

# Chapter 12

## Class actions and legal advice to investors

We entered into a Class Action with M & K [Macpherson+Kelley Lawyers], which again cost monies, and after about four years the Class Action lost. The original \$133,000 loan has now been demanded from us at the cost of \$245,000—with compounding interest.<sup>1</sup>

12.1 While the committee is of the view that the banks should have been more diligent and careful when providing finance for retail investors to fund their agribusiness venture, they cannot be held responsible for the actions of growers who followed legal advice to stop repayments on their loans. In this chapter, the committee considers the advice given to investors to cease repayments on their loans. Investors who followed this advice found themselves in a financial situation far worse than when the schemes initially collapsed.

### Compound interest and mounting debt

12.2 Many investors saw their debts increase markedly from the time their scheme folded to the current time, in some cases more than double under what some described as 'crippling', 'exorbitant' and 'punitive' rates.<sup>2</sup> Compound interest meant that original loans grew substantially.<sup>3</sup> For example, one couple saw their loans from Timbercorp, which initially totalled between \$200,000 and \$300,000 accrue, and continue to accrue, with compounded interest, to nearly \$700,000.<sup>4</sup> Similarly, Mr Wayne Grumley stated:

I'm 53 years old and this was going to be my/our long term investment for retirement. I cannot see retirement for me in the near future, looks like I will [be] working until the day they put me in the ground. Now with the collapse of timber-corp, I'm left with a debt (originally \$340,000) now

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1 Robert and Lynne Powell, *Submission 5*.

2 Ms Barbara Gray, *Submission 54*, p. 1; and Mr Mark Laszczuk, *Submission 157*, p. [1]. *Submissions 68*, p. [1]; *Submission 104*, p. 1; *Submission 131* and *Submission 153*, p. [2]. *Confidential Submissions 88*, 116, p. 1; *Confidential Submission 140*, p. 1; *Confidential Submission 155*.

3 *Confidential Submission 141*, p. 1.

4 Ms Barbara Gray, *Submission 54*, p. [1]; *Submission 55*, p. 1; *Submission 66*, p. 1; *Submission 72*, p. 1; *Submission 74*, p. 3; name withheld *Submission 96*, p. 1; *Submission 109*, p. 2; *Submission 110*, p. 1; *Submission 119*, p. [2]; *Confidential Submission 130*, p. 1. See also name withheld, *Submission 62*, p. 1—they owe \$270,000 which is growing each month with a penalty interest rate of 13.2% from an initial \$100,000 loan. Also *Confidential Submission 140* and *Confidential Submission 141*.

around the \$600,000 and growing each month with a penalty interest rate of 13.2%.<sup>5</sup>

12.3 Many investors who saw their loans continue to mount were not making repayments.

### **Class action—advice not to repay**

12.4 After the collapse of some of the major MIS, there were a number of prolonged class actions challenging the standing of the PDS attached to the respective MIS.<sup>6</sup> During this period, a number of submitters received and followed legal advice not to repay their loans.<sup>7</sup> For example, Bendigo and Adelaide Bank noted that after Great Southern was placed in administration, various law firms advised their clients to cease making payments on their loans, including the law firm representing the lead plaintiffs in the class actions and a law firm representing clients of Mr Steve Navra. It observed:

...it is difficult to understand how the law firms had sufficient information to properly assess the merits of any claims available to borrowers so soon after the collapse of Great Southern. Navra [an adviser who recommended Great Southern] also advised his clients in lengthy 'blogs' that he intended to cease making payments on his Great Southern loans. The inference was that his clients should do the same.<sup>8</sup>

12.5 M+K Lawyers, in particular, represented 'several thousand investors' seeking remedies following the collapses of Timbercorp and Great Southern REs.<sup>9</sup> It explained that the primary focus of the class actions was to seek an order from the court that the loans were unenforceable as well as to obtain compensation for damages. The basis of their claim in May 2010 was that:

...at the time our clients invested in the respective schemes, the responsible entity failed to disclose key information concerning its financial position, and as a result our clients have been misled into investing. They were

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5 *Submission 2*, p. 1.

6 Name withheld, *Submission 97*, p. [2]; name withheld, *Submission 94*, p. [1] and Mr Mark Laszczuk, *Submission 157*, p. [1]. *Confidential Submission 36*, p. [4];

7 See, for example, name withheld, *Submission 75*, p. [1]; Mr Con Solakidis, *Submission 119*, p. [2]; *Confidential Submission 124*, pp. 1–2. Mr Bernard Kelly, *Proof Committee Hansard*, 12 November 2014, p. 7.

8 Bendigo and Adelaide Bank, response to *Submissions 52, 63, 175 and 176*, dated 24 December 2014, p. [16].

9 According to M+K, as at 31 May 2010, it was acting for over 2,400 Timbercorp clients, with over 2,100 of these participating in the class action; and over 1,600 Great Southern investors. M+K submission to Consultation Paper 133: Agribusiness Managed Investment Schemes: Improving Disclosure for Retail Investors, 31 May 2010, paragraph 3.

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deprived of the opportunity to make an informed decision about whether or not to invest and whether or not to obtain finance in order to invest.<sup>10</sup>

12.6 As noted in chapter 9 and the previous chapter, the courts rejected the argument, which meant that the former members of the failed schemes, who had anticipated being released of their loan obligations, were obliged to repay their original loan and the compounding interest.<sup>11</sup> Thus, during the protracted class actions, the many investors who took advice not to repay their loans found that their initial debt had blown out considerably and was continuing to mount on a daily basis. The situation arose with both Timbercorp and Great Southern. As one such investor noted:

The reason why we did not act quicker regarding this matter is that we were part of a class action that took 5 years to go through the courts and then no positive outcome and not to mention out of pocket legal costs for what, just for some judge to tell us tough luck and pay up.<sup>12</sup>

12.7 Another investor who ceased repayments stated:

The banks who took over the loans from Great Southern are chasing us for double what is owed due to us stopping payment to pursue this matter via legal avenues (which has added to our already large debt).<sup>13</sup>

12.8 Mr Mazzucato, another grower who did not keep up his repayments, informed the committee:

The next 5 years was the time of the McPherson and Kelly Class action against Timbercorp. I did not see that there was any point taking legal action against the financial planner until the class action had ended. Over the time of this court case, the debt had ballooned to over \$175,000 due to the extortionate interest rate applied to the loan. I now have a debt that is unserviceable.<sup>14</sup>

12.9 Concerns about ever increasing debt were all too common. For example, in one case, an investor initially had a debt of \$240,000 at the time of Timbercorp's collapse, which had climbed to around \$445,000 by 2014 with 'bank interest escalating daily'.<sup>15</sup> One couple explained that in 2009 they were advised to cease repayments on their Timbercorp loans pending a favourable outcome from the class action. They stated:

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10 M+K submission to Consultation Paper 133: Agribusiness Managed Investment Schemes: Improving Disclosure for Retail Investors, 31 May 2010, paragraph 5.

11 See paragraphs 9.36–9.46 and 11.70.

12 Name withheld, *Submission 33*, p. [1].

13 Andigone Aguilar, *Submission 50*. See also, *Submission 44*, p. 1.

14 *Submission 40*, p. [2].

15 *Confidential Submission 37*, p. 2. Also Mr Mark Laszczuk, *Submission 157*.

Unbelievably the legal action was unsuccessful and to add insult to injury our combined initial investment of \$158,100 has since doubled to \$355,000 due to highly unreasonable penalty interest that accrued.<sup>16</sup>

12.10 Yet another spoke of the legal proceedings dragging out for four or five years with initially the company and later the receiver continuing 'to stack on large amounts of interest to the borrower'.<sup>17</sup> Another couple recalled their story which replicates those of many others:

Since the collapse of Timbercorp in April of 2009, 9 months after our initial investment, we've been unable to make sense and understand what went wrong. Our investment was gone, but where did the funds go? As a result, we joined a class action run by M&K Lawyers. Along the way, we received more bad advice, to stop paying the loans.

...

In April 2014, we have lost our legal battle, after one trial in the Supreme Court of Victoria, an appeal and a High Court dismissal. Unbelievably the loans have doubled from \$178,570 to \$326,998 due to highly unreasonable penalty interest that accrued. This is totally unrealistic for an investment. As we speak these loans are getting charged at 13.2% interest, when the market rate is around 5%. There is no income return that we will ever receive and this loan is not repayable over our lifetime given our age.<sup>18</sup>

12.11 ANZ was aware that M&K lawyers had provided advice to suspend payments during the class action involving Timbercorp. It advised that because ANZ did not provide the loans, which were under the management of KordaMentha, ANZ had 'no specific information on their status'. It was also of the view that it was 'inappropriate for ANZ to get between the lawyers and their clients'.<sup>19</sup> KordaMentha noted that the borrowers who stopped making repayments in breach of their obligations had interest accruing at the higher rate of interest 'in accordance with the terms of the loan agreements, which caused loan balances to increase ever since'. It stated:

Timbercorp Finance has continued to provide annual loan statements to Borrowers. We submit that insofar as Borrowers have acted on advice to cease making loan repayments and have suffered loss and damage as a result, they should carefully consider claims which may be available to them against those that proffered the advice.<sup>20</sup>

12.12 With regard to Great Southern, Bendigo and Adelaide Bank noted that it wrote to borrowers on a number of occasions outlining the financial implications of ceasing to make repayments, in particular, the effect of compounding interest on the

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16 Name withheld, *Submission 75*, p. [1].

17 Name withheld, *Submission 94*, p. [1].

18 Name withheld, *Submission 102*, p. [1].

19 ANZ, answer to question on notice, No. 3, taken on 6 August 2015.

20 KordaMentha, additional Information, dated 4 December 2014, p. 2.

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balance of their loan.<sup>21</sup> It informed the committee that 'compounding interest is a powerful tool for depositors, but it is debilitating for borrowers'.<sup>22</sup>

### *Committee view*

12.13 The investors who took legal advice to cease their repayments are faced with a loan substantially greater than at the time their schemes collapsed. The committee is concerned that vulnerable people who joined the various class actions hoping to, in effect, have their loans deemed unenforceable are now in a financial position far worse than when the class actions started.

12.14 The committee is firmly of the view that the legal profession has the responsibility to inform itself of the circumstances around the advice that was provided to retail investors in collapsed agribusiness MIS to cease repayments on their outstanding debts. Accordingly, the committee contends that a review needs to take place to determine whether action should be taken to ensure that the profession maintains high ethical standards and that its members adhere to best interest obligations towards their clients.

### **Recommendation 18**

**12.15 The committee recommends that the Victorian Legal Services Commissioner and Legal Services Board thoroughly review the conduct of the lawyers who provided advice to retail investors in collapsed agribusiness MIS to cease repayments on outstanding debts and the circumstances around this advice.**

**12.16 The intention would be to determine whether the profession needs to take measures to ensure it maintains high ethical standards and that its members adhere to best interest obligations towards their clients. The investigation would include making recommendations or determinations on:**

- **remedies available to investors belonging to the class actions who have suffered considerable financial loss as a result of following advice to cease repayments on their outstanding loans;**
- **whether disciplinary action should be taken against the lawyers who provided the advice to stop repayments;**
- **whether the matter warrants any form of compensation; and**
- **whether the matter should be referred to any appropriate disciplinary body.**

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21 Response from Bendigo and Adelaide Bank, dated 24 December 2014, p. [16].

22 Confidential correspondence to committee, dated 19 October 2014, p. [2].

