HIGH COURT OF AUSTRALIA

Gibbs C.J., Mason, Wilson, Brennan and Deane JJ.

KENNETH RUSTON HUTCHENS v. DEAUVILLE INVESTMENTS PTY LTD
16 December 1986

Decision

GIBBS C.J., MASON, WILSON, BRENNAN AND DEANE JJ.: This is an appeal by special leave from a judgment of the Full Court of the Supreme Court of Victoria affirming the decision of a single judge

dismissing an appeal to him from an order made by a Master. The appellant is Kenneth Ruston Hutchens ("Hutchens") who was the defendant in the Supreme Court in an action brought by the respondent, Deauville Investments Pty. Ltd. ("Deauville"), for possession of certain land registered under the Transfer of Land Act 1958 (Vict.). The basis of the action was alleged default by Hutchens as mortgagor under a registered mortgage of the land. By his order, the Master gave the respondent leave summarily to enter final judgment for possession of the land and thereby precluded the matter going to trial.

2. The facts are complicated and the evidence is unsatisfactory. Since, for the reasons appearing hereunder, we consider that the appeal should be upheld and that the matter should be remitted to the Supreme Court for further pleading leading to a trial in which any outstanding issues of fact may be resolved, it is desirable that we refrain from unnecessary canvassing of the incomplete evidence at present before the Court. It is, however, necessary to indicate the essential factual context within which the issues canvassed on the present appeal arise for consideration. Subject to elucidation and correction by further evidence at the trial, that factual context would appear to be as follows.

3. In July 1977, a proprietary company called The Kenbrite Corporation Pty. Ltd. ("Kenbrite"), of which Hutchens was a director, agreed to borrow money from General Credits Limited ("General Credits"). As security for the repayment of the loan and payment of interest, Kenbrite executed in favour of General Credits a first mortgage debenture ("the first mortgage debenture") containing a floating charge over its assets while Hutchens executed a deed of guarantee and indemnity whereby, among other things, he guaranteed the payment of any moneys then, or thereafter to become, owing by Kenbrite to General Credits on any account whatever. Some twelve months later, General Credits advanced further moneys to Kenbrite and, by way of further security, Hutchens executed the mortgage ("the real property mortgage") which lies at the heart of the present case. That mortgage was in favour of General Credits. It mortgaged the subject land to secure the payment to General Credits of "each and all sums of money in which (Hutchens) may now or hereafter be indebted or liable or contingently indebted or liable to the Mortgagee on any account whatever ... including ... any moneys owing under pursuant to or in connexion with" the guarantee and indemnity executed by Hutchens in July 1977. In October 1979, Kenbrite executed in favour of Helvetic Investment Corporation Pty. Ltd. ("Helvetic") a second-ranking mortgage debenture deed ("the second mortgage debenture") containing a floating charge over its assets to secure its indebtedness in respect of past and future borrowings from Helvetic.

4. By February 1982, Kenbrite was insolvent. On 5 March 1982, General Credits appointed Messrs. Hodgson and Judson as receivers and managers of the assets and business of Kenbrite under the first mortgage debenture. As at that date, according to a statement of affairs subsequently prepared on behalf of Kenbrite and verified by Hutchens as a director, Kenbrite had estimated realizable assets of approximately $1.5m., preferred creditors of approximately $0.43m. and secured liabilities of more than $3m. consisting of approximately $0.89m. owing to General Credits (under the first mortgage debenture) and approximately $2.14m. owing to Helvetic (under the second mortgage debenture). If the assets of Kenbrite were applied to discharge its liability to preferred and secured creditors in conformity with the priority of their claims to payment, the indebtedness of Kenbrite to General Credits would, on those figures, have been extinguished and Hutchens would have been under no liability under the guarantee and mortgage given by him in favour of General Credits. Alternatively, if General Credits had obtained payment of the debt owing by Kenbrite from Hutchens pursuant to the terms of his guarantee, Hutchens would, subject to an argument about the effect of cl.2 of the guarantee which we find it unnecessary to pursue, have been subrogated to General Credits' rights against Kenbrite under the first mortgage debenture and would, on those figures, have obtained full reimbursement of the amount which he had been required to pay as guarantor. In that regard, it is relevant to note that there would seem to be no suggestion that Hutchens was or is under any relevant liability otherwise than such as flows from his guarantee of moneys owed by Kenbrite to General Credits. On 12 March 1982, Helvetic appointed Mr. Dulhunty as receiver and manager of the assets and business of Kenbrite under the second mortgage debenture. By a demand dated 16 March 1982, General Credits demanded of Hutchens payment of "all sums of money which are in the definition of 'the principal sum' of the (real property) Mortgage". The demand did not specify the amount alleged to be owing by Hutchens.

5. On 6 April 1982, General Credits assigned to Helvetic, for a stated consideration of $927,580.35, the moneys owing to it by Kenbrite and "all its right title and interest in and to" the first mortgage debenture. As part of the one overall transaction, General Credits, for the same consideration but by a separate (and subsequently registered) instrument of "Transfer of Mortgage", transferred to Helvetic all its estate and interest as registered proprietor of the real property mortgage given to it by Hutchens as security for his liability as guarantor. On the same day, the receivers and managers appointed by General Credits retired and Mr. Dulhunty was appointed as receiver and manager under the first as well as the second mortgage debenture. We shall hereinafter use the phrase "the receiver" to refer to Mr. Dulhunty during the period in which he was receiver and manager under both debentures.

6. While the material presently in evidence is somewhat confusing as to precise amounts, it would seem that between April 1982 and May 1983 the receiver paid to Helvetic (or General Credits and Helvetic) more than $1m. from the proceeds of realization of Kenbrite's assets including $997,000 received in the period between 6 April and 7 October 1982. That last-mentioned amount apparently exceeded the then total liability of Kenbrite under the first mortgage debenture even accepting that, as the statement of affairs indicated, an amount of approximately $.89m. was owing under that debenture as at 5 March 1982. On the other hand, in its amended statement of claim, Deauville alleges that, between 6 April 1982 and 7 October 1983, Helvetic received only the sum of $83,554.19 in reduction of the "credit accommodation" extended by General Credits to Kenbrite (alleged to have totalled $731,093.10) "leaving a balance of $674,538.91" (sic). The wide discrepancy between competing figures is partly, but not completely, to be explained by assertions that most of the moneys paid to Helvetic by the receiver were appropriated to payment of amounts owing under the second mortgage debenture instead of to payment of amounts owing under the first and prior mortgage debenture. In the meantime, in October 1982, Helvetic executed an instrument of "Transfer of Mortgage" whereby it purported to transfer to Deauville, a company with the same managing director (Mr. Messara) as itself, "all its estate and interest" as registered proprietor of the real property mortgage. The consideration for that transfer of mortgage, which was subsequently registered in the Office of Titles, is said (in both the amended statement of claim and the instrument of transfer itself) to have been $927,580.35, that is to say, substantially more than the amount which, according to the amended statement of claim (see above) and the notice of demand which Deauville was subsequently to serve upon Hutchens (see below), was secured by it. There is no suggestion, in either the amended statement of claim or in the present evidence, that Helvetic assigned to Deauville the benefit of the debt owing by Kenbrite to it under the first mortgage debenture or the benefit of that debenture. To the contrary, it was accepted in the judgments in the Supreme Court and was common ground in argument in this Court that the benefit of neither the guaranteed debt nor the first mortgage debenture given to secure it was ever assigned to Deauville. For that matter, the present evidence suggests that there was neither a separate transfer of the benefit of the guarantee nor an express transfer of Hutchens' indebtedness by Helvetic to Deauville. If that be so, questions arise about whether the transfer of the real property mortgage by Helvetic to Deauville could, of itself, suffice to effect a transfer of Hutchens' indebtedness as guarantor which was, as has been seen, the only actual liability which it secured and whether, if it could not, Deauville is entitled as mortgagee to enforce the security of the real property mortgage given to secure the payment of a debt owing to a company other than itself. For reasons which will become apparent, however, we find it unnecessary to pursue those questions in isolation for the purposes of the present application. It suffices, for present purposes, to assume in Deauville's favour that the transfer of the mortgage given by Hutchens

to secure his liability under the guarantee purported to transfer to Deauville the benefit both of the security of the mortgage and of any indebtedness which it secured. On 17 October 1983, Deauville caused to be served upon Hutchens a notice of demand which recited, among other things, the transfer to it of the real property mortgage and went on to demand payment of $647,538.91 being the amount alleged to be owing by Kenbrite to General Credits at the time of the transfer of the mortgage to Helvetic ($731,093.10) less amounts received by Helvetic between 6 April 1982 and 7 October 1983 ($83,554.19). The notice of demand, like that previously served by General Credits, produced no payment by Hutchens.

7. In the Supreme Court, the defences which it was sought to litigate on behalf of Hutchens included an allegation that sums received by the receiver should be deemed to have been applied by him to discharge the debt owed under the first mortgage debenture. Notwithstanding the confused state of the evidence, it was not sought to raise an independent issue about whether the moneys owing by Kenbrite under the first-ranking mortgage debenture had, in any event, been in fact discharged. In the course of argument of the appeal in this Court, however, it became apparent that there exists a serious issue between the parties on that last-mentioned question of fact.

8. One would prima facie assume that the receiver would apply amounts received by him to the discharge of the liability under the first mortgage debenture (i.e. the liability of Kenbrite guaranteed by Hutchens) before applying such sums to the discharge of the amount owing under the second-ranking mortgage debenture which Kenbrite had granted in favour of Helvetic. Indeed, cl.22(b) of the second mortgage debenture required that a receiver appointed under it apply moneys received by him in payment of "liabilities having priority" before appropriating such moneys towards the payment of principal and interest owing to Helvetic under that debenture deed. The material which is presently in evidence does not dispel that prima facie assumption in a way which could properly be treated as adequate to found an order for final judgment. In particular, the material in evidence is inadequate to dispel the assumption that the amounts which were apparently received by the receiver in the period from May to October 1982 and appropriated in payments to Helvetic (or General Credits and Helvetic) would have been so appropriated in extinguishment of Kenbrite's liability under the first mortgage debenture. As has been said, it would seem that, if those moneys were so appropriated, they would have been sufficient to discharge completely the indebtedness under that debenture. If that were so, the result would be that Hutchens' liability as guarantor of that debt would necessarily have also been discharged unless Deauville could somehow assert against Hutchens some higher or different claim as assignee of the real property

mortgage to that which could have been asserted against him by either General Credits or Helvetic.

9. If the above question of fact were the only suggested issue between the parties, there would be something to be said for the argument, advanced on behalf of Deauville, that Hutchens should not be permitted to raise it for the first time in this Court. Against that argument, however, one would have to weigh a number of considerations including the unsatisfactory and incomplete state of the evidence led by Deauville about matters which should essentially lie within its own knowledge or the knowledge of its associated company (Helvetic) or the receiver (Mr. Dulhunty), the fact that further investigation of the facts upon a trial had been precluded by an order made for final judgment on the application of Deauville and the fact that Hutchens has at all times asserted that, if the moneys paid to Helvetic by the receiver were not in fact appropriated to discharge the amount owing under the first mortgage debenture, they should have been. In any event, it is apparent that the above question of fact is not the only live issue in the case. Even if that question were treated as having been resolved by default in favour of Deauville, there would remain, on the present state of the evidence, some formidable difficulties which Deauville must surmount before it would be entitled to judgment for possession of the subject land. The first, and most fundamental, of those further difficulties arises from the absence of any suggestion, in the amended statement of claim or the evidence, that there was any assignment, in law or in equity, to Deauville of the debt owing by Kenbrite to Helvetic or of the benefit of the first mortgage debenture.

10. Assuming that the notice of demand given by General Credits to Hutchens was, notwithstanding the failure to specify the amount claimed, effective to crystallize the debt secured by the real property mortgage, that debt remained owing by Hutchens in his capacity as guarantor of Kenbrite. As has been said, the only debt secured by the mortgage was that which Hutchens was liable to pay by reason of his guarantee of the indebtedness of Kenbrite. After Hutchens became bound to pay that debt as guarantor, it remained a debt owing to General Credits by Kenbrite as the principal debtor. If Kenbrite itself had paid the debt, the liability of Hutchens to pay it as guarantor would automatically have been discharged. If Hutchens had paid the debt to General Credits, he would, subject again to the argument about the effect of cl.2 of the guarantee, have been entitled to be subrogated to the rights of General Credits under the first mortgage debenture. Pending payment of the debt, Hutchens was in what Turner L.J. aptly described (Wheatley v. Bastow (1855) 7 De G. M &G 261, at p 280 (44 ER 102, at p 109)) as the "favoured debtor" position of a guarantor. As guarantor, he had rights against General Credits as creditor including a prima facie right in equity to have his liability reduced if General Credits by negligence or default allowed the benefit of his

rights of subrogation to be lost or diminished (cf. Williams v. Frayne (1937) 58 CLR 710, at p 738; Buckeridge v. Mercantile Credits Ltd. (1981) 147 CLR 654, at p 675).

11. The overall transaction involving the assignment of the principal debt and the securities, including Hutchens' guarantee and supporting mortgage, by General Credits to Helvetic raises no difficulty as a matter of general principle. The effect of it was that Helvetic was substituted for General Credits as creditor. Kenbrite remained liable as principal debtor; Hutchens remained liable as a guarantor upon whom a demand for payment had been made after default by the principal debtor (cf. Wheatley v. Bastow, at p 279 (p.109 of ER)). Where the difficulty in general principle arises is in the suggestion that the benefit of Hutchens' liability as guarantor and the real property mortgage to secure it were alone transferred to Deauville with the result that Kenbrite remained liable as principal debtor to Helvetic. As we followed the argument, it was suggested that, by such a transaction, Hutchens' liability as a guarantor could be transformed into an independent liability to a different creditor from the creditor to whom the guaranteed debt remained owing. That suggestion would seem to lie ill with the basic principle that the debt owed by a guarantor, upon default by the principal debtor, is and remains the same debt as that owing by the principal debtor. Put differently, it would seem to be simply impossible, as a matter of basic principle, to assign the benefit of a guarantee or the security for it (as distinct from the property secured) while retaining the benefit of the guaranteed debt and thereby to convert the one debt owing by both principal debtor and guarantor to the one creditor into two debts, one owing by the principal debtor to the creditor and the other owing by the guarantor to the assignee. If it were otherwise, the position would seem to be that, by assigning the benefit of a guarantee and the guarantor's security and retaining the benefit of a principal debtor's indebtedness and the principal debtor's security, a creditor could effectively divorce the guarantor's liability from that of the principal debtor and effectively deprive the guarantor of the rights which flowed from his position as such including (where available) his rights of subrogation. In that regard, the case of a purported assignment of the debt of a guarantor while retaining the benefit of the guaranteed debt is, subject to one qualification, analogous to that to which Jacobs J.A. referred in International Leasing Corp. Ltd. v. Aiken (1967) 2 NSWR 427, at p 439:

> "If the debt is assigned but the guarantee is not assigned then the right in the original creditor to recover under the guarantee must at least be suspended so long as the debt is assigned. There cannot be two persons entitled to recover the amount of the same debt, one from the principal debtor, and so long as the principal debtor was in default, another from the surety.

> Let it be assumed otherwise and suppose that the original creditor, the assignor of the principal debt, could show that it was overdue and thereupon sued the surety. Let it be assumed that the surety paid. Then, the assignee sues the principal debtor. He must be entitled to succeed unless there are some special circumstances of estoppel in the particular case, a factor which I place to one side. The assignee under an absolute assignment could not be deprived of his right to recover from the debtor because the assignor had recovered from the surety."

The qualification is that the analogy (and the legal consequences) would be less clear if, in the case of assignment of the debt but purported retention of the benefit of the guarantee (to which Jacobs J.A. referred), the assignee of the debt had rights of recourse against the original creditor in the event of default by the principal debtor.

12. It has not been argued, on behalf of Deauville, that the conceptual difficulties involved in the suggestion that the benefit of the real property mortgage and of Hutchens' indebtedness under it could be assigned independently of Kenbrite's liability as principal debtor were purely theoretical for the reason that the consideration paid by Deauville for the transfer of the mortgage should be treated as having been applied to discharge the principal debt originally owed by Kenbrite to General Credits. Nor is the factual basis for such an argument to be found in the evidence. Moreover, such an argument would encounter additional difficulties. It would involve treating the transfer of the instrument of mortgage as the equivalent of the execution of the security which it contains and the novel proposition that Hutchens' indebtedness as guarantor could survive the discharge by payment of the principal debt.

13. It may well be that the abovementioned difficulties of principle would be avoided if, on investigation of the facts at a trial, the proper inference was that there had been an equitable transfer by Helvetic to Deauville of the benefit of the principal debt and of the first mortgage debenture. Even if that were to prove to be the case or if those difficulties were otherwise to be surmounted, however, there would remain at least one further matter which Hutchens is entitled to have investigated upon a trial. If the receiver has, by arrangement between Helvetic and himself, appropriated moneys which have come to his hands as receiver to the payment of the debt owing under the second mortgage debenture in preference to the payment of moneys owing under the prior security, there would, at least prima facie, appear to be grounds for inferring, as Hutchens asserts, that Helvetic and the receiver have so acted for the purpose of enhancing Helvetic's position under the second mortgage debenture by subverting and rendering

valueless Hutchens' rights of subrogation to the benefit of the first mortgage debenture. If such an inference were found to be warranted and subject to possible intervening questions (e.g. notice, estoppel or the effect of particular contractual terms), a serious issue would arise about whether there had been active connivance of a kind which would entitle Hutchens to be discharged from his obligations as guarantor or, at the least, to have his liability under the guarantee, and hence under the mortgage, reduced by the amount which would ordinarily have been, but which was not in fact, appropriated by the receiver to the discharge of the debt owing by Kenbrite under the first mortgage security (cf., e.g., O'Day v. Commercial Bank of Australia Ltd. (1933) 50 CLR 200, at pp 223-224).

14. In what has been written above, we have endeavoured to refrain from expressing any concluded view about the correct resolution of the serious issues of fact and of law which would appear likely to arise on a final trial of the action. The reason for this is that the final issues of law can only be ascertained and resolved in the context of the relevant facts and, as has been seen, the factual material in evidence is unsatisfactory and incomplete. Indeed, as we followed the argument in this Court, it was ultimately common ground that, if the Court were of the view that there were "weighty matters" that had to be resolved, the preferable course was to refrain from attempting to resolve them at this stage but to set aside the order for final judgment and to remit the matter to the Supreme Court of Victoria so that the issues could be more precisely identified by amended and further pleadings and the facts investigated and resolved by a trial in the ordinary way. In all the circumstances of the case, it appears to us that that is clearly the course which should be adopted.

15. The appeal should be allowed and the order for final judgment should be set aside. The matter should be remitted to the Supreme Court of Victoria where Deauville should have leave generally to amend its statement of claim. The question of costs has caused us some concern since, as has been said, the question of fact which the appellant placed in the forefront of the appeal to this Court was not squarely raised until the matter reached here. Doing the best we can, we think that the proper order is that the costs of each party in the Supreme Court (including the costs of the appeal to the Full Court) and of the appeal to this Court be costs in the cause.

Orders

Appeal allowed.

Set aside the judgment and order of the Full Court of the Supreme Court of Victoria and in lieu thereof order as follows:

> Allow the appeal and set aside the order of Gobbo J. and in lieu thereof order that the appeal from Master Brett be allowed and that the order of Master Brett be set aside.

Remit the matter to the Supreme Court of Victoria to proceed in accordance with this judgment.

Order that the costs of each party in the Supreme Court (including the costs of the appeal to the Full Court of the Supreme Court) and the costs of the appeal to this Court (other than the costs of the application made on 13 December 1985 which have already been ordered to be paid by the appellant) be costs in the cause.

Cited by:

Misan v Markham Real Estate Partners (KSW) Pty Ltd [2023] NSWCA 51 (24 March 2023) (White and Mitchelmore JJA, Griffiths AJA)

> *Hutchens v Deauville Investments Pty Ltd* [1986] HCA 85; (1986) 68 ALR 367, distinguished.

Misan v Markham Real Estate Partners (KSW) Pty Ltd [2023] NSWCA 51 (24 March 2023) (White and Mitchelmore JJA, Griffiths AJA)