's jurisdiction as set out in this Position Statement, the borrower may make a complaint to us, following COSL's normal process. The subject matter of the complaint will be the lender's failure to agree to the borrower's request for a stay.

2. The nature and extent of COSL's role

- 2.1** Unlike the courts, COSL has no ability to set aside or interfere with default judgments. COSL will not act in a way which could be perceived as seeking to do so.
- 2.2** In cases where we consider that a borrower has valid grounds for seeking a stay, COSL's role will be to ask or order the lender to stay execution of the default judgment for a particular period of time.
- 2.3** We will determine the appropriate period having regard to the circumstances of each case and taking into account the interests of both the lender and the borrower. The starting point is likely to be the particular grounds on which the stay is sought, and the time reasonably required for the borrower or others to complete any necessary tasks that are related to the borrower's reasons for seeking the stay.
- 2.4** Because the facts and circumstances of each case are likely to be materially different, we do not believe it would necessarily be helpful for us to attempt to indicate what a reasonable period might be for each situation in which a stay of execution may be sought. It may be possible for us to do so in the future when we have had the benefit of working with this area of jurisdiction and acquiring sufficient practical experience.
- 2.5** We will generally expect borrowers who ask us to assist in obtaining a stay, to have:
- (a) considered their position;
 - (b) assessed their options (if any); and
 - (c) committed themselves to achieving the stay of execution that they are requesting before they approach us.

We will expect them to be able to demonstrate their good faith by having already taken substantial steps towards achieving the outcome they are seeking before asking COSL to assist.

- 2.6** For example, we are unlikely to offer assistance to a borrower who comes to us saying that they are considering the possibility of selling their property themselves but has taken no practical steps to prepare the property for sale or appoint a selling agent or identify prospective purchasers. In every case we will expect the borrower to have developed a plan (including a proposed timetable) covering the steps that they propose to take during the period of the stay and to demonstrate that there is a reasonable basis for expecting that by the end of that period, the outcome they are seeking will have been achieved.

- 2.7** We will be realistic in determining the proposed period of any stay, acknowledging where there are things that need to be done which will be beyond the control of the borrower. However, we will expect the borrower to do everything within their control without delay and to demonstrate to us that there are reasonable grounds for expecting that third parties will actually do what is required of them and within a reasonable period.

To put this in context, a stay of execution involves a person (the lender) suspending the enforcement of legal rights which they have become entitled to exercise as a result of the default of the borrower and which, in the absence of the stay, the lender would continue to enforce as the only remaining practical means of achieving repayment of the money they have lent to the borrower. It is only appropriate to require the lender to suspend the exercise of its rights in this way if the borrower is able to present a genuine and specific practical alternative that can realistically be expected to be implemented and completed within an acceptable timeframe, and to be capable of achieving its intended result.

- 2.8** Where appropriate, we can require a lender, among other things, to:

- (a) reconsider its decision to decline the borrower's request to stay execution; or
- (b) stay the execution of the default judgment.

- 2.9** However, we will not order a lender to:

- (a) take action which would require the lender to act in any way contrary to an order made by the court, unless there are reasonable grounds for expecting that the borrower could successfully apply to the court requesting the court to vary its orders to permit the lender to comply with our order;
- (b) suspend the sale of the security property to a third party once the lender has entered into a binding contract for the sale of the property.

- 2.10** A borrower may make a complaint about a lender's failure to agree to a stay of execution regardless of whether the borrower has made any other complaint relating to their loan.

- 2.11** If COSL is dealing with any other complaint relating to the borrower's loan at the time we are considering a complaint relating to a stay of execution of the default judgment relating to the loan, we will consider both complaints when determining what requests or orders (if any) we will make to the lender.

- 2.12** Once we record a complaint from a borrower seeking a stay of execution, the lender is not permitted under our Rules⁵ to act on the default judgment until we close our file on the complaint.

- 2.13** If we are unable to deal with a complaint seeking a stay, or we do not regard the borrower's request to stay a lender's execution of the default judgment as having been made out, the borrower may still apply to the court for appropriate orders. The court's jurisdiction is broader than COSL's jurisdiction in these matters.

3. Requesting COSL's assistance

- 3.1** A borrower who is considering asking COSL to assist in obtaining a stay of execution, should first:

- (a) read this Position Statement;
- (b) satisfy themselves that their reason (or reasons) for seeking the stay falls within the situations set out in paragraph 1.9;

⁵ Rule 17.2(b)(ii)

- (c) ensure that they will be able, or have a reasonable expectation that they will be able to provide us with the documents, information and any other evidence we require to deal with the borrower's complaint; and
 - (d) except in special circumstances (where we may waive this requirement), ensure that they have attempted to obtain the required stay of execution by direct negotiation with the lender and, if those negotiations are unsuccessful, by use of the lender's internal dispute resolution process.
- 3.2** We are more likely to exercise our discretion to waive this requirement if it appears that this will facilitate a more timely, effective and efficient resolution of the complaint. We are unlikely to exercise our discretion if the borrower does not provide us with relevant supporting information.
- 3.3** A borrower may request COSL's assistance to obtain the stay by following COSL's standard procedure for making complaints, set out in Rules 13 and 14, supplemented by the Guidelines. COSL will apply its usual procedures to deal with complaints requesting stays of execution.

4. Factors COSL will consider in dealing with complaints relating to stays of execution

- 4.1** We will consider each request from a borrower to stay a lender's execution of a default judgment on a case-by-case basis. We will review each complaint based on the individual merits of that complaint.
- 4.2** We consider the following when reviewing a complaint relating to a stay of execution:
- (a) whether:
 - (i) the enforcement of the default judgment would be unnecessary because the security property could be sold or the loan refinanced within a reasonable time;
 - (ii) the borrower's possession of the security property should be preserved pending a final determination in court as to whether the default judgment should be set aside; or
 - (iii) the borrower should be given more time to comply with the orders of the court given the nature and extent of the personal hardship affecting them at that time;
 - (b) whether the financial position of the lender is fully protected because the value of the security property significantly exceeds the outstanding balance of the loan;
 - (c) whether the borrower is maintaining the security property in a manner that reasonably preserves the lender's interests in the property (for example and amongst other things, paying council rates and water rates, maintaining insurances in accordance with the lender's security, and ensuring the property is kept in good repair);
 - (d) whether the borrower can show a proper basis for a stay that is fair to both parties;
 - (e) whether, having regard to the borrower's previous payment record, it is possible or likely that their indebtedness will increase following a stay of execution;
 - (f) whether there is a real risk of a shortfall between the sale price of the security property or in the amount of any refinance in a falling property market, and the amount owing on the loan secured over the property; and
 - (g) the terms of any previous stay of execution and the borrower's compliance with those terms.

- 4.3** Where the borrower requests the stay of execution to give them time to sell the property, we will also consider:
- (a) whether the lender's preparation and presentation of the property has proceeded in an orderly manner consistent with the sale of the property on the best terms available at the time the property is offered for sale; and
 - (b) when the borrower decided to sell the property (an early decision is more likely to increase the prospects of COSL ordering the lender to stay execution); and
 - (c) whether or not the proceeds from sale of the security property are likely to be enough to discharge the amounts secured by the property.
- 4.4** Where the borrower seeks a stay to discharge the debt by way of refinance, we will consider:
- (a) whether the borrower's efforts to refinance the loan have proceeded in an orderly manner so as to maximize the prospects of a refinance;
 - (b) when the decision to refinance the loan was made (an early decision is more likely to increase the prospects of COSL ordering a stay of execution); and
 - (c) the likelihood that the debt can be refinanced.

5. What is required for a stay

- 5.1** If a borrower asks for a stay of execution of a default judgment because they wish to sell the security property themselves, they will need to provide us with:
- (a) a copy of the agency sale agreement;
 - (b) a copy of the contract for sale of the property;
 - (c) a copy of advertisements for the sale of the property; and
 - (d) a copy of other relevant documents including proof that the borrower is paying rates on the property and that the property remains insured in accordance with the terms of the lender's security.
- 5.2** We may also require the borrower to agree to some or all of the following:
- (a) that unconditional contracts of sale be exchanged by a certain date;
 - (b) a minimum selling price;
 - (c) that settlement occur within a certain period (we consider six weeks from the date of exchange is reasonable unless there are special circumstances);
 - (d) that if unconditional contracts of sale are not exchanged by a certain date, the borrower will give possession of the property to the lender (if the lender does not already have possession) and not object to the lender executing the default judgment; and
 - (e) that the borrower authorises the lender in writing to obtain updates from the real estate agent from time to time.

Loan refinance

5.3 Where the borrower seeks a stay of enforcement proceedings because they intend to refinance the loan, they will need to demonstrate that there is a reasonable prospect of refinancing the loan in the circumstances, and that they have already taken steps to refinance the loan by providing us with the following:

- (a) a copy of the loan approval⁶;
- (b) correspondence with another or other lenders; and
- (c) any other relevant document or information⁷.

Given the difficulty of refinancing a loan that is in default, we expect that few borrowers will seek stays of execution to refinance their loans.

Personal hardship

5.4 If a borrower is experiencing temporary personal hardship and seeks a stay, we are likely to consider that the lender should stay execution on compassionate grounds.

5.5 Where the borrower seeks a stay because of personal hardship, they need to provide the following:

- (a) information on their circumstances, including evidence that the personal hardship is likely to be temporary; and
- (b) a copy of any other relevant documents (for example: doctor's certificate).

Setting aside the default judgment

5.6 Where the borrower intends to apply to the court to set aside a default judgment, they must have an arguable basis for their application and must have taken material steps to make the application. Only then will we ask or order the lender to stay execution until the application is made. The borrower must demonstrate to us a prima facie case that the judgment is irregular or was obtained in contravention of a legal requirement; or that there is a substantive defence to the lender's claim against the borrower.

6. COSL Rules

6.1 When considering whether we should ask or order the lender to stay execution, we have regard to:

- (a) relevant legal requirements;
- (b) applicable codes of practice;
- (c) good practice in the financial services industry; and
- (d) fairness in all the circumstances.

⁶ We would normally only accept an unconditional loan approval for this purpose, but may also accept a conditional loan approval if the conditions are realistically achievable within a reasonable time and are not onerous.

⁷ In particular, if the borrower is in payment default under their current loan, we will want to understand the basis on which the borrower expects that they will be able to service the refinancing debt. Also, the borrower must satisfy us about the way in which the responsible lending requirements of the National Credit Act have been met with respect to the refinancing debt.

Relevant legal requirements

- 6.2** Where the borrower claims that the default judgment orders are defective or in contravention of certain legal requirements, we may ask or order the lender to stay execution to allow the borrower to apply to the court to set aside or vary these orders.
- 6.3** This is more likely to happen where:
- (a) the default judgment orders are irregular; or
 - (b) the lender obtained the judgment in contravention of a legal requirement; or
 - (c) the borrower wishes to raise a substantive defence.
- 6.4** Where a borrower proposes to raise any of these defences in court, a stay on the execution of the default judgment orders will preserve the subject matter of any subsequent litigation.

Applicable codes of practice

- 6.5** Industry codes of practice may require their subscribing members to observe certain conduct standards in dealings with their customers.
- 6.6** For example, clause 8 of the MFAA Code of Practice imposes on its members a requirement of good faith dealing.
- 6.7** The Mutual Banking Code of Practice imposes similar obligations on its members (credit unions and mutual building societies). These obligations are contained in the 10 key promises made to customers (or 'members' as the Code refers to customers). The key promises include the promise to treat customers fairly and reasonably in all dealings.
- 6.8** We consider that these Code obligations require a member to consider a request to stay the execution of a default judgment reasonably and in good faith. However, this will not oblige the lender to put the interests of a defaulting borrower above the lender's own interests.

Good practice in the financial services industry

- 6.9** Generally speaking, we consider that it is good practice for a lender to consider a borrower's request for a stay of the execution of a default judgment reasonably and in good faith, where the borrower can demonstrate that they:
- (a) are able to sell the security property within a reasonable time; or
 - (b) are able to refinance the loan within a reasonable time; or
 - (c) are in temporary personal hardship and need a reasonable time to organise their affairs; or
 - (d) intend, and need additional time, to seek to set aside the default judgment.
- 6.10** However, in considering and responding to a request for a stay, the lender is entitled to have regard to all the facts and circumstances which relate to the particular matter in question, and to the broader context in which the matter arises.

Fairness in all the circumstances

- 6.11 We consider that if the lender's interests are adequately protected, it would be unfair for a lender to seek to rely on its strict legal rights by executing default judgment orders in circumstances where a stay would facilitate discharge of the loan (either by sale of the security property or refinance of the secured loan).
- 6.12 If a borrower is unable to vacate the security property in an orderly manner because of short-term personal hardship, we consider it would not be fair for the lender to insist on executing default judgment orders, particularly if the borrower has requested a stay for a very short period and that stay would not prejudice the lender's interests.

Credit files and credit reports must be accurate

7. Where we do not consider that a stay is available

- 7.1 If we consider that a stay of execution is not warranted, we will close the file and inform the parties of our decision.
- 7.2 The lender may then resume enforcement action in accordance with the default judgment terms. We would consider another request for a stay of execution only if there are new facts or circumstances that could support that consideration.
- 7.3 Where a borrower has not been successful in obtaining a stay of execution consequent to making a complaint to COSL, the borrower may apply to the court for appropriate orders. Unlike COSL, a court can order a stay of execution in any situation where the requirement of justice demands it.

8. Interpretation

In this Position Statement:

ASIC means the Australian Securities and Investments Commission.

Guidelines means the 4th edition of the Guidelines to the Rules of the Credit Ombudsman Service, effective 1 July 2010.

MFAA Code of Practice means the Code of Practice published by the Mortgage & Finance Association of Australia, as amended, at 4 March 2011.

Mutual Banking Code of Practice means the Mutual Banking Code of Practice, published by Abacus – Australian Mutuals, which commenced on 1 July 2009, as amended, and dated January 2010.

National Credit Act means the National Consumer Credit Protection Act 2009 (Cth).

RG 139 means Regulatory Guide 139 entitled Approval and oversight of external dispute resolution schemes, published by ASIC, April 2011 version.

Rules means the 7th edition of the Rules of the Credit Ombudsman Service, effective 1 July 2010.

Words and phrases which are defined for the purposes of the Rules and which are used in this Position Statement have the same meaning as they do for the purposes of the Rules.