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KNOWING RECEIPT IN THE TORRENS CONTEXT

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I INTRODUCTION

There has long been a tension between indefeasibility and liability *in personam*. Because liability *in personam* provides a means for the knowledge of a registered proprietor to be relevant to their liability even in the absence of statutory fraud, this diminishes the principle of indefeasibility. This situation is exacerbated by recent decisions that seek to align recipient liability with the principle of unjust enrichment.

The judgment of Lord Selbourne LC in *Barnes v Addy*¹ refers to people who ‘receive and become chargeable with some part of the trust property’² – under which the recipient may be liable for receiving trust property that should not have been transferred to them. This principle has been termed ‘knowing receipt’ and is now becoming known as ‘recipient liability’.³ Removal of the term ‘knowing’ from the description has been coincident with calls for the rejection of the requirement of any kind of knowledge.⁴ This change has been driven by a desire to bring coherency to the law through recognising that recipient liability should be classified as part of the law of unjust enrichment, and should not require knowledge as a condition of liability.

The paper begins by contrasting the fraud exception with liability *in personam*. It examines the question whether or not recipient liability should be strict, and demonstrates difficulties with this outcome that can be seen by considering decisions in States that have rejected the principle of strict recipient liability.

II IMPACT OF THE FRAUD EXCEPTION

Although Australian and New Zealand Torrens statutes do not expressly allow liability *in personam* in relation to registered titles,⁵ the possibility of such a claim

¹ (1874) 9 Ch App 244 (*Barnes v Addy*)

² *Ibid* 251.

³ LexisNexis NZ, *Land Law in New Zealand*, vol 1 (at service 12) ¶9.055.

⁴ Peter Birks, ‘Misdirected funds: restitution from the recipient’ [1989] *Lloyds Maritime and Commercial Law Quarterly* 296, 298; Keith Mason, ‘Where has Australian restitution law got to and where is it going?’ (2003) 77 *Australian Law Journal* 358, 368.

⁵ Except in s 185(1)(a) of the *Land Title Act 1994* (Qld).

was confirmed by the Privy Council in *Frazer v Walker*⁶ where it was held that the principle of indefeasibility ‘in no way denies the right of a plaintiff to bring against a registered proprietor a claim *in personam*, founded in law or in equity, for such relief as a Court acting *in personam* may grant’.⁷ This statement was adopted by the High Court of Australia in *Breskvar v Wall*⁸ where it was recognised that ‘[p]roceedings may of course be brought against the registered proprietor... by persons setting up matters depending upon the acts of the registered proprietor himself’.⁹

In the context of Torrens land, the concept of knowledge as it relates to liability of a registered proprietor has traditionally been governed by the fraud exception. Fraud in the context of New Zealand Torrens legislation has been explained as meaning¹⁰

...actual fraud, eg, dishonesty of some sort, not what is called constructive or equitable fraud –... brought home to the person whose registered title is impeached or to his agents.... The mere fact that he might have found out fraud if he had been more vigilant, and had made further inquiries which he omitted to make does not of itself prove fraud on his part. But if it be shewn that his suspicions were aroused, and that he abstained from making enquiries for fear of learning the truth, the case is very different, and fraud may be properly ascribed to him.

This test imports a notion of dishonesty greater than mere negligence. In Australia, it has been recognised that the concept of fraud in Torrens statutes is narrower than the full extent of equitable fraud,¹¹ requiring that the conduct ‘has that element of dishonesty, of conscious moral turpitude or wickedness such as would justify the intervention of a court...’.¹² From the addition of this more serious requirement, it seems that ‘New Zealand courts are much readier than their Australian counterparts to

⁶ [1967] NZLR 1069.

⁷ Ibid 1078.

⁸ (1971) 126 CLR 376.

⁹ Ibid 384-385.

¹⁰ *Assets Co Ltd v Mere Roihi* [1905] AC 176, 210.

¹¹ *Bahr v Nicolay (No 2)* (1988) 164 CLR 604, 614.

¹² *Russo v Bendigo Bank Ltd* [1999] 3 VR 376, [42].

find a purchaser fraudulent on the basis of notice'.¹³ However, a recent decision of the New Zealand High Court provides authority that supports the distinction between fraud and recipient liability where the recipient is a volunteer.¹⁴

III SHOULD RECIPIENT LIABILITY BE STRICT?

The late Professor Birks claimed that a person who comes under recipient liability has been unjustly enriched by the receipt of property that does not belong to them. The recipient is then liable either to be made a trustee (and therefore to hand back the property) or to pay back a sum equivalent to the value of the asset received by an action in unjust enrichment.¹⁵ An action in unjust enrichment relating to recipient liability must conform to the principles of unjust enrichment, namely that there is no requirement of knowledge (also called 'strict liability').¹⁶

The unjust enrichment model advocated by Birks is based on his taxonomy of causative events. Birks claimed that 'rights realized by courts can be said to arise from four genera of events, from wrongs..., from manifestations of consent, from unjust enrichment, and from miscellaneous other events'.¹⁷ Birks places recipient liability under the category of unjust enrichment, requiring the receipt of property belonging to another. The response of the law is then to raise a right in the plaintiff to restitution.

However, Professors Grantham and Rickett maintain that the taxonomy of events has five categories, not four. They claim that 'once the right *in rem* is in existence there is no conceptual impossibility in the notion that the property right can generate further rights'.¹⁸ This means that when a property right is interfered with, a right *in personam* can arise that allows the right holder to vindicate their property right against the

¹³ Elizabeth Cooke and Pamela O'Connor, 'Purchaser Liability to Third Parties in the English Land Registration System: A Comparative Perspective' (2004) 120 *Law Quarterly Review* 640, 647.

¹⁴ *Smith v Hugh Watt Society Inc* [2004] 1 NZLR 537.

¹⁵ Peter Birks, *Unjust Enrichment* (2nd ed, 2005) 68.

¹⁶ *Ibid* 157.

¹⁷ Peter Birks, 'Rights, Wrongs, and Remedies' (2000) 20 *Oxford Journal of Legal Studies* 1, 27.

¹⁸ Ross Grantham and Charles Rickett, 'Property Rights as a Legally Significant Event' (2003) 62 *Cambridge Law Journal* 717, 734.

defendant. In effect, this is equivalent to claiming that a property right is an ongoing event that generates personal rights when the property right is interfered with by another person. It is these personal rights that allow the original proprietary right to be vindicated. Their thesis is that in respect of recipient liability, 'the relevant event is property'.¹⁹ This primary right can then inform the action in recipient liability, whether it is articulated as restorable enrichment or wrongdoing.

Moreover, they claim that the event cannot be sourced in the event of unjust enrichment as the very assertion that the plaintiff retains beneficial title to an asset in the defendant's hands doubles as a denial of unjust enrichment.²⁰ The argument for exclusivity between property and unjust enrichment has the support of the House of Lords.²¹

However, the next section will detail recent Australian and New Zealand cases that have expressed sympathy for Birks' approach in the area of recipient liability where the property is Torrens land. This trend must be resisted if the law of unjust enrichment is to be contained within the conceptual bounds propounded by Grantham and Rickett. To give primacy to the law of unjust enrichment in relation to Torrens land is equivalent to a rejection of the principles Torrens originally stood for. Land would become less marketable as prospective purchasers became concerned that they might be subject to strict recipient liability.

IV JUDICIAL SYMPATHY FOR STRICT RECIPIENT LIABILITY

In Victoria, in *Koorootang Nominees Pty Ltd v Australia and New Zealand Banking Group Ltd*²² the managing director of a trustee company also operated his own separate business which needed to borrow money from a bank. The managing director provided securities over property of the trustee company. This was an unauthorised

¹⁹ Ross Grantham and Charles Rickett, *Enrichment and Restitution in New Zealand* (2000) 36.

²⁰ Ross Grantham and Charles Rickett, 'Property Rights as a Legally Significant Event' (2003) 62 *Cambridge Law Journal* 717, 743.

²¹ *Foskett v McKeown* [2001] 1 AC 102, 127, 132.

²² [1998] 3 VR 16 ('*Koorootang*')

act as regards the trust. The bank was aware that the securities, which included a mortgage, were being provided by a trustee company, and it acted both dishonestly and fraudulently when it received the trust property as security without inquiring of the other directors or beneficiaries as to the power of the trustee company to mortgage the land. Due to the fraud, the bank did not obtain an indefeasible title in respect of the mortgage. As the bank had not yet enforced the mortgage, it was set aside.

In respect of the mortgage, Hansen J favoured the thesis of Professor Birks that 'the liability of a person in receipt of misapplied trust property is most appropriately governed and explained by the law of restitution of unjust enrichment'.²³ Under this principle, the plaintiff need not prove knowledge to establish prima facie liability against a recipient of trust property. This was obiter because Hansen J found that the bank had acted fraudulently due to the wilful failure of the bank's agent to direct his mind to the correct course of inquiry.²⁴

The New South Wales Court of Appeal has developed strict recipient liability in *Say-Dee Pty Ltd v Farah Constructions Pty Ltd*²⁵ where a property developer company owed fiduciary duties to another company that it was in a joint venture with. It breached these fiduciary duties through abusing information it had gained with respect to the development potential of a particular site. The defendant developer had caused parties associated with it to purchase adjoining sites, preventing the development of the original site unless the adjoining sites could also be purchased for the benefit of the joint venture. The associated parties were required to hold the adjoining sites on constructive trust for the joint venture.

Tobias JA (delivering the unanimous judgment of the Court of Appeal which included Mason P and Giles JA) stated;

²³ Ibid 100.

²⁴ Ibid 126.

²⁵ [2005] NSWCA 309.

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‘I see no reason why the proverbial bullet should not be bitten by this Court in favour of the Birks/Hansen approach. In my opinion there is support for the adoption of the restitutionary approach in *Lipkin* in the House of Lords and in the exposition on the subject by Hansen J in *Koorootang*...’²⁶

It appears that the statements of Tobias JA were obiter as the recipients in *Say-Dee*²⁷ had knowledge of the breach of fiduciary duty. Taken to its logical conclusion, this argument shows that it was unnecessary for the court to even refer to the principle of unjust enrichment. The view that unjust enrichment is a subsidiary doctrine would hold that the recipients were not enriched at all as they remained under an equitable obligation to give up the gain (in the form of monopoly development rights) to the subject of the fiduciary duties.

In *Tara Shire Council v Garner*²⁸ the council had purchased a bore from the owners, which was the water supply for the township of Moonie. Unfortunately, the council did not register the transfer. When the owners sold the property (the Moonie Motel), they informed the purchaser that they did not own the bore, and that the sale did not include lot 3, which was the bore subdivision. The purchaser registered the transfer and then refused to convey the bore to the council. The case was an appeal against the interlocutory decision to join the purchasers as a defendant. In refusing the appeal, it was held that an arguable case existed that the vendor held the bore on constructive trust for the council. This trust had arguably been breached when the vendor transferred the whole property to the purchaser, and the purchaser registered the transfer with knowledge of the breach of trust, so as to make the purchaser hold the bore on constructive trust for the council.

In the Queensland Court of Appeal, Atkinson J said that ‘[a] possible explanation for the absence of a dishonesty requirement under the first limb is that it is a restitution-

²⁶ [2005] NSWCA 309 [232].

²⁷ [2005] NSWCA 309.

²⁸ [2002] QCA 232.

based principle aimed at avoiding unjust enrichment'.²⁹ However, the Queensland Court of Appeal was unwilling to rule out knowledge as a condition of liability.

The result in this case appears to be contradictory. In choosing unjust enrichment as the basis of the claim in recipient liability, Atkinson J has impliedly rejected the view that property is a category of event that can be the basis of the claim. On the other hand, allowing property to be considered an event that generates the claim in recipient liability tends toward an acceptance that property is the basis of the claim. It would follow that knowledge is relevant to a claim in recipient liability and therefore strict liability does not apply.

In *Smith v Hugh Watt Society Inc*³⁰ members of the New Zealand Labour Party had conducted fundraising activities to buy a hall for the benefit of the members of the Labour Party in the Onehunga electorate. Although registered in the name of one person, it was held on trust for all the members in the electorate. The hall was eventually transferred, without consideration, to the Hugh Watt Society Inc. This was a breach of trust because the consent of the beneficiaries had not been obtained. Later, the society sold the hall and used the proceeds to purchase a residential unit. The rules of the society were then changed so as to exclude members of the Labour party from having the benefit of the unit. The members claimed that the society had been unjustly enriched at their expense.

Randerson J found that the society had imputed knowledge of a breach of trust and imposed a constructive trust as a remedy for recipient liability 'probably on the basis of unjust enrichment...'.³¹ The society held the unit in trust for the members of the Labour Party in the Onehunga electorate at the time the electorate ceased to exist. Although this result appears to follow the argument of Professor Birks, strict liability was not adopted, and therefore indefeasibility is not challenged by unjust enrichment in this jurisdiction. The same conflict is raised here as in the previous case.

²⁹ Ibid [61].

³⁰ [2004] 1 NZLR 537.

³¹ Ibid [67].

Acceptance of unjust enrichment as the basis of recipient liability is equivalent to rejecting a knowledge requirement, yet the knowledge requirement was retained (meaning that the true basis of recipient liability is in the law of property not the law of unjust enrichment). The argument that there is a natural exclusivity between the principles of unjust enrichment and property must be therefore regarded as true, especially when the principle of indefeasibility is brought to bear on the issue.

V JUDICIAL OPPOSITION TO STRICT RECIPIENT LIABILITY

Some recent cases have rightly opposed the idea that recipient liability can be strict. Recipient liability was discussed by the Victorian Court of Appeal in *Macquarie Bank Ltd v Sixty-Fourth Throne Pty Ltd*³² where a bank had lent money on the security of a mortgage that was forged by the debtor. The bank had not been fraudulent within the Australian definition of Torrens fraud, but it did have information that could have led it to conclude that the debtor did not have the power to mortgage the assets. It did not make such a conclusion, but it did not stand to gain from failing to come to such a conclusion. It was claimed that the bank was liable for knowing receipt of trust property. Winneke P thought that

[e]quitable claims should not be emasculated by setting the threshold level of conduct, short of statutory fraud, too high; on the other hand it is, in my view, an argument of equally compelling force that the threshold should not be set so low as to defeat the concept of indefeasibility... If, therefore, the registration of a mortgage over trust property is to be regarded as a 'knowing receipt of trust property', the balancing of the competing philosophies requires, in my view, that the registration has been achieved as a result of conduct by the mortgagee amounting to want of probity before its registered interest can be defeated.³³

This want of probity was not to be found where, as in the instant case, registration of the mortgage had been honestly obtained. The fact that the bank had not diligently

³² [1998] 3 VR 133.

³³ Ibid 136.

checked the ability of the debtor to mortgage the assets could have amounted to a want of probity, but it was to the bank's disadvantage that it did not do this. Winneke P thought that this made it significantly different to *Koorootang*³⁴ where such failure was in the interests of the lender. Winneke P further thought that authorities on constructive notice such as *Baden, Delvaux and Lecuit v Société General pour Favouriser le Développement du Commerce et de l'Industrie en France SA*³⁵ were inapplicable to Torrens land because they did not consider the possible impact of the concept of indefeasibility.

Tadgell JA stated that the doctrine of the bona fide purchaser for value without notice was at odds with the Torrens system.³⁶ No alternative system of constructive notice for the purposes of Torrens land was embarked on. *Koorootang*³⁷ was distinguished on the basis that there had been no fraud in the instant case.

This position in Victoria has been cited with approval in Western Australia in *Conlan v Registrar of Titles*³⁸ where a contributory mortgage scheme had collapsed. Most of the difficulties in this case arose from insufficient record keeping, but recipient liability was relevant as the trustee company sometimes transferred mortgages to certain named investors. Owen J expressed sympathy for the decision in *Macquarie Bank*.³⁹ However, it was not necessary to go further than this because an *in personam* cause of action had not been fully argued, or even identified.⁴⁰ Nevertheless, Owen J stated that a court 'must not... develop a rule of equitable principle that is so broad as to make inroads into the principle of indefeasibility. That principle must be paramount'.⁴¹

³⁴ [1998] 3 VR 16.

³⁵ [1983] BCLC 325.

³⁶ [1998] 3 VR 133, 152.

³⁷ [1998] 3 VR 16.

³⁸ (2001) 24 WAR 299.

³⁹ *Ibid* [285].

⁴⁰ *Ibid* [286].

⁴¹ *Ibid* [289].

If recipient liability is based on property rights, or in the law of wrongs then this appears to mandate some kind of requirement of knowledge as a condition of liability. Apart from an ‘instinctive preference for liability grounded in conscious fault...’⁴² there is also the view that absence of a requirement of knowledge would throw inappropriate liability on third party recipients,⁴³ and that this would challenge the ‘defendant’s interest in the security of his receipt’⁴⁴ This view is based on the idea that equitable property rights are more difficult for a defendant to discover than legal property rights and therefore should not apply where the defendant has no knowledge of them.

VI CONCLUSION

Unjust enrichment must not be allowed to undermine the principle of Indefeasibility. There has been considerable tension between indefeasibility and the *in personam* doctrine, and this tension would be increased if the dominant view of unjust enrichment is accepted in relation to Torrens land. Recent judgments in several Australian States and New Zealand have included unnecessary references to unjust enrichment. As a subsidiary doctrine, unjust enrichment does not require strict recipient liability and therefore poses no threat to the principle of indefeasibility.

The judgment of Lord Selbourne LC in *Barnes v Addy*⁴⁵ provided the basis of the claim under which the recipient may be liable as if they were a constructive trustee. Originally termed ‘knowing receipt’, the evolution of this concept into ‘recipient liability’ should not be sidetracked onto the path that was first suggested by Professor Birks. Rejection of the strict liability argument has the benefit of bringing coherency to the law through recognising that indefeasibility is paramount in Torrens systems.

⁴² John Stevens, ‘No New Landmark – An Unconscionable Mess in Knowing Receipt’ [2001] *Restitution Law Review* 99, 103.

⁴³ Struan Scott, ‘Recovery of Misappropriated Trust Money From Third Parties: Knowing Receipt and the Law of Restitution’ (1996) 8 *Otago Law Review* 467, 469.

⁴⁴ Ross Grantham and Charles Rickett, *Enrichment and Restitution in New Zealand* (2000) 288.

⁴⁵ (1874) 9 Ch App 244.