THE EXTENT TO WHICH UNCONSCIONABILITY AT GENERAL LAW, THE SPECIAL EQUITY IN *GARCIA* AND PART IVA OF THE *TRADE PRACTICES ACT 1974* (CTH) ARE AVAILABLE TO A DEBTOR OR GUARANTOR WHEN A FINANCE PROVIDER SEEKS TO ENFORCE A SECURITY

by

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CERTIFICATE OF AUTHORSHIP/ORIGINALITY

I certify that the work in this thesis has not previously been submitted for a degree nor has it been submitted as part of requirements for a degree except as fully acknowledged within the text.

I also certify that the thesis has been written by me. Any help that I have received in my research work and the preparation of the thesis itself has been acknowledged. In addition, I certify that all information sources and literature used are indicated in the thesis.

Geoffrey Nigel O'Shea

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LIST OF ABBREVIATIONS

Abbreviation	**Definition**
ACCC	Australian Competition and Consumer Commission.
ADI	Approved Deposit Institution.
APRA	Australian Prudential Regulatory Authority.
ASIC	Australian Securities and Investments Commission.
ASIC Act	*Australian Securities and Investments Commission Act 2001* (Cth).
Corporations Act	*Corporations Act 2001* (Cth).
EFM	Equity Finance Mortgage.
L/C	Letter of Credit.
NCC	National Credit Code.
SAM	Shared Appreciation Mortgage.
TPA	*Trade Practices Act 1974* (Cth).
VCAT	Victorian Civil and Administrative Tribunal.

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ABSTRACT

AIM AND FIELD OF RESEARCH

Debtors and guarantors of loans by finance providers often endeavour to escape liability by relying on disentitling conduct on the part of their finance provider.

Over the last twenty-six years, a body of jurisprudence has developed around s 52 of the *Trade Practices Act 1974* (Cth). This has enabled debtors and guarantors of loans by finance providers to escape liability where there has been misleading or deceptive conduct by the finance provider.

Recently the Australian Consumer Law[1] has been enacted. Over time it is anticipated that debtors and guarantors of loans by finance providers will be able to escape liability by reason of conduct which contravenes this legislation.

This thesis examines the circumstances in which guarantors and debtors are able to escape liability by relying on unconscionability under the general law, unconscionability under the *Trade Practices Act 1974* (Cth) or by relying on the special equity considered in *Garcia v National Australia Bank Limited*[2] (*Garcia*). The special equity in *Garcia* is sufficiently closely related to the doctrine of unconscionability to warrant its examination in this thesis.

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[1] The first part of the Australian Consumer Law (the *Trade Practices Amendment (Australian Consumer Law) Act (No. 1) 2010* (Cth)) has already commenced. On 15 April 2010, the Australian Competition and Consumer Commission received a wide range of new enforcement powers. New provisions were created in the *Trade Practices Act 1974* (Cth) on unfair contract terms to commence on 1 July 2010.
The main part of the Australian Consumer Law (the *Trade Practices Amendment (Australian Consumer Law) Act (No. 2) 2010* (Cth)) commences on 1 January 2011. On that date, the existing consumer protection provisions in Parts IVA, V, VA and VC of the *Trade Practices Act 1974* (Cth) will be repealed and replaced with the Australian Consumer Law. The *Trade Practices Act 1974* (Cth) will also be renamed as the *Competition and Consumer Act 2010* (Cth). The States and Territories are also intended to amend their existing laws with effect from 1 January 2011 to adopt the Australian Consumer Law as a uniform national law, but all the necessary legislation has as yet not been enacted.

[2] (1998) 194 CLR 395.

In addition to examining the circumstances under which guarantors and debtors are able to escape liability by relying on unconscionability under the general law and/or unconscionability under the *Trade Practices Act 1974* (Cth) and/or by relying on the special equity considered in *Garcia,* this thesis also examines the future direction of this area of the law, together with its likely future impact on the provision of finance in Australia.

The first area examined by this thesis is unconscionability claims in equity.

The second area examined by this thesis is the special equity, which was identified by Dixon J in *Yerkey v Jones,*[3] and reaffirmed and extended by the High Court of Australia in *Garcia.* The special equity in *Garcia* is seen to be a special extension to the doctrine of unconscionability.

The third area examined by this thesis is unconscionability under Part IVA of the *Trade Practices Act 1974* (Cth). Here it is recognised that Part IVA unconscionability allows courts to consider both the existing 'unwritten law'[4] of what is unconscionability, as well as statutory unconscionability under ss 51AB and 51AC of the *Trade Practices Act 1974* (Cth).

This thesis spans the period up until 28 May 2010.

The following questions are asked:

1. What is unconscionability under the general law?
2. Having regard to the High Court's decision in *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd*[5]

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[3] (1939) 63 CLR 649.

[4] 'Unwritten law' being the term referred to in s 51AA.

[5] (2003) 214 CLR 51.

(*Berbatis*), what legislative changes are needed in ss 51AB and 51AC in Part IVA of the *Trade Practices Act 1974* (Cth) in order to extend the statutory definition of unconscionable conduct?

3. If there were changes made to ss 51AB and 51AC so as to extend the liability of parties who engage in unconscionable conduct, what would be the likely impact on financiers?
4. Post *Garcia*, has there been a willingness by courts to extend the types of relationships that will attract the special equitable relief in *Garcia*, beyond the confines of the wife-and-husband marital relationship?

MAIN RESULTS AND CONCLUSIONS

1. The meaning of unconscionability under the general law has been firmly established by the High Court in cases such as *Commercial Bank of Australia Ltd. v Amadio*[6] (*Amadio*). An unconscionability claim requires the establishment of two elements. The first element is that the guarantor was under a special recognised class of disability. The second necessary element is that the stronger party knew, or ought to have known, of the weaker party's special disability and was unfairly abusing its dominant position. There has been no expansion of the definition of unconscionable conduct outside this rigid definition.

   Courts have been reluctant to utilise the indicators of unconscionable conduct listed under the *Trade Practices Act 1974* (Cth) ss 51AB for consumers and 51AC for small business and have generally narrowed their consideration to determining if the elements of *Amadio* are evident so as to determine under s 51AA if unconscionability has been established 'within the meaning of the unwritten law'. This has limited the effectiveness of ss 51AB and 51AC.
2. If the Federal Government wants Part IVA of the *Trade Practices Act 1974* (Cth) (and its mirrored provisions in the *Australian Securities and Investments Commission Act 2001* (Cth)) to provide more effective cover against unconscionable conduct, one of the options that could be considered would be to add further provisions to Part IVA in order to assist with the definition of what is unconscionable conduct. The provisions could adopt French J's approach from the Federal Court decision at first instance in *Berbatis.*
3. If this approach was adopted in Part IVA, then Australian banks would need to be more rigorous in the exploration of their client's circumstances and take a more conservative approach in regard to their willingness to provide finance and accept security.

[6] (1983) 151 CLR 447.

4. In regard to the special equity in *Garcia*, there has been some willingness of the lower courts since the High Court decision in *Garcia* to expand the nature of relationships under which such relief will be provided. The limits of this expansion are not yet finalised.

1. INTRODUCTION

1.1 SCOPE OF THIS THESIS

Over the past twenty-seven years:

- the development of the equitable unconscionability doctrine following such cases as *Amadio*;
- the enactment of the unconscionability provisions in Part IVA of the *Trade Practices Act 1974* (Cth); and
- the reaffirmation of the special equity in *Garcia*

have impacted upon the way financiers structure their facilities, particularly in regard to their treatment of third party security providers.

This thesis explores the extent to which an unconscionable conduct claim at general law and under Part IVA of the *Trade Practices Act 1974* (Cth), and the special equity in *Garcia* which is an extension of unconscionability, are available to a debtor or guarantor when a finance provider seeks to recover a debt and/or enforce a security.

The use of the term 'special equity in *Garcia*' relates to the decision by the High Court in the *Garcia* case to reaffirm the correctness and continued applicability of *Yerkey v Jones* to Australian law.

In the course of its decision in *Garcia*, the High Court recognised the possibility that this special equity may extend beyond a special equity for wives guaranteeing their husbands borrowings to any person who, due to their emotional reliance on the borrower felt compelled to provide a guarantee without receiving any financial benefit from the loan to the borrower.

This thesis specifically considers the following questions:

1. What is unconscionability under the general law? This question is considered in order to understand the extent to which unconscionable conduct has developed in equity in Australia and whether the *Trade*

Practices Act 1974 (Cth) has expanded the definition of unconscionable conduct.

2. Having regard to the High Court's decision in *Berbatis*, what legislative changes are needed in ss 51AB and 51AC in Part IVA of the *Trade Practices Act 1974* (Cth) in order to extend the statutory definition of unconscionable conduct? This question is important, as following the High Court decision not to apply a wider definition of unconscionable conduct, in order to make ss 51AB and 51AC effective for debtors or guarantors when a finance provider seeks to enforce its security, legislative change is required.
3. If there were changes made to ss 51AB and 51AC so as to extend the liability of parties who engage in unconscionable conduct, what would be the likely impact on financiers? This question is considered in order to determine what the ramifications would be if the proposed changes were adopted.
4. Post *Garcia*, has there been a willingness by courts to extend the types of relationships that will attract the special equitable relief in *Garcia*, beyond the confines of the wife-and-husband marital relationship? This question is of interest for financiers in order that they can understand the extent of the risk of challenges to their security from reliance on the special equitable relief.

This thesis does not deal with the entitlement of a debtor or guarantor to escape liability for a debt owed to a finance provider on the grounds that the money was borrowed or guaranteed by reason of:

- undue influence;
- misleading and deceptive conduct (including s 52 of the *Trade Practices Act 1974* (Cth));
- misrepresentation (including false and misleading representations under s 53 of the *Trade Practices Act 1974* (Cth));
- estoppel;
- duress;
- non est factum;

- an application for relief based on s 9 of *Contracts Review Act 1980* (NSW), that a contract or a provision of a contract is unjust;[7] and
- an application to re-open an unjust transaction (which includes a consumer loan contract, or a mortgage or guarantee to secure a consumer loan) under s 70 of the *Uniform Consumer Credit Code*.[8]

It is also outside the scope of this thesis to consider relief under legislation which mirrors the statutory unconscionability provisions of the *Trade Practices Act 1974* (Cth) such as the provisions in the *Australian Securities and Investments Commission Act 2001* (Cth) ss 12CA, 12CB and 12CC.

Any reference in this thesis to the impact on financiers or proposed changes to Part IVA of the *Trade Practices Act 1974* (Cth) is to be taken to also include the mirrored unconscionability provisions to apply to financial services in the *Australian Securities and Investments Commission Act 2001* (Cth) of ss 12CA, 12CB and 12CC (particularly as it is now only small business that can bring unconscionability actions under s 51AC of the *Trade Practices Act 1974* (Cth) for finance transactions).

This thesis is structured as follows. The first chapter defines the scope of the thesis. An understanding is then gained as to what is meant by the term ‘unconscionability’ under the general law. The second chapter undertakes a review of the major Australian and English cases,

[7] Section 4(1) defines ‘unjust’ as ‘includes unconscionable, harsh or oppressive’.

[8] The Federal Government is replacing the State-based *Uniform Consumer Credit Code* (‘*UCCC*’) with the new *National Credit Code* (‘*NCC*’), which is contained as schedule 1 within the *National Consumer Credit Protection Act 2009* (Cth). The Act received royal assent on 15 December 2009 and provides in s 2(1), that schedule 1 (and thus the *National Credit Code*) will commence on the date to be proclaimed (1 April 2010). The Australian States are expected to pass State Referral Bills and repeal their State laws before 1 July 2010, when the new National Consumer Credit regime will take effect (registrations of existing credit providers by the Australian Securities and Investment Commission will take effect from 1 July 2010, with applications for credit licences opening on 1 July 2010).

particularly as applicable to finance scenarios, with the *Amadio* case examined in detail.

Aside from the invoking of principles of law of unconscionability, this thesis also explores the extension of unconscionable conduct in the special equity in *Garcia*. The third chapter commences with an examination of the prelude to *Garcia*, *Yerkey v Jones*, and then analyses the decision by the High Court of Australia in *Garcia*. The chapter concludes with an examination of level of knowledge required for a *Garcia* special equity claim in order for a transaction to be set aside.

The fourth chapter analyses the impact of the decision by the High Court of Australia in *Garcia* and highlights how the *Garcia* special equity has been increasingly raised as a counter claim to avoid liability by the providers of guarantees when under the influence of strong emotions. Attempts to widen the special classes of relationships under which a court will find a special equity exists are examined in order to answer the question as to whether there is a limit to the types of relationships the courts will recognise for these special equity claims.

The special equity in *Garcia* is examined in this thesis because Kirby J, in his dissenting judgment in that case, viewed the special equity as part of an overarching doctrine of unconscionability. While this view of the law was rejected by the judicial colleagues of Kirby J, the special equity in *Garcia* is seen to be sufficiently closely related to the doctrine of unconscionability to warrant examination in this thesis.

The fifth chapter examines Part IVA of the *Trade Practices Act 1974* (Cth) unconscionability provisions as applicable to finance. This entails a review of the background of the creation of the unconscionability provisions. In addition, the level of knowledge required by a financier in order for a transaction to be set aside under Part IVA is examined. The fact that misleading and deceptive conduct counter claims are often

brought in tandem with unconscionable conduct counter claims against financial institutions trying to enforce a liability, and an analysis of the difference in remedies and which is the better approach, will also be examined in this chapter.

The *Berbatis* decision is studied in the sixth chapter in order to determine the likely future implications for financiers, specifically in regard to determining if there is any recognition by the courts of a widening of the classes of disadvantage that would attract relief under Part IVA of the Act.

In the seventh chapter some specific *Trade Practices Act 1974* (Cth) s 51AC cases are examined, as well as future developments as a result of the December 2008 Senate Report into Unconscionable Conduct under Part IVA and the Government changes (including the Australian Consumer Law).

The need for legislative amendment in light of the High Court rejection of the French J decision in the Federal Court at first instance, in addition to what the impact would be of such a change, is considered in the eighth chapter.

The ninth chapter deals with the recent developments in finance products, considering such products as reverse mortgages, the implications of the National Consumer Credit Code and considers their impact on unconscionable conduct.

The tenth chapter contains the conclusions of this thesis.

1.2 DEFINITION OF UNCONSCIONABILITY

What is meant by the word 'unconscionability'? The word is not defined in the *Trade Practices Act 1974* (Cth). Mahoney JA of the New South Wales Court of Appeal has said that unconscionability is 'better described than defined'.[9] Unconscionability is said to cover a situation where there is found to be 'a want of probity', 'oppression', 'abuse' or 'injustice'.[10]

It needs to be recognised that the overall aim of all equitable principles is the prevention of unconscionable conduct, that is, to prevent another party exercising its rights in an unconscionable manner.[11]

Professor Paul Finn has defined unconscionability as having four possible meanings in Australia.[12]

First, Professor Finn saw it as '… an organising idea informing specific equitable rules and doctrines which do not in terms refer to, or require an explicit finding of, unconscionable conduct.'[13] This application of unconscionable conduct as a principle applied in other equitable rules, is demonstrated in the rules in equity for the time and notice to complete contracts. Professor Finn referred to the comments of Deane and Dawson JJ in *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd*[14] where they had said:

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[9] *Antonovic v Volker* (1986) 7 NSWLR 151, 165.

[10] IJ Hardingham, 'Unconscionable Dealing', Paul Finn (ed), *Essays in Equity*, The Law Book Company Ltd (1985) 25.

[11] Gummow and Hayne JJ in *Australian Broadcasting Corp v Lenah Game Meats Pty Ltd* (2001) 208 CLR 199, 245 [99], who quote with approval French J in *Australian Competition and Consumer Commission v C G Berbatis Holdings Pty Ltd* (2000) 96 FCR 491, 498.

[12] Paul Finn, 'Unconscionable Conduct' (1994) 8 *Journal of Contract Law* 37. Note the Full Federal Court utilises Professor Finn's four meanings of unconscionability in *Australian Competition and Consumer Commission v Samton Holdings Pty Ltd* (2002) 117 FCR 301.

[13] Ibid, 38.

[14] (1989) 166 CLR 623, 654.

> The whole point of equity's intervention in relation to stipulations as to time was that, in the absence of express or implied contractual provision to the contrary, it regarded it as inequitable or unconscionable for a party to a contract to rescind for breach of a time stipulation without having given reasonable warning to the party in default.[15]

Secondly, Professor Finn saw unconscionability as referring to specific equitable doctrines that are designed to prevent an unconscionable insistence on strict legal rights.[16] Examples given included '… estoppel, unilateral mistake, relief against forfeiture and actual undue influence/pressure …'[17] In this regard, Professor Finn provided the examples[18] of *Walton Stores (Interstate) Ltd v Maher*[19] (equitable estoppel), *Stern v McArthur*[20] (forfeiture) and *Taylor v Johnson*[21] (unilateral mistake).

Thirdly, Professor Finn referred to the classic Australian banking guarantee enforcement case of *Amadio*, where the '… link between equitable doctrine and preventing unconscionable behaviour …'[22] was taken one step further, by classifying a doctrine of unconscionable conduct.

Fourthly, Professor Finn recognised unconscionability as a cause of action,[23] giving direct legal effect to a finding that a party has acted

[15] Ibid.

[16] Paul Finn, 'Unconscionable Conduct' (1994) 8 *Journal of Contract Law* 37, 38.

[17] Ibid.

[18] Ibid.

[19] (1988) 164 CLR 387.

[20] (1988) 165 CLR 489. The decision in this forfeiture case was subsequently distinguished by the High Court in *Tanwar Enterprises Pty Ltd v Cauchi* 2003) 217 CLR 315. For relief against forfeiture for a purchase of land, the vendor's conduct has to have caused or contributed to circumstances rendering it unconscionable for the vendor to insist upon its legal rights, before equity would intervene, and then only if it could be shown that it was against conscience for the vendors to terminate the contract.

[21] (1983) 151 CLR 422.

[22] Paul Finn, 'Unconscionable Conduct' (1994) 8 *Journal of Contract Law* 37, 38.

[23] Ibid, 39.

unconscionably[24] ie the behaviour was not governed by a separate doctrine that dictates the cause of action and relief available.[25]

Professor Bryan Horrigan of the University of Canberra saw that:

> Related to or flowing through these four meanings is the notion of 'unconscionability' as a unifying concept or underlying rationale for a variety of equitable doctrines including the doctrine of penalties, economic duress, constructive trusts, restitution or unjust enrichment, and so on. Here, the primary rationale of equity to ensure that someone comes to equity with clean hands and otherwise acts in good conscience translates into a variety of more specific doctrines, not all of which necessarily 'are united by the idea that equity will prevent an unconscionable insistence on strict legal rights' even though they are clearly related to that central idea.[26]

The old equity term of unconscientious bargains (or catching bargains) is a term that also describes present day unconscionable conduct. Meagher, Gummow and Lehane describe the jurisdiction for catching and unconscientious bargains as being a branch of the general equitable jurisdiction in fraud, with the English cases centred in the 19th century whilst in Australia the jurisdiction still flourishes.[27]

Sir Anthony Mason[28] has used this equity term of 'unconscionable bargain' to trace the rise of good faith to become an element of contract law in Australia,[29] having stated of unconscionable bargains, that:

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[24] Ibid. Professor Finn provided an example of the de facto marriage case of *Baumgartner v Baumgartner* (1987) 164 CLR 137.

[25] Paul Finn, 'Unconscionable Conduct' (1994) 8 *Journal of Contract Law* 37, 39. Professor Finn also noted, in regard to this fourth usage, that it was potentially a cause for real uncertainty.

[26] Bryan Horrigan, 'Unconscionability Breaks New Ground – Avoiding and Litigating Unfair Client Conduct after the ACCC Test Cases and Financial Services Reforms' *Deakin Law Review* (2002) 7(1) 73 at 82. The quotation provided by Professor Horrigan is from Professor Paul Finn, 'Unconscionable Conduct' (1994) 8 *Journal of Contract Law* 37, 38.

[27] Meagher, Gummow and Lehane, *Equity Doctrines and Remedies,* Butterworths LexisNexis, (4th ed, 2002), [16-005].

[28] Sir Anthony Mason, 'Contract, Good Faith and Equitable Standards in Fair Dealing' (2000) 116 *Law Quarterly Review* 66.

[29] In regard to the aspect of good faith having become an element of contract law in Australia, subsequent to Sir Anthony Mason's article [ibid], the position in New South Wales was clarified in 2004 by the New South Wales Court of Appeal's decision in *Vodafone Pacific Ltd v Mobile Innovations Ltd* [2004] NSWCA 15 (unreported, 20 February 2004, BC200400571). Giles JA (with whom Sheller JA and Ipp JA agreed) held that an obligation of good faith can be implied

> Here relief is granted when a transaction, considered in the light of the circumstances in which it was entered into, is so unconscionable that it cannot be allowed to stand. What is required is that there be an unconscientious taking advantage of the serious disability.[30]

Throughout this paper, mention will be made of the doctrine of undue influence. In order to 'set the scene' at an early stage of examining how undue influence and unconscionable conduct interact in Australia, the views of Sir Anthony Mason are noted. Sir Anthony stated:

> In Australia, the emergence from the shadows of this ground of equitable relief has relegated the doctrine of undue influence to a position of relative unimportance. Unconscionability and undue influence overlap, the latter being more limited in scope, concerned as it is with the exercise by the contracting party of an independent and voluntary will.[31]

Sir Anthony also observed the changing notion of unconscionability, which, though originally used to define conduct that shocked the conscience, or was unscrupulous or harsh, may now mean conduct that is unfair.[32] Sir Anthony concluded that:

> Already one can detect the balance towards the less strict standard – note the use of the word "unconscientious" and the emphasis given to "equity" and "good conscience" which may develop into synonyms for "good faith" and "fair dealing".[33]

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into a commercial contract '… unless excluded by express provision or because [it became] inconsistent with the terms of the contract ...' [191]. Therefore at present in New South Wales, the position of the law would appear to be that not all commercial contracts have a duty of good faith implied into the contract, but the duty may be implied provided that it is not expressly excluded and is not inconsistent with the terms of the contract.

[30] Sir Anthony Mason, 'Contract, Good Faith and Equitable Standards in Fair Dealing' (2000) 116 *Law Quarterly Review* 66, 87. Sir Anthony referred to cases where the relief was granted to a party suffering from a special disability or disadvantage such the inebriated farmer who was incapable of formulating a rational judgment in *Blomley v Ryan* (1956) 99 CLR 362. In addition, Sir Anthony also referred to expectant heirs as being in this class.

[31] Ibid, 89.

[32] Ibid, 89–90.

[33] Ibid, 90.

Sir Anthony's argument recognised that a duty of good faith and fair dealing are likely already implied by law in all contracts in Australia.[34]

[34] Ibid, 66–67. Reference is made to the conclusion to this effect by Finn J. *Hughes Aircraft Systems International v Airservices Australia* (1997) 76 FCR 151, 191–193; (1997) 146 ALR 1, pp. 36–37, that good faith and fair dealing are implied by law in all contracts. Reference is also made to the New South Wales Court of Appeal decision in *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349, which supports the concept that good faith may form part of a contract.

1.3 CATCHING BARGAINS FOR EXPECTANT HEIRS

One of the principles of equity is that it will seek to relieve a party from an unconscionable bargain. In the early reported English cases the doctrine of catching bargains is reported as being used to cope with a concern for the maintenance and protection of family estates.[35] It was applied to protect potential heirs of estates from the unsavoury actions of moneylenders and the potential dissipation of their inheritance prior to their receiving it.[36] In such an 18th century case, *Earl of Chesterfield v Janssen,*[37] the action of moneylenders was characterised as being unconscionable. Lord Hardwicke LC stated:

> The principle, on which the court has gone in these cases, is an unconscionable bargain, and it being contrary to public convenience to encourage it. Such contracts are generally founded in oppression by taking advantage of the borrower's necessity; which is the general ground of the malignancy of the usury; they are of public mischief by encouraging extravagance of young men.[38]

Meagher, Gummow and Lehane observe that catching bargains for heirs was, by the mid 19th century, an impediment to fair and reasonable transactions. The cause of action did not distinguish between the following. First, it did not distinguish between those expectant heirs who were of mature years as opposed to those who were not of mature years. Secondly, it did not distinguish between those who understood the transaction and were not at the time in financial distress as opposed to those who did not understand the transaction and were not at the time in financial distress. Thirdly, it did not distinguish between those who were

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[35] Robert Lawson, 'Unconscionable Conduct – the Golden Threat', *The Law Society of South Australia Continuing Legal Education Publication*, 6 November 1991, 2.

[36] Meagher, Gummow and Lehane, *Equity Doctrines and Remedies*, Butterworths LexisNexis, (4th ed, 2002), [16-040]. Comment is made that the right to seek relief was extended not only to heirs, but to those who expected or had received remainders in property from an estate.

[37] (1751) 2 Ves Sen 125; (1751) 28 ER 82.

[38] Ibid, 84.

being pressed by the financier to enter the transaction as opposed to those who were not being pressed by the financier to enter the transaction.[39]

This caused a reluctance on the part of lenders to provide funds to heirs against the security over the estate expected to be inherited. This in turn led to the enactment of the English *Sales of Reversions Act 1867*, which provided a level of certainty for parties dealing in good faith, without fraud or unfairness with expectant heirs.[40]

Equity protected parties other than plaintiffs in estate cases, provided that they could establish:

- the parties met on unequal terms;
- the harshness of the bargain; and
- that the bargain was obtained by the stronger party unconscientiously taking advantage of the weaker party.

When these elements were proven by the weaker party, the onus moved to the stronger party to show that their conduct had been reasonable, just and fair. These principles were considered by Kay J in *Fry v Lane.*[41] Kay J reviewed a number of earlier decisions and concluded:

> The result of the decisions is that where a purchase is made from a poor and ignorant man at a considerable undervalue, the vendor having no independent advice, a Court of Equity will set aside the transaction.[42]

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[39] Meagher, Gummow and Lehane, *Equity Doctrines and Remedies*, Butterworths LexisNexis, (4th ed, 2002), [16-045].

[40] Subsequently replaced in England by s 174 of the *Law of Property Act 1925* (Imp), and in various Australian States ie s 37C of the *Conveyancing Act 1919* (NSW) etc. See Meagher, Gummow and Lehane, *Equity Doctrines and Remedies*, Butterworths LexisNexis, (4th ed, 2002), [16-045]-[16-050], which comments that for cases to which this section applies no presumption arrises merely by proof of inadequacy of consideration, and that bargains with heirs would be viewed with the same eyes as for any other allegation of unconscionable conduct.

[41] (1888) 40 Ch D 312.

[42] Ibid, 322.

2. CASE LAW ON UNCONSCIONABILITY

2.1 *WILTON V FARNWORTH*

The first important High Court case dealing with unconscionable conduct was *Wilton v Farnworth*.[43] The High Court was asked to consider an appeal against the decision by Wolff J of the Supreme Court of Western Australia. Wolff J had ordered that a deed signed by a Kalgoorlie miner, Mr Farnworth, in regard to the assignment of his interests in his late wife's estate, be set aside. *Wilton v Farnworth* was interesting as it was an Australian 20th century case that strongly reflected the origins of unconscionability from early English cases of the past two centuries, in which unconscionability was used as relief to protect heirs of estates from the potential dissipation of their inheritance.

The facts of the case dealt with the imprudent actions of Mr Farnworth, who was described as being 'markedly dull-witted and stupid'[44] as well as having '… no education, small intelligence and a history of curious conduct.'[45] In addition, he was completely deaf in one ear and considerably deaf in his other ear. Mr Farnworth was aged in his forties when he married a Mrs Wilton (aged in her mid-sixties – hereafter referred to as Mrs Farnworth) and gave her his savings. Mrs Farnworth subsequently left him, moved to Perth and set up a boarding house business. At the same time Mrs Farnworth was claiming and receiving maintenance from Mr Farnworth. Mrs Farnworth died intestate two years after the marriage and Mr Farnworth inherited 1,800 pounds from her estate.

Mrs Farnworth's son from a former marriage, Mr Wilton, had documents prepared by his solicitor that, as well as applying for a grant of administration for the estate, included a deed for Mr Farnworth to assign to Mr Wilton the whole of his interest in his late wife's estate. Mr Wilton

[43] (1948) 76 CLR 646.

[44] Ibid, 650.

[45] Ibid, 655.

travelled to Kalgoorlie to bring the papers to Mr Farnworth. Rich J of the High Court summarised Wolff J's finding of facts as follows:

(1) The deed and its implications were not explained to Mr Farnworth, and he signed it without knowing that he was making a gift of his share in his late wife's property.
(2) Mr Farnworth did not know the extent of the share of his late wife's estate to which he was entitled, or its value.
(3) Mr Farnworth was bustled into executing the deed with unseemly haste.
(4) A copy of the deed was not left with Mr Farnworth.
(5) Mr Wilton made no attempt to explain the nature of the transaction beyond some reading of the deed. It was extremely doubtful that Mr Farnworth could have heard the reading. Even if Mr Farnworth had heard it, it would have not have been understood by a person with Mr Farnworth's 'mental equipment' and would have been quite a meaningless proceeding.[46]

Rich J noted that it is up to the donor of a gift to prove some substantial reason for setting a transaction aside and that:

> It has always been considered unconscientious to retain the advantage of a voluntary disposition of a large amount of property improvidently made by an alleged donor who did not understand the nature of the transaction and lacked information of material facts such as the nature and extent of the property particularly if made in favour of a donee possessing greater information who nevertheless withheld the facts.[47]

The capabilities of Mr Farnworth and Mr Wilton were unequal, Rich J observed, as Mr Farnworth's hearing deficiency and low intelligence did not allow him to understand the facts of his late wife's estate, his share of it and the impact of the assignment deed that Mr Wilton asked him to sign.[48] Mr Wilton must have been aware of all these factors and that it

[46] Ibid, 655.

[47] Ibid.

[48] Ibid.

was '… an improvident transaction entirely voluntary springing from no sensible motive.'[49] Rich J dismissed the appeal and concluded that the assignment of his property to Mr Wilton 'was neither fair nor righteous and in the view of a court of equity it must be regarded as unconscientious for the defendant to take the gift or retain it.'[50] Dixon and McTiernan JJ agreed with Rich J. Latham CJ also dismissed the appeal and stated that different considerations apply to business transactions as opposed to gifts, which this transaction was.[51]

This 1948 High Court granting of relief due to unconscionability set the scene for its wider usage in the years ahead.

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[49] Ibid.

[50] Ibid.

[51] Ibid, 649.

2.2 *BLOMLEY V RYAN*

The next important High Court case dealing with unconscionable conduct following *Wilton v Farnworth* was *Blomley v Ryan*.[52] The facts of the case revolved around a 78-year-old farmer (the defendant) who was a heavy drinker, poorly educated and rather infirm in health. Ownership of the farmer's sheep / cattle property ('Worrah' situated near Boggabilla NSW) was the subject of the dispute. The defendant had entered into a contract of sale to sell the property for £25,000, after a considerable period of inebriation lasting a number of days. The plaintiff had been aware of the defendant's alcohol and health position, and had produced a bottle of rum for consumption during the contractual negotiations. The court accepted evidence that the property was worth £30,000. The defendant refused to settle the contract and the plaintiff brought an action for specific performance.

Both Taylor J at the first High Court hearing, and then a majority of judges at the Full High Court hearing (Taylor, McTiernan, and Fullagar JJ – Kitto J dissenting), dismissed the plaintiff's action for specific performance and ordered that the contract be rescinded. Fullagar J stated:

> I am satisfied that we have here an example of a thoroughly unconscionable transaction, which no court of equity could possibly enforce itself, or allow to be enforced at law. I would regard specific performance as out of the question, and to let the contract be enforced at law would, in this particular case, be, in effect, to allow the overreaching party to reap the full reward of his inequitable conduct.[53]

Fullagar J described various scenarios where equity's intervention would be justified and saw the defendant's position as qualifying for such intervention when he stated:

> The circumstances adversely affecting a party, which may induce a court of equity either to refuse its aid or to set a transaction aside, are of great variety and can hardly be satisfactorily classified. Among them are poverty or need of any kind, sickness, age, sex, infirmity of

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[52] (1956) 99 CLR 362.

[53] Ibid, 406.

> body or mind, drunkenness, illiteracy or lack of education, lack of assistance or explanation where assistance or explanation is necessary. The common characteristic seems to be that they have the effect of placing one party at a serious disadvantage vis-a-vis the other.[54]

In Kitto J's dissenting judgment he did not disagree that relief would be given against an unconscionable transaction. Kitto J observed that:

> It applies whenever one party to a transaction is at a special disadvantage in dealing with the other party because illness, ignorance, inexperience, impaired faculties, financial need or other circumstances affect his ability to conserve his own interests, and the other party unconscientiously takes advantage of the opportunity thus placed in his hands.[55]

Kitto J, whilst he agreed that equity provided relief against unconscionable conduct, disagreed that the facts of the case attracted the doctrine. It also should be noted that Kitto J's definition of the equitable doctrine of unconscionable conduct was slightly wider in approach than that of Kay J in the English case, *Fry v Lane*. Kitto J saw that the factors constituting a special disadvantage position were broadly extended beyond just ignorance (with no specific mention of poverty by Kitto J).[56] Furthermore, rather than requiring the bargain to be of considerable undervalue, Kitto J used a clearer test. Kitto J saw that there had to be an exploitation of the disadvantage.

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[54] Ibid, 405.

[55] Ibid, 415.

[56] For further discussion on poverty as a potential factor of disadvantage for unconscionable conduct, see Gibbs CJ's discussion in *Commercial Bank of Australia Ltd v Amadio* (1983) 151 CLR 447, 460, where he briefly considered what 'poor' meant in the modern context, for unconscionability. Gibbs CJ referred to *Cresswell v Potter* (1978) 1 WLR 255, 257, where he stated 'Megarry J suggested that in this context "poor" should, under modern conditions, be read as "a member of the lower income group" and "ignorant" as "less highly educated". With all respect, I would need to consider further that proposition before completely accepting it.'

2.3 *COMMERCIAL BANK OF AUSTRALIA LTD V AMADIO*

Commercial Bank of Australia Ltd v Amadio[57] (‘*Amadio*’) was a case where two elderly Italian migrant parents had been asked by their son to execute a mortgage (over their home) and guarantee in favour of a bank to secure an overdraft for the son’s company (the company had been in a joint venture to develop and sell residential property with a finance company, General Credits Ltd, which was a subsidiary of the bank). The parents were unfamiliar with the written English language and were also unaware of the precarious financial position of the son’s company, and that the bank had been dishonouring cheques on the company’s bank account. The son had advised his parents that the guarantee would only cover an amount of $50,000 for a period of six months.

When the bank manager brought the security documents to the parents’ house, the bank manager had relied on the son having previously explained to them the nature of the documents, which in fact covered an unlimited amount of liability and for an unlimited period of time. The documents were signed in front of the bank manager in the kitchen. The bank manager advised that he did correct the father’s belief that the document only covered a six-month time period, but the trial judge held that the father was of the opinion the document was only current for a six-month period. The company then defaulted and the bank took action under the guarantee and mortgage.

The majority of the High Court (Deane, Wilson and Mason JJ, with Dawson J dissenting and Gibbs CJ finding for the Amadios on other grounds) held that the Amadios had been at a special disability due to the weak position they were in compared to the bank. The Amadios had argued that the bank had had knowledge of the difficulties the parents were under, with Mason J emphasising, though, that that was not enough to establish unconscionable conduct. Mason J observed that ‘… the

[57] (1983) 151 CLR 447.

disabling condition or circumstance [must be] one which seriously affects the ability of the innocent party to make a judgment as to his own best interests.'[58] The majority were satisfied that the bank was on notice of the disability that the parents were under, and that the bank did not take adequate steps to ensure that they were provided with independent advice. The majority of the High Court found that the bank's actions constituted unconscionable conduct in procuring the execution of the mortgage / guarantee, and dismissed the appeal from the bank seeking enforcement of its security against the parents.

Gibbs CJ found that there was no taking of advantage by the bank of the Amadios' position of inequality. Instead Gibbs CJ concluded that the son '… did not give his parents a true explanation of the effect of the guarantee, and the bank did not disclose those matters which it should have disclosed.'[59] As relief for misrepresentation was available, Gibbs CJ felt there was no need to resort to the rules for unconscientious bargains. Gibbs CJ therefore found in favour of the Amadios due to misrepresentation of the transaction by both the son and the bank.

Deane J provided a useful distinction between the ingredients of unconscionable conduct and undue influence:

> The equitable principles relating to relief against unconscionable dealing and the principles relating to undue influence are closely related. The two doctrines are, however, distinct. Undue influence, like common law duress, looks to the quality of the consent or assent of the weaker party. ... Unconscionable dealing looks to the conduct of the stronger party in attempting to enforce, or retain the benefit of, a dealing with a person under a special disability in circumstances where it is not consistent with equity or good conscience that he should do so. The adverse circumstances which may constitute a special disability for the purposes of the principles relating to relief against unconscionable dealing may take a wide variety of forms and are not susceptible to being comprehensively [catalogued].[60]

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[58] Ibid, 462.

[59] Ibid, 460.

[60] Ibid, 475. Meagher, Gummow and Lehane, *Equity Doctrines and Remedies*, Butterworths LexisNexis, (4th ed, 2002), [1602], states 'However, there have been cases where the weaker

Mason J expressed disappointment with the Amadios' pleadings in their failure to have argued undue influence in regard to the relationship with their son (the pleadings had argued undue influence by the bank). Mason J said:

> It is to be hoped that the respondents' amended statement of claim does not find its way into the precedent books. It leaves much to be desired. It alleges unconscionable conduct and alternatively undue influence on the part of the bank. It does not, as it might have done, allege undue influence on the part of the respondents' son Vincenzo, with notice on the part of the bank. The findings, and indeed the evidence, contradict or fail to support the alleged case of undue influence on the part of the bank. The critical issue then is whether, in accordance with the principle already explained, the respondents are entitled to relief on the ground of unconscionable conduct.[61]

The decision re-invigorated the doctrine of unconscionability rather than the established course of pleading, undue influence, by making it clear that the doctrine applied to guarantees, and also that aged parents could use the doctrine to have guarantees set aside.[62] Duggan noted this change was not followed in England, where undue influence remained as the usual pleading for guarantor cases.[63]

Janine Pascoe has made the point that it is extremely difficult for an *Amadio* type of unconscionability claim to succeed.[64] An unconscionability claim requires the establishment of two elements.

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party set aside a dealing in reliance both upon the presumption arising from the rules as to undue influence and upon the principles as to unconscientious bargains, citing *Symons v Williams* (1875) 1 VLR (E) 1999; *Dobson v Dobson* (1879) 13 SALR 137; *Robertson v Robertson* [1930] QWN 41; *Alderton v Prudential Assurance Co Ltd* (1993) 41 FCR 435; *Geelong Building Society (in liq) v Thomas* (1996) Aust Contract R 90-068 and cf *Credit Lyonnais Bank Nederland NV v Burch* [1997] 1 All ER 144 at 151.'

[61] Ibid, 464.

[62] Fiona R Burns, 'The Equitable Doctrine of Unconscionable Dealing and the Elderly in Australia' (2003) 29 *Monash University Law Review* 335, 352.

[63] Anthony J Duggan, 'Unconscientious Dealing' in Patrick Parkinson (ed), *The Principles of Equity* The Law Book Company (2nd ed, 2003), [506].

[64] Janine Pascoe, 'Recent developments in the law relating to guarantees of business debts' in Wickrema Weerasooria (ed), *Perspectives on Banking, Finance and Credit Law*, Prospect Media (1999) 107, 109.

The first element to establish unconscionability is that the guarantor was under some kind of special disability when the guarantee was entered into (and courts will generally only find this in an extreme case).

The second element to establish unconscionability is that the lender knew, or ought to have known, of the guarantor's special disability and was unfairly abusing its dominant position in regard to the guarantor (this element is often even more difficult than the first element to establish).[65]

Establishment of both of these elements has proven difficult. Janine Pascoe has stated:

> There is a long list of failed unconscionability cases where the court was unable to discern any evidence of actual or constructive knowledge of a special disability on the part of the guarantor.[66]

This paper subsequently explores the special equity in *Yerkey v Jones* / *Garcia*. There it will be seen that the absence of having to prove that the financier had actual or constructive knowledge of any disability, is an advantage for persons in arguing relief under the special equity, as opposed to *Amadio* unconscionability, as the financier's knowledge of the marriage relationship or other relationship of trust and confidence is the only notice required for relief under a *Yerkey v Jones* / *Garcia* special equity case.

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[65] Mason J in *Amadio* makes it clear [at 467] that for the elements of unconscionable conduct to be established, that as well as one party to a transaction being in a position of special disability and the stronger party being aware of the disability, there must also be a taking of advantage by the stronger party:

> As we have seen, if A, having actual knowledge that B occupies a situation of special disadvantage in relation to an intended transaction, so that B cannot make a judgment as to what is in his own interests, takes unfair advantage of his (A's) superior bargaining power or position by entering into that transaction, his conduct in so doing is unconscionable. And if, instead of having actual knowledge of that situation, A is aware of the possibility that that situation may exist or is aware of facts that would raise that possibility in the mind of any reasonable person, the result will be the same.

[66] Ibid. Pascoe quoted as examples *European Asian of Australia Ltd v Kurland* (1985) 8 NSWLR 192; *ANZ Banking Group v Durnosa* (1995) ANZ ConvR 86 and *Garcia v National Australia Bank Ltd* (1998) 194 CLR 395.

When faced with an *Amadio* type argument for relief by a guarantor, there is no requirement for a financier to seek out details of a possible special disability where there is nothing in the facts before the financier to put it on notice that a special disability may be in existence. This point is clearly expressed by Mahoney JA's comments in the NSW Court of Appeal case of *Younan and Bechara v Beneficial Finance Corporation Ltd*,[67] which dealt with an elderly mother-in-law (Mrs Younan – aged 66, with only a limited education, little understanding of business and no benefit from the transaction) and daughter (Mrs Bechara) guaranteeing the daughter's husband's family property development company (owned by the daughter's husband and his siblings).

Mahoney JA stated:

> However, where it appears that a guarantor, of whatever gender, is "under a special disability" in the transaction and "that disability was sufficiently evident to the stronger party to make it prima facie unfair or 'unconscientious' that he procure, or accept, the weaker party's assent to the impugned transaction in the circumstances in which he procured or accepted it", then relief may be available under the general law: see *Commercial Bank of Australia Ltd v Amadio* (1983) 151 CLR 447 at 474, per Deane J. But I do not think that this Court is bound to hold, or should hold, that there is under the general law a duty upon a creditor, even in the broad sense, to seek out the details of the, [sic] position of a guarantor where there is, on the material in the ordinary course available to it, nothing to indicate "a special disability" or the like.[68]

The case dealt with an unjust (which includes unconscionable under the definition of 'unjust' in s 4) contract claim for relief under s 7 of the *Contracts Review Act 1980* (NSW). Beneficial Finance was not aware that it was dealing with a mother-in-law of one of the company's principals, nor that she was elderly, had little business experience and had

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[67] [1995] ANZ ConvR 213.

[68] Ibid, 217 [15]. For the reference by Mahoney JA to Deane J's decision in *Amadio* at 474, Deane J clarifies (after the circumstances are established that a party to a transaction was under a special disability and the stronger party had knowledge of the disability) that 'Where such circumstances are shown to have existed, an onus is cast upon the stronger party to show that the transaction was fair, just and reasonable …' i.e. the stronger party needs to establish that they were not abusing their dominant position (such as by having insisted upon independent legal advice being provided to the weaker party) to defend successfully against a claim of unconscionable conduct.

no financial benefit in the transaction (nor that she was reliant on the son-in-law for guidance). Beneficial Finance was therefore able to successfully argue that in the absence of being on notice of these facts, there was no duty to make further enquiries as to the possibility of undue influence being present, or that the guarantor may have been taken advantage of.[69] Comparing the facts to Mr and Mrs Amadio, the bank manager had not met and sat down with the mother-in-law guarantor as had happened with the parents in *Amadio*, and thus the financier had not been put on notice of the mother-in-law's position.

[69] Beneficial Finance had received solicitors' certificates of explanations of liability from the guarantors' own solicitor.

2.4 *LOUTH V DIPROSE*

Post *Amadio*, the next important case on unconscionability to be heard by the High Court of Australia was *Louth v Diprose*.[70] This was an unusual case in that the party disadvantaged was a solicitor, and the transaction in question was a real estate transfer which the solicitor himself prepared, and of which he understood the legal implications.

Mr Diprose became infatuated with Mrs Louth during a period stretching from 1981 to 1988 following the breakdown of their respective marriages. Although Mr Diprose followed Mrs Louth when she relocated from Tasmania to South Australia, it was a one-sided relationship. Deane J described it in the following terms:

> There was an extreme contrast between their respective attitudes to one another. For his part, the respondent was "utterly infatuated" by the appellant. He was "completely in love" with her. In contrast, the appellant had become "quite indifferent to" the respondent. The motives for her continued association with him "were of a material nature". His infatuation placed the respondent "in a position of emotional dependence upon the appellant and gave her a position of great influence on his actions and decisions".[71]

Mrs Louth created a crisis situation (where none existed) when she told Mr Diprose that the house she rented in Adelaide from her brother-in-law was going to be sold, when there was no intention to do so. Mrs Louth advised that she did not know what she would do if she was forced to move out and that she would kill herself if that occurred. Despite Mr Diprose being of limited financial means, he used the majority of his assets to purchase the house for her in her own name at a cost to him of $59,206.55. This was after Mrs Louth had rejected offers from Mr Diprose of other various ways to assist her to remain in the property, which fell short of her fully owning the house.

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[70] (1992) 175 CLR 621.

[71] Ibid, 635.

After Mr Diprose's infatuation with Mrs Louth came to an end, he asked her to transfer the title in the house to him. She refused. Proceedings were commenced by Mr Diprose in the Supreme Court of South Australia to recover his gift.[72] The trial judge, King CJ, found that Mrs Louth's conduct was dishonest, smacked of fraud and that she had engaged in unconscionable conduct in procuring and retaining the gift of $59,206.55.[73] On appeal to the Full Court of the Supreme Court of South Australia, the decision was affirmed (Jacobs ACJ and Legoe J, Matheson J dissenting).[74] Mrs Louth then appealed to the High Court (Mason CJ, Deane, Dawson, Gaudron, McHugh, Toohey and Brennan JJ).

Mason CJ commented that he could find no basis on which the High Court should interfere with the primary findings of fact made by King CJ. He noted that:

- there had been a manufacturing of an atmosphere of crisis by Mrs Louth when none existed;
- Mrs Louth's conduct was dishonest and smacked of fraud;
- Mr Diprose was in a position of emotional dependence upon Mrs Louth and she had been in a position to influence him; and
- it was an improvident transaction in light of Mr Diprose's limited financial position.[75]

Mason CJ concluded, in dismissing the appeal, that Mrs Louth's conduct was unconscionable in that it was dishonest and was calculated to induce Mr Diprose to enter into a transaction that was improvident and conferred a great benefit upon her.[76]

[72] *Diprose v Louth (No1)* (1990) 54 SASR 438.

[73] Ibid, 447–448.

[74] *Diprose v Louth (No2)* (1990) 54 SASR 450.

[75] *Diprose v Louth* (1992) 175 CLR 621, 638–639.

[76] Ibid.

Brennan J closely referred back to the High Court's prior decision in *Amadio,*[77] noted that the elements to establish unconscionability were present and agreed with King CJ's finding that Mrs Louth engaged in unconscionable conduct, and thought that the appeal should be dismissed.

Deane J also agreed that the elements of unconscionability were present, and noted that the special disability that Mr Diprose was under did not arise just from his infatuation with Mrs Louth, but also was due to his vulnerability as a result of the false atmosphere of crisis created by the woman he loved being under threat of eviction and suicide.[78] Deane J therefore also favoured dismissing the appeal. Dawson, Gaudron and McHugh JJ agreed with Deane J.

Toohey J, in dissent, rejected the idea that Mr Diprose was a weaker party and that any special situation of disadvantage, such as the unfamiliarity with English in *Amadio* or the lack of intelligence and deafness in *Wilton v Farnworth*, was present.[79] Toohey J saw that Mr Diprose was aware that the relationship with Mrs Louth had little to offer and although he persisted she did not misrepresent her feelings towards him. Mr Diprose was emotionally involved but was not emotionally dependent upon her.[80] Mr Diprose was a legal practitioner and understood the implications of the purchase of the house in Mrs Louth's name. Toohey J concluded:

> That knowledge and his clear appreciation of the consequences of what he was doing run directly counter to a conclusion that he was suffering from some special disability or was placed in some special

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[77] Ibid, 626–627. Brennan J listed from *Amadio* three factors in order to establish unconscionable conduct:

(1) a relationship between the parties which, to the knowledge of the donee, places the donor at a special disadvantage vis-a-vis the donee;

(2) the donee's unconscientious exploitation of the donor's disadvantage; and

(3) the consequent overbearing of the will of the donor whereby the donor is unable to make a worthwhile judgment as to what is in his or her best interest.

[78] Ibid, 638.

[79] Ibid, 654.

[80] Ibid, 655.

situation of disadvantage.[81]

Despite Toohey J's dissent, the majority of the High Court found in favour of Mr Diprose, and this provided direction to future courts that 'romantic' relationships such as the one between Mr Diprose and Mrs Louth fall within the special type of relationship needed to attract *Amadio* type unconscionability. The facts of the case and type of relationship are so unusual, though, that the precedent value of this case might be questioned.

[81] Ibid.

2.5 ENGLISH CASES

2.5.1 LLOYDS BANK V BUNDY

The 19th century development in English equity for catching bargains for expectant heirs (discussed in an earlier chapter) was referred to by Lord Denning MR of the English Court of Appeal in *Lloyds Bank v Bundy*[82] (*Bundy*). Lord Denning in *Bundy* attempted to relay a doctrine of unconscionability applicable at the common law and in equity.

Lord Denning considered the position of an elderly farmer who had provided mortgage guarantees to support the bank borrowings of his son's business, which was not trading well. The bank did not require the farmer to obtain independent advice. The farmer had always relied upon the bank for advice. The other two judges, Cairns LJ and Sir Eric Sachs, held that the guarantee and mortgage should be set aside due to undue influence. Lord Denning, however, saw the need for the law to take a broader view of cases such as this. Lord Denning stated:

> There are cases in our books in which the courts will set aside a contract, or a transfer of property, when the parties have not met on equal terms, when the one is so strong in bargaining power and the other so weak that, as a matter of common fairness, it is not right that the strong should be allowed to push the weak to the wall. Hitherto those exceptional cases have been treated each as a separate category in itself. But I think the time has come when we should seek to find a principle to unite them. I put on one side contracts or transactions which are voidable for fraud or misrepresentation or mistake. All those are governed by settled principles. I go only to those where there has been inequality of bargaining power, such as to merit the intervention of the court.[83]

Lord Denning attempted to set down a general doctrine of unconscionability based on five categories as follows.

[82] [1975] QB 326.

[83] Ibid, 336–337.

The first category of Lord Denning was duress of goods. Lord Denning provided the following example of what he meant:

> A typical case is when a man is in a strong bargaining position by being in possession of the goods of another by virtue of a legal right, such as, by way of pawn or pledge or taken in distress.[84]

The second category of Lord Denning was unconscionable transaction. Lord Denning explained it as:

> A man is so placed as to be in need of special care and protection and yet his weakness is exploited by another far stronger than himself so as to get his property at a gross undervalue.[85]

In this regard Lord Denning gave the case of *Fry v Lane* dealing with expectant heirs as an example of this category of unconscionability. Lord Denning noted that this second category is said to extend to all cases where an unfair advantage has been gained by an unconscientious use of power by a stronger party against a weaker.[86]

The third category of Lord Denning was undue influence. Lord Denning referred to the general principle on undue influence stated by Lord Chelmsford LC in *Tate v Williamson*: [87]

> Wherever two persons stand in such a relation that, while it continues, confidence is necessarily reposed by one, and the influence which naturally grows out of that confidence is possessed by the other, and this confidence is abused, or the influence is exerted to obtain an advantage at the expense of the confiding party, the person so availing himself of his position will not be permitted to retain the advantage, although the transaction could not have been impeached if no such confidential relation had existed.

The fourth category of Lord Denning was undue pressure. Lord Denning referred to an example of undue pressure in *Williams v Bayley*:[88]

> … where a son forged his father's name to a promissory note and,

[84] Ibid, 337.

[85] Ibid.

[86] Ibid, 337–338.

[87] (1866) LR 2 Ch App 55, 61.

[88] (1866) LR 1 HL 200.

> by means of it, raised money from the bank of which they were both customers. The bank said to the father, in effect: "Take your choice – give us security for your son's debt. If you do take that on yourself, then it will all go smoothly: if you do not, we shall be bound to exercise pressure." Thereupon the father charged his property to the bank with payment of the note. The House of Lords held that the charge was invalid because of undue pressure exerted by the bank.[89]

Lord Denning also detailed as an example of undue pressure the scenario where one party insists upon an unfair advantage to which the other party has no option but to submit. The example was a builder who asked to be paid by his employer for moneys properly due, where the employer refused to pay unless an added advantage was given to the employer.[90]

The fifth category of Lord Denning was salvage agreements. This category of unconscionable conduct was summarised by Lord Denning as follows:

> When a vessel is in danger of sinking and seeks help, the rescuer is in a strong bargaining position. The vessel in distress is in urgent need. The parties cannot be truly said to be on equal terms. The Court of Admiralty have always recognised that fact.[91]

Lord Denning concluded that:

> Gathering all together, I would suggest that through all these instances there runs a single thread. They rest on "inequality of bargaining power". By virtue of it, the English law gives relief to one who, without independent advice, enters into a contract upon terms which are very unfair or transfers property for a consideration which is grossly inadequate, when his bargaining power is grievously impaired by reason of his own needs or desires, or by his own ignorance or infirmity, coupled with undue influences or pressures brought to bear on him by or for the benefit of the other.[92]

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[89] [1975] QB 326, 338.

[90] Ibid, 338 referring to *Ormes v Beadel* (1860) 2 Giff. 166, 174 (reversed on another ground, 2 De GF & J 333) and *D & C Builders Ltd v Rees* [1966] 2 QB 617. Undue pressure is not explored further in this paper, as it is essentially classified in Australia as a fraud in equity, outside the scope of the thesis topic. For further discussion on pressure as fraud, see Meagher, Gummow and Lehane, *Equity Doctrines and Remedies*, Butterworths LexisNexis, (4th ed, 2002), [1210] – [1217].

[91] Ibid, 338–339. Lord Denning's categorisation of salvage agreements as an area that may attract the doctrine of unconscionability is not explored further in this thesis, as it has no practical connection with financial services.

[92] Ibid, 339.

2.5.2 THE REJECTION OF LORD DENNING'S APPROACH

Subsequent English courts were not prepared to accept Lord Denning's approach. Lord Scarman, when he delivered the unanimous decision in the House of Lords in *National Westminster Bank plc v Morgan*,[93] rejected the approach and stated:

> The doctrine of undue influence has been sufficiently developed not to need the support of a principle which by its formulation in the language of the law of contract is not appropriate to cover transactions of gift where there is no bargain. The fact of an unequal bargain will, of course, be a relevant feature in some cases of undue influence. But it can never become an appropriate basis of principle of an equitable doctrine which is concerned with transactions "not to be reasonably accounted for on the ground of friendship, relationship, charity, or other ordinary motives on which ordinary men act ..." (see *Allcard v Skinner* (1887) 36 Ch D 145 at 185, [1886-90] All ER Rep 90 at 100-101 per Lindley LJ).[94]

Lord Scarman noted that it was the role of parliament to legislate on providing a general doctrine, should there be a need. Lord Scarman then quoted various English Acts already in existence (in 1985), which guarded against the mischief outlined by Lord Denning, and stated 'I doubt whether the courts should assume the burden of formulating further restrictions.'[95]

Lord Denning's approach has also been rejected in the Australian courts in *Amadio*.[96]

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[93] [1985] AC 686.

[94] [1985] AC 686 at 708.

[95] Ibid.

[96] *Commercial Bank of Australia Ltd. v Amadio* (1983) 151 CLR 447, 462–463, Mason J.

2.5.3 BARCLAYS BANK PLC V O'BRIEN

The 1994 decision of the House of Lords in *Barclays Bank plc v O'Brien*[97] (*O'Brien*) sets out '… the definitive legal principles to be applied at English law in the context of a vulnerable surety seeking to set aside a transaction entered with a lender.'[98] The case of *O'Brien* dealt with a wife who had given security over a home owned jointly with her husband, to secure a guarantee provided to Barclays Bank by the husband to secure his company's business debts. The wife did not receive an independent explanation of her liability.

The wife was ultimately successful in avoiding enforcement of the charge she had provided. Her success was based on undue influence and the bank's failure to take steps to ensure she was informed of the details of the transaction she had entered into at her husband's request. Although the case dealt essentially with undue influence, the decision of Lord Browne-Wilkinson (with whom the other four Law Lords agreed), set down some important concepts in equity for the English position on undue influence, which would also apply to the doctrine of unconscionability.

First, his Lordship rejected any concept that wives should be allowed a special equity ('I can find no basis in principle for affording special protection to a limited class in relation to one type of transaction only').[99] The English position on undue influence looks at all types of vulnerable guarantors (not just spouses), and is gender-neutral.

Secondly, his Lordship '… brought the concepts of constructive notice and "on inquiry" into the realm of surety law in the UK.'[100]

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[97] [1994] 1 AC 180.

[98] Janine Pascoe, 'Wives, Lenders and Guarantees – New Law in the UK and Lessons for Australia' (2002) 17(8) *Australian Banking and Finance Law Bulletin* 117, 118.

[99] [1994] 1 AC 180, 195.

[100] Janine Pascoe, 'Wives, Lenders and Guarantees – New Law in the UK and Lessons for Australia' (2002) 17(8) *Australian Banking and Finance Law Bulletin* 117. Lord Browne-Wilkinson states 'Therefore, in my judgment a creditor is put on inquiry when a wife offers to

Thirdly, his Lordship enunciated certain criteria for banks to follow, in order to avoid being 'fixed with constructive notice' and thus risking having their security put aside.

Lord Browne-Wilkinson stated:

> But in my judgment the creditor, in order to avoid being fixed with constructive notice, can reasonably be expected to take steps to bring home to the wife the risk she is running by standing as surety and to advise her to take independent advice. As to past transactions, it will depend on the facts of each case whether the steps taken by the creditor satisfy this test. However for the future in my judgment a creditor will have satisfied these requirements if it insists that the wife attend a private meeting (in the absence of the husband) with a representative of the creditor at which she is told of the extent of her liability as surety, warned of the risk she is running and urged to take independent legal advice. If these steps are taken in my judgment the creditor will have taken such reasonable steps as are necessary to preclude a subsequent claim that it had constructive notice of the wife's rights.[101]

Janine Pascoe has commented that the advice of Lord Browne-Wilkinson was in too general terms for it to be of much use to financiers, particularly in regard to the contents of the legal advice and the action that should be taken in the event the wife declines to obtain legal advice.[102]

Lord Browne-Wilkinson's criteria have been expanded in *Royal Bank of Scotland v Etridge (No 2)*[103] (*Etridge*).

O'Brien has not been followed by the Australian courts (*Garcia* though reaffirmed that special equity still exists in Australia, as will be seen later in

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stand surety for her husband's debts by the combination of two factors: (a) the transaction is on its face not to the financial advantage of the wife; and (b) there is a substantial risk in transactions of that kind that, in procuring the wife to act as surety, the husband has committed a legal or equitable wrong that entitles the wife to set aside the transaction.' [1994] 1 AC 180, 196.

[101] [1994] 1 AC 180, 196.

[102] Janine Pascoe, 'Wives, Lenders and Guarantees – New Law in the UK and Lessons for Australia' (2002) 17(8) *Australian Banking and Finance Law Bulletin* 117, 119.

[103] [2002] 2 AC 773.

this paper). Sir Anthony Mason was quoted[104] in *Garcia* '… [t]he plethora of cases may suggest that all is not well with the *O'Brien* principle …'[105] Further, this broad usage, in England of undue influence to avoid enforcement of charges in England has not been followed in Australia.

[104] Sir Anthony Mason, 'The Impact of Equitable Doctrine on the Law of Contract' (1998) 27 *Anglo-American Law Review* 1, 15.

[105] (1998) 194 CLR 395, 402 [15] (Gaudron, McHugh, Gummow and Hayne JJ).

3. THE *GARCIA* CASE

3.1 THE DECISION IN *YERKEY V JONES* – PRELUDE TO *GARCIA*

The 1939 Australian High Court case of *Yerkey v Jones*[106] concerned a wife (Mrs Jones) who provided a guarantee and mortgage over land owned by her, in order to secure vendor finance for her husband to purchase a poultry farm. The husband was a clerk who had no prior farm experience. His wife did not trust his business sense, however she reluctantly went along with his request to provide security. The financier's solicitor explained the documentation to her. The husband defaulted on the debt and the security from Mrs Jones was called up. At first instance before the South Australian Supreme Court (Napier J),[107] Mrs Jones succeeded in her claim that she had been subject to undue influence (as well as that unilateral mistake had applied).

Mrs Jones' claim was rejected in the High Court by Latham CJ due to a lack of evidence to support the claim. Latham CJ noted that there was evidence that the documentation was executed in the office of the financier's solicitor and that the solicitor had advised that he had explained the documentation to Mrs Jones. His Honour observed that Mrs Jones had agreed that the solicitor had provided an explanation but that she could not remember what was said.

Latham CJ concluded that:

> Accordingly the case for Mrs. Jones must depend upon some special rules applying to a wife who becomes a surety for her husband. The rule relied upon is a rather vague and indefinite survival from the days when a married woman was almost incapable in law and when the courts of equity gave her special protection in relation to transactions affecting her separate property…There are no corresponding features in the present case.[108]

[106] (1939) 63 CLR 649.

[107] *Yerkey v Jones* [1938] SASR 201.

[108] (1939) 63 CLR 649, 664.

Rich J took the approach that the facts were 'not established which would as between him [the husband] and her [the wife] create an equity sufficient to avoid the dealing if it had been confined to themselves …'.[109] Rich J also saw that the steps taken to explain the security documentation were sufficient and that there was no evidence to show that the wife had assumed that the financier's solicitors who explained the security documents to her had acted on her own behalf (as opposed to the fact that the solicitor acted on the financier's behalf).

Dixon J first looked at the undue influence argument raised by the wife and summarised the position as follows (referred to in subsequent cases as the first limb in *Yerkey v Jones*):

> … if a married women's consent to become a surety for her husband's debt is procured by the husband and without understanding its effect in essential respects she executes an instrument of suretyship which the creditor accepts without dealing directly with her personally, she has a prima-facie right to have it set aside.[110]

Given that the wife did not in any case trust her husband's decision to purchase the farm, she was not deluded, and there was no evidence that she was coerced or that her will was overborne.

By way of contrast, to the approach of Latham CJ and Rich J, Dixon J proceeded to explore English cases over the previous two centuries in which equity had provided relief to married women. Dixon J held that married women guarantors when acting as surety for the debt of their spouse or their spouse's business were in a special class which equity should assist.

Dixon J reasoned:

> If undue influence in the full sense is not made out but the elements of pressure, surprise, misrepresentation or some or one of them combine with or cause a misunderstanding or failure to understand the document or transaction, the final question must be whether the

[109] Ibid, 665.

[110] Ibid, 683.

> grounds upon which the creditor believed that the document was fairly obtained and executed by a woman sufficiently understanding its purport and effect were such that it would be inequitable to fix the creditor with the consequences of the husband's improper or unfair dealing with his wife.[111]

Thus for equity to provide this special relief, four elements needed to be established. The first element is that the husband obtained the wife's consent. The second element is that the wife had not understood the nature and effect of the transaction. The third element is that the financier took the security without dealing with the wife. The fourth element was that there was an absence of any explanation or independent advice.

Dixon J looked at the aspect of the financier's solicitor's explanation of the mortgage and the guarantee to Mrs Jones. Dixon J's analysis on this point differed from the trial judge (Napier J). Napier J had concluded that Mrs Jones had not understood the explanation provided by the solicitor.[112] Napier J also dismissed the relevance of the solicitor's explanation, as Mrs Jones had erroneously supposed that the financier's solicitors were acting in her interests as well as in the interests of the vendors, and she was led to do so by the vendors.[113] This led Napier J to provide equitable relief to Mrs Jones from enforcement of her security. Dixon J concluded that the key aspect was not whether or not Mrs Jones now claimed not to have understood the solicitor's explanation, but the fact that the solicitor's explanation was provided, and that:

> … the solicitor had no reason to suppose that she did not grasp the essentials of the transaction and on reasonable grounds the appellants and their solicitor believed that she had understood the substantial effect in all material respects of the obligations she was undertaking. In my opinion the respondent failed to make out a case which under the principles I have discussed entitled her to equitable relief.[114]

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[111] Ibid, 686.

[112] *Yerkey v Jones* [1938] SASR 201, 213.

[113] Ibid, 209.

[114] (1939) 63 CLR 649, 690.

Although Mrs Jones was not entitled to equitable relief, the reasoning of Dixon J remained important in his clear defining of the special equity that the courts would be prepared to provide to wives.

3.2 AN EXAMINATION OF *GARCIA*

3.2.1 OVERVIEW

In *Garcia v National Australia Bank Limited*[115] (*Garcia*), the majority judgment of Gaudron, McHugh, Gummow and Hayne JJ of the High Court established that a married woman who had been a surety for her husband could rely on the reasoning of Dixon J in the High Court case of *Yerkey v Jones*. The High Court reaffirmed that *Yerkey v Jones* remained good law.

The facts

Mrs Garcia (aged 52 at the time the case first went to trial) had a tertiary education (Diploma in Physiotherapy) and owned her own physiotherapy practice through a structure involving companies and trusts. The trial judge described her as a capable and presentable professional. Her husband operated a gold bullion trading business, Citizens Gold Exchange Pty Ltd. In 1979 Mrs Garcia and her husband provided an all-moneys mortgage over their Wahroonga family home (the property was originally owned by Mrs Garcia in her own name alone, but was transferred to their joint names for nil consideration to enable a building society loan to be obtained in order to build the family residence). The mortgage initially secured a $5,000 overdraft to her husband for his business, and then subsequently a $10,000 personal loan made to both of them. By 1985 Mrs Garcia advised that she believed all the liability under the mortgage had been repaid (with the bank retaining the mortgage document).

During the period 1985 to 1987, Mr and Mrs Garcia provided a series of guarantees (the last one being for $270,000 in 1987) to support Mr Garcia's company's borrowings to the National Australia Bank Ltd ('NAB'). Despite the fact that Mrs Garcia was a director and shareholder of the company, the trial judge held that the company was under the complete control of Mr Garcia (as Mr Garcia insisted that all the business decisions be left to him,

[115] (1998) 194 CLR 395.

Mrs Garcia did not do any work for the company, and allegations that her signature was forged on a number of documents lodged with ASIC were not defended).

In 1989 the company was wound up and debts were left outstanding to the NAB (Mr Garcia having been arrested and charged earlier in the year in Queensland). Mrs Garcia and her husband had separated in 1988 and were divorced in November 1989, and it appeared that Mrs Garcia received the family home. Mrs Garcia then sought from the Supreme Court of New South Wales a declaration that the mortgage and guarantees were void. The NAB then served a demand on Mrs Garcia for $327,189.69 under the 1987 guarantee and the 1979 mortgage. The NAB lodged a defence to Mrs Garcia's action and a cross claim judgment pursuant to the demand made and possession of the Wahroonga home was also sought. Mrs Garcia's statement of claim (and the NAB's cross claim) were amended on numerous occasions prior to the hearing, with Mrs Garcia's claim finally being based on *Amadio* type unconscionability, undue influence, *Yerkey v Jones* special equity and the *Contracts Review Act 1980* (NSW).

The decision of the trial judge

The case[116] came before Young J of the Supreme Court of New South Wales, and he rejected the *Amadio* unconscionability argument. Young J was of the view that the bank had not been put on notice of any circumstances that required the bank to take special care to ensure that Mrs Garcia had been informed of her legal position prior to her having provided the security. Young J stated:

> … what in fact occurred was that an intelligent articulate lady with a professional position called at the Bank, appeared to be voluntarily signing a guarantee in respect of an account of which she was a director of the company concerned, and there was nothing to give the Bank even suspicion. If one applies the test of Deane J in *Amadio's* case at 474, there was nothing to show that the disability of the plaintiff was sufficiently evidenced to the Bank to make it unconscientious that it accept the plaintiff's assent to the impugned

[116] *Garcia v National Australia Bank Ltd* (1993) NSW ConvR 55-662.

> transaction.[117]

Young J also rejected the application for relief under s 7 of the *Contracts Review Act*, as there was no evidence of any substantive injustice. He commented that the existence of procedural injustice alone will not generally render a contract unjust under the Act, as established in *West v AGC (Advances) Ltd.*[118] Young J stated:

> However, the mere fact that unjust consequences flow from a contract is insufficient. It does not matter whether the contract is the causa sine qua non of an unjust consequence or even the causa causans. Unless one can see that there is some substantive injustice in the contract itself or there was procedural injustice leading up to the making of the contract the *Contracts Review Act* is of no assistance.[119]

Young J did not make a positive finding that Mrs Garcia's execution of the 1987 guarantee had been procured by actual undue influence. He did however find that 'the husband pressured the wife to sign the document'[120] and that:

> She appeared to have done so because her husband consistently pointed out what a fool she was in commercial matters whereas he was an expert, and trying to save her marriage.[121]

Young J then considered the argument of Mrs Garcia that she was entitled to the special equitable relief available to her as a wife under *Yerkey v Jones*. From the facts of the case the four necessary elements for establishment of equitable relief under *Yerkey v Jones* were apparent. They were as follows:

1. The husband obtained the wife's consent.
2. The wife had not understood the nature and effect of the transaction.
3. The financier took the security without dealing with the wife.
4. There was no explanation or independent advice.

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[117] Ibid, 59,791 [37].

[118] (1986) 5 NSWLR 610, 620.

[119] *Garcia v National Australia Bank Ltd* (1993) NSW ConvR 55-662, 59,792 [41].

[120] Ibid, 59,789 [31].

[121] Ibid.

Young J then undertook an extensive examination of the reasons why *Yerkey v Jones* could also apply when the security provided was to benefit a company, and not specifically benefiting the spouse (eg in *Yerkey v Jones*, Mrs Jones provided security in order to secure her husband's liabilities):

> In *Re Halstead; ex p Westpac Banking Corp* (1991) 31 FCR 337, Heerey J said at 353 that even if the wife was a shareholder in the company if she was not apparently involved in the day to day running of the company in the absence of evidence that she had a direct or indirect interest in the debt, she could rely on the principle in *Yerkey v Jones*.[122]

Young J then dealt with the defence's argument that the principle in *Yerkey v Jones* has been replaced by the *Amadio* unconscionability principles. Young J made it clear that he did not think that it was his place to find that *Yerkey v Jones* had been subsumed into the *Amadio* principle. Young J stated:

> It seems to me that the Court of Appeal has taken the view that *Yerkey v Jones* is until the High Court decides otherwise, a separate principle and I should maintain that point of view. In *Warburton v Whiteley* [1989] NSW ConvR 55-453 at 58,287, Kirby P thought that the rule was anomalous, anachronistic and inappropriate, yet recognized that the Court of Appeal must still follow it until the High Court decided otherwise.[123]

Young J held that Mrs Garcia was entitled to equitable relief under the *Yerkey v Jones* principle. He dismissed the NAB's cross claim for judgment and possession of the Wahroonga home, and ordered that the guarantees be set aside.

The appeal to the New South Wales Court of Appeal

The NAB appealed successfully to the Supreme Court of New South Wales Court of Appeal.[124] Sheller JA held (and Mahoney P and Meagher JA agreed) that *Yerkey v Jones* was no longer good law in NSW, and that the principle had been subsumed by *Amadio*. Sheller JA used as justification for his decision an analysis of case law post *Yerkey v Jones*, and particularly

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[122] Ibid, 59,787 [13].

[123] Ibid, 59,786 [11].

[124] *National Australia Bank Ltd v Garcia* (1996) 39 NSWLR 577.

referred to the then-recent New South Wales Court of Appeal case of *Akins v National Australia Bank*,[125] where Clarke JA stated:

> Indeed, if relief is available on either the ground articulated in *Yerkey* or the ground in *Commercial Bank of Australia v Amadio* there is a theoretical possibility that conduct found not to be unconscionable (or unconscientious) could nevertheless provide grounds for relief under *Yerkey*. This is, in my view, quite inconsistent with the principles which inform equitable relief.[126]

Sheller JA also made reference to *European Asian Of Australia Ltd v Kurland,*[127] where Rogers J of the Supreme Court of New South Wales had voiced in 1985 a strong opinion against the special equity principle, when he stated that:

> In more recent times it has been acknowledged that the concept appealed to, in relation to a married woman, is at best a survivor from the days when a married woman was almost incapable in law. I feel compelled to say that in the year 1985 it seems anachronistic to be told that being a female and a wife is, by itself, a sufficient qualification to enrol in the class of persons suffering a special disadvantage. However, counsel for Mrs Kurland submitted that the iron grip of precedent requires me to submit to such a finding. Were this to be correct, it would affix a badge of shame to this branch of the law. In my opinion, stated in the extreme form embraced by counsel, the proposition is not correct but, nonetheless, it has sufficient claim to accuracy to require a review of this branch of the law so as to bring it into conformity with current thinking and standards. That being a female spouse should place a person shoulder to shoulder with the sick, the ignorant and the impaired is not to be tolerated.[128]

The appeal to the High Court

Mrs Garcia was then successful in obtaining leave to appeal the decision to the High Court of Australia.[129]

The issues before the High Court, as seen by Kirby J, were threefold. The first issue was whether *Yerkey v Jones* was still good law in Australia (and thus the question of whether Dixon J's decision was still binding). The

[125] (1994) 34 NSWLR 155.

[126] Ibid, 170.

[127] (1985) 8 NSWLR 192.

[128] Ibid, 200.

[129] *Garcia v National Australia Bank Ltd* (1998) 194 CLR 395.

second issue was the question if *Amadio* had subsumed the *Yerkey v Jones* principle. The third issue was, if Dixon J's decision was no longer law or had been absorbed within general equitable principles, '… does the exposition of such doctrine in *Amadio* sufficiently meet the particular problem of sureties who are emotionally vulnerable or dependent on the debtor?'[130]

The High Court majority (Gaudron, McHugh, Gummow and Hayne JJ) concluded that Dixon J's principle of special equity given to married women which he had discussed in obiter in *Yerkey v Jones,* was still good law in Australia. They stated '… that the principles spoken of by Dixon J in *Yerkey v Jones* are simply particular applications of accepted equitable principles which have as much application today as they did then.'[131]

The majority of the High Court, with Kirby J in dissent, held that it was not correct to conclude that *Amadio* had subsumed the decision in *Yerkey v Jones.* Their Honours stated:

> It was submitted that *Yerkey v Jones* has been overruled by *Amadio* or that the principles applied in *Yerkey v Jones* had been subsumed in principles applied in *Amadio*. There are several answers to this contention. First, there is nothing in *Amadio* that suggests that it was intended to overrule *Yerkey v Jones* or to subsume the rules applied there in some broader principle enunciated in *Amadio*. Secondly, far from anything said in *Amadio* suggesting that it was intended to mark out the boundaries of the whole field of unconscionable conduct, as Mason J said [(1983) 151 CLR 447 at 461]: "It goes almost without saying that it is impossible to describe definitively all the situations in which relief will be granted on the ground of unconscionable conduct." Thirdly, *Amadio* was a case of unconscionable conduct very different from the cases considered in *Yerkey v Jones*.[132]

By way of contrast, Kirby J reasoned:

> The majority in their reasons have shown that *Amadio* was not intended, or aptly expressed, to cover the whole field of unconscionable conduct. The fact that the *Amadio* principle is

[130] Ibid, 413 [49].

[131] Ibid, 403 [18].

[132] Ibid, 407–408 [27]-[30] (Gaudron, McHugh, Gummow and Hayne JJ).

> incapable of protecting volunteers who, because of the vulnerability of their personal relations with a borrower, and the lack of advice and information, bind themselves to a potentially prejudicial transaction, has been demonstrated several times. Suggestions, including some that I have made myself, that *Amadio* covered the field of available equitable relief must now be regarded as incorrect. There is, it seems to me, no difficulty in recognising that the same set of facts might give rise to two types of liability in the credit provider: one coming from the credit provider's own wrongful conduct and the other from the credit provider's notice of someone else's wrongful conduct. However, the two are analytically distinct. Constructive notice should not be sufficient for unconscientious dealing.[133]

Gaudron, McHugh, Gummow and Hayne JJ in *Garcia* explained that the rationale in *Yerkey v Jones* was based on a relationship of trust and confidence between the parties, rather than any mere disadvantage being suffered by married women. This relationship of trust and confidence may cause the disadvantaged party to suffer from a lack of information that pertained to the transaction.[134]

In *Garcia*, Mrs Garcia had understood that she was signing a limited guarantee to secure her husband's foreign exchange / gold broking business Citizens Gold Bullion Exchange Pty Ltd. But the NAB had not explained to her that the guarantee was not limited to the company's overdraft, plus that her existing all-moneys mortgage over the family home supported the guarantee. The NAB had also not insisted that she seek independent legal advice.

There were two other keys factors in regard to Mrs Garcia's provision of security. The first key factor was that she had not received a benefit for providing the security – the High Court accepted the trial judge's view that the transaction was voluntary, in that Mrs Garcia did not receive any gain from the facilities she guaranteed, nor did she benefit from her husband's business. The second key factor was that the High Court accepted the trial judge's finding that her husband had pressured her into signing the guarantee

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[133] Ibid, 430 [72].

[134] See Daniel Clough, 'Trends in the Law of Unconscionability' (1999) 18 *Australian Bar Review* 34, 34.

documents and belittled her when she queried the documents, and that Mr Garcia had lied to her that his dealings with the bank were safe as there was gold held to support them.

Given that:

- Mrs Garcia did not understand the transaction;
- she was a volunteer;
- the bank understood that, as a wife, Mrs Garcia would repose trust and confidence in her husband, and therefore understood that he may not have accurately explained the effect of the transaction to his wife; and
- the lender did not take steps to explain the transaction to the wife by ensuring that she obtained independent advice,

Mrs Garcia was successful in her appeal to the High Court and established that she was entitled to the *Yerkey v Jones* special equity relief. The security that Mrs Garcia had provided for her husband's company was set aside.

The dissenting approach of Kirby J

Kirby J in dissent rejected what he described as the 1930's stereotyping of relationships from *Yerkey v Jones* being limited to married couples.[135] His Honour explored types of relationships other than marriage that may put a credit provider on inquiry that a surety has a level of trust and confidence existing in the debtor. These other types of relationships included a relationship involving co-habitation, as may:

> … de facto marriage, or long term relationships with respect to sureties and borrowers of either sex. So may other information as to the relationships of the parties which comes to the notice of the credit provider or which it, out of prudence, requests and obtains. A rudimentary question as to the address of the parties and the discovery that they are (or have been) co-habitees would ordinarily be enough to set alarm bells ringing. This is because of the added vulnerability which co-habitation may bring to a relationship, otherwise unexplained, under which one person guarantees the debt of another by assuming their risks if things go wrong.[136]

[135] (1998) 194 CLR 395, 429 [68].

[136] Ibid, 433 [76].

Kirby J still found in favour of Mrs Garcia, but relied upon a recasting of the *Amadio* principles for emotionally dependant sureties, modified in line with the analysis used by Lord Browne-Wilkinson in the House of Lords decision in *Barclays Bank plc v O'Brien*[137] (*O'Brien*) (which had already been discounted by the majority in *Garcia*), rather than any reliance on a special equity existing only for wives. Kirby J had concluded that Mr Garcia had misrepresented the transaction to Mrs Garcia, there was constructive notice to the bank of Mrs Garcia's potential vulnerability and the bank had not taken steps to ensure that Mrs Garcia had entered the obligation freely and with knowledge of the relevant facts.

Kirby J then suggested an approach that should be followed post Lord Browne-Wilkinson's decision in *O'Brien.*[138] Kirby J's view was that this approach should be adopted where a financier knows (or ought to know) that security is being offered from a surety in an emotionally dependant relationship with the debtor. In that situation, the surety's obligations under the security would be enforceable unless the obligation was obtained from the surety as a result of undue influence, misrepresentation or from another legal wrong of the debtor.

In the event that any of the above three factors apply, then unless the financier had taken reasonable steps to satisfy itself that the surety entered the obligation freely and in knowledge of the true facts, then the security would be unenforceable.

The reasonable steps that a financier must have taken are clarified as being to warn the surety, at a meeting from which the debtor is absent, of the amount

[137] [1994] 1AC 180.

[138] Mrs Garcia had raised in her notice of appeal to the High Court that, as an alternative to reliance on *Yerkey v Jones*, she was entitled to equitable relief on the basis of *O'Brien*. The Court of Appeal had already rejected that approach on the basis that *Amadio* was the principle source of relief for Australian courts.

of the surety's potential liability, the risks involved to the surety's own interests, and to advise the surety to take independent legal advice.[139]

Kirby J then noted in regard to this new approach:

> In this way, equity is capable of affording a principle for relief in cases of this kind which (1) is expressed in non-discriminatory terms; (2) is addressed to the real causes of the vulnerability; and (3) recognises the credit provider's superior powers to insist that volunteers in a vulnerable position are afforded access to relevant information and, where necessary, independent advice. The House of Lords concluded in this general way in *O'Brien*. This Court should follow and adopt that decision. It is applicable to the circumstances of this case. The Court can properly do so without procedural unfairness to the Bank. The point was reserved and argued below. It was also debated at some length on the hearing of this appeal. No different evidentiary foundation is suggested by the wife. She merely sought the application of the applicable equitable principles to the facts as found by the primary judge.[140]

Kirby J then applied this new approach to Mrs Garcia's facts, and determined that the decision by the trial judge Young J to find in favour of Mrs Garcia had been correct (although for reasons different than Young J expressed).[141] The bank was therefore unable to enforce the security held from Mrs Garcia, Kirby J concluded.

Kirby J's adoption of Lord Browne-Wilkinson's approach was in contrast to its rejection in *Garcia* by Gaudron, McHugh, Gummow and Hayne JJ. where their Honours stated:

> As is implicit in what we have said, we prefer not to adopt the analysis made by Lord Browne-Wilkinson in *Barclays Bank Plc v O'Brien* which proceeded from identifying "the circumstances in which the creditor will be taken to have had notice of the wife's equity to set aside the transaction".[142]

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[139] (1998) 194 CLR 395, 430–431 [73].

[140] Ibid, 431 [74].

[141] Ibid, 434–435 [81]–[83].

[142] Ibid, 410–411 [39].

The possible future widening of the type of relationship which might give rise to a special equity

Gaudron, McHugh, Gummow and Hayne JJ left open in *Garcia* the possibility of the widening of the types of relationship that the *Yerkey v Jones* situation may apply to. They stated:

> It may be that the principles applied in *Yerkey v Jones* will find application to other relationships more common now than was the case in 1939 – to long term and publicly declared relationships short of marriage between members of the same or of opposite sex – but that is not a question that falls for decision in this case. It may be that those principles will find application where the husband acts as surety for the wife ... The resolution of questions arising in the context of other relationships may well require consideration of other issues.[143]

Certainly such an opinion was not out of step with the thoughts of Kirby J, that essentially a new principle needed to be created encompassing various types of relationship, not just one for married women.

Callinan J in his decision (which found in favour of Mrs Garcia, based on Callinan J's view that the trial judge was bound to follow the decision in *Yerkey v Jones*) did not support extending the types of relationships the courts would recognise as attracting a special equity beyond that of married wives to their husbands. He stated:

> Indeed, given the diversity of human relationships, it would not only be imprudent but probably also impossible to do so. I would not, with respect, adopt the principle settled by the House of Lords in *Barclays Bank Plc v O'Brien*, that any exceptional rules formerly applicable to guarantees by wives of husbands' obligations should be extended to co-habitees in cases in which the creditor is aware of an emotional relationship between the co-habitees. Such a principle might, in some circumstances (leaving aside potential difficulties associated with the proof and definition of an emotional relationship) narrow the range of people deserving of protection by reason of their occupation of a special position, or the suffering of a special disability of the kind considered by the Court in *Amadio*. Indeed, this may, in any event, be an area more fit for legislative than judicial intervention.[144]

[143] Ibid, 404 [22].

[144] Ibid, 442 [109].

So Callinan J saw that if such a widening of the types of relationship which equity will recognise as deserving a special equity was justified, then it was a matter for the legislature to address, and not the courts.

The difference between the need for 'notice' being established in an unconscionable action in an *Amadio* type unconscionable conduct action, as opposed to a *Garcia* special equity action, is also important to distinguish. The *Amadio* doctrine of unconscionability involved a deliberate shutting of the eyes by the financier, whereas in the *Garcia* special equity case, the financier was 'taken to appreciate' the likelihood that no sufficient explanation of the guarantee was provided, due to the special relationship established. In an *Amadio* type action, the financier may defend such an action to set aside a guarantee in its favour by showing it did not have knowledge of any undue influence being enjoyed by the debtor over the surety (of course the financier may also defend the action by showing that it had taken adequate steps to ensure the surety had been provided with the opportunity to make an informed independent decision to enter into the guarantee) – this 'lack of knowledge' defence is not available for a *Garcia* special equity type claim, as presumably the financier, in its assessment to consider and approve the credit and security, would be inferred to have the knowledge of the marriage relationship between the surety and the debtor.

It is interesting to note how unexpected the *Garcia* decision was to some commentators.[145] For instance, Michael Main in his article '*Garcia v National Australia Bank* – Having it Both Ways',[146] stated:

> In Family Law, in Equal Opportunity Law, and in Employment Law, we are seeing more than ever the enshrinement of substantive social values about human dignity and equality before

[145] See comments in this regard from Su-King Hii, 'From *Yerkey* to *Garcia*: 60 Years on and Still as Confused as Ever!' (1999) 7 *Australian Property Law Journal* 47, and Jenny Lovric and Jenni Millbank, NSW Law Reform Commission and the University of Sydney, *Darling, Please Sign this Form: A Report on the Practice of Third Party Guarantees in New South Wales*, Research Report 11 (2003), comments at [7.35] recognising the fears at the time of the *Garcia* decision that it would unleash a torrent of claims against lenders.

[146] Michael Main '*Garcia v National Australia Bank* – Having it Both Ways' published in 'Nuts & Bolts of Securities Law – Guarantees 1999 Seminar Papers 1999', Legal and Accounting Management Seminars Pty Ltd (1999).

> the law, as expressed in the workplace, in education and at the time of dissolution of marital relationships. Yet the High Court has taken what could be considered to be a backward step into the messy assumptions of an earlier and perhaps less-enlightened time, where all sorts of expressions that would now make us cringe were used quite unselfconsciously and even with a tinge of male pride; eg "don't worry your pretty little head about that", or "man's business".[147]

This surprise by some commentators was not only due to the assumption by many that *Amadio* had overruled or subsumed the principle from *Yerkey v Jones*, but also to the fact that *Yerkey v Jones* had not been followed in some instances by lower courts.[148]

3.2.2 LEVEL OF KNOWLEDGE REQUIRED FOR A GARCIA SPECIAL EQUITY ACTION IN ORDER FOR A TRANSACTION TO BE SET ASIDE

For the *Garcia* special equity, the majority in *Garcia* ruled out that a financier's constructive knowledge that a security provider is the wife of the debtor would be sufficient for a wife to obtain relief.[149] The special equity cases require the financier having actual knowledge[150] that a security provider (or a co-debtor) is the wife of the debtor. This is not normally a contentious issue as the knowledge of the marriage would usually be disclosed to the financier from the assessment of the finance application, as the financier seeks to understand the relationship both between the finance applicants as well as between the finance applicants and the proposed security providers. As Bryson J stated in the previously discussed Supreme

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[147] Ibid, 3.

[148] See examples such as the Supreme Court of New South Wales Court of Appeal in *Akins v National Australia Bank* (1994) 34 NSWLR 155 (see in particular Clarke JA comments at 329), *European Asian of Australia Ltd v Kurland* (1985) 8 NSWLR 192 and *Commonwealth Bank of Australia v Cohen* (1988) ASC 55-681 at 58,159 etc.

[149] *Garcia v National Australia Bank Ltd* (1998) 194 CLR 395, Gaudron, McHugh, Gummow and Hayne JJ at 410–411 [39], Kirby J at 430 [72].

[150] With 'actual knowledge' including, use of the 'knowledge of awareness' scale formulated by Gibson J in *Baden*:

(i) actual knowledge;

(ii) wilfully shutting one's eyes to the obvious; and

(iii) wilfully and recklessly failing to make such inquiries as an honest and reasonable man would make.

Court of New South Wales case of *State Bank of New South Wales v Hibbert; Groom v Hibbert* (which explored the possibility of extending the special equity to de facto wives), '[t]he question whether a proposed guarantor is the wife of a proposed borrower is readily ascertainable; people usually behave responsibly in handling information like that.'[151]

If the unusual set of facts was to arise that a financier was not aware that a co-debtor or security provider was the wife of a debtor, and a *Garcia* special equity action was commenced based on allegations of the financier's constructive knowledge, equity would be unlikely to provide relief. This is because the financier could not have exploited the special position of reliance that a wife may place in her husband, if the financier was unaware of the married relationship.

If the law for the *Garcia* special equity was to extend to other types of close relationships, beyond wives' relationships to their husbands, would a financier only be affected by actual knowledge of such a relationship? Difficulties for financiers emerge in capturing an awareness of other types of relationships that may exist. Bryson J, in commenting that emotional relationships between co-habitees (as well as other relationships where a surety reposes trust and confidence in the principal debtor) would be the only extensions possible of the special equity that seriously falls for consideration,[152] stipulated that where one co-habitee stands surety for another co-habitee's debts, the financier would be required to have been aware of such a relationship between the co-habitees in order for the special equity to have possibly applied.[153] The financier only having constructive knowledge would appear to be insufficient to meet Bryson J's requirement of being 'aware' of the relationship.

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[151] (2000) 9 BPR 17,543, [58].

[152] Ibid, [60], referring to Kirby J in *Garcia* and the House of Lords in *O'Brien.* Bryson J also stated that there was no judicial authority for any '… extension of the principles acted on in *Garcia* from wives to all married persons, or to all women, or all persons who are living in de facto relationships, or all persons who share domestic relationships …'.

[153] Ibid.

In another de facto wife case previously referred to, *Liu v Adamson*, Macready M of the Supreme Court of New South Wales commented that the scenario around a financier's receipt of actual knowledge of a de facto relationship differed little to that applicable to a married relationship. He commented that:

> The extension of the rule to the situation of a man and a woman living in a de facto relationship involves no difficulty with notice nor does it involve any constructive notice of the type rejected by the majority in *Garcia*. For a lender there is no more difficulty with enquiries than when the parties are married and the female is being asked to give a guarantee as she is shown on the title.[154]

In other types of relationships where an extension of the *Garcia* special equity has been tested, the need for actual knowledge by the financier of the special relationship has been required. Examples are provided as follows.

Relationships between brothers-in-law

In a Supreme Court of Victoria Court of Appeal decision which will be considered in detail later in this thesis, *Kranz v National Australia Bank Ltd*,[155] a special relationship that existed between brother-in-laws was examined. Charles JA, after recognising the principle in *Garcia* that the financier had to be aware of the relationship of trust and confidence between the guarantor and the debtor whose debt has been guaranteed, stated:

> In Australia it remains therefore for the debtor to establish that the bank was aware of a relationship that put the bank on enquiry, such as that of husband and wife or solicitor and client, or that there was a relationship of trust and confidence between the debtor and third party.[156]

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[154] (2004) Q ConvR 54-601, 61,093 [22].

[155] (2003) 8 VR 310.

[156] Ibid, 322 [31].

Relationships between close friends

In a Queensland Court of Appeal decision which will be considered in detail later in this thesis decision, *ANZ Banking Group Ltd v Alirezai*,[157] a dealing between a close friend of the same ethnic descent and religion providing security to a bank for the friend's company debt was examined. McMurdo P supported the finding of the trial judge that the absence of the bank being on actual notice of any special relationship defeated the surety's claim for relief under unconscionability or the *Garcia* special equity. McMurdo P stated:

> Her Honour was right to conclude on the facts found by her, which were open on the evidence, that ANZ did not know the relationship between Mr Sarlak and the appellant was one where the level of trust and confidence made it objectively unreasonable for a volunteer to provide the surety, requiring ANZ to be on inquiry that the appellant may be in a situation of general disadvantage.[158]

Summary of the level of knowledge required for either an unconscionability or a *Garcia* special equity action

So what can be gleaned as to the level of knowledge required by Australian financiers for either a successful relief claim based on the *Garcia* special equity or unconscionability to be brought against them? That in the absence of actual knowledge being held by the financier of a type of relationship / special circumstances that would indicate the probability of likely exploitation of a debtor or security provider, equitable relief would normally not be available.

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[157] [2004] ANZ ConvR 132.

[158] Ibid, 135 [55]. Jerrard JA looked at Lord Nicholls' decision in *Etridge* and whether constructive notice of the special relationship could apply, and in rejecting such an approach, stated 'That "deemed notice" approach is certainly a far wider proposition than any which can be supported by the observations in *Amadio* or *Garcia*.' 140 [97]. Wilson J similarly found that even if *Garcia* could apply to this type of special relationship, in the bank's absence of knowledge, '… it was not unconscientious of it to proceed with the transactions without itself explaining them or knowing that a third party had done so.' 145 [117].

Can any assistance be gleaned from examining how English cases have treated the level of notice in undue influence cases?

How has English law approached the 'notice' issue in regard to undue influence cases? As previously referred to in *Etridge,* where Lord Nichols saw that, for undue influence, in the absence of banks evaluating in each case the extent to which a debtor may have influence over a guarantor:

> … the only practical way forward is to regard banks as "put on inquiry" in every case where the relationship between the surety and the debtor is non-commercial. The creditor must always take reasonable steps to bring home to the individual guarantor the risks he is running by standing as surety. As a measure of protection, this is valuable. But, in all conscience, it is a modest burden for banks and other lenders. It is no more than is reasonably to be expected of a creditor who is taking a guarantee from an individual. If the bank or other creditor does not take these steps, it is deemed to have notice of any claim the guarantor may have that the transaction was procured by undue influence or misrepresentation on the part of the debtor.[159]

So for undue influence cases in England, the question of a financier's level of notice for a surety to have been subject to undue influence or misrepresentation is not at issue. The financier is on notice in every instance where the relationship between the surety and the debtor is non-commercial ie unless a commercial benefit for the surety to provide security is apparent, the financier is deemed to have constructive notice that the transaction may have been procured as a result of undue influence or misrepresentation and must take action to ensure that the surety independently has the transaction and their level of liability explained to them.

[159] [2002] 2 AC 773, 815 [87].

4. THE SPECIAL EQUITY POST *GARCIA*

4.1 THE EXTENT TO WHICH *GARCIA* HAS BEEN FOLLOWED FOR WIVES SEEKING RELIEF UNDER GUARANTEES

There have been a number of cases where wives providing guarantees have been successful in relying upon the decision in *Garcia*. There are also cases where wives have attempted to widen the limits of *Garcia*, without success.

Armstrong v Commonwealth Bank of Australia

One of the early cases to be decided after the August 1998 decision of *Garcia* was the Supreme Court of New South Wales decision of *Armstrong v Commonwealth Bank of Australia*.[160] The facts of this case differed from *Garcia* in that the wife surety, Mrs Armstrong, was not a capable and presentable professional business woman like the physiotherapy practice manager Mrs Garcia. Mrs Armstrong had had a limited education (having only completed one year of high school, and a one year nursing aide course) and largely had confined herself to home duties during her marriage to Mr Armstrong. She had also been subjected to physical assaults from her husband.

The facts of the case were that in 1983, Mrs Armstrong provided a guarantee and mortgage over two properties – the Blakehurst home that she and her husband had jointly owned, as well as an investment property she owned in Tweed Heads – in order to secure the borrowings of her husband's company, D J Armstrong Investments Pty Ltd, from the Commonwealth Bank of Australia. The transaction the funds were borrowed for was the company's purchase of a half-interest in a resort development at Salamander Bay NSW.

Mrs Armstrong commenced proceedings in the Supreme Court of New South Wales to have her guarantee and mortgages set aside. The bank by its cross claim sought to recover the moneys owed and to enforce its securities. Mrs

[160] [2000] ANZ ConvR 470.

Armstrong's claim for relief was based on the special equity from *Yerkey v Jones* and *Garcia*.

Mrs Armstrong alleged that she had signed the main security documents with only her husband present, whereas the bank alleged the documents were signed in the bank's presence and that the bank provided an explanation of the documents. She claimed that her husband told her that neither she nor her properties would be at risk as a result of signing the documentation. In regard to the acknowledgement of debt forms the bank had required her to sign, Mrs Armstrong alleged that her husband assaulted her (this claim being supported by NSW Police records and an apprehended violence order made against Mr Armstrong) when she initially refused to sign some of these forms (she subsequently signed them under duress, she advised). Her reason for having executed the forms was advised as being that:

> I was concerned that if I did not do what my husband wanted me to do I believe I would have been subjected to abuse and physical violence. Eventually I signed the documents to keep the peace.[161]

The bank's testimony had largely been based on their staff recalling what they would normally do in circumstances of security explanation to a surety, the bank having been unable to supply records in this regard for what had occurred 14 years prior to the trial commencement. Hamilton J had found that some of the bank's witnesses were not very credible, but had found Mrs Armstrong to generally be a credible witness.

Mrs Armstrong argued that she did not receive independent legal advice in regard to the transaction. She had, however, received legal advice in August 1989 in regard to matrimonial matters and the status of her property. Legal advice had again been received in August and September 1990, when the solicitors she consulted both advised her not to sign any more documents that her husband gave her.

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[161] Ibid, 470 [6].

Following the September 1990 visit to the solicitor, she had executed the remaining bank security documents.

The Salamander Bay project that the funds were borrowed for was not successful and in 1993 the company was wound up. Mr Armstrong was subsequently made bankrupt and Mrs Armstrong's security was called upon by the bank. Mrs Armstrong argued a number of counter claims, including undue influence and the special equity based on the decision in *Yerkey v Jones* and *Garcia*.

Hamilton J was satisfied that Mrs Armstrong had not signed any of the security documents in the presence of the bank staff and that she had signed the documents under the undue influence of Mr Armstrong in the sense in which that term was used in *Garcia*.

Having established the circumstances under which Mrs Armstrong had signed the security documents, his Honour then examined the facts in order to determine whether Mrs Armstrong was a volunteer. Despite being a 25% shareholder in the debtor company, Mrs Armstrong did not benefit from her shareholding. Whatever benefit the bank had argued that she had received from the company (a transfer some years previously of a Tweed Heads property to her, from the company, plus the lifestyle that she enjoyed), had been conferred upon her in her capacity as a wife of Mr Armstrong and not as a company shareholder. His Honour stated:

> The shareholding of 25 per cent may not have been insubstantial or nominal in amount, but was insubstantial or nominal in the sense that Mrs Armstrong in fact exercised no rights and received no benefits by reference to her shareholding (cf *Commonwealth Bank of Australia v Khouri* [1998] VSC 128 [65]).[162]

Mrs Armstrong had been a volunteer in the *Garcia* sense.

On the question as to whether independent advice was received, his Honour was of the opinion that Mrs Armstrong had not received independent advice

[162] Ibid, 474 [33].

on the transaction – the advice she did obtain did not relate to the key security documents in question (and that the bank was unaware of her having obtained any advice), or was '… not of the quality necessary to relieve the Bank from the consequence of actual undue influence.'[163] In addition, that advice had been overborne by her husband's insistence for her to sign and the threat of violence against her.

Having established that the above criteria were met, Hamilton J determined that Mrs Armstrong was entitled to relief under the *Yerkey v Jones* and *Garcia* principles, and thus her guarantee and mortgages of the Blakehurst family home and a home unit she owned in Tweed Heads were set aside.

From a comparison of facts to the *Garcia* case, Mrs Armstrong was in a stronger position than Mrs Garcia in terms of the following.

Mrs Armstrong's was more able to sustain an argument that she did not understand the transaction she was asked to guarantee for her husband's company. She did not have to defend any arguments that she was a businesswoman and professional person, and thus did not have to overcome any argument that her experiences would have better placed her to have been able to understand the transaction.[164]

The other strength was the level to which Mrs Armstrong was a volunteer to the transaction. Not only did she have in common with Mrs Garcia that there was not any material benefit accrued to her as a result of having guaranteed the transaction to her husband's company, but the application of violence to her when Mrs Armstrong initially declined to execute the security, assisted her case for being classed as a volunteer.

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[163] Ibid, 475 [34].

[164] Although this was perhaps countered by the fact that Mrs Armstrong had received some limited legal advice, albeit advice that was neither overly relevant nor applicable to the key documents in question, plus this was overborne by her husband's action.

So Mrs Armstrong's security being set aside was an early example of the success in applying *Garcia* to obtain the special equity relief for a wife.

Bylander International Consortium (Aust) Pty Ltd v Multilink Investments Pty Ltd

The Supreme Court of New South Wales Court of Appeal 2001 case of *Bylander International Consortium (Aust) Pty Ltd v Multilink Investments Pty Ltd*[165] (*Bylander*) dealt with a wife's successful attempt to widen the circumstances under which a person would be considered a volunteer under *Garcia*. In this case, the husband and wife, Mr and Mrs Satchi, guaranteed the husband's company Bylander International Consortium (Aust) Pty Ltd, for a $275,000 loan for 30 days. The loan funds were initially drawn down to the joint bank account of Mr and Mrs Satchi, prior to the bulk of the moneys being taken out and being sent offshore for her husband's business purposes. Mrs Satchi was unaware that all of the loan funds had not been transferred out of the joint account. The loan was not repaid and recovery action against the company and sureties was commenced.

Before Boland ADCJ in the District Court Mrs Satchi was unsuccessful at first instance. The financier successfully argued that the elements of a special equity claim were not present. Further, even if the requirements of a special equity claim were established, the fact that the loan funds were paid directly into the joint account Mrs Satchi had with her husband, defeated the necessary voluntary aspect for a *Yerkey v Jones* or *Garcia* claim (as there was an apparent direct benefit to her from the company's loan). This fact, combined with the financier's evidence that Mrs Satchi had previously been involved in directly borrowing funds from the financier in her and her husbands' names, for similar purposes, prior to the purchase of the company (as well as evidence that Mrs Satchi was involved with discussions with the Standard Chartered Bank in regard to the operations of the company), led

[165] [2001] NSWCA 53 (unreported, 14 March 2001, BC200101189).

Boland ADCJ in the District Court to reject Mrs Satchi as being classed as a volunteer.

In the Court of Appeal, Handley JA (with whom Giles and Heydon JJA agreed) first determined that nothing Mrs Satchi's lawyers had expressed in the pleadings for the trial amounted to their having abandoned a *Yerkey v Jones* claim (and thus such a claim was open to be pleaded). Handley JA then looked at *Garcia* and applied the principle that the court needs to inspect the substance of the transaction before determining whether or not the wife meets the criteria of being classified as volunteer or not. He stated:

> The High Court made it clear in *Garcia* that the characterisation of a guarantee as a voluntary transaction did not fall to be determined by the presence or absence of sufficient consideration to support the validity of a simple contract. There must be consideration in that sense for any such guarantee to be legally enforceable. The question whether the transaction was a voluntary one, so far as the surety is concerned, falls to be decided as a matter of substance, and guidance has been given as to the type of benefits which will not exclude such a finding.[166]

Handley JA then examined the factors that *Garcia* had determined would not exclude a party from being classified as a volunteer, noting that Mrs Garcia had:

- been a director and shareholder in the debtor company; and
- in the past received some benefit from her husband's company, but that the company was in the complete control of her husband.

Handley JA observed that despite these factors, the High Court had nevertheless ruled that Mrs Garcia had obtained no real benefit from having entered into the transaction, and was a volunteer.

Handley JA then dealt with the evidence of the $275,000 loan being passed through the joint account Mrs Satchi held with her husband, and the residual amount of $16,000 that was not withdrawn on the same day (but $7,500 of

[166] Ibid, [15].

which was withdrawn the next month or so). Handley JA concluded in regard to these moneys, that:

> In substance the loan funds were used solely for the benefit of the company and the husband and any incidental benefits flowing to the wife from payments out of the joint bank account are not sufficient to distinguish this case from *Garcia* and the other cases which have followed it.[167]

Handley JA accordingly found that Mrs Satchi was entitled to relief under *Yerkey v Jones* and *Garcia* principles and set aside the judgment against her.

Prima facie, on the facts of this case it would have appeared not to be sustainable to argue a *Garcia* cross-claim given the wife's evidentiary burden against her in regard to maintaining her volunteer status, as loan funds were credited to her joint account ie loan proceeds were credited to an account that was partly owned by the wife and thus a direct benefit to her appears to have resulted. The versatility of *Garcia* was demonstrated by the wife's success, with the court's preparedness to determine the materiality of any benefit allegedly accruing to a wife as a result of transactions done for her husband's purposes. In this case, the majority of the loan proceeds were transferred out of the joint account and into the company account on the same day the funds were deposited, showing there was little benefit to the wife and, thus, that she was a volunteer.

Garcia principles applied to a wife who was not a volunteer, without success – the case of Elkofairi v Permanent Trustee Co Ltd

In *Elkofairi v Permanent Trustee Co Ltd*[168] the NSW Court of Appeal was asked to consider a claim for relief based on the *Contracts Review Act 1980* (NSW), unconscionability and the *Garcia* equity. Relief was sought by a wife in circumstances where there was no guarantee involved; instead, relief was sought from a mortgage over the family home taken by a husband and wife to secure borrowings in their own names. The difficulty of trying to establish an unconscionability claim or a *Garcia* special equity claim is immediately

[167] Ibid, [20].

[168] (2003) Aust Contract R 90-157.

apparent, as the question of the wife having been a volunteer (in terms of not having received any benefit) does not readily appear sustainable, in regard to prima facie there being a benefit to the wife from a loan that she was a joint debtor to.

The circumstances were unusual, however, in that:

- the wife was aged in her fifties and was unable to read or write;
- the wife did not speak English (she was born and raised in poverty on a farm in Syria until she married at age 24 and then moved to Australia – she had never attended school nor received any education);
- the wife had hardly any income;
- the husband was uncommunicative and violent to the wife (an AVO had previously been taken out by the wife against her husband);
- the wife's signature on the loan application form, where she was shown as being a businesswoman with five years' experience in business with her husband, was forged; and
- a solicitor's certificate of explanation of liability under the mortgage had been provided by the mortgagor's solicitors.

The financier, Permanent Trustee Co Ltd, was not aware of most of these circumstances, except for the fact that Mrs Elkofairi did not have any significant income, and that a solicitor's certificate of liability explanation had been provided.

A loan of $746,000 had been taken out, of which $470,000 was applied to refinance an existing St George bank loan in their joint names. The balance of the loan, after payment of various legal and other expenses, was paid via a cheque in favour of Mr and Mrs Elkofairi for $250,234.59. There was no evidence submitted as to how these funds were applied, and it was submitted without rebuttal that these funds were not applied to directly benefit Mrs Elkofairi. Immediately the loan was defaulted upon (no loan repayments were ever made). The financier sought an order for possession of the family

home, which was defended by the wife (the husband was bankrupt by the time the case went to trial).

Mrs Elkofairi sought relief from her obligations on a number of grounds, including a cross-claim based on the special equity as per *Yerkey v Jones* and *Garcia*, *Amadio* unconscionability and s 9 of the *Contracts Review Act 1980* (NSW).

In regard to the cross-claim based on *Yerkey v Jones* and *Garcia*, Beazley JA (with Santow JA and Campbell AJA agreeing) was not prepared to accept that relief was available. Beazley JA noted that, whilst it was not required that the financier had any notice of any unconscionable dealing between the husband and wife, that as made clear in *Garcia*, the party seeking relief must meet the following criteria. They must have been a volunteer and not obtain any financial benefit from the transaction, In addition, the party must not have understood the transaction. Lastly, the financier must not have taken any steps either to have explained the transaction to the party, or to have had a stranger explain it to them.[169]

There were two additional complexities, Beazley JA said, for a joint debtor in trying to rely on a *Yerkey v Jones* and *Garcia* claim (other than the volunteer aspect). The first complexity was whether *Yerkey v Jones* and *Garcia* applied other than in a guarantee situation. The second complexity was whether the financier was still understood to be automatically on notice that a wife may place trust and confidence in her husband in matters of business and that a husband may not explain accurately the transaction to the wife, when the wife was a co-debtor and co-security provider with her husband. Beazley JA concluded that unless this was established, '… the underlying premise upon which the principle operates is missing.'[170]

[169] Ibid, 92,234 [41].

[170] Ibid, 92,235 [47].

Beazley JA did not find a need to explore these aspects further, as she noted that there was nothing to put the financier on notice that Mrs Elkofairi had even partially been a volunteer, given that the loan application showed Mrs Elkofairi as a businesswoman with five years experience in a previous business with her husband, and that the financier had not been aware that her signature on the application was forged. Therefore Beazley JA found that no relief was available under *Yerkey v Jones* and *Garcia*.

Santow JA approached the position of a joint debtor seeking the special equitable relief under *Yerkey v Jones* from a different perspective to that of Beazley JA. Santow JA (with whom Campbell AJA agreed) saw that a joint debtor may well be a volunteer as they may be in the position of being a constructive surety as per the comments of Lord Selborne in the 1880 House of Lords decision in *Duncan, Fox & Co v North and South Wales Bank* (1880) 6 App Cas 1.[171] Santow JA referred to Lord Selborne's judgment that a constructive suretyship was not dependent upon a contract of suretyship being in existence. Instead, constructive suretyship may arise when there was a primary and secondary liability of two persons for the same debt, but the debt was, as between the two, the debt of only one of them.[172] Santow JA concluded (with Campbell AJA concurring):

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[171] Ibid, 92,244-92,245 [93–95].

[172] Ibid, 92,243 [93]. Lord Selborne, in his explanation as to the types of suretyship that exist, described this type of suretyship (constructive suretyship) as applying to the following situations ((1880) 6 App Cas 1, 12):

> Those in which, without any such contract of suretyship, there is a primary and a secondary liability of two persons for one and the same debt, the debt being, as between the two, that of one of those persons only, and not equally of both, so that the other, if he should be compelled to pay it, would be entitled to reimbursement from the person by whom (as between the two) it ought to have been paid.

Lord Selborne describes three types of suretyship. The first is the traditional guarantee for a particular purpose, between the principal and surety, to which agreement the creditor thereby secured is a party (ie a typical guarantee that an Australian financier would take from a third party to secure a debtor's obligations). The second type is a similar guarantee between the principal and surety only, to which the creditor is a stranger. The third type of suretyship is constructive suretyship; 11–12. Santow JA *Elkofairi v Permanent Trustee Co Ltd* (2003) Aust Contract R 90-157, 92,244 [93] also makes reference to Lord Selborne's comments having been referred to by James O'Donovan and John Phillips, *The Modern Contract of Guarantee*, Law Book Company, 1996, at 8.

> The relevance of this analysis in the present context is not to anticipate what the High Court might, or might not, do in extending the doctrine of *Yerkey v Jones* to cases outside the conventional guarantee by a wholly volunteer wife. It is not for an intermediate appellate court to do that. Rather it is to support the proposition that, when resorting instead to the wider doctrine of unconscionability, here in granting relief to the wife (compare *Commercial Bank of Australia Ltd v Amadio* (1983) 151 CLR 447) the fact that the transaction is in the strict sense not one of guarantee need not provide an insuperable obstacle to relief. Nor that the wife is only a volunteer as to a portion of the loan. Each circumstance must be taken into account in looking at all the circumstances, to see if indeed it would be unconscionable for the lender to enforce the rights against the wife.[173]

The fact that Mrs Elkofairi was only a partial volunteer, in that the St George Bank joint loan for which she was co-debtor had been refinanced with part of the new loan proceeds, was not seen by Santow JA as a factor to deny her relief under the special *Garcia* equity or under unconscionability.

Looking at whether *Amadio* type unconscionability could be established, Beazley JA (with Santow JA and Campbell AJA agreeing) saw it as a case where the financier, although not having been put on notice in regard to such elements as Mrs Elkofairi's lack of English, education, business experience or the nature of the domestic relationship she had with her husband, had been put on notice in regard to her lack of income. The absence of Mrs Elkofairi's financial information on the loan application form '… was sufficient to put the respondent on notice of the appellant's lack of capacity to meet the repayment obligations under the mortgage.'[174] Beazley JA concluded that it was unconscientious to lend a large amount of money to a person with no income, with the knowledge that if repayments were not met, the financier would sell that person's only asset.[175]

Beazley JA also found that the loan contract was unjust in terms of s 9 of the *Contracts Review Act 1980* (NSW) (given that it was a substantial loan

[173] Ibid, 92,243 [96].

[174] Ibid, 92,237 [56].

[175] Ibid, 92,237 [59].

against Mrs Elkofairi's only asset, and the financier was aware she had no income) and that relief was therefore available to her under s 9 of the Act.

Mrs Elkofairi was awarded relief from having to pay the total debt owing to the Permanent Trustee Co Ltd. However, she was found liable for the benefit she had received; half of the St George mortgage of $469,000 that the Permanent Trustee Co Ltd had refinanced with its $746,000 loan. As Santow JA stated (with Campbell AJA agreeing), 'When a transaction is set aside for unconscionability or fraud, such order may be conditional on the repayment of any unwarranted benefit.'[176]

The important outcomes of this case were as follows. Santow JA and Campbell AJA's agreement that *Yerkey v Jones* and *Garcia* could apply to mortgages as well as guarantees was significant (Beazley JA had recognised this issue but not found it necessary to decide on this question).

An additional important outcome was Santow JA's finding (agreed to by Campbell AJA) that a joint debtor may well be a volunteer as they may be in the position of being a constructive surety, and was not ruled out from being able to obtain relief under *Yerkey v Jones* and *Garcia*.

The next important outcome was that only being a partial volunteer did not prevent a special *Garcia* equity claim or an unconscionability claim from being successful.[177]

The last important outcome was Mrs Elkofairi being liable for the 'unwarranted benefit', her portion of the original debt that was refinanced (ie for the portion of the debt for which she was not a volunteer).

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[176] Ibid, 92,243 [98]. Beazley JA (with Campbell AJA agreeing) also supported that Mrs Elkofairi must be made to bring to account the benefit that she has received from her mortgage being refinanced.

[177] Ibid, 92,244–92,245 [92–97] (Santow JA, agreed to by Campbell AJA).

Some 2005 cases where wives seek relief under the Garcia principles:

Willis and Bowring Mortgage Investments Ltd v Ziade Investments (No.2) Pty Ltd

In 2005, an unsuccessful attempt to widen the application of *Garcia* occurred in the Supreme Court of New South Wales case of *Willis and Bowring Mortgage Investments Ltd v Ziade Investments (No.2) Pty Ltd.*[178] The facts of the case revolved around an $11.5 million loan to assist a developer, Mr Ziade, undertake a residential property development at Coogee in Sydney's eastern suburbs. The money was borrowed by Mr Ziade's company, Ziade Investments No. 1 Pty Ltd (Mr Ziade being the sole shareholder and director). The funds were then on-lent to Ziade Investments No. 2 Pty Ltd. Ziade Investments No. 2 Pty Ltd owned the Coogee development site, with Mr Ziade's wife being the sole shareholder and director of that company. The loan was secured by:

- mortgages over the Coogee site;
- interlocking guarantees from Ziade Investments No.1 Pty Ltd (which owned the Ziade's residence) and Ziade Investments No.2 Pty Ltd;
- charges over the assets of the companies; and
- a guarantee from Mr and Mrs Ziade.

To meet the financier's requirement, Mr and Mrs Ziade attended the office of a solicitor who was Mr Ziade's uncle, Mr Anthony Ziade. The solicitor advised Mrs Ziade that if the loan was not repaid, the finance company could *come after everything,* including her jewellery and their house.[179] Mr Ziade told Mrs Ziade that her assets were safe. In response to Mr Ziade's statement that the home was protected, the solicitor advised the Ziades 'I don't know about that – it isn't explained that way in the contract.'[180] Mrs Ziade admitted that she had known that she was borrowing money and that she might be called upon to repay the amount borrowed.

[178] [2005] NSWSC 952 (unreported, 23 September 2005, BC20050715).

[179] Ibid, [101].

[180] Ibid, [102].

Ziade Investments No. 1 Pty Ltd defaulted on the loan, and the security was called up, including the guarantee from the Ziades. Ziade Investments No. 2 Pty Ltd went into liquidation and Mr Ziade became bankrupt. The financier applied for a writ of possession for the mortgaged land and cross-claims seeking to set aside the guarantees were lodged by Mrs Ziade.

The case was heard by White J in the Supreme Court of New South Wales, with the Ziades having appeared for themselves. A number of cross-claims were argued by Mrs Ziade, including *Garcia*. White J noted that in regard to the claim for relief under the principles of *Garcia* that Mrs Ziade knew what a guarantee and a mortgage were, she had understood she was signing as a guarantor and that that meant she could be called upon to repay the loan and that her solicitor had warned her of the implications of signing the guarantee.[181]

White J held that the argument by the Ziades, that Mrs Ziade did not receive the legal advice from someone who was a stranger to her, was not grounds for Mrs Ziade to escape liability on her guarantee on reliance of the special equity in *Garcia*.[182] White J noted that Mrs Ziade had received advice from the solicitor of the consequences of signing the guarantee, but chose to accept her husband's assurance that the home was protected rather than the warning given to her by her solicitor.[183] She thus failed to sustain a *Garcia* special equity cross-claim on the basis that she did not understand the transaction.

Mrs Ziade also failed to meet the *Garcia* requirements on a second basis, in that she was not a volunteer. White J observed the following relevant facts. The first fact was that Mrs Ziade was the beneficial owner of shares in Ziade Investments No. 2 and that company in turn owned the land upon which the home unit development was being built. The second fact was that the company was the ultimate recipient of the loan funds. The third fact was that

[181] Ibid, [101]–[102].

[182] Ibid, [97].

[183] Ibid.

if the development had been successfully completed, the company stood to make a profit from the development and this would have benefited the company owner, Mrs Ziade.

Thus, Mrs Ziade had a financial interest in the successful completion of the development for which the loan was made that she had guaranteed ie she was not a volunteer.[184]

This attempt to widen the application of *Garcia* was thus not successful. Mrs Ziade had clearly not been in the same position as Mrs Garcia – Mrs Ziade had benefited from a solicitor's explanation of her liability, and had stood to benefit directly from the transaction and thus failed the volunteer requirement. The facts had not lent themselves to any possibility of widening the *Garcia* boundaries.

CBA v Thompson

Another 2005 case, this time a single-judge decision of the District Court of South Australia, *CBA v Thompson*,[185] provides a more recent example where a wife guarantor was successful in seeking relief based on the principles of *Garcia*. In this case, the guarantor, Mrs Thompson, was in a similar position to Mrs Garcia.

The first similarity with Mrs Garcia was that Mrs Thompson had provided a guarantee for a company, Eden Valley Wines Pty Ltd, in which she and her husband were both shareholders and directors (similar to Mrs Garcia being a director and shareholder of her husband's business, Citizens Gold Exchange Pty Ltd).

Another similarity was that Mrs Thomson had not taken any active part in the management of the company she guaranteed, but instead had left the control

[184] Ibid, [98].

[185] [2005] SADC 156 (unreported, 29 November 2005).

and management of that company to her husband (as Mrs Garcia had left control and management of Citizens Gold Exchange Pty Ltd to Mr Garcia).

The fact that Mrs Thompson did not receive independent legal advice was a further similarity to Mrs Garcia's circumstances. Mrs Thompson received the documents when she and her husband met with the bank, and then signed them straight away in the presence of the bank officers. There was even doubt whether it was recommended to her that she obtain independent legal advice – the opinion on this issue differing amongst the bank staff who provided evidence (Mrs Garcia similarly had not received independent advice).

The next similarity was that the explanation of liability provided by the bank staff was inadequate to have made Mrs Thompson appreciate the true extent of her liability. Robertson J was satisfied that it was not apparent to the bank officers themselves that her guarantee to Eden Valley Wines Pty Ltd would not be limited to securing the liability of that company alone. As the bank was also taking a third-party equitable mortgage from Eden Valley Wines Pty Ltd to secure a separate loan to another company in Mr Thompson's group of companies, her liability was wider than the Thompsons had agreed with the bank (the procedure to be followed as per the Commonwealth Bank's own staff manuals for explanation of liability, were also not followed by the bank's Mr Buxton, Robertson J found).[186]

This lack of comprehension of the full extent of her liability was similar to Mrs Garcia not appreciating that the guarantee she signed was not limited to the company's overdraft, and that Mrs Garcia's existing all-moneys mortgage over the family home supported her guarantee. Mrs Thompson's evidentiary burden of proving she did not understand her liability under the security documentation had perhaps even been easier to establish than Mrs Garcia's

[186] Ibid, [123] 'Although he [Mr Buxton] was not directed to the Plaintiff's instruction manuals, which I mentioned earlier, his evidence regarding explanations of documents stands in stark conflict with the instructions in the manuals.'

position. Mrs Garcia had been a businesswoman in her own right, running a physiotherapy practice, and thus would have had more experience of dealing with banks. Compare Mrs Garcia's position with that of Mrs Thompson, whose primary duty was as a home-keeper for her husband and children, with no business experience (she had only occasionally helped out in the winery's restaurant, in a cooking and cleaning capacity, and had assisted with occasionally pruning or tying some of the grape vines).

The last similarity was that Mrs Thompson had not received any direct benefit from the transaction. In this regard, Robertson J looked to the judgment of Handley JA (with whom Giles and Heydon JJA agreed) in the previously mentioned New South Wales Court of Appeal case of *Bylander*. In Robertson J's examination of this question of voluntariness, he noted Handley JA's comments that the High Court made it clear in *Garcia* that in regard to whether a transaction was a voluntary one, it 'falls to be decided as a matter of substance, and guidance has been given as to the type of benefits which will not exclude such a finding …'[187] (ie that having been a director and shareholder of the husband's company, and having received some benefit from the company which the husband controls, does not disqualify a wife being considered a volunteer).

Robertson J then referred to Harper J's comments from the Victorian Supreme Court case of *Commonwealth Bank of Australia v Khouri*,[188] with Harper J comparing the facts of that case to *Garcia*, that even though a husband may rely upon his company to earn his living and support his family (and thus, as argued by the bank, the company indirectly benefits the wife), any benefit the wife gained from a company controlled by her husband came not as a right, but as a result of discretion exercised by the husband, thus making the wife a volunteer.[189]

[187] [2001] NSWCA 53 (unreported, 14 March 2001, BC200101189), [15].

[188] [1998] VSC 128 (unreported, 4 November 1998, BC9806127).

[189] Ibid, [65].

Robertson J noted that 'The question of whether she is a volunteer or not must be viewed as a matter of substance.'[190] In order to do so, he looked at Mrs Thompson's position, noting the defence's argument that for some time Mrs Thompson had lived at the winery owned by the company, and that she and her family had benefited from the supply of funds for her household from the company and other businesses in the group. Robertson J concluded that these benefits were received through Mr Thompson exercising his discretion, were incidental benefits and 'not of a sufficient benefit to be classified as a "real benefit" and, therefore, lead to the conclusion it was a voluntary transaction.'[191] Mrs Thompson's position, in regard to whether or not she had received a benefit as a matter of substance from the transaction, was probably not as strong as Mrs Garcia's position was. Mrs Garcia also had income from her own physiotherapy practice, and thus was not solely reliant upon her husband's discretion to receive income for herself and her family, whereas Mrs Thompson did not have the benefit of an independent income.

Robertson J referred to the combination of four circumstances listed in the joint judgment of Gaudron, McHugh, Gummow and Hayne JJ in *Garcia*, which attracted the special equity as per *Yerkey v Jones* to obtain relief from the enforcement of a guarantee. These circumstances were:

> (a) in fact the surety did not understand the purport and effect of the transaction;
> (b) the transaction was voluntary (in the sense that the surety obtained no gain from the contract the performance of which was guaranteed);
> (c) the lender is to be taken to have understood that, as a wife, the surety may repose trust and confidence in her husband in matters of business and therefore to have understood that the husband may not fully and accurately explain the purport and effect of the transaction to his wife; and yet
> (d) the lender did not itself take steps to explain the transaction to the wife or find out that a stranger had explained it to her.[192]

[190] [2005] SADC 156 (unreported, 29 November 2005), [180].

[191] Ibid.

[192] Ibid, [159], referring to *Garcia v National Australia Bank Limited* (1998) 194 CLR 395, 408 [31].

Robertson J's provided an analysis as to whether each of these four circumstances was met.

Circumstance (a)

Mrs Thompson did not understand the extent of her liability, in that she was also guaranteeing (due to the third-party equitable mortgage Eden Valley Wines also provided) other companies in her husband's group of companies, and not just the debts of Eden Valley Wines (nor was she aware of the extent of those other company's liabilities). The total liability being guaranteed by Mrs Thompson was therefore $4 million, not just the $290,000 debt of Eden Valley Wines. This was material to Mrs Thompson's case as, had Eden Valley Wines facilities had stood alone (ie without the third-party equitable mortgage being taken), the fact that Eden Valley Wines was trading profitably and meeting its financial obligations would have meant Mrs Thompson's guarantee would not have been called upon.

Circumstance (b)

Robertson J examined whether Mrs Thompson gained any real benefit from providing her guarantee, and concluded that any benefit gained was only an incidental benefit, and at the discretion of Mr Thompson. Mrs Thompson was thus a volunteer.

Circumstance (c)

Robertson J noted that the bank was aware that Mrs Thompson was Mr Thompson's wife, and that evidence from the bank's Mr Buxton was that the bank was aware Mr Thompson was the driving force in the group and that management rested with him.

Circumstance (d)

As the bank did not require Mrs Thompson to obtain an independent solicitor's explanation of her liability under the security documentation she executed, Robertson J only had to concern himself with determining whether or not the bank staff had taken steps to explain the transaction to the wife or

find out that a stranger had explained it to her. Robertson J noted that the documents were first shown to Mrs Thompson when the bank called at the winery in the morning, for her to execute the documents immediately. The bank was aware that Mrs Thompson had not read any of the bank's documents that they expected her to sign. Also, the bank's explanation of liability to her was not satisfactory, the bank staff themselves were not aware of the extent of her liability, and there had been non-adherence to the bank's own written instructions in regard to explaining surety liability. As was very often the case, the bank's written records (diary notes) regarding the execution of the security, were inadequate. This led to the bank staff having to rely on their memory for events which occurred four years prior to the trial (with the bank staff generally limited to stating what they would normally do in a surety explanation situation, as opposed to being able to remember what was said to Mrs Thompson – this created an evidentiary burden for the bank, in trying to discount allegations of what the surety claimed bank staff said to her at the time of document execution).

As the four *Garcia* principles were satisfied, and the misunderstanding by Mrs Thompson was material, the bank's claim to enforce the security against her was dismissed.

Mrs Thompson had also argued for relief under the unconscionability principles in *Amadio*. Robertson J first looked at Mason J's explanation in *Amadio* of what was meant by a special disadvantage, which was a 'disabling condition or circumstance is one which seriously affects the ability of the innocent party to make a judgment as to his own best interests …'[193] Despite Mrs Thompson not having the English language difficulties of Mr and Mrs Amadio, and having been considerably younger than the Amadios,[194] Robertson J agreed with the submission by Mrs Thompson's counsel that a

[193] [2005] SADC 156 (unreported, 29 November 2005), [208], quoting *Commercial Bank of Australia Ltd v Amadio* (1983) 151 CLR 447, 462, per Mason J.

[194] Mrs Thompson was approximately 41 years of age when she provided the security that was subsequently called upon, whereas Mr Amadio was 76 years of age and Mrs Amadio was 71 years of age when they signed their mortgage and guarantee.

combination of factors were sufficient for her to meet the first limb of *Amadio*. These factors which identified Mrs Thompson as being in a special class of persons that possessed the necessary characteristics to be considered for an *Amadio* special disadvantage were:

- a lack of education;
- no involvement in the affairs of running the winery or in the other companies in Mr Thompson's group of companies;
- a lack of understanding of the complete transaction;
- Mrs Thompson's subservience to her husband in financial and business matters; and
- her lack of understanding of commercial documents.[195]

Having decided that Mrs Thompson was in an *Amadio* type special disadvantage 'class', the next element necessary to establish an *Amadio* unconscionability claim was examined, whether the stronger party (the Commonwealth Bank of Australia) had knowledge of the special disadvantage. Robertson J noted Mason J's comments in *Amadio* that this knowledge does not have to be actual; all that is required is that on an objective test basis, the stronger party is aware of 'the possibility that that situation may exist or is aware of facts that would raise that possibility in the mind of any reasonable man …'.[196]

Robertson J concluded that the bank did not have actual knowledge of Mrs Thompson's special disability, nor were there sufficient facts on Mrs Thompson's position available to the bank's staff to raise awareness of the possibility of Mrs Thompson being in a position of special disadvantage (ie the bank was not on constructive notice). Mrs Thompson's *Amadio* unconscionability claim thus failed on the grounds of the bank being unaware of her special disability (once again evidencing the difficulty of being successful with an *Amadio* claim).

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[195] [2005] SADC 156 (unreported, 29 November 2005), [209].

[196] Ibid, [211], quoting *Commercial Bank of Australia Ltd v Amadio* (1983) 151 CLR 447, 467, per Mason J.

4.2 IS THERE ANY LIMIT TO THE TYPE OF SPECIAL RELATIONSHIPS THE COURTS WILL RECOGNISE?

There have been a number of instances where the courts have considered the application of *Garcia* to relationships other than the wife / husband relationship.

***Garcia* and de facto wives – not successful**

In *State Bank of New South Wales v Hibbert; Groom v Hibbert*[197] Bryson J of the New South Wales Supreme Court looked at a situation that involved a guarantee and mortgage from a de facto wife (Mrs Groom) to her de facto husband (Mr Hibbert).[198] The guarantee and mortgage in favour of the State Bank of New South Wales ('State Bank') were to secure a loan to Mr Hibbert's company, Vertee Pty Ltd, the proceeds of which were to enable Mr Hibbert to invest in his employer's company. The husband misled Mrs Groom in regard to the details of the investment. The investment was not successful, Vertee Pty Ltd defaulted and the State Bank commenced recovery proceedings and claimed possession of the house, relying on defaults which had occurred under the mortgage. Mrs Groom cross-claimed, seeking relief based on the *Garcia* special equity.

Although Bryson J found that there was a failure by the guarantor to understand the true nature of the transaction, her claim for relief under the *Garcia* principles failed (although Bryson J ultimately found in favour of Mrs Groom, utilising the *Contracts Review Act 1980* (NSW)). Bryson J's comments in obiter were of value. Bryson J was critical of the attempt in *Garcia* to provide a wider application of the special equitable claim to other types of relationships other than those involving married women to their husbands, stating:

> … application of the presumptions to some other relationship is not possible without a large departure from a chain of historical circumstances which brought this body of law into being, and it is

[197] (2000) 9 BPR 17,543.

[198] The de facto relationship had existed for eight years and no mention was made of there being any progeny from the relationship.

> also impossible without a large departure from the terms in which it has been and can be expressed. The principal judgment in *Garcia* contains no authority for either of these large departures.[199]

Bryson J further stated that:

> … [e]xtension of the principles acted on in *Garcia* ....[to] all persons living in de facto relationships, or all persons who share domestic relationships ... does not appear to me to be a development the law can realistically be expected to take.[200]

Interestingly, Bryson J at first appeared to offer some support for Kirby J's approach in *Garcia*, when Bryson J considered the application of Kirby J's views to the de facto relationship of Mrs Hibbert and Mr Groom. Bryson J stated:

> The only extension which seriously falls for consideration if persons other than wives are to be protected appears to me to be an extension of the kind addressed by Kirby J and acted on by the House of Lords in *O'Brien*, that is, to all cases where one co-habitee stands surety for the co-habitee's debts and the creditor is aware that there is an emotional relationship between the co-habitees, and to other relationships where the creditor is aware that the surety reposes trust and confidence in the principal debtor.[201]

Bryson J then curtailed any further consideration of Kirby J's comments in his conclusion that there was no judicial authority to consider extending the methodology taken by Kirby J in *Garcia*.[202]

The second case this thesis will examine where *Garcia* was argued by a de facto wife, in a counter-claim to avoid enforcement of a guarantee and mortgage, is *Liu v Adamson*.[203] In this case the Supreme Court of New South Wales heard a *Garcia* special equity relief claim argued for a de facto wife, Mrs Liu, who had signed a mortgage and a guarantee to secure her de facto partner's cost agreement with a solicitor. The de facto wife had been with her partner for 17 years and had five children from the relationship. From a

[199] (2000) 9 BPR 17,543, [55].

[200] Ibid, [60].

[201] Ibid.

[202] Ibid.

[203] (2004) NSW ConvR 56-074.

practical sense, the relationship closely resembled a marriage. The solicitor who took the security had called at Mrs Liu's home to get the security executed and was aware of the relationship that existed between the couple. Master Macready, in comparing marriage to a de facto relationship, saw that this involved no difficulty in regard to constructive notice for parties that deal with de facto couples, as there was no greater difficulty in establishing that parties are married than there is in establishing that they are in a de facto relationship. Macready M stated:

> The same trust and confidence which leads to the female surety receiving no sufficient explanation of the transactions purport and effect equally applies to a de facto relationship as to a marriage.[204]

Macready then concluded in his obiter remarks, that '… in these circumstances it seems to me that the principle in *Yerkey v Jones* should be extended to cover the situation presently before me.'[205]

The claim under the *Yerkey v Jones* / *Garcia* argument was not accepted, however, as Mrs Liu was not a volunteer. She was both a director and shareholder in some of the companies, and she had previously received a dividend of $55,000 from one of the companies. Mrs Liu was, though, granted relief under the *Contracts Review Act 1980* (NSW), as the contract was construed to be unjust. The comments of Master Macready in *Liu v Adamson* raised the clear possibility that, under a slightly different set of facts (where the de facto was a volunteer), some courts may be prepared to extend the *Garcia* special equity to de facto partners.

To what degree are the decisions of Bryson J in *State Bank of New South Wales v Hibbert; Groom v Hibbert* and Macready M in *Liu v Adamson* reconcilable with each other, and with *Garcia*? Macready M was dealing with a relationship that on the surface had the attributes of being equal or stronger (except for the existence of a marriage certificate) than Mrs Garcia's

[204] Ibid, 58,976 [22].

[205] Ibid, 58,977 [23].

or Mrs Groom's relationships, in that the relationship was long and had produced children. This comparison is summarised as follows:

Case name	Married or de facto?	Length of relationship	Number of progeny
Garcia	Married	18 years	2
Groom v Hibbert	De facto	8 years	0
Liu v Adamson	De facto	17 years	5

The decision of Macready M in *Liu v Adamson*, in accepting that the special equity could have applied to Mrs Liu's de facto relationship (if she had been a volunteer), was reconcilable to *Garcia,* in that:

- the de facto relationship Mrs Liu enjoyed was an exceptionally strong one in terms of its length and that children were raised;[206] and
- Macready M was satisfied that the financier was aware of the existence of Mrs Liu's de facto relationship.

Bryson J, in *State Bank of New South Wales v Hibbert; Groom v Hibbert*, was prepared to acknowledge that there was room to consider co-habitees and other relationships where the financier was aware that the surety reposed trust and confidence in the principal debtor, as Kirby J did in *Garcia*, but differed from Macready M in that he felt he was restrained due to a lack of judicial authority to extend *Garcia*.

Garcia and brothers-in-law – not successful

In *National Australia Bank Ltd v Starbronze Pty Ltd*[207] there was another type of relationship that may have come under the types of special relationships that *Garcia* made mention of, this time between brothers-in-law. The case involved Mr Lefkovic, who had a limited education in Israel and could not write in English. He provided security over his interest in a

[206] Particularly reconcilable to Kirby J's views in *Garcia* that, rather than limiting the equitable relief to one class of persons, married wives, the courts should instead be applying the relief to relationships that demonstrate particular needs and vulnerabilities.

[207] [2001] ANZ ConvR 247.

property so as to assist his brother-in-law, Mr Kranz, with a bank loan to Mr Kranz's company. The borrowing was to fund a speculative acquisition of shares. Mr Kranz was also Mr Lefkovic's accountant and had been his business adviser for some 12 years. The loan was defaulted upon and Mr Lefkovic sought relief against the bank's enforcement claim. Among other cross-claims, an extension of the special equity from *Garcia* was argued.

Coldrey J of the Victorian Supreme Court, after extensive reference to the decision in *Garcia*, was not prepared to extend the application of the *Garcia* principles to brothers-in-law. He stated:

> In my view, therefore, the current state of the law is that relationships of trust and confidence do not extend beyond the most intimate of family relationships. The fact that a person may have trust and confidence in another, (which trust and confidence may prove to be misplaced), cannot, without the added dimension of intimacy, attract this aspect of the equitable doctrine of unconscionability.[208]

On appeal[209] to the Supreme Court of Victoria Court of Appeal, Charles JA (with whom Winneke P and Eames JA agreed) affirmed the Victorian Supreme Court's decision. Charles JA, however, stated 'The application of *Garcia* is not, in my view, to be limited to the most intimate of family relationships.'[210] Charles JA went on to state that:

> The principle stated by the High Court in *Garcia* would make it unconscionable for a bank to enforce a guarantee given by a volunteer if it has not explained the situation to the guarantor, and does not know that an independent person has done so, if the bank knows that there was a relationship of trust and confidence between the guarantor and the debtor whose debt has been guaranteed. In Australia it remains therefore for the debtor to establish that the bank was aware of a relationship that put the bank on enquiry, such as that of husband and wife or solicitor and client, or that there was a relationship of trust and confidence between the debtor and third party.[211]

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[208] Ibid, 255 [84].

[209] *Kranz v National Australia Bank Ltd* (2003) 8 VR 310.

[210] Ibid, 319–320 [24].

[211] Ibid, 322 [31].

Even though there may have been trust and confidence between the brothers-in-law, there was no indication, on the facts of the case, that the bank should have been aware of the nature of the relationship between these brothers-in-law. Charles JA stated:

> Given the limited extent of the information available to the bank, I do not accept that the bank knew or should have assumed that there was a relationship of trust and confidence between Kranz and Tom Lefkovic, so as to bring into play the principles acted on in *Garcia*.[212]

The decision of the Court of the Appeal indicated the possibility that, faced with the right set of facts, a court in the future may be prepared to extend the type of special relationships where relief will be found to brothers-in-law (if a bank was on notice of there being a special relationship between the brothers-in-law).

Garcia and strong friends – not successful, but the court prepared to consider extension of _Garcia_ special relationships to include strong friendships

Will the *Garcia* principles be widened to include long-term friends? In *Equitiloan Securities Pty Ltd (formerly MC Mortgage Service Pty Ltd) v Mulrine*[213] the Australian Capital Territory Supreme Court examined a case where a Mr Mulrine mortgaged a block of land for security to a loan from Equitiloan Securities Pty Ltd to Mr Mulrine's friend. The purpose of the loan was to assist Mr Mulrine's friend with the set-up of a real estate agency business. In return for providing the loan, Mr Mulrine was offered the work of doing any maintenance tasks that the real estate agents required. The business subsequently failed, the loan was defaulted upon and an action seeking possession of Mr Mulrine's land was commenced by the financier. Mr Mulrine pleaded allegations that the financier acted unconscionably and by a cross claim repeated allegations of unconscionable conduct within the meaning of s 51AA of the *Trade Practices Act 1974* (Cth). Mr Mulrine's

[212] Ibid, 327 [44].

[213] [2000] ACTSC 48 (unreported, 16 June 2000, BC200003214).

counsel traced the development of the law on unconscionability, including discussions on such cases as *Amadio* and *Garcia*.[214]

Connolly J discussed the evidence that Mr Mulrine provided in regard to the relationship he had with his friend, and after examining the decision in *Garcia*, concluded that even though 'he "thought he was God" [in regard to how Mr Mulrine viewed his friend], there is nothing in the nature of the relationship that takes it beyond a long-term friendship.'[215] Connolly J could find no justification to extend the *Garcia* relationships to include strong friends. Connolly J also stressed the fact that Mr Mulrine would receive a benefit from providing the security, as important (eg he was not a disinterested party). Mr Mulrine failed in his unconscionability claim and the financier was granted possession of Mr Mulrine's land.

A more recent case where the courts have considered the friendship issue was the 2004 Queensland Court of Appeal decision in *ANZ Banking Group Ltd v Alirezai*.[216] The court was asked to consider whether in the case of an Iranian immigrant, Mr Alirezai, the types of relationships that might attract the special equity principles in *Garcia* should be extended to include an old trusted friendship that Mr Alirezai had developed. Mr Alirezai had developed a friendship with a fellow Iranian, Mr Sarlak, and had come to rely upon Mr Sarlak's support and advice. Mr Sarlak had, over a 13-year period, loaned money to Mr Alirezai. In 1991 at Mr Sarlak's request, Mr Alirezai provided a third party mortgage over Mr Alirezai's property at lot 2 Mount Rascal Rd, Toowoomba, in favour of the ANZ Banking Group Ltd (ANZ). The mortgage was to secure export facilities provided to Mr Sarlak's company, Sarlak Enterprises Pty Ltd. An additional third party mortgage over Mr Alirezai's property at lot 6 Mount Rascal Rd was provided to the ANZ in 1993 to secure Sarlak Enterprises Pty Ltd's facilities. At the ANZ's request, Mr Alirezai had obtained independent legal advice prior to executing the

[214] Ibid, [12].

[215] Ibid, [17].

[216] (2004) Q ConvR 54-601.

mortgages and had provided the ANZ with the solicitor's certificates of explanation of liability.

The company defaulted upon its borrowings and the ANZ issued proceedings against Mr Alirezai to recover possession of both properties. Summary judgment was obtained by the ANZ against Mr Alirezai and the ANZ sold lot 2. Mr Alirezai successfully appealed the ANZ's summary judgment for possession of lot 6. The ANZ prosecuted its claim for lot 6 in the Queensland Supreme Court. Mr Alirezai defended the claim and counter-claimed that the mortgages over both lots 2 and 6 should be set aside, and that lot 6 was sold at a gross under-value. A number of grounds were claimed in Mr Alirezai's counter claim, including unconscionable dealing and that the circumstances from *Yerkey v Jones* / *Garcia* where the special equity applied specifically to wives, should be widened to include other types of relationships such as the one Mr Alirezai enjoyed with his friend Mr Sarlak. Mr Sarlak claimed that this friendship had placed him in a position of disadvantage.

At first instance,[217] Mr Alirezai was unsuccessful before Mullins J of the Queensland Supreme Court, in having the court recognise that a relationship between friends was one contemplated to be caught under the special equity in *Yerkey v Jones* / *Garcia*. Mullins J stated that:

> Where the joint judgment in *Garcia* predicted that the principles applied in *Yerkey v Jones* may apply to other long term and publicly declared relationships short of marriage between members of the same or opposite sex, they were confining the development of the principles applied in *Yerkey v Jones* to relationships of a like nature to marriage. The principles in *Yerkey v Jones*, as the joint judgment in *Garcia* makes clear, have no application whatsoever to Mr Alirezai's relationship with Mr Sarlak.[218]

In regard to unconscionability, Mullins J found that as the elements set down in *Amadio* had not been proved, no such cause of action existed for Mr Alirezai.[219] This was due to two reasons. First, that the ANZ were unaware

[217] *Australian and New Zealand Banking Group Ltd v Alirezai* [2002] ANZ ConvR 597.

[218] Ibid, 613 [168].

[219] Ibid, 613 – 614 [170] – [175].

that Mr Alirezai did not stand to obtain any financial benefit out of the transaction. Second, that the ANZ was also unaware that he was in a situation of special disadvantage (due to the level of trust that Mr Alirezai placed in his old friend Mr Sarlak) in relation to providing his security, and even had the bank been aware, the independent legal advice that Mr Alirezai had obtained, defeated such a claim.[220]

The matter was heard on appeal by the Supreme Court of Queensland Court of Appeal (McMurdo P, Jerrard JA and Wilson J).[221] In a two to one decision, the Court of Appeal (Jerrard JA dissenting) dismissed the appeal from Mr Alirezai, with McMurdo P having observed that:

> A close friendship between borrower and surety based on shared cultural and religious values does not in itself require a banker to do more than what was done here, namely, ensure the surety obtains independent legal advice on the transactions.[222]

McMurdo P's comments were interesting, in that she saw no reason why there should not be a widening of the *Garcia* classification of special relationships beyond a wife and husband relationship. McMurdo P stated:

> I do not understand *Garcia* to necessarily limit appropriate equitable relief to marriage or marriage-like relationships, which involve what is sometimes referred to as sexually transmitted debt. What was important in *Garcia* was that the marriage relationship itself put the bank on notice that there was a relationship of trust and confidence between the debtor and the surety so that it was unconscionable for the bank to enforce the surety without having explained, or having had explained to the surety, the effect of the transaction. Special relationships of sufficient trust and confidence in which one party could abuse that trust and confidence so as to invoke equitable relief for transactions entered into by the other are not a closed category; they could, for example, arise in some parent-child relationships or perhaps in the relationship between a disabled person and carer; many other potential examples can be envisaged.[223]

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[220] Ibid.

[221] *ANZ Banking Group Ltd v Alirezai* (2004) Q ConvR 54-601.

[222] Ibid, 61,093 [53].

[223] Ibid, 61,090 [39].

Jerrard JA also agreed with this widening of *Garcia* to include relationships such as close friendships, and referred[224] to Charles JA's judgment in the Victorian Court of Appeal case of *Kranz v National Australia Bank Ltd*.[225]

Wilson J, while acknowledging the trial judge's decision that *Garcia* was limited to marriage and similar intimate relationships and that that may be a too narrow approach, stated that he believed that the Court of Appeal did not have any authority to widen the *Garcia* principle – that this was a question for the High Court to determine in an appropriate case.[226]

Jerrard JA differed from McMurdo P and Wilson J, in his view of the importance of the failure of the bank to explain the full borrowings and financial position of the debtor to the surety. Jerrard JA decided that this failure denied the bank the ability to defend the claim of unconscionability, or a *Garcia* special equity argument, based on a reliance on the surety having received independent legal advice. Jerrard JA stated:

> …I am suggesting that it is not sufficient for a bank in those circumstances simply to rely upon the giving of advice where the bank has no reason to believe that either the solicitor who certifies the advice was given, or that the surety who enters into the transaction, understands at all any details of the financial circumstances that make it unlikely that the property will ever again be beneficially enjoyed by the surety.[227]

Jerrard JA then referred to the High Court decision in *Amadio* and the House of Lords decision in *Royal Bank of Scotland v Etridge (No 2)*[228] as authority for this proposition.

Wilson J concurred with McMurdo P, that the non-provision of financial data did not negate the effectiveness of independent legal advice in satisfying a

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[224] Ibid, 61,096 [82].

[225] See, in this thesis, prior discussion of that case, which dealt with the relationship between brothers-in-law.

[226] Ibid, 61,103–61,104 [115].

[227] Ibid, 61,097 [89].

[228] [2002] 2 AC 773.

bank's obligations to ensure that a surety in a position of special disadvantage is not taken unconscientious advantage of. Wilson J quoted Mason J in *Amadio*, where Mason J stated:

> It has been said that this duty to disclose does not require a bank to give information as to matters affecting the credit of the debtor or of any circumstances connected with the transaction in which he is about to engage which will render his position more hazardous (*Wythes v Labouchere*, (1859) 3 De G & J 593 at p 609 [44 ER 1397, at p 1404] per Lord Chelmsford LC). No surety is entitled to assume that the debtor has not been overdrawing, the proper presumption being in most instances that he has been doing so and wishes to do so again (*London General Omnibus Co Ltd v Holloway* [1912] 2 KB 72, at pp 83–84, 87).
>
> But the fact that a bank's duty to make disclosure to its intending surety, arising from the mere relationship between principal creditor and surety, is so limited [that it] has no bearing on the availability of equitable relief on the ground of unconscionable conduct. A bank, though not guilty of any breach of its limited duty to make disclosure to the intending surety, may none the less be considered to have engaged in unconscionable conduct in procuring the surety's entry into the contract of guarantee.[229]

So even though the guarantor was not successful in *Alirezai*, the importance of the case was that the decision made it clear that at least two of the judges of the Queensland Court of Appeal were prepared to entertain widening of the class of special relationships that a *Garcia* claim would recognise to include strong friendships.

Garcia and a wife who is separated from her husband - successful

In *Wenczel v Commonwealth Bank of Australia*[230] the Supreme Court of Victoria looked at whether the special *Garcia* equity still applied in a scenario where, at the time of the loan being made, the husband had left the wife, but the couple were still married. The bank had argued that the confidence a wife has in her husband included confidence in his ability to manage the financial affairs of the marriage, and that where the marital relationship was severed by separation then so too was the confidence in the husband's management of the wife's financial affairs.

[229] (1983) 151 CLR 447, 463–464.

[230] [2006] VSC 324 (unreported, 8 September 2006, BC200607068).

The facts were that Mr Wenczel had left the family home on 13 February 2001. Subsequent to his leaving, he incurred the lease liability for some luxury cars (a BMW and Range Rover), as well the liability for other debts. On 11 July 2001 Mr Wenczel obtained approval from the Commonwealth Bank for a business loan of $76,000 in the name of his company, Wenczel Consulting Services Pty Ltd. Mr Wenczel was the sole director and shareholder of this company. Security for the loan was to be a second mortgage over the family home owned by Mrs Wenczel as well as a guarantee by Mrs Wenczel to secure the company's liability to the bank.

The bank had identified Mrs Wenczel in its own security classification terms as a 'vulnerable guarantor'. The bank's procedures for this type of guarantor required such things as:

- for the documents to be signed in front of a bank staff member, with the debtor (husband) not present;
- for the bank to ask if the guarantee had been signed by Mrs Wenczel in her own free will;
- for the bank to ask if Mrs Wenczel understood what giving a guarantee meant; and
- for Mrs Wenczel to be given the opportunity to seek legal advice.

The documents were posted out to Mrs Wenczel with a request that she contact the bank to arrange for the documents to be signed at the bank. The bank did not follow its own procedures and the documents were not witnessed before a member of the bank's staff. No independent legal advice was obtained by Mrs Wenczel.

Mrs Wenczel alleged that some time after she had received the loan documents, her husband called at her home to see her. Mrs Wenczel advised that she asked her husband for details as to his financial position and the reasons for the loan. She claimed that in response to these queries her husband became aggressive and verbally abused her, and threatened that he would sell her property unless she signed the security documentation. Mrs

Wenczel signed the documentation because she was '… in reconciliation mode, hoping that he would come to his senses and return to his devoted wife and loving children …'[231] The couple did not become reconciled. The loan was drawn down and, after its having fallen into arrears, the bank served demand upon Mrs Wenczel for her liability under the guarantee and mortgage. Mrs Wenczel sought a declaration that her security be set aside in equity on the basis that it was procured in circumstances amounting to unconscionable conduct, or alternatively undue influence or duress. Mrs Wenczel also sought to rely on the special equity in *Garcia*. The bank counterclaimed for recovery of its debt and possession of the property, as well as joining Mr Wenczel and the company to the counterclaim.[232]

In rejecting the argument of the bank that the *Garcia* special equity could not apply between a separated wife and her husband, Habersberger J stated:

> Whatever may be the position in family law, it seems to me that in this context the mere fact of separation is not necessarily fatal to the plaintiff's case. What is important, in my opinion, is whether the confidence that is said to be reposed by the wife in the husband still subsists in circumstances where they have been separated for a period of over five months.[233]

Habersberger J looked at the essence of the dependence of the wife on the husband in this relationship, and saw that '… the emotional vulnerability of a woman such as the plaintiff who was vainly trying to hold a failing marriage together is the very weakness which this equity seeks to protect.'[234] Despite Mrs Wenczel being separated she had still reposed trust and confidence in her husband.

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[231] Ibid, [42].

[232] Neither the company nor Mr Wenczel entered a defence and default judgment was entered against them. Mr Wenczel subsequently became bankrupt.

[233] [2006] VSC 324 (unreported, 8 September 2006, BC200607068), [135]–[136].

[234] Ibid, [136].

Mrs Wenczel was successful in establishing that the *Garcia* special equity applied and a declaration was made that her mortgage be set aside.[235] So the mere fact that a wife may be separated from her husband is not necessarily a factor that would defeat a *Garcia* special equity claim. If the financier is unable to establish that the normal confidence a wife placed in her husband ceased due to separation, then such a defence by a financier to reject a claim for the special *Garcia* equity will likely not succeed.

***Garcia* and a wife who subsequently divorces - successful**

In *Commonwealth Bank of Australia v Horkings*,[236] the Victorian Court of Appeal looked at the position of a wife (Mrs Khouri, who upon re-marriage becomes Mrs Horkings) who had guaranteed several bank debts belonging to her husband (Mr Khouri). Mrs Khouri subsequently divorced and re-married without having first obtained the release from her guarantee. The guarantee was supported by a mortgage over the family home. Mr Khouri then defaulted and became bankrupt, and action was taken under Mrs Khouri's guarantee and mortgage for recovery of the debt and possession of the property. Mrs Khouri sought relief based on both *Amadio* unconscionability and the *Garcia* special equity and was successful at first instance. The bank appealed the decision to the Victorian Court of Appeal.

In the circumstances, Winneke P (with Phillips and Buchanan JJA agreeing) concluded that the CBA would be '… obtaining an unconscientious advantage …' over the respondent if it were permitted to enforce that security. Winneke P found, in respect of this transaction, that the principles explained by the High Court in *Yerkey v Jones* and *Garcia* were applicable.[237] What was surprising was that Mrs Khouri was found to be a volunteer, despite her having been both a director and company secretary for

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[235] Habersberger J also found in favour of Mrs Wenczel in regard to both her undue influence and duress claims. Given that Habersberger J had found in favour of Mrs Wenczel for three of her four causes of action, he ruled that he had no need to consider whether relief as a result of unconscionable conduct was also warranted [161].

[236] [2000] VSCA 244 (unreported, 22 December 2000, BC200008340).

[237] Ibid, [21].

the debtor company (Mrs Garcia had only been a director of her husband's company, as opposed to the dual office holding of Mrs Khouri).

Garcia and ex-wives – successful

Simos J in the NSW Supreme Court, in the case *Fraser v Power*,[238] examined the ability of the law to assist an ex-wife (Mrs Fraser) who had signed a mortgage to benefit her ex-husband (Mr Fraser). The couple had acquired the property in their joint names whilst married in 1975. They were divorced in 1979, with the property remaining in their joint names. The ex-wife maintained that the husband held his interest in the property upon trust for her. In 1987 they executed a third party mortgage over the property in favour of National Westminster Finance Australia Ltd to secure the ex-husband's business liabilities. Independent legal advice was not provided. National Westminster Finance Australia Ltd subsequently assigned the mortgage to the first (Ms Power) and second (Denkirst Investments Pty Ltd) defendants, who relied upon covenants in the memorandum to the mortgage to hold the ex-wife severally liable under the mortgage for the liabilities of her ex-husband to them. The ex-husband became bankrupt in 1992. The ex-wife sought a declaration that she was the beneficial owner of the whole of the property, as well as a declaration that the mortgage was void on a number of grounds, including unconscionability and that the mortgage was unjust within the meaning of the *Contracts Review Act 1980* (NSW). The proceedings were defended by the first and second defendants, who also joined National Westminster Finance Australia Ltd to the action.

Although the ex-wife had argued for relief to have the mortgage terminated on the basis of unconscionability, the defendants had argued that *Garcia,* as it interpreted *Yerkey v Jones*:

> … was authority for the proposition that in the present case the third defendant [the mortgagee] could not be held to have taken unconscientious advantage of the position of special disadvantage in which the plaintiff was placed because of the fact that at the time of the execution of the subject mortgage the plaintiff and her former

[238] (2001) Aust Contract R 90-127.

husband had been divorced for some time.[239]

Simos J quoted[240] from the joint judgment of Gaudron, McHugh, Gummow and Hayne JJ in *Garcia* to rebut the defence's argument, as follows:

> The resolution of questions arising in the context of other relationships may well require consideration of other issues. Thus to take one example, if cohabitation is taken as a criterion, what should a lender know or seek to find out about the nature of the relationship between the parties? But those issues did not arise and were not debated on the hearing of this appeal.[241]

Simos J therefore did not feel restricted that *Garcia* could not be extended to the relationship between ex-wife and ex-husband. Simos J had found that the ex-wife had trusted her ex-husband and that it was unconscionable conduct[242] for the mortgagee to take the mortgage in the manner in which they did. Simos J ordered the mortgage to be set aside.

Garcia principles applied to an ex-wife surety despite evidence of self-interest (ie the surety was not a volunteer) – unsuccessful upon appeal to the Full Federal Court

In *Westpac Banking Corporation v Paterson*[243] the Full Federal Court examined the position of Mrs Jonnie Paterson, a third party mortgagor, who had provided a mortgage over a North Rocks residence she had lived in. The property was owned jointly by herself and her ex-husband, Mr David Paterson. Mrs Jonnie Paterson was financially dependent upon Mr Paterson and retained trust and confidence in him for financial matters. They had divorced in the 1980s and a Family Court settlement had provided that her former husband was responsible for the debt. The property was subject to a home loan from Barclays in favour of Mr David Paterson and Mrs Jonnie

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[239] Ibid, 91,526 [110].

[240] Ibid, 91,626 [112].

[241] (1998) 194 CLR 395, 403–404.

[242] The *Garcia* special equity was not specifically mentioned by Simos J as the reason for finding in favour of the security provider – Simos J found that the bank's actions constituted unconscionable conduct. Taking of the security was also found to have been 'unjust' within the meaning of the *Contracts Review Act 1980* (NSW).

[243] (2001) 187 ALR 168.

Paterson. A Westpac Banking Corporation ('Westpac') home loan in the names of Mr David Paterson and his new wife Mrs Tracy Paterson had been used to refinance the Barclays home loan, with the mortgagors being Mr David Paterson and Mrs Jonnie Paterson. The refinancing of the home loan to Westpac had been argued by the Patersons as being necessary in order for Mr Paterson's company business, Endormer Pty Ltd, to obtain an overdraft. The property was also used as security for a guarantee to the company from Mr David Paterson and Mrs Tracy Paterson. Westpac had argued that Barclays had told the Patersons they needed to refinance. Like Mrs Garcia, Mrs Jonnie Paterson had maintained that she had misunderstood the transaction she had provided security for, particularly the risks involved.

Mrs Jonnie Paterson's position was markedly different from that of Mrs Garcia in three areas.

The first difference was that the bank had recommended to Mrs Jonnie Paterson to obtain independent legal advice prior to the execution of the mortgage. She had declined the recommendation, having advised that she had already obtained such advice in connection with a prior facility with Barclays.

The next difference was that the bank staff had provided a detailed explanation of Mrs Jonnie Paterson's liability to her, in contrast to the one-minute explanation that Mrs Garcia had received, ie Mrs Jonnie Paterson could not have been mistaken about the effect of the mortgage.

The final difference was that the Westpac debt had related to refinance of a loan originally advanced to assist with Mrs Jonnie Paterson's purchase of the North Rocks home (the security property) ie Mrs Jonnie Paterson had not been a volunteer.

O'Connor J of the Federal Court at first instance,[244] after discounting that *Amadio* unconscionability applied,[245] formed the view that relief should be granted due to the special equity in *Yerkey v Jones* and *Garcia* applying (despite recognising that Jonnie Paterson was not a volunteer), as:

> She was in the Court's view in a worse situation than if she had been still married to Mr David Paterson. She demonstrated her "trust and confidence" in him by allowing him to deal with the bank in all respects in relation to the transaction.[246]

Clearly O'Connor J was bringing the ex-spousal relationship into the context of that discussed in *Garcia*, as being one of those *other relationships*, which '… may well require consideration of other issues …'[247]

As the essential requirements previously mentioned for a *Yerkey v Jones* and *Garcia* special equity relief claim were not met, on appeal the Full Federal Court declined to follow O'Connor J's decision.[248] This absence of the essential requirements led the Full Federal Court to find that it was not necessary to consider whether the principles in *Garcia* could apply to a relationship of former spouses where financial dependence and trust still existed.[249]

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[244] [2001] FCA 556 (unreported, 14 May 2001, BC200102333).

[245] There was no evidence that Mr David Paterson made any misrepresentation to Mrs Jonnie Paterson about the transaction. In addition, the evidence suggested that Mrs Jonnie Paterson was not a volunteer, and made the decision to enter into the transaction with Westpac with a clear appreciation of the risks she was undertaking, and had declined to take independent legal advice. 'The court should not find that Westpac took any unconscientious advantage of Jonnie Paterson's position.' Ibid, [75].

[246] Ibid, [89]. This was despite O'Connor J previously having stated, at [81]: 'In *Garcia*, the High Court imposed a special obligation on creditors dealing with married women as sureties because, it held, the creditor ought to suppose that a married woman would trust and confide in her husband. But there is no reason why a creditor should make any such assumption with respect to an ex–wife whose ex-husband has remarried and is living elsewhere.'

[247] As per Gaudron, McHugh, Gummow and Hayne JJ in *Garcia v National Australia Bank Limited* (1998) 194 CLR 395, 404 [22].

[248] *Westpac Banking Corporation v Paterson* (2001) 187 ALR 168.

[249] Ibid, 174 [26].

Janine Pascoe in her article '*Garcia* extended – inch by inch'[250] hints at the possibility, following the Federal Court's deliberations on Mrs Paterson's circumstances, that if the appropriate case came before the Federal Court for an ex-wife securing a former husband's liability, the Federal Court might apply the *Garcia* principles, given that both the Federal Court at first instance, and the Full Court on appeal, conceded that an ex-wife may place trust and confidence in her former spouse.[251]

Garcia principles applied to married men - unsuccessful

In the Victorian Supreme Court, Hansen J, in dealing with a case of undue influence touched on the issue whether *Garcia* principles could be applied to married men, in *Commonwealth Bank of Australia v Longo*.[252] In that case a husband alleged that his wife had exercised undue influence over him, in regard to a mortgage they had signed over their farm to benefit the wife and their adult children. The husband alleged that his wife spoke better English than him and that she had dealt exclusively with the bank. He claimed that he had relied on and trusted her in regard to her dealings with the bank, that she had placed emotional pressure upon him to sign the mortgage and that she had not explained to him the nature and effect of the mortgage.

Hansen J acknowledged that:

> … the relationship of husband and wife is not one that gives rise to a presumption of undue influence. It is a relationship in which the parties may take different roles in relation to business or financial matters, or any other type of matter, and in which one party, be it husband or wife, may leave the relevant inquiry and judgment to the other. That is not inconsistent with, but consistent with, the trust and confidence which underlies the relationship and which one party has in the other.[253]

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[250] Janine Pascoe, '*Garcia* Extended – Inch by Inch' (Pt 1) (2004) 19(7) *Australian Banking and Finance Law Bulletin* 107; Janine Pascoe, '*Garcia* Extended – Inch by Inch' (Pt 2) (2004) 19(8) *Australian Banking and Finance Law Bulletin* 120.

[251] Janine Pascoe, '*Garcia* Extended – Inch by Inch' (Pt 1) (2004) 19(7) *Australian Banking and Finance Law Bulletin* 107, 109.

[252] [2001] VSC 191 (unreported, 15 June 2001, BC200103198).

[253] Ibid, [115].

Hansen J then referred to the judgment of Gaudron, McHugh, Gummow and Hayne JJ in *Garcia*. He quoted their discussion in regard to the marriage relationship, having noted that it was not in the context of undue influence but in the context of unconscionability that it was examined:

> The marriage relationship is such that one, often the woman, may well leave many, perhaps all, business judgments to the other spouse. In that kind of relationship, business decisions may be made with little consultation between the parties and with only the most abbreviated explanation of their purport or effect. Sometimes, with not the slightest hint of bad faith, the explanation of a particular transaction given by one to the other will be imperfect and incomplete, if not simply wrong. That this is so is not always attributable to intended deception, to any imbalance of power between the parties, or, even, the vulnerability of one to exploitation because of emotional involvement. It is, at its core, often a reflection of no more or less than the trust and confidence each has in the other.[254]

The majority in *Garcia* unfortunately did not explore the husband-wife relationship to any great extent. They stated 'It may be that those principles will find application where the husband acts as surety for the wife but again that is not a problem that falls for decision here.'[255]

Hansen J concluded that those observations from *Garcia* were born of commonplace experience in human affairs.[256] Unfortunately he did not explore the relationship further, as he decided on the facts of the case that the wife had not put undue emotional pressure upon the husband.[257] Hansen J also noted that in a practical sense the husband acted like a partner in the business and shared in all the profits, and was thus not just an innocent bystander to the transaction (ie the husband was not a volunteer).[258]

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254 Ibid.

255 *Garcia v National Australia Bank Limited* (1998) 194 CLR 395, 404 [22] (Gaudron, McHugh, Gummow and Hayne JJ).

256 [2001] VSC 191 (unreported, 15 June 2001, BC200103198), [116].

257 Ibid, [118].

258 Ibid.

Garcia principles applied to the relationship of siblings - unsuccessful

Hedigan J in the Supreme Court in Victoria in the case of *Equuscorp Pty Ltd v Worts*[259] was called upon to examine whether the special equity in *Garcia* would extend to include a sibling relationship.

Mr Syd Worts had guaranteed his brother, Alan Worts, in regard to equipment finance for two vehicles for his brother's business use. The business had subsequently failed, the finance facility had gone into default and Mr Syd Worts' guarantee was called upon and proceedings for recovery were commenced by the financier. It was argued by Mr Syd Worts' counsel that a presumption of trust and confidence arose from the sibling relationship with his brother Alan, and that this relationship attracted equity's intervention as it had for wives, in *Yerkey v Jones* and *Garcia*.

Hedigan J, however, had not found a need to explore to any length whether this special relationship extended to siblings. He found two grounds to distinguish the facts of the Worts case from *Garcia*. The first difference was that in *Garcia* it had been left to a person (the husband of Mrs Garcia) in whom the trust and confidence was reposed, to explain to the surety the relevant facts of the transaction. This was not the case with the Worts. In the Worts case, the financier had spoken directly to the guarantor and had explained the transaction conditions. 'Here the fact is that the guarantor was told everything …'[260] Hedigan J concluded.

The second difference was:

> … the evidence concerning Syd Worts' business acumen. The second defendant was neither [in the same category as] *Amadio* nor *Yerkey*. He was a very experienced businessman, knew about guarantees, had them explained in the past and entered into them in the past. He had, as I have found, a detailed conversation with the mortgagee (with whom he had a long and well-developed commercial connection) concerning the state of the principal's indebtedness and the risks.[261]

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[259] [2000] VSC 179 (unreported, 10 May 2000, BC200002667).

[260] Ibid, [29].

[261] Ibid, [30].

Clearly this was not the same position as Mrs Garcia had been in. Although Mrs Garcia had limited business experience in running her physiotherapy practice and had previously signed some mortgages, she was not an experienced business person, and not one who had benefited from an informed conversation with the financier in regard to a detailed analysis of the debtor's liability and the risks involved.

Hedigan J saw that '… it would strike one as a palpable absurdity to suggest that this was a case which attracted the intervention of equity to prevent imposition.'[262] In addition, counsel for the financier argued that the relationship between these two brothers was not one where one could establish any presumption of trust and confidence. Hedigan J argued that at no time did Syd Worts place any reliance, let alone trust and confidence, in Alan Worts at the time of entering into the guarantee. The Worts had last been in business together 35 years ago, and generally (other than at the time of providing the guarantee) spoke once every two or three months, if that. Hedigan J concluded that it was '… a hopeless case to suggest that the guarantor fell within the range of equitable protection established by the cases to which I have referred [*Yerkey v Jones* and *Garcia*].'[263]

Garcia principles applied to the relationship of parent and child – mixed results

In the Western Australia Supreme Court case of *Choules v Siglin*,[264] Bredmeyer M was asked to consider whether the special equity under *Garcia* could be extended to apply to a situation where a 75-year-old widowed mother had borrowed and mortgaged her home to secure a $400,000 debt to assist her 47 year old son with an investment (and in the process refinance an existing St George Bank mortgage the mother had taken out). Although Bredmeyer M had found that *Garcia* did not apply, given that the mother was not a volunteer (as the transaction allowed her prior mortgage to be

[262] Ibid.

[263] Ibid, [32].

[264] [2001] WASC 234 (unreported, 31 August 2001, BC200105150).

refinanced) and that she was not a surety (but the debtor), in terms of whether the special equity in Garcia could have had a wider application, Bredmeyer M stated:

> Those principles in *Garcia* taken from *Yerkey v Jones* are not limited to wives and husbands. It so happened that *Yerkey v Jones* and *Garcia* each concerned a wife and a husband but the majority of the High Court in *Garcia* at para 22 said, in effect, that the principles applied in *Yerkey v Jones* may well find application to other relationships.[265]

Having found that *Garcia* did not apply to the mother (and nor did *Amadio* unconscionability), Bredmeyer J found in favour of the financier. Although this decision was reversed on appeal on other grounds by the Full Supreme Court of Western Australia,[266] Scott J (with whom Wallwork J agreed) stated:[267]

> That is not, however, to exclude the possibility that the law may extend to cover situations of the type presently under consideration. The mortgage by an elderly mother of her property in order to raise money for a child might well come within that category.[268]

Elizabeth Stone, however, commented in regard to this decision, that she believes that the lengthy analysis that the High Court provided in *Garcia*, in regard to it being common for a wife to leave her affairs to her husband, does not justify an assumption in this case that a parent and child relationship was the same type of relationship, nor one which third parties would assume existed.[269]

In the Supreme Court of the Australian Capital Territory Court of Appeal case of *Watt v State Bank of NSW*,[270] the court was asked to consider that the relationship between parents and their children was one which should attract

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[265] Ibid, [19].

[266] *Siglin v Choules* [2002] ANZ ConvR 345.

[267] Note, though, that Scott J had referred to *Royal Bank of Scotland plc v Etridge* (No 2) [2002] 2 AC 773 prior to reaching the above conclusion, which dealt with Dixon J's first category (undue influence) in *Yerkey v Jones*, and not the second category of the special equity. So one might question the guidance that can be obtained from this decision.

[268] [2002] ANZ ConvR 345, 352 [54].

[269] Elizabeth Stone, 'The Distinctiveness of *Garcia*' (2006) 22 *Journal of Contract Law* 170, 181.

[270] [2003] ACTCA 7 (unreported, 13 March 2003, BC200300833).

the same type of equity given to wives. The case involved parents guaranteeing their daughter and son-in-laws' company borrowing facilities (the company operated a newsagency). Higgins CJ and Crispin P noted Kirby J's comments at page 431 in *Garcia*, that the special equity is referred to generally as being applicable to '… a relationship involving emotional dependence on the part of the surety towards the debtor …'[271] and noted that this broad formulation was not followed by the other court members in *Garcia*. Higgins CJ and Crispin P discussed at some length the parent and child relationship, and concluded that:

> Parents do not normally leave business decisions to their children or rely unquestioningly on their judgment. On the contrary, the role of parents involves being mentor and guide and parents tend to remain concerned about the wisdom of their child's decision, even when they reach adulthood. … it cannot be said that the relationship of parent to child or parent to son or daughter-in-law is of such a character that any potential lender who is aware that the child or a partner of the child of the surety must by reason of that fact alone be taken to appreciate that the surety "may well receive from the debtor no sufficient explanation of the transaction's purport and effect" (*Garcia* at 409 [33]).[272]

Higgins CJ and Crispin P then went on to discuss that the real vulnerability of parents stems from their love for their children and that 'The principles in *Yerkey v Jones* and *Garcia* offer no protection for people lured into improvident transactions by feelings of this kind.'[273]

To the detriment of the parents' case was that they were not volunteers, as they were both shareholders and directors in the business that was guaranteed (and at the time they initially provided their guarantee, the business was performing well).

The court therefore declined to find that equity's intervention could be justified and found in favour of the financier.

[271] Ibid, [20].

[272] Ibid, [21].

[273] Ibid, [22].

An earlier single judge decision by Levine J in the Supreme Court of NSW, *State Bank of New South Wales Ltd v Layoun*[274] (*Layoun*), was not referred to by the Supreme Court of the Australian Capital Territory Court of Appeal in *Watt v State Bank of NSW*. In *Layoun,* Syrian parents had guaranteed their eldest son's loans. The guarantors argued that the special relationship in *Garcia* extended to parents and child (a separate argument that the special relationship should be considered in a cultural context as well, on the basis of the trust and confidence imposed in the parent-first son relationship as part of the Syrian culture, was not accepted by the court).[275] Although it was acknowledged that the facts of *Garcia* did not extend to cover the scenario presently before the court, Levine J accepted that 'Those principles are applicable on a "case by case basis" and this case is one of them.'[276] In addition, *Amadio* unconscionability was also argued. The value of the judgment is somewhat complicated by the fact that Levine J dealt with both the *Garcia* and *Amadio* arguments together.[277] Levine J therefore found that the special equity under *Garcia* applied to the Syrian parents (and that *Amadio* unconscionability was also established)[278] and the parents thus were successful in obtaining relief.

As *Layoun* was not subsequently followed in *Watt v State Bank of NSW*, and there was little by the way of detailed discussion justifying the expansion of relationships as per *Garcia* to include parent and child, it is felt the *Layoun* decision should be viewed as an anomaly and one unlikely to be followed.

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[274] (2001) NSW ConvR 55-984.

[275] Ibid, [48]–[49].

[276] Ibid, [75].

[277] Elizabeth Stone, 'The Distinctiveness of *Garcia*', (2006) 22 *Journal of Contract Law* 170, 183.

[278] (2001) NSW ConvR 55-984, [75].

4.3 SUMMARY OF *GARCIA* – HAS THE *GARCIA* DECISION PRODUCED SIGNIFICANT ADVANTAGES FOR POTENTIAL LITIGANTS AGAINST FINANCIAL INSTITUTIONS?

There has been some willingness of the lower courts, since the High Court decision in *Garcia*, to expand the nature of relationships under which a special emotional relationship may exist, to enable guarantors who were under such a special relationship and could demonstrate that they were volunteers to obtain relief under the special equity in *Garcia*. Clearly though, the cases this thesis has examined from the years since the *Garcia* decision do not indicate any consistency in the approach by the various courts to expand the class of emotional relationships beyond married women. This is somewhat surprising, given the assumptions that *Garcia* makes about the nature of a marital relationship. As Michael Main commented:

> Hypothetically, there are probably as many different sorts of marital relationships as there are marriages and at the very least, it seems that there is an extremely negative stereotype of marriage to the effect that a male spouse is presumed to be incapable of accurate or honest communication to a female spouse, which from a male perspective is just as offensive as the outmoded stereotype of a wife with no capacity to comprehend financial or business matters.[279]

Elizabeth Stone in her article 'The Distinctiveness of *Garcia*'[280] was, however, critical of commentators and judges who too readily attempt to extend the relationship of trust and confidence beyond that of a wife to her husband. Stone commented:

> Unfortunately, many commentators and judges have used the phrase ["relationship of trust and confidence"] in shorthand, and appear to have overlooked for what purpose the trust and confidence must be established. It is not enough to show that the relationship could, within the ordinary English meaning of the words, be described as one of "trust and confidence". It must be established that it is one of such unusual trust and confidence that

[279] Michael Main, '*Garcia v National Australia Bank* – Having it Both Ways' in 'Nuts & Bolts of Securities Law – Guarantees 1999 Seminar Papers 1999', Legal and Accounting Management Seminars Pty Ltd (1999), 5.

[280] (2006) 22 *Journal of Contract Law* 170.

> ignorance of one's own affairs is an outcome both likely and defensible. … The reasoning in *Garcia* is based on the second category in *Yerkey v Jones*, and its grounding on the extraordinary intimacy of the marriage relationship limits its proper application to circumstances where a choice to remain ignorant of one's own financial and legal affairs is not merely possible but normal; not merely understandable but excusable. Beyond marriage, de jure or de facto, such relationships are unlikely to be found. [281]

There has been little significant movement away from the position taken by Bryson J of the NSW Supreme Court in *State Bank of New South Wales v Hibbert*, where his Honour concluded that it is not reasonable to consider any widening of the special equity class established for married women in *Garcia* (when called upon to determine if de facto relationships could be included), even after specifically considering Kirby J's approach in *Garcia*, but then noted that there was no judicial authority to follow it. It is suggested, though, that there is no reason why the law will not continue to develop in this area of how equity recognises and treats different types of relationships. Whether this be through an approach adopting Kirby J's methodology in *Garcia,* or some other, and reflecting the expectations of present day society – that there are many equally valid strong relationships of trust similar to the relationship married women have with their husbands (in terms of vesting close trust in them). These relationships are just as deserving of the courts' recognition and protection that Mrs Garcia benefited from.

In examining the impact of the development of the special *Garcia* equity in regard to its widening applicability to special relationships, the comments of Dal Pont[282] need to be considered, that the law provides little encouragement for certain guarantors to take positive steps to understand the nature and effect of guarantee commitments, but rather shifts the onus to creditors to ensure such understanding. Blanchard J of the New Zealand Court of Appeal

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[281] Ibid, 180 and 188.

[282] G Dal Pont, 'The Varying Shades of "Unconscionable" Conduct — Same Term, Different Meaning' 2000 (19) *Australian Bar Review* 135. Dal Pont saw *Garcia* as an example of '… the chameleon-like characteristics of the concept of "unconscionable" conduct in modern Australian contract law', at 137.

in *Wilkinson v ASB Bank Ltd*,[283] however, expressed a view that questions the impact on the finance industry from the wider interpretation:

> Sympathy for a victim of undue influence or misrepresentation should not lead a court into the error of imposing upon lenders an unrealistic standard. Transactions in which one relative assists another to borrow are commonplace. It would be unfortunate if a few hard cases were to discourage financiers from lending to borrowers in need of such assistance for fear of being found to have fallen short of perfection in their lending practices.[284]

Dal Pont also lamented the lack of clarity that applies to different relationships for unconscionability (Dal Pont 'grouping' the special equity as being part of unconscionability), and saw the law as discriminating by making it easier to set aside a guarantee for undue influence or unconscionability against some classes of persons as opposed to others (similar to the discussion of Kirby J in *Garcia*). Dal Pont saw that this lack of neutrality was emphasised in the High Court's adoption in *Garcia* of the special relationship that exists for married women. An examination of the cases subsequent to *Garcia*, and the preparedness of the Justices of the High Court in *Garcia* to acknowledge a possibility that other relationships may be considered as deserving of application of the special equity found in that case, could indicate the beginnings of development in this area of law to recognise other types of relationships and avoid allegations of a lack of neutrality.

As to what rules can be determined for future cases, concerning how the courts will apply *Garcia* and extend the concept of special relationships, looking at Deane J's statement (even though it only mentions unconscionability) in the case of *Commonwealth v Verwayen*,[285] is of value:

> Ultimately … the question whether departure from the assumption [or representation] would be unconscionable must be resolved not by reference to some pre-conceived formula framed to serve as a universal yardstick but by reference to all of the circumstances of the case, including the reasonableness of the conduct of the other party

[283] [1998] 1 NZLR 674.

[284] Ibid, 689.

[285] (1990) 170 CLR 394.

> in acting upon the assumption [or representation] and the nature and extent of the detriment which he would sustain by acting upon the assumption [or representation] if departure from the assumed state of affairs were permitted.[286]

A practical summary of the lesson for financiers from the *Garcia* case is provided for in the Su-King Hii article 'From *Yerkey* to *Garcia*: 60 Years on and Still as Confused as Ever!',[287] where Hii states:

> Independent advice, and in appropriate cases, financial advice will serve as an adequate protection for creditors. In essence, the *Garcia* decision has once again reminded creditors not to assume facts from one's outward appearance, especially where the guarantor may appear to be well-educated and runs her own business. It must adopt a prudent course to ensure that the guarantor understands the essential respects of the transaction.[288]

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[286] Ibid, 445.

[287] (1999) 7 *Australian Property Law Journal* 47.

[288] Ibid, 63.

4.4 FUTURE DEVELOPMENTS FOLLOWING *GARCIA*

In regard to what future developments *Garcia* may lead to in other areas of the law, *Garcia* does not explain why imperfect understanding in a special relationship suffices to negate a guarantee**, but does not suffice to negate any other transaction**, for which imperfect understanding is present. It is possible that the courts may one day choose to widen the application to go beyond guarantee situations (although in non guarantee transactions, there would more likely be an absence of the volunteer concept, thus the parties would enter a transaction on the anticipation of receiving some benefit – perhaps the guarantee situation is unique enough that special treatments given to guarantees should not flow on to other types of transactions).

In the NSW Law Reform Commission and University of Sydney's Research Report 11 dated October 2003[289] ('Research Report'), the Research Report found that the fears following the *Garcia* decision, that the floodgates were going to be opened in regard to guarantors bringing legal actions, were unfounded. In 58% of the cases that were surveyed for the Research Report,

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[289] Jenny Lovric and Jenni Millbank, NSW Law Reform Commission and the University of Sydney, *Darling, Please Sign this Form: A Report on the Practice of Third Party Guarantees in New South Wales*, Research Report 11 (2003). At *vii* the Terms of Reference dated 2 March 1999 for the Report from the Attorney General state that '… the New South Wales Law Reform Commission is requested to inquire into and report on the legal framework for the protection of guarantors of small business and other loans and in particular, to consider:

1. whether the present legal framework adequately protects the interests of personal guarantors of small business and other loans;
2. whether there is a reasonable level of satisfaction in the community with the operation and application of the existing laws protecting guarantors of small business and other loans, in particular, whether those guarantors, financiers and principal borrowers are satisfied with the present legal framework;
3. whether there are more practical and effective strategies for the provision of personal guarantees of small business and other loans that would enhance the development of conscientious lending practices while not placing undue constraints on small business lending; and
4. any related matters.'

In carrying out the review, the Commission was to consider various matters, including 'The need to ensure that any legal framework governing this issue adequately and effectively protects the interests of personal guarantors; promotes commercial stability and certainty; and does not unduly restrain small business lending.'

the guarantors sought to rely on the *Garcia* principle.[290] Of these 58% of cases, only 27% of guarantors were successful in their *Garcia* argument. The authors of the Research Report also conducted a survey of lawyers, asking the question whether the *Garcia* principles had made any difference to their practice. Most responses indicated that it had not made much difference as it merely supplemented existing law.'[291]

In regard to whether the special equity reaffirmed for wives in *Garcia* extends to cover other types of relationships, the Research Report finds that 'It appears that other courts have been hesitant to apply the principle to relationships other than marriage.'[292]

The Research Report noted that even though de facto relationships appear to be closely analogous to formal marriages, there is uncertainty whether the *Garcia* principles extend to that type of relationship.[293] The report then concludes on this aspect by examining the English position in *Etridge,* where Lord Nichols of Birkenhead held that there is a rational cut-off point for the kinds of relationships which may be susceptible to undue influence in surety transactions, and that in the absence of banks evaluating in each case the extent to which a debtor may have influence over a guarantor, '… the only practical way forward is to regard banks as "put on inquiry" in every case where the relationship between the surety and the debtor is non-commercial.'[294]

Other issues that the Research Report raised as being inconclusive following *Garcia* were as follows.

[290] Ibid, [7.35].

[291] Ibid, [7.37].

[292] Ibid, [7.39].

[293] Ibid, [7.40].

[294] Ibid, [7.43].

The first issue was the difficulty courts have had in interpreting who is a volunteer in guarantee transactions, especially guarantees taken to support a family business. Lack of certainty in determining who is a volunteer[295] is particularly difficult in cases where a wife guarantees a loan to a family company in which she is also a director and shareholder. The Research Report comments that in some cases, courts have been prepared to look at the substance rather than the form of the wife's involvement in the company, whereas other decisions have imputed a director with the knowledge of the company.[296]

The second issue raised as being inconclusive was the difficulty of establishing whether a benefit applies to the guarantor.[297]

[295]·Ibid, [7.44].

[296] Ibid, [7.47].

[297] Ibid, [7.50].

5. TRADE PRACTICES ACT 1974 (CTH) AND UNCONSCIONABILITY

5.1 INTRODUCTION TO THE *TRADE PRACTICES ACT 1974* (CTH) AND UNCONSCIONABILITY

5.1.1 THE EARLY HISTORY OF THE UNCONSCIONABILITY PROVISIONS IN THE TRADE PRACTICES ACT 1974 (CTH)

The development of the unconscionable conduct provisions in the *Trade Practices Act 1974* (Cth) can be traced back to the Swanson Committee's review of the Act in 1976.[298] The Swanson Committee suggested that unconscionable conduct should be prohibited by the Act and considered what provisions should be introduced.[299] The report from the Swanson Committee did not result in any legislative changes being introduced for unconscionability. A Green Paper entitled *Trade Practices Act: Proposals for Change* and an accompanying draft bill issued by the Government in 1984, preceding the 1986 amendments to the *Trade Practices Act 1974* (Cth), proposed a prohibition on unconscionable conduct in relation to contracts, and was not limited to consumer-type transactions. Ultimately the provision, s 52A, enacted in 1986[300] was confined in scope to consumer-type transactions[301] and was the forerunner to the current s 51AB. Section 52A(1) stated:

> A corporation shall not, in trade or commerce, in connection with the supply or possible supply of goods or services to a person, engage in conduct that is, in all the circumstances, unconscionable.

The introduction of s 52A allowed the remedies provided by the *Trade Practices Act 1974* (Cth) to be available for unconscionable conduct, and enabled the involvement of the Australian Competition and Consumer Commission.

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[298] Trade Practices Review Committee, Report to the Minister for Business and Consumer Affairs, 20 August 1976 ('Swanson Report').

[299] Ibid, [9.59].

[300] *Trade Practices Revision Act 1986* (Cth).

[301] The coverage of this section was limited to consumer transactions by s 52A(5); ie to 'goods or services of a kind ordinarily acquired for personal, domestic or household use of consumption'.

The Swanson Committee did, however, open the way for the possibility of future reform to provide relief to business from unconscionable conduct transactions:

> However, we do see advantages in prohibiting, but as a civil matter only, unconscionable conduct or practices in trade or commerce. The Committee so recommends, principally to give the Act a greater ability to deal with the problem outlined in the first paragraph of this chapter - the general disparity of bargaining power between sellers and buyers.[302]

In 1990 the Beddall Committee recommended to the Parliament that the unconscionability provisions of the *Trade Practices Act 1974* (Cth) should be extended to include small businesses '… where a small business is disadvantaged in the same way as a consumer, in its dealings with other parties.'[303] Despite a subsequent report[304] recommending that the Act not be extended to cover small business, two subsequent reports supported amendments to provide for small business protection.[305]

In 1992, in recognition that unconscionable conduct should not be limited to consumer transactions, but should also cover commercial transactions, Parliament created a new Part IVA and introduced ss 51AA (replacing the previous s 52A). Section 51AA stated:

> (1) A corporation must not, in trade or commerce, engage in conduct that is unconscionable within the meaning of the unwritten law, from time to time, of the States and Territories.
> (2) This section does not apply to conduct that is prohibited by section 51AB.

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[302] Trade Practices Review Committee, Report to the Minister for Business and Consumer Affairs, 20 August 1976 ('Swanson Report'), [9.59].

[303] The House of Representatives Standing Committee on Industry, Science and Technology, *Small Business in Australia: Challenges, problems and Opportunities* report of January 1990 ('Beddall Committee Report'), [4.16], recommendation No. 20.

[304] Senate Standing Committee on Legal and Constitutional Affairs, *Mergers, Monopolies and Acquisitions: Adequacy of Existing Legislative Controls*, December 1991 ('Cooney Report').

[305] Report of the Trade Practices Commission to the Attorney General and Minister for Small Business and Customs, *Unconscionable Conduct and the Trade Practices Act: Possible Extension to Cover Commercial Transactions*, July 1991; The Report of the Franchising Taskforce to the Minister for Small Business and Customs (December 1991).

The *Trade Practices Amendment (Fair Trading) Act 1998* (Cth) was finally introduced in order to provide protection to small businesses. Section 51AC was created accordingly and came into force on 1 July 1998. The former s 52A was criticised on the basis that the use of the word 'unconscionable' sets too strict a standard.[306] Section 51AAB provided that ss 51AA and 51AB (mirroring the old s 52A), do not apply to conduct engaged in relation to financial services. Importantly, however, s 51AC was not excluded from applying to financial services.

The term 'financial services' is defined in s 4 of the *Trade Practices Act 1974* (Cth), in the form of the definition of the same expression in the *Australian Securities and Investments Commission Act 2001* (Cth). Part 2 of that Act mirrors the *Financial Services Reform Act 2001* (Cth) definition, in that 'financial services' only apply as per s 12BAB of the *Australian Securities and Investments Commission Act 2001* (Cth). A person provides a financial service if they:

- provide financial product advice;
- deal in a financial product;
- make a market for a financial product;
- operate a registered scheme;
- provide a custodial or depository service;
- operate a financial market (eg a stock exchange or futures exchange) or clearing and settlement facility;
- provide a service that is otherwise supplied in relation to a financial product; or
- engage in conduct of a kind prescribed in regulations made for the purposes of this paragraph.

[306] CCH, *Trade Practices Commentary*, (at 8 October 2006), Unfair Conduct Part IVA: Unconscionable Conduct, Section 51AB ¶20-806. The authors state that how the unconscionability standard would be enforced will depend on judicial interpretation, but the legislative direction given by use of a word like 'unfair' would certainly have led to a wider interpretation of the original s 52A.

'Financial product' is defined in s 12BAA as a facility through which a person makes a financial investment, manages financial risk or makes non-cash payments – thus it includes bank deposit accounts, investment securities, futures contracts, insurance contracts, retirement savings accounts (RSAs), life policies and superannuation. Post 11 March 2002 (changes introduced in the *Financial Services Reform Act 2001* (Cth)), the *Australian Securities and Investments Commission Act 2001* (Cth) definition was expanded to also specifically include:

- derivatives;
- foreign exchange contracts;
- interests in managed investment schemes; and
- a credit facility.[307]

Prior to the 11 March 2002 changes, it was determined that *security* did not include a mortgage over real estate, as *security* just referred to share security, as per the decision of O'Keefe J in *Manso v David*.[308] So up until 11 March 2002, the *Trade Practices Act 1974* (Cth) ss 51AA and 51AB could also be used for unconscionability actions in regard to loans, mortgages and guarantees given for loans by financial institutions, in addition to s 51AC, as they fell outside the definition of being covered as financial products.[309]

After 11 March 2002, in regard to the *Trade Practices Act 1974* (Cth) relief for unconscionable conduct, the only section that a financial services debtor or security provider could seek relief under was s 51AC.[310] Note though that

[307] Which, as per Regulation 2B and 2BA of the *Australian Securities and Investments Commission Regulations 2001* (Cth), includes loans, commercial bill facilities, margin lending facilities and mortgages and guarantees given to secure a credit contract.

[308] [2003] NSWSC 905 (unreported, 3 October 2003, BC200305872).

[309] *Spira v Commonwealth Bank of Australia* (2003) 57 NSWLR 544. Handley JA commented at [39] in regard to an unconscionability claim made under s 51AA of the *Trade Practices Act 1974* (Cth) (prior to the 11 March 2002 changes to the definition of financial products to include bank loans and mortgages and guarantees given to secure loans), of a bank refusing to allow a customer to fully draw down a $3 million loan facility, that: 'This section is relevant because it seems that the financial accommodation provided to the Borrower did not involve the provision of financial services within the meaning of s 51AAB. The contrary was not suggested.'

[310] Initially a $3 million limit applied. Following the enactment of the *Trade Practices Legislation Amendment Act (No.1) 2007* (Cth) on 25 September 2007, the limit increased from $3

relief under the unconscionability provisions of ss 51AA and 51AB of the Act was available to financial services debtors and security providers in the mirrored provisions of those sections in the *Australian Securities and Investments Commission Act 2001* (Cth).

5.1.2 SECTION 51AA

Section 51AA provides that:

> A corporation must not, in trade or commerce, engage in conduct that is unconscionable within the meaning of the unwritten law, from time to time, of the States and Territories.

The section was introduced by the *Trade Practices Legislation Amendment Act 1992* (Cth) and was described in the second reading speech as extending and modifying the prohibition in the former s 52A to commercial transactions. The speech also noted 'All transactions covered by the new provision are already covered by the equitable doctrine.'[311] The benefit of having legislative relief for what is already in existence in equity, is that the plaintiff can obtain remedies available under the *Trade Practices Act 1974* (Cth) (plus the potential involvement of the Australian Competition and Consumer Commission). The section only applies to unconscionable conduct by corporations in which the constitutional requirements of fulfilling 'in trade and commerce' as defined in ss 5 and 6 are being met. Section 51AA(2) provides that s 51AA does not apply to conduct that is prohibited by ss 51AB or 51AC.

Some important wording to be noted in s 51AA is the use of the words 'conduct that is unconscionable within the meaning of the unwritten law'. The courts have generally chosen to utilise the narrow definition of what is the 'unwritten law' for unconscionability,[312] falling back on the *Amadio*

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million to $10 million. The *Trade Practices Legislation Amendment Act 2008* (Cth) then removed the limit altogether on 21 November 2008.

[311] Mr Duffy (Member for Holt – Attorney General) *Trade Practices Amendment Bill 1992* (Cth), Second Reading Speech, in the House of Representatives, 3rd November 1992.

[312] *GPG (Australia Trading) Pty Ltd v GIO Australia Holdings Ltd* (2001) 117 FCR 23.

special disability approach (ie one party has a special disability that affected their ability to understand the impact of the transaction, and the other party is aware of the special disability and takes advantage of it to the detriment of the weaker party). This is as opposed to applying the broader equitable principle of unconscionability, which, as was discussed in the introduction section, Professor Finn saw as the second usage of the term 'unconscionability'. These are specific equitable doctrines such as estoppel, unilateral mistake, relief against forfeiture and actual undue influence/pressure, united by the idea that equity will prevent an unconscionable insistence on strict legal rights.

Cases examining the narrow application of s 51AA

In *GPG (Australia Trading) Pty Ltd v GIO Australia Holdings Ltd*[313] (*GPG*), Gyles J of the Federal Court applied the narrow definition of 'conduct that is unconscionable within the meaning of the unwritten law' when the court looked at announcements made by GIO and AMP in regard to information GIO disclosed for offers made by AMP to purchase GIO shares. A breach by GIO of s 12CA of the *Australian Securities and Investments Commission Act 2001* (Cth) (which mirrored s 51AA of the *Trade Practices Act 1974* (Cth)) was alleged by a shareholder of GIO who had suffered a loss as a result of relying upon the announcement. Gyles J stated his reasons for applying the narrow definition as follows:

> In my opinion, it is that equitable doctrine [the narrow *Amadio* definition] which is picked up by the reference to the unwritten law in s 12CA of the *ASIC Act*, rather than other situations in which unconscientious conduct is relevant to the grant of equitable relief, such as equitable estoppel ... It is not pleaded or suggested that this doctrine has application here. As counsel for AMP reminded me on more than one occasion, this is not a case between GIO and AMP either in contract or based upon equitable estoppel ...
>
> The argument to the contrary of my conclusion must involve the proposition that there is an overarching or general doctrine of unconscionability recognised by equity which encompasses all circumstances in which behaviour which can be described as unconscionable plays a part in the entitlement to relief. No authority

[313] (2001) 117 FCR 23.

[314] Ibid, 76–77 [123]–[125].

> has been cited to support that proposition, apart from the obiter dicta of French J in *Berbatis*. In my respectful opinion, it is contrary to established authority.[314]

Philip Tucker in his article 'Unconscionability: The Hegemony of the Narrow Doctrine under the *Trade Practices Act*'[315] noted that there was a case that Gyles J had not referred to,[316] where the wider definition of unconscionability was applied. Tucker was referring to *Asia Pacific International Pty Ltd v Dalrymple*[317] (*Dalrymple*). In *Dalyrmple*, Shepherdson J of the Queensland Supreme Court was asked to determine if a compound rate of interest of 20% per month for a short-term commercial loan of $15,000 had caused the loan contract to become unconscionable in terms of s 51AA. Shepherdson J reviewed various Australian and New Zealand decisions on unconscionability[318] before he concluded (and ordered that the interest rate be amended) that:

> I should say now that in my view those views of the law have to some extent been overtaken by the equitable doctrine of granting remedies for unconscionable conduct, the boundaries of which have never been and cannot be stated.[319]

In the Full Federal Court case of *Australian Competition & Consumer Commission v Samton Holdings Pty Ltd*,[320] the charging of a significant premium by a landlord to renew a lease when the tenant had not exercised a renewal option clause prior to its expiry, was claimed by the tenant to be unconscionable in terms of s 51AA. Gray, French and Stone JJ, in their joint judgment, found that unconscionability in terms of the unwritten law can not

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[315] (2003) 11 *Trade Practices Law Journal* 78.

[316] Gyles J dismissed in *GPG* two interlocutory cases where a wider definition was explored, as not providing any authoritative guidance. Gyles J referred to these two cases at 75 [119]: '*Pritchard v Racecage Pty Ltd* (1997) 142 ALR 527, where a strike-out application was unsuccessful, but in which Branson J, who gave the leading judgment, appeared to indicate a preference for the narrower view of the section (see her Honour's judgment at 545). The second case was *Olex Focas Pty Ltd v Skodaexport Co Ltd* [1998] 3 VR 380 where Batt J granted an interlocutory injunction (at 402–404).'

[317] [2000] 2 Qd R 229.

[318] Including *Amadio*, Deane J in *Commonwealth v Verwayen* (1990) 170 CLR 394 and Sir John Salmond in *Brusewitz v Brown* [1923] NZLR 1106 at 1110.

[319] [2000] 2 Qd R 229, 238 [52].

[320] (2002) 117 FCR 301.

be confined to a narrow doctrine and is capable of variable meanings depending on the circumstances of the case, provided they fall within an identifiable equitable doctrine. They stated:

> It [unconscionable conduct] is a term which has various shades of meaning according to its context. There are different thresholds of conduct in various categories, all of which may be described as unconscionable ...[321]

A wider reading of the term unconscionability within the unwritten laws for s 51AA was later explored by French J in the first instance in the Federal Court in *Australian Competition & Consumer Commission v CG Berbatis Holdings Pty Ltd*.[322] French J's decision plus its rejection by the Full Federal Court[323] and then the High Court[324] are discussed in detail in a later chapter.

So where is s 51AA heading? Philip Tucker in his 2003 article[325] suggested that s 51AA as well as s 51AC should focus on vulnerability (including situational disability) rather than special disability, within the narrow doctrine of unconscionability.[326] Tucker saw that if vulnerability was to become the key determining element in s 51AA, then the courts could look to the factors listed in s 51AC as markers to determine if circumstances indicate an '… inequitable exploitation of "situational disability" arising from the totality of the circumstances.'[327] Otherwise s 51AA does not expand the doctrine of unconscionability beyond what is already provided for in equity, and provides only the advantage that the *Trade Practices Act 1974* (Cth)

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[321] Ibid, 317–319 [46]–[50], with reference made to G Dal Pont, 'The Varying Shades of "Unconscionable" Conduct – Same Term, Different Meaning' (2000) 19 *Australian Bar Review* 135 at 165. See also Phillip Tucker, 'Unconscionability: The Hegemony of the Narrow Doctrine under the *Trade Practices Act*' (2003) 11 *Trade Practices Law Journal* 78, 85–86.

[322] (2000) ATPR 41-778.

[323] *Australian Competition & Consumer Commission v CG Berbatis Holdings Pty Ltd* (2000) 96 FCR 491.

[324] *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd* (2003) 214 CLR 51.

[325] 'Unconscionability: The Hegemony of the Narrow Doctrine under the *Trade Practices Act*' (2003) 11 *Trade Practices Law Journal* 78. The article was written post the High Court decision in *Berbatis*.

[326] Ibid, 90.

[327] Ibid.

remedies may be used (and it allows the Australian Competition and Consumer Commission to become a party to an unconscionability action).

5.1.3 SECTION 51AB

Section 51AB was introduced in 1986 and is aimed at unconscionable conduct engaged in by corporations in trade or commerce in relation to consumers. It only provides relief for transactions involving consumer goods eg '… ordinarily acquired for personal, domestic or household use or consumption', provided that they have not been obtained for the purpose of resupply or '… using them up or transforming them in trade or commerce' (ss 51AB(5) and 51AB(6)).

Uncertainty is raised as to whether the definition of consumer goods used in s 4B is relevant to s 51AB. Section 4B(1)(a)(i) defines consumer goods as being of no more than $40,000 in value (regardless of whether they are for commercial or consumer use, provided they are not for resale or resupply), whereas the references in s 51AB make no mention of dollar limitations.

Section 4B(1)(a)(ii), however, adds an exception that goods will still be considered to be for consumer use, even when they are above $40,000 in value, where the goods '… were of a kind ordinarily acquired for personal, domestic or household use or consumption or the goods consisted of a commercial road vehicle' (again provided the goods are not for resale or resupply). Therefore under s 4B(1)(a)(ii) it could be argued that a purchase of a painting or other artwork valued at over $40,000 by a business for its use could be classified under s 4B(1)(a)(ii) as consumer goods, given that they are the type of product which are ordinarily acquired for personal usage. Given the absence of any dollar limit in s 51AB, it is taken that the $40,000 restriction does not apply to s 51AB, provided that the goods are of a kind

normally bought for personal, domestic or household consumption or use (and are not used for resale or resupply).[328]

In order to counter the reluctance of courts to enforce broad prohibitions, s 51AB specifically provides that the court will have regard to the following matters, in order to determine if conduct is unconscionable:

- the relative bargaining strengths of the parties;
- whether contractual conditions were not reasonably necessary for the protection of the supplier;
- whether the consumer understood the documents;
- whether any undue influence was exerted, or any unfair tactics used; or
- the amount for which and circumstances under which a consumer could have obtained the goods or service elsewhere.

The above list is not an exhaustive list, however, of what the court may consider in determining whether or not unconscionable conduct has occurred. The introduction to s 51AB(2) is as follows:

> Without in any way limiting the matters to which the Court may have regard for the purpose of determining whether a corporation has contravened subsection …

For factors falling outside the list provided in this section, s 51AB does not have the limitations that s 51AA imposes in regard to the need for the courts to consider what constitutes unconscionable conduct within the 'unwritten law'. This was expressed by Gyles J in the Federal Court decision of *GPG*:

> An aspect of the legislation relevant to the construction of s12CA of the *ASIC Act* is the presence of s 12CB which I need not reproduce. Unconscionability is not limited by reference to the unwritten law in that section. If unconscionability in s 12CB is not limited to the meaning of the term within the unwritten law, but is at large, some support is provided to the argument that unconscionable conduct in s 12CA of the *ASIC Act* is a limited concept, with an extension

[328] 'Looking at sec 51AB(2), one can see that the insertion of the word "consumer" in its general, and not sec 4B sense, serves to emphasise that the section is one aimed at the disparity in bargaining power between sellers and buyers.' CCH, *Trade Practices Commentary*, (at 15 October 2006), Unfair Conduct Part IVA: Unconscionable Conduct, Section 51AB, Limitation to consumer-type transactions ¶20-802.

> effected by s 12CB, albeit in a narrower range of consumer transactions than encompassed by s 12CA. There is a debate in the authorities as to the similar question which arises as to the proper construction of s 51AB and s 51AC of the *TPA*. The preponderance of opinion seems to be that unconscionable conduct in these sections is not restricted to the meaning within the unwritten law (see *Australian Competition & Consumer Commission v Simply No-Knead (Franchising) Pty Ltd* (2000) 104 FCR 253 at para [30] to para [37]). The history of the *TPA* provisions, recently traced by Lindgren J in *Monroe Topple & Associates Pty Ltd v Institute of Chartered Accountants in Australia* [2001] FCA 1056 (at para [256] to para [262]), supports that conclusion.[329]

5.1.4 SECTION 51AC

The *Trade Practices Act 1974* (Cth) was viewed as not providing small business with protection against unconscionable conduct.[330] This was because there was no recognised class of special disability for small business applicants so as to be able to successfully run an *Amadio* type unconscionability claim under s 51AA.[331] This led to the 1 July 1998 introduction of s 51AC.

Section 51AC deals with the protection of small business. Publicly listed companies are excluded from the definition, plus initially a maximum value of goods or services level as per s 51AC(10) applied (this section was subsequently repealed). In addition to the aspects the court considered in s 51AB being repeated in s 51AC (but in regard to a small business as opposed to a consumer), s 51AC(3) provides the court may also consider the following procedural and substantive factors:

- the extent to which the supplier's conduct towards the business consumer was consistent with the supplier's conduct in similar transactions;
- the requirements of any applicable industry codes;[332]

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[329] (2001) 117 FCR 23, 75–76 [120].

[330] Ayman Guirguis and Daniel Preston, 'Unconscionability under the *Trade Practices Act*. Does it Undermine Commercial Certainty?' (2001) 75(2) *Law Institute Journal* 52.

[331] Tony Ciro and Vivien Goldwasser, *Law and Business Text and Tutorials* Oxford University Press (2004).

[332] The Regulations under s 51AE have only prescribed three codes – The Franchising Code, the Horticulture Code and the Oil Code, each of which are mandatory codes. Given the banking industry has created its own industry standard in the Code of Banking Practice, this Code may

- the requirements of any other industry code, if the business consumer acted on the reasonable belief the supplier would comply with that code (eg for a bank, an assumption by a business consumer that the bank would act in terms of the Electronic Funds Transfer Code of Conduct published by ASIC, even though the bank in question may not have adopted that code);
- the extent to which the supplier failed to disclose any intended conduct that might affect the business consumer's interests, or any risks not disclosed;
- the extent to which the supplier was willing to negotiate the terms and conditions; and
- the extent to which the supplier and business consumer acted in good faith.

Like s 51AB, this range of matters that may be considered allows the term 'unconscionable' to be interpreted more broadly than just relying on the interpretations provided by the existing common law cases on unconscionable conduct as is the approach for s 51AA.[333]

Section 51AC(10) was repealed and thus there is no longer any limit to the maximum value of goods or services to which this section applies (up until 21 November 2008 a limit of $10 million applied).[334] Section 51AC does not have the restriction on the types of goods or services that s 51AB imposes ie there is no equivalent s 51AB(5) restriction that goods or services have to be of the type acquired for personal, domestic or household use or consumption.

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have the potential to be relevant to claims brought under s 51AC of the *Trade Practices Act 1974* (Cth) or its equivalent, s 12CC of the *Australian Securities and Investments Commission Act 2001* (Cth). See comments by Elizabeth Sexton, General Counsel to the Banking and Financial Services Ombudsman (now known as the Financial Ombudsman Service), 'The New Code of Banking Practice and Guarantees: What Lawyers Need to Know' (Speech presented to the Law Council of Australia and Law Institute of Victoria, 16 October 2002).

[333] As per the comments in regard to the mirrored provision of s 12CC of the *Australian Securities and Investments Commission Act 2001* (Cth) made by Tamberlin, Finn and Conti JJ in the Full Federal Court of Australia decision in *Australian Securities and Investments Commission v National Exchange Pty Ltd* (2005) 148 FCR 132, 140 [30].

[334] Section 51AC(10) and the $10 million limit were removed on 21 November 2008 by the *Trade Practices Legislation Amendment Act 2008* (Cth).

An observation of the differences that constitute unconscionability under s 51AB, as compared with under s 51AC, was made by Sundberg J of the Federal Court in *Australian Competition and Consumer Commission v Simply No-Knead (Franchising) Pty Ltd.*[335] There Sundberg J stated:

> The s 51AB(2) factors do not so clearly suggest, as do the s 51AC(3) factors, that unconscionability in s 51AB is a more ample concept than the unwritten law's unconscionability. Nevertheless, as with s 51AC(3), s 51AB(2) does not limit the factors the Court may consider. It would be curious if "unconscionable" in the two provisions had different meanings - in s 51AB the same as in s 51AA and in s 51AC a wider meaning. The Full Court in *Hurley v McDonald's Australia Ltd* [2000] ATPR 41-741 seems to have assumed the word had the same meaning in both sections: at 40,585.[336]

This observation of Sundberg J, that he did not believe the courts will interpret the elements of what would constitute unconscionability under ss 51AB and 51AC differently, is puzzling given the additional matters that a court may consider under ss 51AC(3) and 51AC(4) that are not listed in s 51AB. These additional matters include:

- willingness of parties to negotiate terms (ss 51AC(3)(j) and 51AC(4)(j));
- extent to which the stronger parties conduct was consistent with its conduct in similar transactions (ss 51AC(3)(f) and 51AC(4)(f));
- compliance with industry codes (ss 51AC(3)(g) and 51AC(4)(g));
- acting in good faith (ss 51AC(3)(k) and 51AC(4)(k)); and
- extent to which the stronger party failed to disclose intended conduct (or risks that should have been foreseen) that might affect the interests of the small business (ss 51AC(3)(i) and 51 AC(4)(i)).

In addition, the previously mentioned *Trade Practices Legislation Amendment Act (No.1) 2007* (Cth), assented to on 24 September 2007, also widened the factors a court may consider in identifying unconscionable conduct under ss 51AC(3) and 51AC(4) to include whether the supplier has a contractual right to vary unilaterally a term or condition of the contract with

[335] (2000) 104 FCR 253.

[336] Ibid, 265–266 [35].

the supplier.[337] This may potentially be an issue for financiers, given that most terms and conditions for commercial loans include unilateral variation clauses in regard to the pricing (interest rates and fees) that may be charged.[338] Such clauses are often linked, with these pricing variations being allowed as a result of a review being conducted on the finance facility, due to certain changes. One change that may trigger a pricing increase is an increase in risk due to a decline in the financial position of the debtor or a decline in the security value. The increase in pricing being justified by the lender as being necessary to provide the financier with an adequate return for an increased risk. Structural changes in regard to how the financier raises the funding for the facility may also trigger pricing increases.[339]

One wonders whether there would be any significant impact on pricing by financiers as a result of the amendments, as the majority of pricing for small business loans invariably refer to an interest rate as being a specific reference rate plus a margin. Variations to the actual interest rate applying to the loan occur throughout the term of the loan, as the reference rate varies due to market movements. It would appear unlikely that courts would consider these types of unilateral variations as being conduct identifying unconscionable conduct.

The comments made by the former Chairman of the Trade Practices Commission, Professor Bob Baxt, are interesting in that he sees that the additional provision provides little new benefit to small business, because the

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[337] Sections 51AC(3)(ja) and 51AC(4)(ja).

[338] The Explanatory Memorandum discusses mainly the impact of this proposed change on interest rate clauses (at [2.165]–2.166]). The ability for a financier to vary its interest rate has traditionally been documented via a unilateral term in the finance contract. It notes that it could impose a higher cost on small business via increased interest rate costs due to financiers having to pass on (by way of a higher interest rate) the risk that interest rates would increase during the course of a loan. It also notes that any falls in interest rates would not be passed on to the borrower.

[339] Such as Government-imposed new fees and taxes, as with the GST last decade, or a change in APRA's *APS 111 Capital Adequacy: Measurement of Capital* weighting applied to loan types or security types that results in higher capital holdings. The increased cost in such higher capital holdings is passed on to the debtor (such as extra conditions added to low doc and no doc housing loans in order to qualify for the 50% capital concession that applies to standard housing loans under *APS 111*).

courts already have a wide discretion in regard to matters they may consider under s 51AC. The inclusion of this additional wording is only one of many factors that may be considered and the subsection notes that these factors may be considered without in anyway limiting the areas the court may wish to consider.

Professor Baxt laments that the Australian Competition and Consumer Commission's record with s 51AC is poor to date, with only 20 cases having been brought by the Commission since the legislation was introduced in July 1998 (and of these, only one case has been run by the Commission in the last five years to July 2007).[340] Clearly to date s 51AC has not effectively extended the liability of parties who engage in unconscionable conduct against small business.

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[340] Professor Bob Baxt, 'Trade practices proposals still fail to protect needy', *Australian Financial Review* (Sydney), 6 July 2007, 66. Professor Baxt also discussed, as one of the reasons for the Australian Competition and Consumer Commission's lack of success in prosecuting cases, a restriction by government policy from paying senior counsel more than a benchmark rate in fees, whereas the private sector was under no such limitation in being able to attract the best senior counsel.

5.2 THE *TRADE PRACTICES ACT 1974* (CTH) AND THE LEVEL OF KNOWLEDGE REQUIRED BY A FINANCIER IN ORDER FOR A TRANSACTION TO BE SET ASIDE

The financier's knowledge of the special disadvantage of the debtor or security provider is a necessary element in order for those parties to establish an unconscionability action. The degree to which that knowledge is held for an unconscionability action, according to Kirby J in *Garcia*, can not include constructive knowledge of the disadvantage.[341] This brings into question the types of knowledge that are adequate in order to satisfy the application of the unconscionability doctrine. Rick Bigwood[342] refers to the 'knowledge of awareness' scale formulated by Gibson J in the English Chancery Division decision in *Baden v Société Générale pour Favoriser le Développement du Commerce et de l'Industrie en France SA*[343] (*Baden*) to examine all possible levels of awareness. These are:

> (i) actual knowledge;
> (ii) wilfully shutting one's eyes to the obvious;
> (iii) wilfully and recklessly failing to make such inquiries as an honest and reasonable man would make;
> (iv) knowledge of circumstances which would indicate the facts to an honest and reasonable man;
> (v) knowledge of circumstances which would put an honest and reasonable man on inquiry.
>
> More accurately, apart from actual knowledge they are formulations of the circumstances which may lead the court to impute knowledge of the facts to the alleged constructive trustee even though he lacked actual knowledge of those facts. Thus the court will treat a person as having constructive knowledge of the facts if he wilfully shuts his eyes to the relevant facts which would be obvious if he opened his eyes, such constructive knowledge being usually termed (though by a metaphor of historical inaccuracy) "Nelsonian knowledge". Similarly the court may treat a person as having constructive knowledge of the facts (type (iv) knowledge) if he has actual knowledge of circumstances which would indicate the facts to an honest and reasonable man.[344]

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[341] *Garcia v National Australia Bank Ltd* (1998) 194 CLR 395, 430[72], where Kirby J stated 'Constructive notice should not be sufficient for unconscientious dealing'.

[342] Rick Bigwood, *Exploitative Contracts* Oxford University Press (2003), 252.

[343] [1992] 4 All ER 161. The case dealt with knowing assistance in a breach of fiduciary duty, rather than unconscionable dealing.

[344] Ibid, 236.

These first three categories have been taken to constitute actual knowledge, whilst the last two categories have been taken to constitute constructive knowledge.[345] Bigwood commented in his examination of these five levels of knowledge, that Mason J in *Amadio* envisaged the first four levels as being adequate for the unconscionability doctrine to be established.[346]

Bigwood also observed that there are some recent cases where the fifth level of knowledge (knowledge of circumstances which would put an honest and reasonable man on inquiry) has been accepted as adequate for the purposes of establishing unconscionability.[347]He disagreed with this approach and nor did he agree that constructive notice should establish unconscionability, because the use of the knowledge by the stronger party should be exploitative (and it can not be exploitative if the stronger party is not consciously utilising the knowledge, even though he or she has 'carelessly failed to know and appreciate facts').[348]

Bigwood saw a difference between the stronger party acting obtusely, and unconscionably, with there needing to be intention / deliberateness on the part of the stronger party which should be assessed in the light of what they knew, as distinct from what a reasonable person should have known or appreciated.[349]

Bigwood summarised his conclusions by stating that:

> Carelessness cannot suffice in equity to signify victimization – or an exploitative state of mind – for the purpose of supporting an unconscionability judgment. Constructive notice in its strictest sense can not suffice because its effect is to impute knowledge by a fiction: it deems D [the defendant stronger party] to know facts that it conceded he did not know at the relevant time.[350]

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[345] Rick Bigwood, *Exploitative Contracts* Oxford University Press (2003), 252–253.

[346] *Commercial Bank of Australia Ltd v Amadio* (1983) 151 CLR 447, 467 per Mason J.

[347] Supreme Court of South Australia Full Court decision in *Micarone v Perpetual Trustees Australia Ltd* (1999) 75 SASR 1.

[348] Rick Bigwood, *Exploitative Contracts* Oxford University Press (2003), 255.

[349] Ibid.

[350] Ibid.

So having rejected traditional constructive knowledge as being able to be used to establish unconscionable conduct, Rick Bigwood concluded that, in practice, the knowledge necessary to establish a successful unconscionable conduct claim was any of the following:

1. By virtue of the weaker party's observable appearance, speech, behaviour, or circumstances.
2. Through the stronger party having had prior dealings with the weaker party.
3. Through the stronger party possessing a special expertise, while the weaker party is inexperienced in transactions of the type under negotiation.
4. From the glaring disproportion of benefits and burdens distributed under the transaction materially to the disadvantage of the weaker party (though preferably in combination with other observable phenomena).[351]

[351] Rick Bigwood, *Exploitative Contracts* Oxford University Press (2003), 260. Bigwood cites the following: *Blomley v Ryan* (1956) 99 CLR 362 with the obvious inebriation of the 78-year-old farmer Mr Ryan in that case is referred to for point one; *Louth v Diprose* (1992) 175 CLR 621 and other cases are referred re relationships of intimacy, and relationships of dependency – and of which, from prior dealings, the other party was aware – for point two; cases involving companies that were professional lenders dealing with inexperienced borrowers such as in *Amadio*, was referred to for point three; *Nichols v Jessup* [1986] 1 NZLR 226, 231 per Cooke P was referred to, where there was a 'glaring' or 'overwhelming' imbalance such that the defendant 'must have known or suspected that she was no judge of her own interests', for point four.

5.3 *TRADE PRACTICES ACT 1974* (CTH) AND THE LEVEL TO WHICH A FINANCIER IS PUT ON NOTICE OF THE INCAPACITY OF A BORROWER – *ACCC V RADIO RENTALS LTD*

In the Federal Court case of *Australian Competition and Consumer Commission v Radio Rentals Limited*[352] there was an innovative attempt by the Australian Competition and Consumer Commission to expand the circumstances under which unconscionability could be found to have occurred. Justice Finn, the author of the previously referred to 1994 article on unconscionable conduct,[353] heard the case. The Australian Competition and Consumer Commission no doubt expected that the facts of the case presented the appropriate vehicle in which a favourable decision could be laid down expanding the obligation of financiers and other businesses in regard to vulnerable customers re unconscionability under ss 51AA and 51AB of the *Trade Practices Act 1974* (Cth).

The case involved a South Australian man (Mr Groth - aged in his sixties) with a range of intellectual disabilities, ranging from a low IQ (various evidence was submitted putting his IQ in a range from 50 to 80), to being diagnosed as mentally retarded and suffering from schizophrenia. Evidence however was submitted that any indication of Mr Groth's intellectual challenges was not readily determinable from entering into short- or even medium-length discussions with him. Mr Groth entered into 15 rental agreements for household electronic goods, two loan agreements and 17 service agreements from November 1996 to October 2002 with Radio Rentals / Walker Stores (Walker Stores provided leased electrical equipment, with its agent in South Australia being Radio Rentals). Payments made by Mr Groth totalled $20,700.43. He had enjoyed a good credit history, even to the extent that there was a record of overpayments having been made by him on

[352] (2005) 146 FCR 292.

[353] Paul Finn, 'Unconscionable Conduct' (1994) 37 *Journal of Contract Law* 8. The article was written when his Honour was a Professor of Law at ANU.

a number of occasions. In any case, due to Mr Groth's income being limited to a disability pension, as he continued to increase his commitments, the inevitable happened and he was placed in a position where he could no longer maintain the payments on his electrical goods, especially when coupled with payments needed to other creditors.

The Australian Competition and Consumer Commission argued that there were breaches of both ss 51AA and 51AB by Radio Rentals / Walker Stores. The Commission contended that Radio Rentals, in its dealings with Mr Groth, knew, or had reason to know of, Mr Groth's disability, including that he could not read the agreements nor understand the terms and conditions, and that it was unlikely to be in his best interests to enter into the agreements.

The Australian Competition and Consumer Commission examined the accumulated knowledge of Radio Rentals from the whole range of Radio Rental employees that dealt with Mr Groth. The first source of accumulated knowledge deemed to Radio Rentals was from the technicians on the phone support desks for after-sales service, who took 329 phone calls during a period stretching from February 1998 to November 2001. The second source of accumulated knowledge was from the various salespersons that dealt with him over a large range of individual electronic good sales. The final source of accumulated knowledge was from the accounts staff that were aware of his overpayments.

The Australian Competition and Consumer Commission alleged that if this accumulated knowledge had been analysed by Radio Rentals, it would have put Radio Rentals on notice both of Mr Groth's intellectual disability and his financial hardship. Finn J rejected the contention that the circumstances of the case justified Radio Rentals being attributed with this combined knowledge of its employees. Finn J saw that 'the state of mind to be attributed to Radio Rentals can be no different from, and no less innocent

than that of, the personnel who made the entries in its records.'[354] He therefore found that 'no justification for the aggregation (eg participation by several employees in the same transaction) has been made out.'[355] Finn J saw that the situation might be different if it were only the one transaction (as opposed to Mr Groth's position where there had been numerous purchases financed over a long period of time), and the information was able to be accumulated by a team working on that single transaction.

Finn J also saw that 'too much cannot be expected of ordinary people doing routine jobs by way of critical appraisal of their employers' customers and their affairs.'[356] It could not be expected for a salesman dealing with hundreds of customers a week with relatively short time spans spent with each customer, to be able to detect that any one customer may have had intellectual challenges which were not readily apparent.

Finn J saw that the case highlighted the:

> … peculiar vulnerability of persons like Mr Groth who are unable in fact to conserve their own interests but who do not, as of course, put people with whom they deal on notice of their incapacities. They are, in consequence, attributed innocently with powers they do not possess. This can rebound to their distinct disadvantage, as the circumstances of this matter demonstrate.[357]

Radio Rentals did not knowingly take advantage of Mr Groth, so the ss 51AA and 51AB actions failed.

It is interesting that although Finn J rejected the argument for accumulated knowledge of a variety of employees over a period of time on different transactions equalling knowledge of a consumer's special disabilities, in what could be construed to be a warning being delivered to Radio Rentals, Finn J advised that companies should be expected to have in place appropriate risk

[354] (2005) 146 FCR 292, 326 [179].

[355] Ibid, 327 [183].

[356] Ibid, 330 [198].

[357] Ibid, 330 [197].

management practices to avoid breaching the *Trade Practices Act 1974* (Cth). These risk management practices would put financiers on notice in regard to dealing with persons at disadvantages like Mr Groth, and the risks involved (for both parties) in providing finance and possibly breaching the *Trade Practices Act 1974* (Cth) unconscionability provisions (with Finn J having noted that such risk management practices are now facilitated by modern technology).[358]

Although Finn J offered no suggestion as to the kind of risk management practices that would be adequate to detect circumstances of consumers having special disabilities, one envisages that such practices should include the following.

An assessment system for an application for finance that assigns high risk to applicants indicating reliance on welfare pension payments from the Government as the predominant source of income (which banks usually treat as a factor warranting automatic decline of the loan request) should be established.

The risk management practices should also include the use of a finance assessment system that takes into account the level of surplus disposable income available after meeting all existing commitments plus any proposed new commitment requested by the transaction at hand (which is standard for any bank consumer finance request, with minimum acceptable disposable incomes based on an indices such as the Henderson Poverty Index or the [higher] Household Expenditure Survey data,[359] which is used to determine what is a minimum acceptable disposable income on which to live, usually after deduction for an allowance for the number of dependants plus a tolerance to allow for movements in interest rates if the loan is at a variable interest rate).

[358] Ibid, 330 [198].

[359] Dr John F Laker, Chairman APRA, 'The Regulator's Approach to Compliance: Crackdown, Confrontation or Compliance Culture' (Speech delivered to The Institute of Chartered Accountants in Australia, Melbourne, 20 June 2007), 4.

The final risk management practice that should be included is an assessment of the repayment history on any existing prior loan / rental contracts with the financier. This repayment history should be a factor in the finance assessment system (although a history of over-repayment of loans, argued by the Australian Competition and Consumer Commission as an aspect putting the financier on notice of Mr Groth's intellectual ability, would not normally be a factor to be considered in an automated credit scoring system as adding any negative value to the overall credit score achieved by an applicant – as it normally would for under-payment of regular commitments leading to an arrears or default history).

Finn J noted specifically, after discussion of the above risk management point, that 'I would emphasise in passing that the present case as pleaded was not about the respondents' risk management practices as such.'[360] The Australian Competition and Consumer Commission did not make any argument in the pleadings as to whether or not Radio Rentals may have breached their own credit policies and procedures in the assessment and approval process for Mr Groth's facilities (and it is unknown whether there was any breach, or not). If in the future a similar set of facts was to be presented to the Australian Competition and Consumer Commission, it is probable that the Commission would attempt to discover:

- what the credit policies and procedures were for the financier;
- what the financier's *Trade Practices Act 1974* (Cth) compliance program was; and
- what the organisation's compliance and internal audit reports indicated in regard to the employees' level of compliance with the previously mentioned organisation's policies, procedures and programs.

A postscript to this case is that the Australian Competition and Consumer Commission on 15 August, 2005 (ie two days prior to the decision in the case

[360] Ibid.

being published) released a brochure entitled 'Don't take advantage of disadvantage – A compliance guide for businesses dealing with disadvantaged or vulnerable consumers'. The Commission quotes on their website in regard to this publication, that:

> This brochure will help businesses recognise when they are dealing with disadvantaged or vulnerable consumers and outline the factors they may need to consider in these situations with reference to recent court decisions.[361]

The publication identifies to businesses various classes of consumers who may be disadvantaged or vulnerable, such as consumers with the following characteristics:

- low income;
- poor English language skills;
- disabilities, whether it be intellectual, psychiatric, physical, sensory, neurological or a learning disability;
- serious or chronic illness;
- poor reading, writing and numeric skills;
- being homeless;
- being very young or very old;
- coming from a remote area; or
- having an indigenous background.[362]

The publication puts businesses on notice that these bodies of consumers are especially vulnerable to unfair business conduct, and that business needs to make sure that these consumers understand everything that is said to them, and that if the business is unsure, the consumers should be given an opportunity to think about the transaction or discuss it with someone.[363]

The publication of the above document by the Australian Competition and Consumer Commission, when seen in context with Finn J's comments in

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[361] Australian Competition and Consumer Commission, 'Don't take Advantage of Disadvantage: a Compliance Guide for Businesses Dealing with Disadvantaged or Vulnerable Consumers' <http://www.accc.gov.au/content/index.phtml/itemId/704340> at 11 November 2006.

[362] Ibid, 2.

[363] Ibid, 4.

regard to his expectations for risk management practices, no doubt will assist the evidentiary burden of the Commission in future cases with similar facts. The Commission will be able to refer to its published document as having put the finance industry on notice as to the consumer characteristics that financier's risk management practices should concentrate upon in order to detect and protect consumers like Mr Groth.

On the flipside of the coin, some smaller financiers[364] might be concerned that it could actually increase their credit risk profile if they were to detail within their credit processes the requirement to recognise as detracting features (and accordingly undertake mitigative action) many of the personal characteristics contained within the Australian Competition and Consumer Commission's publication. The existence of such risk management procedures may facilitate their admission into evidence through discovery proceedings, and thus create for smaller financiers a higher standard of conduct required, as opposed to if they had not strengthened their risk management procedures to recognise the Australian Competition and Consumer Commission's list of possible disadvantaged scenarios.

[364] It is seen as being more an issue for small financiers, as large financiers usually place significant importance on being good corporate citizens, and adopting into their procedures regulators recommendations and guidelines.

5.4 THE CIRCUMSTANCES IN WHICH UNCONSCIONABLE CONDUCT ACTIONS AND MISLEADING AND DECEPTIVE CONDUCT ACTIONS OVERLAP

As there are a number of cases where relief is sought using both the *Trade Practices Act 1974* (Cth) s 52 misleading and deceptive conduct provisions and the Part IVA unconscionability provisions, some of these cases will be examined to determine first whether there is a 'common thread'. Secondly, whether there are reasons for one type of action being more successful than the other, or whether it merely reflects the prevalence with which s 52 is argued as an alternative action in so much commercial litigation.

Crisp v Australia & New Zealand Banking Group Ltd

In a single judge (Northrop J) decision in the Federal Court case of *Crisp v Australia & New Zealand Banking Group Ltd*,[365] both s 52 and *Amadio* unconscionability were argued. The facts revolved around the Australia and New Zealand Banking Group Ltd ('ANZ'), which sought a mortgage from Mr Crisp to secure the existing debts of a company owned by his wife and daughter. Essentially, the mortgage was to 'prop up' the ANZ's existing exposure, which was largely unsecured. The company was in financial difficulties, with the bank having dishonoured cheques and having threatened to cancel a temporary overdraft facility.

Despite the claims of the bank to the contrary, Northrop J was satisfied that the bank had not advised Mr Crisp that cheques were being returned, or that his mortgage would secure the company's total liabilities as opposed to just an overdraft facility. Northrop J held that if Mr Crisp had been aware of the fact that cheques were being dishonoured, then he would not have provided his mortgage. Northrop J stated:

> On these findings, it is not necessary to consider the other basis for the relief sought by Mr Crisp. Where a statute imposes a legal obligation on a corporation, in trade or commerce, not to engage in conduct which is misleading or deceptive or is likely to mislead or

[365] (1994) ATPR 41-294.

> deceive and confers a remedy on a person who suffers loss by reason of that conduct, and that case is established, it is unwise for a Court to consider an equitable claim which has technical difficulties, both of law and of fact, and which would result in no greater remedy to the claimant. This view is strengthened when consideration is given to subsequent actions which could constitute a good defence to the equitable claim but do not constitute a defence to the claim under the *Trade Practices Act*.[366]

Given that the withholding of vital facts can constitute misleading and deceptive conduct,[367] and despite the fact there was no intention from the ANZ to mislead or deceive, the bank was found to have breached s 52 and thus relief under s 87 was granted. The mortgage was declared void ab initio and was set aside.

Northrop J indicated that as a breach under s 52 had been established, there was no need for the Court to express an opinion on the *Amadio* unconscionability claim.[368]

National Australia Bank Ltd v Nobile

The Full Federal Court decision in *National Australia Bank Ltd v Nobile*[369] is a case where one set of guarantors (Mr and Mrs Nobile) were not successful in an unconscionability claim to have their guarantee and mortgage set aside, but were successful with a s 52 claim, whereas the other guarantors (Mr and Mrs Martelli) were successful in their unconscionability claim to have their guarantee set aside.

Carlo Martelli and his wife Pierina Martelli owned a building company, Suesha Nominees Pty Ltd. The business was under-capitalised and not performing well, with the National Australia Bank Limited ('NAB') having dishonoured cheques the company had written, due to the debt in the overdraft account being outside limit arrangements. The NAB requested

[366] Ibid, 41,940.

[367] For example, see *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546.

[368] (1994) ATPR 41-294, 41,941–41,942.

[369] (1988) 100 ALR 227.

additional security to regularise the debt in the overdraft account, so Carlo Martelli and Pierina Martelli each approached their respective parents with a request to provide security. Pierina Martelli's parents, Mr and Mrs Nobile ('Mr and Mrs N'), provided a guarantee as well as a mortgage over land. Carlo Martelli's parents ('Mr and Mrs M') provided a guarantee only. The parents were emigrants from Italy aged in their fifties, had a limited education or understanding of complex business transactions and did not have a good understanding of the English language. The NAB did not require the parents to obtain independent legal advice prior to providing their security.

The circumstances in regard to the two sets of parents providing their security differed in an important respect. Mr and Mrs N were not aware that the company was in serious financial difficulty and relied upon the NAB Manager's advices that the company was going well. This was despite the Manager knowing that this was not true.

The company subsequently was wound up and Mr and Mrs M were made bankrupt on their own petitions. The guarantees and supporting security were called upon by the bank to satisfy the company's debts, and the matter was at first instance heard by Jackson J of the Federal Court.[370] Jackson J set aside the guarantee and mortgage from Mr and Mrs N on the basis of a breach of s 52 of the *Trade Practices Act 1974* (Cth) and unconscionable conduct by the NAB in procuring the execution of the security. Jackson J also set aside the guarantee from Mr and Mrs M, but only on the basis that the NAB's conduct constituted unconscionable conduct in procuring their execution of the guarantee. The decision was appealed by the NAB to the Full Federal Court (Davies, Neaves and Spender JJ).

Davies, Neaves and Spender JJ all agreed that the misrepresentation by the NAB to Mr and Mrs N constituted a breach of s 52. Neaves and Spender JJ

[370] *Nobile v National Australia Bank Ltd* (1987) ATPR 40-787.

disagreed that there was any unconscionable conduct involved in the NAB taking the security from Mr and Mrs N.

This decision was reached due to the following considerations. First that Mr and Mrs N were not customers of the NAB branch. Secondly, the fact that they had come forward and offered to provide their security to assist the business being run by their daughter and son-in-law. Thirdly, even though it is possible that Mr and Mrs N had been induced by their son-in-law to provide their security, and that what they had been told by the son-in-law was misleading or untrue, the bank was not aware of this possibility and thus the trial judge was in error taking that into consideration when he found that Mr and Mrs N were at a special disadvantage vis-à-vis the bank.[371]

All three Justices however agreed with the trial judge that the NAB's behaviour in taking the guarantee from Mr and Mrs M constituted unconscionable conduct. The relevant facts in establishing that there had been unconscionable conduct, were as follows. Mr and Mrs M had been customers for 24 years of the NAB branch that had taken the guarantee, and therefore Mr and Mrs M were entitled to rely upon proper dealing by the bank and its manager with them. In addition, the limited financial position of Mr and Mrs M made the provision of the guarantee very disadvantageous to them[372] and only advantageous to their son and the bank. Given their poor knowledge of the English language and absence of understanding of complex financial arrangements, Mr and Mrs M must have entered the guarantee without a proper understanding of the transaction[373] and without the benefit of independent advice.

The Full Federal Court's decision probably does not provide any value in terms of indicating any link between s 52 actions and unconscionable

[371] *National Australia Bank Ltd v Nobile* (1988) 100 ALR 227, 252, Neaves J.

[372] With Neaves J noting at 252 that if Mr and Mrs M were required to discharge their liability under the guarantee then it would totally, or almost totally, exhaust their assets.

[373] Ibid, 241.

conduct claims, other than that when there is a general failing on the part of bank staff to properly ensure that third party security providers are honestly and accurately informed of the nature of their liability, misleading and deceptive conduct as well as unconscionable conduct should both be explored to provide possible relief against enforcement of the security.

The other interesting aspect of this case is the weight placed on the fact that the guarantors had a long relationship with the bank and branch that sought the provision of their security, and that this was seen by the majority as an important factor in determining that reliance could be placed on the bank by Mr and Mrs M (and not by Mr and Mrs N, who did not have such a relationship with the bank and that branch).

Australian Competition and Consumer Commission v Oceana Commercial Pty Ltd

A later case (2003) where the Federal Court (Kiefel J) had to consider both a s 52 claim for relief, as well as an unconscionability claim under the *Trade Practices Act 1974* (Cth), was *Australian Competition and Consumer Commission v Oceana Commercial Pty Ltd.*[374] This case dealt with the purchase of a Gold Coast investment property by a married couple, the Gleesons. The Gleesons were exploited by a property investment company, Oceana Commercial Pty Ltd ('Oceana'), who persuaded them to make a negatively geared investment into property. The Commonwealth Bank were the Gleeson's financiers and had no connection with Oceana. The bank was made aware from its security property valuation that the Gleesons had entered a contract of sale to pay above the market price for the security property.

The Federal Court was asked to consider a number of arguments, the most important for our purposes being whether it was either misleading and deceptive, or unconscionable, for the bank not to inform the Gleesons of the lower than expected valuation amount or to advise the Gleesons to obtain

[374] (2004) Aust Contract R 90-193.

independent advice in regard to the value of the property. Kiefel J rejected the notion that the bank had acted either in breach of s 52 or had acted unconscionably. Kiefel J found that the bank had acted correctly.

His Honour observed that the Gleesons had committed to purchase the property before they had approached the bank, that the bank had not advised the Gleesons they would be informed of the bank's own valuation details, and that the Gleesons were not under any disability that would have prevented them from making a judgment in their own best interests.

The case went on appeal to the Full Federal Court (although the appeal did not include an appeal on Kiefel J's decision that a s 52 action against the bank had no foundation), where Heerey, Sundberg and Dowsett JJ agreed with the decision of Kiefel J.[375]

In determining whether the loan applicants suffered under a special disadvantage for purposes of ss 51AA or 51AC of the *Trade Practices Act 1974* (Cth), Heerey, Sundberg and Dowsett JJ agreed with the trial judge, Kiefel J, that the loan applicants did not suffer from a special disadvantage for the purposes of *Amadio*. 'Her Honour described the Gleesons as "… educated, intelligent people, well able to comprehend that the price sought for a property may not be the same as its market value''.'[376]

Heerey, Sundberg and Dowsett JJ concurred with the trial judge that the loan applicants would have been able to protect their own interests if they had obtained their own valuation of the property, and that this oversight by the Gleesons did not constitute a disability or weakness of the type necessary to establish an *Amadio* action.[377] This decision by their Honours was not

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[375] *Australian Competition and Consumer Commission v Oceana Commercial Pty Ltd* (2004) ASAL (Digest) 55-128; (2004) 139 FCR 316; (2004) ATPR (Digest) 46-255; [2004] FCAFC 174 (5 July 2004, BC200404122). Subsequent citations for this case refer to the last-mentioned unreported citation as the reported sources do not report the case in full.

[376] Ibid, [25].

[377] Ibid.

surprising given that the male loan applicant had for 20 years been an architect and licensed builder. Senior counsel for the bank commented that there was never any person less likely to fall within the categories of persons able to invoke the *Amadio* principles.[378]

The Gleesons specifically argued that under the relevant matters which the court may consider under s 51AC(3) in order to determine if behaviour was unconscionable, that s 51AC(3)(i) was relevant. The Gleesons applied to the facts of their case the extent to which a

> … supplier unreasonably failed to disclose to the business consumer … any risks to the business consumer arising from the supplier's intended conduct (being risks that the supplier should have foreseen would not be apparent to the business consumer);[379]

The Gleesons were not successful in having the court see this as relevant to the facts for their claim under s 51AC, given that the Bank had told them that they would not make the valuation available and that the loan applicants should not draw any conclusions in regard to the fact that the bank was prepared to make a loan based upon the valuation. Similarly, nothing had stopped the loan applicants from making their own inquiries to determine the value of the property.[380] So although the bank was aware that the applicants were paying too much for the property, they were not required to be property valuer advisers to their loan applicants. The bank knew that the Gleesons were paying too much for the property, but not that the Gleesons were being misled (as the Gleesons were free to make their own inquiries in regard to the wisdom of the purchase price). Gail Pearson aptly summed up this predicament when she stated:

> In this situation, to decline to act in a way that was tantamount to giving advice was not unconscionable. The decision raises a neat problem as to the boundaries between disclosing risk and giving advice.[381]

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[378] Ibid, [172].

[379] Ibid, [179].

[380] Ibid, [26]–[27].

[381] Gail Pearson, 'The Ambit of Unconscionable Conduct in Relation to Financial Services' (2005) 23 *Company and Securities Law Journal* 105, 125.

In regard to s 52, the trial judge's dismissal of such an action against the bank (which the Australian Competition and Consumer Commission chose not to argue on appeal) was based on the fact that there was no fiduciary relationship between the finance applicant and the bank, nor did the loan applicants give any evidence to show that over time they had come to rely upon advice from the bank. The trial judge distinguished this decision from the Full Federal Court decision of Davies, Sheppard and Gummow JJ in *Commonwealth Bank of Australia v Smith*.[382] This was a case where s 52 was successfully applied. The bank manager had not only given advice to the loan applicants (without having the knowledge to do so), but had also told the applicants that the vendor of the property banked with him, strengthening the expectation that the bank manager's knowledge was correct.

Collection House Ltd v Taylor

Collection House Ltd v Taylor[383] dealt with the approach taken by a collection agency to recover a debt sold / assigned to them by a financier, and whether the collection agency's actions were unconscionable or misleading and deceptive conduct.

The Supreme Court of Victoria heard an appeal from the Victorian Civil and Administrative Tribunal ('VCAT'), in regard to a car loan from Australian Guarantee Corporation Limited ('AGC'). The debt was defaulted upon and sold to a collections agency, Collection House Ltd ('Collection House'). Collection House is a publicly listed company and is one of the largest debt collecting agencies in Australia.

The facts were as follows. An employee of Collection House had phoned the residence of the debtor (Ms Taylor – unemployed mother with deaf children) at 6.30 pm one evening, identified himself as working for ALR Lawyers, and requested repayment of a debt totalling $10,870. At the time the phone call

[382] (1991) 42 FCR 390; (1991) 102 ALR 453.

[383] (2004) ATPR 41-989.

was made, the debt was statute barred as it was ten years old (ie there was no ability to commence legal action to recover the debt, as no action had been taken to 'refresh' the debt in the past ten years – under s 5 of the *Limitation of Actions Act 1958* (Vic), recovery action for a debt is statute barred after six years). Collection House had advised Ms Taylor that legal action would be commenced unless arrangements to repay the debt were put in place. It was agreed the debtor would pay $5,000 in full satisfaction of the debt, and $4,500 was debited to the debtor's credit card in part satisfaction of that arrangement (the residual $500 amount was also subsequently paid).

The next day the debtor asked for advice from the Victorian Citizen's Advice Bureau. The advice provided by the Bureau was that any legal action for recovery of the debt would be statute barred under the *Limitation of Actions Act 1958* (Vic), given it was more than six years old. Before Ms Taylor paid the additional $600, Collection House had told Ms Taylor that the Act did not prevent the recovery of the debt (Collection House subsequently argued at the VCAT hearing that the debt was refreshed by the repayment of the $4,500).

Ms Taylor commenced legal action before the VCAT claiming an order against Collection House for payment of the $5,000, alleging that Collection House had engaged in misleading and deceptive conduct and unconscionable conduct in breach of ss 7 and 9 of the *Fair Trading Act 1999* (Vic) (ss 7 and 9 corresponded respectively with ss 51AA and 52 of the *Trade Practices Act 1974* (Cth)). A breach of s 12 of the *Fair Trading Act 1999* (Vic), in that false representations were made in relations to goods and services, was also alleged by Ms Taylor.

The misleading and deceptive conduct was alleged in regard to two aspects of the advice from the Collection House employee. The first aspect was the advice that the debt was not statute barred. The second aspect was the Collection House employee claim to be from a legal firm. The Member from the VCAT determined that 'I regard the way the approach [was made] and

the whole concept of the discussions and conversation, as being misleading and deceptive.'[384]

As well as engaging in misleading and deceptive conduct, the Member also found that Collection House had engaged in unconscionable conduct and had made false representations. Judgment was entered for Collection House to repay the $5,000 to the debtor.

On appeal by Collection House to the Supreme Court of Victoria it was argued, amongst other matters, that Ms Taylor's lack of knowledge of the matters in issue did not disable her from making a decision in her best interests. This was demonstrated by her actions in seeking external advice on her position the following day after paying the $4,500 (and before she paid the $500 residual). Nettle J upheld the decision in regard to the unconscionability finding, stating that:

> In my view the fact that any impoverished debtor is willing to pay $5,000 in settlement of a 10 year old statute barred finance company debt of $11,000 is probably sufficient without more to raise in the mind of a reasonable person the possibility that the debtor does not know of the limitation period and might not have agreed to pay it if they had known. In any event, the facts would be sufficient to cast upon the beneficiary of the transaction the burden of establishing that the transaction was fair, just and reasonable; and in this case it was not. Once one adds to the equation the impecuniosity and ignorance and perhaps also emotional difficulties of the kind from which the respondent was known or believed to suffer, the case becomes a clear one.[385]

Nettle J accordingly dismissed the appeal, as the conduct of the appellant was unconscionable. Nettle J did not need to decide on one of the questions in the grounds of appeal: of whether the VCAT had been in error in regard to its finding of misleading and deceptive conduct. Nettle J found that it was an open question whether the Tribunal had erred on this issue.[386]

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[384] Ibid, 48,591 [17].

[385] Ibid, 40,514 [58].

[386] The VCAT at its hearing had declined an adjournment to allow Collection House to supply evidence clarifying the arrangement that existed between the employee from Collection House and their legal advisers (Collection House had alleged the employee was seconded to the legal

Australian Competition & Consumer Commission v 4WD Systems Pty Ltd

In the Federal Court case of *Australian Competition & Consumer Commission v 4WD Systems Pty Ltd*[387] it was established that misleading and deceptive conduct by itself is not sufficient to attract the unconscionability provisions of the *Trade Practices Act 1974* (Cth).

The Australian Competition and Consumer Commission alleged that 4WD Systems Pty Ltd and its directors breached ss 51AC, 52 and 53(a)[388] in its sale of franchises for retailing and fitting differential locks to 4WD vehicles. 4WD Systems Pty Ltd sold the franchises to the franchisees claiming that it was distributing a US make of the differential locks. 4WD Systems Pty Ltd, however, subsequently substituted the US brand for a product it made itself and packaged it in a manner similar to the US product. Delay in supply of differential locks to the franchisees also became an issue, with manufacture of the parts not being commenced until the franchisees had first ordered and paid. The Australian Competition and Consumer Commission tried to establish 4WD Systems Pty Ltd's behaviour as unconscionable, and stated that all of the circumstances of 4WD Systems Pty Ltd's behaviour needed to be considered (ten pages of circumstances were listed).

Selway J stated:

> In order to find that conduct is "unconscionable" it is necessary to do more than merely show that the behaviour is misleading or deceptive, or otherwise in breach of some other provision of the *TPA*. What is necessary is to show that the conduct is so unacceptable that it can properly be described as "unconscionable". Normally it might be expected that behaviour would only be

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firm). Collection House argued that if they had been allowed to supply this evidence, it would have established that there was a basis for their employee to claim he worked for the legal firm.

[387] (2003) 200 ALR 491.

[388] Section 53(a) False or misleading representations

A corporation shall not, in trade or commerce, in connexion with the supply or possible supply of goods or services or in connexion with the promotion by any means of the supply or use of goods or services:

(a) falsely represent that goods are of a particular standard, quality, value, grade, composition, style or model or have had a particular history or particular previous use; …

> "unconscionable" if some moral fault or responsibility is involved. Normally it might be expected that this would involve either a deliberate act, or at least a reckless act. Mere unreasonableness or unfairness may not be sufficient, at least in the absence of some moral fault.[389]

[389] (2003) 200 ALR 491, 544 [185].

Summary

These cases demonstrate that it is not unusual for misleading and deceptive conduct to be argued by the debtor or security provider, in conjunction with unconscionability. This is likely due to the following reasons.

If a finance provider has a lack of procedures/compliance programs or lack of ethics that contributes to the adoption of behaviour that is construed to be unconscionable, there may be an increased likelihood these same factors lead their staff to engage in misleading or deceptive conduct when they deal with debtors and security providers.

Another possible reason is due to the volume of financial information that a financier is normally in receipt of when a finance application is made. In addition, if the application is from an existing customer, the accumulation of data that a bank financier receives during the normal course of business, allows a perception to be formed as to how the business venture is performing. This weight of data held by the financier increases the possibility that financiers may, in error, not disclose correctly to a security provider the facts in regard to a borrower.

The final possible reason is the increased prevalence in modern commercial litigation cases for a party to allege misleading and deceptive conduct as an alternative cause of action.

The tendency of the Australian Competition and Consumer Commission to argue a case in the alternative as having both misleading and deceptive conduct aspects and unconscionability aspects, was explained by the Commission's Chairman, Graeme Samuel, in his speech delivered on 3 July 2007.[390]

> In most unconscionable conduct cases there is also an element of

[390] Graeme Samuel, Chairman Australian Competition and Consumer Commission speech, 'Competition and fair trading: a fair go for small business' (Speech delivered at the National Small Business Summit, Sydney, 3 July 2007).

> misleading and deceptive conduct, which is much easier to prove. As a result there has been a tendency for us to say, "let's just tackle the misleading and deceptive conduct rather than take the more difficult route of going after the unconscionable conduct elements of a case". While this approach often works in shutting down the conduct, it is sometimes a bit too easy for our investigators to let the unconscionable behaviour slide.[391]

The Chairman announced that the Commission was changing its focus to take a much more aggressive approach to pursuing unconscionable conduct and to get more cases before the courts, and that this may result in a better definition of what constitutes unconscionable conduct.[392]

We may therefore see a growth in Part IVA of the *Trade Practices Act 1974* (Cth) unconscionability actions for cases where both unconscionable conduct and misleading and deceptive behaviour occur, where previously the more tried path of only a s 52 action has been run. The elements necessary to establish unconscionability and misleading and deceptive conduct remain quite distinct, however.

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[391] Ibid, 3.

[392] Ibid. This speech was made within a fortnight of the *Trade Practices Legislation Amendment Bill (No.1) 2007* (Cth) being introduced into the Parliament. That Bill proposed a new Deputy Commissioner to look after the interests of small business, increased the upper limit from $3 million to $10 million for cases that could be prosecuted under s 51AC, as well as added within that section the ability for the court to consider that the right of the stronger party to make unilateral changes as an aspect that may be indicative of unconscionable conduct. The Bill was passed and received Royal Assent on 24 September 2007. On 21 November 2008 the *Trade Practices Legislation Amendment Act 2008* (Cth) removed the $10 million limit, so that now no limit applies.

6. *AUSTRALIAN COMPETITION AND CONSUMER COMMISSION V CG BERBATIS (HOLDINGS) PTY LTD*

6.1 INITIAL FEDERAL COURT AND FULL FEDERAL COURT DECISIONS

One of the more important decisions during the last decade concerning the *Trade Practices Act 1974* (Cth) sections on unconscionability, was the High Court decision in *Australian Competition and Consumer Commission v CG Berbatis (Holdings) Pty Ltd*[393] (*Berbatis*). Once s 51AC was inserted into the Act, the Australian Competition and Consumer Commission saw retail tenancy disputes as a 'high litigation priority area'.[394]

The case involved a tenancy dispute in a shopping centre known as 'Farrington Fayre' located at Leeming, Western Australia. A number of the tenants had been litigating against the landlord, Berbatis (Holdings) Pty Ltd ('Berbatis Holdings'). The lease over the premises became due for renewal for some of the tenants involved in the litigation, including the Roberts.[395] The Roberts had arranged for the sale of their business that used the leased premises, the sale being dependent upon the lease being renewed and assigned to the purchasers. The sale was necessary for the Roberts as their daughter was ill with encephalitis. Her illness required a lot of attention from the Roberts and added great personal stress and emotional strain to the Roberts' lives. The Roberts were also under financial pressure.

Berbatis Holdings was aware of the disadvantages the Roberts were under; eg the emotional issues with their daughter's illness and the financial pressures

[393] (2003) 214 CLR 51.

[394] Michelle Sharpe and Christine Parker, 'A bang or a whimper? The impact of ACCC unconscionable conduct enforcement' (2007) 15 *Trade Practices Law Journal* 139, 147, quoting Professor Allan Fels (then the Australian Competition and Consumer Commission Chairman) from an article by B Wilson, 'Watchdog Targets Bad Landlords', *The Courier Mail* (Brisbane), 16 April 1999. The Australian Government had directed the Commission to commence representative actions with a view to developing legal precedents on matters of concern to small business.

[395] There was an absence of an option to renew in the existing lease agreement; ie the Roberts were unable to compel Berbatis Holdings to renew the lease as Berbatis Holdings had no contractual obligation to renew the lease.

they were under, plus the need for the extension and assignment of the lease to be approved in order to facilitate the sale of the business. The Roberts approached Berbatis Holdings with a request for extension in contemplation that the lease would need to be assigned to new purchasers. Berbatis Holdings made it a condition for the lease renewal that the Roberts' litigation against the company must be abandoned.

The Australian Competition and Consumer Commission ran the case as a test case and argued that as Berbatis Holdings were aware of the Roberts' situational disabilities, the company's conduct in inserting the offending provisions (the abandonment of the litigation) in the lease renewal contract had breached the unconscionability provisions of s 51AA. The actions took place before the small business provisions in s 51AC came into existence on 1 July 1998. The case was, however, probably a good indicator of how the courts may consider a s 51AC case. That is, if it had been a s 51AC case, even though there is a broad range of factors that the court may consider under ss 51AC(3) or 52AC(4),[396] there is nothing to indicate that a court would deviate from its usual position of limiting the factors that it considers to only be those of traditional unconscionability within the meaning of the unwritten law.

The arguments presented by counsel for the Australian Competition and Consumer Commission, both at first instance and at subsequent appeals, were that the Roberts' facts fell within the narrow equitable category of unconscionable dealing under s 51AA, as opposed to arguing a wider interpretation of s 51AA.

At first instance, Justice French in the Federal Court had found in favour of the Australian Competition and Consumer Commission.[397] Justice French

[396] These factors include the court considering the relative strengths of the bargaining positions of the parties, whether the conduct of the supplier was not reasonably necessary for the protection of the legitimate interests, whether the supplier acted in good faith or observed industry codes etc.

[397] The decisions of French J are in two separate reported cases. In the first case, *Australian Competition & Consumer Commission v CG Berbatis Holdings Pty Ltd* (2000) 96 FCR 491,

decided that the class of disadvantage that would attract the unconscionability provisions of s 51AA would include positions of 'situational disadvantage' such as the Roberts were under in regard to the impending expiry of their lease. Justice French stated:

> The use of the word "special" to describe the class of disadvantage or disability which will attract the application of the doctrines of equity is not to be treated as one would treat the word in a statute. It indicates that the requisite disadvantage will not necessarily be found in the normal run of bargaining inequality between large landlords and small tenants. In my opinion, however, the circumstances in which a business operator on a lease may effectively lose the value of that business upon expiry of the lease does place the tenant at a special disadvantage in dealing with the owner.[398]

Having concluded that the Roberts were in position of disadvantage due to a situational circumstance, Justice French found that Berbatis Holdings had exploited the Roberts unfairly by inserting the additional term in the lease renewal. Justice French summarised the reasons for this conclusion as follows:

> Unfair exploitation of disadvantage amounting to unconscionable conduct may occur when an owner uses its bargaining power to extract a concession from the tenant that is commercially irrelevant to the terms and conditions of any proposed new lease. … This is an area of evaluation and assessment where there are few hard and fast guides. In my opinion for the owners to insist, as they did through Mr Sullivan in this case, upon the Roberts abandoning their rights to proceed with bona fide litigation in relation to their rights under their existing lease was to engage in unconscionable conduct. … The way in which the owners acted, through their agent Mr Sullivan and his company, was a grossly unfair exploitation of the particular vulnerability of the Roberts in relation to the sale of their business.[399]

French J considered whether s 51AA was, in terms of the Constitution, beyond the power of the Commonwealth Parliament to have enacted. French J concluded that s 51AA was within the power of the Parliament and provided a detailed analysis of unconscionability. Having established that there were no constitutional issues, in *Australian Competition & Consumer Commission v CG Berbatis Holdings Pty Ltd* (2000) ATPR 41-778, French J examined the behaviour of Berbatis in order to determine if a breach of s 51AA had occurred based on his interpretation of that section advanced in the earlier case, *Australian Competition & Consumer Commission v CG Berbatis Holdings Pty Ltd* (2000) 96 FCR 491.

[398] *Australian Competition & Consumer Commission v CG Berbatis Holdings Pty Ltd* (2000) ATPR 41-778, 41,198 [123].

[399] Ibid, 41,198 [123]–[124].

On appeal to the Full Federal Court,[400] Hill, Tamberlin and Emmett JJ, overturned the decision of French J. Their Honours adopted a narrower definition of unconscionability under s 51AA, and accordingly held that the Roberts were under no special disadvantage. Their Honours reasoned:

> A distinction can be drawn between parties who adopt an opportunistic approach to strike a hard bargain and parties who act unconscionably - see *ACCC v Samton Holdings Pty Ltd* [2000] FCA 1725 at [99]. It cannot be said that the Roberts' wills were so overborne that they did not act independently and voluntarily. Unfortunately for the Roberts, the Owners were under no obligation to renew or extend their lease. The Roberts had the choice of either maintaining their legal claims against the Owners and losing the opportunity to sell their business or abandoning their claims and gaining the opportunity to sell their business. They made that choice of abandoning their claims. That may have been a hard bargain, but it was not an unconscionable one.
>
> It is inappropriate to characterise the detriment that a tenant has by reason of the imminent expiration of a lease as a special disadvantage. His Honour appears to have accepted that proposition. His Honour erred, however, in concluding that the Roberts were under a special disadvantage such that the arrangements that they entered into in December 1996, with proper legal advice, were unconscionable. It follows that there was no contravention of s 51AA in relation to the conduct of the Owners from October to December 1996.[401]

The matter proceeded on appeal to the High Court by the Australian Competition and Consumer Commission.

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[400] *CG Berbatis Holdings Pty Ltd v Australian Competition and Consumer Commission* (2001) 185 ALR 555.

[401] Ibid, 571 [81]–[82].

6.2 HIGH COURT OF AUSTRALIA DECISION

The High Court (Gleeson CJ, Gummow, Hayne and Callinan JJ, with Kirby J dissenting) upheld the Full Federal Court decision. [402]

Gleeson CJ explored the background to s 51AA (looking to the Explanatory Memorandum), and commented that unconscionability was a legal term and not a colloquial expression.[403] He then went on to make a broad observation of the purpose of s 51AA in specific regard to the type of dilemmas that people like the Roberts find themselves in:

> Unconscientious exploitation of another's inability, or diminished ability, to conserve his or her own interests is not to be confused with taking advantage of a superior bargaining position. There may be cases where both elements are involved, but in such cases, it is the first, not the second, element that is of legal consequence. It is neither the purpose nor the effect of s 51AA to treat people generally, when they deal with others in a stronger position, as though they were all expectant heirs in the nineteenth century, dealing with a usurer.[404]

Gleeson CJ also drew a clear distinction that the absence of a contracting party being able to 'get their own way', does not entitle them to the availability of relief under the *Trade Practices Act 1974* (Cth):

> Reference was earlier made to counsel's submission that there was here a disabling circumstance affecting the ability of the lessees to make a judgment in their own best interests. In truth, there was no lack of ability on their part to make a judgment about anything. Rather, there was a lack of ability to get their own way. That is a disability that affects people in many circumstances in commerce, and in life. It is not one against which the law ordinarily provides relief.[405]

His Honour held that being at a disadvantage[406] was not adequate grounds for unconscionable conduct to be established. Rather it was necessary for a party

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[402] *Australian Competition and Consumer Commission v C G Berbatis Holdings Pty Ltd* (2003) 214 CLR 51.

[403] Ibid, 63.

[404] Ibid, 64.

[405] Ibid, 65.

[406] Even if there was, as French J viewed it, a grossly unfair exploitation of that disadvantage.

to be at a special disadvantage, which the stronger party exploits. Gleeson CJ acknowledged the possibility that, on a different set of facts, a special disadvantage could be situational, provided that such a description did not '… take on a life of their own, in substitution of the language of the statute, and the content of the law to which it refers'.[407]

Gummow and Hayne JJ saw that the withdrawal of the litigation was not relevant to the extension of the lease. This was a matter which should be left to the parties to decide. Gummow and Hayne JJ also held that for unconscionability to be established, the Roberts would have had to prove that a special disadvantage resulted in their loss of capacity to make a decision in their own best interests (which was not the case – 'the situation in which the Roberts were placed did not necessarily support the conclusion that they lacked the capacity to make a judgment about their best interests.').[408]

Callinan J also dismissed the appeal. His Honour observed that the case did not provide the opportunity for a complete exposition of s 51AA.[409] In addition, the case did not establish an answer to the question as to whether that section's reference to unconscionable conduct within the unwritten law was limited to the equitable doctrine of unconscionability. Dal Pont and Chambers believe that a wider reference was possible:

> It cannot be said that that which is unconscionable within the unwritten law is limited to the equitable doctrine of unconscionability. Numerous equitable doctrines are grounded, at least in part, in the notion of unconscionable conduct, including estoppel, unilateral mistake, undue influence, economic duress, constructive trusts and relief against forfeiture.[410]

It should be noted that the majority Justices, Gleeson CJ, Gummow, Hayne and Callinan JJ, did not close off the possibility that a wider interpretation of

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[407] *Berbatis* (2003) 214 CLR 51, 63.

[408] Ibid, 77–78.

[409] Ibid, 114.

[410] Nicole Dean, 'Cases and Comments *ACCC v Berbatis Holdings* (2003) 197 ALR 153' (2004) 26 *Sydney Law Review* 255, 257, quoting Gino E Dal Pont and Donald R C Chalmers, *Equity and Trusts in Australia and New Zealand* (2nd ed, 2000), 273.

what is unconscionable may occur. For example Justices Gummow and Hayne saw that:

> It is unnecessary to resolve these questions concerning the reach of s 51AA because …. the litigation was conducted on the footing that the facts fell within that well-established area of equitable principle concerned with the setting aside of transactions where unconscientious advantage has been taken by one party of the disabling condition or circumstances of the other.[411]

Kirby J, in contrast, explored the doctrinal criteria of unconscionable dealing, by reference to the purpose of equity, which was to relieve against an unconscionable dealing. Rather than just stating that equity's motivation is to moderate the common law with a desire to 'do more perfect and complete justice' than would be the result of leaving the parties to their remedies at common law,[412] Kirby J clarified that equity's purpose as being:

- protection of the integrity of the contracting process;[413]
- 'protection of the assumptions and conditions necessary to make effective the freedom to contract of the parties';[414]
- maintenance of 'broader principle of ethical behaviour';[415]
- achievement of 'justice in the individual case';[416] and
- prevention of 'behaviour contrary to conscience.'[417]

Kirby J looked at the entire background to the Roberts' negotiations with Berbatis Holdings, and saw as important that Berbatis Holdings, through their agents, were aware of the factors that contributed to the Roberts' need to sell the business (the emotional stress from the daughter's illness).

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[411] *Berbatis* (2003) 214 CLR 51, 74.

[412] Rick Bigwood, 'Curbing Unconscionability: *Berbatis* in the High Court of Australia' (2004) 28 *Melbourne University Law Review* 203, 217, with reference to Lord Selborne LC's comments in *Wilson v Northampton & Banbury Junction Railway Co* (1874) LR 9 Ch App 279, 284.

[413] *Berbatis* (2003) 214 CLR 51, 83.

[414] Ibid, 91.

[415] Ibid, 82.

[416] Ibid, 95.

[417] Ibid, 84.

Kirby J commented on the 'warning effect' to others that a favourable decision for the Roberts under the *Trade Practices Act 1974* (Cth) unconscionability provisions could result in, when he stated:

> By upholding the rights of the Roberts – on the face of things small and objectively of limited significance – a message is delivered that that Act is not to be trifled with.[418]

Kirby J found in favour of the Australian Competition and Consumer Commission:

> Given that the relevant factual findings are undisturbed and that the primary judge did not make any error of legal principle, this Court should affirm his Honour's judgment.[419]

A former Commissioner of the Australian Competition and Consumer Commission, Sitesh Bhojani, has since commented on the reasons why the Commission had taken a limited approach to its pleadings in *Berbatis*, saying that:

> … we were trying to get guidance as to how the three provisions [sections 51AA, 51AB and 51AC] interacted … So we put forward an *Amadio* type interpretation or approach but the High Court rejected it and didn't comment on its reach. This was very disappointing. The High Court didn't have to say anything of course but they usually do say something in obiter that would have given us some guidance. In hindsight we could have reached further, taken a broader approach of the section.[420]

Lynden Griggs concludes in his article 'Unconscionability in the High Court – the ACCC on the receiving end again!'[421] that 'one can only hope that the ACCC has not been so exhausted by its recent losses that it will stop searching for the appropriate vehicle to enable this exposition to occur.'[422]

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[418] Ibid, 95–96.

[419] *Australian Competition and Consumer Commission v C G Berbatis Holdings Pty Ltd* (2003) 214 CLR 51, 79–80.

[420] Michelle Sharpe and Christine Parker, 'A Bang or a Whimper? The Impact of ACCC Unconscionable Conduct Enforcement' (2007) 15 *Trade Practices Law Journal* 139, 149, citing an interview by Sharpe with Sitesh Bhojani (22 May 2006).

[421] (2003) 19(2) *Trade Practices Law Bulletin* 21.

[422] Ibid, 23.

7. *TRADE PRACTICES ACT 1974 (CTH)* S 51AC RELEVANT CASES AND FUTURE DEVELOPMENTS AS A RESULT OF THE 2008 SENATE REPORT

7.1 EARLY ACCC ACTION UNDER S 51AC - *AUSTRALIAN COMPETITION AND CONSUMER COMMISSION V SIMPLY NO-KNEAD (FRANCHISING) PTY LTD*

The Federal Court case *Australian Competition and Consumer Commission v Simply No-Knead (Franchising) Pty Ltd*[423] was the first s 51AC case to be decided by a court. The case was heard post the decision in *Berbatis* at first instance by French J in the Federal Court, but prior to that decision being reversed by the Full Federal Court. Simply No-Knead (Franchising) Pty Ltd ('SNK') conducted a franchise business providing to its franchisees bread making training and ingredients for making bread at home.

SNK had commenced proceedings in State Courts against four of its franchisees for alleged breach of their franchise agreements, aimed to prevent the franchisees from carrying on similar bread making businesses. The franchisees counterclaimed, alleging that SNK had itself breached the franchise agreements and had misled them in order to induce them to enter the franchise agreements. The Australian Competition and Consumer Commission sought through the Federal Court an interlocutory injunction to restrain the continuance of SNK's State Court proceedings, in order that the matters could be brought before a more appropriate forum for the Commission to contest the cases, the Federal Court.[424] The Commission alleged conduct by SNK that breached the unconscionability small business provisions of s 51AC as well as breaching of a mandatory industry code (the Franchising Code of Conduct) under s 51AD. SNK applied for a stay in the Federal Court proceeding on the ground that it was vexatious or oppressive.

[423] (2000) 104 FCR 253.

[424] The Federal Court was seen as the more appropriate forum as the Australian Competition and Consumer Commission usually commenced proceedings in the Federal Court and if it were left to the State Courts, differing interpretations of s 51AC might result.

Sundberg J of the Federal Court had to determine whether to grant the interlocutory injunction sought by the Australian Competition and Consumer Commission or the stay of the Federal Court proceedings sought by SNK.

It was alleged by the Commission that SNK had breached the unconscionable conduct provisions of s 51AC(1) on a number of grounds.

One of the breaches alleged was SNK's refusal to deliver franchised products to the franchisees. Here Sundberg J made particular reference to the one of the factors listed in 51AC(3) that may be used to guide the court to determine if unconscionable conduct has occurred, s 51AC(3)(d). That subsection deals with undue influence or pressure, or any unfair tactics in relation to the supply of goods. Sundberg J stated 'The refusal to supply was the exertion of pressure on, and the use of unfair tactics against, the franchisees within factor (d) in s 51AC(3).'[425]

A further breach alleged was SNK's deletion of three of the franchisees' telephone numbers from Telstra's 013 Telephone Directory Assistance Service without the consent or the knowledge of the franchisees.

Unreasonably refusing requests from the franchisees to negotiate matters in dispute with SNK and to discuss matters of concern were also alleged as actions by SNK that had breached the unconscionable conduct provisions.

In addition, further breaches were alleged by SNK's producing and distributing advertising and promotional material which omitted the names of the franchisees and their franchised businesses; SNK selling and offering to sell its products in the territories of the franchisees and in areas proximate to their territories. Sundberg J stated that this behaviour '…demonstrated a lack of good faith on the part of SNK within factor (k) [in s 51AC(3)].'[426]

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[425] Ibid, 268 [40].

[426] Ibid, 269 [46].

Lastly, SNK's refusal to provide current disclosure documents to some of the franchisees in response to written requests was also alleged as being a contravention of s 51AD.[427]

Sundberg J referred to French J from *Berbatis* in support that the court was not limited to a narrow interpretation of s 51AC by the cases of equitable or unwritten law which were the subject of s 51AA:

> *Australian Competition and Consumer Commission v Berbatis Holdings Pty Ltd* (2000) 169 ALR 324 concerned s 51AA. French J examined at length the ambit of the unwritten law of unconscionability: at 330–5. At 335 his Honour said there was no reason to suppose that the unconscionable conduct prohibited by ss 51AB and 51AC is limited by reference to "specific equitable doctrines", and pointed out that the factors to which the court is required to have regard for the purpose of determining whether there has been a contravention, "include undue influence and duress and other issues falling outside the equitable doctrines to which reference has been made". [428]

Sundberg J saw the relevance of the s 51AC(3) factors that a court may have regard to in determining whether conduct has breached s 51AC, as being:

> The principal pointer to an enlarged notion of unconscionability in s 51AC lies in the factors to which subs (3) permits the court to have regard. Some of them describe conduct that goes beyond what would constitute unconscionability in equity.[429]

Sundberg J clarified that the court was 'aided but not controlled by the factors listed in subs (3).'[430]

After reviewing SNK's behaviour, Sundberg J concluded that it disclosed 'an overwhelming case of unreasonable, unfair, bullying and thuggish behaviour in relation to each franchisee that amounts to unconscionable conduct by SNK for the purposes of s 51AC(1).'[431] In addition, the failure to have

[427] Ibid, 255 [3].

[428] Ibid, 265 [33].

[429] Ibid, 265 [31]

[430] Ibid, 267 [37].

[431] Ibid, 270 [51].

provided current disclosure documents to the franchisees was a contravention of s 51AD.[432] Sundberg J granted the interlocutory relief sought by the Australian Competition and Consumer Commission and refused SNK's application to stay the Commission's proceedings against it.

Michelle Sharpe and Associate Professor Christine Parker summarised the important impact of this case as follows:

> The *Simply No-Knead* case was also successful in highlighting the existence of the unconscionability provisions and in changing business practices. The ACCC officer noted that the case was "well publicised and it shook up the businesses and practitioners". Another ACCC officer noted that "[s]hortly after the judgment came down, the Franchising Council had a meeting that discussed it". A number of law firms issued circulars to their clients advising them to "take careful note" of the case. The case also attracted a good deal of media and academic attention.[433]

The Australian Competition and Consumer Commission appears to have made a greater impact in changing the business culture of franchising than it did in retail leasing.[434]

A number of important factors can be drawn from this Federal Court decision. The first is that support was given to French J's decision in *Berbatis* that a wider application should be given to s 51AC and that the courts should not be limited to a narrow interpretation of unconscionable conduct.

Another important factor is that Sundberg J used the factors listed in s 51AC(3) that a court may have regard to in order to determine if unconscionable conduct has occurred, to assist in this wider application of unconscionable conduct.

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[432] Ibid, 271 [52].

[433] Michelle Sharpe and Christine Parker, 'A Bang or a Whimper? The Impact of ACCC Unconscionable Conduct Enforcement' (2007) 15 *Trade Practices Law Journal* 139, 151.

[434] Ibid. Sharpe and Parker suggest that the Commission may have been more successful in changing the franchising industry behaviour as a result of its administration of the mandatory Franchising Code of Conduct than through its enforcement litigation.

A further important factor is that this Federal Court decision demonstrated that s 51AC could be used successfully against a combination of ‘sharp’ business practices, from refusal to supply goods, to exclusion from advertising, and refusal to negotiate matters in dispute.

7.2 *TRADE PRACTICES ACT 1974* (CTH) AND STANDBY LETTERS OF CREDIT - *SCAFFOLDING PTY LTD V ACTION MAKERS LTD (IN ADMINISTRATIVE RECEIVERSHIP)*

The *Boral Formwork & Scaffolding Pty Ltd v Action Makers Ltd (in Administrative Receivership)*[435] (*Boral*) case is interesting in that it extended the scenarios where parties may seek relief under the *Trade Practices Act 1974* (Cth) unconscionability provisions for financial matters, to standby letter of credit (L/C) scenarios. Given the reliance of businesses on the ability to make claims on standby L/Cs with absolute assurance that the claims will be paid by banks in terms of the L/C conditions, this use of the *Trade Practices Act 1974* (Cth) unconscionability provisions deserves examination in this thesis. *Boral* was heard shortly after the High Court decision in *Berbatis* and is referred to.

Boral Formwork & Scaffolding Pty Ltd ('Boral Formwork') sought to first stop the beneficiary of a L/C, the Administrators appointed to Action Makers Ltd, from making further claims under the L/C. Secondly Boral Formwork sought to stop the bank that provided the L/C from paying out further claims received under the L/C.

The L/C was in place to ensure payment for goods ordered by Boral Formwork from Action Makers Ltd, in the event Boral Formwork defaulted upon payment. The first lot of goods (scaffolding components) delivered to Boral Formwork was, however, faulty, and Boral Formwork advised the Administrator to Action Makers Ltd (the Administrator) on 21 February 2003 that Boral Formwork would like to rectify the faults and deduct the costs of the rectifications ($24,057.93) from the amount owing to the Administrator. Boral Formwork followed up on 11 March 2003 with a subsequent advice to the Administrator, in which Boral Formwork advised that the rectification work on the initial shipment had nearly been completed, and that more rectification work was likely to be required on the remaining goods.

[435] (2003) ATPR 41-953.

The Administrator did not respond to any of Boral Formworks advices and on 5 June 2003 issued an invoice for the full amount outstanding (without any deduction for the repair costs) and advised Boral Formwork that unless full payment was made, a claim would be made under the L/C. On the same day (5 June 2003), the Administrator claimed under the L/C for an amount equal to the value of the goods already supplied (which was greater than the amount in dispute) and provided a certificate to the bank in terms of the L/C, which stated that a demand had been made on Boral Formwork and that the demand had not been satisfied. The bank paid out under the claim.

Boral Formwork unsuccessfully attempted to negotiate with the Administrator the settlement of the matter, including a request for an undertaking that rights under the L/C would not be exercised. The negotiations were not successful and so Boral Formwork sought injunctive and final relief from the Supreme Court of New South Wales, to prohibit the bank from paying out any further claims under the L/C, as well as prohibiting the Administrator from making further claims under the L/C.

Boral Formwork argued in its injunctive relief application that the Administrator's actions of claiming under the L/C constituted unconscionable conduct under ss 51AA and 51AC of the *Trade Practices Act 1974* (Cth). An argument was made in the alternative that there was an implied negative stipulation in the supply agreement, which prevented the Administrator from making a claim under the L/C when there was a dispute – this argument failed.

Austin J was prepared to interpret unconscionable conduct in s 51AC in a wider sense than just the narrow interpretation in s 51AA. His Honour stated: '…the word "unconscionable" in s 51AC is not limited to conduct that would be unconscionable according to equitable principles.'[436]

[436] Ibid, 47,493–47,494 [91].

Austin J found that the Administrator's actions in demanding payment under the L/C from the bank was seen as being in close connection with the supply of goods under the commercial contract, and thus s 51AC covering unconscionability in regard to the supply of goods could apply. Austin J also decided that, on the facts, it was unconscionable (in terms of s 51AC) that the Administrator's certification to the Bank – that the claim was an amount due to be paid – was false, as the amount was under dispute, and also that there had been insufficient time between the Administrator demanding payment from Boral Formwork and certifying that the amount had been unpaid, as these events occurred on the same day.

Austin J determined that Boral Formwork was entitled to various orders. Declaratory orders were made under s 51AC that the Administrator's actions in making the demands under the L/C were unconscionable. Final orders were made requiring the Administrator to countermand the demand for payment already made for the disputed amount under the L/C. In addition, orders were made restraining the Administrator from making any further demands under the L/C.[437]

Boral Formwork subsequently agreed that no injunction was required to be taken out against the bank, due to the above orders having been made against the Administrator.[438]

Austin J also stated that relief for the same reasons as relief being granted under s 51AC would have been possible under s 51AA(1) (and despite Boral Formwork not having been under any special disadvantage), except that s 51AA(2) provided that such relief was not possible for conduct prohibited by either ss 51AB or 51AC. His Honour had distinguished the High Court decision in *Berbatis* as being limited to its facts and having been run as a 'special disadvantage case' by the Australian Competition and Consumer

[437] Ibid, 47,494 [91].

[438] Ibid, 47,494 [92].

Commission.[439] Austin J's decision in regard to the interpretation of s 51AA has not been followed.

Austin J distinguished the special facts in the *Boral* case as providing an exception to distinguish that relief should be granted preventing the Administrator's use of the L/C. Austin J held that this decision did not impact on the principle that unconditional undertakings contained in L/Cs issued by banks should remain autonomous from the commercial contract set up between the supplier and purchaser. Austin J stated:

> I hope it is clear that, in deciding to grant the relief sought by Boral, I have given anxious consideration to the principle of autonomy and the dangers associated with any judicial intervention with the performance of unconditional commercial obligations. … Even if the conduct is unconscionable, the principle of autonomy is relevant to the exercise of the Court's discretion to grant injunctive relief or leave the plaintiff to other remedies. Here the circumstances, involving as they do a call on the letter of credit on a false basis, are sufficiently special to overcome the hesitation which the principle of autonomy generates.[440]

Regardless of Austin J's above hope, however, the decision to some degree lessens the degree of reliance that parties can place on standby L/Cs. In addition it encourages future beneficiaries relying upon standby L/Cs to insist that the applicant opens the L/C on the basis that wordings contained within the L/Cs covering the conditions under which drawings can be made, state the minimum constraints possible, such as reciting that *payment will be made by the bank upon written demand being made by the beneficiary upon the bank*.

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[439] See the Editorial Comment in the reporting of this case at (2003) ATPR ¶41-915, 47,479. Reference is made to *Australian Competition and Consumer Commission v CG Berbatis (Holdings) Pty Ltd* (2003) 214 CLR 51 and the comments of Gleeson CJ at 64 [11], Gummow and Hayne JJ at 71 [39] and 74 [46] and Callinan J at 98 [184]. Austin J saw that (at 47,492 [76]):

> *Berbatis* was in terms limited to its facts, and by the way in which the hearings had been conducted in the courts below and in the High Court – the case was run as a "special disadvantage" case (at para [5] per Gleeson CJ; para [45]-para [46] per Gummow and Hayne JJ; para [77] per Kirby J; and para [160]-para [161] per Callinan J).

[440] *Boral Formwork & Scaffolding Pty Ltd v Action Makers Ltd (in Administrative Receivership)* (2003) ATPR 41-953, 47,493 [90].

Two noteworthy aspects relevant to statutory unconscionability can be drawn from Austin J's decision. The first is the expansion of the s 51AC unconscionability provisions into the area of L/Cs provides evidence of the broadening applications to which the section may be applied to seek relief, that financial institutions in Australia need to consider.

The second noteworthy aspect is that Austin J's decision that he would have granted relief under s 51AA despite the absence of a special disadvantage (and seeking to limit the High Court decision in *Berbatis* to its facts), has not been followed.

7.3 *TRADE PRACTICES ACT 1974* (CTH) S 51AC EQUIVALENT SECTION IN THE *ASIC ACT* EXAMINED BY THE FULL FEDERAL COURT

The decision of the Full Federal Court in *Australian Securities and Investments Commission v National Exchange Pty Ltd*[441] is an example of a finding of unconscionable conduct having been engaged in for provision of financial services, by applying the mirrored provision to s 51AC of the *Trade Practices Act 1974* (Cth) in the *Australian Securities and Investments Commission Act 2001* (Cth), s 12CC. There is no reason why the rationale applied by the Full Federal Court cannot be applied equally to s 51AC.[442]

National Exchange Pty Ltd had made unsolicited offers to shareholders in companies which were the subject of continual takeover activity or other corporate change. The offers to purchase the shareholdings were significantly below market value. ASIC alleged that the company had engaged in unconscionable conduct[443] in regard to an offer made to purchase shares in a demutualised company, Aevum Ltd. ASIC were unsuccessful at first instance before Emmett J in the Federal Court[444] in establishing that National Exchange Pty Ltd's conduct was unconscionable under s 12CC. ASIC appealed the decision to the Full Federal Court.[445]

Although the appeal was unsuccessful as the transactions did not meet the prerequisite of having been in trade or commerce, the conduct of National

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[441] (2005) 148 FCR 132.

[442] Ibid, 140 [30]. Tamberlin, Finn and Conti JJ refer to [3.7] of the Explanatory Memorandum to the *Financial Services Reform (Consequential Provisions) Bill 2001* (Cth), which concerned the proposed s 12CC of the *ASIC Act*, as evidence that this section was intended to operate as a mirror provision to s 51AC of the *Trade Practices Act 1974* (Cth); see also *Debates*, vol 216, at 8,767 (Ministerial Statements) and 8,800 (Second Reading Speech).

[443] As well as being misleading and deceptive and breaching the *Corporations Act 2001* (Cth) requirements against making unsolicited offers.

[444] *Aevum Ltd v National Exchange Pty Ltd* (2004) 142 FCR 316.

[445] As well as claiming that Emmett J had made an error in not finding that National Exchange Pty Ltd had engaged in unconscionable conduct, ASIC also claimed that Emmett J had made two other substantial errors: in failing to find that National Exchange Pty Ltd made any misleading statements in relation to the offers; and in failing to find that the acceptance of the offers by the shareholders was for the purpose of trade or commerce.

Exchange Pty Ltd was established by the Full Federal Court (Tamberlin, Finn and Conti JJ) as having been unconscionable. In rejecting Emmett J's limitation of interpreting s 51AC in narrow terms of the 'unwritten law', Tamberlin, Finn and Conti JJ cite French J from the initial Federal Court hearing of *Berbatis*[446] as well as Mansfield J from *Australian Competition and Consumer Commission v Keshow*[447] as authority that:

> s 51AC supports the proposition that the prohibition in s 12CC is not to be read down by limiting its operation only to circumstances where the common law would grant relief in respect of unconscionable conduct…[448]

Tamberlin, Finn and Conti JJ recognised a need for a wider interpretation of s 51AC, as the wording of the section 'must be given its ordinary meaning and must not be qualified by pre-existing constraints on liability ...'[449] and was 'intended to build on and not to be constrained by common law case law …'.[450]

The methodology that the Full Federal Court applied was to consider and weigh as a whole the factors listed in s 12CC(2) of the *Australian Securities and Investments Commission Act 2001* (Cth) (mirroring the factors listed in s 51C(3) to the facts of the case).[451] The Full Federal Court reasoned that there were several factors that clearly applied in this case to support a characterisation of the conduct as unconscionable.[452]

The first factor supporting the conduct as being unconscionable was the doubt as to whether the recipients who accepted the offers to purchase their shares were able to understand the offer document.[453]

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[446] *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd* (2000) 96 FCR 491, [22].

[447] [2005] ATPR (Digest) 46-265, [97].

[448] (2005) 148 FCR 132, 140 [30].

[449] Ibid.

[450] Ibid.

[451] Ibid, 142 [40].

[452] Ibid.

[453] Ibid.

Another factor supporting the conduct as being unconscionable was the amount and circumstances under which the recipient could have acquired an equivalent offer. The Full Court noted that there was no equivalent offer and that there was no room for negotiation between the parties. The shares came on the market shortly after the offer closed and sold for 440% of the price offered by National Exchange Pty Ltd.[454]

The final factor supporting the conduct as being unconscionable was that the transaction was not undertaken in good faith.[455] Tamberlin, Finn and Conti JJ commented that the offeror had:

> …set out to systematically implement a strategy to take advantage of the fact that amongst the official members there would be a group of inexperienced persons who would act irrationally from a purely commercial viewpoint and would accept the offer. They were perceived to be vulnerable targets and ripe for exploitation … This is not a case of obtaining a low price by shrewd negotiation. It is predatory conduct designed to take advantage of inexperienced offerees.[456]

After having applied the relevant s 12CC(2) factors, Tamberlin, Finn and Conti JJ observed that s 12CC required the Court 'to focus primarily on the unconscionable conduct of the offeror and to determine whether that conduct is contrary to the norm of conscientious behaviour.'[457] The Court found that the conduct of National Exchange had clearly offended against basic notions of good conscience and fair play and had engaged in unconscionable conduct.[458]

So what relevance for future claims under s 12AC *Australian Securities and Investments Commission Act 2001* (Cth) or s 51AC *Trade Practices Act 1974* (Cth) can be taken from the Full Federal Court decision in *Australian*

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[454] Ibid, 142 [41].

[455] Ibid, 142 [42].

[456] Ibid, 142 [43].

[457] Ibid, 143 [44].

[458] Ibid.

Securities and Investments Commission v National Exchange Pty Ltd? The first observation is that despite Tamberlin, Finn and Conti JJ being prepared to move beyond the limitations of the 'unwritten law' and to apply the factors that a court may consider that are listed in the sections, since this case was decided in 2005 there have not been a significant number of successful cases brought under the sections.

The other relevant matter for financiers dealing with small businesses to consider is the choice of factors that a court may consider listed in s 12 AC and s 51AC, that the Full Federal Court found applied to the behaviour of National Exchange. These factors are pertinent for financiers to consider in their dealings with borrowers and security providers.

The first factor pertinent for financiers to consider is whether borrowers and security providers are able to understand the loan and security documentation – most major financiers use plain English standardised documentation for lending to small businesses plus recommend to third party security providers that independent legal advice be obtained.

The second factor pertinent for financiers to consider is the amount and circumstances under which the recipient could have acquired an equivalent offer. An example of where this factor would need to be considered by a financier is where a small business borrower who is in financial difficulty, seeks additional finance from his or her financier. The client is likely unable to be able to obtain finance elsewhere. The existing financier may make the risk decision that it is better to provide additional modest funding levels in the hope that the client can trade out of their difficulties and thus eventually repay their existing borrowings. If the financier's terms for the additional finance are overly harsh or oppressive, or priced at too high a premium, then this exploitation as a result of a client being unable to acquire an equivalent offer may be indicative of unconscionable conduct.

The third and final factor pertinent for financiers to consider is the extent to which the financier's conduct was not undertaken in good faith. Financiers could breach the good faith requirement in any scenario where, like National Exchange, they take advantage of a vulnerable person (including any disadvantaged or inexperienced person) who acts irrationally from a purely commercial viewpoint and transact with the financier. For example, if a financier takes security from a vulnerable third party in order to improve the security position on an existing exposure the financier has to a debtor in financial distress, without first ensuring that the security provider understands their liability and is aware of the precarious financial position of the debtor.

7.4 *TRADE PRACTICES ACT 1974* (CTH) S 51AC SUCCESSFUL ACTION AGAINST AN UNSCRUPULOUS FINANCIER

The 2006 Federal Court case of *Coggin v Telstar Finance Company (Q) Pty Ltd*[459] is an example of a successful application by a security provider for a loan, for relief under the small business unconscionability provisions of s 51AC.

Mr Coggin was retired and aged in his late sixties in 1999 when the following transaction took place. He was asked to help his son-in-law (and thus from Mr Coggin's viewpoint, more importantly, indirectly assist his daughter) by providing a fishing boat he owned as security for a $65,000 loan that was to be taken out in Mr Coggin's own name. The loan funds were to assist the son-in-law with the acquisition of a franchise, 'Easy Drink' (involved in the distribution of plastic lids that fit over drink cans). The franchise was to be purchased in Mr Coggin's name, but was to be operated by his son-in-law. A fringe financier from Queensland, Telstar Finance Company (Q) Pty Ltd ('Telstar'), had agreed to provide finance, but with a number of unusual aspects applying.

The first unusual aspect was the interest rate, which was 10% per month.

Another unusual aspect was that rather than taking a ship's mortgage or a similar form of charge over the boat, Telstar required Mr Coggin to enter a contract of sale over the boat for $35,000, with a 'right to buy back' clause in the contract – the reasons for this was advised as being due to a problem with obtaining insurance for the boat at a level that was satisfactory to Telstar (note the boat was estimated at that time to be worth $210,000).

The final unusual aspect was that Telstar's employee entered into a secret agreement with 'Easy Drink', that he would receive three cents for every

[459] (2006) ATPR 42-107.

plastic lid the son-in-law was able to sell plus 10% of the value of any sub-distributorships sold in Victoria (all this being unbeknown to Mr Coggin).

The business venture was not successful and the loan fell into default. Telstar entered into possession of the boat and sold it for $95,000. Telstar retained the total sales proceeds which included a surplus above the loan amount. Mr Coggin then brought an action before Heerey J of the Federal Court seeking orders for:

- the transaction to be set aside as unconscionable under s 51AC; and
- recovery of the loss suffered from the sale of the boat and damages under s 82.

Heerey J referred to *Hurley v McDonald's Australia Ltd*[460] to determine how the Full Federal Court had interpreted unconscionability under s 51AC:

> For conduct to be regarded as unconscionable, serious misconduct or something **clearly unfair or unreasonable**, must be demonstrated — *Cameron v Qantas Airways Ltd* (1994) 55 FCR 147 at 179. Whatever "unconscionable" means in sections 51AB and 51AC, the term carries the meaning given by the Shorter Oxford English Dictionary, namely, actions *showing* **no regard for conscience, or that are irreconcilable with what is right or reasonable** — *Qantas Airways Ltd v Cameron* (1996) 66 FCR 246 at 262. The various synonyms used in relation to the term "unconscionable" import a **pejorative moral judgment** — *Qantas Airways Ltd v Cameron* (1996) 66 FCR 246 at 283–4 and 298.[461]

With that interpretation in mind, Heerey J examined Telstar's conduct to see if any serious misconduct or something clearly unfair or unreasonable was evident. Heerey J recognised that the driving forces behind the project for the purchase of the Easy Drink franchise were the son-in-law, his friend Mr Pavia, and Telstar's representative, Mr Cunningham. Heerey J explained Mr Coggin's position aptly, with assistance from biblical quotes, when he stated:

> Like the certain man who went down from Jerusalem to Jericho (Luke 10.25–30), Mr Coggin fell among men who were, if not thieves in the legal sense, totally opportunistic in the advantage they took of him. To

[460] (2000) ATPR 41-741, 40,585 [22].

[461] (2006) ATPR 42-107, 44,904 [58].The original emphasis is included.

> their knowledge, Mr Coggin not only happened to be the owner of an asset which could provide collateral to get finance which seemed otherwise unobtainable, he had filial motives for assisting his daughter and her family.[462]

Heerey J then went on to itemise the other key aspects of the case that attracted the unconscionability provisions of s 51AC. A key aspect was the overwhelming weighting of the transaction against any rational assessment of what was in Mr Coggin's interests, that is, having provided security of $200,000 for a loan of $65,000.[463] Another key aspect was the fact that Telstar had taken secret profits from the Victorian Easy Drink franchise, which Heerey J had commented appeared far removed from the operations of a Brisbane based finance company.[464] The final key aspect was that Telstar had changed the security from being a mortgage to a sale of the boat, which had enabled Telstar to retain the funds in excess of the loan amount when the boat was sold (as opposed to having to account to the mortgagor for surplus funds when a mortgagee sale was conducted) – and without any independent legal or business advice having been provided to Mr Coggin.[465]

Given the above factors, Heerey J found that unconscionable conduct was established under s 51AC, and Telstar were ordered to pay Mr Coggin the proceeds of the boat sale ($95,000) plus interest and costs (Mr Coggin failed in his attempts to get the court to agree on the boat's value of $210,000 that he saw as the value at the time the transaction was entered into, as opposed to the price that Telstar were able to achieve when they sold the boat after widely advertising it – $95,000). No examination was made as to whether any of the numerous factors listed in s 51AC(3) that a court may consider (but is not bound to consider) in order to establish unconscionability had been evident in the facts of this case.

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[462] Ibid, 44,904 [63].

[463] Ibid, 44,904-44,905 [65].

[464] Ibid, 44,905 [66].

[465] Ibid, 44,905 [67].

An aspect Heerey J dismissed as being outside the matters that the court should consider as indicating unconscionability, was the effect of a spider bite Mr Coggin sustained earlier in the month prior to entering into the transaction. The bite had been quite serious, Mr Coggin advised, and had caused his leg to swell, tremors and hallucinations to occur and the lapsing into a coma for three days. Mr Coggin advised that the after-effects of the spider bite were that he felt constant pain, was 'dull-minded' and not 'with it' when he entered into the transaction.[466] Heerey J saw that this was a relatively minor feature in the circumstances and that 'It would be simplistic to regard this case as one which merely adds spider bites to the classic equitable disability categories of drunkenness, illiteracy etc.'[467]

Heerey J clearly had enough 'traditional' elements established that justified a finding of unconscionability, without having to resort to a widening of the established factors that could be considered. Arguably, under another set of circumstances where all the other indicators of unconscionability that were in this case were not present, the ill-effects of the spider bite may have been a factor to consider as relevant by the court in establishing unconscionability, if the stronger party were aware of such a debilitating factor. This is a relevant question to ask, given that the effects of the spider bite which caused Mr Coggin to be 'dull-minded' would have some similarities with the effects of drunkenness in the case of *Blomley v Ryan* (and one might ask from a moral viewpoint, which perhaps is relevant given we have just dealt with a case applying biblical quotations, whether the court should not view the effects from an unintentional disability of suffering the spider bite, as opposed to a self-inflicted disability of being inebriated, as more deserving of recognition as a disability category for unconscionability).

Clearly financiers need to be aware of the willingness of courts to award relief for unconscionability under s 51AC, but given the extreme behaviour taken by this fringe financier, there is probably little that the banks can take

[466] Ibid, 44,897 [16].

[467] Ibid, 44,904 [64].

heed of from this decision. Banks do not usually enter secret negotiations with the end recipients of loan funds in order to obtain secret profits, nor retain surplus values above debt amounts when security is sold, nor charge 10% monthly interest, nor normally lend to retired persons in their late sixties where there is no benefit to them from the transaction (or if they do, they do not normally do so without the benefit of independent financial or legal advice being received).

The case demonstrates that it is usually only extreme behaviour that attracts a finding of unconscionable conduct.

7.5 THE DECEMBER 2008 SENATE REPORT INTO UNCONSCIONABLE CONDUCT UNDER PART IVA AND THE RESULTANT CHANGES

On 16 of September 2008 the South Australian Senator Nick Xenophon moved a second reading amendment to the *Trade Practices Legislation Amendment Bill 2008* (Cth). The Bill provided for the removal of the $10 million limit for the maximum value of goods or services to which s 51AC applied.[468] Senator Xenophon's amendment also provided 'for an inquiry on the need to develop a clear statutory definition of unconscionable conduct and the scope and content of such a definition', citing the comments of Associate Professor Frank Zumbo:

> ...unless you change the substantive meaning or the substantive flaws in 51AC as they currently exist - that is, a lack of definition of unconscionable conduct in the section itself - removing the cap will not be of any practical assistance.[469]

The result was the Senate Standing Committee on Economics inquiry which reported in December 2008 on unconscionable conduct under Part IVA of the *Trade Practices Act 1974* (Cth) and recognised the limitations of s 51AC.[470] The report stated:

> The committee is in no doubt that section 51AC of the *Trade Practices Act* has fallen short of its legislative intent. The law as it currently operates only addresses unconscionable conduct in the process of contracting (51AA), but not - save for few exceptional cases - in the substantive bargain struck (51AC). The regulator and the courts have not pursued the crucial test cases which would extend the judicial interpretation of section 51AC beyond the equitable concept established in section 51AA. A very poor record of prosecutions reflects a lack of clarity and guidance in section 51AC as to what constitutes "unconscionable conduct". In consequence, many smaller businesses with well-grounded allegations of unethical and unconscionable conduct against large businesses have been denied proper access to the judicial process.[471]

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[468] The Bill was passed into law, and on 21 November 2008 the $10 million limit was removed.

[469] Senator Nick Xenophon, Senate Hansard, 16 September 2008, at 4,791.

[470] Senate Standing Committee on Economics, *The Need, Scope and Content of a Definition of Unconscionable Conduct for the Purposes of Part IVA of the Trade Practices Act 1974*, December 2008.

[471] Ibid, 43.

The Coalition senators and Senator Xenophon recommended the following definition of unconscionable conduct – proposed by Associate Professor Frank Zumbo – be inserted into s 51AC (with a similar definition in 51AB):

> For the purposes of this section "unconscionable conduct" includes any action in relation to a contract or to the terms of a contract that is unfair, unreasonable, harsh or oppressive, or is contrary to the concepts of fair dealing, fair-trading, fair play, good faith and good conscience.[472]

The Coalition senators and Senator Nick Xenophon believed that the inclusion of this definition would make it clear to the courts that unconscionable conduct would be interpreted in a manner that prohibits unethical conduct in general, whilst at the same time allowing pre-existing common law and equitable principles for unconscionable conduct to also apply, provided that they are not inconsistent with the definition.[473]

Although the Committee saw merit in introducing a definition of unconscionable conduct into s 51AC, they did not believe that it was the right forum to recommend such a change, as it would require a 'coordinated institutional dialogue and an action plan to ensure that the different statutory regimes are in sync with the amended *TPA* …'[474]

To assist with providing clarity to s 51AC the Committee did however make recommendations to insert examples and statements of principle into s 51AC.

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[472] Ibid, 45–47, with reference to the definition provided in the Submission by Associate Professor Frank Zumbo, Submission 11, October 2008, 12.

[473] Ibid, 46–47.

[474] Ibid, 34–35, with reference made to Professor Bryan Horrigan, Submission 15, at 10. The Committee's other reservations to recommending the adoption of a definition, were as follows:

First, that the terms used in the definition would themselves need to be carefully considered for their judicial meaning. Secondly, providing a definition was not necessarily the priority of the Committee (in terms of the amount of time that would need to be spend in legally defining the terms used within the definition and then consulting with interested parties), and that there were 'lower-hanging fruit' that could be more readily inserted in the Act and which would be more effective (that is, the inclusion of examples and clarifying that s 51AC applies both to the terms of the contract and the ongoing operation of the contract).

In its deliberations as to whether principles and examples should be included in s 51AC, the Committee referred to the comments in Professor Bryan Horrigan's submission: 'The unconscionable conduct general law steps in at the extremes. It does not step in at the middle.'[475] As a result the Australian Competition and Consumer Commission have not pursued many s 51AC breach allegations where the conduct was not extreme.[476] To assist with providing clarity to s 51AC the Committee therefore made recommendations to insert examples and statements of principle into s 51AC.

The inclusion of examples was seen as addressing the challenge for courts in determining at what point hard bargaining becomes unethical behaviour under s 51AC. For the inclusion of examples, the Committee recommended that the Government engage with various industry participants so as to produce a list of clear examples of what constitutes 'unconscionable conduct' for incorporation into the section.[477]

The Committee summarised how the examples would work:

> Inserting a statutory list of examples of the types of conduct ordinarily considered unconscionable into section 51AC may provide practical statutory guidance for the courts. They are all pitched in terms of what the supplier did or did not do, which clearly directs the courts to the behaviour that the section is trying to remedy. They would also provide guidance for small businesses in deciding whether to take action against the larger party and how to frame their arguments for the court.[478]

For the second recommendation of the Committee, the addition of a statement of principles into the section, the principles '… would fall somewhere between a list of examples and a broad overarching definition of "unconscionable conduct".'[479] The statement of principles differed to the factors presently listed that a court may consider under s 51AC(3), as the

[475] Ibid, 36, with the report making reference to Professor Bryan Horrigan, *Proof Committee Hansard,* 3 November 2008, 22.

[476] Ibid, 36.

[477] Ibid, 38–39.

[478] Ibid, 36–37.

[479] Ibid, 38.

principles would be a list of factors that the courts must consider.[480] An example was provided as to how the principles would operate. If there was a principle that terms of a contract should not unduly advantage the larger party as a result of the difference in bargaining power, '… then the court must find that unconscionable conduct has taken place or give reasons why this ruling should not be made.' [481]

As well as adding clarity, the Senate Standing Committee expected that both the statement of principles and the examples would also act as a deterrent to larger businesses in a way that s 51AC(3) does not.[482] In addition, the Committee supported that s 51AC be amended to specify that it applied to the actual operation of a contract ('substantive unconscionability') and not just its formation ('procedural unconscionability').[483] This would hopefully address the existing reluctance to date for relief to be sought under s 51AC for substantive unconscionability.

On 5 November 2009 the Federal Minister for Competition Policy and Consumer Affairs, the Hon Dr Craig Emerson MP, announced that, having considered the Senate Standing Committee's Report, amendments to the *Trade Practices Act 1974* (Cth) would be made to make it clear that protection from unconscionable conduct relates '… not only to the process of settling a contract but to the terms and conditions of the contract and the ongoing behaviour of the parties to the contract.'[484] In addition, the question

[480] Ibid.

[481] Ibid.

[482] Ibid.

[483] Ibid, 35–36. The Senate Standing Committee's support to this amendment is subject to a response supporting such a change being received by the parliamentary Joint Committee on Corporations and Financial Services inquiry into the Franchising Code of Conduct, which investigated this issue. Section 22(2)(j) *Trade Practices Amendment (Australian Consumer Law) Act (No. 2) 2010* (Cth), amending the equivalent to s 51AC, now contains this amendment.

[484] The Hon Dr Craig Emerson MP, Federal Minister for Competition Policy and Consumer Affairs, 'Government to Strengthen Franchising Code of Conduct and Unconscionable Conduct Law' (Media Release, 5 November 2009). The proposed amendments to the *Trade Practices Act 1974* (Cth) are also planned to strengthen the Franchising Code of Conduct as part of the Government's response to the Parliamentary Joint Committee on Corporations and Financial Services inquiry into Franchising.

as to whether a list of examples of unconscionable conduct or a statement of principles of what constitutes unconscionable conduct should be incorporated into the Act, would be considered by an Expert Panel.[485] Following the receipt of submissions from interested parties,[486] the Expert Panel reported to the Government in February 2010.[487]

The Terms of Reference for the Expert Panel were published,[488] in addition to Treasury releasing an Issues Paper to assist the considerations of the Expert Panel.[489] Although the Senate Report only dealt with changes to s 51AC, [490] the Government widened the scope of the potential changes to the whole of Part IVA of the Act[491] (ie initially the proposal for examples or statement of principles as to what constitutes unconscionable conduct were only to be introduced into s 51AC). The application of examples or principles to Part IVA as opposed to only s 51AC is a practical approach, to avoid

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[485] Ibid. The appointees to the Expert Panel were Professor Bryan Horrigan, Mr David Lieberman and Mr Ray Steinwall – see The Hon Dr Craig Emerson MP, Federal Minister for Competition Policy and Consumer Affairs, 'Government Appoints Expert Panel on Franchising and Unconscionable Conduct' (Media Release, 27 November 2009).

[486] 'That expert panel will engage in consultation with the Australian Competition and Consumer Commission (ACCC), retail tenancy and franchising industries, and small business organisations, as well as any other interested parties, in considering the need for a list of examples or statement of principles for Part IVA.' Treasury, Australian Government, 'Commonwealth Government Response to the Senate Standing Committee on Economics Report on the Need, Scope and Content of a Definition of Unconscionable Conduct for the Purposes of Part IVA of the *Trade Practices Act 1974*' (5 November 2009), 8.

[487] Treasury and Department of Innovation, Industry, Science and Research, 'Strengthening Statutory Unconscionable Conduct and the Franchising Code of Conduct', report to the Minister for Small Business, Independent Contractors and the Service Economy and the Minister for Competition Policy and Consumer Affairs (February 2010).

[488] Minister for Competition Policy and Consumer Affairs' 'Expert Panel to Advise on Strengthening the Franchising Code Of Conduct and the Unconscionable Conduct Provisions of the *Trade Practices Act 1974*' (Terms of Reference, 27 November 2009).

[489] Treasury, Australian Government, 'The Nature and Application of Unconscionable Conduct Regulation – Can Statutory Unconscionable Conduct be Further Clarified in Practice?' (Issues Paper, November 2009).

[490] 'The committee's preferred option is to target those areas of section 51AC that could clarify the meaning of 'unconscionable conduct' in the context of section 51AC, without affecting or forcing major change to the wider legislative framework.' Para. 5.57, at 31, Senate Standing Committee on Economics, *The Need, Scope and Content of a Definition of Unconscionable Conduct for the Purposes of Part IVA of the Trade Practices Act 1974*, December 2008.

[491] Both the Terms of Reference (at bullet points 4 and 5) and the Issues Paper (at *iv*) clarify that any amendments are to apply to Part IVA as a whole.

possible differing interpretations between the sections in Part IVA as regards what constitutes unconscionable conduct.

The Issues Paper also makes mention of a number of provisions incorporated into the *Trade Practices Amendment (Australian Consumer Law) Bill 2009* and the *Trade Practices Amendment (Australian Consumer Law) Bill (No. 2) 2010.* The *Trade Practices Amendment (Australian Consumer Law) Bill 2009* was introduced into Parliament on 24 June 2009 and assented to on 14 April 2010 as the *Trade Practices Amendment (Australian Consumer Law) Act (No. 1) 2010.*[492] The *Trade Practices Amendment (Australian Consumer Law) Bill (No. 2) 2010* was introduced into Parliament on 17 March 2010.[493] These changes provided for the following provisions in the *Trade Practices Act 1974* (Cth) and the equivalent provisions in the *Australian Securities and Investments Commission Act 2001* (Cth):

Pecuniary Penalties

Pecuniary penalties of up to $1.1 million for corporations and $220,000 for individuals apply for contraventions of the unconscionable conduct provisions.[494]

[492] The Bill was passed by the House of Representatives on 20 October 2009. The Bill was then introduced and read for a first time in the Senate on 26 October 2009, with a second reading moved on the same date. The Senate required changes to the Bill which were agreed to by the House of Representatives on 17 March 2010. The Bill provided for a commencement date of the day after the Act receives the Royal Assent (Assent was provided on 14 April 2010), for the provisions referred to above. The Bill was enacted as the *Trade Practices Amendment (Australian Consumer Law) Act (No. 1) 2010* (Cth). The unfair contract terms provisions in the Act will come into effect on 1 July 2010.

[493] The *Trade Practices Amendment (Australian Consumer Law) Bill (No. 2) 2010* was enacted as the *Trade Practices Amendment (Australian Consumer Law) Act (No. 2) 2010* (Cth) and received Royal Assent on 13 July 2010, with the main provisions to commence on 1 January 2011. On 1 January 2011, Parts IVA (as well as other consumer protection provisions in Parts V, VA and VC) of the *Trade Practices Act 1974* (Cth) will be repealed and replaced with the Australian Consumer Law. The *Trade Practices Act 1974* (Cth) will also be renamed on 1 January 2011 as the *Competition and Consumer Act 2010* (Cth). Subject to the States and Territories amending their existing laws, the Australian Consumer Law will become a uniform national law.

[494] The Explanatory Memorandum to the *Trade Practices Amendment (Australian Consumer Law) Bill 2009* stated:

Infringement Notices

Infringement notices, which the Australian Competition and Consumer Commission and the Australian Securities and Investments Commission may issue for alleged contraventions of the unconscionable conduct provisions.[495]

Disqualification Orders

Disqualification orders, allowing the court to ban those involved in a contravention of the unconscionable conduct provisions from managing corporations.[496]

Public Warning Notices

Public warning notices, which the Australian Competition and Consumer Commission and the Australian Securities and Investments Commission may issue where reasonable grounds exist to suspect that a corporation has contravened an unconscionable conduct provision.[497]

Court Orders

Court orders to redress loss or damage suffered by non party consumers as a result of a contravention of an unconscionable conduct provision.[498]

These provisions provide a number of advantages in combating unconscionable conduct.

> The lack of availability of civil pecuniary penalties and disqualification orders for enforcement of consumer law represents a significant gap in the range of enforcement options available to the Australian Competition and Consumer Commission (ACCC) and the Australian Securities and Investments Commission (ASIC). While criminal sanctions provide an important deterrent against the most serious forms of contravening misconduct, and civil remedies can achieve timely outcomes for consumers, there is currently no means of obtaining sanctions in the timely manner available under the civil regime.

At [4.3], 53. Schedule 1 (which repeals Schedule 2 of the *Trade Practices Act 1974* (Cth) and replaces it with a new Schedule 2 The Australian Consumer Law), Chapter 5, Part 5:2, Division 1, section 224 of the *Trade Practices Amendment (Australian Consumer Law) Act (No. 2) 2010* (Cth), contains this amendment.

[495] Schedule 2, Part XI, Division 5 *Trade Practices Amendment (Australian Consumer Law) Act (No. 2) 2010* (Cth), contains this amendment.

[496] Section 248 *Trade Practices Amendment (Australian Consumer Law) Act (No. 2) 2010* (Cth), contains this amendment.

[497] Schedule 1, Part 5-1, Division 3, section 223 *Trade Practices Amendment (Australian Consumer Law) Act (No. 2) 2010* (Cth) contains this amendment.

[498] Treasury, Australian Government, 'The nature and application of unconscionable conduct regulation - Can statutory unconscionable conduct be further clarified in practice?' (Issues Paper, November 2009), 4. Schedule 1, Part 5-2, Division 4, Subdivision B *Trade Practices Amendment (Australian Consumer Law) Act (No. 2)* 2010 contains this amendment.

One advantage is the size of the pecuniary penalties acts as a significant deterrent against engaging in unconscionable conduct, particularly for small financiers.

Another advantage is the civil pecuniary penalties and disqualification orders bring Part IVA of the *Trade Practices Act 1974* (Cth) into line with the restrictive trade practices provisions in Part IV of the Act (with the same applying for the corresponding parts in the *Australian Securities and Investments Commission Act 2001* (Cth)).[499]

A further advantage is the Australian Competition and Consumer Commission and the Australian Securities and Investments Commission benefit by being able to ensure that for any relief which they are able to obtain from a court as a result of a successful unconscionable conduct action, the court may extend (if applicable) the relief provided to redress loss or damage suffered by non party consumers.

The final advantage is that public warning notices issued by the regulator where there is reasonable grounds to suspect a contravention of an unconscionable conduct provision, are an effective measure against large financial institutions who are careful to manage their reputation.

These provisions have been described by Michael Terceiro, the former Director of Enforcement with the Australian Competition and Consumer Commission, as:

> … a quite remarkable suite of new enforcement powers and remedies to the *TPA*. With the power to issue substantiation notices, public warning notices and infringement notices, the ACCC will have unparalleled powers to take aggressive and pre-emptive enforcement action against businesses which it believes have contravened the consumer protection laws. … With this new legislation, it seems clear that the balance of power in terms of the investigation and prosecution of suspected breaches of consumer

[499] The Explanatory Memorandum to the Bill, at [4.4], 53.

> protection laws is titled heavily in favour of the ACCC. Whether the ACCC will seek to fully utilise its new investigatory powers and use the new remedies aggressively as leverage in settlement negotiations, remains to be seen.[500]

These onerous provisions should prompt financiers to review their lending and risk management procedures so as to ensure that they have adequate staff training, policies and systems in place to identify and correct behaviour that could constitute unconscionable conduct.

The Expert Panel Report

The Expert Panel Report[501] to the Government in February 2010 had a number of key findings.[502] Most importantly, the report determined that a list of examples would not improve the understanding of s 51AC.[503] Instead, a statement of interpretative principles is better suited to clarifying Part IVA than a list of examples.

The report also recommended that consideration should be given to unifying the provisions in ss 51AB and 51AC. Addressing the educational requirements, the report saw a need for national, state and territory regulators to work together to provide more guidance and educative materials on unconscionable conduct, including the proposed changes to s 51AC.

To aid in the interpretation of recent and proposed amendments to the unconscionable conduct provisions, the report recommended that both the Australian Competition and Consumer Commission (for the *Trade Practices Act 1974* (Cth)) and the Australian Securities and Investments Commission

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[500] Michael Terceiro, 'Ramping up the Powers of the Consumer Regulator and the Court – The ACCC's New Powers Under the *Trade Practices Act*' (2010) 48 (3) *Law Society Journal* 66, 70.

[501] Treasury and Department of Innovation, Industry, Science and Research, 'Strengthening Statutory Unconscionable Conduct and the Franchising Code of Conduct', report to the Minister for Small Business, Independent Contractors and the Service Economy and the Minister for Competition Policy and Consumer Affairs, February 2010.

[502] The key findings are listed at 17 in the Expert Panel Report.

[503] A variety of reasons for rejecting inclusion of examples was provided in the Expert Panel Report. These included: 'Many submissions point to a judicial tendency to reading examples as though they limit the scope of the provisions they exemplify.' (at 26 in the Expert Panel Report).

(for the *Australian Securities and Investments Commission Act 2001* (Cth)) should continue to pursue test cases in diverse industries.

So as to ensure that a future assessment is undertaken of the level of success of the proposed changes to the unconscionable conduct provisions, including the proposed interpretative principles, the report recommended that a review should be held after three to five years.

The Statement of Principles

The Expert Panel viewed the statement of principles as being interpretative principles, assisting the courts and others in interpreting the unconscionable conduct provisions. They were seen as '[g]uiding principles of interpretation provide an indication of the law's effect without unduly confining the law's development.'[504]

The Expert Panel saw it as desirable that the principles for statutory unconscionability under s 51AC (and arguably s 51AB) cover the following areas.

The principles need to make clear that unconscionability '… is not limited to the scope of equitable and common law doctrines of unconscionability',[505] as well as that both substantive and procedural unconscionability is covered by s 51AC, in line with the amendments the Government has promised.[506]

That systemic conduct or patterns of behaviour (rather than an individual transaction) may be indicative of unconscionable conduct, also needs to be included into the principles. [507]

[504] Expert Panel Report, 29.

[505] Ibid, 32.

[506] Ibid, 32–33.

[507] Ibid, 33.

The principles should also address that it is not necessary to identify that a party is at a special disadvantage in order for unconscionable conduct to be established. 'Establishing that a person is at a special disadvantage may be sufficient, but it is not a necessary condition for access to the provision.'[508]

On the question as to whether or not the principles should be mandatory considerations by a court, the Expert Panel has recommended that the principles do not operate as mandatory considerations. The Expert Panel acknowledged that they received submissions pointing out the risk in not making the principles mandatory means that courts may ignore them (much as the existing factors in ss 51AB and 51AC have been largely unused).[509] Making the principles mandatory would be problematic, the Expert Panel determined, as Parliament could not know ahead of time whether '… any factor will be relevant or even if it will exist in the context of any particular case that comes before the court.'[510] The Expert Panel still anticipates that the non-mandatory interpretative principles will extend unconscionable conduct in ss 51AB and 51AC beyond the principles developed in the common law and equity, so as to give the courts a clear intention as to how the provisions of the sections are to be interpreted.[511]

What will be achieved by these proposed changes? It is contended that very little is likely to be achieved by these changes, given the failure to re-define unconscionable conduct and to make the interpretative principles mandatory.

[508] Ibid, 34. The Expert Panel Report elaborates further by stating: 'The question, rather, is whether a party has done "what should not be done in good conscience" [*Australian Securities and Investments Commission v National Exchange* (2005) 148 FCR 132 at 140 per Tamberlin, Finn and Conti JJ], or has engaged in conduct attracting "a high degree of moral obloquy" [*Attorney General of NSW v World Best Holdings Ltd* (2005) 63 NSWLR 557 at 583, per Spigelman CJ].' Expert Panel Report, 34.

[509] Ibid, 29.

[510] Ibid, 30.

[511] Ibid.

Failing to provide a definition

The main problem with existing statutory unconscionable conduct is the inconsistent interpretations applied by courts as to what the term actually means, with a reluctance to provide an expanded application of the term. The provision of factors that may be considered provided in ss 51AB and 51AC have to date largely not been used by courts. As Associate Professor Associate Professor Zumbo stated in his submission to the Expert Panel,[512] the omission of a definition has been a longstanding gap in the present approach to unconscionable conduct under the *Trade Practices Act 1974* (Cth) and has created uncertainty and confusion.[513]

Associate Professor Zumbo saw that the successful application of statutory unconscionability in the *Trade Practices Act 1974* (Cth) required a combination of changes. These main changes were the inclusion of a definition, a rationalisation of the three provisions into one provision dealing with unconscionable conduct in trade and commerce and a recasting of the existing list of factors that may be considered to evidence unconscionability, into a list of non-exhaustive examples (with a rebuttable presumption that those examples would constitute unconscionability).[514]

Associate Professor Zumbo concluded that:

> Anything short of adopting such a holistic approach would unfortunately amount to window dressing and ensure the continuation of the present uncertainty and confusion in relation to the nature and application of unconscionable conduct for the

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[512] Associate Professor Frank Zumbo, 'Issues Paper into the Nature and Application of Unconscionable Conduct Regulation', Submission to the Federal Treasury (December 2009).

[513] Ibid, 2.

[514] Ibid, 3. Associate Professor Zumbo also saw that there was a need to do the following:

First, to provide a guiding principle that the courts when dealing with unconscionable conduct would have regard to the common law requirements of good faith.

Secondly, to apply a range of additional strategies for promoting ethical business conduct in trade or commerce generally.

Thirdly, reinstating business to business contracts involving small businesses back into the unfair contract terms provisions of the Australian Consumer Law.

Fourthly, to apply a range of franchise-specific strategies for effectively dealing with unethical business conduct in the franchising industry.

purposes of the *Trade Practices Act*.[515]

The Expert Panel failing to make the interpretative principles mandatory

Given the reluctance of courts to date to consider the matters listed in the subsections of 51AB and 51AC as factors that may indicate unconscionable conduct, it is difficult to understand how the addition of further non-mandatory interpretive principles would change the courts' approach and thus achieve greater enforceability against unconscionable conduct. The Expert Panel's concern as to the future relevance of any mandatory interpretive principles or their ability to apply in every context could have been addressed by drafting the principles very broadly.[516]

[515] Ibid.

[516] And one might query why the Expert Panel was reluctant to provide draft principles to the Government, for the Government to then consider and engage the industry for feedback.

8. THE NEED FOR LEGISLATIVE AMENDMENT IN LIGHT OF THE HIGH COURT REJECTION OF THE FRENCH J DECISION IN *BERBATIS*

8.1 PROPOSED LEGISLATIVE AMENDMENT TO ENACT THE FRENCH J DECISION

There has been a subsequent change in the composition of the High Court bench since *Berbatis* (ie only Gummow and Hayne JJ remain from the five judges that heard the case), with the trial judge, French J, now being the Chief Justice of the High Court. Although there is some slight possibility that, if a differently argued set of facts was to come before the High Court, there might be some wider meaning applied to statutory unconscionable conduct, this would appear unlikely.

The failure of the Australian Competition and Consumer Commission to bring the facts of *Berbatis* within statutory unconscionability under Part IVA of the *Trade Practices Act 1974* (Cth) raises the issue of how it might be possible to amend the legislation so that statutory unconscionability under Part IVA would extend to fact scenarios such as those in *Berbatis*. A potential starting point would be to enshrine the reasoning of French J at first instance, in legislation.

According to French J the special disadvantage required as one of the elements for unconscionability conduct under Part IVA of the *Trade Practices Act 1974* (Cth) was not limited to the common law restrictions of constitutional disadvantage, as found in cases such as *Amadio* and *Blomley v Ryan.* Situational circumstances arising out of the intersection of the legal and commercial circumstances in which the weaker party found themselves, could also meet the criterion of a disadvantage under Part IVA.[517]

[517] *Australian Competition & Consumer Commission v CG Berbatis Holdings Pty Ltd* (2000) ATPR 41-778, 41,197 [123].

In determining what distinguishes a special disadvantage from a normal disadvantage, French J, reviewing the facts in *Berbatis,* clarifies that '[i]t indicates that the requisite disadvantage will not necessarily be found in the normal run of bargaining inequality between large landlords and small tenants.'[518] From a financier's viewpoint, the mere fact of the difference in financial strength between a bank and its client does not mean that the client is at a special disadvantage. There needs to be something more to make the disadvantage, a special disadvantage. In *Berbatis* that additional element was the circumstance that the Roberts would have lost the value of their business with the expiry of the lease (in addition to the financial pressures they were under with the daughter's illness).

In terms of what would constitute the stronger party unfairly exploiting the special disadvantage that the weaker party was under, French J saw a usage of that unfair exploitation as being the stronger party using its bargaining power to extract a concession from the weaker party that is commercially irrelevant to the terms and conditions of any proposed transaction (eg the lessor's requirement that legal action cease before the lease would be renewed).[519]

French J dealt with the difficulty of defining the term 'unconscionable conduct within the meaning of the unwritten law' and commented that the term was not one that could be determined by reference to a legal dictionary and has no settled meaning. Instead '[i]t offers a standard determined by judicial decision-making rather than a rule …'[520]

In regard to ss 51AB and 51AC, his Honour stated that the term 'unconscionable conduct' is not limited by reference to specific equitable doctrines; ie reference to the matters to be considered in the subsections of

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[518] Ibid, 41,197 [123].

[519] Ibid, 41,198 [124].

[520] *Australian Competition & Consumer Commission v CG Berbatis Holdings Pty Ltd* (2000) 96 FCR 491, 502 [21].

those provisions should be made, and not just be limited to the existing 'unwritten law' mentioned in s 51AA.[521] This view of his Honour, that courts should consider the elements listed in each of ss 51AB and 51AC that are described in those subsections as issues that a court may have regard to, is important, as to date there has not been any widespread utilisation by the courts of those factors.

The Australian Government could consider amendment in Part IVA to ss 51AB and 51AC of the *Trade Practices Act 1974* (Cth)[522] as follows.

For s 51AB dealing with unconscionable conduct against consumers, after the existing wording in s 51AB(1):

(1) A corporation shall not, in trade or commerce, in connection with the supply or possible supply of goods or services to a person, engage in conduct that is, in all the circumstances, unconscionable.

Insert the following new subsections:

(2) Unconscionable conduct occurs in subsection (1) if in a transaction:
    (a) there has been an unfair usage by a corporation or person of their superior bargaining position to extract a concession from a consumer; and
    (b) the consumer was at the time of entering the transaction in a position of special disadvantage due to either constitutional or situational circumstances[523] which the corporation or person was aware of or should have been aware of.

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[521] Ibid, 503 [24]-[25].

[522] As well as the Government extending the provisions to the mirrored sections in the *Corporations Act 2001* (Cth) and in the *Australian Securities and Investments Commission Act 2001* (Cth).

[523] The special disadvantage may be either of a 'constitutional' kind, for example 'deriving from age, illness, poverty, inexperience or lack of education', or it may be of a 'situational' kind, 'deriving from particular features of a relationship between actors in the transaction such as the emotional dependence of one on the other'. *Australian Competition and Consumer Commission v Samton Holdings Pty Ltd* (2002) 189 ALR 76 at 91 (applied at 92), per Gray, French and Stone JJ.

(3) For purposes of determining in subsection (2) what constitutional circumstances may place a consumer in a position of disadvantage, this includes any inherent infirmity, weakness or deficiency of the consumer.

(4) For purposes of determining in subsection (2) what situational circumstances may place a consumer in a position of disadvantage, this derives from the legal and commercial factors impacting upon the consumer, and includes:

(a) the impact on the consumer if the transaction did not proceed;

(b) the nature of the relationship between parties to the transaction such as the emotional dependence of one on the other; or

(c) any other disability that impacted on the ability of the consumer to negotiate the transaction in their own best interests.

(5) For purposes of determining in this subsection (2) whether a concession has been extracted, a concession may include (but is not limited to) a transaction not being provided on normal commercial terms that would have been provided for a similar transaction or obtaining a concession that was commercially irrelevant to the transaction being entered into.

The remaining ss 51AB(2) – 51AB(7) would then be renumbered to ss 51AB (6) – 51AB(11). Similar changes would be made to s 51AC dealing with unconscionable conduct against small business (with 'business consumer' replacing 'consumer' in the above suggested wording).

8.2 WHAT WOULD BE THE IMPACT IF THESE STATUTORY CHANGES WERE MADE?

If his Honour's views from *Berbatis* at first instance were embedded into statute,[524] it would impose a greater burden on financiers to more thoroughly explore the full range of circumstances of their loan applicants and potential security providers. As well as understanding the loan applicant's full financial position (which financiers would nearly always be doing, in any case), financiers would need to be able to gather data and be able to consider such extrinsic factors in their risk rating approval process for finance as follows.

The first additional factor that financiers would need to consider is what, if any, situational disadvantages might apply to the applicant. Financiers would have to look more broadly at the applicants' circumstances. This would include determining if there are any emotional stresses being imposed upon the applicants that could influence their decision to borrow (such as the serious illness of the Roberts' daughter in *Berbatis* that created financial pressures and influenced their behaviour in the leasing renewal negotiations).

Included within situational disadvantages that the financier would need to consider, is the repercussion to the applicants in the event that the finance is not approved, such as whether it would cause a business to fail. An example would be that in *Berbatis*, if the lessees had not agreed to drop their litigation against the lessor, the lessor would not have agreed to the extension of their lease, and that agreement was in turn crucial to facilitating the continuation of the business and its planned sale.

A second additional factor to consider would be the need for the financier to consider if they are extracting a concession that is commercially irrelevant to

[524] This assumes that similar amendments were also made to these mirrored provisions in the *Corporations Act 2001* (Cth) and the *Australian Securities and Investments Commission Act 2001* (Cth), given that only the protection for small business provisions in s 51AC of Part IVA of the *Trade Practices Act 1974* (Cth) applies to finance.

the transaction, particularly when approving additional finance requests to existing clients who are identified as being at a potential disadvantage (such as facing financial pressures and additional moneys are being advanced as a 'work out' from the client's financial difficulties). This includes the need for a financier to carefully consider any opportunity the financier may want to take to improve the structure on other finance facilities already in place for the borrower. This could include the financier improving their security, pricing or repayment arrangements, or any insistence by the financier on the sell down of assets in other businesses / entities controlled by the debtor.

The third additional factor to analyse, in order to assist in mitigating against any allegation of unfair usage of a superior bargaining position, would be greater analysis being undertaken by the financier as to whether the facility requested is in the overall best interests of the applicants (ie can the financier be satisfied that the applicant is obtaining an adequate benefit from entering the transaction).[525]

In order to be able to address these above factors, financiers would in practice need to undertake a wide range of activities commencing with the need to amend their loan application forms so that indications of the existence of some of these factors could be disclosed. Secondly, financiers would next need to revise their credit procedures manuals so as to recognise these factors as additional risks that would need to be mitigated against, as well as provide additional training for credit staff so as to ensure they make adequate inquiries to 'tease out' these issues. The third step would be to consider the need for mandatory risk mitigants such as greater use of independent legal advice and independent financial advice by loan applicants / security providers.[526]The last step would be for financiers to review the risk

[525] Much as financiers will need to do when the responsible lending requirements come into force under the National Consumer Credit Code requirements, which is a matter dealt with in a later chapter of this thesis.

[526] Appreciating that obtaining such will not in all cases protect the financier if the lending proposal was one that was very much to the disadvantage of the client and one that a reasonable financier should not have approved.

‘weighting’ provided in their credit scoring approval system to recognise these additional risk factors that might cause clients to challenge the enforceability of their loans.

These steps would add to the cost of providing finance, which would ultimately be passed on to loan applicants via higher finance charges. In addition the financier would likely experience a modest increase in the write off amounts due to bad debts. This would follow on from a lower debt recovery success rate due to the wider statutory relief available. Financiers typically would increase the interest margins on their loans to offset that higher risk of loss.

The impact on consumers and small business, apart from the increased cost, would be both positive and negative. On the positive side, applicants and security providers would find that financiers are more discerning in relation to whom they choose to lend, and from whom they accept security. This will ultimately prevent some consumers and small businesses from borrowing and providing security and ending up in financial difficulties / losing their security properties / home. In addition, a financier’s clients who believe that the financier’s conduct has been unconscionable will have a clear statutory definition to rely upon which will hopefully lead to wider relief under statutory unconscionability being obtained in a consistent manner from the courts.

On the negative side, finance applicants will find that financiers will be more invasive in terms of the amount of information they require in order to ensure they are fully aware of the applicants’ and security providers’ circumstances and relationships between them. In addition, some consumers and small business applicants will experience difficulty in obtaining finance, due to financiers being wary that these applicants or their security providers may fall in the high risk area of being able to meet the requirements of obtaining relief from the broader legislative framework for unconscionability.

Whilst recognising that these additional steps being imposed upon financiers would be onerous, and that there are some negative impacts upon finance applicants, the improvement in the quality of finance decisions being made and thus a lessening in the number of people who take on ill-advised risk (with a corresponding decrease in the number of challenges made to the validity of loans and security provided),[527] the protection it would provide to sureties and debtors placed into unconscionable situations from being exploited is seen as justifying such an approach.

[527] Kirby J in *Garcia* at 434 [79] also saw similar benefits in the adoption of the approach that he favoured; namely, re-formulating Lord Browne-Wilkinson's approach in *O'Brien*.

9. RECENT DEVELOPMENTS IN FINANCE PRODUCTS

There has been a huge development in finance products over the last decade. This chapter will examine what those changes are, plus determine to what extent the legislative changes proposed to Part IVA in this thesis will have on providers of finance for both these new products as well as existing products.

9.1 DEVELOPMENT IN FINANCE PRODUCTS OVER THE LAST DECADE

9.1.1 LOW DOC AND NO DOC LOANS

A low-doc loan is a type of finance where in the financier's assessment of the loan applicant's ability to service the loan, only limited evidence is required to support the applicant's claims as to their income and outgoings details. A no-doc loan is where the financier assesses the loan applicant's ability to service the loan, but does not require evidence to support the applicant's income and outgoings details.

Both these types of loans were in growth mode in Australia until recent times. For the month of September 2006, 10% of new housing loans made for that month were low-doc loans[528] and were being offered by all the major banks (but as a percentage of the banks' total loan book, remained low).[529] The low-doc figure as a percentage of all housing loans decreased to 7% (-3%) in 2007 and has stayed at that level up to March 2010, as a combination of factors such as higher interest rates and global credit market uncertainties and the impact of changes to the higher capital weighting assigned for low-doc loans for banks by the Australian Prudential Regulatory Authority ('APRA').[530] With the United States sub-prime credit crisis impact on

[528] Dr John F Laker, Chairman APRA, 'The Regulator's Approach to Compliance: Crackdown, Confrontation or Compliance Culture' (Speech delivered to The Institute of Chartered Accountants in Australia, Melbourne, 20 June 2007), 8.

[529] The APRA Insight Issue One 2006, 8.

[530] Reserve Bank of Australia and APRA submission to the House of Representatives inquiry into home loan lending practices and processes, quoted in Treasury, Australian Government, 'Green Paper - Financial Services and Credit Reform - Improving, Simplifying and Standardising Financial Services and Credit Regulation' (June 2008), p. 3, and Lucy Ellis, Head of Financial Stability Department, Reserve Bank of Australia, 'Recent Developments in the Housing Market

Australian mortgage originators in 2008 and turning into the Global Financial Crisis, tightening lending criteria by financiers and a lack of market depth to syndicate these loans by the financiers once drawn down, saw the number of low-doc loan products on offer by lenders fell by 15% in the first seven months of 2008 and such banks as HSBC and Macquarie withdrawing their low-doc products from the market (but still leaving 38 Australian financiers offering low-doc loans).[531]

With these types of loans, stronger reliance is placed by the financier upon the ability to recoup the loan from sale of the security, as opposed to the detailed analysis and verification of the serviceability and analysis of the viability of the loan purpose that is carried out when a loan is for a business or investment purpose.[532]

9.1.2 EQUITY RELEASE PRODUCTS

These are promoted as a way for people to use their home to generate an income, usually when they retire, when they are asset rich but income poor.[533]

The main equity release product is the reverse mortgage. As at 30 June 2009 the Australian reverse mortgage market had $2.6 billion outstanding in 38,100 loans, with an average loan amount of $68,000.[534] A reverse mortgage is where the home owner makes no principal or interest repayments

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and its Financing' (speech delivered at the Financial Review Residential Property Conference 2010, Sydney, 18 May 2010), 8, citing APRA preliminary data for March 2010.

[531] Stephen Johnson, 'Self Employed Face Loan Troubles', *AAP* (Sydney), 1 August 2008, quoting financial research group Cannex figures.

[532] See Spigelman CJ (with Handley and Basten JJA agreeing) in *Perpetual Trustee Company Limited v Khoshaba* [2006] NSWCA 41 (unreported, 20 March 2006, BC200602108), [92]. His Honour comments on one of these types of loans in regard to the financier not investigating the viability for an investment loan, noting that the indifference to the likelihood of success of the investment suggested that the financier was '… content to proceed on the basis of enforcing the security …'.

[533] Simon Hoyle, 'Pensioning Off Bricks and Mortar', *Sydney Morning Herald* (Sydney), 19–20 November 2005, Business Section, 45.

[534] *Deloitte / SEQUAL Research Report*, June 2009, at 4–5 (SEQUAL is the Senior Australians Equity Release Association of Lenders). The 30 June 2009 reverse-mortgage figure represented a 5% growth since 30 June 2008.

on the loan until they die or vacate the home.[535] ASIC provides the example of a $50,000 reverse mortgage which over a 15 year period at compound interest at the rate of 10% p.a. would increase the debt to $232,000 (and to $1,041,000 over 30 years).[536]

Another equity release product is a home reversion scheme. This product is not technically a loan as the facility involves the consumer selling up to usually a maximum of half the equity in their home in exchange for receiving an up front lump sum payment now. This lump sum payment is discounted to reflect the consumer's age and life expectancy. The financier receives a fixed proportion of the future value of the home, payable from the proceeds of the home sale once the consumer dies or vacates the home.[537] ASIC notes that these facilities are currently only available to consumers aged 60 or over living in certain areas in Sydney or Melbourne.[538]

Centrelink and the Department of Veterans' Affairs also offer an equity release product called a pension loan scheme. This product is only available to those consumers who are either already receiving a part aged pension, or those who though not receiving an aged pension would be eligible to receive it if they had not failed to meet either the asset or income test (but not both).[539] The consumer provides a mortgage over their residential property in exchange for receiving a fortnightly amount up to the maximum amount of the aged pension.[540] Interest is charged at a lower rate than normal equity release products and compounds to the loan account. The loan is repayable upon either the sale of the security or the death of the consumer.

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[535] ASIC, *Equity release products,* (Report 59 November 2005), 4.

[536] ASIC consumer guide, *Thinking of Using the Equity in Your Home? An Independent Guide to Reverse Mortgages and Other Equity Release Products* (22 June 2009), 9.

[537] Ibid, 12.

[538] Ibid.

[539] Ibid, 14.

[540] Centrelink, *Pension Loans Scheme Fact Sheet* <http://www.centrelink.gov.au/internet/internet.nsf/filestores/fis018_0809/$file/fis018_0809en.pdf> at 9 May 2010). If the consumer is already receiving a part aged pension, they may receive a top-up to their fortnightly aged pension up to the maximum amount of the aged pension.

Also classified by ASIC as equity release products are shared appreciation mortgages ('SAMs'), where a consumer gives up the right to some of the capital gain on the property in return for paying a reduced rate or no interest at all on that part of his or her borrowings. These mortgages are also known as equity finance mortgages ('EFMs').

ASIC notes the risks that reverse mortgages and home reversion schemes have for consumers. The first concern is that they are usually secured by the family home. The second concern is that the loans are targeted at consumers at the end of their working lives, when consumers need to ensure that they manage their home equity and income to last for the rest of their lives.

The third concern is that complex issues arise, such as projected movements in property prices and interest rates (including the impact of capitalising interest if interest rates rise significantly). In addition, variations in consumers' life expectancies and old age caring and housing needs have to be considered, and questions asked of who meets the cost of repairs and renovations (and who obtains the financial benefit of such).[541]

The fourth concern is the question of what happens in the event that negative equity should occur when the debt exceeds the realisable market value, as occurred in the English property market in the late 1980s and in some parts of the United States between 2007 and 2009.[542] Most reverse mortgages in Australia protect the consumer against this risk by limiting the liability of a debtor with a No Negative Equity Guarantee (NNEG).[543]

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[541] The ASIC November 2005 report *Equity Release Products*, 5–6.

[542] Robert Shiller, 'Volatility is Home to Roost', *Australian Financial Review* (Sydney), 6 January 2010, 46, cites the S&P/Case–Shiller 10-City Home Price Index report that for the four months to March 2009, US home prices fell by 7% (21% annualised), prior to then bouncing back with a 5% (15% annualised) increase for the for the result to August 2009. Recent housing price increases in the United Kingdom and Australia are also reported.

[543] ASIC, *Thinking of Using the Equity in Your Home? An Independent Guide to Reverse Mortgages and Other Equity Release Products*, 11.

9.1.3 CHANGING LOAN DELIVERY CHANNELS

Over the last decade there has been a growth in finance brokers and mortgage originators, where the financiers themselves do not normally meet the loan applicant or security provider, but place reliance on these third parties to interview and accurately document to the financier the loan purpose and relationship between the parties. In an APRA housing loan survey for the month of September 2006, 35% of loans made for that month were originated through third parties such as mortgage brokers.[544] In March 2007 the Reserve Bank of Australia estimated that '… as much as one third of small to medium-sized businesses currently access finance through brokers.'[545]

APRA has recognised the risks to banks from the increased reliance on brokers and has commented:

> The greater reliance on brokers for residential lending, and increasingly for business lending, requires appropriate monitoring by ADIs and the verification of critical borrower information provided to ADIs on loan applications.[546]

Coupled with the growth of loans being written by financiers through broker and mortgage originators is the increasing automation of the consumer and small business loan approval process to assess finance applications from these sources. Computer system-based credit scoring does not usually readily accommodate the input of a detailed explanation of the relationship between the finance applicants and the security providers. The risks for the finance applicant or the security provider in entering the transaction, of particular concern where the family home is provided as security, are also not readily captured in computer system-based credit scoring.

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[544] Dr John F Laker, Chairman APRA, 'The Regulator's Approach to Compliance: Crackdown, Confrontation or Compliance Culture' (Speech delivered to The Institute of Chartered Accountants in Australia, Melbourne, 20 June 2007), 6.

[545] Treasury, Australian Government, 'Green Paper – Financial Services and Credit Reform – Improving, Simplifying and Standardising Financial Services and Credit Regulation' (June 2008), 3–4, referring to the Reserve Bank of Australia, Financial Stability Review of March 2007.

[546] APRA Insight Issue One 2006, 9.

The ultimate provider of the finance usually does not meet the applicants and security providers, but instead places reliance upon the integrity of the finance data input by the third party. In addition the finance provider usually undertakes verification checks on the documentation supplied by the third party. Such things as the finance applicant's identity, income and expense details, financial position and the place of residence / business address are all usually verified by the financier.

For these loans introduced by third parties, financiers run a number of risks. The first risk is that the third party may not act honestly and diligently in processing the finance application through to the financier and in their advices to the loan applicant and security providers, given that the third party is only paid their commission when the loan is approved and has been drawn down.

The second risk is that because the financier does not meet with the finance applicants, the financier may not appreciate the nature of any special relationship between the applicants and security providers, or any duress or deliberating circumstances that they may be under.

9.2 IMPACT ON UNCONSCIONABLE CONDUCT FROM THESE DEVELOPMENTS IN FINANCE PRODUCTS PLUS THE NCC INTRODUCTION

Given the vulnerable class of borrowers that reverse mortgages and home reversion schemes target (the elderly with low income) and that the debt clearance only has one source, that being the sale of the family home, these types of loans have the potential in the future to stretch the ambit of what would attract relief on the basis of unconscionability, particularly if the legislative amendment of French J's view was adopted.

The age of the applicants often places these potential borrowers in the class of constitutional special disadvantage. In addition, the issue that their cash flow is often inadequate to meet the interest and the resultant eroding impact the capitalising debt has on their equity in their home security property, places these applicants at a situational special disadvantage. So if French J's changes previously mentioned were embedded into statute, in order to avoid the unconscionable conduct requirement of there also being an unfair usage by the bank of any superior bargaining position, it would be essential for financiers to insist upon independent legal advice and, in some instances, independent financial advice, first being obtained prior to these loans being drawn down.

Reverse mortgages are specifically made mention of by ASIC in their Regulatory Guide 209 *Credit licensing: responsible lending conduct* ('RG 209'). RG 209 sets out ASIC's expectations for financiers meeting the responsible lending obligations for consumer credit in Chapter 3 of the *National Consumer Credit Protection Act 2009* (Cth). These responsible lending conduct requirements will come into force from 1 July 2010 (1 January 2011 for banks and registered financial corporations).

The *National Consumer Credit Protection Act 2009* (Cth) came into force on 1 January 2010 and imposed the requirement on providers of consumer finance providers to register with ASIC before 30 June 2010 and apply for an

Australian Credit Licence between 1 July 2010 and 31 December 2010. ASIC will from 1 July 2010 be the national regulator for consumer credit.[547] Schedule 1 of the Act contains the National Credit Code ('NCC') which will replace the existing States based Consumer Credit Codes. The Act requires national licensing for consumer credit providers,[548] as well as introducing other significant additional requirements such as the responsible lending requirements.

The responsible lending requirements introduce important obligations for financiers. These include the need not to suggest, recommend or provide unsuitable finance;[549] that licensees must conduct reasonable inquiries and verify the consumer's financial situation;[550] and that upon request consumers be provided with a copy of their finance assessment.[551]

The guidance provided in the responsible lending requirements in RG 209 as to what reasonable inquiries and verifications need to be undertaken by financiers for reverse mortgages requires financiers to undertake a high standard of investigation and verification of the finance applicant's position.[552] In addition ASIC expects the finance provider to undertake a high standard of investigation and verification of the loan applicant's understanding of the loan contract and its possible consequences.[553]

So to some degree the tightening or requirements on financiers for consumer lending that the NCC will impose, higher than the existing Uniform Consumer Credit Code that it replaces, could lessen the possibility of

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[547] The Australian States are expected to pass State Referral Bills and repeal their State laws before 1 July 2010, when the new National Consumer Credit regime will take effect.

[548] Chapter 2 *National Consumer Credit Protection Act 2009* (Cth).

[549] Ibid, s 118.

[550] Ibid, s 117.

[551] Ibid, s 120.

[552] RG 209, 18.

[553] Ibid.

consumers being put into a disadvantageous position where the elements of statutory or equitable unconscionable conduct would be satisfied.

When scenarios do emerge that would appear to meet the requirements of seeking relief under statutory unconscionable conduct, it is possible that for consumer lending that claims for relief based on breaches of the NCC may be argued as well, once the NCC comes into force.

10. CONCLUSIONS

Any reference in these conclusions to the impact on financiers or proposed changes to Part IVA of the *Trade Practices Act 1974* (Cth) is to be taken to also include the mirrored unconscionability provisions that apply to financial services in the *Australian Securities and Investments Commission Act 2001* (Cth) of ss 12CA, 12CB and 12CC. The conclusions are as follows.

1. There has been a significant growth in the last few years in the number of unconscionability cases and legislation being created. This is a concern for financiers, especially given the growth of finance brokers and mortgage originators, the increased automation of the credit assessment process and the new types of higher-risk loan products that have come on to the market,

2. The meaning of unconscionability under the general law has been firmly established by the High Court in cases such as *Amadio*. An unconscionability claim requires the establishment of two elements. The first element is that the guarantor was under a special recognised class of disability. The second necessary element is that the stronger party knew, or ought to have known, of the weaker party's special disability and was unfairly abusing its dominant position. There has been no expansion of the definition of unconscionable conduct outside this rigid definition.

3. Courts have been reluctant to utilise the indicators of unconscionable conduct listed under ss 51AB and 51AC, and have generally narrowed their consideration to determining if the elements of *Amadio* are evident so as to ascertain under s 51AA if unconscionability has been established 'within the meaning of the unwritten law'. Although there has been a lot of flurry about the introduction of ss 51AB and 51AC to the *Trade Practices Act 1974* (Cth), which was designed to improve the effectiveness of the unconscionability provisions in Part IVA, the sections to date have not effectively extended the liability of parties who engage in unconscionable conduct.

4. The view of the majority in the High Court decision in *Berbatis*, where the Court rejected providing a wider view of the unconscionability provision of s 51AA of the *Trade Practices Act 1974* (Cth), eases any initial concerns financiers may have had that debtors or security providers might have been able to obtain widespread relief from the courts (eg the widespread relief covering misleading and deceptive conduct that s 52 provided, following its introduction) under Part IVA of the Act.

5. The subsequent change in the composition of the High Court bench that heard *Berbatis*, including the appointment of the Federal Court trial judge, French J, as the Chief Justice of the High Court, may influence how the High Court in future interprets unconscionability under Part IVA of the *Trade Practices Act 1974* (Cth). However, recognising the strength of the majority decision in *Berbatis,* such a change by the High Court would appear unlikely.

6. The possibilities that Australian financiers need to be aware of, in regard to statutory unconscionability, is that if a case similar to *Berbatis* were to come before the High Court, the High Court may either do one of two things. The first option would be to adopt the Federal Court trial judge approach of French J from *Berbatis* and not be restrained by the common law in construing Part IVA – in which case, Australian financiers need to be mindful of their increased liability. Given the strength of the majority decision in *Berbatis*, this is unlikely. The second option is to agree with the High Court approach on *Berbatis* to limit the scope of applicability of Part IVA – in which case Australian financiers need to be aware that that may be the catalyst (particularly if it was the Australian Competition and Consumer Commission failing again on Part IVA before the High Court) for Parliament to consider making changes to Part IVA so as to adopt French J's approach.

7. Recognising that it is likely that the High Court will continue to follow its decision in *Berbatis*, in line with the decision of the trial judge in

Berbatis, French J, sections 51AB and 51AC of the *Trade Practices Act 1974* (Cth) could be amended as outlined in this thesis so as to provide a clear definition as to the factors that the court must have regard to for the purpose of determining whether conduct is unconscionable.

8. The implication for financiers if the High Court were to provider a wider interpretation to unconscionability, or if the suggested legislative amendment were made, would be that financiers would need to take a more conservative approach in regard to their willingness to provide finance and accept security. Greater analysis would be required by financiers of applicants' and security providers' position and greater insistence placed on independent advice being provided to security providers.

9. The Australian Government appears committed to bolstering the unconscionable conduct provisions in Part IVA through the imposition of pecuniary penalties and additional powers for the regulators and the courts provided for in the *Trade Practices Amendment (Australian Consumer Law) Act 2010* (Cth), the Government announcement that amendments would be made to Part IVA to make it clear that it applies to both to substantive unconscionability and procedural unconscionability, and that a statement of principles of what constitutes unconscionable conduct would be included (however ineffectual that may be).

10. There has been some willingness of the lower courts, since the High Court decision in *Garcia*, to expand the nature of relationships under which a special emotional relationship may exist, to enable guarantors who were under such a special relationship and could demonstrate that they were volunteers to obtain relief under the special equity in *Garcia*. The limits of this expansion are not yet finalised. These lower courts have been guarded about the breadth of that extension. The various lower court judgments also indicate a lack of consistency.

Financiers need to consider ensuring that they more fully explore finance applications where uncertainty (or a lack of knowledge) exists in regard to the relationship between a provider of security and a debtor, and where there is no apparent direct benefit accruing to the provider of the security as a result of the transaction. This includes recognising relationships demonstrating trust and reliance of one party on another – similar to a wife's relationship to her husband – such as that which may exist between a husband and his wife, parties in de facto relationships regardless of gender, siblings and parent and child etc.

In cases where there is any doubt as to the type of relationship and its strength, and a commercial decision is made to allow the finance to proceed, the financier should require the security provider to obtain independent legal advice (and if the circumstances warrant, independent financial advice), with the financier retaining evidence of such.

11. Financiers must ensure they follow rigid criteria in order to avoid the possibility of having their contracts challenged with a special equity *Garcia* claim or an unconscionability claim.

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