Case Notes

Garcia v National Australia Bank Ltd HCA 48, 6 August 1998[1]

Introduction: It's the Little Woman After All[2]

The issue of wives guaranteeing their husbands' business debts has been a vexed one in Australian law. A decision of the High Court in *Yerkey v Jones*,[3] particularly the approach of Dixon J who had found a "special equity" for wives who did not understand the nature of the transaction, was at odds with the more recent House of Lords decision in *Barclays Bank plc v O'Brien (Barclays Bank)*,[4] which rejected the "special equity" approach. The High Court has now decisively put the issue to rest in Australia in *Garcia v National Australia Bank Limited (Garcia)*. In doing so the court, by 5 to 1, favoured Dixon J's approach over that of the House of Lords. Gaudron, McHugh, Gummow and Hayne JJ delivered the main judgment. Callinan J separately supported the "special equity" approach. Kirby J, while agreeing with the orders, rejected the *ratio* of Dixon J and adopted a modified *Barclays Bank* approach.

One issue in the case was whether "special equity" was indeed the basis for the High Court's decision in *Yerkey v Jones* or whether it was an opinion of Dixon J alone. If the High Court held that *Yerkey v Jones* established a "special equity", then it could have overruled its earlier decision on the basis of changes in society. In doing so it would then be overruling a principle which had been part of the law since 1939. The NSW Court of Appeal had found that it was an opinion of Dixon J only and held therefore that they were not bound by it.[5] Kirby J also found that it was an opinion of Dixon J, spending some time on the point:

> "... to dispel any suggestion of disobedience to authority on the part of the

---

1 At the time of writing the case is unreported but it is available on the web at <austlii.edu.au/au/cases/cth/high_ct/1998/48.html>.

2 After S.M. Cretney, "The Little Woman and the Big Bad Bank", (1992) 108 *Law Quarterly Review* 534.

3 (1939) 63 CLR 649.

4 [1993] 4 All ER 417.

5 (1996) 39 NSWLR 577 at 598.

> Court of Appeal [indicating that] Dixon J's opinion is more vulnerable to revision when the law moves from protection of a single category to protection of defined relationships of which that category was at one time considered to be an illustration ... [and to remove] any impediment to this Court's reviewing the issue as one of legal principle rather than long-standing authority of the Court."[6]

But Gaudron, McHugh, Gummow and Hayne JJ considered "... the reasons for decision of Dixon J in *Yerkey v Jones* were not significantly different from the reasons of the other members of the Court ..."[7] and, in an implied criticism of the Court of Appeal, "... emphasised that it is for this Court alone to determine whether one of its previous decisions is to be departed from or overruled ...".[8] However, their Honours then indicated that their decision was not based:

> "... upon some confined analysis of the case intended to identify its ratio decidendi. Rather, we consider that the principles spoken of by Dixon J in *Yerkey v Jones* are simply particular applications of accepted equitable principles which have as much application today as they did then ..."[9]

The Facts

Mr and Mrs Garcia executed a mortgage over their home in favour of the bank in August 1979. The mortgage was an "all moneys" one given to secure a $5,000 loan to Mr Garcia for use in his business, although it was later also used to secure a joint personal loan. The home was jointly owned but was built on land which had been purchased by Mrs Garcia with financial help from her father. The bank had insisted on the land being put in their joint names when the matrimonial home was being built so that there would be a "breadwinner" on the title. From 1985 to 1987 Mrs Garcia signed four guarantees in favour of the bank. Three concerned her husband's business, Citizens Gold, and one other business. The guarantee of November 1987 was limited to $270,000 plus interest, costs and charges. The couple separated in September 1988 and in October 1989 there was an order to wind up Citizens Gold. Mrs Garcia was granted a decree nisi in November 1989 which became absolute in January 1990. In June 1990 she commenced proceedings in the Supreme Court that the mortgage and guarantees were of no effect or void. She sought relief under the principles of *Yerkey v Jones* and *Commercial Bank of Australia v Amadio*

---

6 *Garcia v National Australia Bank* HCA 48, 6 August 1998, at para 64.
7 Above n 6, at para 17
8 Above n 6.
9 Above n 6, at para 18.

(Amadio)[10] and under the *Contracts Review Act* 1988 (NSW). In August 1990 the respondent bank demanded payment under the November 1987 guarantee and mortgage for amounts owing by Citizens Gold.

The Trial

Mrs Garcia was successful in the Supreme Court on the basis of the "special equity" approach in *Yerkey v Jones*.[11] Young J said it was not open to a single judge to find that the *Yerkey v Jones* principle had been subsumed into the principle of *Amadio*, or alternatively such a step by a single judge would be most unwise.[12] The basis for the finding in favour of Mrs Garcia was that Mr Garcia had misrepresented the nature of the guarantee telling her it was to guarantee the overdraft of Citizens Gold only which would allow the company to deal in larger amounts of gold and that it was "risk proof" because it would always be backed by either money or gold. Young J found that the appellant did not understand that the guarantee was secured by the "all moneys" mortgage over the house and that she had signed it believing it was safe to do so. He preferred the evidence of Mrs Garcia over that of the bank on the issue of whether the bank had provided her with any explanation, finding that none was given. His Honour denied relief on the *Amadio* principle and said no case for relief was made out under the *Contracts Review Act*. The basis of the holding on the *Amadio* principle was the finding that, although the behaviour of Mr Garcia was unconscionable, the bank had no notice of the unconscionability because there was nothing to "... show the disability of the plaintiff was sufficiently evidenced to the bank to make it unconscientious that it accept [her] assent ...".[13]

Although actual undue influence was pleaded in the case neither the trial judge nor the Court of Appeal made any finding that it had been present. Still, Young J did find "pressure" had been used and that Mrs Garcia:

> "... appeared to have [signed] because her husband consistently pointed out what a fool she was in commercial matters whereas he was an expert, and because she was trying to save her marriage ..."[14]

Had the bank entrusted Mr Garcia to obtain Mrs Garcia's consent, that is, had he been regarded as its agent, then the bank would have been visited with any vitiating conduct of Mr Garcia, such as misrepresentation.

---

[10] (1983) 151 CLR 447.
[11] *Garcia v National Bank of Australia Ltd* (1993) 5 BPR 11,996.
[12] Above n 11, at 12,001.
[13] Above n 11, at 12,012.
[14] Above n 11, at 12,009.

But this was not the case. The claim under the *Contracts Review Act* did not succeed because there was nothing unconscionable about the bank's behaviour in the making of the contract. In the absence of a finding of actual undue influence or that the bank had notice of the husband's unconscionability, Young J was left with the principle of *Yerkey v Jones*, as enunciated by Dixon J:

> "... 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 ..."[15]

Earlier Dixon J referred to the relation of a husband and wife as "... not being divested completely of what may be called equitable presumptions of an invalidating tendency ...".[16] Given the misrepresentation by the husband and the lack of explanation by the bank Young J set aside the guarantees and made a declaration that Mrs Garcia owed no monies to the bank under the mortgage. Mrs Garcia obtained the declaration despite being a director and shareholder in Citizens Gold with his Honour holding that the companies were "... [nothing] more than Mr Garcia's creation and he was in complete control of them ...".[17]

The Court of Appeal

The Bank appealed to the Court of Appeal and Mrs Garcia cross-appealed.[18] The Court of Appeal held that it was not bound to follow *Yerkey v Jones* on the basis that the "special equity" approach of Dixon J had not been expressly adopted by the other members of the Court in their judgments and it noted there had been other recent cases doubting an assumption that a married woman was under any special disadvantage in transactions involving her husband.[19] The Court of Appeal also had the benefit of the House of Lords' decision in *Barclays Bank*,[20] rejecting the "special equity" in *Yerkey v Jones*. But it did not choose to follow the House of Lords' approach. Rather, it held that *Yerkey v Jones* had been subsumed

---

[15] Above n 3, at 683.

[16] Above n 3, at 675.

[17] Above n 11, at 12,006.

[18] Above n 5, at 598. There were two judgments: Mahoney P and Sheller JA. Meagher JA agreed with Sheller JA.

[19] *European Asian of Australia Ltd v Kurland* (1985) 8 NSWLR 192 at 200, per Rogers J; *Warburton v Whiteley* (1989) 5 BPR 11,628 at 11,629-30, per Kirby P, who had referred to the principle as "... anomalous, anachronistic and inappropriate ..."; *Akins v National Australia Bank* (1994) 34 NSWLR 155; *Teachers Health Investments v Wynne* (1994) 6 BPR 13,449.

[20] Above n 4.

by *Amadio* and it agreed with the trial judge that there was no basis for a finding for Mrs Garcia on the *Amadio* principle since she was under no "special disability". It also found no basis for relief under the *Contracts Review Act* and accordingly granted the appeal by the bank.

Barclays Bank plc v O'Brien

In *Barclays Bank* the House of Lords had sought to clarify the law on the place of wives as sureties. Speaking for the court, Lord Browne-Wilkinson rejected any theory that wives[21] be accorded special rights with regard to surety transactions. In doing so he indicated that the Australian High Court decision in *Yerkey v Jones*, along with the English Court of Appeal's "special equity" approach in the instant case,[22] were not to be followed. Lord Browne-Wilkinson indicated that the proper application of the doctrine of notice would obviate the need for any "special equity" for wives.[23] The court said if it could be shown that the lender ought to have made an inquiry when a reasonable man might have suspected fraud, that is, that it had constructive or actual notice of the debtor's undue influence or misrepresentation, then the creditor may not be able to enforce the surety. Constructive notice, an equitable concept, will arise where the lender is aware of facts which put it on inquiry as to the possible existence of an earlier equity.[24] In the case of a wife acting as a surety, Lord Browne-Wilkinson identified two factors which should put a creditor on notice: that the transaction on its face was not to the advantage of the wife and the "substantial risk" in such transactions that the husband has committed a legal or equitable wrong which would entitle the wife to set aside the transaction as between her and her husband.[25] He thought it "plainly impossible" to require the financial institution to inquire of one spouse whether they have been unduly influenced or misled by the other but thought it was reasonable to require the institution to take steps to bring home to the wife the risks she is running and to advise her to take independent advice.[26] The decision rested on the stated policy of balancing the:

> "... sympathy for the wife who is threatened with the loss of her home at the suit of a rich bank ... [with] an important public interest, viz the need to ensure that the wealth currently tied up in the matrimonial home does not become

---

[21] Lord Browne-Wilkinson did not confine the principles to wives and held they were equally relevant to all other cases where "... there is an emotional attachment between cohabitees ...", above n 4, at 431.

[22] [1992] 3 WLR 593.

[23] Above n 4, at 431.

[24] Above n 4, at 429, per Lord Browne-Wilkinson.

[25] Above n 4.

[26] Above n 4.

economically sterile. If the rights secured to wives by the law renders vulnerable loans granted on the security of matrimonial homes, institutions will be unwilling to accept such security, thereby reducing the flow of loan capital to business enterprises ..."[27]

The High Court decision

Gaudron, McHugh, Gummow and Hayne JJ acknowledged changes in Australian society since Dixon J had passed judgment but nevertheless found that a "significant number" of Australian women are in relationships "... marked by disparities of economic and other power ...".[28] But they said this is not the basis for the decision in *Yerkey v Jones*. Rather, *Yerkey v Jones* is based on the "trust and confidence" in the marriage relationship where, they said, one party, often the woman, may leave business judgments to the other spouse. In that context, the court said, the explanation given to the other may be incomplete, even wrong, sometimes without "... the slightest hint of bad faith ...".[29] Their Honours identified two classes of circumstances which Dixon J had said might affect the enforceability of a guarantee given by a wife:

"... actual undue influence by a husband over a wife [or] no undue influence but failure to explain adequately and accurately the transaction which the husband seeks not for the immediate economic benefit of the wife but of the husband ..."[30]

The appeal concerned the latter kind. Gaudron, McHugh, Gummow and Hayne JJ cited Dixon J in *Yerkey v Jones*[31] and said in the former class of case no explanation by the creditor will be sufficient, there must be independent advice or relief from the ascendancy of the husband.[32] The transaction would be voidable against the husband and against the creditor if it had left it to the husband to obtain the consent. In the second class of case, characterised by their Honours more as a lack of proper information than as an imbalance of power, they said the amount of reliance the creditor places upon the husband, for the purpose of informing his wife, must be of great importance.

"... If the creditor itself explains the transaction sufficiently, or knows that the surety has received 'competent, independent and disinterested' advice from a third party, it would not be unconscionable for the creditor to enforce it against

---

27 Above n 4, at 422.
28 Above n 6, at para 20.
29 Above n 6, at para 21.
30 Above n 6, at para 23.
31 Above n 3, at 684 - 686.
32 Above n 6, at para 23.

> the surety even though the surety is a volunteer and it later emerges that the surety claims to have been mistaken ..."[33]

Their Honours said that the only relevant question of notice was whether the creditor knew at the time of the taking of the guarantee that the surety was then married to the creditor. The majority also said there was nothing in *Amadio* to show that it overruled *Yerkey v Jones* or had been subsumed in it.[34] Unlike *Amadio*, the court said, the principles of *Yerkey v Jones* do not depend on the creditor, having at the time of guarantee, taken notice of some unconscionable dealing between the wife and husband. *Yerkey v Jones* begins with the recognition that the surety is a volunteer: a person who obtained no financial benefit from the transaction[35] and it depends on the surety being mistaken about the purport and effect of the transaction.[36] Their Honours cited Cussen J in *The Bank of Victoria Ltd v Mueller*[37] who drew a comparison with equity's treatment of gifts by a mistaken donor. They said the creditor could avoid the possibility that the surety will later claim not to have understood if it adequately explains the transaction. The court found Mrs Garcia was a volunteer who obtained no real benefit from the guarantee and allowed the appeal.

Principle confined to Married Women

Gaudron, McHugh, Gummow and Hayne JJ acknowledged that issues might emerge with regard to other like relationships short of marriage, including same sex relationships. They also acknowledged that there could be cases where it was the husband who was the surety. However, the majority, unlike the House of Lords, confined its finding to married women suggesting that any extension to other relationships may require consideration of additional issues, saying for example, that if cohabitation was the criterion then there would be questions about what the lender should know about the relationship.[38] Callinan J went further, indicating that he would not adopt the wider approach of the House of Lords, believing if such an extension was warranted it should be by legislative rather than judicial intervention.[39]

---

[33] Above n 6, at para 41.
[34] Above n 6, at para 28.
[35] Above n 6, at para 31.
[36] Above n 6, at para 33.
[37] [1925] VLR 642.
[38] Above n 6, at para 22.
[39] Above n 6, at para 109.

Kirby J

In a strong dissent, Kirby J rejected *Yerkey v Jones* and said the court should look for a "broader principle" not just married women, a classification he said, "... at once too narrow and too broad ..."[40]: too narrow in ignoring others areas of social inequality and too broad in ignoring "... the diversity and experiences of Australian women ...".[41] His Honour preferred to cast the obligation in terms of relationships of "emotional dependence". He rejected *Yerkey v Jones* on several grounds: that it is an historical anachronism; that the court should reject discriminatory stereotypes; that marriage is not "a suspect category" and on the basis of the economic arguments advanced in *Barclays Bank*. He also cited Cretney, that "... with capacity comes obligation ...",[42] suggesting that the principle would encourage people to seek to escape "their lawful obligations". Kirby J viewed the decision in *Yerkey v Jones* as unacceptable discrimination and said the court should "... avoid unprincipled discriminatory categories ... where so much legislative and judicial effort in Australia has been directed at removing [them] ...".[43] Kirby J favoured a reformulation of *Barclays Bank*, adopting a "relationship of emotional dependence" as the basis and it was on this ground that he found for Mrs Garcia.

Explanation or Advice

Because the surety-wife is said to be at risk of both undue influence and misrepresentation/ misunderstanding there is the practical question for banks of what they must do to counter these. An explanation by the bank to overcome any misunderstanding will be insufficient for actual undue influence. Actual undue influence occurring between a husband and wife is, by its very nature, not always easy for an outsider to detect. The approach of both Kirby J and the House of Lords in *Barclays Bank* emphasises independent advice and this may assist in protecting the bank. The majority approach, on the facts of *Garcia*, places less emphasis on the need for independent advice, yet the judgment demonstrates the risk a bank may run if it relies on its own explanation.

---

[40] Above n 6, at para 66.
[41] Above n 6.
[42] Above n 2, at 538 - 539.
[43] Above n 6, at para 66.

The Wife as Volunteer

The principle of *Yerkey v Jones* depends partly on the fact that the wife is a volunteer: that she has nothing to gain from the transaction because she hazards her own property to benefit her husband. However, frequently a wife does gain the benefit of enhanced prospects for the success of her husband's business. In this regard the surety-wife is unlike other sureties, such as parents, who are unlikely to gain any material benefit from its success. In *Garcia* the trial judge held that Mrs Garcia obtained no real benefit from entering into the transaction based on the fact that the companies were in the "complete control" of the husband.[44] But the facts do not suggest that any profits were quarantined from the family. In the High Court only Kirby J acknowledged that:

> "... [i]f the financial transactions in which Citizens Gold was involved had proved profitable, and if the personal relationships of the husband and wife had improved, it scarcely seems likely that the wife would have disclaimed the economic benefits as vigorously as she has now sought to escape the economic burdens ..."[45]

Unfortunately, with respect, this was not an issue which was extensively explored by the majority. The decision rested on a well recognised equitable principle of protecting a volunteer, but it missed the opportunity to relook at the issue of what constitutes a volunteer in the marriage relationship where potentially profits, as well as losses, might be shared.

Conclusion

The High Court has now given very strong support for the principle that married women, who guarantee their husbands' business debts, have a special place in the law. This special place arises because of the risk that women in a marriage relationship may be vulnerable to being misled or pressured by their husbands. The High Court has adopted an approach which recognises that, despite the many advances which Australian women have made in the past 60 years, decisions about money are still frequently taken by the husband. The High Court's approach also recognises that the principles of *Amadio*, which have gone a long way to protecting other vulnerable sureties, are often unsuited to protecting wives whose vulnerability, where it is present, is of a different type and is one which may not be apparent to a third-party. The majority approach, unlike that of the House of Lords, does not depend on there being a legal

[44] Above n 11, at 12,006.
[45] Above n 6, at para 53.

wrong, mere misunderstanding may be sufficient. This special treatment means that banks and other creditors who deal with married women must, to protect themselves, ensure that the wife has received a sound explanation of the transaction. The bank can counter any misrepresentation by its own explanation, if sufficient, but because of the danger of undue influence, a prudent bank will insist that the woman receives independent advice. Whether the fears of Kirby J that women may use the "special equity" to escape their "lawful obligations" are realised remains to be seen. Callinan J considered that many women, as a result of enhanced opportunities, would find it difficult to satisfy the court that they had "succumbed" to pressure or been misled by their husbands.[46] Interestingly, despite being a company director, running her own business and with a history of other investments, Mrs Garcia was able to satisfy the trial court that she did not understand the nature of the obligation into which she had entered. In the light of that finding, there is now a strong onus on banks to ensure their documentation is clear, their explanations thorough and comprehensible and old notions that they are not obliged to disclose risks to sureties are done away with, at least where the guarantor is a wife dealing with her husband's debts.

Anne Finlay
Senior Lecturer in Law
The University of Newcastle

[46] Above n 2, at para 112