DOES TITLE TO PROPERTY PASS WHERE ITS PURPORTED TRANSFER IS CAUSED BY THE PURPORTED TRANSFEROR'S MISTAKE?

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The following issues will be examined:

(1) Does title to property pass where its purported transfer is caused by the purported transferor's mistake?

(2) If the purported transferor's mistake prevents title from passing to the purported transferee, does the purported transferee:

   (a) receive neither the legal nor the equitable title to the property, so that he will be liable to the purported transferor in conversion; or

   (b) receive the legal title to the property as an innocent volunteer; or

   (c) receive the legal title to the property as a resulting trustee; or

   (d) receive the legal title to the property as a constructive trustee?

(3) If title does not pass to the purported transferee, and if the purported transferee does *not* receive the property as a *trustee*, is the defence of adverse change of position available to the purported transferee where the property remains traceable by the purported transferor?

Does title to property pass where its purported transfer is caused by the purported transferor's mistake?

In *David Securities Pty Limited v Commonwealth Bank of Australia*[1] the High Court decided that property is prima facie recoverable not only when it has been purportedly transferred under a mistake of fact made by the transferor but also when it has been purportedly transferred under a mistake of law made by the transferor.

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1 (1992) 175 CLR 353.

In doing so, the High Court rejected the rule in *Bilbie v Lumley*[2] which had decided that recovery was precluded where property was purportedly transferred under a mistake of law. In *Kleinwort Benson Ltd v Lincoln City Council*[3] the House of Lords overruled *Bilbie v Lumley*,[4] so that, in Australia as well as in England[5], property purportedly transferred under a mistake (whether of law or of fact) is now prima facie recoverable, subject to the defence that the purported transferee's position has changed so adversely to himself that it would be inequitable to require him to restore the property to the transferor.

Does the right of the purported transferor (the transferor) to recover property transferred under a mistake (whether of fact or of law) mean that the basis of recovery is now the same with respect to both these types of mistake? In *David Securities*,[6] the High Court observed:[7]

> …It would be logical to treat mistakes of law *in the same way* as mistakes of fact, so that there would be a prima facie entitlement to recover moneys paid when a mistake of law or fact has *caused* the payment. …

Thus, in order to ground a prima facie right to recover property ineffectually transferred by reason of mistake, all that it is necessary for the transferor to show is that his mistake *caused* the transfer to be made. The transferor does not have to prove, additionally, that the purported transferee (the transferee) has been unjustly enriched[8] by the transfer. It is for the *transferee* to prove that the receipt of the property has *not* unjustly enriched him, if he is to defeat the transferor's prima right to restitution.[9]

Furthermore, the transferor does not have to show that his mistake was fundamental. As it was made clear in *David Securities*:[10]

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2 (1802) 2 East 469; 102 ER 448.
3 [1999] 2 AC 349.
4 (1802 2 East 469; 102 ER 448.
5 The position is the same in New Zealand: *National Bank of New Zealand Ltd* v *Waitaki International Processing (NI) Ltd* [1999] 2 NZLR 211.
6 (1992) 175 CLR 353.
7 Ibid, at 376 (per Mason CJ, Deane, Toohey, Gaudron and McHugh JJ). Emphasis added. At 402, Dawson J concurred in this view. In similar vein is the opinion of Neuberger J in *Nurdin & Peacock Plc v DB Ramsden & Co Ltd* [1999] 1 WLR 1249, at 1273.
8 *David Securities* (1992) 175 CLR 353, at 379 (per Mason CJ, Deane, Toohey, Gaudron and McHugh JJ).
9 Ibid.
10 (1992) 175 CLR 353, at 378 (per Mason CJ, Deane, Toohey, Gaudron and McHugh JJ). Emphasis added.

> …There is…no place for a further requirement that the *causative mistake* be *fundamental*; insistence upon that factor would only serve to focus attention in a non-specific way on the nature of the mistake, rather than the fact of enrichment. …

Does a transfer which has been caused by the transferor's mistake have the consequence that the title to the property remains in the transferor at the moment of the transferee's purported receipt of it? In principle, such a causative mistake should make the purported transfer a nullity, so that the transferee does not acquire title to the property. In *David Securities*,[11] the High Court clearly thought so, saying:

> …[I]f the payer has made the payment because of a mistake, his or her *intention to transfer* the money is *vitiated* and the recipient has been enriched.[12] …

If the intention to transfer is vitiated then, there having been no intention to transfer the property, the effect of the transferor's mistake is that the title to the property remains in him. The transferor will continue to retain title unless the property, subsequently to its purported receipt by the transferee, becomes *untraceable,* or, alternatively, unless the title to that property is extinguished by the transferee's adverse change of position where such an adverse change would make it inequitable for the transferor to claim restitution.[13]

That, in the absence of a defence of an adverse change in the transferee's position, the transferor's title to the property survives the purported transfer, and that the title is lost only when the property becomes untraceable, appears from the following observation of Mason CJ in *Commissioner of State Revenue (Vic) v Royal Insurance Australia Limited*:[14]

> When the plaintiff succeeds in a restitutionary claim, the court awards the plaintiff the monetary equivalent of what the defendant has taken or received, except in those cases in which the plaintiff is entitled to *specific proprietary relief*. …

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11 (1992) 175 CLR 353, at 378 (per Mason CJ, Deane, Toohey, Gaudron and McHugh JJ). Emphasis added.

12 It is distinctly incongruous for the High Court to suggest that a transferee would be *enriched* by a purported transfer which is *vitiated* by the transferor's mistake. If the transferor's intention to transfer is vitiated by mistake, then there will be no intention to transfer. If there is no intention to transfer the property, then the transferee will have, at most, received only legal title to the property, so that the vitiated transfer will not have *enriched* the transferee in any way.

13 *Australia and New Zealand Banking Group Limited v Westpac Banking Corporation* (1988) 164 CLR 662, at 673.

14 (1994) 182 CLR 51, at 73-74. Emphasis added.

Support for the proposition that a purported transfer caused by the transferor's mistake does not deprive the transferor of his title to the property, and thus enables him to trace the property, can also be found in *Sinclair v Brougham*.[15]

The effect of a causative mistake on a purported transfer of title is clearly stated by Lord Hope in *Kleinwort Benson Ltd v Lincoln City Council:*[16]

> What, then, is the function of mistake in the field of restitution on the ground of unjust enrichment? The answer, one may say, is that its function is to show that the benefit which has been received was an *unintended* benefit. …A mistake…will be enough to justify the restitutionary remedy, on the ground that a benefit which cannot be legally justified should not be retained where it was a *mistaken* and *thus unintended* benefit.

Furthermore, in *Australia and New Zealand Banking Group Limited v Westpac Banking Corporation*,[17] the High Court assumed that causative mistake would prevent the transferee from acquiring title to the property at the moment of its purported receipt. This assumption clearly emerges from the comparison made by the High Court of the common law action for money had and received (which is a non-proprietary remedy), with the proprietary remedies in equity. The High Court there said:[18]

> …The basis of the common law action of money had and received for recovery of an amount paid under fundamental mistake of fact[19] should now be recognised as lying not in implied contract but in restitution or unjust enrichment: …The common law right of action may arise in circumstances which *also* give rise to a *resulting trust* of *specific property or funds* or which would lead a modern court to grant relief by way of *constructive trust*. However, …the action itself is not for the enforcement of a trust or for tracing or the recovery of specific money or property. It is a common law action for recovery of the *value* of the unjust enrichment and the fact that specific money or property received *can no longer be identified*

15 [1914] AC 398.

16 [1999] 2 AC 349, at 408. Emphasis added.

17 (1988) 164 CLR 662.

18 Ibid, at 673 (per Mason CJ, Deane, Toohey, Gaudron and McHugh JJ). Emphasis added.

19 This proposition was enunciated *before* the High Court's decision in *David Securities* where it was held that in order to ground recovery of property transferred by mistake, the mistake in question may be either a mistake of law, or a mistake of fact, made by the transferor, and that, in either case, the mistake need only be one which *caused* the transfer of the property, and need *not* be one which was of a fundamental nature: (1992) 175 CLR 353, at 378.

> in the hands of the recipient *or traced into other specific property* which he holds does not of itself constitute an answer in a category of case in which the law imposes a prima facie liability to make restitution. …

By alluding to the case of 'specific money or property received'[20] by the transferee from the transferor where such property could '*no longer* be identified…or traced into other specific property'[21] held by the transferee, the High Court was necessarily assuming that the mistaken transfer of property was a nullity and that, at the moment of the transferee's purported receipt, the title to that property remained in the transferor, so that, in the absence of a successful defence of an adverse change in the position of the transferee, the transferor's title would be lost only if it subsequently became impossible to trace it.

The High Court's recognition that, in the absence of a successful defence of change of position, title to property transferred under a causative mistake is retained by the transferor until it ceases to be traceable is of critical importance to the transferor in the event of the transferee becoming bankrupt. If title to the property so remains in the transferor, then the transferor's right to claim the property in specie, by the process of tracing, is not defeated by the transferee's subsequent bankruptcy. Even if the legal, as distinct from the equitable, title to the property, or even if the legal, as distinct from the equitable, title to the traceable proceeds of that property, has vested in the bankrupt transferee, that property, or its proceeds, being property held in trust by the bankrupt transferee for the benefit of the transferor, will not be divisible amongst the creditors of the bankrupt transferee.[22]

Such a beneficial outcome for the transferor may be contrasted with the transferor's plight if the law had been that title *did* pass to the transferee under a transfer caused by the transferor's mistake. If title did pass to the transferee at the moment of its purported transfer, then no proprietary remedy would be available to the transferor, who would then be reduced to having only a personal remedy in the form of an action for money had and received against the transferee for the recovery of the mere *value*[23] of the property, as distinct from the property itself. In the event of the transferee's subsequent bankruptcy and in the event of the transferee's assets being then insufficient to meet his liabilities in full, the transferor, if his remedy is no more than the non-

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20 (1988) 164 CLR 662, at 673 (per Mason CJ, Deane, Toohey, Gaudron and McHugh JJ).

21 Ibid, Emphasis added.

22 *Bankruptcy Act* 1966 (Cth) section 116(2)(a).

23 *Australia and New Zealand Banking Groups Limited v Westpac Banking Corporation* (1988) 164 CLR 662 at 673 (per Mason CJ, Wilson, Deane, Toohey and Gaudron JJ).

proprietary common law action for money had and received, will become a mere unsecured creditor of the bankrupt transferee, and, as such an unsecured creditor, the transferor will be entitled to recover from the transferee's bankrupt estate only a proportion of what he is owed.[24]

The View that Title passes notwithstanding a Causative Mistake in the Transfer: the Westdeutsche View

In *Westdeutsche Landesbank Girozentrale v Islington London Borough Council*[25] the House of Lords decided that title to property did pass to the transferee notwithstanding that the contract under which it was purportedly passed was void at ab initio.[26] Consequently, the House of Lords decided that the transferor's only cause of action against the transferee was the non-proprietary common law action for money had and received.[27] The House of Lords determined that, because the transferor's mistake had not prevented the title to the property (money) from passing to the transferee, no proprietary remedy was available to the transferor as against the transferee. Thus, the position so posited by the House of Lords is in direct conflict with the view expressed by the High Court in *David Securities.*[28]

Background to Westdeutsche

In *Hazell v Hammersmith and Fulham London Borough Council*[29] the House of Lords declared that it was ultra vires for local councils in England to enter into interest rate swap contracts, with the consequence that such purported contracts were void ab initio when purportedly entered into with those local councils. An interest rate swap contract is a contract where, with respect to an agreed notional principal sum existing for an agreed period, one party, called the notional fixed interest rate payer, agrees with another party, called the notional variable interest rate payer, that whichever party is notionally liable to pay the larger of the two interest payments on the agreed notional principal sum, will pay to the other party the monetary difference between the larger and the smaller interest payments. In some of such contracts one of the parties will, in exchange for paying a lower rate of interest than it would otherwise have

24 *Bankruptcy Act* 1966 (Cth), section 108.
25 [1996] AC 669.
26 *Ibid*, at 689-690 (per Lord Goff); at 708 (per Lord Browne-Wilkinson); at 718 (per Lord Slynn); at 720 (per Lord Woolf); and at 738 (per Lord Lloyd).
27 Ibid.
28 (1999) 175 CLR 353, at 378 (per Mason CJ, Deane, Toohey, Gaudron and McHugh JJ).
29 [1992] 2 AC 1.

had to pay, pay to the other party an upfront (ie, an initial) payment.[30] This upfront payment is in substance, although it is not so in legal theory, a loan from the party who makes the payment to the party who receives the payment. The *difference* between the payer's *lower* notional interest rate and the payee's *higher* notional interest rate is the *real* interest rate payable by the payee of the upfront payment (in substance the borrower) to the payer of the upfront payment (in substance the lender).

In *Westdeutsche*, an interest rate swap contract had been purportedly entered into between a bank (Westdeutsche) and a local council (the Islington London Borough Council). The bank (the notional fixed interest rate payer) had made to the local council (the notional variable interest rate payer) an upfront payment of •2.5m. In effect, although not in form, this payment was a loan made by the bank to the council. Subsequently, the council, in ignorance of the fact that the purported contract was void ab initio, made a number of payments to the bank because the variable interest rate liability from time to time (the council's notional liability) exceeded the fixed interest rate liability at those times (the bank's notional liability). When the council eventually discovered that it's purported contract with the bank was void ab initio, it stopped making such payments to the bank. The bank's upfront payment to the council of •2.5m exceeded by a little over •1m the total amount of the payments made by the council to the bank.

The bank, relying on the fact that the contract was void ab intio, claimed the excess, namely, the sum of more than •1m, together with interest, from the council. The English Court of Appeal held that the bank was entitled to recover the excess sum either at common law, in an action for money had and received or, alternatively, in equity, under a resulting trust of the upfront payment. Additionally, the Court of Appeal held that this excess sum had to be paid to the bank with *compound* interest as from the date of the council's receipt of the bank's upfront payment, irrespective of whether the council's liability was based on an action for money had and received or on a resulting trust of the upfront payment.

In the House of Lords, the local council accepted that it was liable to pay the excess sum to the bank in an action for money had and received, but it denied that it was liable to account to the bank as a resulting trustee. The identification of the nature of the council's liability to the bank was crucial because the majority[31] of the law lords held that compound interest could be awarded, and then only in equity, only where the defendant had been fraudulent or,

30 *Westdeutsche* [1996] AC 669 (per Lord Browne-Wilkinson).

31 *Westdeutsche* [1996] AC 669, at 701 and 702 (per Lord Browne-Wilkinson); at 718 (per Lord Slynn); and at 738 (per Lord Lloyd).

alternatively, where the defendant was a trustee or other fiduciary who was accountable for profits made from the misuse of his position.[32]

If the council was merely liable to the bank in an action for money had and received, then, given that the council had not been fraudulent, and given, further, that the council did not at any stage owe any fiduciary duty to the bank, the bank would only have been entitled to be paid simple interest, and not compound interest, by the council on the excess sum. In the view of the majority of the law lords, the bank could recover the money, with compound interest, only if it could prove that the council had received the upfront payment as a resulting trustee for the bank, given that the council had not been fraudulent in receiving the money purportedly for its own benefit. So, for the majority of the law lords, it became necessary to decide whether or not the council had received the upfront payment from the bank as a resulting trustee for the bank. For those law lords, if the council had not received the upfront payment as a resulting trustee for the bank, the latter would have been entitled to be repaid the excess sum by the council with simple interest only.

The bank argued that the council had received the upfront payment as a resulting trustee.[33] The bank did not argue that the council had received that payment as a constructive trustee,[34] presumably because the council could not have had notice at the time of its receipt of the upfront payment that the interest rate swap contract was a nullity,[35] since it had not then been decided that such a contract was one which it was ultra vires for the council to enter into.

Lord Browne-Wilkinson, with Lord Slynn[36] and Lord Lloyd[37] concurring, rejected the bank's argument that the council had received the upfront payment as a resulting trustee, saying:[38]

> …[A]ny presumption of resulting trust is rebutted since it is demonstrated that the bank paid, and the local authority received, the upfront payment with the *intention* that the moneys so paid should become the *absolute property* of the local authority. It is true that the parties were under a misapprehension that the payment was made in pursuance of a valid contract. But that does not alter the actual intentions of the parties at the date the payment was made…

32 *President of India v La Pintada Company Navigation SA* [1985] AC 104, at 116 (per Lord Brandon).
33 *Westdeutsche* [1996] AC 669, at 701 and 702 (per Lord Browne-Wilkinson).
34 *Westdeutsche* [1996] AC 669, at 701 and 703 (per Lord Browne-Wilkinson).
35 *Westdeutsche* [1996] AC 669, at 701 and 707 (per Lord Browne-Wilkinson).
36 [1996] AC 669, at 718.
37 [1996] AC 669, at 738.
38 [1996] AC 699, at 708. Emphasis added.

Lord Browne-Wilkinson's conclusion is directly opposed to the opinion expressed by Lord Wright in the Privy Council in *Norwich Union Five Insurance Society Limited v Wm H Price Limited*,[39] where Lord Wright observed:[40]

> …The mistake…*prevented* there being that *intention* which the common law regards as essential to the making of an agreement or *the transfer of money or property*. …

Lord Wright added in *Norwich Union*:[41]

> …[P]roof of mistake affirmatively excludes intention. …

In *Westdeutsche*, Lord Browne-Wilkinson seems to have assumed that the bank's intention to pay the council was *unconditional*, namely, that the bank would have intended to pay the council even if it had known, at the time of the payment, that the purported contract between it and the council was a nullity (ie, was void ab initio). This is an astonishing assumption. The bank purported to pay the council pursuant to the purported contract. The bank had no other reason to pay the council. The bank's intention to pay the council was therefore *conditional* on the purported contract being *valid*. Since the purported contract was void, the bank's intention to pay the council was thereby vitiated ab initio. Thus, in the event, the bank did *not* intend to pay the council. At the time of the purported payment the council received legal, but not equitable, title to the money which the bank paid into the council's account with another bank (the receiving bank). Since the account into which the money was paid was held in the name of the council, the council thereby unavoidably, but only through the accident of the paying bank's mistake, acquired the legal title to that money (ie., the legal title to the legal chose in action obtained by the council against the *receiving* bank in respect of the money paid into the council's account at the receiving bank by virtue only of the paying bank's mistake); but it did not follow that the council, merely by its unavoidable but accidental acquisition of the legal title to the money, also acquired *equitable* title to that money. The council had not given any contractual consideration to the bank in exchange for that money, nor had the bank intended to transfer to the council the title to that money, given the bank's causative mistake in making the payment.

Lord Browne-Wilkinson's view in *Westdeutsche*[42] is also irreconcilable with the law stated by the High Court in *David Securities*.[43] There the High Court made it

39 [1934] AC 455.
40 Ibid, at 462. Emphasis added.
41 [1934] AC 455, at 463.
42 [1996] AC 669, at 708.

clear that a payment made pursuant only to the discharge of a legal obligation, which the payer believed to exist, is *conditional* on the existence of that obligation, so that the intention to make the payment is vitiated if the payer did not have any legal obligation to make the payment which was purportedly made,[44] namely, if the payer's mistake had caused the payer to pay the payee.

It is suggested that the majority[45] of the law lords in *Westdeutsche*[46] were wrong to decide that an intention to make a payment pursuant only to a contract which the payer mistakenly assumed to be valid is not vitiated by the voidness of that contract.

If the intention to transfer property is vitiated by a mistake which caused the transferor to form that intention, what is the position of the transferee with respect to the property at the moment of its purported receipt?

Conversion/Action for money had and received

Suppose A, mistakenly believing himself to be indebted to B in the sum of $1000, purports to discharge that non-existent debt to B by handing to B ten $100 notes. Suppose that B, whether or not he has notice of A's mistake, purports to assume ownership of the notes, namely, purports to make himself the owner of those notes.

At common law, as distinct from equity, what is B's position with respect to the notes at the moment of his purported receipt of them? Since the intention to transfer title to the notes to B is vitiated by A's mistake,[47] A has not intended to transfer to B either the possession or the ownership of those notes. It was never A's intention to constitute B a mere bailee of the notes, nor was it A's intention to make B the absolute owner of those notes.

As B has nevertheless purported to assume ownership of the notes, he has denied A's immediate right to possession of them, and, consequently, B has converted A's notes. As Dixon J said in *Penfolds Wines Proprietary Limited v Elliott:*[48]

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43 (1992) 175 CLR 353.

44 Ibid, at 381. See also *Porter v Latec Finance (Qld) Pty Limited* (1964) 111 CLR 177, at 194 (per Kitto J).

45 Lord Browne-Wilkinson, Lord Slynn and Lord Lloyd.

46 [1996] AC 667.

47 *Kelly v Solari* (1941) 9 M&W 54, at 59; 152 ER 24, at 26: per Parke B.

48 (1946) 74 CLR 204, at 229.

> …The essence of conversion is a dealing with a chattel in a manner repugnant to the immediate right of possession of the person who has the property or special property in the chattel. …

Alternatively, A may sue B in an action for money had and received.[49]

Constructive Trustee

Suppose, in the hypothesis given above, B takes the ten $100 notes with notice of A's mistake.

At the moment of B's purported receipt, notwithstanding his notice of A's mistake, B does not become a constructive trustee of the notes because he does not have legal title to them. B does not have anything to hold in trust, and there cannot be a trust without trust property.[50] At the moment of receipt by B, it is A who has absolute title to the notes.

Suppose that, subsequently to his receipt of the notes, B uses them to open a bank account for himself. Because B's bank will have acquired the notes for value and without notice of B's lack of title to them, B's bank will have acquired absolute title to them as currency.[51]

Because B has used the ten $100 notes to open a bank account in his own name, he will be the legal owner of a chose in action against the bank to the value of $1000.[52] The question here is this: is B also the equitable owner of that chose in action? Since B has acquired the legal chose in action with notice that the bank notes, used by him to acquire that chose, belonged to A, B will have acquired that chose in action as a constructive trustee for A.[53]

As a constructive trustee of the legal chose in action for the benefit of A, B will be accountable to A for the legal chose in action and for all the profits derived from that chose in action.[54]

Innocent Volunteer

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49 *Kelly v Solari* (1841) 9 M&W 54, 152 ER 24; *United Australia Limited v Barclays Bank Limited* [1941] AC 1.

50 *In re Goldcorp Exchange Ltd* [1995] 1 AC 74.

51 *Miller v Race* (1758) 1 Burr 452; 97 ER 398. See also *Sinclair* v *brougham* [1914] AC 398, at 418 (per Viscount Haldane LC).

52 *Foley v Hill* (1848) 2 HLC 28; 9 ER 1002.

53 *Nelson v Larholt* [1948] 1 KB 339; *In re Diplock* [1948] 1 Ch 465, at 522 (per Lord Greene MR, Wrottesley and Evershed LJJ).

54 *Attorney-General for Hong Kong v Reid* [1994] 1 AC 324.

Suppose that, in the above hypothesis, B takes the ten $100 notes from A *without* notice of A's mistake. At the moment of B's receipt, A remains the absolute owner of those notes because A's mistake has vitiated his intention to transfer the title to those notes to B.[55] At the moment of receipt, B is *not* what equity calls an innocent volunteer. This is so because, at that moment, B has not obtained even the legal title to the notes, whereas an innocent volunteer is someone who has received the legal title to property but who has not given value for it and who, at the time of the receipt of the legal title, did not have notice that the equitable title to the property was vested in a third party.[56]

Suppose that B, being still unaware of A's mistake, uses the notes (which are owned by A both at law and in equity but which are within B's physical control) to open a bank account for himself (B). The bank, in acquiring those notes from B, for value and without notice of B's lack of title to them, will obtain title to them as currency.[57] B will correlatively acquire the legal title to a chose in action against the bank, that legal chose being constituted by his credit balance in the bank of $1000. However, B will not acquire the equitable title to that legal chose in action because, although B had no notice of A's mistake when B acquired the legal chose in action by using the ten $100 notes to open B's account at the bank, A's intention to transfer the title to the ten $100 notes to B was vitiated by A's causative mistake.

B has legal title to the chose in action but he does not have the equitable title to it. Does this separation of the legal title from the equitable title make B a trustee of the chose in action for A?

In *Hardoon v Belilios*[58] Lord Lindley, speaking for the Privy Council, observed that all that was necessary to establish the relation of trustee and beneficiary was to prove that the legal title to property was in one person and that the equitable title to it was in another person.[59] If this rule in *Hardoon v Belilios*[60] were to be applied without exception, then B would have to be regarded as a constructive trustee of the legal chose in action for A, notwithstanding B's lack of notice of A's mistake when B acquired his legal title to the legal chose in action.

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55 *David Securities* (1992) 175 CLR 353, at 378 (per Mason CJ, Deane, Toohey, Gaudron and McHugh JJ).

56 *In re Diplock* [1948] 1 Ch 465, at 522 and 524 (per Lord Greene MR Wrottesley and Evershed LJJ).

57 *Miller v Race* (1758) 1 Burr 452; 97 ER 398.

58 [1901] AC 118.

59 Ibid, at 123.

60 [1901] AC 118.

However, in *In re Diplock*[61] the English Court of Appeal determined that a person who acquired legal title to property without giving value for it, but who had no notice of another person's existing equitable interest in it, was, in equity, an innocent volunteer in relation to that property, and not a constructive trustee of it.[62] In *Westdeutsche*[63] a majority[64] of the law lords endorsed this proposition of law. It is suggested that this proposition of law constitutes an exception to the rule, enunciated in *Hardoon v Belilios*,[65] that the separation of equitable title from legal title necessarily creates a trust. It is further suggested that a person who accidentally receives legal title to a chose in action by virtue of a mistaken payment into his bank account, but who, at the time of the mistaken payment is not aware of the payer's causative mistake, is an innocent volunteer, so that the equitable title to that chose in action is vested in the payer, and not in the payee, although the payer's equitable title does not make the payee a constructive trustee of that chose for the payer.

Returning to the hypothesis, B will hold the legal title to the chose as an innocent volunteer, and A will hold the equitable title to it. Nevertheless, as B is an innocent volunteer and not a constructive trustee of the chose in action for A, B will not, in equity, be liable to pay to A, from what equity would regard as B's own money (which does *not* include the chose in action), the value of the chose, although, at common law, B will be liable to pay to A, in an action for money had received, the value of the bank notes ($1000) which he originally received from A.

Thus, in equity, B will be liable to A in a tracing action only , namely, A will in equity have a proprietary[66] remedy only, whereas at common law B will be liable to A in an action for money had and received, namely, A will at common law have only a personal[67] remedy as against B.

If the money in B's bank account is *not* at any stage withdrawn by B, and if B becomes bankrupt after the opening of the bank account, then section 116(2)(a) of the *Bankruptcy Act* 1966 (Cth), which in terms applies to prevent only

61 [1948] 1 Ch 465.
62 Ibid, at 522 (per Lord Greene MR, Wrottesley and Evershed LJJ).
63 [1996] AC 669.
64 Ibid, at 707 (per Lord Browne-Wilkinson). Lord Slynn (at 718) and Lord Lloyd (at 738) concurred with Lord Browne-Wilkinson. The other (dissenting) law lords (Lord Goff and Lord Woolf) did not examine this issue.
65 [1901] AC 118.
66 *In re Diplock* [1948] 1 Ch 465.
67 *Australia and New Zealand Banking Group Limited v Westpac Banking Corporation* (1988) 164 CLR 662, at 673 (per Mason CJ, Wilson, Deane, Toohey and Gaudron JJ).

property held *in trust* by a bankrupt from being distributable amongst the bankrupt's creditors, should be extended, by analogy, to prevent property held by the bankrupt *as an innocent volunteer* for the benefit of another person from being distributable amongst the bankrupt's creditors.

Resulting Trustee

In *Westdeutsche*[68] the House of Lords unanimously[69] scouted the view that payment made pursuant to a contract that was void ab initio rendered the purported payee a resulting trustee for the benefit of the purported payer where the purported payee had no notice of the voidness of the contract when the purported payment was made.

The House did so principally on the ground that the nullity of the contract did not suffice to vitiate the payer's intention to transfer to the payee both the legal and the equitable title to the money.[70]

The House of Lords also advanced an alternative reason to support its view that there was no resulting trust. It ruled that the council could not have received the payment as a resulting trustee because, at the moment of receipt, the council did not have notice that the contract purportedly entered into between it and the bank was void ab initio, and so the council's conscience was not affected by its receipt of the bank's money.[71] Furthermore, the House of Lords held that by the time the council discovered that the contract was void ab initio, the money paid to the council had ceased to be traceable, so that at no time was there *concurrently* a receipt or retention of the property by the council *and* notice by the council that the property so received or so retained was received or retained pursuant to a putative but non-existent contract.[72]

It may be suggested that if the council had received the *legal* title to the money with notice that the contract was void ab initio, then the council would have become a *constructive*[73] trustee of the money, and not a resulting trustee of it. Notice by the council could not have made it a *resulting* trustee because, in

68 [1996] AC 669.

69 Ibid, at 689-690 (per Lord Goff); at 708 (per Lord Browne-Wilkinson); at 718 (per Lord Slynn); at 720 (Per Lord Woolf); and at 738 (per Lord Lloyd).

70 Ibid.

71 *Westdeutsche* [1996] AC 669, at 689 (per Lord Goff); at 706 and 709 (per Lord Browne-Wilkinson); at 718 (per Lord Slynn); at 720 (per Lord Woolf); and at 738 (per Lord Lloyd).

72 Ibid.

73 *Nelson v Larholt* [1948] 1 KB 339.

order to create a resulting trust, the settlor must have *intended*,[74] albeit only impliedly, the transferee to receive the property *as trustee*, whereas the bank in *Westdeutsche*[75] had intended, on the assumption made by the House of Lords in that case that such intention was not vitiated by the voidness of the contract, the council to receive the money, not as a mere trustee, but as an absolute owner. But even assuming that the intention to transfer absolute title to the money to the council *was* vitiated by the voidness of the contract, there would still not have been a *resulting* trust, because there would still not have been any implied *intention* by the bank to make the council a *trustee* of the money transferred to it. If the council had the relevant notice, then it would have received the money (the legal chose in action) as a constructive trustee, and not as a resulting trustee.

Defences to an action brought by the transferor to recover property ineffectually transferred by virtue of the transferor's mistake

In *Barclays Bank Ltd v W J Simms & Cook (Southern) Ltd*,[76] Goff J said:[77]

> …(1) If a person pays money[78] to another under a mistake of fact[79] *which causes him to make the payment*, he is prima facie entitled to recover it as money paid under a mistake of fact. (2) His claim may however fail if (a) the payer intends that the payee shall have the money *at all events*, whether the fact be true or false, or is deemed in law so to intend; or (b) the payment is made for good consideration, in particular if the money is paid to discharge and does discharge, a debt owed to the payee (or a principal on whose behalf he is authorised to receive the payment)by the payer or by a third party by whom he is authorised to discharge the debt; or (c) the payee has changed his position in good faith, or is deemed in law to have done so.

Proposition 2(a) is logically not a defence to a claim to recover property ineffectually transferred under a mistake. If there was a transfer made under a mistake, then the transfer was *caused* by the mistake. But if the transfer was *caused* by a mistake, the transferor could not have concurrently intended the

74 *Westdeutsche* [1996] AC 669, at 708 (per Lord Browne-Wilkinson).

75 [1996] AC 669.

76 [1980] 1 QB 677.

77 Ibid, at 695. Emphasis added.

78 This proposition applies also to *other* forms of property: *David Securities Pty Limited v Commonwealth Bank of Australia* (1992) 175 CLR 353, at 393 (per Brennan J).

79 This proposition has since been extended to include a mistake of law: *David Securities Pty Limited v Commonwealth Bank of Australia* (1992) 175 CLR 353; *Kleinwort Benson Ltd v Lincoln City Council* [1999] 2 AC 349.

transferee to have the property *'at all events'*.[80] There was *either* a causative mistake *or* there was not. This means that the transferor's intention that the transferee should have the title to the property *at all events* precludes the possibility that the transferor was induced to make the transfer on a mistaken assumption. An intention that the transferee is to have the property *at all events* is not a defence against the transferor's prima facie right of recovery: such an intention prevents the transferor's prima facie right of recovery from arising.

Proposition 2(b) is also not a defence to the transferor's prima facie right of recovery because in a case where the transferee gives good consideration to the transferor, the transferor does not at any time have a prima facie right of recovery. No such prima facie right of recovery is capable of arising because the transferee is, in such a situation, legally entitled to obtain the absolute ownership of the property at the moment of its receipt.[81]

However, Proposition 2(c) is a defence to the transferor's prima facie right of recovery. This is so because, at the moment of the transferee's receipt, there is created in favour of the transferor a prima facie right of recovery. This prima facie right may be only *subsequently* defeated by the transferee's adverse change of position in good faith and in reliance on the transfer.[82] However, it has been argued that the transferee's defence is not so restricted, and that even a change in the transferee's position which has *not* been brought about by the transferee, but which has been made for him, as a result of circumstances beyond his control, will constitute a defence *if* the change in the transferee's position would make it inequitable to compel him to make either complete or partial restitution to the transferor.[83] It is suggested that this argument is persuasive.

In *Kleinwort Benson Ltd v Lincoln City Council*[84] Lord Hope said that another defence to recovery was money paid in pursuance of a compromise over a disputed claim. Lord Hope was there echoing the view expressed by Brennan J in *David Securities*.[85] Nevertheless, where property is transferred pursuant to an agreement to compromise a disputed claim, it is the performance of that

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80 *Barclays Bank Ltd v WJ Simms & Cooke (Southern) Ltd* [1980] 1 QB 677, 695 (per Goff J). Emphasis added.

81 *David Securities* (1992) 175 CLR 353, at 378 (per Mason CJ, Deane, Toohey, Gaudron and McHugh JJ).

82 *Australia and New Zealand Banking Group Limited v Westpac Banking Corporation* (1988) 164 CLR 662; *David Securities* (1992) 175 CLR 353, at 385 (per Mason CJ, Deane, Toohey, Gaudron and McHugh JJ).

83 *National Bank of New Zealand Ltd* v *Waitaki International Processing (NI) Ltd* [1999] 2 NZLR 211, at 228-229 (per Thomas J, in the New Zealand Court of Appeal).

84 [1999] 2 AC 349, at 412.

85 (1992) 175 CLR 353, at 394-395.

agreement to compromise, and not any mistake made as to the merits of the original claim, which *causes* the transfer to be made.[86] Since the making of the transfer is not *caused* by any mistake on the part of the transferor, the transfer is valid, and the transferor will not have even a prima facie right of recovery.

Is the defence of adverse change of position available to the transferee where property which has been ineffectually transferred because of a mistake is traceable by the transferor?

Suppose that A, mistakenly believing that he owes B the sum of $10,000, hands to B a cheque for $10,000 in which B is named as the payee, and thereby purports to discharge the non-existent debt. Suppose that B shares A's mistake at the time of payment.

B uses this cheque to open a bank account for himself. B thereby becomes the legal owner of a chose in action against the bank for the repayment of the value of the cheque, plus interest (if any).[87] At this stage, B is an innocent volunteer who must recognise A's equitable ownership of the money in the bank.[88] Suppose that B does not make any other deposit into this account, and he does not make any withdrawals from it.

Relying on his bank balance of $10,000, namely, relying on the apparent validity of A's payment to him, B enters into a contract in which he agrees to pay C the sum of $10,000 for a package tour to be provided to him by C. B would not have entered into his contract with C, but for B's mistaken assumption that A had paid him (B) the sum of $10,000 in discharge of a debt of $10,000 owed to him by A.

By entering into a contract with C, B has adversely changed his position in reliance on A's payment, because if B refuses to proceed with the tour, he will be liable in damages to C for breach of contract. Assume that the damages for the breach of this contract would be $10,000.

Before B pays C the sum of $10,000 for the package tour, A discovers his mistake. A alerts B to their common mistake. A claims to be entitled to the sum of $10,000 in B's bank account on the ground that B, having now become aware of their common mistake, has become a constructive trustee for A of the

86 Ibid, at 395.
87 *Foley* v *Hill* (1848) 2 HLC 28; 9 ER 1002.
88 *In re Diplock* [1948] 1 Ch 465, at 522 (per Lord Greene MR, Wrottesley and Evershed LJJ).

legal chose in action which B has against the bank.[89] B disputes A's claim, invoking the defence of adverse change of position made by him before he received notice of their common mistake.[90]

Will A's claim succeed? It is suggested that, notwithstanding B's adverse change of position, A should be able to claim equitable title to the money in B's bank account because, A's money being still traceable in equity, the position in equity is that the title to the proceeds of the cheque has never left A. It should be open to A to argue that B's defence of adverse change of position would impact inequitably on A because A continues to be able to trace the proceeds of the cheque which he had mistakenly, and therefore ineffectually, given to B, being proceeds which remain intact in B's hands.

In such a situation, A, despite B's adverse change of position, is the more innocent of the two parties. Because A is able to trace the proceeds of the cheque, A is merely claiming continuing ownership of his own money. A is *not* claiming that B should pay him with B's *own* money. Technically, therefore, A is not making any claim which would diminish B's assets, and B's adverse change of position should not entitle him to obtain for himself an asset which, by using the process of equitable tracing, is seen to continue to belong to A.

89 *Westdeutsche* [1996] AC 669, at 715 (per Lord Browne-Wilkinson).

90 *David Securities* (1992) 175 CLR 353, at 385 (per Mason CJ, Deane, Toohey, Gaudron and McHugh JJ).