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An Investment Contract or Unlicensed Moneylending?

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Introduction

In its recent decision in *Ochroid Trading Ltd and another v Chua Siok Lui (trading as VIE Import & Export) and another* [2018] SGCA 5 ("***Ochroid***"), the Singapore Court of Appeal has provided valuable guidance in the area of contract illegality generally, and specifically, on the enforceability of illegal money lending transactions.

No recovery of monies pursuant to an illegal loan

In *Ochroid*, the plaintiff sought to recover monies which it had disbursed to the defendants under what was referred to as an "investment contract". The plaintiff attempted to recover the monies it had disbursed in two different ways.

Firstly, the plaintiff sought to characterize its transaction to lend monies to the defendants as an "investment in a joint venture" and thereby, sought to enforce its contractual rights to recover its "investment".

In considering this aspect of the claim, the Court made it clear that the labels or titles that were put on a transaction by the parties are not determinative of the nature of the transaction. The Court will carefully consider the form and substance of the transaction as well as the parties' position and relationship in the context in order to determine the true nature of the transaction.

After reviewing the contract and the evidence, the Court found that whilst the parties labelled their transaction as an "investment contract", it was in fact an illegal loan transaction in contravention of the *Moneylenders Act* ("**MLA**"). An illegal loan in contravention of the MLA was not enforceable and the plaintiff's claim under this head must therefore fail.

Secondly, the plaintiff sought to recover just the principal loan amount (without any interest) disbursed under the illegal loan transaction on the grounds that to allow the defendants to retain the principal loan amount would be tantamount to unjust enrichment on the part of the defendants. In other words, the plaintiff sought to recover the loan amount under the independent claim of unjust enrichment even though the transaction itself was illegal since it contravened the MLA.

The Court in *Ochroid* recognised a plaintiff's right to seek restitutionary recovery through an independent claim in unjust enrichment. The Court however ruled that such a restitutionary claim is "*subject to the defence of illegality and public policy in unjust enrichment".* In arriving at its decision, the Court considered the principle of stultification and expressly endorsed it. Under the principle of stultification, a party would be precluded from claiming in unjust enrichment if to do so would undermine the fundamental policy that rendered the underlying contract void and unenforceable in the first place.

Applying these principles to the facts in *Ochroid*, the Court of Appeal held that the Plaintiff's claim cannot succeed because to "*permit recovery of even the principal sums would undermine and stultify the fundamental social and public policy against unlicensed moneylending which undergirds the MLA*" and "*[p]ermitting restitution of the principal sums lent would make a nonsense of this policy and render ineffectual the prohibition in s 15, which reflects the strong need to deter illegal moneylending due to its status as a serious social menace in Singapore.*"

The Court also ruled that there was also "*no doubt that the rationale of s 15 of the MLA, and its efficacy in deterring illegal moneylending, would be severely undermined and made a nonsense of if the courts were to permit an unlicensed moneylender to recover the principal sums disbursed through an independent claim in unjust enrichment... [T]he availability of the claim in unjust enrichment for the principal sums would provide illegal moneylenders with leverage to compel their debtors to make full repayment despite the prohibition of the loan agreement. The claim would also provide them with a "safety net" by allowing them to recover their principal sums.*"

In summary, the effect of the Court of Appeal's decision in *Ochroid* is that once the Court characterizes a transaction as an illegal loan in contravention of the MLA, **no recovery of monies, whether principal or interest, will be permitted**.

Moneylending under the MLA

In the context of the Court of Appeal's recent decision in Ochroid, it would be helpful to consider briefly the salient features of the MLA.

Under the MLA, a person can only carry on or hold himself out in any way as carrying on the business of moneylending in Singapore with a licence under the MLA. Agreements made in pursuit of the business of unlicensed moneylending are unenforceable.

The provisions of the MLA are not in favour of lenders. Under the MLA, any person (other than an "excluded moneylender", which we will consider below) who lends a sum of money in consideration of a larger sum being repaid shall be presumed, unless otherwise proved, to be a person who carries on or holds himself out in any way as carrying on the business of moneylending.

A license is therefore required unless a person can show that:

- he is not carrying out the “business of moneylending”. The “business of moneylending” in Singapore refers to where: (1) there is a system and continuity in the loan transactions; or (2) the alleged moneylender is ready to lend to all who fall within his eligibility criteria; or
- he is an “excluded moneylender” or an “exempt moneylender” under the MLA, failing which the loan transactions made by the alleged moneylender will be unenforceable.

Under the MLA, a person is an “excluded moneylender” if he is:

- a person licensed, approved, registered or otherwise regulated by the Authority under any other written law, to the extent that such person is permitted or authorised to lend money or is not prohibited from lending money under that other written law;
- a society registered as a credit society under the Co-operative Societies Act (Cap 62);
- a licensed pawnbroker licensed under the Pawnbrokers Act 2015;
- a person who lends money solely to:
    - his employees as a benefit of employment;
    - accredited investors within the meaning of section 4A of the Securities and Futures Act (Cap. 289);
    - corporations;
    - limited liability partnerships;
    - trustees or trustee-managers, as the case may be, of business trusts for the purposes of the business trusts; or
    - trustees of real estate investment trusts for the purposes of the real estate investment trusts, or who carries on any combination of such activities or services.

Implications of Ochroid

An unlicensed moneylending transaction or an investment contract? The Court of Appeal’s decision in *Ochroid* makes it vital for businesses to ensure that their transactions do not constitute unlicensed moneylending or illegal loans within the meaning of the MLA.

It does not matter what parties label their agreements. The Court, when looking at whether a transaction was an illegal loan within the meaning of the MLA, will consider “*the form and substance of the transaction as well as the parties’ position and relationship in the context of the entire factual matrix*”.

Given the decision in *Ochroid*, if you have or do lend money to other individuals or entities in the course of your business, it would be advisable for you to obtain legal advice on whether your proposed transactions could fall within the meaning of unlicensed moneylending under the MLA.

Unless you are an excluded or exempted moneylender, moneylending is illegal under the MLA. In order to qualify as an “exempt moneylender”, an application must be made to the Registry of Moneylenders and exemptions are granted on a case by case basis.

This update is provided to you for general information and should not be relied upon as legal advice.

Authors

- Subramanian Pillai
- Randall Perera
- Ervin Roe
- Benita Koh
- Samuel Ling

Contacts

Subramanian PILLAI
Partner

Randall PERERA
Senior Associate

Authors

Subramanian PILLAI
Randall PERERA
Ervin ROE
Benita KOH
Samuel LING

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