

Equity and Trusts
Exam Notes Autumn
2014

Unconscionable Transactions

- Equitable fraud
- Undue influence
- Unconscionable conduct

Equitable Fraud

Common law fraud requires proof of *conscious dishonesty*, i.e. there must be an element of *mens rea*. Therefore, a party alleging “fraud” must show that some false representation has been made in the **knowledge** that it was untrue (or at least with *reckless indifference* to its truth or falsehood: *Derry v Peek* (1889)). This element of “knowing dishonesty” **restricted** common law actions for deceit to a *narrow* field and a heavy **onus** was placed on a plaintiff seeking to avoid the contract for “fraud” at common law.

Equitable fraud, however, includes not only unconscionable transactions, but also any behaviour which is unjust, unfair or which breaches equitable principles.

Nocton v. Ashburton [1914] has established that equitable fraud does *not necessarily* involve **intentional fraud**. Fraud when used in this *wider* sense means, **not** moral fraud in the ordinary sense, but a breach of the sort of obligation, which is enforced in a court of Equity. *No actual intention to cheat need be proven*. It is **sufficient** if a person misconceived the extent of an obligation imposed on him or her by a court of equity, the fault being that that person violated, however *innocently*, an obligation which he or she must be taken by the court to have known.

Furthermore even where the party committing equitable fraud acts in good faith, equitable fraud may arise: *Boardman v Phipps*.

Undue Influence

According to *Blomley v Ryan* where a person is in a position of influence over another, and the subordinate party transfers to the dominant party, equity will presume that the transfer was brought about by the exercise of undue influence & will strike the transaction down – unless the dominant party can show that it was a product of the free & independent will of the other.

The will of the weaker party is overborne by the stronger.

There are two types of undue influence:

- (i) **presumed undue influence**
- (ii) **actual undue influence**

Presumed undue influence

The complainant has to show that there was a pre-existing relationship of trust and confidence between the complainant and the wrongdoer of such a nature that it is fair to **presume** that the wrongdoer abused that relationship to enter into the impugned transaction. It is necessary to show that the relationship between the parties comes within one of the ‘presumed’ categories.

Where the third party has actual or constructive notice of undue influence and proceeds to obtain the benefit of a transaction entered into as a result of such undue influence, the transaction may be set aside: *Bank of NSW v Rogers*.

There are a number of classes of relationship that attract the presumption. These include:

- Solicitor/client
- Trustee/beneficiary
- Doctor/patient
- Parent/child or guardian/ward
- Spiritual leader/ follower

Solicitor/client

A solicitor must take additional steps to ensure the independent and informed decision-making capacity of their client. According to *Bester v Perpetual Trustee* it is not sufficient for the solicitor to explain to the client the situation and ask if they have any questions regarding the transaction.

Trustee/beneficiary

The trustee-beneficiary relationship will only attract the doctrine of undue influence where there is a personal connection between the trustee and the beneficiary as to constitute an interference with the beneficiary's independence in decision making: *Whereat v Duff*.

Doctor/patient

A doctor-patient presumption arises where the subordinate party is excessively ill and relying on the advice of their medical advisors: *Haskew v Equity Trustees Executors; Breen v Williams*.

Parent/child or guardian/ward

This relationship is one of perceived dependency in respect of fulfilling basic needs, advice and decision making. Thus, a child need not show that their parent acted in bad faith with regards to transactions entered between them. The onus is on the parent to establish the freedom of the child: *Lamotte v Lamotte*.

Even if the parent executes the best interests of the child, the transaction will be set aside if the child was denied the ability to make their own judgement through the exertion of influence by the parent: *Bullock v Llyods Bank Ltd*.

Further, not only does this presumption operate against the parent/guardian, but also against third parties who benefit from the transaction and who were aware of the situation between the parties: *Bank of NSW v Rogers*.

Spiritual leader/ follower

According to *McCulloch v Fern*, presumed undue influence arises where the spiritual leader deliberately took advantage of his/her domination over the follower to procure the follower's consent to the transaction, in which the spiritual leader knowingly and intentionally places the follower in a position of special disadvantage in respect of the transaction that has occurred in which the follower would have found it difficult to refuse.

Actual undue influence

Actual undue influence arises where an aggrieved party cannot satisfy the court that the relationship with the alleged party falls within the categories of presumed undue influence.

An aggrieved party may seek to set aside a transaction by proving that the alleged party had come to occupy or assume a position of ascendancy or influence over the other or a dependence of trust on his part: *Johnson v Buttress*. Involving the subordinate party to take a position of dependence or subjection: *Goldsworthy v Brickell*

Additionally according to *Allcard v Skinner* there must have been some unfair and improper conduct, coercion, some form of overreaching, cheating and generally some personal advantage placed by the donee in some close and confidential relation to the donor.

In *Bank of Credit and Commerce International SA v Aboody* (1989) it was held that the requirements for proving actual undue influence are:

- dominant party has **capacity** to influence the other;
- the influence is actually **exercised**;
- the exercise of influence is **undue**; and
- the relevant transaction was the **result of** the exercise of influence

Rebutting the Presumption of undue influence

Undue influence is a presumption and therefore may be rebutted by evidence to the contrary. Therefore, the wrongdoer (i.e., the dominant party) bears the onus of rebutting the presumption.

One factor which may rebut the presumption of undue influence is independent legal advice: *Bester v Perpetual Trustee Co Ltd*. Where the dominant party can show that the weaker party entered into the transaction on the grounds of independent and informed decision as a result of independent legal advice, this is sufficient to rebut the presumption. However, independent legal advice must constitute more than superficial questioning: *Bester v Perpetual Trustee Co Ltd*. The advice must simply be sufficient to arm the weaker party with the legal effects and options available to them and an understanding as to what the transaction encompasses: *Brusewitz v Brown*; *Bester v Perpetual Trustee Co Ltd*

According to *Bester's case* (citing *Everitt v Everitt*) there are three elements, which detract the strength of the independent advice:

- the absence of any power of revocation
- the absence of the right to have resort to corpus
- the absence of any power or removal or appointment of the trustees or intervention in their activities.

Furthermore, it is not essential that the alleged subordinate party acted in accordance with the independent advice received: *Banco Exterior v Thomas*.

Other considerations that may rebut this presumption of undue influence

The consideration or lack thereof, provided from the dominant party – although consideration in and of itself does not prove that the subordinate party's decision to enter the transaction was independent and informed: *Commercial Bank of Australia v Amadio*. The Courts have developed a strict approach in establishing undue influence where adequate consideration has been provided will be more onerous on the dominant party: *Watkins v Combes*. In determining whether the subordinate party made an independent and informed decision the court will have regard to all these factors. These factors in support of the dominant party's defence will be offset against either the presumption of undue influence/ factors establishing the actual undue influence and determined on the balance of probabilities: *Stivactas v Michaletos (No2)*.

Spousal guarantees: a wife's special equity

Although the relationship between husband and wife **does not** give rise to *presumed* undue influence, there may be circumstances in which the wife can obtain relief against a husband in regard to a guarantee given by the wife over property in which she has an interest.

The principle in *Yerkey v Jones* is that a wife need not prove actual or constructive notice (by the third party) of the undue influence. The conduct of the husband binds the third party (e.g. a bank), independently of agency or notice.

According to Garcia v. National Australia Bank it would have been unconscionable for the respondent to enforce the guarantee against the appellant as:

- (a) the appellant did not understand the purport and effect of the transaction;
- (b) the appellant was a volunteer because she did not obtain any financial benefit from the transaction;
- (c) the respondent was taken to have understood that, as a wife, the appellant may have reposed trust and confidence in her husband in matters of business and therefore to have understood that the husband may not have fully and accurately explained the purport and effect of the transaction to the appellant; and

(d) the respondent took no steps to explain the purport and effect of the transaction to the appellant or to ascertain whether the effect of the transaction had been explained to her by a competent, independent and disinterested stranger.

Unconscionable conduct/ unconscionability

Amadio's case have established the circumstances under which unconscionability arises:

(i) a party to a transaction was under a special disability in dealing with the other party with the consequence that there was an absence of any reasonable degree of equality between them. The special disability must seriously affect the ability of the innocent party to make a judgment as to his own best interests and

(ii) 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.

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: *Blomley v Ryan*

Relief from unconscionable conduct is available in transactions where one party is at a special disadvantage or disability vis a vis the other due to factors such as *poverty* or *need of any kind*, sickness, age, sex, infirmity of body or mind, drunkenness, illiteracy or lack of education, lack of assistance or explanation where assistance or explanation is necessary: *Blomley v Ryan*.

If unconscionability is established the party at a disadvantage is entitled to a remedy unless the stronger party establishes that the transaction was fair, just and reasonable: *Amadio's* case.

However, it is arguable that in the decision in *Kakavas v Crown Melbourne Ltd*, by the High Court has narrowed the application of the principles relating to unconscionable conduct. It appears as though the High Court has restricted the application of the principles of unconscionable conduct to situations in which the weaker party not only suffers from a disability of which the stronger party is aware, but must also be socially disadvantaged in other ways and that this special disability should extend to the weaker party's ability make decisions on his/her best interest in his/her everyday life and not to a particular transaction.

Defences to undue influence and unconscionable conduct

The onus of proof initially falls upon the plaintiff to establish a sufficient degree of disadvantage, and then shifts to the defendant to prove that the transaction was just and reasonable: *Amadio*; *Aboody*. In the light of *Kakavas*, it may also be possible for a defendant to argue that in entering into the transaction with the plaintiff and despite the fact that it was aware of the plaintiff's disability, it was merely acting in the ordinary course of its business.

The defendant may raise the equitable defences of:

- **Laches**
- **Acquiescence**
- **Independent advice – legal or other professional**

Independent advice – legal or other professional

In regard to independent legal advice, lawyer advising the plaintiff must be ‘independent’ in the true sense of the word and must not have any form of relationship or connection to the defendant: *Aboody*. **For more info refer to rebuttal of presumption of undue influence.**

Remedies

- Rescission
- Refusal of specific performance

**UNDUE INFLUENCE AND UNCONSCIONABLE CONDUCT
COMPARATIVE TABLE**

UNDUE INFLUENCE	Must Show...	Characteristics	Rebuttal	Remedy
presumed	Pre-existing relationship of trust and confidence – presumed categories not closed	The will of the influenced party must be overborne – action not voluntary	*independent advice *laches *influence of 3 rd party	Rescission
actual	Relationship of ascendancy and dependence	As above	As above	As above
UNCON. CONDUCT	Pl. under a special disadvantage or disability of which the defendant was aware	Will of the pl. not overborne BUT the def exploits the disadvantage/disability	*as above *the transaction was fair and reasonable	Transaction set aside or refusal of specific performance

Equitable Property and Assignments

- The nature of property in equity
- Categories of Equitable Interests and Priorities
- Assignments and Future Property

The nature of property in equity

Equitable property or an equitable interest is any interest in real or personal property that is held and has been created pursuant to the application of equitable principles.

Interest in property takes many forms. If the rights are recognised by the common law, they are regarded as legal interests. If recognised by equity, they are regarded as equitable interests.

Whether the interest is legal or equitable is a question of whether (*Yanner v Eaton* 1999) a specific legal relationship with a thing recognised by the courts of common law or equity. If it is the former, the interest is a legal interest. If it is the latter the interest is an equitable interest. Equity follows the law. This is an important principle in the area of property law. For every legal interest there is a corresponding equitable interest. This doesn't mean, however that in every piece of property there exists concurrent legal and equitable interest.

According to *Commissioner of Stamp Duties v Livingstone* (1965) where a legal and equitable interest in land unites, the equitable interest merges with the legal. Whereby both common law and equity, then the owner of that interest is said to hold only the legal interest, with all the rights and incidents that attach to that estate.

Millet J in *Macmillan v Bishopgate Investment* (1995) stated that:

‘The essence of the distinction (between legal and equitable interests) is that a legal estate binds all the world, where as an equitable interest binds only the transferor and those deriving title under him with a notice of that interest’.

Categories of Equitable Interests and Priorities

The nature of an equitable interest is determined by the extent to which a court of equity will protect it by granting equitable remedies. It is essential to identify the nature of an equitable interest or estate in order to determine:

- The nature of rights to property
- The nature of any litigation which may be necessary to defend or pursue those rights
- Whether the rights are transmissible or assignable
- If so, what are the formal requirements for a valid assignment of that type of property in equity; and

- The obligations, if any, under revenue and other statutes: eg stamp duties, bankruptcy, taxation or conveyancing: (*The Trustees of the Estate Mortgage Fighting Fund Trust v FCT* (2000)).

The classification of equitable interests involves a two-stage approach:

- Is the right personal or proprietary?
- Where does it fit in the hierarchy of interests?

<p>Personal rights Personal rights are only enforceable against the person and do not attach to property: <i>National Provincial Bank v Ainsworth</i>. - <u>Personal rights give rise to personal equities</u></p>	<p>Proprietary rights Proprietary rights are those affecting property, giving a claimant an interest in that property or a right affecting it: <i>National Provincial Bank v Ainsworth</i>. - <u>Proprietary rights give rise to equitable proprietary interests</u></p>
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