CURRENT DEVELOPMENTS:
CURRENT ISSUES ON THE LAW OF GUARANTEES
RECENT CASE LAW

ALAN CAMERON

(Presented by JOHN KENCH)

Dawson Waldron
Solicitors, Sydney

Kennard v. AGC (Advances) Ltd, (1986) ATPR 40-747.

(a) The Facts

The Kennards owned certain property as joint tenants with their friends the Dempsters, the two groups holding as tenants in common in equal shares. In 1985, the Kennards and the Dempsters executed a second mortgage as security for money advanced by AGC to the Dempsters. The mortgage made both the Kennards and the Dempsters liable for a sum in excess of $1,000,000. It was alleged by the Kennards that an agent of AGC represented, both before the relevant documents were prepared and at the time of signing, that if they executed the security in question, it would not charge their interest in the land, nor would it make them personally liable to AGC. In essence, it was alleged that they were informed that the documents were required simply to enable the Dempsters to utilise their equity in the property to obtain the loan from AGC. In due course, notices of default were served both on the Dempsters and on the Kennards, and AGC sought to recover from the Kennards as well as the Dempsters.

(b) The Decision

The Kennards sought and were granted an interim injunction in the Federal Court restraining the exercise of AGC's powers under the mortgage. The Kennards also successfully claimed that AGC had contravened section 52 of the Trade Practices Act.

The effect of the mortgage was akin to a guarantee by the applicants. Pincus J, in language reminiscent of Amadio's case held:

> "The law is particularly careful to ensure that prospective guarantors are not in any way misled. The obligation goes to the extent of positively requiring disclosure 'where there

> are some unusual features in the particular case relating to the particular account which is to be guaranteed' ... Further, if the creditor should reasonably have known that the proposed surety was acting under a misconception, the guarantee is unenforceable if he did not dispel it."

In this case, not only was there a positive obligation to disclose the true effect of the guarantee, but it was held as a matter of fact that AGC's agent actively misled the applicants. Pincus J continued:

> "It is my opinion that, in the circumstances, the respondent was under an obligation, if it wished to enforce the transaction against the applicants, positively to draw their attention to the fact that (contrary to any reasonable expectation) the request that they lend their names to a mortgage to enable access to the ... property as further security had led to the preparation of a document putting at risk not only their interest in the ... property, but all their assets.
>
> It is my view, then, that the applicants are entitled to succeed on the basis of the misleading statements made by (AGC's agent) ... and also under the general law as to guarantees."

The Court also considered the claim for rectification, and held that the first respondent knew or ought to have known that the applicants were under a misapprehension as to the nature of the document they were being asked to sign, and the effect of the document, and were thereby entitled to relief by way of rectification.

Bawn v. Trade Credits Limited, Australian and New Zealand Conveyancing Report - September 1986, page 709.

(a) The Facts

Mrs Bawn was a director of a company in which she held 375 shares and her husband held 2,625 shares. She owned the matrimonial home and a commercial property, and was a woman of substance. In 1981, Mr Bawn became interested in the development of land he owned in Brisbane, as part of a venture with others. She was reluctant to participate, but he would not accept her resignation as a director of the company. In 1982, she was asked to sign documents including a personal guarantee and a collateral mortgage in relation to a loan exceeding $3 million. She was not made aware of what she was signing. When it was subsequently sought to enforce the guarantee and security, she instituted proceedings asking that the guarantee be declared not to be binding on her, on the grounds that it was entered into as a consequence of undue influence, or due to misrepresentation, or because of unconscionable conduct.

(b) The Decision

Needham J held that Mr Bawn did mislead her as to the nature of the documents, and that he "exercised upon her will a considerable influence". She was accepting a liability for $3.5 million plus interest, for a project in which her potential share was 4.16 percent, and it was a reasonable inference that, without her guarantee, the project would not have begun, because it was she who provided financial strength greater than the properties themselves and the other personal guarantees.

Among the "many remarkable features" in the case, the learned judge noted that Mrs Bawn was not personally involved in the negotiations, and that Trade Credits had no contact with solicitors for the guarantors "except with" solicitors for the venture. He continued:

> "They carried on practice in Brisbane, while the plaintiff lived in Sydney. By forwarding the unexecuted guarantees to the solicitors for the joint venture and requiring those guarantees to be executed by, inter alia, the plaintiff, the defendant was content to leave it to the borrowers to obtain a guarantee from the plaintiff, a guarantee which was, on its face, and to the actual knowledge of the defendant, an improvident transaction. The defendant knew that the plaintiff's assets did not cover the proposed debt, and so must be taken to know if they proceeded solely against her under her guarantee, she would lose all her assets, including her home. They made no enquiries as to her interest in the project. They made no enquiry as to whether the document had been explained to her or as to whether she had obtained separate advice. The question to be answered is whether the defendant, in such circumstances, may enforce against the plaintiff a guarantee extracted from her pursuant to the misrepresentation of her husband and in such circumstances that, had the document been one as between the plaintiff and her husband under which he benefited at her expense, it would have been set aside."

His Honour referred in some detail to the similarities between Amadio's case and the facts in this matter. He referred in particular to the fact that the "omission to make further investigation into the matter, once the primary fact appears, cannot excuse the creditor" and to the fact that "it is sufficient ... if it appears that there was an opportunity for the exercise of undue pressure, a lack of proportion in the benefits and detriment to the guarantor and the lack of any evidence of explanation or independent advice."

Other Recent Cases

General Credits Limited v. Ebsworth, (1986) 1 QdR 162.

In this decision of the Full Court of the Supreme Court of Queensland, the appellant sought to set aside a consent order

under which she had consented to judgment for a sum of around $44,000.00. She now claimed that she had been induced to consent to the judgment under a mistake, made by her solicitor as to liability under the document, when she had signed personally, although it had been prepared with respect to her mother-in-law. The court refused to upset the consent order on the basis that the only relevant mistake was that of the appellant herself, which occurred without the knowledge or complicity of the respondent, but the question of any liability that the solicitor might have to her for the advice that she had no defence to the claim against her on the document itself, was left open.

In the course of its judgment, the Full Court, although only obiter, described the alleged advice given by the solicitor that the appellant had no choice but to consent to judgment, as incorrect.

> "The mere circumstance of the appellant's signature on the guarantee could not be conclusive of her liability upon it. No doubt it is true to say that the signature of the party charged ordinarily imports personal liability: Leadbitter v. Farrow (1816) 5M of S.345, 349; 105 ER 1077, 1079. There are, however, strong indications in this instrument of guarantee - which an ordinarily prudent solicitor would have immediately appreciated - that the appellant was signing only as agent for Mrs E.M. Ebsworth. In particular it is Mrs E.M. Ebsworth, not the appellant, who is named as surety, and it is her name which appears in typescript opposite the position apparently intended for signature."

Australian Bank Limited v. Stokes, (1985) 3 NSWLR 174.

While only indirectly a case with respect to guarantees, this case is of some interest because it deals with the circumstances in which relief might be denied under the New South Wales Contracts Review Act because the transaction complained of is "in the course of or for the purposes of a business carried on by a particular person". The bank sought possession of certain premises owned by the defendants. The defendants had mortgaged the premises to secure liabilities entered into by a proprietary of company which they were the owners. The Contracts Review Act would clearly have not applied to the original borrowing, as it was by a corporation. The question was whether the guarantee given by the individuals, was excluded because it was entered into in a course of or for the purposes of trade. Rogers J said:

> "It seems illogical in the extreme that Parliament should have excluded, from the purview of the Act, relief to a two dollar company which is carried on by the corner grocer and to the grocer carrying on business in his own name, yet if that grocer carries on business in the name of the two dollar company and then gives a guarantee in respect of the business of the company, on the face of it he is not carrying on business for the purposes of section 6(2) and

> the Act operates in relation to a guarantee. With the most profound desire to pay deference to the Parliamentary intention, I must say that I am confused. I cannot identify the clear strand of reasoning which will allow me to give the provision the purposive interpretation that I am called upon to give it. There are difficulties ... of working out what is meant by the expression 'carried on by him'. Does it mean that the person in question has to hold 100% of the shares, 50% of the shares or a controlling interest? Does it mean that the person has to have a beneficial interest in the entity at all? The trading trust which may be carried on for the benefit of discretionary beneficiaries is but one example of the difficult type of situation which one would have to confront if one were to depart from the strict separation of entities commanded by the decision in Salomon v. Salomon. If I may say so with the utmost deference, these difficulties do not seem to have troubled or found a reflection in the judgment of McLelland J. in Toscano v. Holland Securities Pty Limited (1985) 1 NSWLR 145. His Honour was apparently content to accept the view that in circumstances such as the present and those which obtained before him, if the business is carried on in the name of the company then that is the end of the matter. Because of the difficulty of ascribing a clear Parliamentary intention to section 6(2) and because of the real difficulties which I think would be occasioned by departing from the prima facie effect and words of the sub-section, I think it is appropriate to hold that the meaning to be given is the one which appears on its face and which was the one adopted by McLelland J."

Comments

My role is to introduce some of the recent cases and raise some issues. The comments which are to follow from others will be with regard to the way in which the cases need to be taken into account in practice. I will therefore restrict myself only to the following comments:

Kennards' and Bawn's cases are very much cases in which the learned trial judges were responding to unusual and, it is hoped, extreme factual situations. One wonders what formal precautions taken in such cases would have produced a different result, and therefore vigorous adherence to guidelines may not always save a financier if extreme facts arise.

The growing extent to which the Trade Practices Act will be relied upon to supplement common law ought not to be overlooked. In addition to Kennards' case, there have been other recent cases in which the Trade Practices Act has been successfully relied upon in financial transactions, including Eltran Pty Ltd v. Westpac Banking Corporation (1986) ATPR 40-738 and Morenita Pty Ltd v. AGC (Advances) Ltd and another (1986) ATPR 40-689, as well as further cases under the New South Wales Contracts Review Act,

such as West v. AGC (Advances) Ltd and others (1986) ASC 55-500. Cases under the Trade Practices Act in particular pre-date the introduction of section 52A dealing with unconscionable conduct. There is no reason to believe that section 52A does not apply to lending transactions, although there may be some interesting questions as to whether very large multi currency facilities with new fangled options and devices ought to be characterised as "services of a kind ordinarily acquired for personal, domestic or household use or consumption".