WHEN BLOOD IS NOT THICKER THAN WATER

Darryl Browne examines the liability of a wife as her husband's attorney, her children as knowing third-party recipients, and solicitors as negligent advisors

This is a tale of two cases[1] with facts so similar that they could be read as one. In both instances, there was an enduring power of attorney (EPA);[2] the principal was the husband and father; the wife was the attorney (a donee of the power); and the attorney transferred the principal's property to the attorney's offspring with no, or nominal, consideration. The cases produced court orders whereby the deceased principal's estate recovered the property from the attorney's offspring.

SMITH

THE FACTS

Ronnie Smith appointed his second wife, Joy, as his attorney. The authority conferred on her by his EPA did not allow her to use his property to confer benefits on anyone. Legislation, reflecting the common law, prohibited this authority unless expressly conferred.[3]

Ronnie made a will giving some specific assets and half the residue to Joy. The other half-residue was divided equally between his sons from his first marriage, Ron and Neville. At the time, his estate was worth about AUD1.5 million. Soon after, he transferred his home from his name to his and Joy's names as joint tenants.

Almost immediately after, Ronnie descended into the mental fog of dementia, and was no longer able to manage his financial affairs. Joy assumed that role. She immediately sold some of his shares for AUD440,000. Two years later, she sold more shares (AUD377,000) and the home (AUD400,000). She spent some of the proceeds on herself: holiday cruises with her side of the family, an expensive car, expensive jewellery, gambling and regular entertainment.

However, Joy also used AUD347,000 of Ronnie's money to fund the purchase of a residence in the names of her daughter (from an earlier marriage) and the daughter's husband. When she sold the additional assets after two years, she used AUD200,000 to construct and fit out a 'granny flat' for herself on their property. The court concluded that these expenses were for her benefit and not Ronnie's.

KEY POINTS

WHAT IS THE ISSUE?
The liability of an attorney for acting without authority, and the liability of third parties who receive the principal's property with knowledge of the attorney's unauthorised actions.

WHAT DOES IT MEAN FOR ME?
Lawyers should warn appointed attorneys of the risk of acting without authority. If the attorney persists, the lawyer is under a duty to decline to act.

WHAT CAN I TAKE AWAY?
An attorney, including a spouse, has limited ability to personally benefit from, or benefit others with, the other spouse's property, unless that authority is expressly conferred.

THE PROCEEDINGS

At Ronnie's death, his estate was valued at AUD75,000. His sons brought derivative proceedings on behalf of his estate against Joy, the executor, and the daughter and son-in-law. Joy was found to have obligations to Ronnie as a fiduciary: 'She was no less the deceased's agent, constrained by the terms of the power of attorney, because she was the deceased's wife.'[4]

Joy argued that, having discharged her wifely duties to Ronnie, she should be excused from any breach of fiduciary duty attending her dealing with his property. First, Joy relied on legislation[5] that imposed a liability on one spouse to maintain the other if the other was unable to receive adequate support. (However, no application was formally made.)

Second, she argued that the court could make provision for the maintenance of the family of an incapable person out of their estate. (This jurisdiction, recognised in *Brown* v *Smith*[6] and *Countess of Bective* v *Federal Commissioner of Taxation*,[7] allows a care provider to receive 'incidental benefits' without being called to account. The judge said that an attorney would comfortably fit within this principle, but it did not operate retrospectively as a licence for the attorney to disregard the principal's interests.)

Third, she argued she was her husband's 'agent of necessity'. (The court found this to be contrary to legislative emancipation of married couples.)[8]

Fourth, she asked that her personal liability as fiduciary be excused.[9] The court decided that '[s]he cannot be found to have acted honestly or reasonably so as to warrant an order... that she ought fairly to be excused from personal liability for her misapplication of the deceased's property'.

Through current impecuniosity, Joy was unable to make good the property she was held liable to restore to Ronnie's estate. The sons claimed against the daughter and son-in-law as volunteers in receipt of trust money paid in breach of trust[10] and, alternatively, as knowing recipients of trust property pursuant to the first limb in *Barnes* v *Addy*.[11] The daughter and son-in-law knew that Joy had no financial means of her own, and that Ronnie maintained her financially. This and other facts conferred constructive knowledge by reason of wilfully and recklessly failing to make inquiries that an honest and reasonable person would have made. Accordingly, they were bound in conscience to account for his property, and not to apply it to their own use.

Last, the defendants contended that the sons were denied equitable relief because they were guilty of laches, acquiescence and delay in asserting those entitlements. However, as Joy had warned them off communicating with their father without her consent, the court was not satisfied that the sons had engaged in deliberate and informed inaction.

THE OUTCOME

The daughter and son-in-law's residence was held beneficially for Ronnie's estate, with the sons taking the whole as tenants-in-common in equal shares, to the exclusion of Joy. Any entitlement she had to participate in the estate as a residuary beneficiary was taken, on an application of the rule in *Cherry* v *Boultbee*, to have been satisfied from that part of the deceased's estate for which she had not accounted.

REILLY

THE FACTS

Frank Reilly made the same type of power of attorney as Ronnie Smith. His enduring attorneys were his wife, Peg, and his son, Joe. They were authorised to act severally, but all the relevant acts were performed by Peg. There was no authority given to the attorney to confer benefits. After Frank lost mental capacity, he was admitted to a nursing home. As his attorney, Peg transferred Frank's 550-hectare (1,359-acre) farm to their four daughters for AUD1 million. (At that time, the farm was valued at AUD815,000.) One solicitor performed all aspects of the legal work involved in this transaction for all persons.

Peg's primary motivation for the transfer was found to be her notion of fairness between her children. The court found that a secondary motivation was that, by divesting him of assets, Peg would reduce the costs associated with Frank's nursing home care. The court considered that this motivation was not objectionable unless tainted by revenue fraud.

THE PROCEEDINGS

By his will, Frank left the farm to his and Peg's son, Joe.[12] After Frank's death, Joe brought a derivative action against Peg, his four sisters and the solicitor. All were liable for various reasons and to varying degrees.

As with *Smith*, the judge observed that there was no general rule of agency between married, or cohabiting, couples. The transfer was a 'fraud on the power', because Peg, as attorney, exercised her power 'for a purpose, or with an intention, beyond the scope of or not justified by the instrument creating the power'.[13]

Joe's claim against his sisters was based on the first limb in *Barnes* v *Addy*. The required knowledge was imputed to the sisters, as their solicitor was involved 'on both sides of the conveyancing transaction from start to finish'. The solicitor knew the facts, because he held the EPA in his possession; he knew that the deceased lacked the mental capacity to confer additional authority on the attorney; and he knew the terms of Frank's will. The court considered that the solicitor ought to have appreciated that the attorney had no authority (actual or ostensible) to do what she sought to do in Frank's name.

At about the time the farm was transferred, Peg told her son that she proposed to transfer the farm to her daughters. However, she did not disclose to him the terms of Frank's will. Joe had no knowledge that he was to inherit the farm. Accordingly, the court found that the defence of acquiescence could not succeed, for similar reasons to *Smith* – namely an absence of informed inaction.

THE SOLICITOR'S LIABILITY

Joe claimed that he was personally owed a duty of care incidental to, and consistent with, a duty of care owed by the lawyers to his father. The judge observed that the solicitor was bound to exercise reasonable care in performance of his retainer, recognising that he was retained by the attorney 'in a representative capacity that required him to protect the interests of the deceased (and, incidentally, the plaintiff as an intended beneficiary of the deceased)'. The solicitor should have recognised that he could not act for all parties to the proposed intergenerational transfer. Better options were available to Peg, such as invocation of the protective jurisdiction exercised by the Supreme Court and the availability of jurisdiction to make a statutory will.

Crucially, the solicitors should have warned the attorney of the risks associated with the course she proposed to take: 'If, duly warned, she persisted in instructions to take that course, they were under a duty to decline to act for her. They could not act for her without exposing her and themselves to substantial risks of the nature illustrated by the current proceedings'.[14]

1 *Smith* v *Smith* [2017] NSWSC 408 (*Smith*) and *Reilly* v *Reilly* [2017] NSWSC 1419 (*Reilly*) **2** A power of attorney that confers authority even when the donor (called the principal) has lost mental capacity **3** *Powers of Attorney Act 2003*, NSW, ss12 and 13 **4** [2017] NSWSC 408, [424] **5** *Family Law Act, 1975 (Cth)*, s72 **6** (1878) 10 Ch D 377 **7** [1932] HCA 22 **8** *Married Persons (Equality of Status) Act, 1996*, NSW **9** *Trustee Act, 1925*, NSW, s85 and the court's inherent jurisdiction **10** *Black* v *S Freedman & Co* [1910] HCA 58 **11** (1874) 9 Ch App 244 **12** This was the result after rectification of an omission in the will **13** [2017] NSWSC 1419, [127] **14** *Id* at [405]

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