

## PART VI – UNCONSCIONABLE DEALING

### I INTRODUCTION

#### A Definition

Unconscionable dealing is the 'unconscientious use of a superior position to the detriment of a party who suffers from some special disability or is in some special position of disadvantage' (*Amadio* per Mason J at 461).

Such dealing is said to occur 'whenever one party by reason of some condition or circumstance is placed at a special disadvantage vis-à-vis another and unfair or unconscientious advantage is then taken' (*Amadio* per Mason J at 462).

Several elements must be established:

- 1 *Special disability*
  - Not mere inequality
  - Impaired judgment
- 2 *Taking advantage*
  - Knowledge of disability
  - Procedural unconscionability
  - Substantive unconscionability
  - Onus of proof
- 3 *Causation*
  - Of entry into the contract by unconscionable conduct

#### B Preliminary Requirements

Restitutio is (surely) a requirement, but seldom (if ever) mentioned.

#### C Distinguishing from Other Bases for Rescission

The distinction between undue influence and unconscionable dealing is somewhat subtle; in both cases, contracting parties are apparently willing to enter into the transaction. The difference lies in the reasons for which they are willing:

*Although unconscionable conduct bears some resemblance to undue influence, there is a difference. In the latter the will of the innocent party is not independent because it is overborne. In the former advantage is taken of an innocent party who, though not deprived of an independent will, is unable to make a worthwhile judgment as to what is in his best interest (Amadio per Mason J at 461).*

In the case of undue influence, contractual intention is not the product of a free and voluntary will (but rather the dominance of the other party); by contrast, in the case of unconscionable dealing,

assent is willed but impaired (due to the other party unconscionably taking advantage of their special disability):

- Duress: party unwilling, but compelled to enter into the contract by the coercing party's illegitimate pressure (lowest degree of volition)
- Undue influence: dominant party's unfair abuse of their position causes the contracting party's will to become overborne such as to desire entry into the contract
- Unconscionable dealing: unconscientious party takes advantage of contracting party's special disadvantage, giving rise to a desire to enter into the contract, but one based on an impaired judgment about their best interests (highest degree of volition)

For example, *Louth* is not a case of undue influence because the will of the donor was not overborne by Diprose; instead, it was simply impaired by his special disability (emotional dependence).

## II CREATION OF THE RIGHT TO RESCIND

### A Special Disability

#### 1 Not mere inequality

A special disability is a circumstance or characteristic which

*seriously affects the ability of the innocent party to make a judgment as to his own best interests* (*Blomley v Ryan*).

#### ***Blomley v Ryan* (1956) HCA:**

##### Facts

- Blomley, the plaintiff sought specific performance of a contract of sale made by Ryan, a 78 year old farmer, the subject of which was his grazing property, for £25 000
- The defendant alleged that, at the time of the signing, he was 'an old man, lacking in education, suffering from the effects of intoxication, mentally and physically weak, without proper advice, unable to protect himself and on unequal terms with the plaintiff'
- Findings by Taylor J, the trial judge:
  - The defendant had on many previous occasions engaged in drinking bouts during the post-harvest season
  - The contract was signed during such a bout
  - On 20 April, when the contract was negotiated, the defendant's condition was such that he was 'incapable of considering the question of the sale with any real degree of intelligent appreciation of the matters involved'
  - This was reasonably apparent to the plaintiff
  - The defendant's condition left him at a serious disadvantage when negotiating the contract
  - The land was sold for £8-9000 under its market value
  - As a result, the plaintiff's claim was dismissed and the defendant's counter-claim for rescission granted

##### Issue

- Was the defendant suffering from a special disability such as to allow equity to intervene in the unconscionable advantage taken of his condition by the plaintiff?

#### Reasoning

- Fullagar J (at 405):
  - ‘The circumstances adversely affecting a party which may induce a court of equity either to refuse its aid or to set a transaction aside are of great variety and can hardly be satisfactorily classified.’
  - ‘Among them are
    - poverty or need of any kind,
    - sickness,
    - age,
    - sex,
    - infirmity of body or mind,
    - drunkenness,
    - illiteracy or lack of education, and
    - lack of assistance or explanation where assistance or explanation is necessary.
  - The common characteristic seems to be that they have the effect of placing one party at a serious disadvantage vis-à-vis the other.’
- Kitto J: special disability includes illness, ignorance, inexperience, impaired faculties, financial need, or other circumstances which affect his ability to conserve his own interests
- Was the defendant suffering from a special disability?
  - Yes, he was utterly incapable of forming a rational judgment about the sale
  - The transaction was procedurally unconscionable
    - The buyer knew of his special disability
    - Indeed, a bottle of rum was brought along to the negotiations for the very purpose of maintaining Ryan’s state of inebriation
  - Substantive unconscionability was also present
    - The sand was sold well under its market value
    - A very small deposit (£5) was provided
    - A comparatively low interest rate was specified for repayment
  - The transaction was procured by the unconscionable dealing constituted by Blomley’s taking advantage of, inter alia, Ryan’s drunkenness
- Did the defendant affirm the contract after regaining a normal state of mind?
  - Equity will not relieve unless there has been a prompt repudiation after a cessation of any vitiating circumstances
  - The defendant delayed, failing to repudiate until 22 July, by which time he had bought another property
  - On the facts, the defendant had not been supplied with a copy of the contract and did not have any real understanding of his position until early July (after obtaining a copy)
  - It was only once ‘the booze got out of his system’ that he was able to consider what had occurred in April
  - Because he did not appreciate what he had done until early July, repudiating in late July was sufficiently prompt

#### Decision

- The transaction was ‘thoroughly unconscionable’, one which ‘no court of equity’ could ‘allow to be enforced at law’; specific performance is ‘out of the question’

- To allow the contract to be enforced would be to allow the overreaching party to reap the full reward of his inequitable conduct
- The appeal is dismissed and the application for specific performance denied

The special disability may also be constituted by 'emotional dependence' (*Louth v Diprose*).

### ***Louth v Diprose* (1992) HCA:**

#### Facts

- Diprose was besotted with Louth; he bestowed various gifts and benefits upon her, despite her unwillingness to return his affections
- The transaction in question is Diprose's purchase and transfer of title in a house to Louth
- Diprose argues that the transfer should be invalidated on the basis that it was procured by unconscionable dealing on the part of Louth, who, it is claimed, took advantage of his special disability of 'emotional dependence or attachment'

#### Issue

- Is 'emotional dependence or attachment' a special disability the taking advantage of which may be said to constitute unconscionable conduct?

#### Reasoning

- Special disability
  - Fullagar J's list of special disabilities in *Blomley v Ryan* was non-exhaustive
  - 'Emotional dependence or attachment' is another such category capable of placing a party at a serious disadvantage vis-à-vis the other and impairing their ability to make a judgment as to their own best interests
- Knowledge
  - Yes, because Louth created it and was its continuing subject
- Procedural misconduct
  - Louth 'manufactured a false atmosphere of crisis', leading Diprose to believe that she required a house
- Substantive unconscionability
  - The Court reasons, somewhat mysteriously, that substantive unconscionability is present
- Causation
  - The transaction was procured by the unconscionable dealing

#### Decision

- The transaction is unconscionable and will not be enforced by a court of equity

## 2 *Impaired judgment*

The *Blomley* list has since been qualified by *Amadio*, which emphasises that more is required than a mere disparity in the bargaining power of the parties. What is required is an impairment of judgment:

*I qualify the word 'disadvantage' by the adjective 'special' in order to disavow any suggestion that the principle applies whenever there is some difference in the bargaining power of the parties and in order to emphasise that the disabling condition or circumstance is one which seriously affects the ability of the innocent party to make a judgment as to his own best interests (Amadio per Mason J at 462; emphasis added).*

### **Commercial Bank of Australia v Amadio (1983) HCA:**

#### Facts

- The Amadios seek to rescind a guarantee of their son's creditworthiness made with the bank
- The Amadios' son, a land developer, lived an opulent lifestyle, and had a close relationship with the bank (CBA) whereby they embarked on a profit-sharing venture
- However, his overdraft was rising and his company was going out of business
- V tells the bank that his parents will provide a guarantee of future creditworthiness
- V sees his parents and asks them for a guarantee, telling them it will only last 6 months
- The bank manager visits the Amadios; they sign the agreement
  - Mr Amadio is under the impression that the guarantee only lasts for 6 months
  - The guarantee is actually in perpetuity
- The Amadios argue that the guarantee is void because their son's unconscionable dealing induced their entry into the contract

#### Issue

- Can the Amadios rescind the agreement of guarantee with the bank on the basis of unconscionable dealing by the son, the borrower?

#### Reasoning

- The Amadios were under a special disability
  - The impropriety lies in the Amadios being deceived by their son
  - Their special disability is that they were dependent upon their son
    - They were old and illiterate, and thus dependent on V for explanation
    - The only information they were provided about the agreement was incorrect
    - There was no independent advice
    - There was a 'lack of assistance or explanation' (under Fullagar J's list in *Blomley*) on the part of the bank manager
  - Mason J at 464:
    - 'The respondents stood in a position of special disadvantage vis-a-vis the bank. The respondents' ability to judge whether the transaction was in their own interests was sadly lacking.'
    - 'The situation of special disadvantage in which the respondents were placed was the outcome of their reliance on and their confidence in their son, due in no small degree to their infirmities – they were Italians of advanced years, aged 76 and 71 respectively, having a limited command of written English and no experience of business in the field in which their son engaged. They believed that the business was a flourishing and prosperous enterprise, though temporarily in need of funds. In reality, as the bank well knew, the company was in a perilous financial condition.'
- The bank manager knew of the special disability
  - Mason J at 466-7:
    - 'Virgo was aware that the respondents were of advanced years and did

not have a good command of English. He had no reason to think that they had received advice from anyone but their son. Virgo knew that it was vital to Vincenzo to secure his parents' signature so that the company could continue in business.'

- 'It must have been obvious to Virgo that the transaction was improvident from the viewpoint of the respondents. It is inconceivable that the possibility did not occur to Virgo that the respondents' entry into the transaction was due to their inability to make a judgment as to what was in their best interests. Indeed, the inquiry by Mr Amadio Senior as to the duration of the arrangement should have alerted Virgo to the likelihood that Vincenzo had not adequately explained the transaction to them.'
  - 'The facts as known to him were such as to raise in the mind of any reasonable person a very real question as to the respondents' ability to make a judgment in their own best interests.'
- The bank took advantage of the Amadios' special disability by allowing the contract to be signed unaided
    - Mason J at 468:
      - 'The bank was guilty of unconscionable conduct by entering into the transaction without disclosing such facts as may have enabled the respondents to form a judgment for themselves and without ensuring that they obtained independent advice.'
    - Deane J at 479:
      - 'The bank cannot shelter behind its failure to [make a simple inquiry as to whether the transaction had been properly explained to Mr and Mrs Amadio]'
      - 'Wilful ignorance is not to be distinguished in its equitable consequences from knowledge' (*Owen and Gutch v Homan* per Lord Cranworth LC)
      - 'Mr and Mrs Amadio's disability and the inequality between themselves and the bank must be held to have been evident to the bank and in the circumstances it was prima facie unfair and "unconscientious" of the bank to proceed to procure their signature on the guarantee/mortgage'
      - 'The onus is cast upon the bank to show that the transaction was "in point of fact fair, just, and reasonable"'
  - There was substantive unconscionability
    - Mason J at 465:
      - 'The effect of the respondents' execution of the mortgage guarantee was disastrous for them though advantageous to the bank. The bank's security, inadequate before, was significantly improved. The value of the security provided by the mortgage guarantee exceeded the increase in the bank's exposure.'
  - The Amadios were induced to enter into the contract on the basis of the unconscionable dealing by the bank manager (in failing to disclose relevant facts to enable them to form a judgment for themselves)
    - 'The judge found that if Vincenzo "had disabused his parents' minds of their confidence in him, his parents would not have helped him". Any rational person knowing the circumstances of the company at the time would not have executed the instrument which they signed.'

#### Decision

- The Amadios can rescind their agreement with the bank on the basis of V's unconscionable dealing (4:1 majority)

A special disability can arise from either situational disadvantage (the result of a party's position in a relationship with another: *Bridgewater v Leahy*) or constitutional disadvantage (an inherent disposition of frailty). The Amadios suffered from both constitutional (by their age, general infirmity, and lack of education) and situational (by Vincenzo's abuse of his parents' confidence in him) disadvantage.

Though not conclusive of the matter, inadequacy of consideration (as where, for example, a house is sold at well below market value) is evidence which may support an inference of disadvantage (*Blomley v Ryan* per Fullagar J).

Subsequent treatments of unconscionable dealing in the context of s 51AA indicate that an experienced or well advised party will be far less likely to be deemed to suffer from a special disadvantage:

*In the case of an experienced business person who was legally advised, there must be something more than commercial vulnerability (however extreme) to elevate disadvantage into special disadvantage (ACCC v Samton Holdings).*

## B Taking Advantage

### 1 Knowledge

A disability may only be taken advantage of when the other party knows (or should have known) of it. However, wilful ignorance to a disadvantage or infirmity (eg, by failing to make relevant enquiries) cannot be relied upon to avoid unconscionable conduct. Thus, in *Amadio*, '[t]he bank cannot shelter behind its failure to [make a simple inquiry as to whether the transaction had been properly explained to Mr and Mrs Amadio]' (*Amadio*).

- In some circumstances, '[w]ilful ignorance is not to be distinguished in its equitable consequences from knowledge' (*Owen and Gutch v Homan* per Lord Cranworth LC)
- Mr Virgo (the bank manager in *Amadio*) knew of the Amadios' disabilities. The facts were such as to raise in the mind of any reasonable person a very real question as to the Amadios' ability to make a judgment in their own best interests.
- Similarly, in *Kranz*, having failed to assert undue influence, the applicant sought to invoke unconscionable dealing to avoid performance
  - There, the disability was alleged to be not knowing of the risks and nature of the transaction
  - The bank testified that they should have provided more information about the transaction
  - However, despite this admission, the Court held that there was no reason for the bank to be on notice
  - Thus, because the bank had no knowledge (and ought not to have known) of Kranz' special disability, there was no unconscionability in acting the way it did

### 2 Procedural unconscionability

The party attempting to have the contract set aside by a court of equity on the basis of an unconscionable dealing must establish that the party taking advantage has engaged in an unfair act or omission (ie, one that is procedurally unconscionable).

A procedurally unconscionable act or omission is something that the other party did (or should have done) during the course of the transaction:

- Typically, this will involve a positive act that is unfair (eg, manipulating or lying)
- However, a failure to take action (or even a concealment of facts) are still sufficient to constitute procedural unfairness (*Amadio*)

For example, in *Amadio*, the procedural unconscionability lay in the bank's failure to make inquiries as to whether the transaction had been properly explained.

### 3 Substantive unconscionability

Substantive unconscionability is concerned with the *outcome* of the transaction, which is measured by reference to its effect upon the parties' fortunes. Thus, for example, a property may have been sold for less than its market value (*Blomley v Ryan*) or an elderly couple may have forfeited a valuable security in exchange for a bank extending its exposure very little (*Amadio*).

To satisfy the requirement that there be an unfair taking advantage of a special disability, the innocent party must show procedural unconscionability (*Amadio*). However, there does not need to be shown substantive unconscionability. The fact that the transaction *is* substantively unconscionable is neither necessary nor sufficient to establish that an unfair advantage has been taken.

That said, the substantive outcome of the transaction is often considered.

For example, in *Amadio*:

- Procedural unconscionability (Mason J at 468):
  - 'The bank was guilty of unconscionable conduct by entering into the transaction without disclosing such facts as may have enabled the respondents to form a judgment for themselves and without ensuring that they obtained independent advice.'
- Substantive unconscionability (Mason J at 465):
  - 'The effect of the respondents' execution of the mortgage guarantee was disastrous for them though advantageous to the bank. The bank's security, inadequate before, was significantly improved. The value of the security provided by the mortgage guarantee exceeded the increase in the bank's exposure.'

### 4 Onus

Having shown the presence of a special disability and adduced evidence of the other party's knowledge of it, the onus shifts from the innocent party.

It is now presumed that advantage was taken, with the effect of dispensing with the need to show substantive or procedural unconscionability, so that the alleged wrongdoer must prove that the transaction was 'in point of fact fair, just, and reasonable' (*Amadio* per Deane J).

However, this reversal of onus is not consistently followed; it seems, however, to be supported by:

- Kitto J in *Blomley*;



- Deane J in *Amadio*; and
- Deane J in *Louth*.

It is not mentioned in *Bridgewater*, or, significantly, in any of Mason J's judgments. This seems indicative of the fact that it is not yet an established rule of law. It is thus advisable to adduce evidence of procedural unconscionability in addition to special disability and knowledge thereof.

### C Causation

The innocent party must have entered into the contract as a result of the unconscionable conduct. This is a 'reasonable person' test of causation; knowing the relevant facts and removed of their impaired judgment, a rational, reasonable person must not have chosen to freely enter into the contract.

For example, in *Amadio* (per Mason J at 466):

*The judge found that if Vincenzo 'had disabused his parents' minds of their confidence in him, his parents would not have helped him'. Any rational person knowing the circumstance of the company at the time would not have executed the instrument which they signed.*

Further examples:

- *Blomley v Ryan*: the farmer's participation in the transaction was procured by the unconscionable conduct of the buyer in ensuring his drunkenness
- *Louth v Diprose*: Diprose's gift was procured by Louth's unconscionable conduct in manufacturing a false atmosphere of crisis

#### ***Bridgewater v Leahy* (1998) HCA:**

##### Facts

- Bill York gave three properties to his nephew, Neil, with options to buy the remaining properties of his estate at extremely favourable prices in his will
- In 1988, Neil suggested Bill sell him and his wife, Beryl, some of the land specified in the option in Bill's will, for the price of selling his old land (\$150 000)
- Bill agreed to the proposal, and his solicitor drew up the contract of transfer
- The transfers took place in November 1988
- The solicitor did not advise Bill to obtain independent advice, but did have him examined by a doctor prior to executing the transfers; Bill was of sound mind and capable of making decisions about his personal affairs
- Evidence presented at trial suggests that, even if Bill had been advised by another lawyer about the transaction, the same result would have occurred
- Bill dies in 1989
- Neil subsequently exercises the option, paying \$200 000 for the remaining properties
- The value of the properties by this time totalled \$696 811
- This figure was divided among Bill's immediate family, who obtained \$50 000 each
- Bill's immediate family now seeks to have the transfer overturned on the basis of unconscionable conduct on the part of Neil, who is alleged to have taken advantage of Bill's trust

##### Issue

- Was the transaction procured unconscionably?

#### Reasoning

- Gleeson CJ and Callinan J (dissenting):
  - The essence of a special disadvantage is that the party is unable to judge for himself (*Blomley v Ryan* per McTiernan J)
  - ‘Absence of independent legal advice, like age, or infirmity, or some other condition or circumstance of the kind referred to may, in a given case, be of factual importance in determining whether special disability or weakness, of the relevant kind, exists, but it is important to bear in mind the essence of the supposed disability or weakness’
  - Bill York understood the transaction and appreciated the value of the land in question
  - When challenged by his daughter in November 1988, he indicated independence of mind and determination
  - There was thus no special disability on the part of Bill York
- Gaudron, Gummow and Kirby JJ:
  - Special disability
    - Bill’s special disability consisted of his emotional dependence and attachment (and also his physical dependence) upon his nephew, Neil
    - Enthusiasm itself may be the result of the exercise of undue influence
    - The question is not whether the transfer was procured with Bill’s assent but how that assent was produced (ie, whether it was a product of Neil’s taking advantage of Bill’s affection for him)
  - Taking advantage
    - Neil appreciated the ‘enormous affection’ and trust of his uncle of which he was the subject
    - ‘The equity to set aside the deed may be enlivened not only by the active pursuit of the benefit it conferred but by the passive acceptance of that benefit’
      - Just because Neil did not actively pursue the transfer with the intention of forestalling Bill changing his will, it does not mean his acceptance of the benefit was not unconscionable
    - There is procedural unconscionability in Neil’s bargaining misconduct
      - But surely: Bill is doing what he wants to do
      - Neil initiated the transaction but did so to get money for his family
      - HCA: the lack of *independent advice* is what constitutes the procedural unconscionability (Bill’s solicitor had him medically examined and declared to be of sound mind prior to the transfer, but not independent advice was given)
    - There is also substantive unconscionability
      - Neil obtained nearly \$1 000 000 in assets for just \$350 000
      - This represents an extreme undervaluing of the property
    - Importantly, it is mentioned that passive receipt of a benefit from the transaction may be enough to constitute taking advantage
  - Causation
    - Even if York’s judgment had not been impaired by the lack of independent advice, he would still have acted the way he did
    - It is thus difficult to say he was induced by Neil’s taking advantage of York’s emotional attachment to enter into the contract

#### Decision

- Rescission of the contract is granted (3:2)
- Majority: the status quo cannot be restored; instead, the deed of forgiveness should instead be set aside but not the transfers allowed to stand (thus, Neil is obliged to pay the remaining \$546 811 of the purchase price)

## II EXERCISE OF THE RIGHT TO RESCIND

### A *Partial Rescission*

In *Amadio*, Deane J mentioned the possibility of partial rescission as a remedy for unconscionable dealing. Where the innocent party indicates a willingness to participate in the transaction to a particular extent or of a certain nature, but, by virtue of the other party's unconscientious taking advantage of their impaired judgment, they enter into a transaction of a different nature or to a different extent, the transaction may only be set aside to the extent that it differed to that to which the innocent party was prepared to assent.

For example, in *Amadio*, the Amadios indicated a willingness to sign a guarantee for the period of six months and to the extent of \$50 000 (though the actual guarantee was not time-limited and had no upper threshold). It might thus be possible to argue for partial rescission of the guarantee, so that only \$50 000 would be owing for future losses incurred by their son.

Ultimately, on the facts, the full transaction was set aside by Deane J, because had the Amadios known the truth of their son's accounts (ie, had the bank manager explained the relevant facts about their son's business dealings and advised that they seek independent advice) they would not have signed the guarantee *at all*. No partial rescission is possible, because the special disability impaired their judgment for the entirety of the transaction – including previous representations of extravagance and opulence made by their son.

*Bridgewater v Leahy* affords an example of partial rescission. Deeds for the transfers of property to Neil were left un-rescinded; only the deed that absolved Neil from payment of the full amount owing was rescinded. Further, Neil was obligated to pay an allowance. This constituted partial rescission of the contract of transfer on the basis of unconscionable dealing.

### B *Equitable Remedies*

Where it can be shown that the contract was induced by unconscionable dealing, equity will intervene to relieve against obligations it imposes. Equitable rescission involves rendering a contract 'voidable' – a process slightly different to common law voiding of a contract. A voidable contract is one which the parties can elect to void. It does not occur automatically.

### C *Statutory Remedies*

Section 51AA of the *Trade Practices Act 1974* (Cth) allows ss 80, 82 and 87 to grant relief against unconscionable conduct. The unconscionable conduct prohibited by s 51AA is that within the meaning of the unwritten law, (probably, though still somewhat controversially) as mediated by equitable principles of unconscionable dealing.

## II LOSS OF THE RIGHT TO RESCIND

### A *Lapse of Time*

If the innocent party discovers that they have been taken advantage of the other party, but does nothing about it for some time after this point, it may not be possible to seek to rescind the agreement (since this gives rise to the inference that they were either under no especial disability during the period of the transaction or have ultimately affirmed the contract by conduct; the latter possibility was mentioned in *Blomley v Ryan*).

In *Blomley*, it was only when Bill's neighbour told him that he had been 'ripped off' by the buyer that Bill suddenly developed the urge to rescind the contract. This was several months after the transaction, so it was alleged that the contract had been affirmed by Bill's failure to rescind it. However, the Court ruled that Bill rescinded the contract as soon as he understood its full nature and effect, which was when the effects of the intoxication had worn off, he had been delivered a copy of the contract of sale, and had some time to consider its meaning.