

LENDER LIABILITY IN UNJUST ENRICHMENT TO THIRD PARTY SERVICE PROVIDERS

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I. INTRODUCTION

Claims of unjust enrichment in respect of services, performed under contract which incidentally benefit a third party, are on the rise in Australia. This article examines this phenomena, and looks at the availability and desirability of causes of action against the third party. Particular implications for lenders of the acceptance of such a cause of action in Australian law are discussed. Future legal developments in this area may be of concern to lenders in situations where a borrower has contracted for services for which it is unable or unwilling to pay. The service provider may sometimes be in a position to bring an action against the lender if the lender can be said to have been unjustly enriched by the provision of services to the borrower. This may be the case where, for example, the value of the lender's security has been increased by the efforts of the service provider.

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II. THE ISSUE FOR LENDERS: THIRD PARTY UNJUST ENRICHMENT CLAIMS FOR THE PROVISION OF SERVICES

This article is concerned with recent developments in the Australian law of restitution,¹ which arguably have the potential to affect certain operations of financial institutions. Many claims of unjust enrichment for the provision of services where third parties to the contract have benefited have been made recently in the Australian courts. However, these claims are usually as an argument of last resort by the plaintiff because they are of questionable validity at law. Even if such claims are accepted, a significant amount of doubt remains as to their appropriate scope and operation.

In recent years, the general availability of unjust enrichment claims has been more readily recognised by Australian courts, particularly in light of comments made in landmark High Court decisions such as *Pavey & Matthews Proprietary Limited v Paul*² and *David Securities Pty Ltd v Commonwealth Bank of Australia*.³ Comments made by two High Court judges, Deane and Gaudron JJ, in *Trident General Insurance Co Limited v McNiece Bros Proprietary Limited*⁴ have also sparked a significant amount of academic debate about the validity of claims of unjust enrichment in Australia.⁵ Additionally, the legal community is becoming more willing to entertain the idea of unjust enrichment claims and, more generally, the validity of the law of restitution, on which such claims are based.⁶

At its bare minimum, the doctrine of unjust enrichment involves attempting to reverse enrichments of defendants which have come about 'at the expense' of a particular plaintiff in circumstances where the enrichment may be seen objectively as being 'unjust'. 'Enrichment' appears to include, amongst other things, both actual receipt of moneys by the defendant which were not intended for the defendant's use and the obtaining by the defendant of some benefit from services provided by the plaintiff in the absence of any recompense (by the

1 This article assumes that there is a separate 'law of restitution' in Australia, or at least a body of 'restitutionary principles' in light of recent High Court decisions which are discussed below. See for example *Pavey & Matthews v Paul* (1987) 162 CLR 221 and *David Securities Pty Ltd v Commonwealth Bank of Australia* (1992) 175 CLR 353, as well as some obiter comments in *Trident General Insurance Co Limited v McNiece Bros Proprietary Ltd* (1988) 165 CLR 107. However, the author is aware that some would dispute this view. Consideration is given to this issue below, at Part IIIA.

2 *Ibid.*

3 Note 1 *supra*. Note, however, that this case dealt with an unjust enrichment claim in a different context to that which arose in *Pavey*. The earlier case involved an unjust enrichment claim in the context of an unenforceable contract for services, whereas *David Securities* dealt with unjust enrichment in the context of a mistaken payment, which is perhaps the more traditional sense of a restitutionary claim.

4 Note 1 *supra* at 146, per Deane J; 175-177, per Gaudron J.

5 Justice Gaudron's judgment in particular in this case has attracted a significant amount of criticism from the legal community. Her views, and their critics, are discussed in more detail below, in Part IIIA.

6 In recent years, particularly since the handing down of the High Court decisions mentioned above, academic teaching and writing on the law of restitution in Australia has increased. One significant example is the recent publication of the first Australian comprehensive textbook on the law of restitution: K Mason and JW Carter, *Restitution Law in Australia*, Butterworths (1995).

defendant to the plaintiff) for those services. These are both considered as examples of the category of 'enrichment by subtraction from the plaintiff', the other major category of unjust enrichment claims being based on restitution for 'wrongs done to the plaintiff'.⁷

Although there are several recent Australian restitutionary developments which may be of concern to lending institutions,⁸ this article focuses on situations where a lender may potentially be held liable in an unjust enrichment claim in relation to services provided to its customer where that customer has been unable or unwilling to pay for those services. If the lender may be said to have received some benefit from those services as a third party, it may potentially attract a claim in unjust enrichment. The usual case will be where the services provided to the principal borrower have in some way increased the value of the lender's security interest over a particular part of the borrower's property, hence constituting the relevant 'enrichment'. Obviously, such an enrichment would also have to be 'unjust' for such a claim to succeed.

Although this type of action against a lender has been unsuccessful in Australia to date,⁹ there is no strong authority to suggest that financiers may never be liable in such situations. There is certainly authority from some jurisdictions in the United States that there will be circumstances in which this type of claim against a lender in unjust enrichment will succeed.¹⁰

In order to fully examine this issue in the context of Australian law, this article deals with the following:

1. A discussion of the basic concepts underlying unjust enrichment claims in general, including the distinction between unjust enrichment 'by subtraction from the plaintiff' and 'by wrong committed against the plaintiff'.
2. An examination of the class of unjust enrichment cases that may loosely be described as arising from 'ineffective contracts'. This is the basis for the Australian jurisprudence on unjust enrichment claims for services provided as opposed to claims based on return of mistakenly paid funds (although, as noted above, both are subsets of the category of unjust enrichment claims based on 'subtraction from the plaintiff').

7 See for example P Birks, *Introduction to the Law of Restitution*, Clarendon Press (1985) p 106. The difference between these two categories of restitutionary claims is considered in more detail below at Part IIIB.

8 One obvious example is the development of restitutionary claims in Australia in the context of "mistaken payments" situations. The *David Securities* case is a good example of such a case involving a financier. See also the earlier case of *Australia and New Zealand Banking Group Limited v Westpac Banking Corporation* (1988) 72 ALR 157 involving mistaken payments between two financiers. This case also explored the defence of "change of position" in the context of claims for mistaken payments.

9 See for example *Winterton Constructions Pty Ltd v Hambros Australia Ltd* (1992) 111 ALR 649; *Marriott Industries Pty Ltd v Mercantile Credits Ltd* (1990) 55 SASR 228.

10 See for example Chief Justice Merritt's dissenting judgment in *Bluebonnet Warehouse Cooperative v Bankers Trust Co* 89 F 3d 292 (1996); *Ninth District Production Credit Association v Ed Duggan, Inc* 821 P 2d 788 (1991).

3. The relevance of the doctrine of privity of contract to unjust enrichment actions in 'ineffective contract' situations. This forms the basis for subsequent discussion as to whether third parties (such as lenders) could be liable in unjust enrichment for services provided under an ineffective contract between two other parties where some benefit might be said to have accrued to the third party.
4. A specific examination of the position of third party lenders in relation to benefits they may be said to have received unjustly under a contract between a borrower and its service provider. Reference will be made here to relevant United States jurisprudence on this issue in comparison with the current Australian position.

III. THE UNJUST ENRICHMENT CONCEPT

A. Elements of Unjust Enrichment

The first, and most obvious feature of the doctrine of unjust enrichment in Australia is its uncertainty. It is not settled in Australian jurisprudence that there is a wide-ranging doctrine of unjust enrichment, particularly as a cause of action in its own right. Cases such as *David Securities* and *Pavey* may, in the future, be strictly confined to their facts. This would severely limit future applications of an unjust enrichment doctrine in a broader sense in Australian jurisprudence.

Even if such a doctrine or cause of action may be accepted, its exact scope remains unclear. There is obviously some role for a concept of unjust enrichment in the context of 'mistaken payments' cases¹¹ as well as in the field of quasi-contract, although in this latter context the application and boundaries of the concept are a little hazy.¹²

Some commentators have harshly criticised the apparent judicial acceptance of an unjust enrichment concept as a separate principle of law in Australia. In the wake of the controversial High Court decision in *Pavey*, Getzler stated:

The notion of unjust enrichment may now be emerging as a general principle of intervention augmenting the unconscionability principle...[C]oncepts of unjust enrichment are gaining some currency in the thinking and language of the High Court as a basis or inspiration for judicial imposition of obligations, not only in the quasi-contractual fields of money had and received and quantum meruit, but also in the wider areas of contract and equity. It is questionable, however, whether it is necessary or desirable that a notion of 'unjust enrichment' be adopted as a general source of rights and obligations.¹³

Finn acknowledged some of the obvious problems inherent in the increase of unjust enrichment doctrine in Australian law in the preface to his collection of essays on restitution law:

11 See note 8 *supra*.

12 This becomes obvious from a consideration of the diversity of views on the point expressed by the judges of the High Court in the *Pavey* case considered below.

13 J Getzler, "Unconscionable Conduct and Unjust Enrichment as Grounds for Judicial Intervention" (1990) 16 *Monash University Law Review* 283 at 323-4.

In the climate of re-appraisal that now affects our common law, new and not-so-new ideas are staking their claim as basal ones in the making and shaping of legal doctrine. "Unjust enrichment" and "restitution" - terms the precise significations of which are not altogether agreed - are among those cast in this role. They suggest for us a number of issues. Are these simply explanatory aids to an understanding of the (or a) burden of some established doctrines? Do they provide signposts to the direction of future doctrinal development? Do they themselves embody discernible principles capable of providing a new and more satisfactory rationalisation for a range of existing doctrines? Are they merely easy distractions from more precise and sensitive analysis? What cannot be denied is the powerful attraction that the language of unjust enrichment is exerting today on judges and scholars alike throughout the common law world.¹⁴

Since Finn and Getzler wrote these words, the influence of concepts of unjust enrichment and restitution have not obviously decreased in Australian law and legal theory. Litigants in Australian courts continue to plead unjust enrichment and academic work continues to be done in the area. It is therefore unlikely that the concepts of unjust enrichment and restitution will die out in the foreseeable future. The more significant question for Australian lawyers will be not whether a doctrine of unjust enrichment exists in Australian law, but rather to determine its exact boundaries and potential impacts on various activities.

As other jurisdictions such as the United Kingdom and the United States have a more fully developed history of restitution jurisprudence and commentary, it seems reasonable to draw, at least in part, on the experience of unjust enrichment claims in those countries in attempting to establish the boundaries of the doctrine in Australian law. Such comparisons, however, must be made with due care because of differences in development of restitutionary principles and other doctrines that may have impacted on the development of restitutionary remedies in the relevant jurisdiction.

The concept of 'unjust enrichment' has had a somewhat chequered history as legal doctrine in most jurisdictions which have adopted it. Some commentators have viewed the uncertainties surrounding the development of the concept and its current and future status within a particular legal system as one of its main strengths. The argument has been made that this inherent vagueness has allowed the concept to remain flexible and to apply to new types of situations in a fair and sensible manner. However, the disadvantage with this has been the lack of a system of clear rules to apply in any given case. In the context of the development of restitution and unjust enrichment in United States jurisprudence in the early 1950s, Dawson noted that:

The most obvious comment about the American law of restitution is that it lacks any kind of system. This condition is not peculiar to the law of restitution. We generally pride ourselves on our lack of system. When anyone ventures to construct a system we all set cheerfully to work to destroy it. The price we pay for this includes, among other things, a serious and growing confusion in analysis, a lack of overall intelligibility, and much difficulty in prediction. This price we are paying now in the field called restitution. Confusion is probably inevitable in any large body of doctrine that has grown so rapidly, from so many different directions, by the methods of case law. To this point our gains have also been great; we have been enriched through our own loss. It has been necessary to keep our judges fully

14 PD Finn (ed), *Essays on Restitution*, Law Book Company (1990) p v.

exposed to all kinds of new experience, to give them time and opportunity to see their way into the problems. Any impartial critic should freely concede that they have responded remarkably well. Specific solutions in restitution cases are still, on the whole, both ingenious and sensible. It is only when one tries to string them together that one becomes confused.¹⁵

Notwithstanding the merits of a vague and flexible unjust enrichment concept, there appears to be consensus in most jurisdictions in which the concept is accepted that there must be some rough framework which can be employed to explain the doctrine. There needs to be some set of rules, albeit vague and flexible, which can explain the types of situations in which the unjust enrichment doctrine may come into play. Even Dawson himself recognised this need:

No matter how much attention is devoted to refining and elaborating other legal techniques, there will remain situations in a great variety for which standard techniques do not apply. The only common feature in these situations, apart from their unforeseeability, is the acquisition by one person of a gain through another's loss. When lawyers reach the stage of dealing with these situations, results can be made intelligible only through expressing this common feature in the form of a kind of "rule".¹⁶

In the context of recent Australian legal developments in the area of restitution, Mason and Carter have made similar comments, emphasising that a doctrine of unjust enrichment without some clearly formulated legal basis is of questionable use:

No branch of the civil law (other than the law of restitution) has sought to use the prevention or reversal of unjust enrichment as its norm. The idea that we should recognise as a principle that the law provides a remedy whenever a defendant would otherwise be unjustly enriched at the plaintiff's expense is an appealing one. However, it suffers from its generality. Just as we recognise general ideals, such as that the law should not suffer a wrong without a remedy, that the operation of legal rules should promote certainty of decision, and that persons should not be permitted to benefit by their own wrongs, so we can suggest as a general proposition that persons should not unjustly enrich themselves at the expense of others. A generalisation is not, however, a legal principle, and ideals are not themselves doctrine. It follows that merely to say that the law is concerned to prevent or reverse an unjust enrichment is not to state a principle of law. The reference may simply be to a 'non-technical' sense of unjust enrichment. Even so, it does provide both an aspiration and a norm or standard for judgment.

The task presented is to translate the ideal into legal principle. Only if it is possible to define a legal concept of unjust enrichment can we suggest a principle of restitution.¹⁷

Many lawyers over the years have attempted to do just this. However, attempts to frame clear rules to satisfy a claim in restitution based on the unjust enrichment concept have proved somewhat vague. This is probably because of the desirability of maintaining enough flexibility in the relevant principles to cover the full gamut of situations where restitutionary remedies might be considered appropriate.

15 JP Dawson, *Unjust Enrichment*, Little Brown and Co (1951) pp 111-2.

16 *Ibid*, pp 150-1.

17 Note 6 *supra*, p 6.

It should be noted here that it is probably more correct technically to refer to a claim in restitution based on the unjust enrichment principle than to refer to a claim in unjust enrichment itself as a separate cause of action. However, lawyers do tend to speak of claims "in unjust enrichment" in colloquial parlance.¹⁸ Burrows has explained the interrelationship between the terms as follows:

Like contract and tort the law of restitution can be viewed as comprising, on the one hand, causes of action and, on the other, remedies responding to those causes. The principle underpinning restitutionary causes of action is a defendant's unjust enrichment at the plaintiff's expense. Restitutionary remedies are then concerned to reverse that unjust enrichment.¹⁹

Significant attempts to define the limits of the unjust enrichment principle have appeared in relevant literature from the United Kingdom. Legal commentators such as Birks and Burrows have set out lists of elements which should be satisfied before a claim in restitution based on unjust enrichment may be established. Burrows, for instance, sets out his formulation of the cause of action as follows:

Stripping the cause of action principle [sic] down to its component parts, there are four questions to be answered:

1. has the defendant been *benefited* (ie enriched)?
2. was the enrichment *at the plaintiff's expense*?
3. was the enrichment *unjust*?
4. are there any *defences*?

If the first three questions are answered affirmatively and the fourth negatively the plaintiff will be entitled to restitution.

The law of restitution is therefore built around the four concepts of 'benefit', 'at the plaintiff's expense', 'unjust factors', and 'defences'.²⁰

A similar formulation of the cause of action has been recognised by Mason and Carter in the Australian context.²¹

B. Categories of Restitutionary Claims: Unjust Enrichment by Subtraction from the Plaintiff and Unjust Enrichment for Wrongs Committed Against the Plaintiff

Having isolated the above general principles describing an 'unjust enrichment' for the purposes of a restitutionary cause of action, most commentators then broadly group together the types of situations in which these elements may be regarded as being present.

As mentioned previously, claims in unjust enrichment tend to fall within one of two major categories: unjust enrichment by subtraction from the plaintiff or

18 For ease of reading, the author has referred to the terms in both their technical and colloquial usages as appropriate to the context.

19 A Burrows, *The Law of Restitution*, Butterworths (1993) pp 6-7. In the context of the Australian law of restitution, see also note 6 *supra*, p 10.

20 A Burrows *ibid.*, p 7. See also P Birks note 7 *supra*, p 7; A Burrows, "Understanding the Law of Restitution: A Map Through the Thicket" (1995) 18 *University of Queensland Law Journal* 149 at 157; M McInnes, "Contractual Services, Restitution and the Avoidance of Bad Bargains" (1995) 23 *Australian Business Law Review* 218 at 219.

21 Note 6 *supra*, p 10.

unjust enrichment for a wrong committed against the plaintiff.²² Each of these major categories of restitutionary claims is made up of a number of sub-categories of claims which are said to fall under the relevant category.

The major category of restitution by subtraction includes, as two of its 'sub-categories', both mistaken payments cases, such as *David Securities*, and cases involving claims for 'compensation' (for want of a better word) for services provided under an ineffective contract²³ where a defendant has received some gain from the provision of the services.²⁴ It is on this latter sub-category that this article focuses and on possible extensions of this category to encompass third parties arguably enriched by services rendered under an ineffective contract.

By comparison, restitution for wrongs refers to restitutionary claims made in relation to recognised heads of legal wrong such as torts, breach of contract, breach of fiduciary duty or breach of confidence.²⁵ A detailed discussion of this category of restitution claims is beyond the scope of this article.²⁶

The category of potential lender liability cases for discussion in this article is best described as an 'offshoot' of claims to restitution in the 'ineffective contract' sub-category of restitution by subtraction. It is really concerned with a situation where there is no clear contract, ineffective or otherwise, between the party providing services and the party allegedly enriched unjustly by the provision of those services. In fact, the two parties in question may have had no express dealings with each other whatsoever. It thus seems logical briefly to consider both some of the 'ineffective contract' unjust enrichment cases that have arisen to date in Australia and then to examine principles arising in those cases that might be applied to third party unjust enrichment situations.

C. Ineffective Contracts

The most obvious Australian 'benchmark' example of an 'ineffective contract' case raising judicial comment about unjust enrichment is the High Court decision in *Pavey*. This case involved a building contract which was unenforceable for failure to comply with the provisions of s 45 of the *Builders Licensing Act 1971* (NSW). This provision required contracts for building works carried out by licensed builders to be in writing in order to be enforceable

22 See P Birks note 7 *supra*, p 106; note 6 *supra*, Part V.

23 The term 'ineffective contract' in this context is not a particularly legal term. It has been used here (and borrowed from Mason and Carter) to cover a large variety of cases involving benefits received from services with no apparent legal obligation, outside the restitution area, on the party benefited to provide compensation to the other party. This lack of legal obligation may be due to a contract having been brought into existence but being unenforceable for some reason or it may be due to a purported contract never having been brought expressly into existence.

24 There are also circumstances involving what have been described as 'pure services' where the plaintiff has provided services without any particular recompense, but the defendant has received no tangible benefit from the provision of services. It is queried whether restitutionary remedies are appropriate in such cases. An evaluation of this issue is beyond the scope of this paper, but is discussed in EP Pegoraro, "Recovery of Benefits Conferred Pursuant to Failed Anticipated Contracts - Unjust Enrichment, Equitable Estoppel or Unjust Sacrifice?" (1995) 23 *Australian Business Law Review* 117.

25 See for example A Burrows note 19 *supra*, pp 23, 376-419.

26 However, for a simple discussion of the main differences between restitution for wrongs and unjust enrichment by subtraction to the plaintiff see for example *ibid*, p 17.

against the other party to the contract. Such contracts were further required sufficiently to describe the building work which was the subject of the contract. The legislative purpose was to prevent builders from charging their customers for works to which their customers had not expressly agreed.

In *Pavey*, there was no written contract between the licensed builder plaintiff and its customer, the defendant. The defendant had attempted to take advantage of this lack of compliance with s 45 to avoid paying the builder for works undertaken under the oral contract. A majority of the High Court held that the builder was entitled to recover reasonable remuneration from the defendant in a claim in *quantum meruit* which was now properly to be regarded as being based on restitution or unjust enrichment independently of notions of implied contract.²⁷

Justice Brennan dissented, largely on the ground that a contract made unenforceable by words of Parliament is not capable of giving rise to any type of restitutionary action²⁸ and, additionally, because it seems contrary to public policy to go against the clear words of the statute and allow a builder to recover moneys under a contract which does not comply with the relevant legislation.²⁹ Justice Dawson, whilst agreeing that the plaintiff's claim should succeed, felt that the claim was properly to be regarded as being based on an implied promise to pay the builder rather than on unjust enrichment *per se*.³⁰ Interestingly, some judges in lower courts in Australia faced with similar factual situations have subsequently agreed in policy with Justice Brennan's reasoning, but have felt constrained to follow the majority decision in *Pavey*.³¹

Although it is easy to understand Justice Brennan's point of view, it is difficult to see why unjust enrichment should not, as a matter of policy, be accepted as a basis for civil liability in circumstances such as these. This is particularly so where accepting such a basis for liability does not contradict the clear policy aims of the legislation in question.

Probably the most significant aspect of *Pavey* in relation to the development of unjust enrichment principles was the apparent willingness of the majority to accept an action based on notions of unjust enrichment in the absence of an implied contract. The more traditional legal view of such situations in Australian law had been that espoused by Dawson J; that is, that for such an action to succeed, the court must be able to find an implied promise on the facts that the defendant would pay the plaintiff reasonable remuneration for the relevant services.

Of the majority judges in *Pavey*, it was Deane J who most decisively recognised and advocated some kind of enforceable concept of unjust enrichment in Australian law. In the course of his judgment, he made the following now oft-quoted comments:

27 Note 1 *supra* at 227-8, per Mason CJ and Wilson J and at 256-7, per Deane J.

28 *Ibid* at 238.

29 *Ibid* at 244.

30 *Ibid* at 267.

31 See for example the judgment of Bollen J in *Tea Tree Gully Builders Co Pty Ltd v Martin* (1992) 59 SASR 344.

To identify the basis of such action [ie those arising out of unenforceable contracts] as restitution and not genuine agreement is not to assert a judicial discretion to do whatever idiosyncratic notions of what is fair and just might dictate. The circumstances in which the common law imposes an enforceable obligation to pay compensation for a benefit accepted under an unenforceable agreement have been explored in the reported cases and in learned writings and are unlikely to be greatly affected by the perception that the basis of such an obligation, when the common law imposes it, is preferably seen as lying in restitution rather than in the implication of a genuine agreement where in fact the unenforceable agreement left no room for one. That is not to deny the importance of the concept of unjust enrichment in the law of this country. It constitutes a unifying legal concept which the law recognizes, in a variety of distinct categories of case, an obligation on the part of the defendant to make fair and just restitution for a benefit derived at the expense of a plaintiff and which assists in the determination, by the ordinary processes of legal reasoning, of the question whether the law should, in justice, recognize such an obligation in a new or developing category of case...³²

Justice Deane did not describe unjust enrichment in terms of a cause of action or a 'doctrine'. He used the looser terminology of "unifying legal concept" which merely explains certain results in particular categories of case. His judgment therefore does not explain the exact foundations of the unjust enrichment concept in Australian law. It does, however, recognise the importance of unjust enrichment theory to the ongoing development of Australian law and the fact that unjust enrichment principles may well be applied in new and developing classes of cases. This may be of particular significance in cases such as *Pavey* where there is a clear moral obligation on a defendant to compensate a plaintiff for a gain made by the defendant at the plaintiff's expense and an absence of remedy for the plaintiff in other branches of the law.

IV. PRIVACY ISSUES

Having accepted a doctrine of unjust enrichment in the context of recompense for services provided under an unenforceable (or otherwise ineffective) contract, the next question is whether such reasoning will apply to a third party situation outside the parameters of the ineffective contract. If the existence of a valid and enforceable contract is not a necessary prerequisite for a claim in unjust enrichment for services provided to a defendant, should it be necessary for the plaintiff to prove any semblance of a contract at all? Might it simply be sufficient for the plaintiff to prove that it provided services which somehow benefited the defendant unjustly in a context where the defendant was aware of the provision of the services and possibly had even encouraged the provision of the services in some way? What is really being asked here is whether there is any equivalent to the contractual privity rule in the context of such unjust enrichment claims.

There has been some judicial and academic comment in the past about the application of the privity doctrine to unjust enrichment situations. However,

³² Note 1 *supra* at 256-7. These words of Deane J mirror comments made by Birks. See note 7 *supra*, pp 17-27.

very little, if any, of such comment has been directed at lender liability for provision of services by a third party to a customer of the lender. Previous commentary has focused on tripartite situations which operate significantly differently to such a scenario.

Burrows, for example, takes the view that claims in unjust enrichment by subtraction cannot be maintained successfully in the absence of some kind of privity relationship between the plaintiff and the defendant.³³ However, Burrows' views in this respect are focused on situations where a third party, rather than the plaintiff itself, has conferred some kind of enrichment on the defendant, which enrichment may somehow be regarded as being to the detriment of the plaintiff. This is clearly different to the lender liability situation where the plaintiff *itself* may be said to have enriched the defendant lender.

Probably the most contentious judicial comments about unjust enrichment and privity of contract in Australian law were made by Gaudron J, with some support from Deane J, in *Trident's* case. On their face, some of Justice Gaudron's comments would seem to be directly applicable to the third party situation here under discussion:

[T]here is no legal principle to preclude the recognition of an obligation and corresponding right as between promisor and third party separate from the contractual obligation existing between promisor and promisee. Rather the fact that the law, as it is presently understood, permits of the possibility of unjust enrichment provides a compelling reason for the recognition of such an obligation in the same nature of the obligation imposed by law to compensate for a benefit received under an unenforceable contract.³⁴

However, two points need to be made about Justice Gaudron's judgment in *Trident*. First, the judgment dealt with a significantly different tripartite situation than the lender liability situation here under discussion. Second, it has been widely criticised for its incongruity with basic principles of restitution.

To take these issues in order, the judgment dealt with a situation involving an insurance contract between two parties expressed to be for the benefit of various third party contractors, subcontractors and suppliers of the primary insured. One of these subcontractors had caused an injury to a workman in circumstances which appeared to be covered by the contract of insurance. The subcontractor brought a claim against the insurer when it refused to reimburse the subcontractor for the damages it had been forced to pay to the injured worker. The insurer argued that, as the subcontractor was not a party to the contract of insurance, the privity of contract rule precluded it from bringing an effective action against the insurer.

The High Court found against the insurer, but largely on the basis of finding an implied exception to the privity rule in cases of specific insurance contracts expressed to be for the benefit of third parties. Only Gaudron J based her judgment on unjust enrichment. Other judges discussed principles of trust and

33 A Burrows note 19 *supra*, p 45-6.

34 Note 1 *supra* at 176.

agency and Deane J additionally made some *obiter* comments about unjust enrichment.³⁵

The important point, however, is that the situation under consideration was significantly different to the lender liability situation here under discussion. In *Trident*, the tripartite arrangement involved a third party *plaintiff* suing one of the parties to a contract who was refusing to perform contractual obligations which were expressed to be for the benefit of the third party plaintiff. The lender liability situation, by comparison, involves a third party *defendant* incidentally benefited by the performance of contractual obligations in respect of a contract to which the defendant is not expressed to be a party.

The second problem with applying Justice Gaudron's general comments about unjust enrichment and privity to the lender liability situation relates to repeated suggestions in subsequent literature that her comments in the case were misconceived. In relation to unjust enrichment jurisprudence, to the extent that it is accepted in Australia at all, it is clear that a defendant's 'enrichment' has to correspond with a plaintiff's 'loss' for a claim in unjust enrichment by subtraction to be made out. In *Trident*, the defendant was arguably enriched as a result of keeping moneys it would otherwise have had to pay out. However, the enrichment did not really correspond to the plaintiff's loss. Rather, it was the primary insured party to the contract that had arguably suffered the loss of its insurance premiums paid to the defendant insurer without receiving, either for itself or for a third party, any services in respect of those payments.³⁶

Further criticisms have been levelled at Justice Gaudron's judgment on policy grounds. Her solution to the *Trident* situation has been regarded by some as an inappropriate attempt to use unjust enrichment jurisprudence to avoid directly confronting difficulties with the privity of contract rule:

[A]n unjust enrichment solution to the third party contract issue evades the basic questions concerning the purpose and policy of the privity and consideration rules of contract. It is submitted that Chief Justice Mason, Justices Wilson and Toohey's policy oriented reform of the privity rule [in *Trident's* case] is the preferable approach, and that the use of unjust enrichment arguments to bridge perceived deficiencies in classical contract law in an ad hoc fashion is an undesirable form of judicial creativity.³⁷

Although these comments relate specifically to the privity problem in *Trident*, it might be said that such considerations should generally preclude Australian judges from readily accepting new classes of unjust enrichment cases where to do so may be contrary to other legal principles. Such reasoning may therefore be applied to the lender liability situation as a potentially unjustifiable attempt by a contracting party to seek to obtain redress from a third party lender where usual contract remedies against the other contracting party have proven inadequate for some reason. This issue will be considered in more detail below. However, it is worth here noting what Mason and Carter have to say on the matter:

35 *Ibid* at 145-6.

36 On this issue, see also: J Getzler note 13 *supra* at 321-2; K Mason, "Restitution in Australian Law" in P Finn (ed), *Essays on Restitution*, (1990) p 20.

37 J Getzler *ibid*.

The rule that no claim in restitution may be brought while an effective contract is in existence will also affect restitutionary claims brought against third parties who happen to be benefited by the plaintiff's performance of a contract to which the defendant was not a party. For example, where services are rendered by A at the request of B, on the understanding that the services will be paid for by B, the fact that C stands, under a contract with B, to benefit from those services does not provide a basis for restitution by A against C. Thus, if a sub-contractor cannot recover a contract debt from a contractor, a restitutionary claim for reasonable remuneration brought against the proprietor *or financier* must generally fail.³⁸

Here, Mason and Carter not only suggest that unjust enrichment solutions should not be available in Australian law to avoid contractual privity rules, but they make this point in relation to the exact class of privity situation under discussion in this paper. However, it remains to be seen whether this view will hold true in all relevant cases in Australian law. It is therefore necessary to examine the third party financier scenario in more detail with specific reference to the elements of unjust enrichment claims to ascertain whether there may be circumstances in which a third party financier might be liable for such unjust enrichment.

V. THIRD PARTY LENDER LIABILITY FOR UNJUST ENRICHMENT

A. The Current Position in Australia on Third Party Liability for Services Provided

The crux of the issue is to what extent a lender may be liable in an unjust enrichment claim for services provided by a person who has contracted not with the lender itself, but with a customer of the lender. Obviously, for any such claim to arise, the services must somehow be seen to have benefited or 'enriched' the defendant in an 'unjust' manner. Some such claims have been pleaded in Australian courts in recent years,³⁹ but generally with no success. However, courts have not necessarily ruled out such causes of action altogether.⁴⁰ Many commentators have also suggested that, as with negligence in the law of tort, the categories of potential unjust enrichment claims are not closed.⁴¹ Even some Australian judges have advocated considering potentially new applications of unjust enrichment doctrine on a case by case basis to allow natural development of this area of law.⁴²

38 Note 6 *supra*, p 282 (emphasis added).

39 See note 9 *supra*.

40 See for example, *obiter* comments of Byrne J in *Brenner v First Artists' Management* [1993] 2 VR 221 at 260-1; *Stowe v Stowe* (unreported, Ipp, Owen and White JJ, Supreme Court of Western Australia, 22 May 1995) at 27; *Winterton Constructions Pty Ltd v Hambros* (1991) 101 ALR 363 at 375, per Gummow J, who held that it would be inappropriate to strike out such a cause of action if pleaded correctly. On appeal, Justice Hill later implicitly disagreed with this in deciding the substantive issues arising in the case. This point is taken up below.

41 See for example Burrows note 20 *supra* at 159-160.

42 See for example *Angelopoulos v Sabatino* (Supreme Court of South Australia, Doyle CJ, Duggan, Nyland JJ, 8 September 1995) at 13, per Doyle CJ, Duggan and Nyland JJ concurring.

If a new category of unjust enrichment claim were to be developed along the lines set out above, it would clearly be a new sub-category of unjust enrichment by subtraction from the plaintiff, and would draw on general principles underlying such unjust enrichment claims as well as perhaps some more specific principles derived from the quasi-contractual line of cases.

The policy objective behind such a development would likely be to translate clear moral obligations into legal obligations where there is a perceived 'gap' in the ambit of other civil remedies. One obvious example of such a gap is that identified in relation to the limitations of contractual remedies imposed by the doctrine of privity of contract. Some apparent moral obligations which arise out of situations involving a contract will have no remedy in contract because of the strict application of this doctrine. Although some equitable remedies have been developed to mitigate against the harsh application of this doctrine,⁴³ they do not necessarily cover all possible situations where a defendant has made an unfair gain at the expense of a plaintiff. If remedying such unfair gains is accepted as an aim of the Australian common law, it may be necessary to accept unjust enrichment claims as an alternative form of civil action in these circumstances.

There has been a spate of recent Australian cases, mostly in State courts, dealing with the issue of third party liability for claims in unjust enrichment arising from gains allegedly made by third party defendants in respect of services performed by the plaintiff under contract with another party. The situation has typically arisen where the plaintiff is unable to recover from the other party because of inability to enforce a contractual or similar obligation. Such failure is usually due to lack of compliance with required contractual formalities or insolvency of the other party.⁴⁴ Not all of these cases have involved a lender as the third party defendant, but guidance may perhaps be gained from cases which do not involve a lender as to circumstances in which lender liability might arise.

However, lender liability arguably does need to be considered separately to such general claims against third parties. There may well be issues common to standard lending situations which allow for a specific jurisprudence to develop in relation to such scenarios. This has certainly been the case in various jurisdictions in the United States (see below at Part VC).

One of the most striking examples of a recent Australian case dealing with the third party liability issue is the recent Victorian decision of Byrne J in *Brenner v First Artists' Management*.⁴⁵ This case did not involve lender liability *per se* but did involve general considerations relating to third party liability. The judgment is noteworthy for its detailed analysis of such third party claims for the benefit of

43 For example, equity has developed remedies based in estoppel and trust to counter some of the problems created by a strict application of the privity rule. These issues are canvassed, *inter alia*, in the various judgments in the *Trident* case.

44 See for example *Brenner v First Artists' Management* note 40 *supra*; *Christiani & Neilsen Pty Ltd v Goliath Portland Cement Co Ltd* (1993) 2 Tas R 122; *Winterton Constructions Pty Ltd v Hambros Australia Ltd* note 9 *supra*; *Angelopoulos v Sabatino* note 42 *supra*; *Marriott Industries Pty Ltd v Mercantile Credits* note 9 *supra*; *Strang Patrick Stevedoring v Owners of Motor Vehicle "Sletter"* (1992) 38 FCR 501.

45 *Ibid.*

services provided under unenforceable obligations technically rendered to someone other than the defendant.

The facts of the *Brenner* case were somewhat complex. However, in relation to the unjust enrichment claim against a third party, they may be summarised as follows. The plaintiffs were managers of one of the defendants, Braithwaite, in relation to his career as a singer. Under a series of discussions and negotiations, they performed management services for Braithwaite effectively at the request of the first defendant ("FAM") which was a management company also established to provide management services for Braithwaite. Eventually, relations deteriorated between FAM and the plaintiffs and their arrangements with FAM were terminated. The plaintiffs sought compensation from both FAM and Braithwaite for management services they had provided. However, FAM became insolvent and was dissolved so the plaintiffs⁴⁶ were forced to proceed against Braithwaite alone.

The court found that no valid and enforceable contracts existed between the plaintiffs and Braithwaite in respect of the services provided by them. The plaintiffs were therefore forced to proceed against Braithwaite on the grounds of *quantum meruit* or unjust enrichment.

Justice Byrne held that the plaintiffs had failed to make out a claim against Braithwaite on the facts. However, he was not disposed to rule out such third party causes of action altogether. In examining the relevant rules to apply to such cases, he set out the requisite elements for a successful action in this category of restitution, acknowledging that the application of those rules may well lead to different results in differing circumstances:

The claim of the plaintiffs is that they provided services and that the defendant accepted the benefit of them in circumstances giving rise to an obligation to make restitution. In a case such as this, the plaintiffs must show that the defendant accepted the benefit of their services in circumstances where he, as a reasonable person, should realise that the plaintiffs would expect to be paid for them. It is of significance on the facts of this case that it is *the defendant* who accepts the services in these circumstances for it is the defendant from whom restitution is sought. Where, upon a proper analysis of the facts, it cannot be said that it was the defendant who obtained the benefit of the services or, in this case, it was not in the contemplation of the defendant as a reasonable man that the plaintiffs realised that he would be responsible for payment, then the claim against him in respect of those services must fail. Furthermore, the situation may change as circumstances alter from time to time...⁴⁷

Justice Byrne suggests that the requisite elements a plaintiff must establish to succeed in such a cause of action are: (1) that the plaintiff performed services which somehow benefited the defendant; (2) that the defendant accepted the benefit of those circumstances; and, (3) that the circumstances were such that the defendant should have realised, as a reasonable person, that the plaintiffs would expect to be paid for the services. On the facts in *Brenner's* case, however, Byrne J felt that the plaintiff had failed to establish these elements. He took the

46 At this stage, one of the plaintiffs had himself gone bankrupt and proceedings were re-instituted in his name by his trustee in bankruptcy.

47 Note 40 *supra* at 261.

view that the plaintiffs had agreed to provide services only to FAM at the request of FAM. The fact that Braithwaite, under his own management contract with FAM, stood to benefit from the services provided by the plaintiffs to FAM did not impose a restitutionary obligation on him in respect of those services.

It has subsequently been recognised in some other Australian State courts, both expressly and by implication, that such third party claims may exist in unjust enrichment. In 1995, the Full Court of the Supreme Court of Western Australia found that such a claim would be “arguable” if sufficient particulars were given to support the cause of action, particularly in relation to establishing the alleged “enrichment” of the third party defendant.⁴⁸ Again, in *Angelopoulos v Sabatino*,⁴⁹ in the Supreme Court of South Australia, such a third party action in unjust enrichment failed, but only on the ground that insufficient evidence was presented at the trial as to the enrichment of the third party defendant.⁵⁰ It is therefore submitted that there is now at least some support in Australia for such third party claims in unjust enrichment for services provided under an unenforceable or ineffective contract which have somehow enriched a third party.

B. Lender Liability in Australia: The Current Position

In respect of the lender liability situation, therefore, if a person contracting with a customer of a lender has performed services which have somehow benefited the lender in circumstances where the lender should have realised that the service provider expected some recompense from it, it may be held liable for such a claim. Granted that in the usual situation, where a lender merely holds a security interest in its customer’s property and services are provided by another person in respect of that property, those services do not seem to have a sufficient connection with the lender to attract such liability. However, there may be instances in which a secured lender in such circumstances is in the position of a person who does know or should have known that the service provider would expect some compensation from the lender. There may be examples of this where a lender takes a particular interest in the secured property or in the management of its customer’s business. Examples of this might be where a lender is acting as a mortgagee in possession of secured property or exercises some lesser level of management or control over the property, or perhaps where the lender is involved in the business activities of its customer to the extent that it is fully versed with the service provider’s activities and/or it has even encouraged the customer to obtain the relevant services from the service provider.

There is not a large volume of Australian case law on the position of lenders in such situations. Nothing has been said specifically by Australian judges about the level of knowledge or participation that may be required by a lender to attract such a claim. By and large, the small body of Australian case law in this area

48 *Stowe v Stowe* note 40 *supra* at 27.

49 Note 42 *supra*.

50 *Ibid* at 15.

stands for the proposition that such claims against lenders will generally be unsuccessful.

Two claims involving lenders in such situations are the cases of *Marriott Industries Pty Ltd v Mercantile Credits*⁵¹ and *Winterton Constructions Pty Ltd v Hambros*.⁵² The two Federal Court decisions in *Winterton* are quite interesting in this regard. The cases involved a claim by a building contractor who performed building services for a customer ("Pan") of a particular financier ("Hambros"). Hambros had financed the building development on Pan's land and had taken a registered mortgage over the relevant property. Pan had failed to make the final two progress payments due to the plaintiff under the building contract. The plaintiff then brought an action against both Pan and Hambros on a variety of grounds, one of which was a claim in unjust enrichment against Hambros for the building services provided by it which had increased the value of the secured property and thus arguably enriched Hambros as a secured lender over the property.

In interlocutory proceedings before Gummow J in the Federal Court, Hambros sought, amongst other things, to have the claim in unjust enrichment struck out of the pleadings on the grounds that the relevant pleadings showed no reasonable cause of action. Justice Gummow held that the relevant paragraph of the pleadings should be struck out, but with leave to re-plead. He was not prepared to hold that no such cause of action existed in Australian law against a lender in such circumstances as a potential new sub-category of unjust enrichment by subtraction from the plaintiff.⁵³ He felt that in order to plead such a cause of action, however, a plaintiff would be required to specify in the pleadings the following items: (1) the actual enrichment of the lender; (2) the sense in which that enrichment occurred at the expense of the plaintiff; and, (3) that the enrichment was unjust in the circumstances.⁵⁴ The plaintiff was given leave to re-plead the claim in unjust enrichment with specific reference to these issues. The plaintiff apparently did so as the final hearing of the substantive issues included a determination of the unjust enrichment point.

The substantive issues between the parties in *Winterton* were determined by Hill J in the Federal Court.⁵⁵ The plaintiff was still relying on a number of separate grounds for relief, unjust enrichment for services provided to Hambros being one of them. Justice Hill was quick to dismiss unjust enrichment as a separate cause of action in Australia in respect of this kind of claim. He relied largely on comments made by the High Court judges in the *David Securities* case about restitution for moneys paid under a mistake of law, noting that the plaintiff in *Winterton* seemed to be relying on mistake as to its legal rights against Hambros to support its claim in unjust enrichment. Justice Hill was unable to find such a mistake to be made out on the facts and thus held that the unjust enrichment action could not succeed.

51 Note 9 *supra*.

52 Note 9 *supra*.

53 (1991) 101 ALR 363 at 374-5.

54 *Ibid* at 376.

55 Note 9 *supra*.

His judgment might be criticised in this respect for failure to deal with the correct sub-category of restitution. As noted above, restitution in relation to mistaken payments is but one sub-category of unjust enrichment by subtraction from the plaintiff. What arguably should have been under consideration in *Winterton* is a completely different sub-class of restitutionary claim. It is arguable that Justice Gummow's judgment in the interlocutory hearing actually dealt with an attempt by the plaintiff to plead a new type of action in restitution: a claim based on benefits conferred on a third party as a result of services provided by the plaintiff under a contract with another party, whether or not that contract is independently enforceable by the plaintiff.

Clearly such a new cause of action would be closely related to the 'mistaken payments' sub-category of restitution claims. Each would be based on recompense for some loss suffered by the plaintiff which had somehow benefited the defendant in an unjust way. However, the elements of the actions may be different. The potentially 'new' cause of action against third party lenders may be more complex to prove than a simple 'mistaken payments' case. It may rely, as foreshadowed by Gummow J, on proving exactly how the defendant lender might be enriched by the provision of services by the plaintiff purportedly rendered to the other contractual party as well as determining what factors will amount to an 'injustice' in relation to such enrichment.

This would seem to be a different type of action than an action establishing a payment of moneys under a mistake of fact or law. In fact, it is submitted that the language of 'mistake' should be strictly confined to 'mistaken payments' cases dealing with situations where money has been paid by a plaintiff to a defendant under a misapprehension as to the existence or the amount of the monetary obligation to the defendant. Cases of third party enrichment as a result of benefits rendered by a plaintiff in the form of services provided to a second contractual (or 'quasi-contractual') party arguably deal with quite different issues and require the establishment of different elements for their success. This might be regarded as a new sub-category of unjust enrichment by subtraction from the plaintiff. Although it shares common policy bases with mistaken payments cases, it may be technically a quite different form of action. To the extent that earlier cases involving third party lenders have relied on reasoning from 'mistake' cases, they may perhaps be called into question.

In formulating a new category of restitutionary claim, based perhaps on the Gummow J formula in *Winterton*, regard would need to be had to the policy bases for such an action. Where large scale lenders are involved in the litigation, there may be economic policy reasons for accepting that such parties are generally better able to sustain loss than smaller building companies. However, liability should not automatically be attached to lenders on this basis alone. Some smaller lenders may be less able to sustain such losses. Additionally, it is obviously not in line with notions of a fair and just legal system to attach liability to the party with the greatest financial resources. Clearly, some benchmark standards for 'enrichment' and 'unjustness' in this context would need to be developed by courts on acceptable policy grounds for such a cause of action to be a desirable addition to the Australian common law.

Any such developments might well employ some notions from the 'mistaken payments' line of cases. Arguably, the policy concerns behind such cases are a little simpler than those relevant to the 'service provider' cases. The former class of cases relies heavily on notions of an unintended monetary benefit conferred as a result of a legal or factual mistake. The moral obligation in such a situation is clearly to return such an unexpected windfall.

The main similarity between those cases and the 'service provider' cases is the quality of unintended benefit. Where the cases diverge is in identifying exactly what elements of such a benefit might make its retention unjust in the hands of the receiver. The moral obligations to make good the benefit are not always so clear in the service provider cases. The issue will require further consideration if a new third party service provider cause of action is to develop in Australia.

Some support for Justice Gummow's apparent position in *Winterton* may be found in the judgment of Prior J in *Marriott Industries*, the facts of which were somewhat similar to *Winterton*. The main difference between the two fact situations for present purposes was that in *Marriott Industries* the defendant lender was actually the registered proprietor of the land over which the plaintiff had made improvements. In *Winterton*, the lender was merely registered as holding a security interest in the relevant land. Arguably, therefore, the defendant's degree of interest in the property in question in *Marriott Industries* was greater than that of Hambros in the *Winterton* litigation.

In *Marriott Industries*, Prior J again held that the plaintiff's claim in unjust enrichment could not succeed as it was not a case of conferral of benefit on the defendant by the plaintiff as the result of a mistake or under compulsion.⁵⁶ He did acknowledge, however, that there was some persuasive force in various High Court judgments in cases such as *Pavey* and *Trident* in relation to Australian courts being prepared to accept new classes of unjust enrichment claim under the 'unifying legal concept' of unjust enrichment. He particularly appeared to support the idea from Justice Gaudron's judgment in *Trident* that the existence of other legal causes of action to prevent unjust enrichment in particular circumstances, such as the doctrines of trust and estoppel, should not be seen as a bar to the development of new causes of action based on unjust enrichment. He merely felt that:

Sitting as a trial judge, I feel unable to answer the exhortation of Gaudron J in *Trident*...to identify and apply a "legal principle which will obviate all possibility of unjust enrichment" in this case.⁵⁷

Justice Prior did not seem specifically to agree with Justice Gaudron's reasoning for her decision in *Trident*, reasoning which, as detailed above, has been criticised by subsequent commentators. He seemed rather to agree with the somewhat broader notion underlying her judgment: that the categories of unjust enrichment claims should continue to develop to promote fairness and justice in the Australian legal system. This is consistent with the idea of recognising a new and flexible principle of law to remedy unjust enrichments in general.

56 Note 9 *supra* at 238.

57 *Ibid.*

A detailed examination of the Australian jurisprudence on potential third party lender liability in unjust enrichment for services provided under contract to a customer therefore shows that the Australian law should not necessarily be regarded as settled in this area. Hence Mason and Carter's comments (above) that such claims "must generally fail" should not be accepted at face value. There may, under modern Australian conceptions of unjust enrichment, be room for the acceptance of a new sub-category of claim.

It may be that such a claim would first have to be accepted by a higher appellate court and then filter down through the hierarchy, as suggested implicitly by Prior J in *Marriott Industries*. Alternatively, it may be possible for lower courts to start formulating such principles in their own right based on existing High Court jurisprudence on unjust enrichment. In fact, this would seem to describe Justice Byrne's approach in *Brenner*. Justice Byrne was prepared to accept extensions to existing categories of unjust enrichment action in principle, but was unprepared to allow a particular claim to succeed on the facts before him. This seems also to have been the approach of the Supreme Courts of Western Australia and South Australia respectively in the *Stowe* and *Angelopoulos* cases. Although none of these authorities directly involves lender liability, there would seem to be no reason in principle why such a new sub-class of restitutionary claim should not extend to lenders in certain situations. These situations may be limited to cases in which the lender is exercising some direct management or interest in the property which has been improved by the plaintiff and/or to cases where the lender is exercising a significant degree of control over the business activities of its borrower where it is the borrower who has requested particular services from the plaintiff. In other words, the substance of the relationship between the plaintiff and the defendant lender in such cases is likely to have a direct bearing on the quality of 'unjustness' in any given case.

On the one hand, it may seem objectionable for a lending institution with no particular interest in specific contractual obligations between its customer and a service provider to be burdened with unjust enrichment liability in the event that the service provider is unable to recover under the contract with the customer. On the other hand, if there is some tangible benefit received by the lender from the services provided, in respect of increased value of secured property, there may be good reasons why the lender, particularly in circumstances where it has a specific relationship with the plaintiff, should be subject to such liabilities.

Australian courts to date have generally been slow to discount the availability of such claims, but have given little direct guidance as to the specific legal and policy considerations to be emphasised in relation to them. In this respect, some guidance may perhaps be drawn from various jurisdictions in the United States which have developed some jurisprudence on such issues. Obviously, any comparisons with United States law must be made with caution owing to the significant differences between the two systems in both legal and economic terms. One of the most obvious legal differences is that the United States has a much more clearly recognised law of unjust enrichment embodied largely in the American Law Institute *Restatement on Restitution*. The fact that the United States has a more developed law of restitution than Australia however, may also

be a good reason to look to United States jurisprudence on some of these issues for guidance.

C. The United States Position on Third Party Lender Liability for Services Provided

Section 1 of the American Law Institute *Restatement on Restitution* provides that:

A person who has been unjustly enriched at the expense of another is required to make restitution to that other.

Such a formulation of the underlying rules of restitution for unjust enrichment is clearly similar to concepts derived from United Kingdom and Australian jurisprudence on the basis of a restitutionary claim. Therefore, to the extent that the United States law on lender liability as a third party for services provided is derived from the same basic restitutionary ideas accepted in Australia, relevant American cases might provide some guidance.

A number of United States judges sitting in various different jurisdictions have accepted that lenders may be liable in unjust enrichment claims as third party beneficiaries of services provided to their customers under contract.⁵⁸ Usually, the judges have sought to identify some significant connection between the activities of the lender and that of the service provider before imposing unjust enrichment liability on the lender. Thus, the cases tend to turn on their specific fact situations and judges have been prepared to look closely at the particular commercial and financing arrangements in place between the parties to determine the extent to which a third party lender should be held liable to a service provider in unjust enrichment. This position has been summarised by Murray in his 1991 commentary on the lender liability position in the United States:

To assert recovery based on an unjust enrichment theory, the subcontractor must be able to prove at least two things. First, the subcontractor must prove that there has been a benefit bestowed on the [lender]. Second, the retention of the benefit must be "unjust". The question as to whether the [lender] has been "unjustly enriched" by the efforts of a subcontractor will depend on the individual circumstances of each case.⁵⁹

American judges and commentators have since struggled to identify the types of circumstances that will give rise to unjust enrichment liability on the part of the lender. Drawing on the case of *DA Hill Co v Clevetrust Realty*,⁶⁰ Murray suggested that in order to establish such a claim, the plaintiff must show that the lender has requested the relevant benefit or misled someone.⁶¹ In a later

58 See for example: *Shoemaker v Southeastern Pennsylvania Economic Development Corporation* 419 A2d 60 (1980); *Gee v Eberle* 420 A2d 1050 (1980); *D.A. Hill Co v Clevetrust Realty* 573 A2d 1005 (1990); *Ninth District Production Credit Association v Ed Duggan, Inc* 821 P2d 788 (1991); *Bluebonnet Warehouse Cooperative v Bankers Trust Company* (1996) US App LEXIS 17458 (per Merritt CJ, dissenting); *In Re Gebco Investment Corporation* 641 F2d 143 (1981).

59 J Murray, "Owner/Lender Liability to Unpaid Subcontractors" (1991) 29 *Duquesne Law Review* 661 at 662.

60 Note 58 *supra*.

61 Note 59 *supra* at 667.

commentary, Tighe suggested that unjust enrichment in such situations will occur if a secured lender has “initiated or encouraged” action by a service provider that has enhanced the value of property over which the lender holds a security interest.⁶² This view is largely drawn from the case of *Ninth District Production Credit Association v Ed Duggan Inc.*⁶³

The *DA Hill* case dealt with a claim by a number of subcontractors against a lender who was financing construction work over particular real estate. In this case, the lender was one step further removed from the subcontractors than in the *Winterton* and *Marriott* cases. In *DA Hill*, there was both an owner and a general contractor interposed between the lender and the subcontractors. The lender had no knowledge of who the subcontractors were or specifically what works they were performing in respect of the secured property. Although the lender was financing the building works, the payment mechanism involved submission of invoices by the subcontractors to the general contractor which then submitted them to the property owner. The owner then requested an advance from the lender to pay out the subcontractors. There were no direct dealings between the lender and the subcontractors. When the property owner (the lender’s customer) ran into financial difficulties, the lender eventually refused to release any additional funds under the financing arrangements. In due course, the subcontractors brought an unjust enrichment action against the lender in relation to a purported increase in the value of the lender’s security interest in the property due to the subcontractors’ efforts.

The claim in *DA Hill* failed on two grounds. First, on the evidence at the time of the action, the secured property had not increased in value over and above the amount already paid out by the lender under the financing arrangements. The lender therefore had not been “enriched” at all. Second, even if the defendant lender had been enriched, such enrichment would not have been “unjust”. This was on the grounds that the lender could not be said to have “requested” any services from the subcontractors nor could it be said to have misled anyone. It merely exercised its contractual right to discontinue progress payments under the financing arrangements.⁶⁴ The court considered relevant the fact that it had been open to the plaintiffs to structure their construction agreements in some other way so as to better protect themselves in the event of the insolvency of the building owner. They could, for example, have protected themselves by taking a worker’s lien or performance bond. Having failed to do so, they should not be entitled to seek recompense from a lender completely uninvolved in the specifics of the building arrangements.⁶⁵

Thus, the court in *DA Hill* was apparently prepared to support a lender liability cause of action in unjust enrichment in such circumstances in principle. However, it required clear evidence of both “enrichment” and “injustice” before it would uphold such a claim. A similar result had been reached in the earlier

62 C Tighe, “The Unjust Enrichment Doctrine: An Expanded Definition Threatens the Rights of Secured Lenders” (1993) 25 *Uniform Commercial Code Law Journal* 203 at 205.

63 Note 58 *supra*.

64 *Ibid* at 1010.

65 *Ibid*.

case of *Shoemaker v Southeastern Pennsylvania Economic Development Corporation*⁶⁶ where the court set aside a contractor's claim in unjust enrichment against a lender for the same reasons: that is, that the plaintiff had failed to establish a relevant enrichment in the defendant lender and, even if there was such an enrichment, there would have been no "injustice" about it. It was up to the contractor to take necessary precautions to avoid the risk of loss on the insolvency of the owner of the secured property.⁶⁷

These cases may be contrasted with *Duggan* as well as the cases of *In re Gebco Investment Corporation*⁶⁸ and *Gee v Eberle*.⁶⁹ In each of these cases, the relevant court did find a sufficient relationship between the lender and the service provider's activities to impose unjust enrichment liability on the relevant lender.

The most recent of these cases, *Duggan*, relates to a claim by a corn supplier against a secured creditor who held a security interest in the cattle feedlots of its borrower, a farming company which owned and operated the feedlots as part of its business. The plaintiff was the principal supplier of corn to the feedlots. The defendant lender made annual operating loans to the borrower and held a security interest in its assets.

The lender did not directly supply advances to the plaintiff, but the plaintiff did issue sight drafts against the defendant to pay specific bills in relation to the borrower's indebtedness to the plaintiff. Thus, there was in the first instance a relationship between the plaintiff and the defendant which was closer than in the *DA Hill* and the *Shoemaker* cases.

More importantly, when the farming company's financial position began to deteriorate, the defendant started having a much more significant involvement in the company's business than had previously been the case. The defendant requested that it be informed about day to day operations of the business and that new cattle should not be taken on by the borrower without the defendant's prior approval. At all times, the defendant was aware of the plaintiff's services in supplying corn to the feedlots. Officers of the defendant were often present when the plaintiff made deliveries to the borrower's feedlots. The plaintiff had also sighted a confidential memorandum from the defendant to the borrower which contemplated further sales of corn to the borrower notwithstanding its parlous financial situation. The plaintiff was aware that the defendant had previously always paid for the corn out of the loan commitment and took the memorandum as confirmation that this position would continue even after the farming company ran into financial difficulties.

In this case, the majority of the court held that the plaintiff was entitled to succeed in its claim for unjust enrichment against the defendant when the plaintiff was unable to recover moneys directly from the borrower under its supply contract as a result of the borrower's liquidation. In giving the majority

66 Note 58 *supra*.

67 *Ibid* at 63-64.

68 Note 58 *supra*

69 *Ibid*.

judgment, Lohr J emphasised the basis on which this case might be distinguished from a number of previous cases such as *DA Hill* and *Shoemaker*:

The facts in the [previous] cases denying an unsecured creditor's unjust enrichment claim against a secured creditor are complex. A common thread, however, runs through them. In each, the secured creditor had no more than general knowledge that an unsecured creditor was supplying goods to the debtor. There were no facts to indicate that the secured creditor initiated or encouraged the transaction by which the unsecured creditor enhanced the value of the secured collateral when the unsecured creditor supplied goods or services to the debtor.⁷⁰

This is the part of the judgment from which Tighe drew the "initiated or encouraged" test. Notwithstanding that the defendant in this case had no direct contractual relationship with the plaintiff, nor had it given any express assurances to the plaintiff in relation to recompense for goods and services provided to the borrower, the defendant was held to have "initiated or encouraged" the plaintiff to unjustly benefit the defendant. In this case, the enrichment was the increase in value of the secured business in relation to what it would have been without the plaintiff's actions. Because of the continued supply of corn by the plaintiff, the business was able to continue operating and was thus of more value to the defendant as security than it would have been if it had been unable to continue operations.

In applying the "initiated or encouraged" test to the facts of the case, Lohr J observed:

In a situation where a secured creditor initiates or encourages transactions between the debtor and suppliers of goods or services, and benefits from the goods or services supplied to produce such debts [sic], equitable principles require that the secured creditor compensate even an unsecured creditor to avoid being unjustly enriched. The...claim is at its strongest when the goods or services are necessary to preserve the security...A secured creditor can protect itself from unjust enrichment claims by remaining uninvolved or by informing the proper parties of its intent not to pay for debts incurred in maintaining, enhancing, or making additions to secured collateral. Given the evidence concerning [the lender's] active role in creating a perception that the corn would be paid for, its failure to inform the parties otherwise, and the need for the corn to feed the cattle in order to produce accounts receivable subject to the [lender's] security interest, under appropriate instructions the jury could have found that the doctrine of unjust enrichment required [the lender] to compensate Duggan Corporation for the corn it delivered to the [borrower's] feedlot.⁷¹

From this authority it seems clear that, at least in some United States jurisdictions, a lender may be liable for such unjust enrichment claims where the lender has taken some active interest in the business activities of a borrower in financial difficulties. This may be so even where no express representations have been made by the lender to the plaintiff.

The decision in the *Duggan* case has not gone without criticism in the United States. Tighe has criticised the decision on a number of grounds. First, the loss suffered by the plaintiff was due to the borrower and its deteriorating financial condition, and not due to activities of the lender. To avoid the loss, the plaintiff

70 Note 58 *supra* at 795.

71 *Ibid* at 798.

could have kept itself more closely informed of the borrower's financial circumstances and could have made an appropriate decision to withdraw its services if concerned about the borrower's lack of solvency.⁷²

Second, the *Duggan* case seems to stand for the proposition that a lender must effectively act as a 'guardian' for service providers to a borrower in financial difficulties. As such, the lender has a duty to inform all such service providers of their payment prospects in light of the borrower's financial position. This is an unworkable burden to impose on lenders, particularly considering the usual obligations of confidentiality owed to their customers.⁷³ Putting these obligations to one side for the moment, there are also practical difficulties involved in how appropriately to notify service providers of the borrower's financial problems. Such notification may well hasten the borrower's demise in circumstances where it might have been possible to save the borrower's business, but service providers begin to refuse supply to the borrower because of the threat of non-payment which it discovered from the lender itself. These concerns reflect comments made by Hill J in *Winterton Constructions* to the effect that the law does not impose on a financier an obligation to disclose to a third person the business of its customers.⁷⁴ Justice Hill raised the additional concern that if such a duty did exist, the financier would also potentially run the risk of defamation claims from the borrower in the event that any information it had passed on to third parties about the borrower's financial condition turned out to be inaccurate.⁷⁵

Third, the majority in *Duggan* suggested that a secured lender could escape a guardianship role in relation to service providers of the borrower by "cloaking itself in ignorance about the details of its borrower's operations".⁷⁶ Clearly, this is an undesirable course of action for lenders, particularly as it involves dereliction of its own commercial duties.

These are clearly significant concerns about the direction the United States cases have headed in respect of third party lender liability for unjust enrichment. Tighe does give some suggestions for ways in which lenders might in practice circumvent such liabilities, but most of these suggestions rely on things like obtaining agreements from the borrower to disclose confidential information about its financial position to third party service providers, or to send disclaimer notices to such third party service providers in relation to potential unjust enrichment liability.⁷⁷ Tighe himself acknowledges that these suggestions are unwieldy and expresses a preference for reworking the unjust enrichment principles to impose liability squarely on service providers to ensure that they protect their own commercial interests without having recourse to a third party lender as some kind of commercial "guardian".⁷⁸

72 Note 62 *supra* at 212-3.

73 *Ibid* at 213-8.

74 Note 9 *supra* at 667-8.

75 *Ibid* at 668.

76 Note 62 *supra* at 218.

77 *Ibid* at 219-223.

78 *Ibid* at 223.

As noted above, *Duggan* does not stand alone in United States law as a case imposing third party liability on lenders for such claims. There are other cases, such as *Gee* and *In re Gebco*, where similar cases against lenders have been made out successfully. These cases related to fact situations which fall in between *Duggan* and *DA Hill*; that is, where a lender has taken a less active interest in the borrower's business activities than in *Duggan*, but has had more involvement than was the case in *DA Hill*. In *Gee* and *In re Gebco* the financing agreements provided leeway for lenders to make progress payments directly to service providers, whether they in fact chose to do so or not. The financing agreements included specific references devoting particular earmarked funds for the work of such service providers. Additionally, the agreement in *Gee* required an architect employed by the lender to certify that work over secured property, in respect of which an advance was sought, had been done in a "good and workmanlike manner".⁷⁹ In *Gebco's* case, the lender had made express representations that sums adequate to compensate the relevant subcontractors were being held and would be disbursed by the lender on completion of the work.

A consideration of the fact situations arising in the *Duggan*, *Gee* and *In re Gebco* cases gives some indication of the factors American courts have taken into account in imposing liability on third party lenders in unjust enrichment for services provided. The courts have generally tended to rely both on finding some kind of enrichment to the defendant lender in terms of increased security value over and above what it would have been without the efforts of the relevant service provider; and the necessity for evidence that the defendant lender somehow "initiated or encouraged" the efforts of the service provider in this regard. Factors that will amount to such encouragement appear to include express or implied representations that the service providers will receive payment for their efforts, involvement by the lender in business activities of the borrower which are related to work carried out by the service providers and specific reference in security documentation to efforts of service providers relevant to a project over which finance is being advanced.

Notwithstanding obvious concerns about these legal developments in the United States, it would appear that some United States judges would advocate going even further than this and taking away the "initiated or encouraged" test altogether. Chief Justice Merritt, in a dissenting judgment in *Bluebonnet Warehouse Cooperative v Bankers Trust Company*,⁸⁰ for example, has recently stated:

I disagree with *Duggan* majority's [sic] contention that a secured party must "initiate or encourage the transaction" before an unsecured creditor can ever recover on a theory of unjust enrichment. As conceded in *Duggan* itself, acquiescence by

79 Note 58 *supra* at 1050.

80 Note 58 *supra*.

the secured creditor might be enough if the unsecured creditor's actions were necessary to preserve the secured collateral.⁸¹

Given the difficulties already associated with the *Duggan* principles, it is questionable whether a view such as Chief Justice Merritt's should be supported. It is clearly some way removed from what the current Australian position is, and arguably should remain removed from whatever the Australian position may become in the future.

The post-*Duggan* situation in United States law does, however, raise interesting policy questions about the desirable position for lenders in respect of such claims, some of which may become increasingly relevant to the development of Australian unjust enrichment principles.

VI. FUTURE PROJECTIONS FOR THIRD PARTY LENDER LIABILITY IN AUSTRALIAN UNJUST ENRICHMENT CLAIMS

As the Australian position on third party lender liability for unjust enrichment claims such as those under discussion in this paper is not fully settled, it is clearly possible that US jurisprudence may influence the development of Australian law. There are some strong legal and economic reasons supporting such a development. For one thing, large scale lenders may well be in a better financial position to absorb the risk of such losses than smaller scale service providers such as building contractors and equipment suppliers. Additionally, where lenders have taken some degree of management or control over the business activities of a particular borrower, particularly those relating to a service provider, the basic elements of an unjust enrichment claim may appear to be made out. There may well be an enrichment to the lender through the efforts of a service provider in circumstances where it appears unjust for the lender to retain the benefit without compensating the service provider accordingly.

In such a case, the question would then arise as to the appropriate quantum of restitutionary damages to be paid to the plaintiff by the lender. A detailed discussion of this issue is beyond the scope of this article. It should suffice for present purposes to note that most commentators to date have suggested that the relevant measure of damages in such a situation must be the value of the actual *enrichment* of the defendant, not the market value of the plaintiff's services. The value of the defendant's enrichment in a lender liability case will usually be the increase in value of the defendant's security interest which is attributable to the plaintiff's services.⁸² Thus, the exact value of such an enrichment may not always be easy to ascertain in practice.

A question even more vexing may be to establish a test for the requisite standard of 'unjustness' in relation to a particular enrichment. As seen from

81 *Ibid* at 35. Chief Justice Merritt further supports his view by reference to s 117 of the *Restatement of Restitution* which section is reproduced in his judgment. However, this argument is too far removed from Australian legal principle to be of significant value in a discussion such as the present.

82 See for example M McInnes (ed), *Restitution: Developments in Unjust Enrichment*, LBC Information Services (1996) p 103; *Gee v Eberle* note 58 *supra* at 1062; *In re Gebco Investment Corporation* note 58 *supra* at 148.

both the current Australian and US jurisprudence, no court has yet managed to establish a satisfactory benchmark test for 'unjustness' in this context. The previously mooted tests have tended to revolve largely around the substance of the relationship between the plaintiff and the defendant lender on the facts. The issue has been to ascertain some quality of this relationship that would morally justify the imposition of restitutionary liability on the lender.

Perhaps the key might be to shift the focus away from the relationship between the plaintiff and the defendant in such cases. This would certainly be in line with many of the 'mistaken payments' cases. If the focus was more on ascertaining an actual enrichment and a corresponding unfair detriment to the plaintiff, rather than on attempting to find a quality of 'unjustness' in the defendant's dealings with the plaintiff, it might be easier to frame an effective cause of action. However, this approach would also carry with it clear risks. It may prove quite unfair to defendant lenders who could suffer a marked decrease in the value of a secured property if forced to compensate any contractor who had provided services to a borrower prior to the borrower's insolvency. In such a situation, the lender might in effect suffer a double loss involving initial default by the borrower and then subsequent inability to fully realise a security due to claims by a third party service provider against the lender in unjust enrichment.

Thus, the recognition of such claims in Australian law may have the effect of increasing confidence in the building industry, but correspondingly decreasing financiers' willingness to participate in financing transactions involving proposed property developments. Alternatively, financiers may be willing to engage in such transactions, but fees may be increased commensurate with the financiers' perceived risks. Higher fees may, in turn, contribute to borrowers going into default more often, thus setting the wheel of unjust enrichment claims by their contractors in motion once again. Thus, a vicious circle of increased litigation against lenders and increased financing fees may be set in motion.

On the other hand, disallowing such claims may have the effect of decreasing confidence in the building industry and perhaps increasing the number of contractors and sub-contractors that may go out of business as a result of inability to obtain payment for work done.

Perhaps a sensible 'middle ground' would be for Australian courts to entertain cautiously some unjust enrichment claims with an emphasis on careful pleadings that clearly make out the elements of both 'enrichment' and 'unjustness'. Bearing in mind the usual inequality of bargaining power between large scale lenders and smaller scale contractors, the test for unjustness in this context should not be too onerous for a plaintiff to establish and should clearly be less than the standards of 'unconscionability' required in many areas of equity. On the other hand, it should also not be too harsh on lenders, particularly where a lender has little to no significant relationship with the activities of the plaintiff (provided that the lender has not been wilfully blind to such activities to avoid liability).

Thus, the initiative would be in potential litigants in the area to assist with the development of the correct framing of such claims. Such common law developments could be carefully monitored by state parliaments which could

legislate against such claims if they were becoming overly problematic for the court system or the economy.

Such developments in unjust enrichment may arguably be seen as consistent with developments in other areas of law where a lender may be held liable for obligations usually cast on its borrower in circumstances where it has taken some degree of active management or control interest in the borrower's business activities or property. One example would be under some environment protection legislation where various pollution control obligations may attach to a lender as an 'occupier' of premises where the lender has exercised some degree of management or control over secured property which actually belongs to its borrower.⁸³ Another example might be where lenders potentially attract various corporate liabilities as 'shadow directors' of a borrowing company as a result of a broad interpretation of the extended definition of "director" in s 60(1)(b) of the *Corporations Law*.⁸⁴

Lenders in Australia today should be aware of the possibility that such unjust enrichment claims may begin to gain some currency in Australian courts. Risk management officers should turn their minds to potential mechanisms to mitigate against such liabilities. Drawing from the United States experience, however, it would appear that there may not be many effective risk management options for lenders in this area other than perhaps attempting to insure against such potential claims or identifying relevant service providers and asking them to sign waivers of their rights against the relevant lender.

Neither of these options is particularly attractive. The first may be difficult to achieve in practice and may well be costly. The second may not be possible unless the lender is prepared to give some kind of good consideration to the relevant service providers in exchange for such waivers. Such parties are unlikely to waive their legal rights for nothing. Additionally, under this option, queries may be raised as to whether such an agreement would be consistent with notions of 'natural justice' or might amount to a contractual attempt to oust a court's jurisdiction.

Alternatively, lenders could adopt the option of identifying relevant service providers and keeping them informed periodically of the borrower's financial position with the borrower's consent. However, such a scheme is also unattractive for reasons canvassed above.

Definitive answers to some of the difficult issues raised in this article are unfortunately beyond the power of the author and may well prove unattainable in future legal practice. However, it is hoped that the article is able to stimulate debate on some of these questions and to aid in the future development of this growing area of Australian law.

83 See for example s 4(3)(b) of the *Environment Protection Act 1970* (Vic). Such lender liabilities for environmental damage caused by borrowers is discussed in some detail in J Lipton, "Project Financing and the Environment: Lender Liability for Environmental Damage in Australia" (1996) 11 *Journal of International Banking Law* 7.

84 See for example R Carroll, "Liability for Corporate Activity: Recent Developments", presented at the 1997 Corporate Law Teachers National Conference, University of Melbourne, 11 February 1997, pp 1-2.