

TIL DEATH US DO PART: JOINT TENANCY AND THE TRUSTEE IN BANKRUPTCY

TIM MCGRATH* AND KATE GALLOWAY**

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Overview

Our talk today considers the issues facing a trustee in bankruptcy when attempting to ascertain the extent or existence of a bankrupt's interest in real property. We will highlight issues which a trustee might reasonably encounter in ascertaining the extent of property available for distribution to creditors.

We will consider two elements in particular in light of the recent decision of the High Court in *Cummins (a bankrupt) v Cummins*,¹ and the Federal Court in *Anderson v Peldan*.² Both cases involved an examination of joint tenancy. Joint tenancy is one way for two or more co-owners to hold their estate in common. It will only arise where there is a unity of time, title, possession and interest between co-owners, and then only where there is an intention to hold as such (*Property Law Act* Qld provides for a presumption in favour of tenancy in common). The joint tenancy provides each co-owner the right to survivorship - upon the death of an owner that owner's estate is extinguished and the estate of surviving co-owners are enlarged proportionately to the extent of the deceased's estate. This occurs irrespective of the deceased's testamentary wishes.

Anderson v Peldan concerned the severance by an insolvent of joint tenancy held by the insolvent and his elderly spouse and whether the severance before death is capable of being a "transfer of property" in terms of s121 of the *Bankruptcy Act*.

* Partner, Miller Harris Lawyers, Cairns

** Associate Lecturer, James Cook University, Cairns

¹ [2006] HCA6 (unreported, Gleeson CJ, Gummot, Hayne, Heydon & Gennan JJ, 7 March 2006)

² [2005] FCA 1179 (unreported, Kiefel J, 25 August 2005)

The High Court's decision in *Cummins* examines the scope of s121 (before the enactment of the anti-avoidance provisions this year) and contains enlightening discussion on the nature of a bankrupt's underlying equitable interest in real property, despite the bankrupt's legal interest identified on the face of the title.

Finally, we will look at the doctrine of exoneration and the extent to which a party's estate might be subject to creditor claims.

Anderson v Peldan: The facts

It is difficult to imagine facts which might more clearly illustrate circumstances in which a trustee in bankruptcy might seek to apply s121 to the severance of joint tenancy. The facts can be briefly outlined as follows:

1. Mr and Mrs Pinna purchased a property at Carindale in Brisbane in 1995 and were registered as joint tenants.
2. By August 2003 Mr Pinna was in default of his tax obligations to the tune of \$280,000.
3. On 11 September 2003, Mr and Mrs Pinna executed a form of transfer of a "one-half interest in fee simple". Mr Pinna was said to be both the transferor and transferee.
4. The consideration for the transfer was expressed as "the unilateral severance of a joint tenancy pursuant to s59(2) of the *Land Title Act 1994*" (the Qld Torrens legislation).
5. The transfer registered on 5 November 2003.
6. Mrs Pinna died (unexpectedly) on 12 January 2004.
7. Mr Pinna was declared bankrupt on 21 April 2004.
8. On 28 April 2004 the property was sold to a third party for \$600,000. Half that sum was paid to the bankrupt's estate.

Anderson v Peldan: The issues

The litigation concerned the treatment of the balance sale proceeds. At the time of severance of the joint tenancy Mr Pinna was plainly insolvent. At the time of the sale of the property Mr and Mrs Pinna were registered as tenants in common in equal shares. As a consequence, the share attributable to Mrs Pinna's interest would ordinarily have become part of her deceased estate. Those funds would not have been available to the trustee, or to the bankrupt's creditors.

Mr Pinna's trustee alleged that the severance of the joint tenancy was a transfer which was void as a result of the operation of s121 of the *Bankruptcy Act*.

Joint tenancy intact

If the trustee was correct then the severance of the joint tenancy would have been disregarded. Mr and Mrs Pinna would have continued to hold the property as joint tenants until Mrs Pinna's death. Through his survivorship, Mr Pinna would then have become the sole proprietor of the property. Consequently, the whole of the property (or the proceeds of its realisation) would form part of the bankrupt's estate, and be divisible amongst creditors.

Bankruptcy Act, s 121

Section 121 (in the form which applied at the material time) provided:

A transfer of property by a person who later becomes a bankrupt (the transferor) to another person (the transferee) is void against the trustee in the transferor's bankruptcy if:

- (a) the property would probably have become part of the transferor's estate or would probably have become available to creditors if the property had not been transferred;
- (b) the transferor's main purpose in making the transfer was:

- (i) to prevent the transferred property from becoming divisible among the transferor's creditors; or
- (ii) to hinder or delay the process of making property available for division among the transferor's creditors.

Transfer of Property: s121(9)

The trustee had a second string to his bow.

- (a) For the purposes of this section:
 - (i) transfer of property includes a payment of money; and
 - (ii) a person who does something that results in another person becoming the owner of property that did not previously exist is taken to have transferred the property to the other person.

“Property”, defined in s5, includes any estate or interest, present or future, vested or contingent, arising out of or incidental to any real or personal property.

The decision: Jarrett FM

At first instance Federal Magistrate Jarrett found that Mr and Mrs Pinna had reached an agreement on 11 September 2003 to sever their joint tenancy. He did not accept that severance was unilateral as stated on the face of the transfer documents.

His Honour had no difficulty in concluding that Mr Pinna was insolvent from at least early August 2003. The threshold issue though was whether or not the severance of the joint tenancy was a “transfer of property” in terms of s121(1) of the Act.

His Honour found that there was a transaction which had changed the nature of the bankrupt's interest in property from that of joint tenant to tenant in common. The change in the nature of the interest carried with it a change in the bundle of rights attached to the bankrupt's interest in the property. His Honour concluded that a change in interest must

necessarily amount to a disposition of property interest, notwithstanding that other interests were acquired in their stead.

His Honour was satisfied that had there not been the transfer, the deceased's interest would have become part of the bankrupt's estate. His Honour then concluded, inevitably, that the operation of s121(2) had the effect of deeming the bankrupt to have the requisite purpose required in s121(1)(b)(i) namely to prevent the transferred property from becoming divisible amongst the transferor's creditors.

Appeal decision: Kiefel J

The executors of Mrs Pinna's estate appealed to the Federal Court.

The central submission for the appellant was that the giving up of a right to the whole of the land by survivorship was not a transfer of property within the operation of s121 of the Act. It was merely a change to the character of what they held. Her Honour was greatly influenced by the judgment of Dean J in *Corin v Patton*³ where His Honour identified two steps involved in the severance of a joint tenancy, namely:

1. The creation of a distinct proportionate share of the whole; and
2. The detachment of that share from the property which is subject to the joint tenancy,

with the consequence that the transferee received the share of a tenant in common. Whilst Her Honour observed that the Pinnas' severance was effected by a "transfer" document the transfer was not a transfer "to another person" as required by s121(1). One must consider in light of section 121(9)(b) however whether the reconstitution of rights (independently of a transfer as that might be understood in general parlance) had arisen. Her Honour was satisfied that the severance of the joint tenancy had done something which resulted in the deceased becoming the owner of an interest in property that did not previously exist.

³ (1990) 169 CLR 540, 575.

The difficulty, as Her Honour saw it was that notwithstanding that ‘transfer’ the question posed by section 121(1)(a) could not sensibly be answered:

“Would the property interest created likely have been available to creditors if it had not been created?”

Having regard to the authorities, Her Honour considered that the inquiry should properly be:

“But for the acts undertaken by the bankrupt, would the property held by the bankrupt before the acts were undertaken probably have remained available to creditors”.

In respect of Mr Pinna’s interest the question would undoubtedly be answered “yes” but the inquiry arising under section 121(1)(a) did not extend to Mrs Pinna’s interest. Her Honour concluded:

The purpose of the section is to prevent fraudulent dispositions of property. The question imposed focuses upon the effect of the disposition on the property the subject of it. It is intended to protect creditors from such a dealing. It could not be intended to enlarge their interests because of some unforeseen event.

The question for the High Court to decide is whether the loss of the survivorship interest is a **transfer** of property. Kate will now look at the theoretical foundation of property and whether the right of survivorship fits within it.

The nature of joint tenancy

We’ve now set the scene for discussing the issues raised in *Anderson v Peldan* – this is primarily the *nature* of a co-owner’s interest in land. We’ll examine whether a joint tenancy in itself, and the rights it encompasses, can be considered property. Then we’ll look at the circumstances in which a joint tenant’s interest may differ in *extent* from that expected – namely a notional 50% interest. All this is intended to guide the trustee in bankruptcy to avenues for recovery of assets, or to flag potential problems.

In considering *Anderson v Peldan*, the Federal Court⁴ referred to the severance of a joint tenancy in terms of the alienation of a bundle of rights. This seems to categorise the manner in which property is held (ie as joint tenant) in terms of property itself. We will turn our minds to whether analysing co-ownership as property in itself is accurate; and whether therefore the change of co-owners' relationship from a joint tenancy to a tenancy in common effects some transfer of *property*.

In the context of the *Bankruptcy Act* s121, the questions are:

1. whether rights particular to a joint tenancy ie the right to survivorship (or estate of a deceased joint tenant upon their demise) is 'property' within s5 of the Act;
2. whether the severance of the joint tenancy creates a *new* right in the co-owner of alienability by will; and
3. therefore whether the severance of a joint tenancy represents a *transfer* of that property in terms of s121(1) of the Act.

Is a joint tenancy 'property'

Jarrett FM⁵ found that there was consideration for the severance of the joint tenancy: namely 'relinquishing the beneficial interest of a joint tenant of a common property, including the right of accretion by survivorship in return for the share of a tenant in common'.⁶ Given this, 'and given the nature of the consequences that flow from a change from joint tenancy to tenancy in common, it seems... that what was being disposed of... were property interests'.⁷ Indeed '...the change in the nature of his interest carried with it a change in the bundle of rights attached to his interest in the property.'⁸

A broad interpretation of this analysis implies that there is a transfer of an estate in land: namely the whole of the joint tenant's interest in land, and a taking of a new (proportionate) estate as tenant in common.

⁴ *Anderson v Peldan* [2005] FCA 1179 (unreported, Kiefel J, 25 August 2005), [5].

⁵ *Peldan v Anderson* [2005] FMCA 142 (unreported, Jarrett FM, 21 February 2005).

⁶ *Corin v Patton* (1989) 169 CLR 540, 574.

⁷ *Peldan v Anderson*, [29].

⁸ *Peldan v Anderson*, [28].

Alternatively, this analysis identifies the change as a relinquishment of a property interest: the right of survivorship. Either way, with respect, the federal magistrate does not identify what is the property. Instead the emphasis is on the *consequences* of a transaction rather than the nature of the thing itself the subject of the transaction. This approach was taken on appeal by Kiefel J who said that Mr Pinna could not have ‘forfeited his right and transferred to Mrs Pinna the right to alienate her share by will’⁹ as this was simply the *consequence* of the transaction.

In the Federal Court, Kiefel J then identified the transaction as a ‘transfer which takes place in the detachment of... new shares in the property ... from one former joint tenant to themselves.’ This step represents the broader view of Jarrett FM’s analysis of consideration, but is based on the judgment of Deane J in *Corin v Patton* where he describes the transfer of an interest as joint tenant as a staged process. Deane J however makes this analysis in the context of a *transfer* of an interest as joint tenant to a *third party* – who before the transaction had no interest at all in the property (the land). This analysis is valid in those circumstances, and reflects the nature of the interest held by a joint tenant as a potential divisible share in the land.¹⁰ However it does not seem so clear in circumstances which involve a severance of the joint tenancy by agreement between co-owners – where each co-owner already owns an estate in the land in common. Although Kiefel J found that this is not a transfer of property *to another person*, it is implied that there is property involved.

Lastly Kiefel J analysed s121(9)(b) to ascertain whether the new ‘character’ of the co-ownership as tenants in common was the creation of a new interest. As mentioned, ‘the enquiry arising under s121(1)(a) does not extend to *Mrs Pinna’s* interest. And it does not... extend to what would likely have occurred to *Mr Pinna’s* interest in the event of *Mrs Pinna’s* death.’¹¹ This implies that the property sought by the trustee is really *Mrs Pinna’s* estate in land; that *Mr Pinna’s* interest before the severance does not extend to *Mrs Pinna’s* interest ie that there is no property in her estate. By implication this suggests that the manner in which the estate in land is held is not a property interest itself.

⁹ *Anderson v Peldan* [2005] FCA 1179 (unreported, Kiefel J, 25 August 2005), [10].

¹⁰ Peter Butt *Land Law*.

¹¹ *Anderson v Peldan*, [16].

So far the court has failed to categorise the *property* nature of the joint tenancy independent of the co-owners' estate in the land itself.

Different Conceptions of Property

The possibilities canvassed at first instance and on appeal, are that:

- the transaction severing the joint tenancy was a mutual transfer of a half interest in land; and
- there was a shift in the right to alienate by will which would be categorised as property.

Mr Pinna's estate, always equivalent to a one half share, remained vested in him. The issue is whether he had an interest in *Mrs* Pinna's estate, amounting to property, which he transferred. We'll examine this through the traditional framework of property classification, and through the bundle of rights theory.

Traditional Classification of Property

Traditionally property was classified according to the nature of the remedy available at law. Real property was recoverable in a real action and personal property through an action for damages. The claim to property in *Anderson v Peldan* could be characterised as a right to survivorship, or an interest in *Mrs* Pinna's land – can these be classified within the traditional framework?

A joint tenancy does not represent a 'thing' recoverable if taken away through a transmutation to a tenancy in common. The loss of the right to survivorship which may occur by agreement, by the action of the joint tenant themselves or by intervention of any number of other factors, is not recoverable as a thing. The right to survivorship cannot be categorised as real property under the classical framework.

Neither though can the right to survivorship be categorised as personal property. It can be taken away through the actions of either co-owner, neither of whom will be liable in

damages to the other. It can be destroyed through an external event such as bankruptcy, but will not be compensated for as against any third party.

Alternatively the right of survivorship may give the joint tenant a property interest in the estate of their co-owner which manifests through that right to survivorship ie the estate will be realised after death of the co-owner. Although clearly identifiable as Mrs Pinna's estate in land when in her own hands, for the duration of the joint tenancy is Mrs Pinna's estate also property of Mr Pinna?

The law of course recognises future interests in land, which are categorised as real property but the potential for enlargement of a joint estate to an estate in severalty is by definition not a reversion or remainder: nor can it be classified as an executory interest in land. In one sense the estate of each co-owner *in the whole* is subject to a contingency, namely death of all other joint tenants (and non-severance otherwise). But the unique nature of joint tenancy is considered separately to any other contingency attached to land under the doctrine of estates.

This conclusion can be tested by asking the question: if the joint tenancy were a contingent or executory interest in the whole of the land, could it be recovered in rem if the interest were taken away? The answer is no. The joint tenancy represents the relationship and rights between the parties but not an interest in land separate from that owner's own estate in common. Nor can the relationship be categorised as personal property because it cannot be enforced even in an action for damages for loss. The limitations of trying to represent the joint tenancy in terms of the traditional classification of property are clear - joint tenancy per se is clearly not property. And if there is no property right, then upon severance of a joint tenancy, there is no possibility of a transfer of a property right.

The Bundle of Rights Theory of Property

As their honours have made reference to the bundle of rights associated with the joint tenancy it is relevant to consider the nature of the joint tenancy in terms of the bundle of rights theory of property.

Penner in the ULCA Law Review identifies the bundle of rights theory of property as emanating from Honore's description of the incidents of property.¹² The rights include the right to possess; to use, manage and receive income; to capital; to alienate; to security; of transmissibility and absence of term; prohibition of harmful use; and the liability to execution.¹³

If the bundle of rights theory is accepted, none of these incidents can sensibly be applied to the nature of a right of survivorship, nor to any possible interest of Mr Pinna in the estate of Mrs Pinna.

- The right to possess arises from Mr Pinna's estate, as does his right to receive income and to alienate.
- The right to survivorship itself, or any possible right to the balance of the estate do not give him a right to alienate Mrs Pinna's estate, and he cannot alienate his right to survivorship.
- The right to security implies that ownership continues for as long as the owner chooses, and remains solvent.¹⁴ This is not present in a joint tenancy. There is no absolute interest in Mrs Pinna's estate, and regardless of the choice of Mr Pinna, his right to survivorship may be extinguished by Mrs Pinna.
- Likewise, there is no right to transmit the right to survivorship, or any rights in Mrs Pinna's estate. While Mr Pinna might enter into an enforceable contract to assign the benefit of his right to survivorship, the operation of the *jus accrescendi* will render him the owner first, with the grantee of the right taking a transfer of an interest subsequently. The right of survivorship or his 'interest' in Mrs Pinna's estate are not of themselves transferred.

Remember: Mr Pinna's right to have his estate enlarged depends on the joint tenancy continuing, **and** his survival, **and** Mrs Pinna's death.

¹² JE Penner 'The "Bundle of Rights" Picture of Property' (1996) 43 *UCLA Law Review* 711, n5.

¹³ *Ibid*, 755-65.

¹⁴ *Ibid*, 760.

- There is no liability for execution subsisting in the right of survivorship or in Mr or Mrs Pinna's estate as joint tenants. The right of survivorship does not transfer to a trustee in bankruptcy – indeed the joint tenancy will be severed and survivorship ends. Severance occurs because of the inherent nature of joint tenancy, which will only exist so long as the four unities (time title possession and interest) remain.

Even if one accepts the validity of the bundle of rights theory of property, it is impossible to see how the right of survivorship falls within what is contemplated as forming the bundle or of representing part of the bundle.

Challenging the Bundle of Rights Theory

Penner seeks to challenge the validity of the bundle of rights theory of property on the basis that it shows property as a natural composite which can be carved into free-standing parts.¹⁵ In his view, this represents 'a confusion because of the multiple distinct meanings associated with the term,' which creates a flexible concept without a definable essence.¹⁶ As flexible as the concept is, it is difficult to grasp the essence of what we are looking for. Could it be that Penner's 'unified' definition of property there is scope for conceptualising as property the right of survivorship, or even the potential for the interest of any other joint tenants?

The very nature of property lies in the relationship between a person and a thing, rather than identification of the thing itself. The relationship must however only be **contingent** – if it is not possible for anyone else to have this relationship with this thing, then our relationship cannot be categorised as property: it must be something else. Penner's analysis is useful here to single out the nature of the joint tenancy. Penner looks at a number of different rights which do *not* constitute property because of the lack of a contingent nature – and because they could not exist outside of ourselves. Contracts of employment are not freely alienable due to the specificity of the employee and their skills; licences for professional practice relate to the skill and qualification of the

¹⁵ Ibid, 767.

¹⁶ Ibid, 770.

licensee; body parts which remain attached to our person are contingent on ourselves and cannot constitute a thing capable of being owned by another.¹⁷

A joint tenancy and rights attendant on it is conceivable only in relation to the joint tenants themselves. The four unities¹⁸ as a prerequisite for the existence of a joint tenancy axiomatically create the right of survivorship only in the parties to the transaction creating it. These rights cannot exist outside of those parties, so under this analysis they – in the guise of the right of survivorship or the consequence of that, namely the additional estate itself – cannot be categorised as property.

The Extent of a Joint Tenant's Interest

A joint tenancy characterises the co-ownership relationship rather than property itself, but it does represent the manner in which an estate in land is held, and in that respect represents a potential half share in that land, in common. We turn now to consider the true *extent* of an interest represented by that potential share of a legal joint tenant.

Property available to creditors of a joint tenant may not truly be represented in the legal estate. The High Court has recently considered the extent of the joint tenant's interest in *Cummins v Cummins*.¹⁹ Mr and Mrs Cummins had held land registered as joint tenants, but argued that Mrs Cummins' contribution of roughly $\frac{3}{4}$ of the purchase price meant that while the couple held the legal estate as joint tenants, equity should recognise the beneficial estate as tenants in common in the shares (roughly) $\frac{3}{4}$ to $\frac{1}{4}$.

While the court found in *Cummins* that there was no tenancy in common in equity, the process of examining underlying title is one practitioners need to keep in mind when searching for property available to creditors. A joint tenancy at law may indicate an underlying property interest greater than a mere 50%.

In general, despite a legal estate as joint tenants, equity will find in favour of a tenancy in common of the beneficial interest where the parties provided purchase money in unequal

¹⁷ Ibid 803-4.

¹⁸ Of time, title, interest and possession.

¹⁹ [2006] HCA 6 (Gleeson CJ, Gummow, Hayne, Heydon and Crennan JJ, 7 March 2006).

shares (in which case they would hold in shares proportionate to their contribution). This presumption could be rebutted by evidence that the parties intended equal ownership with a right of survivorship. This in turn could be rebutted by the presumption of advancement also described as the ‘absence of any reason for assuming that a trust arose or... that the equitable right is not at home with the legal title’.²⁰ Traditionally this has only applied to a husband in favour of a wife, but not vice versa.

The presumption of beneficial tenancy in common was found by the court in *Cummins* to be rebutted. When Mrs Cummins had acquired Mr Cummins’ interest, the transfer nominated consideration of **half** the value of the property. The court found this was evidence of the proportion the Cummins considered Mrs Cummins owned. If the parties did intend Mrs Cummins hold a $\frac{3}{4}$ share, then that would have been reflected in the consideration for the transfer.

The court went further though in examining the extent of co-ownership. It found judicial comment to support the rebuttal of the equitable presumption: namely that spousal contribution to property acquisition is taken to indicate an intention of joint beneficial ownership.²¹ The court seems to be looking to the parties’ intention at the time of purchase of the property, but its subsequent discussion and references to the Cummins’ marriage relationship reflects the thinking of the ‘presumption’ of advancement. This sits uneasily with the equitable presumption of tenancy in common.

Gibbs CJ held in *Calverley v Green* that:

the presumption should be held to be raised when the relationship between the parties is such that it is more probable than not that a beneficial interest was intended to be conferred, whether or not the purchaser owed the other a legal or moral duty of support.²²

²⁰ *Calverley v Green* (1984) 155 CLR 242, 247, citing *Martin v Martin* (1959) 110 CLR 297, 303.

²¹ *Ibid* [67], citing *Pettit v Pettit* [1970] AC 777, 815.

²² *Ibid*, 250.

Applied to the Cummins, the court refused to attach a trust to the legal estate 'representing differently proportionate interests as tenants in common'.²³ It was presumed that because the Cummins were married, Mrs Cummins had intended to confer on Mr Cummins the benefit of her proportionately larger contribution to the purchase of the land.

Deane J in *Calverley v Green* acknowledged that the worth of [the presumption of advancement] may be debateable, but that such presumptions are 'too well entrenched as "land marks" in the law of property to be simply discarded by judicial decision'.²⁴ He identified that the class of relationships to which the 'presumption' applies was not closed, and that it should extend to a wife vis-à-vis her husband. While there has traditionally been no presumption of advancement from a wife to a husband this class appears to have been extended by the court in the *Cummins* case. Alternatively, the discussion about the nature of the marriage relationship serves as evidence as to intention of the parties that they hold as joint tenants. Either way a wife who contributes disproportionately to the purchase of property will bear the onus now of rebutting a presumption that she and her husband held other than equally.

The first issue with this is the lack of transparency of the analysis which apparently seeks to establish intention yet using the style of the presumption of advancement. Additionally, the court's comments about the Cummins' transaction highlight the inappropriateness of this kind of presumption in today's law.

The High Court in *Cummins* spent some time examining the nature of the marriage relationship and the presumptions that could be drawn from this about beneficial ownership. The court accepted the view of Professor Scott, author of a 1989 edition on the law of trusts that:

it is often a purely accidental circumstance whether money of the husband or of the wife is actually used to pay the purchase price to the vendor, where both are

²³ *Cummins v Cummins* [2006] HCA 6 (Gleeson CJ, Gummow, Hayne, Heydon and Crennan JJ, 7 March 2006) [71].

²⁴ *Calverley v Green* (1984) 155 CLR 242, 265.

contributing by money or labour to the various expenses of the household. It is often a matter of chance whether the family expenses are incurred and discharged or services are rendered in the maintenance of the home before or after the purchase.²⁵

The court said that this reasoning ‘applies with added force in the present case where the title was taken in the joint names of the spouses’.²⁶ But the fact that the Court sought to justify the application of a presumption which rests solely on the nature of the marriage relationship – whether of advancement or of the nature of property interests between spouses – highlights that the presumption itself must be on shaky ground.

In attempting to examine ‘the particular circumstances of the case’, the court found it ‘unrealistic to suggest that the solicitor for [the] Cummins did not at any point advise his clients on the significance of taking title as joint tenants rather than tenants in common’.²⁷ In fact as the contract settled in 1970, it is not unrealistic at all to assume that the solicitor did no more than present documents to the couple to sign without any such explanation, having assumed that they would hold as joint tenants. It was still not uncommon conveyancing practice in Queensland in 1990 to nominate husband and wife as joint tenants unless they instructed to the contrary. In addition, a traditional marriage may in 1970 have seen the husband take care of legal affairs in which case the wife may not have been advised at all about property interests. This may be so particularly where the husband, in this case Mr Cummins, was a member of the legal profession.

Kirby P pointed out in *Foregard v Shanahan*²⁸ (discussing co-ownership) that it is inappropriate to permit ‘rules’ to govern judicial discretion ‘where the rules were developed long before the existence of the phenomena to which [the law] must now typically apply’. He referred to:

²⁵ *Cummins v Cummins* [2006] HCA 6 (Gleeson CJ, Gummow, Hayne, Heydon and Crennan JJ, 7 March 2006), [70], citing *The Law of Trusts* (4th ed, 1989), 239.

²⁶ *Cummins v Cummins* [2006] HCA 6 (Gleeson CJ, Gummow, Hayne, Heydon and Crennan JJ, 7 March 2006), [71].

²⁷ *Ibid*, [72].

²⁸ (1994) 35 NSWLR 206.

- exceptionally high incidence of home ownership in Australia, including co-ownership, by women and people in de facto relationships; and
- the changed nature and availability of credit and the widespread availability of consumer credit.

The implication of this is that people have access to money and own property in ways and for reasons unthinkable even 30 years before. It is not clear that Professor Scott's statement, accepted by the court in *Cummins*, is truly reflective of marriage relationships. There are any number of relationships in which that may be the case, but any number also in which parties may conduct their affairs differently. A presumption may aid trustees of spouses to claw back property, but fails to recognise the diversity in the nature of property holdings in the first place. In the end Mrs Cummins' disproportionate contribution to the land acquisition, which may have been acknowledged by a court under different circumstances (eg by a Family Court), is denied through the lens of bankruptcy law.

Ultimately, the position of trustees of estates consisting of jointly owned property is not what it may seem on first blush. Firstly, pending the High Court decision on *Peldan v Anderson*, the nature of a joint tenancy appears too ethereal to benefit a creditor in the unusual situation of attempting to seize a right of survivorship. Secondly, the extent of the interest of a joint tenant of a legal estate may be diminished or enlarged by a presumption of a resulting trust. But the impact of a presumption of advancement on this state of affairs may further alter the extent of the interest, aligning it with the legal estate. As with any equitable remedy its application is discretionary. However a diligent trustee may seek to take advantage of these presumptions for the benefit of creditors – and those structuring their affairs will need to be diligent in the application of their funds to truly represent their intended property rights.

Exoneration

We have seen from the foregoing the extent to which equity might adjust each co-owner's proprietary interest in real property. These "adjustments" occur below the surface of legal title and may not be immediately apparent to third parties or to strangers such as a trustee in bankruptcy.

The assessment of a party's equitable interest will determine, for example, the way in which co-owners will participate in the proceeds of sale of an asset. The "adjustment" does not serve to make one co-owner the creditor of another. It operates by adjusting parties proprietary interests.

The doctrine of exoneration operates in a different way. It seeks to address the order in which each co-owner's interest will be made available to satisfy a creditor's claim.

Farrugia v Official Receiver in Bankruptcy

The doctrine gained recognition early in the eighteenth century but its application in the context of torrens title land did not emerge fully until the decision of Dean J in *Farrugia v Official Receiver in Bankruptcy*²⁹.

The facts in that case are by no means extraordinary. Mr and Mrs Farrugia were registered as proprietors as joint tenants of real property at Seven Hills, which constituted the family home. The subject transaction took place on 31 July 1979. Prior to that time there was a first registered mortgage on the land for an amount of \$12,500. That debt related to the cost of acquisition and establishment of the matrimonial home.

On 31 July 1979 the parties refinanced and borrowed an amount of \$23,000. Of that sum:

1. \$12,500 discharged the original mortgage; and
2. \$10,500 was obtained and used by Mr Farrugia in the building business which he carried on and in which Mrs Farrugia had no direct or financial interest.

²⁹ (1982) 43 ALR 700

Mrs Farrugia's evidence

The transcript of Mrs Farrugia's evidence went along these lines:

I asked my husband "what do you want the money for"

He said "that has nothing to do with you; I need the money for the business"

I said "very well, I will sign the mortgage"

Within 18 months Mr Farrugia's business had failed and he was declared bankrupt. At about the same time the parties had signed a contract for the sale of the matrimonial home. The settlement took place in March 1981 and net proceeds of sale after discharge of the mortgage was around \$18,000.

Trustee's figures

Based upon the husband's interest as co-owner, the trustee claimed an entitlement to half of the net proceeds of sale, namely \$9,000.00, calculated as follows:

Sale price	\$41,000
Less "acquisition" finance	(\$12,500)
Sub-total	\$28,500
Less "business" finance	(\$10,500)
Net proceeds	\$18,000



BANKRUPT'S ESTATE \$9,000 WIFE'S SHARE \$9,000

Mrs Farrugia's figures

Mrs Farrugia claimed that the mortgage monies should, to the extent that they were applied to the benefit of the husband only, be discharged from his interest in priority to her own. If accepted, the effect of those submissions is as follows:

Sale price	\$41,000	
Less “acquisition” finance	(\$12,500)	
Sub-total	\$28,500	
	▲ ▼	
Bankrupt’s share	\$14,250	WIFE’S SHARE \$14,250
Less “business” finance	(\$10,500)	
BANKRUPT ESTATE	\$3,750	

Farrugia decision

Mrs Farrugia’s submissions found favour with Dean J, although his reasons seemed to confine the remedy to the female within the marriage context:

Where the property of a married woman is mortgaged or charged in order to raise money for the benefit of her husband, it is presumed, in the absence of evidence showing an intention to the contrary, that, as between her husband and herself, she meant to charge her property merely as surety. In such a case, she is, as between her husband and herself, in the position of surety and entitled both to be indemnified by the husband and to throw the debt primarily on his estate to the exoneration of her own³⁰.

Farrugia remedy

The remedy in that case was recognition that Mrs Farrugia had a charge upon Mr Farrugia’s interest in the land by way of indemnity to secure her right of exoneration.³¹

His Honour considered that the “charge” survived bankruptcy and encumbered the property which passed into the bankrupt estate.³²

³⁰ *Farrugia v Official Receiver* 43 ALR 700 at 702, His Honour citing with approval of the principal as it was described in Halsburys Laws of England (Fourth Edition)

³¹ *Farrugia v Official Receiver* 43 ALR 700 at 703, where His Honour also relied upon the decision in *Gee v Liddell* [1913] 2 Ch 62 at 72

³² *Farrugia v Official Receiver* 43 ALR 700 at 703, where Dean J cites with approval the decision of Riley J in *Re Thompson; Ex parte Smith* (1975) 8 ALR 475 at 477

Exoneration today

The doctrine was more recently considered by the Full Federal Court in *McBain v Parsons*³³ and by Nicholas J of the New South Wales Supreme Court in *Dickson v Reidy*.

³⁴ In circumstances quite similar to *Farrugia*, Nicholas J was asked to consider whether the doctrine of exoneration applied so that the bankrupt's interest was subject to a charge to secure the husband's right of exoneration.

Nicholas J adopted the definition of exoneration set out in *Parsons v McBain*.³⁵ That is, it arises where the circumstances of the matter cast the co-owners in the roles of principal debtor and surety (in respect of at least part of a secured debt). The essential elements are:

1. a charge is created over jointly owned property in favour of a third party creditor;
2. the charge is created in order to raise a fund which is to be applied to the benefit of one/some but not all of the co-owners;
3. the fund is so applied.

Benefits must be direct and tangible

The second requirement, that the applicant co-owner does not benefit from the fund, can be problematic. The benefit, if it is alleged, must relate to a direct and tangible benefit. It is not sufficient that the party who received the fund used it in a business to “bring home money to put food on the table and clothe the children”.³⁶ The proper enquiry is “who got the money”? (*In re Kiely* (1857) Ir Ch Rep 394)

³³ (2002) 192 ALR 772

³⁴ [2004] NSW SC 1200

³⁵ (2002) 192 ALR 772 at 779

³⁶ *Parsons v McBain*

Shortfall scenario

The doctrine does not excuse the party from liability for the creditor's claim. If the bankrupt's share is insufficient to discharge the debt then the wife's share (in the example) is exposed.

Sale price				\$30,000
Less "acquisition" finance				(\$12,500)
Sub-total				\$17,500
		↙	↘	
Bankrupt's share	\$8,750		Wife's interest	\$8,750
Less "business" finance	(\$8,750)		Less "business" finance	(\$1,750)
BANKRUPT ESTATE	NIL		WIFE'S SHARE	\$7,000

The exoneration charge

The equity of exoneration operates in the nature of a "charge upon the estate of the principal debtor by way of indemnity for the purpose of enforcing against that estate the right which [the beneficiary] has, as between [the beneficiary] and the principal debtor, to have that estate resorted to first for the payment of the debt".³⁷

The relationship between the co-owners is properly one of chargee and chargor. As a consequence, circumstances might arise which might lead to abandonment of that charge, and the loss of the right of exoneration. In *Dickson v Reidy*,³⁸ the bankruptcy trustee contended that the husband had abandoned, and therefore lost the benefit of the charge. The jointly owned property had been sold and the net proceeds distributed. The abandonment was said to have arisen by the husband's agreement to complete the sale with the sale proceeds to be distributed equally between the husband and the bankrupt estate. That submission was maintained notwithstanding the husband's indication at the time of settlement that he intended to commence separate proceedings seeking

³⁷ *Gee v Liddell* [1913] 2 Ch D 62 at 72

³⁸ [2004] NSW SC 1200

exoneration. If successful the trustee would have reduced the husband to the position of unsecured creditor. Nicholas J considered that submission of abandonment in those circumstances was without merit.

Abandonment may also occur during the proof of debt process. If a secured creditor proves for the full amount of its debt, that is *prima facie* evidence that it is giving up its security – a contention given more force if the creditor votes or receives a dividend on the strength of the proof of debt.³⁹

This evidence of intention is to be assessed on an objective basis.⁴⁰

The prudent trustee

So what advice does one give to a prudent trustee?

The High Court will hear the trustee's appeal in *Anderson v Peldan* next Tuesday. The transcript of the special leave application reveals a considerable degree of sympathy for the arguments of the appellant trustee. It seems likely that the court will overturn Kiefel's judgement and stretch our understanding of property to include a survivorship interest.

In *Cummins*, the High Court demonstrated the extent to which it is influenced by the policy behind the *Bankruptcy Act*. It has always been open to a trustee to find an underlying beneficial interest which differs in extent from the legal interest. Since *Cummins* however, in the case of matrimonial property in the bankruptcy context, it may well be that there is no difference unless the doctrine of exoneration operates to alter the extent to which that property is available to creditors.

³⁹ *Hewitt v Court* (1983) 1 ACLC 768,771 per Gibbs CJ.

⁴⁰ *Surfers Paradise Investments Pty Ltd (in liquidation) v Davoren Nominees Pty Ltd* [2003] QCA 458.