Bond Law Review

Volume 9 | Issue 1 Article 4

1997

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Abstract
A succession of cases has come before the courts in recent years involving women seeking to set aside secured guarantees given to support the debts of family businesses controlled by their husbands. The legal treatment of guarantees is dichotomous. Where a guarantee is provided for personal or domestic purposes recent consumer credit law reforms have ensured that financiers abide by a common set of rules when entering into the transaction. Guarantees to support business debts are still largely governed by common law principles and some statutes of general commercial applicability. There is a need for law reform to close the 'business guarantee gap' and provide uniformity of treatment for all guarantors. This article examines the treatment of business guarantees, noting the impact of some recent important decisions and law reform proposals.

Keywords
business guarantees, wives

This article is available in Bond Law Review: http://epublications.bond.edu.au/blr/vol9/iss1/4

WIVES, BUSINESS DEBTS AND GUARANTEES

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A succession of cases has come before the courts in recent years involving women seeking to set aside secured guarantees given to support the debts of family businesses controlled by their husbands. The legal treatment of guarantees is dichotomous. Where a guarantee is provided for personal or domestic purposes recent consumer credit law reforms have ensured that financiers abide by a common set of rules when entering into the transaction. Guarantees to support business debts are still largely governed by common law principles and some statutes of general commercial applicability. There is a need for law reform to close the *'business guarantee gap'* and provide uniformity of treatment for all guarantors. This article examines the treatment of business guarantees, noting the impact of some recent important decisions and law reform proposals.

Introduction

The issue of vulnerable guarantors who mortgage their interest in the family home as security for their guarantee is a longstanding problem. The succession of cases which have come before the courts in all Australian jurisdictions in recent years indicates that the problems which arise when guarantees are given for reasons of emotional ties or dependency are almost invariably faced by women, and in particular by spouses.

The issue has been the subject of several persuasive and useful reports[1]. The finance industry has responded to the concerns of the reform bodies, as well as to judicial pronouncements about the circumstances in which a contract of guarantee will be set aside. Consequently, improved lending procedures and practices surrounding the taking of guarantees have been progressively implemented, at least by the mainstream lenders such as banks, building societies and credit unions. The process of self-regulation based on the implementation of

1 Australian Law Reform Commission Report No.69 (1994) Part II, *Equality before the law: women's equality* , Trade Practices Discussion Paper (1992), *Guarantors: Problems and Perspectives*, Report of the Expert Group on Family Financial Vulnerability (1996), *Good Relations, High Risks: financial transactions between family and friends*.

the Code of Banking Practice[2] and the Australian Banking Industry Ombudsman Scheme 'ABIO', as well as statutory intervention through new uniform consumer credit legislation[3], have provided useful benefits for some guarantors. These recent reforms have, in the main, been ‘consumer’ reforms. If a spouse provides a guarantee in circumstances where the principal loan is for a predominantly 'personal household or domestic nature' there is now in place a framework of protective pre-contractual and on going requirements[4].

Unfortunately, the benefits of the recent reforms are not available all guarantors. Experience has shown that the many of the cases coming before the courts involve wives seeking to set aside guarantees provided to support the business debts of their husbands. The debts may have been incurred directly by the husband or by a company substantially controlled by him. In the latter case, the guarantor wife may have been a co-director in the company. Problems may arise where the wife is a non-executive director acting in a 'signing purposes' only capacity[5]. If the business becomes financially distressed and the lender seeks to enforce the guarantee against the wife, under the present legal framework she must demonstrate some form of misconduct on the part of the lender, in order to avoid the guarantee and the possible loss of the family home. Lack of financial information, of comprehension and of independent advice do not of themselves provide a basis at common law for setting a guarantee[6]. Given that these factors are present in many of the cases coming before the courts, it is evident that the process of law reform in the context of guarantees of business debts requires a preventative focus. Establishing workable rules for pre-contractual and on-going information disclosure applicable to all guarantors should be at the heart of the reform process.[7] To achieve this objective there is a compelling need for *uniform* statutory reform. The aim of this paper is to outline the existing avenues of legal redress for spouses who have entered into improvident guarantees of their husband's business debt in order to:

- demonstrate how some recent decisions applying equitable doctrines probably detract from, rather than assist the position of vulnerable women guarantors; and

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2 Which, along with parallel Credit Union and Building Society Codes, came into full effect on 1 November 1996. The full implementation of the Codes was delayed to coincide with the introduction of the new Consumer Credit Code.

3 The Australia-wide Consumer Credit Code came into effect on 1 November 1996. The Code was passed as template legislation in Queensland in September 1994 and has been substantially applied by each State and Territory as local law.

4 Under the uniform Consumer Credit Code Part 3, Div 2 (ss 50-57) and the Code of Banking Practice, Clause 17.

5 Prior to the amendment to the Corporations Law made by the *First Corporate Law Simplification Act* 1995 (Cth.) it was mandatory for proprietary companies to have a minimum of two directors.

6 See, for example, *Akins v National Australia Bank* (1994) 34 NSWLR 155.

7 As recognised by the reform bodies. See fn 1.

- evaluate recent reform proposals which aim to cover the 'business guarantee' gap.

The recent trend of the New South Wales Court of Appeal to subsume existing principles of relief from unfair and improvident guarantees within the '*Amadio*'[8] doctrine of unconscionability necessarily bears close scrutiny. As will be seen, a close analysis of the application of the doctrine will reveal its limitations as a generalised remedy in the business debt context.

Women's Issues ?

It may well be questioned why, in these times of apparent gender equality, the issue of unfair guarantees regarded as essentially a women's issue. In fact, there is no reason why the problem necessarily only effects female spouses. The Australian Law Reform Commission 'ALRC' recognised that while problems concerning improvident, emotionally motivated guarantees, overwhelmingly affected women, it looked at guarantees in the context of 'sexually transmitted debt', which was defined as:

> ...the transfer of responsibility for a debt incurred by a party to his/her partner in circumstances in which the fact of the relationship, as distinct from an appreciation of the reality of the responsibility for the debt, is the predominant factor in the partner accepting liability.[9]

Theoretically therefore, both men and women may be the victims of sexually transmitted debt. In reality, the cases overwhelmingly involve either legal or de facto female spouses. Unfortunately, a stereotyped picture has emerged, in business guarantee cases, of the kinds of women who become victims of sexually transmitted debt.[10] Some features common to many of the guarantor wives include:

- Limited business skills, knowledge and experience;
- Limited involvement in the husband's business affairs;

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8 *Commercial Bank of Australia Ltd v Amadio* (1983) 151 CLR 447.

9 ALRC Report No 69, para 13.4.

10 The list of cases involving most, or all of these listed feature is compendious, but includes: *European Asian of Australia Ltd v Kurland* (1985) 8 NSWLR 192; *Akins v National Australia Bank* (1994) 34 NSWLR 155; *National Australia Bank Ltd v Garcia* (1996) 39 NSWLR 577; *Gough v Commonwealth Bank of Australia*, (1994) ASC 58,831; *Peters v Commonwealth Bank of Australia* (Unreported, NSW Sup Ct, Equity Division, Brownie J, No 4928/91, 26 Feb 1992); *Warburton v Whitely* (1989) NSW Conv R 58,283; *European Asian of Australia Ltd v Lazich* (1987) ASC 57,284.

- Leaving important business and financial decisions to the husbands. Even where the wife had some involvement in the husband's business or company it was generally limited to providing secretarial or book-keeping services;[11]

- A propensity to sign business documents, including security documents such as mortgages and guarantees, unquestioningly upon request by the husband. The failure to seek, or be provided with adequate explanations or advice about the nature and extent of the liability occurs frequently in cases where wives have signed unlimited 'all moneys' guarantees. An inability to understand the link between a guarantee and a mortgage supporting the guarantee was also a common feature;

- Limited education. In many of the cases before the courts the women concerned had not completed secondary education. Even where a higher level of education had been obtained it did not include relevant business accounting or legal skills necessary to redress the obvious imbalance between the spouses so far as business matters were concerned;[12] and

- Marital problems.[13]

The situation is not as bad as it appears !

Although not all of these features are evident in every case, their frequent occurrence gives rise to serious doubts about the degree of advancement of women in society. Clearly, one of the problems occurring in a significant number of the cases coming before the courts is an acute informational disparity between the guarantor spouse on the one hand and the husband and/or creditor on the other. Obviously, lack of information is not the only reason that wives enter into improvident guarantees. Reasons for the general lack of empowerment of women have been addressed by the reform bodies, and in particular by commentators on feminist issues.[14] Implementing suggested law reform proposals, such as

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11 See, for example, *Gough v Commonwealth Bank of Australia* Ibid; *Commonwealth Bank of Australia v ABC Property Planners Pty Ltd*, (Unreported, NSW Sup Ct, Cohen J, No 1450/89 25 May 1991).

12 The guarantor wife in *Garcia* was a physiotherapist, in *Peters* a school teacher, and in *Kurland* she had a science degree.

13 In the cases of *Garcia*, *Peters*, and *Akins*, noted above at fn 10.

14 See, e.g., Baron P, 'The free exercise of her will: women and emotionally transmitted debt', 1995 (13) *Law in Context* 23; Howell, N., 'Sexually transmitted debt', 1995 (4) *Australian Feminist Law Journal* 93.

improved disclosure and independent advice, will be of little avail in cases where a wife feels emotionally compelled to act as a surety. The issue of socially dependent relationships is a difficult one for law reformers to deal with.

Fortunately, however, problems associated with pre-contractual conduct and disclosure may not be quite as serious as the cases seem to indicate. Many of the actions commenced prior to the banks and other financial institutions improving their procedures for the taking of guarantees. Even though recent developments such as the Banking Code and new consumer credit legislation have been targeted at 'consumer guarantors', a flow on effect benefiting all guarantors can probably be expected. Moreover, given that relief is more likely to be granted where the wife presents as vulnerable and lacking business or educational skills, the preparation of a successful case often depends on presenting a skewed picture of both the guarantor and the circumstances surrounding the guarantee transaction. Serious problems are still evident in this area of the law, but things are not as bad as they seem!

Avenues of legal redress

A wife who has entered into an improvident guarantee of her husband's business debts may later seek to have it set aside on a number of grounds. These include:

- The equitable doctrines of unconscionable conduct and undue influence;
- The principle in *Yerkey v Jones*;[15] and
- Reliance on statutory remedies such as the *Trade Practices Act 1974 (Cth.)* ('TPA') and the *Contracts Review Act 1980 (*NSW) ('CRA').

Additionally, the Banking Ombudsman may have jurisdiction to attempt a settlement or make an award of damages in some limited cases of guarantees of business debts.[16]

Invariably a wife seeking to resist enforcement of a guarantee asserts that she was ignorant of, or misunderstood the actual and potential liabilities of a

15 (1940) 63 CLR 649.

16 The ABIO's Terms of Reference cover cases where the dispute does not involve an incorporated body and does not exceed $150,000 (The limit was $100,000 prior to March 4, 1996).

guarantee and lacked the financial information necessary to make an adequate assessment of the risks involved. However, as an analysis of recent case law indicates, the existing remedies are limited in providing relief in such circumstances. Under the present legal framework it is extremely difficult for a wife to have a guarantee set aside on the basis that she was not fully informed of all material facts and lacked full comprehension of the nature of the transaction. In the case of business debts, the spouse will be relying on to a large extent on equitable principles for relief. While there is no doubt that important decisions such as *Amadio* influence financiers in relation to the provision of advice, explanation and information provided in the pre-contractual setting, this effect is indirect. It is the role of the courts of equity to redress wrongdoing, not to regulate information disclosure.

Unconscionable conduct

In Australia the jurisdiction in equity to set aside a contract on unconscionability grounds is firmly based on the well known High Court decision in *Commercial Bank of Australia Ltd v Amadio*.[17] According to Mason J[18] unconscionable conduct refers to:

> ...the class of case in which a party makes unconscientious use of his superior position or bargaining power to the detriment of a party who suffers some special disability or is placed in some special position of disadvantage.

There is no definitive list of 'special disabilities', but both Deane and Mason J J[19] derived some assistance from the passage in the judgment of Fullagar J in *Blomley v Ryan*[20] where his Honour identified some particular examples. These included:

> ...poverty or need of any kind, sickness, age, sex, infirmity of body or mind, illiteracy or lack of education, lack of assistance or explanation where assistance or explanation is necessary.

17 (1983) 151 CLR 447.
18 Ibid at 461.
19 Ibid at 462 and 475.
20 (1956) 99 CLR 362 at 405.

As some judges have observed,[21] being a woman and a spouse does not of itself place a person in the 'special disability' category or in the position where explanation, assistance or legal advice concerning the taking of a guarantee is necessarily called for.

Unconscionable dealing will only be established where two requirements can be satisfied.

- the guarantor is under some kind of disability (as explained above) at the time the guarantee was entered into; and

- the lender had actual or constructive knowledge of the guarantor's disability and was therefore unfairly abusing its dominant position vis-a-vis the guarantor.

Unconscionability is a very broad doctrine, applying to all types of unfair dealing, not just to guarantees. Its focus is clearly on exploitative conduct. The courts in New South Wales now regard the principles of unconscionability, outlined in *Amadio*, as providing sufficient grounds of relief for those seeking relief from unfair guarantees so that there is no need for guarantor wives to resort to the rule in *Yerkey v Jones*. This was recently confirmed by Sheller JA, delivering the leading judgment of the New South Wales Court of Appeal in *National Australia Bank v Garcia*.[22]. However, the evidence does not really bear out the view that the *Amadio* principles furnish adequate grounds of relief. On the contrary, it is very difficult for a wife to succeed in having a guarantee set aside on unconscionability grounds.

There are a number of reasons why it is very difficult for an *Amadio* based claim to succeed.

1. The 'special disability requirement'.

It is now well accepted that merely being a female and a spouse is not enough to establish a special disability. Nor is lack of full comprehension and understanding of the obligations and risks undertaken enough to establish a special disability. It was held in *Akins v National Australia Bank*[23] that a wife who was misled by her husband, had no understanding of, or involvement in the

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21 See, for example, *European Asian of Australia Ltd v Kurland* (1985) 8 NSWLR 192, at 200 per Rogers J; *Commonwealth Bank of Australia v Cohen* (1988) ASC 58,146 at 58,160 per Cole J; *Warburton v Whiteley* (1989) NSW Conv R 58,283 at 58,288 per Clarke JA.

22 1996] 39 NSWLR 577.

23 (1994) 34 NSWLR 155.

business affairs of his companies and signed a series of unlimited guarantees in ignorance of their true effect was not under a special disability. Clarke JA noted that the bank had acted in accordance with its usual practices, even though the explanation of the bank's officers were 'wanting in various respects'.[24] The wife had a broad general understanding of a guarantee[25] and this was enough.

Therefore, so long as a wife generally appreciates that a guarantee may entail some degree of risk to her property it seems she will not be in a position of special disadvantage by virtue of 'lack of education, assistance or explanation where assistance or explanation is necessary'.[26]

A common feature of unconscionability cases is the wife's claim of emotionally vulnerability and a consequent tendency to sign documents upon the husband's request without reading them. This will not usually be enough to establish a position of special disadvantage unless the vulnerability of the wife is such that her will is truly overborne and the decision to sign cannot be said to be a free exercise of her own will.[27]

2. The exploitative conduct requirement.

An essential condition of entitlement to relief is that the special disability is sufficiently evident to the stronger party. This is the most difficult element to establish. Even if a special disadvantage is proved, this is not enough. Exploitative conduct is required on the part of the lender, in that the lender knew, or ought to have known, of the guarantor's disability and unfairly sought to take advantage of that disability. Unfairness is manifested by a failure to provide assistance and explanations or recommend independent advice. There is a long list of failed unconscionability cases[28] where the court was unable to discern any evidence of actual or constructive knowledge of a special disability on the part of the lender.

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24 Ibid at 173.

25 Powell JA observed, at 178, 'at least in broad terms she understood'.

26 *Commercial Bank of Australia v Amadio* (1983) 151 CLR 447 per Deane J at 475.

27 As, for example, in the case of *Teachers Health Investments Pty Ltd v Wynne* (1996) ASC 56-357 where the husband engaged in blatant 'emotional blackmail' to secure his wife's signature to the guarantee.

28 See, for example, *Akins v National Australia Bank Ltd* (1994) 34 NSWLR 155*; National Australia Bank v Garcia* [1996] 39 NSWLR 577; *Peters v Commonwealth Bank of Australia* (Unreported, NSW Sup Ct, Equity Division, Brownie J, No 4928/91, 26 Feb 1992); *European Asian of Australia Ltd v Kurland* (1985) 8 NSWLR 192; *Warburton v Whitely* (1989) NSW Conv R 58,283*; ANZ Banking Group Ltd v McGee* (1994) ASC 58,928.

The courts are particularly reluctant to find that a lender is aware of a special disability where a wife presents herself to the lender in her capacity as a company director. In *Garcia v National Australia Bank Ltd*[29] the New South Wales Court of Appeal agreed with Young J, at first instance, who observed that an apparently articulate and intelligent lady called at the bank and appeared to voluntarily be signing a guarantee in favour of a company of which she was a director. His Honour held that in such circumstances it would be difficult to conceive how a lender could be said to be acting exploitatively in obtaining her assent to the guarantee or in failing to recommend advice. Similarly in *National Australia Bank Ltd v McKay*[30] Hansen J, in the Victorian Supreme Court, expressed strong doubts about the wife's alleged special disability but held that in any event the bank was not aware of any such disability nor taken advantage of it.

3. Scepticism about guarantee claims.

It is an unfortunate aspect of guarantee cases that, in order to succeed, the wife must necessarily be portrayed as subservient, disadvantaged and commercially illiterate. Ironically, the creditor on the other hand, will probably adopt a feminist position, that given the changing position of women in society it is inappropriate to assume that a woman is dependent or unable to make commercial decisions and think critically for themselves.

However, it is now apparent that the courts are becoming cynical about possible exaggerated claims of financial naivety. They are now, in some instances tending to be dismissive of 'Amadio defences'. In *European Asian Ltd v Kurland*,[31] a 1985 decision, Rogers J expressed his suspicions about the demeanour of the apparently well-educated wife saying that:

> I was suspicious that it was an assumed role for the purposes of the case. Rereading the transcript still left me uneasy.

Although Rogers J felt compelled to accept that the wife was in fact financially naive, the unconscionability claim in *Kurland* failed. In more recent decisions, scepticism about commercial illiteracy claims is becoming common. Judges are becoming concerned that such claims are being contrived for the purposes of the case[32] and they are less likely to be accepted where the wife is a company director with some involvement in the husband's business, albeit in a limited capacity.

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29 (1996) 39 NSWLR 577 at 598.

30 [1995] ATPR 40,534 at 40,545.

31 (1985) 8 NSWLR 192 at 198.

32 Concerns about the extent of the wife's financial ignorance were strongly expressed by Meagher JA in *Gough v Commonwealth Bank of Australia* (1994) ASC 58,831 at 58, 856 (a case decided under the *Contracts Review Act 1980* (NSW)) who observed that even though the wife had a very basic level of education, she was 'no gaping rustic'. See also *Commonwealth Bank of Australia v ABC Property*

4. Seemingly inconsistent decisions based on similar facts.

The rules for determining 'special disadvantage' and the circumstances in which a lender is put on notice of a special disadvantage on the part of the guarantor are certainly variable. It is sometimes difficult to reconcile different decisions based on similar facts. Thus, in *Warburton v Whitely*,[33] Kirby P concluded that the guarantor wife was under a special disability, describing her in the following terms:

> Mrs Warburton had no education past the Intermediate Certificate. She was absent from the workforce and business world for a substantial period whilst raising her children. She was always subordinate to her husband in their common business affairs. She took no part in the business affairs of the companies. She was unaware of her husband's business associations with the companies and with creditors in general. In sum, the evidence paints a picture of a woman in a significantly unequal position to her husband, at least in relation to business affairs and the incurring of debts.

However this was the dissenting view in the case. The majority judges, Clarke and McHugh J J A, disagreed with Kirby P's view[34] that Mrs Warburton was under a special disability. On the other hand, in *ANZ Banking Group Ltd v Heyward*,[35] a decision of the Tasmanian Supreme Court, a wife who could equally fit the description of Mrs Warburton outlined above, was held to be in a position of special disadvantage vis-a-vis the bank.

Very recently, in *Teachers Health Investments Pty Ltd v Wynne*,[36] the New South Wales Court of Appeal held that the wife was under a special disability because she was in a vulnerable emotional position and her husband had made numerous inducements and misrepresentations to her about his financial position. However, similar misrepresentations and the emotional vulnerability of a wife with a young family in *Akins v National Australia Bank*[37] were not sufficient to convince the Court of Appeal that the wife was under a special disability. Clearly,

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Planners Pty Ltd (Unreported, NSW Sup Ct, Cohen J, No 1450/89 25 May 1991) and *National Australia Bank Ltd v Di Battista* (Unreported, Vic Sup Ct, Nathan J, No 9856/92, 7 Dec 1995) where a claim of financial ignorance was totally rejected.

33 (1989) NSW Conv R 58,283 at 288.

34 Although Kirby P held the wife to be under a special disability, he concluded that her unconscionability claim failed as the disability was not sufficiently evident to the bank.

35 (Unreported, Sup Ct of Tas, Cox J, No A52/1994, 7 July 1994).

36 (1996) ASC 56-357

37 (1994) 34 NSWLR 155.

some fine and subtle distinctions are often made in applying the elements of the *Amadio* test.

Few Successful *Amadio* Cases

An analysis of the few successful *Amadio* cases indicates that the defence usually only succeeds in exceptional circumstances. It seems that the lender's conduct will generally only be regarded as unconscionable when there is a marked departure from the standards expected of a prudent and responsible financier which the courts perceive as blatant misconduct. Departure from the standards of fair and responsible dealing occur when the lender has actual or constructive notice of unfairness or invalidating circumstances and fails to take steps to redress them. The ALRC, noting the dearth of successful unconscionability cases in the guarantor wife context, reported that:

> Successful cases more often arise when where the professional and social relationship of the lender and borrower renders the guarantor's role in the complete transaction that of an ill-informed and sometimes unwilling participant.[38]

For example, in *Nolan v Westpac Banking Corporation*[39] the plaintiff wife was subject to overbearing tactics by a branch manager of the defendant bank. The plaintiff's evidence that on the day she signed the guarantee she was ‘stressed, agitated, cold wet and miserable’ and that it was patently obvious that she signed merely to get the transaction over with,[40] was accepted. It was held that the limited advice from a solicitor was merely of token value.

In *Guthrie v ANZ Banking Corporation*,[41] where a defendant bank took a guarantee, secured by a mortgage over the family home in the full knowledge that the guarantor wife had a serious drinking problem, was not on good terms with her husband and was reluctant to sign the documents, the bank's conduct was held to be unconscionable. The court reached this decision notwithstanding that the bank had advised her to obtain legal advice.

Unacceptable conduct on the part of the lender was also evident in *ANZ Banking Group v Barry*[42] where the Full Court of the Queensland Supreme Court considered that a defence of unconscionability was possible where the bank manager displayed ‘reckless misconduct’ in not explaining the full effect of the documents in circumstances where the plaintiffs explained they needed more time as they did not have their glasses to read the documents.

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38 Report No.69 (1994) Part II, *Equality before the law: women's equality*, para 13.19.
39 (1989) 51 SASR 496.
40 Ibid at 500.
41 (1989) NSW Conv R 58,349.
42 [1992] 2 Qd R 12.

The recent decision of the New South Wales Court of Appeal in *Teachers Health Investments Pty Ltd v Wynne*[43] also fits into the exceptional case category. Not only was the wife said to be in a position of extreme vulnerability by virtue of her husband's continuing dishonesty, frequent separations from the family and his overbearing tactics, but the lender was fixed with constructive notice of her disability. From glaring inconsistencies in the financial statements of his business, which were available to the lender, it should have been apparent that the transaction was entirely against her interests and called out for independent legal and financial advice.

Undue Influence

Undue influence is often raised as an adjunct to an unconscionability defence, although it is a conceptually distinct doctrine. Like unconscionability, a defence of undue influence is very difficult to establish. In *Amadio*,[44] Mason J observed that while unconscionable conduct bears some resemblance to undue influence there is a difference between the two. In cases of undue influence the will of the innocent party is not independent and voluntary because it is overborne. There is no overbearing of the will in cases of unconscionability, but rather a stronger party unconscientiously taking advantage of a special disability evident in the weaker party.

Cases of undue influence exerted by the principal creditor are very rare indeed and require proof of a special relationship of trust between the creditor and the guarantor.[45] There is no legal presumption that transactions between spouses are affected by undue influence. So a guarantor must overcome the difficult burden of proving that his or her will was overborne. Like unconscionability, there are few successful cases.[46] The lender's actual or constructive knowledge of undue influence will enable the guarantee to be set aside.[47] Actual knowledge on the part of the lender of undue influence which may have been exerted upon the wife is likely to be rare.

These days asserting undue influence on the so-called 'agency'[48] principle, whereby the husband is given the guarantee documents and obtains the signature

43 (1996) ASC 56-357.
44 (1983) 151 CLR 447 at 461.
45 *Lloyd's Bank v Bundy* [1974] 3 All ER 787 ?.
46 Cases unsuccessfully alleging undue influence by the husband include: *Kurland*, *Akins*, *Warburton* and *Garcia*, noted above at fn 10.
47 *Barclays Bank plc v O'Brien* [1994] 1 AC 180.
48 See the judgment of Lord Browne-Wilkinson in *Barclays Bank*, ibid at 191.

of the wife at the behest of the creditor, will be very difficult. It is unusual now for financiers to deal only with the husband. Where the wife attends the financier's office separately, is given some general explanations about the guarantee and/or a recommendation to obtain independent advice, at common the law the courts are unlikely to impute the lender with any constructive notice of the husband's undue influence.

Whether the doctrine of undue influence can only apply to set aside a guarantee where the transaction is manifestly unfair to the wife, and clearly not for her financial benefit, is unclear. The undue influence defence failed in *European Asian Ltd v Kurland*[49] where the wife had a half interest in her husband's company, with benefits flowing to her as a result of the guarantees she provided. The transaction was thus not disadvantageous to her even though the husband was in a clear position of dominance. Recently, however, the House of Lords in *CIBC Mortgages plc v Pitt*[50] rejected the 'manifest disadvantage' requirement as an element of undue influence. It remains to be seen if the same position is adopted in Australia. If it is, the reach of the doctrine will be extended to apply in situations such as *Kurland* where the obvious derivation of benefits flowing from the transaction excluded the wife from relying on the doctrine. Even so, given the difficulties in proving that the creditor was on notice of undue influence, the doctrine is unlikely to provide much solace for wives seek to set aside guarantees.

The principle in Yerkey v Jones[51]

The so-called 'special wives equity', derived from the judgment of Dixon J in *Yerkey v Jones*, has proved a more beneficial form of legal redress than the other common law remedies of undue influence and unconscionability. The principle operates as a rule of evidence, placing the burden on the creditor to establish that the guarantor wife has a full understanding of the transaction. The equitable presumption in favour of wives was expressed by Dixon J in the following terms:

> If a married woman's consent to become a surety for her husband's debt is procured by the husband and, without understanding its effect in essential respects, she executes an instrument of suretyship which the creditor accepts without dealing directly with her personally, she has a prima facie right to have it set aside[52].

The rule is quite distinct from the general principles which afford relief from unconscionable dealing. It is a special rule which applies specifically to

49 (1985) 8 NSWLR 192.
50 [1994] AC 211.
51 (1939) 63 CLR 649.
52 Ibid at 675.

guarantees provided by married women. The lender can assume that a wife is under a disability in dealing with her husband, and will be affected by any wrongdoing unless steps have been taken to alleviate her disability. The burden is thus upon the lender to establish that the guarantee was freely given. If the lender has relied on the husband to procure the guarantee there is no need for the guarantor to prove the lender's actual or constructive knowledge of any improper or unfair conduct on the part of the husband. In this context the word 'procure' means relying on the husband to obtain the consent of the wife to enter into the transaction.[53]

The rule applies where the wife has made an improvident bargain, in the sense of deriving no substantial benefit from the guarantee. It was once thought that this requirement precluded cases where the debtor was not the husband himself, but a company in which both husband and wife were co-directors and shareholders. However, the mere fact that a wife guarantees the debts of a company in which she has some interest should not necessarily preclude the obtaining of relief under the *Yerkey v Jones* or on any other grounds.[54]

Uncertain Status of the Doctrine

The doctrine in nearly 60 years old and its outmoded view of gender relationships creates doubts about its application in the modern era. The New South Wales Court of Appeal has now resolved the longstanding debate about *Yerkey v Jones* in that jurisdiction. The New South Wales courts had continued to apply *Yerkey* largely in deference to High Court precedent.[55] However, in a strong obiter decision in *Akins v National Australia Bank*[56] Clarke JA held that the principles in *Yerkey* were anachronistic and that guarantee cases could be appropriately determined by the principles of unconscionability set out by the High Court in *Amadio*. The Court of Appeal squarely confronted the issue of the continued applicability of *Yerkey* in *National Australia Bank v Garcia*[57] and *Teachers Health Investments Pty Ltd*,[58] two important decisions handed down in 1996. In both cases the Court decided that the principle is no longer good law in New South Wales. An important influence on the Court's thinking was the decision of the House of Lords in *Barclays Bank v O'Brien*[59] which strongly

53 *Peters v Commonwealth Bank of Australia* (Unreported, NSW Sup Ct, Equity Division, Brownie J, No 4928/91, 26 Feb 1992).

54 This extension of the *Yerkey v Jones* rule was accepted in *National Australia Bank v Garcia* (1996) 39 NSWLR 577 at 598.

55 *Warburton v Whitely* (1989) NSW Conv R 58,283.

56 (1994) 34 NSWLR 155 at 173. Powell and Sheller JJA agreed with Clarke JA.

57 (1996) 39 NSWLR 577.

58 (1996) ASC 56-357.

59 [1994] 1 AC 180.

criticised the continuation of a special principle for the protection of wives in guarantee transactions.

An analysis of the New South Wales cases indicates that the *Yerkey* principle has been rejected on two grounds. First, dissatisfaction with the stereotyped portrayal of the dependant wife, which is implicit in the doctrine. Secondly, in *Garcia*, as well as rejecting the rule on policy grounds, it was also rejected as a matter of law. Sheller JA, with whom Mahoney and Meagher J J A agreed, held[60] that Dixon J's principle had been extended too widely, and that none of the other judges in *Yerkey* agreed with Dixon J's proposition. Therefore, the Court held that Dixon J's judgment should not be regarded as good law.

Should the rule in *Yerkey v Jones* be retained ?

The status of *Yerkey* remains uncertain, except in New South Wales where the rule has been rejected. The question of whether there is still a need for a special rule for wives, although answered negatively by the New South Wales Court of Appeal, is still a matter for debate. In *Warburton v Whiteley*[61] Kirby P, although disapproving of the existence of rules of special treatment for women, reviewed some of the feminist and other literature in this area of law. As his judgment indicated, some of the commentators clearly do not agree that the position of women in society is sufficiently advanced to warrant the removal of special legal protection. The difficulty in establishing an *'Amadio'* defence was noted.

Moreover, in a number of guarantee cases all decided in the 1990's, wives who have failed the unconscionability test, have succeeded on the *Yerkey* principle.[62] It must be remembered that these are all cases of guarantees of business debts where common law remedies assume great importance. In *Teachers Health Investments v Wynne,* Hunter J, at first instance,[63] regarded himself as bound by *Yerkey* until the question of its continued application was resolved by the High Court. His Honour's decision was overturned by the Court of Appeal, reiterating the rejection of *Yerkey* in its prior decisions in *Akins* and *Garcia.*

The *Yerkey* controversy has not concerned the courts in Victoria to the same extent as the debate in New South Wales. However, in two recent

60 (1995) 39 NSWLR 577 at 598.
61 (1989) NSW Conv R 58,283.
62 *Peters v Commonwealth Bank of Australia* (Unreported, NSW Sup Ct, Equity Division, Brownie J, No 4928/91, 26 Feb 1992); *Warburton v Whitely* (1989) NSW Conv R 58,283; *ANZ Banking Group Ltd v McGee* (1994) ASC 58,92.
63 (1995) ANZ Conv R 74 at 80.

decisions[64] the Victorian Supreme Court indicated that, like Hunter J in *Teachers Health Investments v Wynne*, the principle in *Yerkey* should be regarded as binding until the High Court decides otherwise. The High Court has now granted special leave to appeal in the *Garcia* case and the decision of the Court is awaited with interest.

It is also significant that the reform bodies have expressed concern about the possible rejection of the special wives equity. Both the ALRC and the Expert Group on Family Financial Vulnerability recognised the ambivalence of the rule. On the one hand it perpetuates a paternalistic approach to women in relation to their financial dealings, on the other hand evidence indicates that many women are still subservient to their husbands in financial dealings and lack financial expertise and therefore some special form of protection is still warranted. To abandon the rule in favour of the uncertainties of the *Amadio* doctrine, prior to effective reform, fails to address the unequal position of women in society. This is clearly illustrated by the outcome in the *Garcia* case, where Mrs Garcia failed to have a number of guarantees set aside. The court accepted evidence that Mrs Garcia had been pressured by her husband to sign the guarantees, that the bank had failed to adequately explain them to her and that the bank had not followed any of its normal practices. The *Amadio* test was not satisfied in the absence of any knowledge on the part of the bank that Mr Garcia was pressuring his wife to sign or that she was doing so other than voluntarily. Under *Yerkey v Jones* her claim for relief would have succeeded.

Married Women as Company Directors

Many guarantee cases coming before the courts involve guarantees of loans to a company which is effectively the alter ego the husband.[65] Prior to the enactment of the *First Corporate Law Simplification Act* 1995 (Cth.), which amended the Corporations Law to permit the incorporation of one person proprietary companies, the incorporation of family businesses frequently involved a wife taking up a directorship in the company to satisfy the former requirements of the Corporations Law for two member/director companies. Problems could, and often did, arise, when a wife took up a directorship 'for signing purposes only', with little involvement in the business affairs of the company or understanding of her obligations as a guarantor or as a company director. Although newly incorporated family businesses now often adopt the sole member model and many conversions to sole membership have also occurred, the two director proprietary company with husband and wife as co-directors is still commonplace. Of course, even if a wife is not a director of a family company she may still be required to act

64 *ANZ Banking Group Ltd v Dunosa* (1995) ANZ Conv R 86; *Geelong Building Society (In liq) v Thomas* (Unreported, Vic Sup Ct, Civil Division, Hedigan J, No 12739/91, 30 April 1996).

65 See, for example, *Garcia, Gough, Kurland, Warburton, Cohen* and *ABC Property Planners*, noted above at fn 10 and fn 20.

as a surety, particularly where the family home is the only significant asset available for use as loan security. However, where married women are directors of the companies whose debts they have guaranteed it will generally be more difficult to resist enforcement of the guarantee when problems arise.[66]

In cases involving company director wives the courts must address issues of public policy concerning the responsibility of company directors, as well as the nature of any benefits flowing to the wife directly, by virtue of her shareholding, or indirectly by way of income and other tangible benefits flowing the family as a whole. Claims of financial naivety and lack of understanding are less likely to be regarded sympathetically in the case of a company director wife, particularly where she has some involvement, albeit it minimal, in the running of the business. However, the fact that the primary debt is that of a company, as distinct from that of the husband himself, does not preclude the operation of equitable doctrines such as unconscionability and undue influence, even where the guarantor wife is also a director of the debtor company. The invalidating presumption in *Yerkey v Jones* may also be relied upon, but only if the transaction is improvident from the wife's point of view, in the sense that she has no substantial stake in the company and therefore does not herself derive a real benefit from the provision of the guarantee. The doctrine of unconscionability is not restricted by the 'substantial benefit' requirement, but as noted above, few guarantor wives succeed in establishing the *Amadio* defence because of its own inherent difficulties.

Public Policy Issues-Higher Expectations on Company Director Wives

Where a female spouse with no apparent intellectual or comprehension disabilities attends a bank or other financial institution unaccompanied, in her capacity as a company director and appears to be voluntarily signing a guarantee to secure the account of the company, the bank is entitled to assume that she has a reasonable understanding of the business and financial affairs of the company. It would not be reasonable to conclude in these circumstances that the lender ought to know that she is in a position of disadvantage. This was certainly the view of the New South Wales Court of Appeal in *National Australia Bank v Garcia*.[67] The Court set aside the decision of Young J in favour of the wife, which was based on the *Yerkey* principle, but accepted his Honour's finding of lack of unconscionablity on the part of the bank. Mrs Garcia was apparently well-

66 Failed cases include: *Gough v Commonwealth Bank of Australia*, (1994) ASC 58,831; *Peters v Commonwealth Bank of Australia* (Unreported, NSW Sup Ct, Equity Division, Brownie J, No 4928/91, 26 Feb 1992); *European Asian of Australia Ltd v Lazich* (1987) ASC 57,284; *Donnelly v National Australia Bank* (Unreported, Full Ct of Sup Ct of WA, No 91/1991, 19 May 1992) *Commonwealth Bank of Australia v Cohen* (1988) ASC 58,146; *National Australia Bank Ltd v Garcia* (1996) 39 NSWLR 577; *Commonwealth Bank of Australia v ABC Property Planners Pty Ltd*, (Unreported, NSW Sup Ct, Cohen J, No 1450/89 25 May 1991).

67 (1996) 39 NSWLR 577.

educated and attended the bank in her capacity as a director and shareholder. In the circumstances there was nothing to put the bank on notice of any improper conduct by the husband.

In *National Australia Bank Ltd v McKay*[68] Hansen J, in the Victorian Supreme Court, implied that he was not satisfied that the wife was as ignorant of business or banking affairs as she claimed to be. He said:

> Even in her allegedly ignorant state, she appreciated that the Bank was advancing considerable sums of money....It was submitted that a person who chose to adopt the role that Mrs McKay did, fulfilling her duties as a director without actively appraising herself of the intricacies of the business but being aware of its involvement in financial transactions and receipt of large sums from the Bank, cannot sign a guarantee or indeed any legally binding document proffered to her by the Bank manager and then, at a later time, come along to a court and say, 'I was under a special disability'.

In the circumstances, Mrs McKay failed to have the guarantee set aside.

It is appropriate that the courts adopt a higher, objective company director standard in relation to financing transactions. Indeed, the rationale for doing so, especially for non-executive directors, has been adequately articulated in a well-known series of insolvent trading cases. Some of the cases involved women who were inactive directors of small family companies seeking to avoid personal liability for the debts of a company under s. 592 (2) of the Corporations Law (now replaced by s 588H).[69] In *Statewide Tobacco Services Ltd v Morley*[70] the director of a family company who had no role in its day to day to management and had sought no information as the company's finances could not escape liability for its debts. In the Victorian Supreme Court, Ormiston J, at first instance, held that a non-executive director could not rely on insolvent trading defences where he or she has taken no part in the management of the company, but totally delegated responsibilities to other directors or managers.[71] In essence, even a non-active director is required to give at least some attention to the affairs of the company and to obtain a reasonable knowledge and understanding of the company's financial position. His Honour suggested that even in a small company a director should seek out information about the company's trading figures on a regular basis. The Victorian Supreme Court, Appeal Division, approved the reasoning of

68 [1995] ATPR 40,534 at 40,544.

69 In particular the defence under s 592 (2) (b) (i) that the director did not have reasonable cause to expect the company would not be able to pay all its debts as and when they became due.

70 (1990) 8 ACLC 827.

71 Ibid at 846.

Ormiston J.[72] A similar approach, applying an objective standard in determining whether a director had reasonable cause to expect the company would be able to pay its debts as and when they fell due,[73] was also adopted in *Commonwealth Bank v Friedrich*[74] and *Rema Industries and Services Pty Ltd v Coad*.[75] The courts now expect that all directors exercise an inquiring mind and will not allow ignorance of the company's affairs to relieve a director of liability for insolvent trading.

So far as the position of inactive women company directors is concerned the comments of Debellle J in *Group Four Industries v Brosnan*[76] in relation to the insolvent trading duty can also be regarded as the benchmark for the level of understanding expected of women company directors in the guarantee context. His Honour said of Mrs Brosnan, a director a family company who claimed she did not know it was insolvent:

> While some might say that it was not unreasonable for a wife who is a part-time employee of the company and who has employment elsewhere to rely on her husband who is engaged full-time in the business of the company, such a view cannot obtain if the wife is a director of the company. Once the wife takes the office of a director, she undertakes duties and obligations which require an active interest to be displayed in the affairs of the company.

The stricter, objective approach to directors' duties, adopted in the insolvent trading cases was reinforced by the introduction of new s.232 (4) into the Corporations Law by the *Corporate Law Reform Act* 1992 (Cth.). The provision provides that an officer of a corporation must exercise the degree of care and diligence that a reasonable person in a like position in a corporation would exercise in the corporation's circumstances. Under both s 232(4) and recent case law such as *Daniels v Anderson*[77] minimum objective standards of care and skill for directors are required. Both the statute and case law recognise, however that the objective standard applies in the context of the particular background and responsibilities of the director concerned and of the size and nature of the corporation.[78]

The improvident transaction

72 *Morley v Statewide Tobacco Services Ltd* (1992) 10 ACLC 1233.
73 In order to establish the defence under s 592 of the Corporations Law.
74 (1991) 9 ACLC 946.
75 (1992) 10 ACLC 530 at 537 per Lockhart J.
76 (1992) 10 ACLC 1437 at 1479.
77 (1995) 13 ACLC 614.
78 Explanatory Memorandum to the *Corporate Law Reform Act 1992* paras 84 to 86.

The unresolved status of the *Yerkey v Jones* principle has been noted above. The Court of Appeal in New South Wales now prefers to adopt a broad unconscionability approach. In other States the position remains unclear. Until the High Court rules otherwise the doctrine still applies in some jurisdictions, but its operation in the company context is curtailed by the 'ubstantial benefit' requirement. The mere fact that the debt is that of a company controlled by the husband, as distinct from the debt of the husband himself, is not fatal to the launching of a *Yerkey v Jones* defence, but the defence will certainly be more difficult to establish. Although Dixon J in *Yerkey* did not indicate the exact extent to which a guarantee must be improvident from the wife's point of view before the invalidating presumption is inapplicable, there is a general consensus in the cases that the wife need not technically be a volunteer for the rule to operate. So long as there is not a substantial benefit flowing to her, equity will assist her. The meaning of 'substantial benefit' is somewhat elusive. A material shareholding in the debtor company would exclude the rule.[79] Differing approaches have been taken in cases where the company director wife has a minimal shareholding in the company, but derives indirect benefits for herself and her family by virtue of her position as director and shareholder of the family company.

In *Warburton v Whiteley*[80] it was held that the fact that a guarantee is made to a family company, thus indirectly improving the standard of living and the income flow to the family, did not mean that the wife could not have the guarantees set aside. The majority held that the onus on the lender of establishing that the wife did not have a material interest in the company was not made out. Similarly, in *National Australia Bank v Garcia*[81] Sheller JA held, obiter, that the fact that money flowed to the wife from time to time from one of her husband's companies for household and family expenses was not decisive.

Other cases have taken a wider view of 'substantial benefit' as including benefits which indirectly improve the family lifestyle and income flow.[82] This wider view would of course displace the *Yerkey v Jones* principle from most cases involving guarantees to a debtor family company. The other equitable doctrines, undue influence and unconscionability, are not technically restricted by the 'substantial benefit' requirement, but as outlined above have their own severe limitations in the guarantee context. So far as unconscionability is concerned,

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79 In *European Asian Ltd v Kurland* (1985) 8 NSWLR 192 the wife guaranteed the debts of a company in which, by shareholding in an interposed company, she had a one-half interest. The guarantee was supported by a mortgage over the matrimonial home which stood in her name only. The principle in *Yerkey v Jones* was held not to apply.

80 (1989) NSW Conv R 58,283.

81 [1996] 39 NSWLR 577 at 598.

82 In particular the cases of *Akins v National Australia Bank Ltd* (1994) 34 NSWLR 155, *ANZ Banking Group Ltd v Dunosa* (1995) ANZ Conv R 74 at 80 and *Commonwealth Bank of Australia v Cohen* (1988) ASC 56,146.

because of higher standards expected under company law principles, a director wife is unlikely, except in unusual circumstances, to satisfy the 'special disability' test.

Statutory provisions relating to guarantees of business debts

There are few statutory provisions which apply to 'business' as opposed to consumer guarantors. There are no specific *Trade Practices Act 1974* (Cth.) 'TPA' provisions targeting guarantees. Some of the well-known general provisions of the TPA affect the conduct of corporations in their contractual dealings, which obviously includes the taking of guarantees. These general provisions have a proscriptive and remedial focus.[83] Section 52 may provide some incidental relief to persons who signed a guarantee on the basis of misleading and deceptive representations and omissions. Section 51AB proscribes unconscionable conduct, but is limited only to consumer transactions.[84] It specifies a number of factors which the court may consider when determining whether a corporation has engaged in unconscionable conduct in consumer transactions.[85] A new s 51AA was inserted into the by amendment effective from 21 January 1993. Section 51AA does not replicate the s 51AB factors but merely gives statutory backing to the equitable doctrine of unconscionability. Its operation extends to goods and services acquired for business purposes. This allows the broad remedies available under the TPA to extend to non-consumer guarantees. Under the s 51AB(2) factors the court may have regard to unfairness both in the bargaining process and in the terms of the contract itself, but the equitable doctrine is not so broad. It concentrates on the pre-contractual conduct, not on the terms and scope of the contract itself.

The *Contracts Review Act 1980*, unique to New South Wales, applies to all contracts except those entered into in a business (other than farming) or professional capacity.[86] A contract of guarantee takes on a 'consumer' characterisation under the Act by virtue of the purpose of the guarantor, rather than the purpose of the primary borrower. In this respect it has a wider ambit than either the new Consumer Credit Code or the TPA unconscionability provisions. The (former) Trade Practices Commission, in its 1992 Discussion Paper,[87] preferred the approach adopted by the *Contracts Review Act*. Section 7 of the Act gives the court a wide discretion to re-open or set aside an 'unjust' contract. A contract may be unjust because of unfairness in the methods used in securing the contract,

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83 The *Fair Trading Acts* of the States and Territories have provisions which mirror ss 52 and 51AB of the TPA.

84 Section 51AB only applies to unconscionable conduct in connection with the supply of goods or services of a personal, domestic or household purpose (s.51AB (5) and (6)).

85 Including such matters as the tactics and conduct of the lender, the strength of bargaining position of the parties and the degree to which the guarantor understood the relevant documents,

86 Section 6(2).

87 See fn 1.

or it may be unjust because its terms are harsh and unfair.[88] However, the ALRC in a Report subsequent to that of the TPC pointed out the weaknesses in the application of the Act to cases of sexually transmitted debt.[89] A finding of unjustness under the Act generally depends on a single factor; whether the wife obtained independent legal advice. In *National Australia Bank v Garcia*[90] Sheller JA emphasised that the discretion of the court to grant relief under the Act will not generally be exercised if the alleged disability of the plaintiff was one which the other party to the contract was unaware. In effect similar rules appear to apply in practice under the *Contracts Review Act* as they do at common law.

The new Consumer Credit Code as a model for Reform ?

The new Code[91] has delivered some obvious benefits to consumer guarantors, including:

- provision by the lender of a warning of potential liability and mandatory recommendations that the guarantor seek independent financial advice and pursue inquiries about the debtor's position;
- a wide of definition of guarantees which includes indemnities;
- a 'cooling-off' between the signing of the guarantee and the drawing down of the loan;
- clearly expressed documentation;
- mandatory pre-contractual disclosure of the debtor's credit contract and information explaining the rights and obligations of guarantors;
- on-going account information to be supplied on request; and
- re-opening provisions, incorporating a 'shopping list' of factor to guide the courts in determining when a guarantee is unjust.

However, the Code has obvious limitations. It merely recommends and does not require independent advice to be provided, although a court may

88 *West v AGC (Advances) Ltd* (1986) 5 NSWLR 610 at 620 per McHugh JA.
89 See fn 1 at para 13.1.
90 (1996) 39 NSWLR 577 at 608.
91 Part 3, Div 2.

consider the absence of advice when it exercises its discretion under the re-opening provisions. Because information disclosure should be at the heart of the reform process it can be argued the changes under the Code do not go far enough. The Consumer Credit Code does not go beyond the position traditionally held at common law, in that it fails to treat guarantees as contracts of the utmost good faith (uberrimae fidei) requiring full disclosure of all material facts.

Proposals for Reform

The most recent and far-reaching proposal for reform was outlined in an important Report by the Expert Group on Family Financial Vulnerability, entitled ‘Good Relations, High Risks: financial transactions between family and friends’ released by the former (Labour) Federal Government in February 1996. The Group was established in the Federal Justice Statement in May 1995 in response to widespread concern about the financial vulnerability of people who enter into financial arrangements on the basis of emotional ties rather than for commercial reasons. Noting that recent reforms did not go far enough in protecting emotionally vulnerable guarantors, the Group proposed significant changes to the law to address the shortcomings in the current rules relating to guarantees. The Report addresses three essential issues that need to be resolved to achieve effective reform in the business guarantee context; consistency in the legal rules applying to all guarantors, workable rules for material information disclosure and clarifying 'independent' advice requirements.

The Group made fourteen valuable recommendations concerning not only guarantees but other financial transactions which are entered into on the basis of emotional and financial vulnerability. So far as the treatment of guarantees is concerned Recommendations 1 and 2 are the most significant.

> **Recommendation 1**
>
> The *Trade Practices Act* should be amended (or a new Commonwealth Act introduced) to require a financier to give a prospective personal guarantor relevant information which a reasonable guarantor would reasonably require in order to decide whether or not to enter into the guarantee.

> **Recommendation 2**
>
> The *Trade Practices Act* should be amended (or a new Commonwealth Act introduced) to require a financier to take all reasonable steps to advise a potential guarantor directly (rather than through the borrower).

- about the legal nature of the guarantee;

- about the financial risks involved in a guarantee;
- that the guarantor should seek independent advice about these matters; and
- to execute the guarantee in the absence of the borrower.

Although Recommendation 1, the 'know your guarantor' rule is couched in broad terms the Group believed that such a general provision could be effective if support by guidelines developed by a regulator such as the Australian Competition and Consumer Commission. Noting that the TPA was well established as the primary Commonwealth consumer legislation, the Group appeared to approve insertion of specific guarantee provisions in the existing *Trade Practices Act*, rather than the enactment of a new Commonwealth Financial Services Act specifically directed at financial service providers. Any small gaps in coverage could be picked up by mirror amendments to the State Fair Trading Acts. Overall, the Group's recommendations provides a total package which covers prevention of problems as well as remedies when things go wrong.

Ideally the TPA changes suggested by the Expert Group should be bolstered by complementary changes to the self-regulatory Codes of Practice now in place across most sectors of the finance industry. For example, there are doubts as to whether the Code of Banking Practice (on which the other industry Codes are based) is binding on any guarantors. The Code only has contractual force in relation a 'banking service' provided to a 'customer'[92] and it is open to question whether the guarantor is receiving a service from the bank. Moreover, while the Banking Code's protective guarantee provisions[93] do not expressly exclude guarantors of business or company debts, they would not meet the definition of 'customer' under the Code, given that they are not acquiring a banking service 'wholly and exclusively for...private or domestic use'. The Code's guarantee provisions need re-drafting to address these anomalies.

In addition, the Code does not apply at all where the guarantee is to secure a loan to a company of which the guarantor is a director secretary or member.[94] The provisions of the voluntary Codes are overridden by statute, so that any changes to the TPA, as proposed by the Expert Group, would have effect regardless of any exclusions expressed in the Banking Code. However, it is appropriate that the finance industry adopts a positive approach to the need for reform concerning the treatment of guarantees.

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92 Cl 1.
93 Cl 17.
94 Cl 17 (1) (ii).

Unfortunately the Federal Liberal Government, elected shortly after the release of the Expert Group's Report, has not acted on any of its proposals to change the law. It is to be hoped that self-regulation by the financial services industry will, in the absence of statutory directive, result in improvements in the provision of advice, explanation and information disclosure across all sectors of the fiance industry, including the finance company sector which at present does not have an applicable Code of Conduct or alternative dispute resolution service for customers. The banks and other finance providers need to demonstrate compliance and commitment to their respective Codes of Conduct, still in the early stages of full implementation. While directly effecting ‘consumers’ improved banking practices will necessarily benefit business customers as well. Ultimately it is to be hoped that the Government does not fail to heed the well documented case for statutory reform in this area.