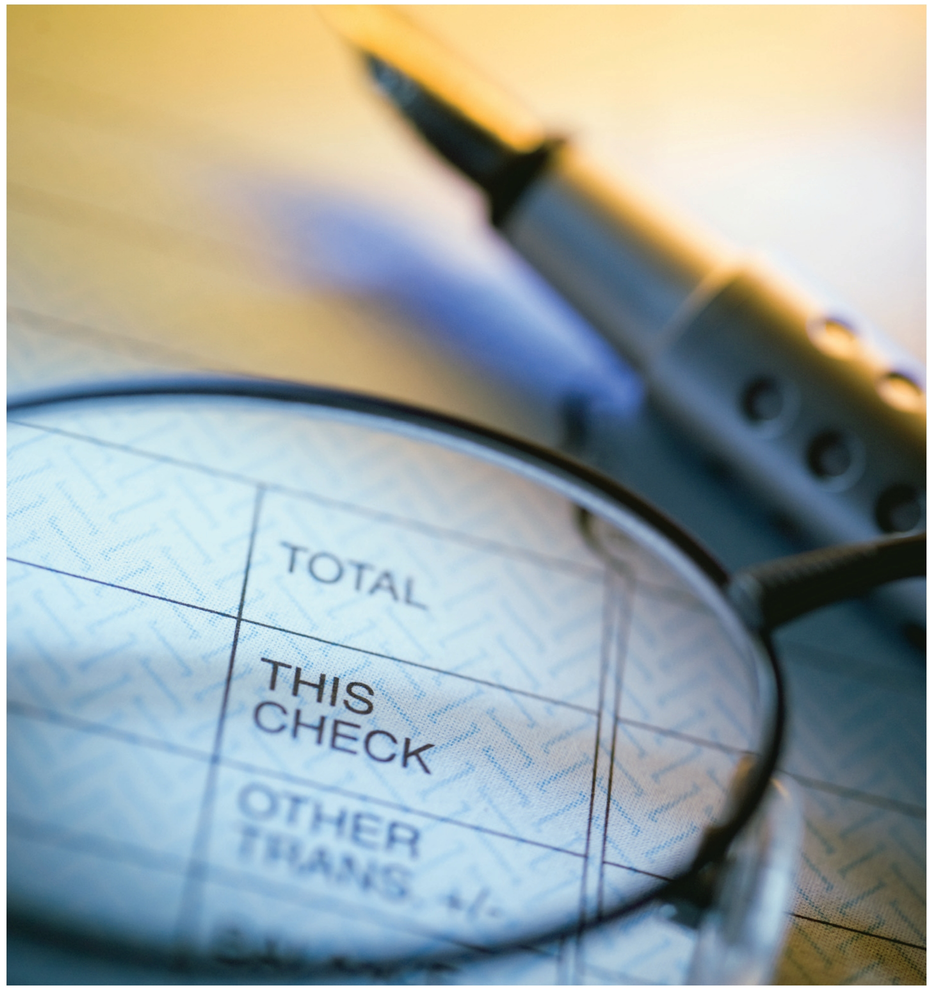
Having a bad influence

Undue influence is a difficult area to navigate, but such claims are likely to become more prevalent in the recession, says Joshua Munro



THE LAW OF undue influence is seen by many practitioners as obscure and difficult but it is likely to gain greater relevance in a worsening economic climate.

Whether it is a husband trying to secure his business debts on assets owned jointly with his wife, or an elderly person targeted by fraudsters seeking to acquire cheap property, mortgage possession claims involving undue influence defences are bound to increase.

Undue influence is a doctrine aimed at helping vulnerable people who have been persuaded to enter a property transaction which is to their detriment. Such a transaction may be set aside for undue influence where, for instance, an elderly lady is persuaded to sell her property at an undervalue to a businessman friend of a friend, or where a wife is pressurised to mortgage the family home to secure her husband's business debts.

An equitable doctrine

Undue influence is an equitable doctrine, which means that, on its face, the property transaction will be perfectly legal, but if you prove that the transaction was procured by undue influence, the court will have a discretion in equity to set aside the transaction, or grant equitable relief.

Only in exceptional circumstances would the court refuse to grant relief once undue influence is proved; for example, if the vulnerable person had later affirmed the transaction with the benefit of independent advice.

But proving undue influence can be difficult. After all, your client is likely to be vulnerable and ill-informed. That is why someone took advantage of them. Or your client may be the executor of the estate of an elderly person who gave away property, or sold it at an undervalue. Your client might not know much about why the deceased did this.

Even when you have evidence of, say, threats or coercion, by the person who influenced the transaction, that person will often contest that evidence.

The law takes into account the difficulty of proving undue influence by allowing claimants to put in evidence which will raise a presumption of undue influence. If the presumption is raised, then the defendant can only rebut the presumption if he can prove that the transaction was made with "full, free and independent" consent (see *Goodchild v Bradbury* [2006] EWCA Civ 1868).

There are two ways of proving the undue influence: either (1) you put in evidence of overt acts of improper pressure or coercion and/or (2) you put in evidence which raises a presumption that undue influence was used.

Presumption of undue influence

How do you raise a presumption of undue influence? In certain obvious circumstances, a court will readily infer that a transaction was tainted by the undue influence of one more powerful party over another, for instance in the case of a real property transaction between doctor and patient, or solicitor and client. However, in most circumstances, including husband/ wife transactions, you will have to show that: (1) there was "a relationship of trust and confidence" between the two parties; and (2) the transaction itself "called for an explanation" (see *Royal Bank of Scotland v Etridge* (No 2) [2002] 2 AC 773).

To show the "relationship of trust and confidence" you need evidence of some dependency of your client on the other party, particularly in relation to financial matters. For example, a wife may leave all the family's financial affairs to her husband. An elderly person may trust someone younger to give him financial advice. The more evidence and examples you can get of dependence and trust, the better. The more evidence you can collate of the dominance and force of the other party, the better.

To show that the "transaction called for an explanation" you should obtain as much evidence as possible that the transaction was unusual, and to the detriment of your client, and to the benefit of the other party. What documents relate to the transaction? Are they fishy? Were false details given? Who else was involved in the transaction? Are they prepared to give evidence for you? What were the terms of the transaction? Were they unusually onerous? Was the transaction risky or imprudent? The more the transaction looks like victimisation or fraud, the more likely the court will be to find that you have satisfied the test.

Beware, though, that when a wife is prepared to secure her husband's business debts by a joint remortgage of the family home, this is not normally a transaction that "calls for an explanation." This is because financing the family business is normally in the wife's interest. Something more will be needed, for instance misrepresentations by the husband as to the transaction, or some other purpose of the finance which would benefit only the husband. Alternatively, there may be evidence of actual undue influence, such as fraudulent misrepresentations, improper pressure, or threats, so that you do not need to rely on raising the presumption in the first place (see *UCB Corporate Services Ltd v Williams* [2002] EWCA Civ 555).

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What about third parties?

Once you have proved undue influence, either by direct evidence, or by raising the presumption, your client has an equity to set aside the transaction against the other party.

But what about where a third party was involved? For example, an elderly lady is persuaded by her son to gift a property to the son's business partner. Or, more commonly, a wife is persuaded to mortgage the family home so as to benefit her husband.

You will need to show that the third party had notice of the undue influence. If you have evidence that the third party actually knew about the undue influence, you are home and dry. This will be the case, for instance, where an elderly lady is duped by her son into gifting a property to the son's business partner, and the son's business partner colluded in the scheme.

Otherwise, if you can show that the third party ought to have known about the undue influence, then the claim against the third party will also succeed, because the third party will be deemed to have constructive notice of the undue influence. An important question in real property cases may be what the third party's solicitors knew or ought to have known. This is because the third party will be deemed to have the knowledge about the transaction that his solicitor ought to have had, pursuant to s.199 of the Law of Property Act 1925.

In mortgage cases, *Royal Bank of Scotland v Etridge* (No 2) provides guidance as to what steps the lender normally has to have taken, in order to avoid being fixed with constructive notice of undue influence. In cases pre-dating that decision, the lender should have obtained confirmation from a solicitor acting for the vulnerable person, to the effect that the mortgage has been properly explained to the vulnerable person. In cases post-dating that decision, the lender should obtain written confirmation from the vulnerable person's solicitor that the vulnerable person has received independent advice about the mortgage.

As a matter of policy, the courts will expect lenders to take these steps whenever there is a transaction where one party gives a guarantee or mortgage for the benefit of another, and the relationship between the two parties is non-commercial. However, even in mortgage cases, if the mortgage advance is paid jointly to the vulnerable person and the other party, the vulnerable party will still have to provide evidence that establishes constructive notice. In such cases, the vulnerable party will still have to show facts that would ring alarm bells with the lender, so as to raise the possibility that the transaction was procured by undue influence (see *CIBC Mortgages v Pitt* [1993] 3 WLR 802; *Chater v Mortgage Agency Services No 2 Ltd* [2003] EWCA Civ 490).

Summary: lenders' cases

In undue influence cases, although both the vulnerable person and the lender can be seen as 'innocent' parties, in the sense of having been exploited by the other party, the lender can often expect to have its security or guarantee struck down, unless it has taken the steps set out above. This is a policy decision of the higher courts that the lenders should bear the brunt of undue influence, unless they have taken steps to give the vulnerable party proper advice.

Even if a transaction is made under a power of attorney, it may still be struck down for undue influence. For example, in *BOS (Shared Appreciation Mortgage) v Brown* (Croydon CC, 18 July 2008) the author successfully ran a defence of undue influence against a lender where the mortgage had been made by the donee of an Enduring Power of Attorney.

Finally, in undue influence cases that go to trial, there will inevitably be cross-examination of the person alleging undue influence, often aimed at establishing that they knew perfectly well what they were doing. As always, it is important to form a view early on as to whether your client is likeable and believable. If so, such cross-examination may well backfire, and, if you have obtained the necessary evidence, the impugned transaction could be declared void.

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SJ takeaway

- Undue Influence is a doctrine which the courts can use to strike down transactions in which one party has been victimised.
- To raise an evidential presumption that a transaction was procured by undue influence, claimants should show that they were in a "relationship of trust and confidence" with the other party, and that the transaction "called for an explanation."
- If undue influence is relied on against a third party (typically a lender), the claimant will have to show that the lender had notice of the undue influence. Lenders will then be expected to have given the claimant independent legal advice, in the absence of which the claimant will be entitled to relief.