THE NECESSITY FOR BANKERS TO ACT REASONABLY AND FAIRLY IN DEALING WITH CUSTOMERS

Comment by

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I wish to address the problems arising out of the Commercial Bank of Australia v Amadio decision and a couple of other similar cases, where banks have lost the benefit of guarantees because of their conduct. It is important to note at the outset that in none of those cases was the bank concerned said to be acting dishonestly. It lost the benefit of guarantees because of the application of various principles which I will get to in just a moment. I think the point to come out of the cases is that perhaps a greater degree of care with procedures will be necessary for bankers in the future.

The Amadio case was mentioned yesterday evening, and the facts were adverted to then. I don't have time to go through them again. You may recall that the decision was that the guarantees and the supporting mortgages were set aside on the equitable principle of unconscionable dealing.

The court decided that the guarantors in that case, were under a special disability which was known to the bank, and it was unfair that the bank took advantage. Disability in this context is not a disability in the legal sense, but merely a lack of adequate understanding as to what was involved in the transaction, and that the transaction was contrary to the interests of the guarantors.

The principle was expressed in the case as being that the equitable doctrine will apply where a party is under a special disability in dealing with the ot'er party, so that there is no reasonable degree of equality, and that the other party is aware of the disability, and it would be unfair or unconscientious to accept the assent given by the weaker party.

The transaction will be set aside unless the stronger party, in this case the bank, can show that the transaction was fair and just and reasonable.

There are no specific guidelines as to what is necessary to establish the disability. In the Amadio case itself there were a range of factors which included the age of the guarantors, the

lack of good English, the lack of knowledge of the serious financial position of the debtor, and failure to appreciate the extent of the guarantee both as to duration and quantum.

The court made it quite clear that the relief which was given, was given under that equitable principle, and not on the basis of undue influence.

The court also looked at the requirement for disclosure and effectively followed a long line of authority, which included the High Court decision in Goodwin v National Bank of Australasia, that the person intending to take a guarantee is under a duty only to disclose to the intending guarantor, facts which are unusual or would not have been anticipated by the intending guarantor. There is no general duty of disclosure. It is not a contract of utmost good faith. You only need to mention anything which is out of the ordinary.

The Chief Justice considered that the failure to make disclosure in fact amounted to a misrepresentation, which would invalidate that guarantee on contractual grounds.

The Amadio decision was recently followed by the Supreme Court of New South Wales in National Commercial Banking Corporation v Roberts, where judgment was given earlier this year. In that case relief was granted to a woman and her daughter. The woman was in fact involved in the company, she became a director, but that was reasonably late in the piece. She had a reasonable degree of financial information as to what the company was doing and the problems it was under, although she can probably be described in some ways as a bit of an innocent, in that she didn't quite understand some of the ramifications.

Relief was granted to both the woman and her daughter, the daughter having been induced to sign a guarantee and give a supporting mortgage, on this equitable principle of unconscionable conduct. Relief was also granted to the daughter on the basis that there had been inadequate disclosure of the surrounding facts, Again applying the equitable principles, the court decided that if the daughter had known the facts as to the financial position of the debtor company, then she would have been unlikely to have given the guarantee.

One other point which had been raised in argument was whether or not there was a fiduciary obligation. The court didn't consider that it was necessary to decide this matter because it was already granting relief.

The disabilities in that case are quite interesting. It does expand, in my view, the extent of Amadio's decision. Amadio was not novel, it was in fact applying a quite well established principle. But I think there is an encroachment on freedom of people to make fools of themselves. The disability was that neither guarantor really knew exactly what was involved in the giving of a guarantee, and didn't have a proper commercial appreciation.

This was despite the fact that the mother had reasonable knowledge of the company. She had in fact been advised by one of the other directors of the company, and the company's own solicitor, before she actually granted the guarantee, that she would be silly to give the guarantee.

The court didn't reject the evidence that the bank manager had in fact told her that she should seek independent legal advice, nor did they reject the fact that the bank manager had said that he had carefully explained the consequences of the transaction to her. So it was actually, in my view, a reasonably onerous decision for the bank.

Clearly the court was trying to do justice in those particular circumstances. There was at least one encouraging statement; that if the bank had made it quite clear to the person that they needed independent legal advice and that there was independent legal advice given, such that the person knew exactly what they were doing, it wouldn't really matter that the person was foolhardy in giving the guarantee.

The next case I want to mention, and fortunately it is the last, is National Westminster Bank v Morgan. This is a decision in 1983 of the English Court of Appeal, which considered the issue of undue influence.

What occurred in that case was that a lady had been induced to give a guarantee and supporting mortgage. The bank manager actually attended her home while the husband was present although the woman had no confidence in her husband's business acumen. There was no suggestion that there had been a long term relationship between the bank manager and the wife such that it gave rise to a duty of "confidentiality", as the relationship of confidence was referred to in that case. It was held that on the particular facts that a single meeting at the woman's home was sufficient to give rise to a degree of confidentiality which imposed on the bank a duty to ensure that there was no undue influence.

There wasn't a long term relationship where the woman looked to the bank manager as a confidant but merely one single meeting, but still the bank was held to be in a position of owing a fiduciary responsibility because the woman was relying on the bank manager as an adviser.

The case is interesting in that it establishes that it is not necessary that the contract be onerous or that there be an inequality of bargain for the other party to be able to get out of the contract. In fact, the giving of the mortgage advance by the bank was probably beneficial to the wife and her husband, because it saved them from a mortgagee's sale by the building society. But that factor was set aside on the basis that that was not a material consideration. Once you have the relationship of confidentiality, there is a suggestion of undue influence, and the bank can only discharge that by establishing that the person has been independently and properly advised and is able to make an informed decision.

So if I can just summarize; the upshot, I think, of all those cases, is that banks, particularly in taking guarantees but also possibly in taking other securities, will really need to be far more careful in making proper disclosure of the surrounding facts to the person giving the guarantee or security and ensuring that that person is making an informed decision. This will usually require independent legal advice unless the particular person is a sophisticated investor or a commercial person. I think you will need to be able to show that the degree of independent advice received and the state of mind of the person giving the guarantee or security is such that it is, in the words of Amadio, "fair, just and reasonable", and in the words of Roberts, "fair, just and equitable", that the transaction be upheld.