

Unconscionable costs agreements

By ROGER MARSHALL



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Solicitors would be wise to ensure that guarantee provisions of a costs agreement have been fully explained to signatories or that they have received independent legal advice.

SEVERAL CLAUSES IN A COSTS agreement between a solicitor and a client were declared void under the provisions of s.7 of the *Contracts Review Act 1980* in the recent NSW Supreme Court case of *Liu v Adamson* [2003] NSWSC 74 decided by Master Macready. During the hearing the Master fulfilled the role of acting judge in the Supreme Court's Equity Division, and heard full argument from the parties on both the *Contracts Review Act* and the general law.

The facts

The solicitor entered into a costs agreement with several related clients. Three of the clients were natural persons while the others were corporations involved in nightclub and restaurant businesses. The plaintiff, Ms Liu, was one of those natural persons. Her de facto husband, Mr Miller, was one of the other parties to the costs agreement. Both were directors and shareholders of most of the companies party to the costs agreement.

The costs agreement contained a guarantee by Mr Miller and Ms Liu of the lia-

bilities of the corporate clients to the solicitor for costs which those companies might incur with him. Further, the costs agreement provided for the granting of security by Ms Liu and Mr Miller over their home in order to secure the guarantee that they had given under the costs agreement.

While Ms Liu had signed the costs agreement and initialled each page of it, it had not been explained to her. Subsequently it became apparent to the solicitor that Ms Liu was emotionally dependent upon Mr Miller as her de facto husband and that she was in essence a homemaker.

Several months after the costs agreement was executed, and after the solicitor had completed much work on behalf of his clients, the solicitor was granted a mortgage by Ms Liu and Mr Miller over their home to secure the payment of his fees due under the costs agreement. Despite not having had the mortgage independently explained to her, the Court found that at the time of executing the mortgage Ms Liu knew the effect of giving such a mortgage and that the failure to make payments under it could mean

attributable to Ms Liu's half-share as tenant-in-common – Ms Liu or the solicitor under the mortgage.

Garcia principles

Ms Liu's primary claim was in equity. She sought to rely on the line of authority recently discussed by the High Court in *Garcia v National Australia Bank Ltd* (1998) 194 CLR 395.

After careful consideration the Court was prepared to extend the principles of that line of authority from wives to parties living in a de facto relationship (c.f. *State Bank of NSW v Hibbert* [2000] NSWSC 628 per Bryson J). In doing so the Court was breaking new ground.

However, the essential element necessary to invoke such authority, that the wife (or now de facto wife) be a volunteer, caused difficulties for Ms Liu. She was in receipt of dividends and other income from the corporations that owned the nightclub/restaurant businesses. As the Master said: "Further, she received no inconsiderable financial rewards from most companies and, having no independent employment or profession of her

"Does a solicitor need to be in receipt of a certificate from an independent solicitor who has advised the client as to the effect of the first solicitor's proposed costs agreement?"

that her house would be sold.

As it turned out, some years later the house was sold up by the trustee in bankruptcy appointed to sequester the estate of Mr Miller. At issue was who was entitled to the net proceeds of sale

own, relied upon the income which they generated. The plaintiff therefore had a substantial interest in the companies run by Mr Miller notwithstanding that she did not actively engage in running the business of the companies" (judgment, para-

graph 40).
The Court found that she volunteered in the costs. Accordingly, it found that it was outside the contemplation in re *Garcia* princ

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The Court therefore found that she was not a volunteer in executing the costs agreement. Accordingly, the Court found that it could not set aside the costs agreement in reliance upon *Garcia* principles.

Section 7 of the Contracts Review Act

As a subsidiary argument, Ms Liu sought relief under s.7 of the *Contracts Review Act*. The Court decided that on the facts of the case, s.6(2) of the Act did not serve to exclude the claim. The solicitor's submission that the costs agreement was a contract entered into in the course or for the purpose of the trade, business or profession carried on by the person was rejected.

Seven factors were identified in this case by the Master for the purposes of s.9(2) of the Act. Set out in full, these were as follows:

"1. The terms of the contract were not the subject of negotiation between the plaintiff and the defendant either at the time of the contract or beforehand. Such negotiations as there were, were between Mr Miller and Mr Adamson.

"2. There is no doubt that the plaintiff would have been free to negotiate or to reject any of the provisions of the contract if they had been explained to her. Given that they had not and the role that her husband played in negotiating the contract, it could be said that it was not practicable for the plaintiff to seek to negotiate the provisions.

"3. A question arises as to whether or not the clause in the costs agreement giving security over the home was not reasonably necessary for the protection of the legitimate interests of Mr Adamson in the contract. Given the extent of the work to be carried on, and which was in fact carried on, it seems to me that I could not say that the clause was not reasonably necessary for his protection.

"4. Although the plaintiff reposed trust and confidence in Mr Miller there is no suggestion that because of her age or the state of her physical or mental capacity

that she was not able to protect her interests.

"5. No independent legal advice was obtained.

"6. The legal and practical effect of the contract was not explained to the plaintiff and, as I have found, she did not understand the nature of the provisions.

"7. No undue influence, unfair pressure or unfair tactics were exerted upon the plaintiff to obtain the execution of the costs agreement."

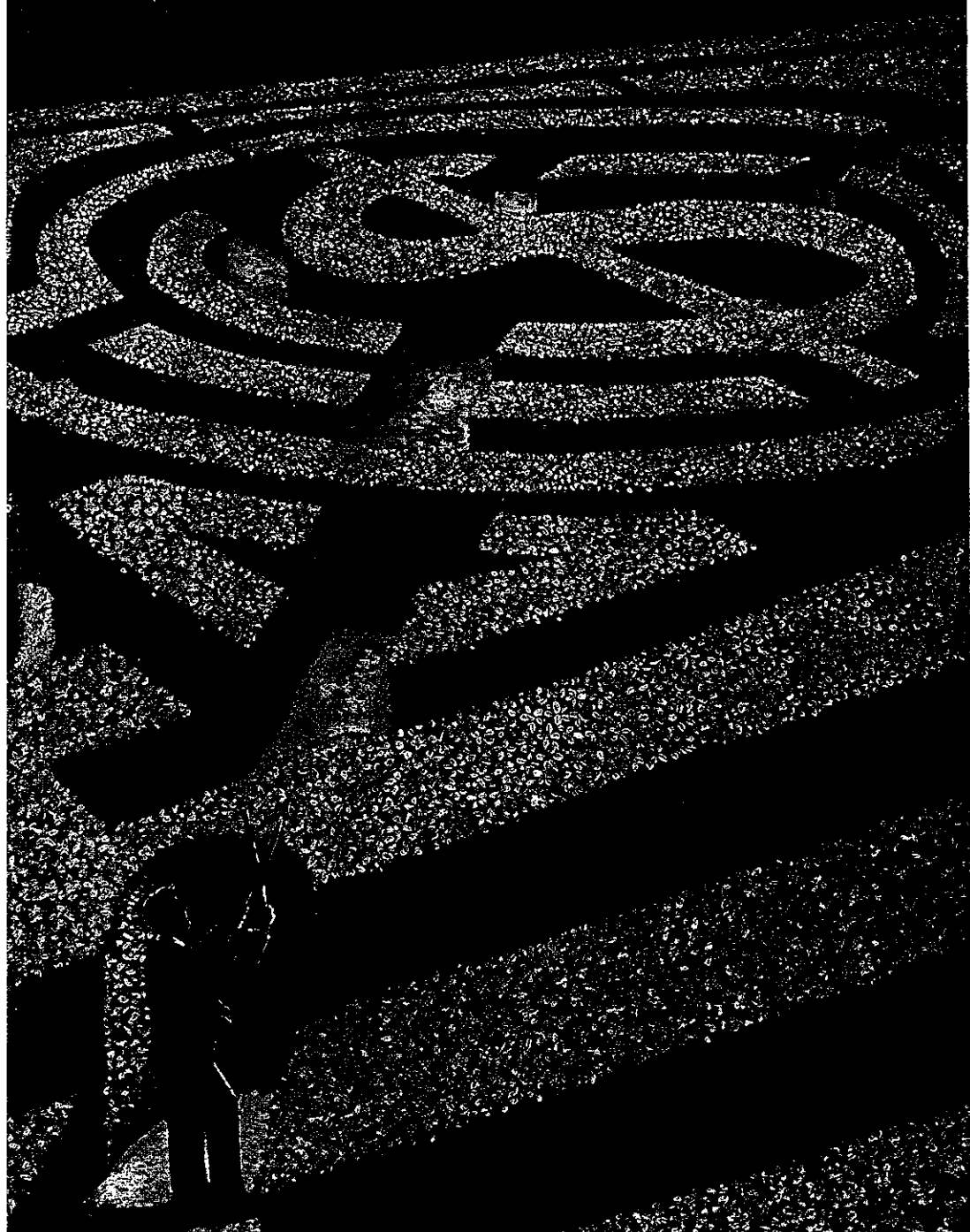
After considering the seven factors, Master Macready concluded that the guarantee provisions of the costs agreement were unjust in the circumstances and should be declared void. Particular weight was placed on the lack of indepen-

dent or any advice given to Ms Liu when she signed the costs agreement. The Master said: "Although he suggested that his prospective clients obtain other independent advice he made no effort to check that they did and had the plaintiff [Ms Liu], whom he met for the first time at the occasion of the signing of the contract, sign the contract without any explanation".

As the guarantee provisions in the costs agreement which gave rise to the right to the mortgage were set aside, the mortgage was also set aside.

Legislative basis for setting aside costs agreements

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■ COSTS AGREEMENTS

have had certain terms of their retainer set aside or parts of the bills disallowed for reasons of unfairness under the general law: *In re Stuart; ex parte Cathcart* (1893) 2 QB 201, *Clare v Joseph* [1907] 2 KB 369, *Burgundy Royale Investments Pty Ltd v Westpac Banking Corporation* (1992) 109 ALR 549 and *Richardson v Lander* (1947) 65 WN (NSW) 74.

More recently, the ability of solicitors' costs agreements specifically to be set aside has been enshrined in State legislation. In 1994 the major amendments to Part 11 of the *Legal Profession Act 1987* included the insertion of s.208D(1) into that Act whereby: "A costs assessor may determine whether a term of a particular costs agreement entered into by a barrister or solicitor and a client is unjust in the circumstances relating to it at the time it was made". (It should be noted that s.208D of the *Legal Profession Act* is couched in very similar terms to s.9(2) of the *Contracts Review Act*.)

While s.208D would appear to be of significance to solicitors when a solicitor's costs are actually being assessed, it remains to be seen exactly how a costs assessor is to determine the unjustness of "the circumstances relating to it" [being a term of a costs agreement at the time it was entered into]. That is because of the absence of any power for a costs assessor

to take sworn evidence under the *Evidence Act* for any reason, including to resolve the conflicting positions of the parties on the issue of whether circumstances were unjust: see *Ryan v Hansen t/as Hansens Solicitors* (2000) 49 NSWLR 184.

However, s.207 of the *Legal Profession Act* gives assessors very wide powers to compel production of documents and provision of information by way of statutory declaration. Moreover, s.208(2) of the *Legal Profession Act* provides that an assessor is not bound by the rules of evidence and may inform himself or herself "on any matter in such manner as he or she thinks fit".

(Note, since the introduction of s.208D, there have been a number of appeals considering the application of that section: *Reynolds Jeanette v Whittens* [2002] NSWSC 155 (O'Keefe J), *Advanced Gaming Technology Pty Ltd v Julieann P. Ahern* [1999] NSWSC 45 (Levine J), *Thurai Rajah Lawyers v Villaneuva* [2001] NSWSC 597 (Malpass M) and *Firth v Kasumovic* [2001] NSWSC 341 (Malpass M)).

Independent legal advice

Solicitors could be forgiven for believing they find themselves in the same situation as lending institutions. In order to have the terms of a retainer regarded as unimpeachable, does a solicitor need to be in receipt of a certificate from an inde-


pendent solicitor who has advised the client as to the effect of the first solicitor's proposed costs agreement?

It is instructive to note that Master Macready was concerned to know whether Ms Liu had been the recipient of an explanation from the solicitor about the nature and effect of the costs agreement. Presumably, if the solicitor had given such an explanation to the client, in the absence of any undue influence by the solicitor or any other clients under the costs agreement, and it were proven that the client understood that explanation, it would not be essential for independent legal advice to be received.

Of course, when, as in Ms Liu's case, mortgage security was promised in the costs agreement on a guarantee basis, prudence would dictate that the solicitor should insist on receiving a certificate of independent legal advice so that the solicitor could call on the certifier to give evidence about the client's understanding.

Conclusion

The moral of this story is for solicitors to ensure, at the very least, that they explain the nature and effect of the cost agreement they offer to each of their prospective clients and their client's guarantors. Where guarantors are proposed, consideration should be given to having the guarantor receive legal advice independently of the prospective clients. □




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