CLE BANKING AND FINANCE LAW INTENSIVE

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SECURITIES CASE LAW – THE YEAR IN REVIEW

THE HON P de JERSEY AC, CHIEF JUSTICE OF QUEENSLAND

It is a pleasure, as always, to be part of the Continuing Legal Education "Intensives".

Last year at your Commercial Law Intensive, I commenced a similar securities review with a discussion of the then recent High Court decision of *Re Wakim (Re Wakim; ex parte McNally and Another* (1999) 163 ALR 270). The past year saw a number of judicial responses, or applications of that important case.

In *Matthews v ASIC* (2000) 170 ALR 149, the Full Court of the Federal Court confirmed that orders made *ultra vires* were not void, but merely voidable, capable of enforcement until set aside[i]. Mr Matthews had appealed against a decision finding him in contempt of Federal Court orders. Proceedings were commenced by ASIC under **s1324** of the *Corporations Law*, seeking that Mr Matthews be restrained from publishing securities reports on the internet, on the basis he did not hold the requisite investment adviser's licence. (Such a licence is issued under *Corporations Law* **s783**.) Interim restraining orders were granted by the Court. It was held Mr Matthews had contravened **s781**, in that, though unlicensed, he carried on a business providing investment advice, and held himself out as such an adviser. ASIC subsequently alleged Mr Matthews was in contempt of Court, continuing to publish securities reports on his website.

Mr Matthews argued that because of *Re Wakim* the Federal Court had had no jurisdiction to make the restraining orders, which were therefore void, and that the Court should set aside any orders in relation to contempt.

However the orders were held merely voidable, and not a nullity. The Court confirmed that until set aside, ultra vires orders remain enforceable. They bound Mr Matthews, and his infringement amounted to contempt. It was held further that it was incorrect to assume the Federal Court had not had jurisdiction. Establishing a ‘territorial nexus’ with a State or Territory was not necessary for alleged breaches of **s781** – the conduct there considered related to use of an internet site, which could be accessed throughout Australia. As such, the evidence had been sufficient to attract federal jurisdiction. The appeal was dismissed.

An attempt to find jurisdiction for the Federal Court in resolving *Corporations Law* disputes was considered by its Full Court in *Edensor Nominees Pty Ltd v ASIC* (1999) 168 ALR 676: whether, where “accrued” jurisdiction arose, the Federal Court had power to make orders pursuant to the *Corporations Law*[ii].

In this case, a takeover bid was made by Yandal Gold Pty Ltd for Great Central Mines Ltd. 94.3% of the shareholders accepted the takeover. However Yandal had failed to disclose that prior to the making of the bid, its principal shareholders, Edensor Nominees Pty Ltd and Normandy Consolidated Gold Holdings Pty Ltd, had entered into an agreement providing for a number of things including the bid’s conduct and funding facility, and the Great Central Mines board’s future structure. At the time, Edensor already held

12.56% of the shares in Great Central Mines, while Normandy held 27.81%, totalling 40 .37%.

ASIC challenged the takeover bid on the basis that the shareholders' agreement breached *Corporations Law* **s 615** – which prohibits the acquisition of shares in certain situations. It alleged that Yandal Gold had engaged in misleading and deceptive conduct in trade and commerce, contrary to *Trade Practices Act* 1874 **s 52**. Alternatively it claimed Yandal had contravened **s 12DA** of the *Australian Securities and Investments Commission Act* 1989, and *Corporations Law* **s 995(2)(b)** – that section outlaws misleading and deceptive conduct in connection with the making of takeover offers.

The matter was heard at first instance prior to the delivery of the High Court's judgment in *Re Wakim*. The primary Judge agreed with ASIC, finding the parties had contravened *Corporations Law* and *Trade Practices Act* provisions. The primary Judge's orders included that Edensor pay $28.5mil compensation to the Great Central Mines shareholders (excluding the respondents, of course).

Following the decision in *Re Wakim*, Edensor appealed to the Full Court of the Federal Court against the compensation order. It submitted this order depended on **s 737** (investor's right to reimbursement) and **s 739** (ASIC "stop orders") of the *Corporations Law*, both sections conferring power on "the Court" with a capital " C" , defined in **s 58AA** to include the Federal Court " when exercising the jurisdiction of this jurisdiction" (ie, of the State). Because *Wakim* made it clear that a State cannot confer jurisdiction upon the Federal Court, the reference to the Federal Court in **s 58AA** was of no legal force. That was the argument of the appellant.

The respondents submitted on the other hand that jurisdiction accrued to the Federal Court as a consequence of the claim under the *Trade Practices Act*, there being a single controversy or " matter". The court could exercise the jurisdiction of the relevant State under the *Corporations Law* to make orders under **ss 737** and **739** once it was seised of the matter under the so-called accrued jurisdiction. (Alternatively it submitted ASIC stood in place of the Crown, giving the Federal Court jurisdiction to make the orders by virtue of **s 75** of the Constitution, being the source of federal jurisdiction where the Commonwealth is a party.)

The Full Court of the Federal Court found that a common substratum of facts existed, conferring jurisdiction on that Court to decide the whole matter. However the orders were not *ipso facto intra vires* – the Court needed to determine the application of the **s 58AA** definition to the 'accrued jurisdiction' concept. Under the common law, the Federal Court, when exercising accrued jurisdiction, is considered to be exercising its federal jurisdiction. Under **s 58AA**, "Federal Court" is defined such that any jurisdiction it exercises under the *Corporations Law* must be <u>State</u> jurisdiction. The Court held the orders were <u>not</u> made under accrued federal jurisdiction, but State jurisdiction. Consequently, because of *Re Wakim*, the State jurisdiction could not be conferred on the Federal Court, and the orders were beyond power. (This also caused the alternative submission to fail.)

The Court then considered whether **s 22** of the *Federal Court of Australia Act* 1976 affected that conclusion. The section provides that in every matter before the Court, it should so far as possible determine <u>all</u> matters of controversy to avoid multiplicity of proceedings. Examining case authorities, the Court affirmed that **s 22** did not <u>confer</u> jurisdiction, but merely confirmed the power to deal with matters where jurisdiction already existed. **Section 22** did not aid the respondent, and the appeal was accordingly allowed.

Further challenges to the validity of the national corporations law scheme were made over the past year.

You may well be aware of such cases, and I will mention but briefly *Hughes* (2000) 171 ALR 155[iii], and *Bond* (2000) 169 ALR 607[iv].

Mr Hughes was a Western Australian businessman charged with *Corporations Law* breaches, who argued that no power existed for his prosecution by the Commonwealth Director of Public Prosecutions. He argued the Commonwealth and Western Australia *Corporations Acts* attempted to convert State law offences into federal offences – an exercise beyond the WA parliament's power.

His argument was rejected by the High Court, which found the State Act operated not to enact, but simply to apply certain "Commonwealth laws" in the State. One such law was the *(Commonwealth) Director of Public Prosecutions Act* 1983, which applies as a law of the State for the purposes of *Corporations Law* contraventions. The State *Corporations Act* then conferred on the Commonwealth Director of Public Prosecutions, really as persona designata, functions under the Commonwealth *DPP Act* in regard to State *Corporations Law* breaches.

This conferral of power on the Commonwealth DPP was held constitutionally valid. It did not amount to an abdication of State power. It was supported by the Commonwealth Act, which a majority of Justices found not only to permit, but to impose State functions on the Commonwealth DPP. While it was submitted by Mr Hughes that the alleged offences were unsupported by any head of power, the High Court found that with respect to the particular offences charged (relating to investment-making in the United States), the trade and commerce power (**s51(i)**) and the external affairs power (**s51(xxix)**) provided appropriate heads of power. The Court emphasised that an appropriate head of power needs to exist where functions affecting individuals' rights are purportedly imposed by the Commonwealth on its officers and bodies. The majority of justices indicated it might not be hard to find a relevant head of power in an individual case – for example, the scope of the incidental or "executive" power (**s 51(xxxix)**) is open to debate, and many offences may be supported by the trading and financial corporations power (**s 51(xx)**).

Mr Bond was sentenced on 5 February 1997 on his own plea of guilty. His offences related to his failure to act honestly when exercising the powers of a company officer, with 'intent to defraud the company and its shareholders'. He was sentenced on two counts to three years' imprisonment, to be served partly cumulatively, so that in total his sentence was four years' imprisonment.

The Western Australia Court of Criminal Appeal subsequently allowed an appeal against sentence by the Commonwealth Director of Public Prosecutions, resentencing Bond to terms of four years' and three years' imprisonment, to be served cumulatively. Bond appealed to the High Court, contending that the appeal was invalid – the Commonwealth DPP lacked the power to institute a sentence appeal. It was his argument that the legislation under which the DPP was proceeding made a distinction between the institution and conducting of prosecutions, and appeals. In effect the legislation reserved appellate capacity to the State.

The High Court agreed: the Commonwealth DPP indeed had no power to institute a sentence appeal. Under the *Commonwealth Director of Public Prosecutions Act* **s17**, a staff member of the office of the Commonwealth DPP could only be given power to <u>prosecute</u> for contraventions of the State law. A State law purporting to confer wider powers would be invalid for inconsistency with a Commonwealth law, to the extent of that inconsistency.

The appeal was allowed, the Court of Criminal Appeal's order set aside and the purported appeal dismissed as incompetent.

I turn now to *Barclays Bank Plc v Boulter* [1999] 1 WLR 1919, where the House of Lords dealt with the right of a surety to avoid liability through reliance on representations by a debtor or other person not an employee of the creditor, representations which have induced the guarantee. Specifically, need this surety have expressly pleaded the creditor bank had actual or constructive notice of the representation made by her debtor husband?

Mr and Mrs Boulter borrowed from Barclays Bank to purchase a house. They gave the bank a charge which secured repayment of both the loan for the house and all other moneys either or both may owe the bank. Mrs Boulter covenanted personally to repay all such sums. Mr Boulter later borrowed a further sum. The Bank demanded payment of him, and commenced proceedings against him when he failed to pay. The bank obtained a possession order, suspended on condition he repay the money by instalments. He again failed to pay, and the Bank obtained a warrant for possession.

Mrs Boulter asked the County Court to set aside that warrant for possession on the ground she had been induced to sign the charge as the result of undue influence and misrepresentation by her husband. Trusting him to deal with their financial affairs, she had accepted his assertion that the charge was to secure only the money borrowed for the house, not all other moneys which might be owed. No one had advised her to the contrary.

Mrs Boulter lost at first instance but succeeded on appeal to a Recorder. He set aside the order for possession, and she served her defence in the action. Her pleading failed to assert expressly that the bank had actual or constructive notice of the misrepresentation and undue influence. Lord Hoffman, with whose reasons the other members of the Court agreed, found that the pleading did allege facts which, if known to the bank, amounted to constructive notice. They were, simply enough, that Mrs Boulter was married to Mr Boulter at the material time, that they lived together as husband and wife, and that the charge was not on its face to her advantage.

While finding the pleadings here were technically adequate, his Lordship noted nevertheless that "[t]he purpose of the pleadings is to define the issues and give the other party fair notice of the case which he has to meet. Concealed and referential allegations do not perform this function." Ordinarily such allegations - that is, notice - must be pleaded specifically, but the absence of the plea was without moment, because it had been made "quite clear" at an earlier hearing that Mrs Boulter would be relying on constructive notice. The bank was aware of the case to be met, and indeed ready to address the issue of constructive notice.

And so the appeal was dismissed. The matter did not however end there. The Court of Appeal had held Mrs Boulter need not prove the bank had constructive notice - it was for the bank to establish the converse. The Court of Appeal had reasoned by analogy with the defence of a bona fide purchaser for value without notice: it falls to the purchaser to establish lack of notice to defeat a prior equitable estate or interest. Lord Hoffman found it a false analogy. The Bank directly took the charge from Mrs Boulter, who had the necessary title to grant it. In the case of the purchaser for value without notice, there is a pre-existing interest the purchaser seeks to displace. A better analogy is with the case of the purchaser of a chattel whose vendor's title is vitiated by fraud. Unlike the holder of a prior interest, the defrauded owner retains no title, and must prove that the purchaser had actual or constructive knowledge of the fraud. Relying on Lord Browne-Wilkinson's approach in *CIBC Mortgages Plc v Pitt* [1994] 1 AC 200, 210, Lord Hoffman held that for a wife to set aside a legal charge as against a bank for reasons of undue influence, she must establish that "in some way" the bank was "affected" by the wrongdoing of her husband. His Lordship held however that burden is easily discharged. A wife need show only that the bank knew she was a wife living with her husband and that the transaction was not on its face to her financial advantage.

The New Zealand Court of Appeal dealt with a similar situation in the case *Wilkinson v ASB Bank Ltd* [1998] 1 NZLR 674, considering banks' obligations where a debtor may have used undue influence to procure a guarantee from a relative.[v]

Here, Mrs Wilkinson, a newly widowed, elderly woman, long disabled by a psychiatric condition, signed a guarantee and mortgage over her house to support her husband's borrowings from ASB Bank. The moneys were borrowed for her husband's accountancy practice, and a family business in which she did not participate.

ASB's loan offer required Mrs Wilkinson to seek independent legal advice, and for the person providing that advice to confirm to the bank that Mrs Wilkinson had understood her obligation and liability when fully explained. This advice and confirmation were given by the family solicitor, Mr Clark, and the ASB made the advances. On the borrowers' default, the Bank obtained summary judgment against Mrs Wilkinson based on the guarantee. She appealed, arguing the guarantee should not be enforced as it had been procured by undue influence on her husband's part. She argued Mr Clark's advice had not been independent. He had been involved in both the accountancy and family practices' dealings over time as the family solicitor. Further, the bank should have been aware of the lack of independent advice, as it knew Mr Clark had acted for the principal debtors in relation to the loan, and was her husband's 'personal solicitor'.

When deciding the case, the New Zealand Court of Appeal noted a balanced approach should be adopted in such cases – the Court should not be swayed by particular sympathy for a 'victim' into the error of imposing upon lenders unrealistic standards.

The Court followed the House of Lords' principle in *CIBC Mortgages plc v Pitt* [1904] 1 AC 200, that a transaction procured by a husband's undue influence may be set aside against a bank where the bank actually knew or should have known of this. That is, where the bank knows that the guarantor has limited commercial experience, that the guarantor has but a minimal financial stake in the guaranteed enterprise, and that a relationship of emotional ties or dependence by the guarantor on the principal debtor exists. In such a case the bank must take 'reasonable steps to ensure the wife's agreement is properly obtained' for the transaction to be capable of enforcement. A prudent bank would, in the Court's view, insist on an independent solicitor giving advice to the guarantor, and certifying that the transaction's effect and implications had been understood when explained. The Court further pointed out the prudence of insisting the advice be given by someone unrelated to the other parties. A bank could not rely on a solicitor's certificate where that solicitor's independence was clearly compromised to an outside observer's eye. Furthermore, a bank would not be entitled to rely on what appeared to be independent advice where a transaction was 'so disadvantageous that no solicitor could properly advise a client to sign it'.

Here, the Court found ASB had known particular facts which should have alerted it to the possible role of undue influence in securing the guarantee and mortgage. Principally, the unusual suggestion had been made by Mr Clark that Mr Wilkinson sign the documents for his wife under a power of attorney, with no reference to her at all. (The bank had rejected this.)

However the Court noted ASB had insisted on independent legal advice from the very start, and that Mr Clark , who did not currently act for Mr Wilkinson, was sufficiently experienced for the Bank to believe him familiar with issues relating to conflict of interest. It would be reasonable to have concluded Mrs Wilkinson chose to receive advice from a person trusted by the family. The Court considered it misconceived to believe a solicitor's involvement to some extent with one party to a transaction, renders him incapable of independently advising another.

Here it was held an outside observer would not have perceived that a conflict of interest might well have existed. The Court saw the Bank's reliance on Mr Clark's certificate as justified. The appeal was dismissed.

A well known decision with apparently increasingly significant implications for parties entering into contractual arrangements is *Astley v Austrust Limited* (1999) 161 ALR 155, where the High Court held an award of damages for breach of contract cannot be reduced to reflect a finding of contributory negligence.

Austrust Limited carried on business as a trustee company, acting in deceased and protected estates, settlements, and for persons under disabilities. Having conducted such a business since 1910, it decided in the early 1980s to enter a new field. In August 1983 it wrote to Mr Astley, the senior partner in an Adelaide solicitors' firm, seeking general advice in relation to its acting as trustee of a trading trust set up to establish a piggery. The trust venture subsequently failed, and Austrust suffered substantial losses.

Austrust sued the solicitors alleging they were negligent in failing to advise that Austrust would be liable in dealings with third parties unless it specifically limited its liability under the trust deed to the extent of the trust assets. It further alleged that the solicitors' failure to provide that advice breached their contract of retainer with Austrust. The solicitors denied having been negligent, or that the scope of their retainer required them to provide such advice. They also alleged Austrust contributed to its own loss, in failing to investigate the venture's viability. They sought thereby to have any liability of their own reduced because of Austrust's contributory negligence, under South Australia's apportionment legislation, the *Wrongs Act* 1936 (SA).

The trial Judge found the solicitors negligent in failing to advise Austrust it would be personally liable in dealings with third parties unless it limited its liability to the extent of the trust assets. The Judge went on to find contributory negligence on Austrust's part, entitling the defendant to have the damages reduced "where the duty of care is the same in contract and in tort and both causes of action are pleaded." Under **s27A** *Wrongs Act*, the Trial Judge apportioned responsibility equally between the parties. The Full Court upheld Austrust's appeal against the finding of contributory negligence, holding that Austrust did not fail to give due consideration to its own interests because it had no reason to think they were at stake. It could not be concluded that Austrust, acting reasonably, ought to have known of that risk. Further, the risk of personal liability to which Austrust was exposed was the very risk against which Mr Astley, discharging his professional responsibility, should have protected it. The solicitors appealed to the High Court against that exclusion of contributory negligence.

The Chief Justice and Justices McHugh, Gummow and Hayne saw, as the points at issue, whether conceptually the plaintiff could be guilty of contributory negligence where the defendant contractually agreed to protect it from the very loss it suffered as a result of the defendant's breach of duty; and second, whether an award of damages for breach of contract could be reduced under apportionment of liability legislation such as **s27A** *Wrongs Act* 1936 (SA), because of contributory negligence, where the defendant was concurrently liable in tort and contract for breach of a duty of care.

The majority of Justices (Callinan J dissenting), found that while Austrust was indeed guilty of contributory negligence, it was entitled to recover for the whole of the damage because, having sued in contract, its damages award could not be reduced by reason of conduct constituting contributory negligence for the purposes of the *Wrongs Act*. This conclusion was drawn by the majority having regard to the history, text and purpose of the Act.

Having reviewed the point at common law, the majority Justices found that apportionment legislation would still operate "in respect of the contributory negligence of a plaintiff where the defendant, in breach of its duty, has failed to protect the plaintiff from damage in respect of the very event which gave rise to the defendant's employment." The conduct of the plaintiff is the focus of contributory negligence, the duty owed by the defendant being but one factor to be considered in determining whether a plaintiff has failed to take reasonable care of its own person or property. It was held on the unchallenged findings of the Trial Judge that Austrust was indeed contributorily negligent. The Justices found "not easy to accept" that "the officers of a trustee company in business for over 70 years believed that it could borrow more than a million dollars in its own name without any primary liability to repay the moneys". Austrust's actions failed to satisfy the objective standard of care required of a plaintiff.

Their Honours then considered the presently more significant issue, whether this contributory negligence required the apportionment of damages where the plaintiff sued in contract in circumstances where it could have sued in tort. Construing **s27A** of the *Wrongs Act* according to its natural and ordinary meaning, they held the section concerned claims in tort, not contract. This accorded with the history and legislative design of the legislation **-** "to remedy the evil that the negligence of a plaintiff, no matter how small, which contributed to the suffering of damage, defeated any action in tort in respect of that damage." Finally, turning to matters of policy, they noted that contracts are attributable to parties' wills, the risk under the contract generally being borne by the party whose breach is causally connected to the damage, while tortious liability is imposed regardless of the parties' wills.

The High Court therefore held the damages could not be reduced, and dismissed the appeal.

A further interesting decision relating to legal privilege is *Australian Hospital Care & Anor v Duggan & Ors* [1999] VSC 96 (31 March 1999). The issue was whether making a copy of a privileged document for a purpose other than obtaining legal advice, or use in legal proceedings, destroyed the privilege. This was the converse situation from that considered by the High Court in *Commissioner of Australian Federal Police v Propend Finance Pty Ltd* (1997) 188 CLR 501, where it was held that a copy of a non-privileged original document could achieve privileged status where made solely for the purpose of obtaining legal advice or use in legal proceedings.

The case arose out of a dispute over the sale of a diagnostic business. A Mr Beatty was appointed by the defendants to act as facilitator and negotiator in the possible sale. A term in his retainer specified that all information pertaining to the retainer and his clients generally was to remain confidential at all times, to be released to no party without the specific consent of his clients. The defendants provided him with copies of documents containing communications between the defendants and their legal advisers. The plaintiffs secured the issue of a subpoena for the production of these documents. The defendants objected on the ground they were protected by legal professional privilege.

The plaintiffs submitted that because the copy documents were supplied to Mr Beatty for a purpose other than seeking legal advice or use in legal proceedings, they did not themselves satisfy the test for legal professional privilege established by *Grant v Downs* (1976) 135 CLR 674. The plaintiff sought to rely on *Propend Finance*, arguing that the particular document in question (here the copy) and its communication had to be examined to determine whether or not it was communicated solely for a purpose attracting legal professional privilege.

Justice Gillard held that such an approach was not required by *Propend Finance*. His Honour saw the issue before the High Court as distinguishable, the former commencing with a document not privileged, and concerning the use of its copy, and the latter starting with a protected document and concerning the effect with respect to that privilege of first making a copy and then handing it to another.

His Honour held that merely copying a privileged document does not destroy the privilege which attaches to the original, and that is so regardless of the purpose for which the copy is made. His words follow:

> Privilege is concerned with communication whether oral or in documentary form. The person who has a document supplied to him by his lawyer in circumstances which makes the communication privileged from production or disclosure is entitled to use the document for his own legitimate purpose. If he makes a copy this does not lose the protection. To hold otherwise would mean emasculating the true object of the rule. In my opinion this conclusion accords with practical common sense giving effect to the policy underlying the privilege.

Justice Gillard found waiver alone would destroy the privilege. The plaintiffs argued that the defendants waived their privilege by providing the documents to Mr Beatty. Pointing out however that they were provided on a confidential basis for him to be fully informed and discharge his retainer in his clients' best interests, the Judge held no waiver, and the privilege survived unimpaired.

Discussing this case in the *Australian Banking And Finance Law Bulletin* ((1999) 15(2) 35), Mr Richard Leder sounds a note of caution. The decision, he argues, is inconsistent with the underlying principle in *Propend Finance*, in that while different factual questions arose, *Propend* advocated an approach focusing on the purpose of the creation of the copy, not the purpose of the communication contained in the document. *Duggan's* case having been decided on the latter approach, Mr Leder argues care must still be taken when copying privileged documents.

The High Court again considered the boundaries of legal professional privilege in *Esso Australia Resources Ltd v the Commissioner of Taxation* [1999] HCA 67, (1999) 74 ALJR 339, substituting for the previous sole purpose test, a dominant purpose test to be applied under the common law[vi].

In this case, Esso appealed to the Federal Court against amended income tax assessments. When discovery orders were made, Esso claimed documents had been made for the dominant purpose of legal advice, and were thus privileged – the broader test set out in the *Evidence Act* applying to discovery as well as adducing evidence. It was unsuccessful at first instance and on appeal to the Full Court. It then appealed to the High Court. While this court rejected the argument brought before the Federal Court, it reconsidered the existing common law test for legal professional privilege – the sole purpose test.

The sole purpose test had been favoured by the majority of Justices in *Grant v Downs* ((1976) 135 CLR 674), where the previously prevailing view, that legal professional privilege would attach to any piece of communication with merely one legal advisory purpose, was unanimously held too wide. In the present case, a 4 – 2 majority reconsidered *Grant v Downs,* finding instead that the dominant purpose test hitherto be the appropriate common law test in this country for legal professional privilege.

In a joint judgment, the Chief Justice and Justices Gaudron and Gummow held the sole purpose test too strict. Read literally, it resulted in the defeating of claims for privilege where one other additional purpose existed, regardless of its importance. Because of this extreme aspect, the test was being ‘watered down’ in some cases, also ‘diluting’ its supposed main advantage – that is, clarity.

The majority, including Justice Callinan, noted that the former test discriminated against corporations, whose internal communications are necessarily predominantly written. It was also noted the new test would beneficially bring into conformity the common law, the *Evidence Act,* and the common law of other jurisdictions. It would strike a just balance.

Accordingly, the appeal was allowed and the dominant purpose test is now the applicable common law test in this country for legal professional privilege.

In *Associated Alloys Pty Ltd v ACN 001 452 106 Pty Ltd* (2000) 171 ALR 568, the High Court held a retention of title clause could effectively be drafted so that the seller might, by way of trust, trace proceeds, in the buyer's hands, of sub-sale products manufactured from the goods sold[vii].

Previously, under the common law, a retention of title clause was generally seen as creating an unregistered charge over the buyer's book debts (thus registrable under s 262). Under s 266, this kind of charge would be void as against an administrator or liquidator.

This case arose out of a sale of steel. Printed on the back of the invoices was a retention of title clause, containing the following sub-clause:

> In the event that the [buyer] uses the goods/product in some manufacturing or construction process of its own or some third party, then the [buyer] shall hold such part of the proceeds of such manufacturing or construction process as relates to the goods/product in trust for the [seller]. Such part shall be deemed to equal in dollar terms the amount owing by the [buyer] to the [seller] at the time of the receipt of such proceeds.

The steel was used in manufacturing items on-sold to a company in Korea. Particular invoices remained unpaid. The buyer underwent voluntary administration, with appointment of a receiver and manager. It was then placed into liquidation. The seller claimed because of debt still owed, it was entitled to proceeds in the buyer's hands.

The High Court held that equitable principles permitted a retention of title clause to be drafted so that by way of trust, the seller could trace sub-sale proceeds. Here, under the sub-clause, the parties had agreed to form a 'trust of future-acquired property', and the sub-clause did not amount to a "charge", or a "registrable charge".

However the majority of Justices found against the seller, as it had failed to establish that existing funds were 'proceeds' for the purposes of the sub-clause. The seller had established the steel it supplied had been used in manufacturing on-sold items, but not that that particular steel and the particular on-sold items were linked. The appeal was dismissed on this factual consideration.

The South Australian Supreme Court decision in *Perkins v National Australia Bank Ltd* (1999) 30 ACSR 256 warns lending officers carefully to review loan facility documentation, in particular a borrower's constitution.

The action concerned whether two security documents were validly executed, available to be relied on by the defendant Bank to establish an entitlement as secured creditor. The plaintiff was the liquidator of the company Sparrow Green Pty Ltd. The company had borrowed substantial sums from the Bank under a loan agreement. At that time, the Bank required the execution of a number of documents. These included a debenture, which created a charge over all of the assets and property and undertaking of the company as security for the Bank's advances, and a Debtor Finance Facility Agreement.

The Liquidator attempted to set aside the loan agreement, contending those transactions were inoperative because the documents were not executed as required by the company's Articles of Association. The company's common seal was affixed to each document, but in the presence of but one director, where the signatures of two directors, or one director and the secretary were needed.

The company was incorporated with two directors, Sparrow and Green. In April 1997 it was agreed that Sparrow resign as director. But while he resigned as an employee on 30 June 1997, he did not resign as a director until 12 February 1998. In the interim period the company had two directors, but only one managed and controlled it. The relevant documents were executed in that period.

Green purported to sign as "sole Director and Company Secretary". Justice Debelle found Green did so believing he had the authority to act as a sole director, and intending to bind the company. However following the approach of Brennan J in *Northside Developments Pty Ltd v Registrar-General* (1990) 170 CLR 146 at 171, and the observations of Diplock LJ in *Freeman And Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 at 503-5, approved by the High Court in *Crabtree-Vickers Pty Ltd v Australian Direct Mail Advertising & Addressing Co Pty Ltd* (1975) 33 CLR 72 at 78, his Honour found Green had no actual authority to act on behalf of the company. Neither had he ostensible authority.

At the time the Bank entered into the lending transaction, it had knowledge of the company's Articles of Association. It knew that a minimum of two directors was required, and that the company seal was to be affixed in the presence of two directors or of one director and the company secretary. The Bank was held to have known that although Sparrow had intended to resign, he was still a company director along with Green. Referring to *Bank Of New Zealand v Fiberi Pty Ltd* (1993) 14 ACSR 736 per Priestly JA at 751, the Judge found that even if the Bank did not have actual knowledge that Green lacked authority to act as sole director, its connection with the company was such that it ought to have known.

At the time of this transaction, **s164(4)** of the *Corporations Law* provided that where persons are entitled to make certain assumptions when dealing with a company, those assumptions cannot be made where the person has "actual knowledge" that the basis for the assumption is incorrect. Having found the Bank had actual knowledge of the Articles of Association, the "indoor management rule" therefore could not apply.

Accordingly, the debenture and Debtor Finance Facility Agreement were held not to have been validly executed, and so the company was not bound by them.

An interesting case reported in the latest part of the Weekly Law Reports, *Crantrave Ltd v Lloyds Bank Plc* (2000) 3 WLR 877 answers the question: if a bank unwittingly and apparently discharges a customer's debt, but without the customer's authority – i.e. the payment from the customer's account is a mistake on the part of the bank, can the customer require the bank to reinstate the original balance? The English Court of Appeal says yes. This customer was subject to a judgment debt to X of ,150,000. X obtained a garnishee order nisi, on which the bank relied in paying X the balance of the customer's account, a sum of about ,13,500. But the garnishee order was not made absolute: it was stayed. The customer's liquidator asserted in substance that the bank had officiously intermeddled in the customer's affairs: the customer had not authorised the payment and it could not even be said that the customer's debt to X was pro tanto discharged. The Court of Appeal agreed. May LJ said this:

> Subject to particular banking arrangements, the customer of a bank is entitled to

> require payment to him by the bank of the full balance credited to his account. It is, in my view, obvious that the bank cannot, without the customer's authority or unless there is an obligation imposed on the bank by due process of law, unilaterally choose to pay money to a creditor of the customer and then reduce the credit balance in the customer's account by debiting the amount of the payment. If the bank purported to do this, the customer would remain entitled to require payment of the full unreduced credit balance. This would be a claim for payment of an amount to which the customer is contractually entitled, not a claim for damages for breach of contract. The customer does not have to prove a loss to justify requiring the bank to pay the full balance of his account … it was a gratuitous payment and the bank had no defence to the claim unless they established additional facts. No equity arises from the circumstances of the payment itself. The bank simply made a mistake. In another case, it might be possible to establish that the customer ratified the gratuitous payment either expressly or by taking advantage of it; or there might conceivably be circumstances not amounting to ratification in which it would nevertheless be unconscionable to allow the customer to recover from the bank the balance of his account without deduction of a payment which the bank had made gratuitously. (Pages 883-4)

An interesting query arises: obliged to reimburse the customer, could this bank have successfully recovered the amount gratuitously paid to X, from X?

I conclude with a rather unusual case, perhaps a little more in line with your banking law focus today, but which may offer some relief to lenders. In *Stergiou v Citibank Savings Ltd* [1999] FCA 1321 (24 September 1999), the Full Court of the Federal Court dismissed an appeal against an order for summary judgment in favour of the defendant Bank, in an action for damages for nervous shock, mental anguish, varied economic loss and medical and legal expenses allegedly incurred following the Bank's negligently debiting the first and second plaintiffs' bank account, consequently commencing legal proceedings, and taking possession of the first and second plaintiffs' property pursuant to a Court order. These two plaintiffs, who had mortgaged their property to the Bank, along with third, fourth and fifth plaintiffs who were other family members, and sixth to eleventh plaintiffs being related companies, sought to recover damages for a variety of psychological damage and economic loss, and contended the mortgage was discharged through the wrongful debits.

As the trial became protracted, summary judgment was sought by the Bank pursuant to court rules. Leave was granted to make this application, and summary judgment was entered. The trial Judge's discretion in granting an extension of time within which to bring the application was challenged on appeal, but no basis was seen for concluding the discretion to extend time had miscarried. The Court then examined the judgment with respect to each of the claims.

The trial Judge found neither the pleadings nor the evidence disclosed a cause of action at the suit of the third to eleventh appellants, the family members, and their appeals were dismissed. The first and second appellants' claim in connection with chattels, lost income and profits was also held unsupported by the evidence. The claim for a discharge of the mortgage failed on the basis it was simply not a remedy available to a mortgagor whose account has been incorrectly debited by a mortgagee. The trial Judge refused claims for damages for removal expenses, accommodation and the like, but invited the first and second appellants to re-plead their claims, noting that a claim to restitution might succeed. The Full Court upheld each of those rulings.

Significantly for the present, it was concluded at trial that whereas reasonable forseeability of psychiatric injury was an indispensable requirement of a successful claim for damages for nervous shock, "making wrongful debits or even instituting and maintaining the proceedings to recover possession of the property" could not give rise to such a foreseeable risk. The Court on appeal agreed, and held further that it was doubtful whether taking possession of property pursuant to a court order could give rise to a foreseeable risk of nervous shock. While the term "physical stress" had been used in the pleadings, it was accepted the plaintiffs sought to claim damages for psychological stress, but again not giving rise to a legitimate claim as it fell short of actual physical or psychiatric injury. "Damage to credit and social rating" was also found irrecoverable in an action in negligence, and in the absence of any allegation of actionable physical or psychiatric injury, medical expenses claimed were found not to be necessitated by actionable misconduct on the part of the Bank.

Having found no merit in the myriad of claims, the appeal was dismissed.

<u>Sources</u>

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[i] Drawn from *Butterworths Australian Corporation Bulletin*, 2000, No 7, [113]
[ii] Drawn from CCH *Australian Corporate News*, 2000, Issue No 1, p 1-3
[iii] Summary drawn from CCH *Australian Corporate News,* 2000, Issue No 10, pp 125-7
[iv] Summary drawn from *Butterworths Australian Corporations Law Bulletin*, 2000, No 6, [100]; CCH *Australian Corporate News*, 2000, Issue No 8, pp 101-3
[v] Drawn from a summary of this case by the Rt Hon Peter Blanchard, a Judge of the Court of Appeal of New Zealand, in a joint presentation with the speaker on "Recent Developments in Banking Law", at the 17th Annual Banking Law & Practice Conference, 9 June 2000.
[vi] Drawn from CCH *Australian Corporate News*, 2000, Issue No 4, pp 46-7
[vii] Drawn from CCH *Australian Corporate News,* 2000, Issue No 12, pp 155-6