

TOPIC TWO – Undue Influence and Unconscientious Dealing

Introduction

- In this topic, we examine two principles we will be looking at on unfair dealing: undue influence and unconscientious dealing
- Undue influence arose out of the deficiencies of the common law of duress
- In many situations, the coercion upon an individual to enter into a bargain was not sufficient to constitute duress because it did not amount to a threat of 'actual violence'
- The unconscientious dealing doctrine is a separate equitable principle focusing upon the unconscientious taking advantage of a recognised disability
- It is the first transactional fairness principle to exist entirely outside the contractual structure
- It is raised whenever it can be established that one party to a transaction has unconscientiously taken advantage of a disability in the other party which equity is prepared to recognise

Undue Influence

- Undue influence covers situations where an agreement has been obtained by certain kinds of improper pressure, including those traditionally thought not to amount to duress at common law because no element of violence to the person was involved
- The doctrine of undue influence looks to the quality of the consent, or assent, of the weaker party
- Wherever the relation between donor and donee is such that the latter is in a position to exercise dominion over the former by reason of the trust and confidence reposed in the latter, the presumption of undue influence is raised: **Dent v Bennett** in **Johnson v Buttress**

There are three ways undue influence can be made out:

1. Actual Influence

- In order to come within this category, it must be established that one party to the transaction was actually pressured by the other to enter into it
- Traditionally this category went further than the common law because the common law was restricted to threats relating to physical violence
- Now that the common law has developed a more flexible approach to include a broader range of threats, the similarity between duress and undue influence has increased
- Actual use of coercion in the form of a threat or proposal or violence that is illegitimate which influences a person to enter into a decision
- Actual undue influence requires proof that the transaction was the outcome of such an actual influence over the mind of the disponor that it cannot be considered to be the free act of the disponor
- To prove actual influence, detailed evidence about the negotiations, the relationship and the conduct of the other party is required

2A. Presumed Influence

- Some transactional relationships are presumed to have arisen from the undue influence exerted by one party
- In these situations, there is no need to show that undue influence actually existed because equity presumes it has occurred
- The dominant party then has the onus of disproving the presumption of influence

The presumption of undue influence arises out of particular relationships of trust and confidence:

1. Guardian-ward
2. Religious advisor-adherent
3. Doctor-patient
4. Trustee-beneficiary
5. Solicitor-client

6. Fiancé-fiancée does not attract presumption (**Thorne v Kennedy**)
7. Parent-child

-In regards to a parent having influence over a child, presumed influence may arise where a child transfers property to a parent: **Powell v Powell**

-The presumption ceases to apply once the child has become "emancipated" from the control and authority of the parent. That is a question of fact. The authorities are not consistent on the question of who bears the onus of establishing emancipation but probably the parent: **Lamotte v Lamotte**

-The presumption does not apply if a parent was to transfer property to a child: **Powell v Powell**

-A child is not presumed to have power over a parent

-More generally, the presumption arises whenever one party occupies or assumes a position that naturally involves influence over another

-Rationale: the recognised categories of relationship are marked by the characteristic that it is not natural to expect that 'one party would give property to the other. That is to say, the character of the relation itself is never enough to explain the transaction and to account for it without suspicion of confidence abused'

-Where a gift is given a category of persons it is presumed to be a consequence of undue influence

-Presumption may be rebutted by proof that the gift was the exercise of the donor's free will

-Need to discharge "the pure voluntary, well understood act of the mind of the donor": **Johnson v Buttress**

2B. Proven Influence

-Where there has been no actual pressure exerted in a relationship and, the relationship does not come within one of the category of 'presumed influence' relationships, it is possible that the relationship may still be held to be one of 'influence' where it can be proven that, in the circumstances, it was a relationship of trust and confidence which resulted in one party being placed in a position of influence over the other

-Whether a relationship can be proven to be one of influence will depend upon a careful examination of the overall character of the individuals involved as well as the circumstances of the relationship

-If a plaintiff successfully proves that a relationship is one of influence, the defendant must then prove that any benefit received has been given over as a result of the free, consenting and independent judgment of the plaintiff

Relevant factors to consider:

- Vulnerability
- Dependence
- Structural inequality
- Emotional or physical impairment
- Financial status
- Age and medical status
- Improvvidence of the gift
- Lack of independent legal/financial advice

Johnson v Buttress

-Buttress was 67, illiterate, had low intelligence, was dependent, needy and his wife had passed away

-Buttress transferred ownership of a piece of land to Johnson without receiving independent legal advice

-After Buttress' death, this transfer was challenged by his son

-The transfer was set aside

-Although there was no evidence that Johnson had actually pressured Buttress to make the transfer, there was an antecedent relationship between them because Buttress placed trust and confidence in Johnson and relied upon her for advice, which cast upon her the burden of proving

that she had not taken advantage of her position

- Johnson was unable to rebut the presumption because no independent legal advice was sought
- Need to discharge "the pure voluntary, well understood act of the mind of the donor"
- The transfer was set-aside on public policy grounds even though there was no proof of exploitation because no independent legal advice had been given

Rebutting the Presumption

-If there is a relationship of influence, presumed or proven, the onus will shift to the dominant party to prove that the impugned transaction was the independent and voluntary act of the claimant: **Powell v Powell**

-Need to discharge "the pure voluntary, well understood act of the mind of the donor": **Johnson v Buttress**

-Seeking independent legal advice is the best way: **Bester v Perpetual Trustees**

-Where independent legal advice is given the dealing will be difficult to impeach because free will is more readily apparent

-Mere fact of independent advice not determinative but an important factor in establishing other elements of undue influence

Consider:

- Was the advice independent?
- Was the advice sufficient – adequate to inform
- Did the donor, in light of the advice, act with free will?

-In **Bester v Perpetual Trustees**, advice given by a solicitor was found to be inadequate because the advice was given to a young girl who was inexperienced who merely read the deed and was asked if she had any questions. This was insufficient

"I am of the view, however, that such part as he played in connection with this settlement could not fairly be described as meeting that degree of independent advice that the plaintiff, as a person subject to a relationship of influence, was entitled to receive. Mr Emmanuel was, I accept, most careful to read the document through, and to invite questions of the plaintiff. But it was not textual advice upon the engrossment which was of prime importance in this regard: rather, it was advice upon the more general topic of whether a settlement should be entered at all and, if so, the general nature of the settlement, which in my view, ought to have been provided for the plaintiff"

Undue Influence and Third Parties

-Where undue influence has been exerted over an individual, compelling them to enter into a transaction, the transaction may not only be set aside against the person who exercised the influence, but also against any third party receiving a benefit from the transaction

-The most usual example of this is a bank guarantee

-Where a guarantor has been unduly influenced into entering into a guarantee for a loan, the bank will be unable to enforce that guarantee against the guarantor

-There are three separate principles applicable in this area:

1. Third Party Actual/Constructive Notice

-Where a third party receives actual or constructive notice that at the time the transaction was executed, it was executed with undue influence

-Where this occurs the third party cannot enforce the transaction

-Actual notice exists where the third party receives actual knowledge that undue influence has been exerted

-Constructive notice exists where the circumstances should have put the third party on inquiry

2. Third Party Agents

-A third party cannot enforce the transaction where the person who has exercised the influence is the agent of the third party

-The agency situation may arise where the third party has entrusted the 'influencing' party with the task of obtaining consent and execution of the document
-It must be established that the third party has actually requested the influencing party to act on their behalf—merely sending the documents may be insufficient
-A third party may not give actual authority to an 'influencing' party, but rather, give ostensible authority in circumstances where there is an external representation by the third party that the 'influencing' party is permitted to hold himself out as being associated within the third party's business—and having ostensible authority to act on behalf of the third party

-The third party financier will be affected by the equity if it appoints or holds out the debtor as its agent to procure the security under the ordinary principles of agency: **Alderton v Prudential Assurance Co Ltd**

-Whether an agency exists is a question of fact
-An agency relationship may be established in circumstances where the financier has entrusted the debtor with the task of obtaining the surety's
-If, however, the bank merely stipulates a need for a guarantee, and the debtor on its own account seeks to procure the support of a surety, characterizing the debtor as an agent of the bank may be artificial: **Ribchenkov v SuncorpMetway Ltd**
-Where no actual agency can be established, the fact that the creditor has entrusted the debtor to obtain the guarantee from the surety may, in combination with other factors, provide evidence that the financier was on notice of a relationship : **Bank of Credit & Commerce v Aboody**

3. Special Wives Equity

-The third situation in which a third party cannot enforce the transaction is where the guarantor is a wife and the third party bank or financier for the loan to the husband has not taken the time to explain the full consequences of the guarantee to the wife
-This is the principle which was first established in **Yerkey v Jones**, the validity of which has now been confirmed by the High Court in **Garcia v NAB**

The principle has been recognised as having two limbs (**Yerkey v Jones**):

The First Limb

-Where the consent of the wife to the instrument of suretyship is procured through actual undue influence by the husband, the wife will be entitled to set aside the instrument against the creditor unless the creditor can prove that the wife received independent legal advice
-In this context, actual influence must be established by the wife
-There is no need to prove that the creditor knew of circumstances surrounding the actual influence
-Proof that the creditor received constructive knowledge of the marriage relationship is sufficient

The Second Limb

-The second limb of the *Yerkey* principle will arise where, in the absence of actual undue influence, the wife fails to fully appreciate the effect of the instrument of suretyship
-In this situation, the wife may set the instrument aside against the creditor unless the creditor took steps to inform the wife about the transaction and reasonably believed that the wife knew what she was entering into
-It is not necessary for the creditor to prove that the wife was independently advised, as long as the creditor is reasonably satisfied as to the wife's comprehension of the transaction

A guarantee given by a wife may be set aside where:

- (a) 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, with notice that the surety was then the wife of the debtor, is 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 purpose and effect of the transaction to his wife; and
(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

-This limb will not apply if the wife is not a surety but a co-borrower and mortgagee as she will not be a volunteer: **Narain v Euroasia (Pacific) Pty Ltd**

Garcia v NAB

- Mrs Garcia (physiotherapist) and her husband executed a mortgage in favour of bank for purposes of securing guarantees under husband's business
- Husband assured Garcia there was no 'danger' in the transaction and no explanation of transaction was given by the bank
- Court found Garcia understood the nature of a guarantee generally, but not the extent of this particular guarantee
- Parties divorced and Garcia sought declaration guarantees void as a result of undue influence
- It was held that there was no actual undue influence under the first limb of special wives equity as Mrs Garcia signed willingly
- However, under the second limb it was found that the bank should have explained the guarantee to her

Relationships Other than Married Women

- Garcia v NAB**: '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'
- Eluded that the *Yerkey* principle could perhaps be extended

Ad hoc development:

- Held not to apply to a de facto relationship: **State Bank of New South Wales Ltd v Hibbert**
- Compare **Liu v Adamson**: de facto relationships involve same trust and confidence
- Applied to a guarantee given by parents and siblings of the borrower: **State Bank of New South Wales Ltd v Layoun**
- Held not to apply to parents guaranteeing adult child's business loans: **Watt v State Bank of New South Wales Ltd**
- Held not to apply to guarantee given by aged parent to child: **Permanent Mortgagees Pty Ltd v Vandenberg**

Permanent Mortgagees Pty Ltd v Vandenberg

- Son and mother (85 years old) joint tenants on property in WA
- Mother moved to WA to be with son
- Son purchased property with inheritance and borrowed another \$46000
- Further extension of loan following financial difficulties of \$143000 - which mother unaware of and did not benefit from
- Son was co-mortgagor with mother
- Son defaulted
- Bank aware that mother did not have independent legal advice
- Mother argued she was in a special equity relationship

Held:

- No extension of special equity relationship to mother/son relationship for three reasons
- First, assuming (without deciding) that the principles apply beyond guarantees, the mother was not a volunteer
- Secondly, the aged parent/child relationship is not of itself to be treated as equivalent to the

wife/husband relationship for the purposes of that doctrine

-Furthermore, even if the mother could be considered a volunteer by virtue of being designated a 'partial volunteer', and the principles apply to any relationship of trust and confidence, a claim based on Garcia does not improve the mother's position in these proceedings beyond her claim for unconscionable dealing, because without Mr Curia's knowledge, the bank had no notice that the mother reposed trust and confidence in the son in the transaction

-Noted that there was no 'direct suggestion' from Garcia that the relationship could be extended to guarantees by a parent for the benefit of a child

-Murphy J came to the specific conclusion that the burden of current authority would not support an extension of the Garcia principle by treating the relationship of aged parents and child as synonymous with husband and wife

-Did however apply unconscientious dealing and held bank to have imputed knowledge of this and therefore bank's acceptance and retention of the mortgage was unconscientious

Remedies

-Once undue influence is established, the usual relief sought is rescission in equity so that the parties can be placed, as far as possible, into the position they were in prior to the tainted transaction