

THIRD PARTY LIABILITY FOR ‘KNOWING RECEIPT’ AND  
‘KNOWING ASSISTANCE’ POST-*GRIMALDI v CHAMELEON*  
*MINING NL (NO 2)*

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## Abstract

This paper examines the position of third party liability for ‘knowing receipt’ and ‘knowing assistance’ under *Barnes v Addy* in Australia following the decision of the Full Court of the Federal Court of Australia in *Grimaldi v Chameleon Mining NL (No 2)*. *Grimaldi* demonstrates that third party liability under *Barnes v Addy* is a primary, fault based liability concerned with the wrongdoing of the third party. There remains a technical distinction between the ‘two limbs’ of *Barnes v Addy* on the basis that a dishonest state of mind on the part of the breaching fiduciary or trustee is required to trigger liability for knowing assistance, but not for knowing receipt. Liability for both knowing receipt and knowing assistance is based on the third party’s level of knowledge relevant to the breach of trust or fiduciary duty. Knowledge falling within categories (i)-(iv) of the *Baden* scale, but not category (v) will trigger liability under both limbs. Corporate property misapplied in breach of fiduciary duty is treated as trust property for the purposes of third party liability under *Barnes v Addy* in Australia, despite recent comments of the High Court suggesting that this position may not yet be confirmed.

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## I INTRODUCTION

A person who has been knowingly concerned in a breach of trust, or who receives trust property transferred in a breach of trust, may be personally liable to the beneficiaries of the trust.<sup>1</sup> This is commonly referred to as the principle derived from *Barnes v Addy*,<sup>2</sup> although it is important to note that there are bases other than those expressed in *Barnes v Addy* under which a third party may become liable because of their involvement in a breach of trust.<sup>3</sup>

In *The Bell Group Ltd (in liq) v Westpac Banking Corporation (No 9)*,<sup>4</sup> Owen J noted that the jurisprudence surrounding the *Barnes v Addy* principle is disparate and complex,<sup>5</sup> and declined to attempt the ‘architectonic task’ of resolving all of the related difficulties and debates.<sup>6</sup>

While the unanimous decision of the High Court in *Farah Constructions Pty Ltd v Say-Dee Pty Ltd*<sup>7</sup> resolved some of the difficulty surrounding the modern-day application of *Barnes v Addy*, some contentious issues remain.<sup>8</sup> Not long after the decision in *Farah*, Owen J considered a number of these issues in *Bell Group*. Justice Owen’s decision provides a substantial and valuable analysis of the state of the law surrounding *Barnes v Addy* up to, and including the decision in *Farah*.<sup>9</sup> More recently, the Full Court of the Federal Court of Australia considered the *Barnes v Addy* principles in *Grimaldi v Chameleon Mining NL (ACN 098 773 785) (No 2) and Another*,<sup>10</sup> hence providing the highest authority on the issue since *Farah*.

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<sup>1</sup> *Bell Group Ltd (in liq) v Westpac Banking Corp (No 9)* (2008) 39 WAR 1 at [4627].

<sup>2</sup> (1874) 9 Ch App 244.

<sup>3</sup> *Bell Group Ltd (in liq) v Westpac Banking Corp (No 9)* (2008) 39 WAR 1 at [4627].

<sup>4</sup> (2008) 39 WAR 1 (‘*Bell Group*’).

<sup>5</sup> *Bell Group* (2008) 39 WAR 1 at [4629].

<sup>6</sup> *Bell Group* (2008) 39 WAR 1 at [4629].

<sup>7</sup> (2007) 230 CLR 89 (‘*Farah*’).

<sup>8</sup> *Bell Group* (2008) 39 WAR 1 at [4630].

<sup>9</sup> See *Bell Group* (2008) 39 WAR 1 at [4627]-[4804].

<sup>10</sup> (2012) 287 ALR 22 (‘*Grimaldi*’).



This paper examines the Full Court position in *Grimaldi* in the context of the wider debate surrounding third party *Barnes v Addy* liability and draws some conclusions as to the current position of such liability in Australia following the *Grimaldi* decision. It commences with an overview of the principles and uncertainties associated with *Barnes v Addy* liability, before considering the justifications for imposing a personal liability on third party participants in breaches of fiduciary duty, which act as a driver for the remedies that may be appropriate. Finally, it considers the Full Court's approach to third party liability and the application of the *Barnes v Addy* principles in *Grimaldi*.

While the decision in *Grimaldi* is important in relation to other aspects of corporations law, in particular the situations in which a person may be considered a de facto director of a corporation under the *Corporations Act 2001* (Cth)<sup>11</sup> and the liability of fiduciaries who receive bribes and secret commissions in breach of duty,<sup>12</sup> this discussion is concerned solely with the aspects of the *Grimaldi* decision relevant to the liability of third party participants in breaches of fiduciary duty.

## II THIRD PARTY LIABILITY UNDER BARNES v ADDY

### *A Barnes v Addy*

*Barnes v Addy* was concerned with trustees of a trust fund who entered into a transaction in breach of trust and subsequently lost trust money. The beneficiaries of the trust sought to recover their losses from both the surviving trustee and the solicitors who had advised in relation to the transaction. The issue in the case was whether strangers to the trust could be held personally responsible for a breach of trust by the trustees. The claim against the solicitors failed as they were found to have no knowledge of, nor any reason

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<sup>11</sup> See *Grimaldi* (2012) 287 ALR 22 at [28]-[143].

<sup>12</sup> See *Grimaldi* (2012) 287 ALR 22 at [188]-[193], [569]-[584].

to suspect, that the relevant transaction involved a dishonest design on the part of the trustees.<sup>13</sup>

In a famous passage from *Barnes v Addy*, Lord Selborne stated that:

Those who create a trust clothe the trustee with a legal power and control over the trust property, imposing on him a corresponding responsibility. That responsibility may no doubt be extended in equity to others who are not properly trustees, if they are found either making themselves trustees de son tort, or actually participating in any fraudulent conduct of the trustee to the injury of the cestui que trust. But, on the other hand, strangers are not to be made constructive trustees merely because they act as the agents of trustees in transactions within their legal powers, transactions perhaps of which a Court of Equity may disapprove, unless those agents receive and become chargeable with some part of the trust property, or unless they assist with knowledge in a dishonest and fraudulent design on the part of the trustees.<sup>14</sup>

While not immune to criticism,<sup>15</sup> Lord Selborne's formula is accepted in Australian law.<sup>16</sup>

It is common to refer to Lord Selborne's statement as containing 'two limbs',<sup>17</sup> from here on described as 'knowing receipt' and 'knowing assistance'. A knowing recipient is someone who receives and becomes chargeable with some part of the trust property as a result of his or her knowledge of the relevant breach of trust.<sup>18</sup> A knowing assistant is someone who acts as an accessory to the relevant breach of trust.<sup>19</sup> Various alternative phrases such as 'knowing participation', 'accessory liability', 'dishonest receipt' and 'dishonest assistance' have also been used in relation to either or both limbs in cases and commentary,<sup>20</sup> further adding to the confusion in the *Barnes v Addy* debate.

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<sup>13</sup> See *Bell Group* (2008) 39 WAR 1 at [4632].

<sup>14</sup> *Barnes v Addy* (1874) 9 Ch App 244 at 251-252.

<sup>15</sup> *Bell Group* (2008) 39 WAR 1 at [4636].

<sup>16</sup> *Farah* (2007) 230 CLR 89; *Bell Group* (2008) 39 WAR 1 at [4640].

<sup>17</sup> *Bell Group* (2008) 39 WAR 1 at [4634].

<sup>18</sup> *Bell Group* (2008) 39 WAR 1 at [4634].

<sup>19</sup> *Bell Group* (2008) 39 WAR 1 at [4634].

<sup>20</sup> *Bell Group* (2008) 39 WAR 1 at [3634]; Joachim Dietrich and Pauline Ridge, 'The Receipt of What?: Questions Concerning Third Party Recipient Liability in Equity and Unjust Enrichment' (2007) 31 *Melbourne University Law Review* 47; Pauline Ridge, 'Justifying the Remedies for Dishonest Assistance' (2008) 124 *Law Quarterly Review* 445.

## B *The Distinction Between the Two Limbs*

Debate abounds as to whether the two limbs of *Barnes v Addy* are distinct and separate liabilities, or merely ‘two different species of a single genus of liabilities’.<sup>21</sup>

In *Consul Development Pty Ltd v DPC Estates Pty Ltd*,<sup>22</sup> Stephen J determined that a distinction between the two limbs existed, with constructive knowledge sufficing for liability under the knowing receipt limb, but actual knowledge required for knowing assistance liability.<sup>23</sup> Despite this, Stephen J was unclear on *why* such a distinction existed, speculating that the basis of the distinction was perhaps a property protection rationale:

[P]erhaps its origin lies in equitable doctrines of tracing, perhaps in equity’s concern for the protection of equitable estates and interests in property which comes into the hands of purchasers for value.<sup>24</sup>

Denis Ong notes that Gibbs J took a contrary position in *Consul Development* in considering that third parties may be liable for knowing assistance where the assistance rendered is solely the knowing receipt of trust property.<sup>25</sup> Gibbs J referred to persons who ‘assist with knowledge in a dishonest and fraudulent design on the part of the trustees’ as including persons who ‘received trust property’ and ‘dealt with it in a manner inconsistent with trusts of which [they were] cognizant’.<sup>26</sup> His Honour also considered that liability for knowing assistance could arise ‘even though’ (rather than ‘only if’) the third party had not received trust property.<sup>27</sup>

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<sup>21</sup> *Grimaldi* (2012) 287 ALR 22 at [257].

<sup>22</sup> (1975) 132 CLR 373 (*‘Consul Development’*).

<sup>23</sup> *Consul Development* (1975) 132 CLR 373 at 410 (Stephen J).

<sup>24</sup> *Consul Development* (1975) 132 CLR 373 at 410 (Stephen J); Denis Ong, ‘The Knowledge or Role that Makes a Person an Accessory Under the *Barnes v Addy* Principle’ (2005) 17(2) *Bond Law Review* 102, 119.

<sup>25</sup> Ong, above n 24, 117.

<sup>26</sup> *Ibid*, 117; *Consul Development* (1975) 287 ALR 22 at 396-397 (Gibbs J).

<sup>27</sup> *Consul Development* (1975) 132 CLR 373 at 397 (Gibbs J).

Of the two other justices determining *Consul Development*, Barwick CJ concurred with the view of Stephen J,<sup>28</sup> and McTiernan J, while not expressly disavowing the existence of two limbs, referred broadly to liability attaching to third parties who ‘participate in’<sup>29</sup> or ‘encourage’<sup>30</sup> breaches of fiduciary duty. Ong argues that the judgment of McTiernan J demonstrates that his Honour considered there to be no distinction between the two limbs of *Barnes v Addy*.<sup>31</sup> While it is difficult to argue that McTiernan J’s judgment demonstrates this view conclusively, it is submitted that Ong’s interpretation is correct. *Consul Development* was a case concerned with knowing receipt; his Honour’s use of language (with participation and encouragement arguably more suggestive of assistance than receipt), coupled with a failure to acknowledge any distinction between knowing receipt and knowing assistance in his discussion, suggest that his Honour considered knowing receipt to be a type of knowing assistance, as versus a distinct and separate liability.

Ong notes that the distinction between the two limbs of *Barnes v Addy* is not one of ‘ancient lineage’.<sup>32</sup> A distinction was first drawn between the limbs in 1971 by Brightman J in the English decision of *Karak Rubber Co Ltd v Burden*,<sup>33</sup> some ninety-seven years after Lord Selborne’s judgment in *Barnes v Addy*.<sup>34</sup> While Brightman J noted the distinction between the limbs, he considered that the level of knowledge required for knowing receipt and knowing assistance was the same for both limbs.<sup>35</sup> Ong notes that it was not until 1973, in the first instance decision of Jacobs P in *Consul Development*, that a distinction was drawn between the knowledge requirements of the two limbs:<sup>36</sup>

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<sup>28</sup> *Consul Development* (1975) 132 CLR 373.

<sup>29</sup> *Consul Development* (1975) 132 CLR 373 at 378 (McTiernan J).

<sup>30</sup> *Consul Development* (1975) 132 CLR 373 at 386 (McTiernan J).

<sup>31</sup> Ong, above n 24, 118.

<sup>32</sup> *Ibid*, 119.

<sup>33</sup> [1972] 1 WLR 602 (‘*Karak*’).

<sup>34</sup> Ong, above n 24, 119.

<sup>35</sup> *Ibid*, 119.

<sup>36</sup> *Ibid*, 119.

[t]he point of the difference between the person receiving trust property and the person who is made liable, even though he is not actually a recipient of trust property, is that in the first place, knowledge, actual or constructive of the trust is sufficient, but in the second place something more is required, and that something more appears to me to be the actual knowledge of the fraudulent or dishonest design, so that the person concerned can truly be described as a participant in that fraudulent dishonest activity.<sup>37</sup>

Stephen J, with whom Barwick CJ agreed, upheld Jacob P's conclusion on appeal.<sup>38</sup>

Ong attacks Jacob P's formulation on several grounds. Firstly, he notes that Jacobs P's conclusion that the defendant must have actual knowledge of the dishonest and fraudulent design is inconsistent with Lord Selborne's position in *Barnes v Addy*, which considered that the defendant's knowledge *or suspicion* would be sufficient to give rise to participant liability.<sup>39</sup> Ong also considers that Lord Selborne made it clear that the sole criterion for *all* classes of agents to whom the liability may attach was fraud and dishonesty, when he stated that:

[T]hose who create trusts do expressly intend, *in the absence of fraud and dishonesty*, to exonerate such agents of *all classes* from the responsibilities which are expressly incumbent... upon the trustees.<sup>40</sup>

Secondly, Ong attacks Jacob P's reliance on the English Court of Appeal decision in *Carl Zeiss Stiftung v Herbert Smith (No 2)*<sup>41</sup> as authority for the conclusion that a greater level of knowledge is required for knowing assistance.<sup>42</sup> Ong notes that *Carl Zeiss Stiftung* did not distinguish between knowing assistance and knowing receipt, and was decided three years prior to such a distinction first being made in *Karak*.<sup>43</sup> While Jacobs P relied on Edmund Davies LJ's comments in *Carl Zeiss Stiftung* as support for the conclusion that a want of probity is necessary for liability as a constructive trustee to

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<sup>37</sup> *DPC Estates Pty Ltd v Grey & Consul Development Pty Ltd* [1974] 1 NSWLR 443 at 459 (Jacobs P).

<sup>38</sup> *Consul Development* (1975) 132 CLR 373 at 410 (Stephen J).

<sup>39</sup> Ong, above n 24, 120.

<sup>40</sup> *Barnes v Addy* (1874) 9 Ch App 244 at 252 (emphasis added); Ong, above n 24, 121.

<sup>41</sup> [1969] 2 Ch 276 ('*Carl Zeiss Stiftung*').

<sup>42</sup> Ong, above n 24, 120.

<sup>43</sup> *Ibid*, 120.

arise where there has been no receipt of trust property,<sup>44</sup> Edmunds LJ in fact considered a want of probity necessary to give rise to liability as a constructive trustee *however created* (that is, regardless of whether or not trust property had been received in relation to the breach).<sup>45</sup> Ong considers that this is consistent with Lord Selborne's position in *Barnes v Addy* that dishonesty is the sole criterion required to give rise to all classes of liability.<sup>46</sup>

Ong questions whether it is even conceptually possible to knowingly receive trust property in breach of trust without also assisting in that breach of trust.<sup>47</sup> Where someone receives property knowingly in breach of trust, Ong considers that they have unavoidably assisted with the breach of trust, as the breach itself is reliant on the transfer of property.<sup>48</sup> In such circumstances, the recipient of the trust property is liable not for knowing receipt, but instead for knowing assistance, with the receipt of the trust property merely the means by which they assisted the breach.<sup>49</sup> Ong considers that a similar situation occurs even where the assistant does not receive the property themselves, but instead persuades the trustee to transfer property to a third party in breach of trust. If this third party has sufficient knowledge of the breach to be charged with knowing receipt, they must also unavoidably have assisted with the breach of trust.<sup>50</sup> Why, Ong postulates, should the level of knowledge required to charge the non-recipient assistant with assistance liability be higher than that required to charge the recipient assistant with recipient liability, where the breach is essentially the same breach?<sup>51</sup>

Likewise, Dietrich and Ridge consider that the proper view is one of no true distinction between knowing assistance and knowing receipt. In their view, recipient liability is subsumed within an equitable regime of participatory liability (by receipt of trust

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<sup>44</sup> *Ibid*, 120.

<sup>45</sup> *Ibid*, 120; *Carl Zeiss Stiftung* [1969] 2 Ch 276 at 302 (Edmund Davies LJ) (emphasis added).

<sup>46</sup> Ong, above n 24, 121.

<sup>47</sup> *Ibid*, 121.

<sup>48</sup> *Ibid*, 121.

<sup>49</sup> *Ibid*, 121.

<sup>50</sup> *Ibid*, 122.

<sup>51</sup> *Ibid*, 122.

property or otherwise) in a breach of trust or fiduciary duty.<sup>52</sup> Recipient liability therefore should be viewed as a subset of, rather than distinct from, knowing assistance liability.<sup>53</sup> The basis for this is the justification for the recipient liability, which Dietrich and Ridge consider to be a fault based liability concerned with the wrongdoing of the recipient.<sup>54</sup> As liability for knowing assistance is also fault based, there is no real need to distinguish between the two limbs of *Barnes v Addy*; both are essentially liability rules focused on participation in wrongs.<sup>55</sup>

Following the High Court's decision in *Farah*,<sup>56</sup> Owen J determined in *Bell Group* that there must be a certain level of dishonesty on the part of the breaching fiduciary in order to give rise to *Barnes v Addy* liability on the part of a third party assistant to the breach. His Honour's considered that the conduct of the fiduciary must be attended by circumstances that would attract a 'degree of opprobrium' raising it above the level of a simple breach of trust or duty.<sup>57</sup> Conversely, there appears to be no need for dishonesty on the part of a knowing recipient.<sup>58</sup> His Honour considered there to be a distinction between the two limbs of *Barnes v Addy* on the basis of this dishonesty distinction:

One significant difference between the two limbs is that a stranger can only be liable for knowing receipt if property has come into his or her hands; while a knowing assistance case does not necessarily involve a transfer of property to the stranger, who might, accordingly, be called to account even though she or he has not enjoyed a personal benefit. This distinction may explain why knowing assistance requires malappropriation on the part of the fiduciary whereas misapplication might suffice in the case of knowing receipt.<sup>59</sup>

Owen J's conclusions contrast with Ong's view of Lord Selborne's single genus of liability and highlight the current difficulty inherent in a one-limb analysis of *Barnes v Addy* liability. If, as Ong suggests, knowing receipt necessarily involves knowing

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<sup>52</sup> Dietrich and Ridge, above n 20, 60.

<sup>53</sup> *Ibid*, 60.

<sup>54</sup> *Ibid*, 51.

<sup>55</sup> *Ibid*, 51.

<sup>56</sup> See *Farah* (2007) 230 CLR 89 at [161]-[163].

<sup>57</sup> *Bell Group* (2008) 39 WAR 1 at [4727].

<sup>58</sup> *Bell Group* (2008) 39 WAR 1 at [4734].

<sup>59</sup> *Bell Group* (2008) 39 WAR 1 at [4737].

assistance, then it follows that, in a case of knowing assistance where the sole assistance rendered is the receipt of trust property, it is both necessary and unnecessary for the fiduciary to act dishonestly. To resolve this paradox, it is submitted that one of the following must be true:

- a) ‘a degree of opprobrium’ is required on the part of the fiduciary in cases of knowing receipt; this seems unlikely following the failure of the High Court in *Farah* to address this as an element of knowing receipt; or
- b) contrary to the conclusion of Owen J in *Bell Group*, no element of dishonesty is necessary on the part breaching fiduciary, and the phrase ‘dishonest and fraudulent design’ is interpreted in the broadest sense to apply to all breaches of fiduciary duty; this formulation is, however, at odds with the inferences drawn by Owen J in *Bell Group* in relation to the High Court’s reasoning in *Farah*;<sup>60</sup> or
- c) the two limbs of *Barnes v Addy* remain distinct and separate liabilities.

Due to the difficulties noted with (a) and (b), it is submitted that conclusion (c) is the most likely position.

A distinction between the two limbs of *Barnes v Addy* only becomes relevant insofar as it gives rise to different liabilities for knowing receipt versus knowing assistance. As Ridge argues, the justifications for the liability, in many cases, suggest the remedies available.<sup>61</sup> If it is accepted that liability under both limbs of *Barnes v Addy* is a primary, fault based liability,<sup>62</sup> any remedy in relation to knowing receipt is based on the third party’s wrongdoing in receiving property where it has knowledge that the property has been derived from a breach of trust; any remedy in relation to knowing receipt is based on the third party’s wrongdoing in assisting a dishonest and fraudulent design on the part of the fiduciary. While knowing assistance liability is dependent on the presence of some degree of dishonesty on the part of the breaching fiduciary, arguably, once this

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<sup>60</sup> See *Bell Group* (2008) 39 WAR 1 at [4727]-[4728].

<sup>61</sup> Ridge, above n 20, 446.

<sup>62</sup> The nature of third party liability is discussed further below at page 26, *Justifying Third Party Liability*.



dishonesty is present and third party liability arises, the dishonesty of the breaching fiduciary has no bearing on the question of the appropriate remedy in the circumstances.

Additionally, as Owen J notes in *Bell Group*, there are bases other than those expressed in *Barnes v Addy* upon which a third party may become personally liable for involvement in a breach of trust or fiduciary duty.<sup>63</sup> This avoids the unsatisfactory outcome of a third party who commits an equitable wrong escaping liability for their wrongdoing on a technicality; that is, simply because there has been no dishonesty on the part of the breaching trustee or fiduciary.

The High Court in *Farah* maintained the position that a distinction could be drawn between the two limbs without addressing the debate surrounding the accuracy of this conclusion.<sup>64</sup> As a result, while debate continues as to whether the two limbs *should* be considered distinct, the current position in Australian law is that the distinction between the two limbs remains.

### *C The Extension of Barnes v Addy to Other Relationships*

While Lord Selborne used the word ‘agent’ in *Barnes v Addy*, liability under *Barnes v Addy* is not confined to agents in the strict sense and can extend to third parties who deal with trustees on their own behalf rather than as agents.<sup>65</sup> Knowing assistance liability has also been extended to those who assist in breaches of fiduciary duty by fiduciaries other than trustees.<sup>66</sup> The position is less certain in relation to knowing receipt liability where the property received is derived from a breach of fiduciary duty.<sup>67</sup>

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<sup>63</sup> *Bell Group* (2008) 39 WAR 1 at [4627].

<sup>64</sup> *Farah* (2007) 230 CLR 89 at [112]-[113].

<sup>65</sup> *Bell Group* (2008) 39 WAR 1 at [4641]; *Montagu’s Settlement Trusts, Re* [1987] Ch 264.

<sup>66</sup> *Farah* (2007) 230 CLR 89 at [179]; *Consul Development* (1975) 132 CLR 373; *Bell Group* (2008) 39 WAR 1 at [4641].

<sup>67</sup> *Bell Group* (2008) 39 WAR 1 at [4635], [4711].

The traditional formulation of Lord Selborne in relation to knowing receipt requires the receipt of ‘trust property’.<sup>68</sup> It is unclear whether company property, which by nature is not trust property in the strict sense, can be treated as ‘trust property’ for the purposes of *Barnes v Addy* in circumstances where a third party receives such property with knowledge of a breach of fiduciary duty.

As noted in *Bell Group*, trust property is unique in that it involves the recognition of two distinct property interests not present in the case of property owned by a company in its own right.<sup>69</sup> These two interests are the legal interest, vested in the trustee, and the beneficial interest, owned by the beneficiary, which itself is a form of proprietary interest capable of assignment.<sup>70</sup> A company differs from a trust in that a company has its own legal personality, and is therefore the absolute owner of its own property.<sup>71</sup> No person other than the company has any beneficial interest in company property, including a company director, who possesses neither a legal nor a beneficial interest.<sup>72</sup>

In *Bell Group*, it was contended that, in order for a third party to be liable for knowing receipt in relation to a breach of trust in the strict sense, the third party must be aware that they are dealing with a trustee, and therefore must also be taken to be on notice that the trustee is not the absolute owner of the trust property concerned.<sup>73</sup> It was argued that, as a recipient of company property is, by analogy, taken to know that the company is the absolute owner of its own property, the application of the same principle applied to knowing receipt of trust property in the strict sense to ‘bargains negotiated at arm’s length between major corporate entities’ is specious.<sup>74</sup>

Owen J rejected this contention on the basis that the weight of authority suggested that ‘trust property’ in a *Barnes v Addy* sense has a broader meaning than that of trust

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<sup>68</sup> *Bell Group* (2008) 39 WAR 1 at [4711].

<sup>69</sup> *Bell Group* (2008) 39 WAR 1 at [4751].

<sup>70</sup> *Bell Group* (2008) 39 WAR 1 at [4751].

<sup>71</sup> *Bell Group* (2008) 39 WAR 1 at [4752].

<sup>72</sup> *Bell Group* (2008) 39 WAR 1 at [4752].

<sup>73</sup> *Bell Group* (2008) 39 WAR 1 at [4753].

<sup>74</sup> *Bell Group* (2008) 39 WAR 1 at [4753].

property in the strict sense.<sup>75</sup> In particular, his Honour noted the decision in *Belmont Finance Corporation Ltd v Williams Furniture Ltd (No 2)*,<sup>76</sup> where the English Court of Appeal considered the liability of third parties who received corporate property misapplied in a breach of fiduciary duty.<sup>77</sup>

If a stranger to a trust (a) receives and become chargeable with some part of the trust fund or (b) assists the trustees of a trust with knowledge of the facts in a dishonest design on the part of the trustees to misapply some part of a trust fund, he is liable as a constructive trustee.

A limited company is of course not a trustee of its own fund: it is their beneficial owner; but in consequence of the fiduciary character of their duties the directors of a limited company are treated as if they were trustees of those funds of the company which are in their hands or under their control, and if they misapply them they commit a breach of trust (citation omitted). So, if the directors of a company in breach of their fiduciary duties misapply the funds of their company so that they come into the hands of some stranger to the trust who receives them with knowledge (actual or constructive) of the breach, he cannot conscientiously retain those funds against the company unless he has some better equity. He becomes a constructive trustee for the company of the misapplied funds.<sup>78</sup>

The *Belmont Finance* characterisation of corporate funds as trust property was applied by the Federal Court of Australia in *Beach Petroleum NL v Johnson*,<sup>79</sup> when von Doussa J rejected an argument that no constructive trust arose in relation to money received in breach of fiduciary duty because the money in question was not strictly trust money.<sup>80</sup> Owen J in *Bell Group* recognised *Beach Petroleum* and other Australian authorities that have applied *Belmont Finance*, noting in particular the comments of Anderson J in *Hancock Family Memorial Foundation Ltd v Porteous*<sup>81</sup> (which were upheld by the Full Court of the Supreme Court of Western Australia on appeal):<sup>82</sup>

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<sup>75</sup> *Bell Group* (2008) 39 WAR 1 at [4754].

<sup>76</sup> [1980] 1 All ER 393 ('*Belmont Finance*').

<sup>77</sup> *Belmont Finance* [1980] 1 All ER 393.

<sup>78</sup> *Belmont Finance* [1980] 1 All ER 393 at 405.

<sup>79</sup> (1993) 43 FCR 1 ('*Beach Petroleum*') at 50.

<sup>80</sup> Hugh Atkin, 'Knowing Receipt Following *Farah Constructions Pty Ltd v Say-Dee Pty Ltd*' (2007) 29(4) *Sydney Law Review* 713, 723.

<sup>81</sup> (1999) 151 FLR 191 ('*Hancock Family Memorial Foundation*').

<sup>82</sup> *Hancock Family Memorial Foundation Ltd v Porteous* (2000) 22 WAR 198 ('*Hancock*').

For the purposes of a general statement of the relevant principles, I take as the starting point to be that the directors of a company should be regarded as holding on trust any property or money of the company under their control. A director who misapplies the money or property of a company by causing the assets to be used for purposes which are not the purposes of the company acts in breach of trust. (References omitted).<sup>83</sup>

Owen J also noted the decision of the New South Wales Court of Appeal in *Robins v Incentive Dynamics*,<sup>84</sup> where Mason P, referring to the passage cited above from *Belmont Finance*, stated that:

[t]hese passages show how the *Barnes v Addy* principle can be applied to money which is not trust money in the strict sense at the time of its misapplication by directors acting in breach of their duties.<sup>85</sup>

However, as Atkin notes, the High Court cautioned against such confident acceptance of the *Belmont Finance* position in Australia in *Farah* when it stated that:<sup>86</sup>

‘[i]n recent times it has been assumed, but rarely if at all decided, that the first limb [of *Barnes v Addy*] applies not only to persons dealing with trustees, but also to persons dealing with at least some other types of fiduciary.

The High Court was not required to determine the correctness of this assumption in *Farah*, instead leaving the question open for further consideration at a later date.<sup>87</sup> Atkin notes that, rather than suggesting that the *Belmont Finance* approach to corporate property is incorrect, the High Court may have merely been cautioning lower courts against adopting a blanket assumption in relation to a question of law on which there is no clear authority.<sup>88</sup> This interpretation of the High Court’s intention is consistent with

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<sup>83</sup> *Hancock Family Memorial Foundation* (1999) 151 FLR 191 at [72]; *Bell Group* (2008) 39 WAR 1 at [4765].

<sup>84</sup> (2003) 175 FLR 286 (*‘Robins’*).

<sup>85</sup> *Robins* (2003) 175 FLR 286 at [64]; *Bell Group* (2008) 39 WAR 22 at [4771].

<sup>86</sup> *Farah* (2007) 230 CLR 89 at [113].

<sup>87</sup> *Farah* (2007) 230 CLR 89 at [113].

<sup>88</sup> Atkin, above n 80, 724.

its scathing indictment of the NSW Court of Appeal's approach to the first instance *Farah* decision.<sup>89</sup>

Owen J in *Bell Group* noted that approach of the High Court in *Farah* to the question of whether liability under the first limb of *Barnes v Addy* extended to breaches of fiduciary duty generally was contradictory.<sup>90</sup> On the one hand, the court questioned whether 'fiduciary obligations' attached to property received in considering whether the recipient may be charged with recipient liability, suggesting a broader formulation of the *Barnes v Addy* principle that could conceivably apply to company property.<sup>91</sup> On the other hand, Owen J considered that the court reverted to a 'more traditional formulation' (that is, a concept of trust property in the strict sense) when it found that the same property was not 'trust property' nor the traceable proceeds of 'trust property' necessary to the liability.<sup>92</sup>

In *Bell Group*, Owen J considered that the previous authority accepted *Belmont Finance* in Australian law and refused to depart from these decisions as a matter of comity in the absence of a concrete High Court decision.<sup>93</sup> His Honour therefore concluded that the first limb of *Barnes v Addy* extends beyond trust property in the strict sense to include property to which fiduciary duty attaches.<sup>94</sup>

Owen J suggested two potential bases as to how the extension of *Barnes v Addy* to corporate property misapplied in breach of fiduciary duty may be justified. The first concerned the analogy that may be drawn between the position of control that a trustee holds over trust property (in the strict sense) in relation to a beneficiary and the control that a company director holds over company property; a director who misapplies the property of a company for purposes that are not the purposes of the company may

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<sup>89</sup> *Ibid*, 724.

<sup>90</sup> *Bell Group* (2008) 39 WAR 1 at [4711].

<sup>91</sup> *Bell Group* (2008) 39 WAR 1 at [4711].

<sup>92</sup> *Bell Group* (2008) 39 WAR 1 at [4711].

<sup>93</sup> *Bell Group* (2008) 39 WAR 1 at [4772]-[4773].

<sup>94</sup> *Bell Group* (2008) 39 WAR 1 at [4776].

therefore be said to be acting in breach of ‘trust’.<sup>95</sup> The second was concerned with the disposal of property to which fiduciary obligations attach; if the property is transferred to a third party in breach of these obligations, it may be considered ‘trust property’ within the extended meaning of the phrase.<sup>96</sup> Importantly, Owen J considers that the outcome (that is, the liability of the third party who receives the property with knowledge) remains unchanged under either basis.<sup>97</sup>

#### D *The Required Level of Knowledge*

Debates have also raged as to what level and type of knowledge is required of a third party to give rise to liability under *Barnes v Addy*.<sup>98</sup> Dietrich and Ridge note that the early authorities on *Barnes v Addy* liability were concerned with the ‘cognisance’ of the third party in relation to the breach of trust.<sup>99</sup> In determining what level of cognisance would suffice to give rise to a liability on the part of a third party, the equitable rules of notice, encompassing actual, constructive and imputed notice, were adopted in the second half of the 20<sup>th</sup> century.<sup>100</sup>

In *Consul Development*, the High Court considered that the knowledge requirement necessary to give rise to *Barnes v Addy* liability was centred on the court ascertaining the facts known to the third party about the trustee or fiduciary’s breach of duty.<sup>101</sup> The debate in *Consul Development* centred on whether actual knowledge by the third party was necessary to give rise to liability, or whether constructive knowledge would suffice. Gibbs J considered that *Barnes v Addy* liability would be established where a person receiving trust property knew of the relevant breach of trust, or an honest and reasonable person with the same knowledge of the facts would have known of the breach.<sup>102</sup>

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<sup>95</sup> *Bell Group* (2008) 39 WAR 1 at [4777].

<sup>96</sup> *Bell Group* (2008) 39 WAR 1 at [4778].

<sup>97</sup> *Bell Group* (2008) 39 WAR 1 at [4779].

<sup>98</sup> *Bell Group* (2008) 39 WAR 1 at [4635].

<sup>99</sup> Dietrich and Ridge, above n 20, 57.

<sup>100</sup> *Ibid*, 57; *Selangor United Rubber Estates Ltd v Craddock (No 3)* [1968] 2 All ER 1073; *Consul Development* (1975) 132 CLR 373.

<sup>101</sup> Dietrich and Ridge, above n 20, 57.

<sup>102</sup> *Bell Group* (2008) 39 WAR 1 at [4659].

Stephen J (with whom Barwick CJ agreed) considered that the knowledge of the third party had to relate specifically to a breach of fiduciary duty; it was not enough for the third party to merely have a sense of wrongdoing unrelated to an awareness of a possible breach of duty.<sup>103</sup> Importantly, his Honour concluded that constructive notice of a breach of duty was insufficient to give rise to *Barnes v Addy* liability for knowing receipt.<sup>104</sup>

Actual and constructive notice in relation to *Barnes v Addy* liability were reorganised in 1992 by Peter Gibson J in *Baden v Societe Generale pour Favoriser le Developpement du Commerce et de L'Industrie en Grance SA*<sup>105</sup> into five further categories of knowledge (known colloquially as the *Baden* scale):<sup>106</sup>

- (i) actual knowledge;
- (ii) wilful shutting of the eyes to the obvious;
- (iii) wilful and reckless failure to make inquiries that an honest and reasonable person would make;
- (iv) knowledge of circumstances that would indicate the facts to an honest and reasonable person; and
- (v) constructive notice.

In England, the *Baden* scale was later rejected as the basis on which liability for third party participation in breaches of trust should be determined, first in *Royal Brunei Airlines Sdn Bhd v Tan*<sup>107</sup> in relation to knowing receipt, and then in *Bank of Credit and Commerce International (Overseas) Ltd v Akindele*<sup>108</sup> in relation to knowing assistance.<sup>109</sup> This rejection of the *Baden* scale occurred in the context of a move by the English courts away from considerations of the required levels of knowledge to an enquiry about whether the third party had themselves acted dishonestly.<sup>110</sup> In *Royal*

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<sup>103</sup> *Bell Group* (2008) 39 WAR 1 at [4660].

<sup>104</sup> *Bell Group* (2008) 39 WAR 1 at [4663]; *Consul Development* (1975) 132 CLR 373 at 412 (Stephen J).

<sup>105</sup> [1992] 4 All ER 161 ('*Baden*') at 235-238.

<sup>106</sup> Dietrich and Ridge, above n 20, 57.

<sup>107</sup> [1995] 2 AC 378 ('*Royal Brunei*').

<sup>108</sup> [2001] Ch 437.

<sup>109</sup> *Grimaldi* (2012) 287 ALR 22 at [263].

<sup>110</sup> *Bell Group* (2008) 39 WAR 1 at [4665].

*Brunei*, the Privy Council considered that a third party could be liable for dishonest procurement of or assistance in a breach of trust, even where the trustee themselves honestly believed that they were applying trust property in a way that was permissible or dealing with the trust property in good faith.<sup>111</sup> While dishonesty was considered an essential element of accessory liability, it was the dishonesty of the third party, and not that of the breaching trustee, that was relevant.<sup>112</sup>

In contrast to the English line of authority, the High Court in *Farah* endorsed the *Baden* scale as a useful tool,<sup>113</sup> and applied it in determining that categories (i)-(iv), but not category (v), of the scale represented the level of knowledge required to attract knowing assistance liability in Australian law.<sup>114</sup>

Their Honours in *Farah* also warned against an adoption by the lower Australian courts of the *Royal Brunei* formulation of accessory liability, noting that it was contrary to the position of the High Court in *Consul Development*.<sup>115</sup> Their Honours' stated that:

whilst the different formulations of principle may lead to the same result in particular circumstances, there is a distinction between rendering liable a defendant participating with knowledge in a dishonest and fraudulent design, and rendering liable a defendant who dishonestly procures or assists in a breach of trust or fiduciary obligation where the trustee or fiduciary need not have engaged in a dishonest or fraudulent design.<sup>116</sup>

The question of whether *Royal Brunei* displaced the decision of the High Court in *Consul Development* in relation to the formulation of the second limb of *Barnes v Addy* did not arise for consideration in *Farah*.<sup>117</sup> The High Court warned, however, that *Consul Development* remains the law in Australia until, if ever, displaced by the High Court itself.<sup>118</sup> As a result, *Barnes v Addy* knowing assistance liability in Australia

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<sup>111</sup> *Bell Group* (2008) 39 WAR 1 at [4670]-[4671]; *Royal Brunei* [1995] 2 AC 378 at 384.

<sup>112</sup> *Bell Group* (2008) 39 WAR 1 at [4672].

<sup>113</sup> *Farah* (2007) 230 CLR 89 at [174], [176]-[178].

<sup>114</sup> *Farah* (2007) 230 CLR 89 at [177]-[178].

<sup>115</sup> *Farah* (2007) 230 CLR 89 at [163].

<sup>116</sup> *Farah* (2007) 230 CLR 89 at [163].

<sup>117</sup> *Farah* (2007) 230 CLR 89 at [163].

<sup>118</sup> *Farah* (2007) 230 CLR 89 at [163].



requires a dishonest and fraudulent design on the part of the breaching fiduciary or trustee, and not merely dishonesty on the part of the assistant.

The question of what level of knowledge sufficed to attract liability for knowing receipt remained open following *Farah*.<sup>119</sup> One of the major reasons that uncertainty has prevailed in relation to this question is the two divergent rationales for recipient liability running through the case law: (i) the protection of the principal's property interests in relation to the trust property; and (ii) redress for the third party's participation in equitable wrongdoing.<sup>120</sup> Dietrich and Ridge note that a property protection rationale justifies liability on the basis of constructive notice.<sup>121</sup> However, where the rationale for liability is based on the third party's participation in equitable wrongdoing, the relevant question becomes whether the defendant behaved wrongfully, and this suggests a stronger degree of cognition of the relevant breach is required.<sup>122</sup>

Dietrich and Ridge argue for the equitable wrongdoing rationale, viewing knowing receipt as a subset of knowing assistance liability<sup>123</sup> and as a result arguing that the same level of knowledge should be required for knowing receipt as for knowing assistance.<sup>124</sup> However, they warn against framing the question of third party liability purely on specific questions of the defendant's notice or knowledge, and reject the use of the *Baden* scale in determining liability.<sup>125</sup> Instead, they prefer the approach of the Privy Council in *Royal Brunei*.<sup>126</sup> Dietrich and Ridge propose the development of:

a general principle for participatory liability (encompassing knowing assistance and knowing receipt) that can be applied to a matrix of facts so as to give appropriate weight to factors such as the defendant's cognisance of the breach, the nature of the defendant's participation (for

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<sup>119</sup> *Grimaldi* (2012) 287 ALR 22 at [262]-[263]; Dietrich and Ridge, above n 20, 62.

<sup>120</sup> Dietrich and Ridge, above n 20, 58.

<sup>121</sup> *Ibid*, 59.

<sup>122</sup> *Ibid*, 59.

<sup>123</sup> *Ibid*, 60. This is discussed further below at page 26, *Justifying Third Party Liability*.

<sup>124</sup> Dietrich and Ridge, above n 20, 60.

<sup>125</sup> *Ibid*, 60.

<sup>126</sup> *Ibid*, 60-61.

example, whether passive or active, procurement, facilitation or professional assistance), the degree of the defendant's involvement and the defendant's personal characteristics.<sup>127</sup>

This approach focuses on the defendant's conduct within the full factual matrix, which includes, but is not solely dependant on, the defendant's level of knowledge.<sup>128</sup> However, Ridge and Dietrich concede that a contrary approach was taken by the High Court in *Farah* (which differentiated the ways in which liability may arise and maintained distinct requirements for each form of liability) and that this remains the current authority in Australia.<sup>129</sup>

Shortly after the decision in *Farah*, and based primarily on an examination of *Consul Development*, Owen J concluded in *Bell Group* that the knowledge requirement is met in relation to knowing receipt where the third party:

- i. has actual knowledge of the trust and the misapplication of the trust property; or
- ii. has deliberately shut his or her eyes to those things; or
- iii. has abstained in a calculated way from making such enquiries as an honest and reasonable person would make, about the trust and the application of the trust property; or
- iv. knows of facts which to an honest and reasonable person would indicate the existence of the trusts and the fact of misapplication.<sup>130</sup>

His Honour's formulation therefore considers that the level of knowledge required to give rise to knowing receipt liability is the same as that required for knowing assistance; that is, levels (i)-(iv), but not level (v) of the *Baden* scale.

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<sup>127</sup> *Ibid*, 61.

<sup>128</sup> *Ibid*, 61.

<sup>129</sup> *Ibid*, 61.

<sup>130</sup> *Bell Group* (2008) 39 WAR 1 at [4748].

## E *The Rescission Requirement*

It appears that, in the case of a contract of loan or sale entered into in breach of fiduciary duty or trust, there is a need for the wronged principal to rescind the contract before proprietary relief may be granted in relation to the misapplied property.<sup>131</sup>

In the case of *Hancock Family Memorial Foundation Ltd v Porteous*<sup>132</sup> it was alleged that Hancock had caused companies controlled by him to pay money to Porteous for use by her in acquiring properties, and had breached fiduciary duties owed by him to the companies in doing so.<sup>133</sup> It was found that no breach of fiduciary duty had taken place as the funds used were loans to Hancock that had since been discharged.<sup>134</sup> Relevantly, it was also held that, on the basis of *Daly v The Sydney Stock Exchange Ltd*,<sup>135</sup> no equitable remedy could have been granted even if there had been a breach of fiduciary duty, as the contracts, which would have been voidable had there been a breach of fiduciary duty, had not been rescinded and had in fact been discharged.<sup>136</sup>

In *Daly*, the plaintiff sought some advice from a firm of stockbrokers, Patricks, in relation to some money that he wished to invest in shares. In breach of fiduciary duty, an employee of Patricks convinced Daly to lend the money to Patricks, who at the time were in a precarious financial situation. Patricks subsequently became insolvent and was unable to repay the loan to Daly. Daly attempted to recover compensation from a fidelity fund but was unable to do so as he had not rescinded the loan contract.<sup>137</sup>

On appeal to the High Court, Gibbs CJ (with whom Wilson and Dawson JJ agreed) found that, while Patricks owed and breached a fiduciary duty to Daly, this was not enough to establish the liability of the fidelity fund. Instead, Daly needed to establish

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<sup>131</sup> R Meagher, D Heydon and M Leeming, *Meagher, Gummow and Lehane's Equity Doctrines and Remedies* (LexisNexis Butterworths, 4<sup>th</sup> ed, 2002) [5-270].

<sup>132</sup> *Hancock* (2000) 22 WAR 198.

<sup>133</sup> *Bell Group* (2008) 39 WAR 1 at [4787].

<sup>134</sup> *Bell Group* (2008) 39 WAR 1 at [4784]-[4785].

<sup>135</sup> (1986) 160 CLR 371 ('*Daly*').

<sup>136</sup> *Bell Group* (2008) 39 WAR 1 at [4784]-[4785].

<sup>137</sup> *Bell Group* (2008) 39 WAR 1 at [4786]-[4787].

that Patricks had received the money for or on behalf of him, or as a trustee.<sup>138</sup> Daly argued that Patricks held the money as a constructive trustee as they had received it in breach of duty. Gibbs CJ concluded that the benefit obtained by Patricks as a result of the breach of duty was a loan, which it was bound to repay to Daly. The ordinary legal remedies available to a creditor were sufficient to prevent Patricks from benefitting from the breach of duty, and the imposition of a constructive trust could lead to unjust consequences in relation to both creditors of Patricks, and Patricks itself.<sup>139</sup>

The Full Court of the Supreme Court of Western Australia in *Hancock* considered it to be clear from the reasoning of Gibbs CJ that a constructive trust is not automatically imposed upon money lent in circumstances that give rise to a breach of fiduciary duty.<sup>140</sup> While a constructive trust may be awarded as a discretionary remedy, such a remedy will not be granted where it is beyond what is necessary to do equity in the circumstances.<sup>141</sup>

In *Daly*, Brennan J (with whom Wilson J agreed) considered that, where a fiduciary receives property from the principal in circumstances where the transfer of property constitutes a breach of fiduciary duty, the transaction is voidable, not void.<sup>142</sup> If the principal chooses to avoid the contract by rescinding it, the fiduciary will hold the property on constructive trust for the principal. The principal may then assert title to the property or trace it. However, the principal cannot at once leave the contract on foot and deny the borrowers title to the property concerned.<sup>143</sup> As the Full Court of the Supreme Court of Western Australia explained in *Hancock*:

It stands to reasons that a party who lends money to another under a voidable contract of loan must avoid the contract before asserting equitable title to the money lent and before seeking relief against third parties by way of tracing. Were that not to be so, the lender would notionally be able to claim repayment of the moneys due as a debt under the contract, and at the same time recover,

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<sup>138</sup> *Daly* (1986) 160 CLR 371 at 377 (Gibbs J).

<sup>139</sup> *Bell Group* (2008) 39 WAR 1 at [4787]-[4788].

<sup>140</sup> *Hancock* (2000) 22 WAR 198 at [177]; *Bell Group* (2008) 39 WAR 1 at [4788].

<sup>141</sup> *Bell Group* (2008) 39 WAR 1 at [4788]; *Hancock* (2000) 22 WAR 198 at [177].

<sup>142</sup> *Bell Group* (2008) 39 WAR 1 at [4790].

<sup>143</sup> *Bell Group* (2008) 39 WAR 1 at [4790].

by equitable remedies, from the borrower, or third parties with knowledge or volunteers, property acquired through the money lent. Such a situation... would give rise to consequences unjust to the borrower and would unfairly benefit the lender.<sup>144</sup>

As their Honours noted in *Grimaldi*, *Daly* was not a case involving the receipt of property by a knowing third party and did not consider *Barnes v Addy* type liabilities.<sup>145</sup> It appears that the rescission requirement was extended to knowing receipt cases in *Greater Pacific Investments Pty Ltd (in liq) v Australian National Industries Ltd*,<sup>146</sup> where McLelland AJA stated:

[i]n general, where there is a contract for the sale of property by A to B made in breach of a fiduciary duty owed to A by B (or by C in whose breach B knowingly participated), pursuant to which the legal title to the property has been transferred from A to B, the transaction is in equity voidable at the instance of A, who may (if necessary) obtain an order for rescission setting it aside. Unless and until A effectively avoids the transaction and (if necessary) obtains an order for rescission, B's property rights as a result of the transaction remain unaffected. However if A does effectively avoid the transaction and (if necessary) obtain an order for rescission, the parties will be treated in equity as if the transaction had never been effected; in other words equity will treat B as if he had held the property in trust for A, that is, as a constructive trustee, ab initio. A constructive trust arises in such circumstances as a consequence of the effective avoidance or rescission of the transaction. Where, for whatever reason, the transaction has not been and cannot be effectively avoided and rescission is unavailable, it remains effective and no constructive trust can arise.<sup>147</sup>

### F *Personal v Proprietary Remedies*

While Lord Selborne's use of the language 'constructive trustee' in *Barnes v Addy* may suggest otherwise, the liability under both limbs of *Barnes v Addy* is a personal one; the 'constructive trusteeship' of the third party recipient or assistant is merely a vehicle by

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<sup>144</sup> *Hancock* (2000) 22 WAR 198 at [183]-[184]; *Bell Group* (2008) 39 WAR 1 at [4791].

<sup>145</sup> *Grimaldi* (2012) 287 ALR 22 at [278].

<sup>146</sup> (1996) 39 NSWLR 143 ('*Greater Pacific Investments*').

<sup>147</sup> *Greater Pacific Investments* (1996) 39 NSWLR 143 at 153; *Grimaldi* (2012) 287 ALR 22 at [279].

which a personal remedy, such as an account of profits or equitable compensation, may be sought by the wronged principal against the third party.<sup>148</sup>

Their Honours in *Grimaldi* noted the ‘latent ambiguity’ in the use of the term ‘constructive trustee’:<sup>149</sup>

In its strictest sense it refers to a person who, as a constructive trustee, holds specific property on trust for another. In its more general sense it can refer to a person who, whether or not he or she holds or has received, trust property, has so acted as to be exposed potentially to the same remedial consequences for his or her actions as would be a trustee who had acted similarly, ie that person as “a constructive trustee” may in appropriate circumstances be decreed, for example, to hold specific property as a constructive trustee, to be subject to an account of profits, or to be liable to pay compensation etc: see eg *Consul Development*, at 396-397. This latter usage is particularly prevalent both in claims against fiduciaries for breach of fiduciary duty or for misuse of fiduciary position and in *Barnes v Addy* claims where, having been described as being liable as a constructive trustee, personal relief only is awarded.<sup>150</sup>

Flowing from this, it is important to note that a distinction exists between remedies in property and personal remedies available against third parties in relation to property received with knowledge of a breach of duty. A knowing recipient in the property sense, and not the *Barnes v Addy* sense, will be liable to make specific restitution to the principal for such of the trust property, or its traceable proceeds, which remain in his or her hands.<sup>151</sup> As their Honours in *Grimaldi* note, while this type of claim may potentially be available in *Barnes v Addy* type knowing receipt case, it is a distinct and separate liability, and essentially a claim to priority.<sup>152</sup> *Barnes v Addy* liability for knowing receipt gives rise to a personal liability on the part of the third party recipient.<sup>153</sup>

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<sup>148</sup> *Grimaldi* (2012) 287 ALR 22 at [253], [699]-[700]; Nyuk Yin Nahan Nee Chin, ‘Practical Justice and Appropriate Relief: *Grimaldi v Chameleon Mining NL (No 2)*’ (2012) 36(1) *University of Western Australia Law Review* 252, 261.

<sup>149</sup> *Grimaldi* (2012) 287 ALR 22 at [667].

<sup>150</sup> *Grimaldi* (2012) 287 ALR 22 at [667].

<sup>151</sup> *Grimaldi* (2012) 287 ALR 22 at [251].

<sup>152</sup> *Grimaldi* (2012) 287 ALR 22 at [251].

<sup>153</sup> *Grimaldi* (2012) 287 ALR 22 at [253].

Dietrich and Ridge explain further that, in a situation where a third party receives trust property as a result of a fiduciary's breach of duty with knowledge, the wronged principal has several primary means of redress against the third party:

1. a claim asserting the principal's equitable proprietary interest on the basis of either:
  - a. priority rules (where the principal claims that their first-in-time interest over the trust property takes priority over the defendant's later-acquired interest); or
  - b. tracing rules (where the principal claims that the value inherent in the original trust property can be traced into mixed or substituted property now held by the defendant);
2. a personal claim asserting that the defendant knowingly received either the trust property itself, or property into which the value of the original trust property can be traced (ie, a claim based on the first limb of *Barnes v Addy*);
3. a claim asserting that the defendant knowingly assisted in the fiduciary's breach of trust (ie, a claim based on the second limb of *Barnes v Addy*).<sup>154</sup>

The first claim above gives rise to proprietary remedies, while the second and third give rise to personal remedies.<sup>155</sup> In regard to the first claim, the priority rules apply where the nature of the property in question has not changed.<sup>156</sup> Conversely, the tracing rules apply to determine whether the equitable proprietary rights of the principal survive in property now held by the defendant that has been either mixed with, or substituted for, the original trust property.<sup>157</sup>

Both the proprietary and personal liabilities in a case of knowing receipt relate to property or its traceable proceeds that once belonged to the claimant. These liabilities

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<sup>154</sup> Dietrich and Ridge, above n 20, 51. Note that the third claim listed here is controversial in relation to knowing receipt of property and the existence of this claim in a case of knowing receipt is dependent on the view that knowing receipt liability is merely a subset of a broader knowing assistance liability.

<sup>155</sup> Dietrich and Ridge, above n 20, 52.

<sup>156</sup> *Ibid*, 52.

<sup>157</sup> *Ibid*, 52.

are distinct from cases of knowing assistance not involving the receipt of trust property, in which the claimant may seek to have a constructive trust imposed by way of remedy over property derived by the third party of their own accord as a result of a breach of duty.<sup>158</sup>

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<sup>158</sup> *Grimaldi* (2012) 287 ALR 22 at [256].



### III JUSTIFYING THIRD PARTY LIABILITY

Some of the uncertainty that exists in Australian law in relation to *Barnes v Addy* liability can perhaps be attributed to a divergence of opinions as to the justifications for third party liability in relation to breaches of fiduciary duty. As Ridge notes, answering the question of why a remedy is warranted will, to a large extent, suggest the appropriate remedy.<sup>159</sup>

#### *A Rationales for Third Party Liability*

Ridge outlines both principled and pragmatic rationales for third party liability. The principled rationale is based on equity's concern in relation to the wrongful conduct of the third party, whereas the pragmatic rationales are concerned with providing a wronged fiduciary with an alternative means of recourse where none can be sought against the breaching fiduciary; and deterring third party participation in breaches of trust or fiduciary duty.<sup>160</sup> Ridge notes that the pragmatic rationales reflect the 'strongly prophylactic' nature of fiduciary obligation;<sup>161</sup> that is, the fiduciary is discouraged from using his or her position of trust and confidence in a manner inconsistent with the interests of the principal, hence bolstering the protection provided by the law to the principals of fiduciary relationships.<sup>162</sup>

Ridge argues that the remedies available for third party participation in a breach of fiduciary duty should depend primarily on the nature of the wrongdoing that equity aims to address, rather than the pragmatic rationales.<sup>163</sup> The pragmatic aspects of the rationale remain relevant, however, in strengthening the justification given by the principled

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<sup>159</sup> Ridge, above n 20, 446.

<sup>160</sup> Ibid, 446.

<sup>161</sup> Ibid, 446.

<sup>162</sup> Ibid, 446.

<sup>163</sup> Ibid, 447.

rationale, and determining the bounds within which the principle-based remedy operates.<sup>164</sup>

### *B Primary or Secondary Liability?*

Elliot and Mitchell argue that third party liability in breaches of duty is a secondary liability, resembling the accessorial liability of those who aid, abet, counsel or procure a crime.<sup>165</sup> The third party's liability derives from and duplicates the liability of the breaching fiduciary (the primary wrongdoer) in whose acts the third party participates. 'Participation' in this sense involves inducing the fiduciary to commit, conspiring with the fiduciary to commit, or assisting the fiduciary to commit, a breach of fiduciary duty.<sup>166</sup> As the third party is liable for the same wrong as the breaching fiduciary, the liability of the third party is joint and equal to that of the fiduciary.<sup>167</sup>

Ridge disagrees, instead arguing in favour of a model of primary liability for the third party, based on their own wrongdoing and not that of the breaching fiduciary.<sup>168</sup> The wrongdoing of the third party in this case is the exploitation of the principal's vulnerability, which arises as a consequence of the fiduciary relationship.<sup>169</sup> Under this model, at the very least the third party is required to compensate the principal for any loss suffered by the principal as a result of the third party's own wrongdoing.<sup>170</sup>

It is submitted that, in light of the principled and practical rationales for third party liability discussed above, Ridge's model of a primary liability based on equitable wrongdoing is preferable to Elliot and Mitchell's secondary liability model.

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<sup>164</sup> Ibid, 447.

<sup>165</sup> Steven B Elliot and Charles Mitchell, 'Remedies for Dishonest Assistance' (2004) 67(1) *Modern Law Review* 16, 17.

<sup>166</sup> Ibid, 17.

<sup>167</sup> Ibid, 17.

<sup>168</sup> Ridge, above n 20, 450-457.

<sup>169</sup> Ibid, 467.

<sup>170</sup> Ibid, 451.

### *C Is a Third Party Required to Account for Profits?*

Ridge questions whether it may be justifiable to require a third party involved in a breach of duty to account for benefits obtained by them personally as a result of their participation in a breach? On the one hand, unlike the breaching fiduciary, the third party has not undertaken any obligation of loyalty to the principal.<sup>171</sup> However, where the third party has exploited the vulnerability of the principal by dishonestly interfering with the fiduciary relationship for their own benefit, Ridge argues that a significant equitable wrong has been committed by the third party, justifying stripping the third party of any benefit obtained as a result of the wrongdoing.<sup>172</sup> The pragmatic role of third party liability in deterring breaches of fiduciary duty provides further justification for requiring the third party to account for any profits flowing from the breach.<sup>173</sup>

Ridge argues that the principled rationale of intervention in an equitable wrong and the practical rationale of deterrence justify stripping a third party of profits even in some cases where the principal has not suffered a loss as a result of the breach of duty.<sup>174</sup> However, the culpability of the third party in the circumstances, or the close relationship between the third party and breaching fiduciary, must warrant the stripping of the third party's profits in such cases.<sup>175</sup>

### *D Can a Proprietary Remedy be Ordered Against a Third Party?*

Given that the principled and pragmatic rationales of third party liability discussed above could all seemingly be met by imposing the personal liabilities of account of profits and equitable compensation, Ridge questions whether there are ever any circumstances in which a proprietary remedy against a third party might be warranted;<sup>176</sup> that is, are there circumstances in which the court may be justified in imposing a

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<sup>171</sup> Ibid, 451.

<sup>172</sup> Ibid, 451.

<sup>173</sup> Ibid, 452.

<sup>174</sup> Ibid, 454-455.

<sup>175</sup> Ibid, 455.

<sup>176</sup> Ibid, 460-461.

constructive trust over property or profits derived by the third party as a result of the breach.<sup>177</sup>

The most apparent benefit of a proprietary remedy is a priority that the wronged principal secures as a result of the proprietary interest over unsecured creditors in the case of insolvency of the third party.<sup>178</sup> Despite this, Ridge noted that the Australian line of cases involving the contemplation or award of a proprietary remedy have been concerned not with the potential insolvency of the third party, but instead with redressing the wrongdoing of the third party in relation to the principal.<sup>179</sup> Additionally, prioritising the rights of third parties against unsecured creditors has no deterrent effect on third party participation in breaches of fiduciary duty, disrupts the operation of statutory insolvency schemes, and disadvantages innocent unsecured creditors.<sup>180</sup>

Ridge argues, however, that alternative rationales may justify the imposition of proprietary remedies in some cases.<sup>181</sup> For example, a proprietary remedy may be justified where it provides a more straightforward means of ensuring that the principal is not disadvantaged by the third party's wrongdoing, such as where the principal may have made better use of a corporate opportunity wrongfully exploited by a third party.<sup>182</sup> In this situation, accurately calculating the loss of the principal is likely to be difficult, and an account of profits made by the third party is unlikely to fully reflect the loss of the principal.<sup>183</sup> Imposing a constructive trust in these circumstances (with an appropriate allowance provided to the knowing assistance to reflect the efforts and expenditure of the knowing assistant to date) would allow the principal to exploit the corporate opportunity for their own benefit.<sup>184</sup>

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<sup>177</sup> Note that an equitable lien is also a proprietary remedy considered by Ridge.

<sup>178</sup> Ridge, above n 20, 461.

<sup>179</sup> Ibid, 461.

<sup>180</sup> Ibid, 461.

<sup>181</sup> Ibid, 461.

<sup>182</sup> Ibid, 461.

<sup>183</sup> Ibid, 461-462.

<sup>184</sup> Ibid, 462.

Another situation in which a proprietary remedy may be justified is where the knowing participant is a company created to dishonestly assist the fiduciary to divert the principal's business to the company.<sup>185</sup> In these circumstances, the company itself may be wholly referable to the breach of duty and wrongdoing of the knowing participant. In such circumstances, a constructive trust over the company (with just allowances made for the expenses, effort and skills of the third party) may be the most effective remedy.<sup>186</sup> Ridge notes, however, that a constructive trust will not be an appropriate remedy in circumstances where, as in *Warman International Ltd v Dwyer*,<sup>187</sup> the success of the company is substantially attributable to the skill and efforts of the breaching fiduciary and third party, and the business opportunity is not one that would have been pursued by the principal.<sup>188</sup>

Finally, a constructive trust may be an appropriate remedy in relation to a third party's participation where the property obtained as a result of the third party's wrongdoing is no longer identifiable in their hands, but can be traced into property held by another who is not a bona fide purchaser for value,<sup>189</sup> such as in *Attorney General for Hong Kong v Reid*.<sup>190</sup> In these circumstances, the principal is limited to the award of a personal remedy against the third party participant, but may be able to assert a proprietary interest in the property now held by the other party.<sup>191</sup>

*E Can a Proprietary Remedy Be Ordered Where the Property of the Principal Cannot Be Traced Into a Third Party's Hands?*

Ridge questions whether the principal can claim proprietary rights over property held by a third party on the basis of their wrongful participation in a breach of fiduciary duty, in circumstances where the principal's property cannot be traced into the property currently held by the third party; that is, where no proprietary link exists between the principal's

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<sup>185</sup> Ibid, 462.

<sup>186</sup> Ibid, 462.

<sup>187</sup> (1995) 182 CLR 544 ('*Warman*').

<sup>188</sup> Ridge, above n 20, 462.

<sup>189</sup> Ibid, 463.

<sup>190</sup> [1994] 1 AC 324.

<sup>191</sup> Ridge, above n 20, 463.

property, and that held by the third party.<sup>192</sup> A constructive trust in this sense would be remedial, as such an order would involve the court granting a proprietary right to someone who previously had no such right.<sup>193</sup> This differs to an institutional constructive trust, which is considered to have existed from the time of the breach giving rise to it; the court's role in relation to an institutional constructive trust involves 'recognising' as versus imposing, the proprietary right.<sup>194</sup> An institutional constructive trust may be recognised by the court, for example, where trust property misapplied in breach of trust can be traced into the hands of the third party who has received the property with knowledge.

Ridge notes that the distinction between institutional and remedial constructive trusts in Australia is blurred,<sup>195</sup> with the institutional/remedial distinction seen as 'connoting a remedial spectrum rather than a remedial dichotomy'.<sup>196</sup> Both versions of the constructive trust were originally considered remedial responses to particular equitable wrongdoings, with institutional trusts merely becoming 'institutional' via repeated judicial recognition and usage.<sup>197</sup> While the institutional trust may be considered to have existed 'in the shadows' prior to recognition by the court, Ridge considers that an element of discretion still remains in relation to the court's recognition of its existence.<sup>198</sup> Likewise, the court retains a discretion as to whether to impose a remedial constructive trust.<sup>199</sup> Ridge notes, however, that the court's discretion may be constrained by recognised principles relating to its exercise.<sup>200</sup>

While proprietary remedies in relation to third party participation in breaches of trust or fiduciary duty are available in Australia at the court's discretion and have been awarded,<sup>201</sup> Ridge notes that there is a great deal of uncertainty as to how the court's

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<sup>192</sup> Ibid, 463.

<sup>193</sup> Ibid, 465.

<sup>194</sup> Ibid, 464.

<sup>195</sup> Ibid, 465; *Muschinski v Dodds* (1985) 160 CLR 583.

<sup>196</sup> Ridge, above n 20, 465.

<sup>197</sup> Ibid, 465.

<sup>198</sup> Ibid, 463.

<sup>199</sup> Ibid, 463.

<sup>200</sup> Ibid, 465.

<sup>201</sup> Ibid, 465.

discretion to award a proprietary remedy in these circumstances may be exercised.<sup>202</sup> Ridge suggests that this is the result of the evolving nature of the jurisdiction, rather than any reluctance on the part of the Australian judiciary to set boundaries to the remedial discretion.<sup>203</sup> Ridge outlines a set of principles related to the exercise of the discretion that may be ‘glean[ed] from the current authorities’:

1. The least intrusive proprietary remedy should be awarded, with the first question always being, ‘having regard to the issues in the litigation, is there an appropriate equitable remedy which falls short of the imposition of a trust?’: *Giumelli v Giumelli*.<sup>204</sup>
2. The interests of innocent third parties, including unsecured creditors, must be protected (although it is not clear whether this requires the refusal of a proprietary remedy altogether where the interests of innocent third parties would be adversely impacted upon): *Muschinski v Dodds*,<sup>205</sup> *Giumelli v Giumelli*.<sup>206</sup>
3. The court retains a residual discretion to refuse a proprietary remedy on established grounds, such as laches: *Chan v Zacharia*,<sup>207</sup> *Warman*.<sup>208</sup>

Based on these principles, Ridge suggests that a constructive trust may be imposed, and should only be imposed, against a third party participant where:

1. the proprietary remedy will be the most effective way to redress the wrong of the third party and would not be otherwise available,<sup>209</sup> and

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<sup>202</sup> Ibid, 466.

<sup>203</sup> Ibid, 466.

<sup>204</sup> (1999) 196 CLR 101 at 113; Ridge, above n 20, 466.

<sup>205</sup> (1985) 160 CLR 583; Ridge, above n 20, 466.

<sup>206</sup> (1999) 196 CLR 101 at 113-114; Ridge, above n 20, 466.

<sup>207</sup> (1984) 154 CLR 178 at 204-205; Ridge, above n 20, 466.

<sup>208</sup> (1995) 182 CLR 554 at 559; Ridge, above n 20, 466.

<sup>209</sup> Ridge, above n 20, 467.

2. the proprietary remedy can be framed so as to protect the interests of third parties (meaning that a constructive trust should not be awarded where the third party is insolvent and the contest becomes between the principal and unsecured creditors).<sup>210</sup>

## *F Should Liability be Joint or Several?*

### *1 Liability for the Losses of the Principal*

Ridge argues that, if a third party's liability in relation to a breach of fiduciary duty or trust is a primary liability based on their own wrongdoing, they should be liable only for the losses 'caused' by this wrongdoing.<sup>211</sup> Once it has been established that the third party has been a 'cause-in-fact' of the losses of the principal or beneficiary, the court should consider the appropriate scope of liability for the third party as a normative question.<sup>212</sup> However, once it is found that the third party has been involved in a breach of trust or duty, they are instead held jointly and severally liable with the breaching fiduciary or trustee for *all* of the losses of the principal or trustee arising from the breach.<sup>213</sup> The difficulty with this is that it can result in the third party being liable for extensive losses even where their wrongdoing may have been relatively minor compared to the wrongdoing of the breaching fiduciary or trustee.<sup>214</sup>

Despite this difficulty, Ridge considers generally that joint and several liability for third party involvement in a breach of duty or trust can be justified on two bases.<sup>215</sup> Firstly, joint and several liability is consistent with the principles of fiduciary law generally, which are based on the discouragement of actions on the part of the fiduciary which are inconsistent with the position of trust and confidence they occupy in relation to the

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<sup>210</sup> Ibid, 463; *Muschinski v Dodds* (1985) CLR 583 at 623 (Deane J).

<sup>211</sup> Ridge, above n 20, 457.

<sup>212</sup> Ibid, 457.

<sup>213</sup> Ibid, 457.

<sup>214</sup> Ibid, 457.

<sup>215</sup> Ibid, 459.



principal.<sup>216</sup> For third party liability to arise, there must be wrongdoing on the part of the third party. In the eyes of equity, this wrongdoing may be significant enough to warrant the third party bearing the risk of full liability for the losses of the principal.<sup>217</sup> Secondly, the joint and several liability of the third party is only in relation to the principal; the breaching fiduciary may be liable to the third party for a contribution towards the full liability, hence providing some protection to the third party where their contribution to the wrongdoing has been relatively minor compared to the actions of the breaching fiduciary.<sup>218</sup>

## *2 Liability for the Gains of the Wrongdoers*

Under a fault based, primary liability model, Ridge notes that the remedies available against the third party should focus on the wrongdoing of the third party themselves, and the third party should not be liable for gains made by the breaching fiduciary.<sup>219</sup> However, Ridge notes that it is possible to conceive of some instances where the joint liability of the third party for gains made by the breaching fiduciary may be justifiable. These include circumstances where the fiduciary is controlled by the third party and acts merely vehicle for the enrichment of the third party.<sup>220</sup>

Ridge considers, however, that joint and several liability for third parties in all instances would likely be ‘penal’, in that it would go beyond what is necessary to fulfil the pragmatic and principled rationales of liability, and may in fact amount to a punitive measure against the third party.<sup>221</sup>

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<sup>216</sup> Ibid, 458.

<sup>217</sup> Ibid, 458.

<sup>218</sup> Ibid, 458-459.

<sup>219</sup> Ibid, 459.

<sup>220</sup> Ibid, 459.

<sup>221</sup> Ibid, 460; *Ultraframe (UK) Ltd v Fielding* [2006] FSR 17 at [598], [600].

#### IV CHAMELEON MINING NL v MURCHISON METALS LTD<sup>222</sup>

##### *A Factual Background*

Chameleon Mining NL was a start-up mining company incorporated in November 2001 and listed on the Australian Securities Exchange (“ASX”) in April 2003. In November 2007, Chameleon lodged claims in the Federal Court of Australia against their former managing director, Gregory Barnes, and an alleged de facto or shadow director, Phillip Grimaldi, alleging breaches of fiduciary and statutory duties owed to Chameleon.<sup>223</sup> The alleged breaches related to a number of transactions involving Chameleon over the course of 2001 – 2004, notably the Cadetta and Cheques transactions outlined below.

Chameleon also claimed that three companies, Winterfall (later known as Crosslands Resources Ltd), Murchison Metals Ltd (formerly known as Weboz Ltd and NiCu Metals Ltd) and Pinnacle Nominees Pty Ltd, were liable as knowing recipients and/or assistants to the breaches of fiduciary duty and/or accessories under the Corporations Act. Grimaldi was a director and the controlling mind of Murchison.<sup>224</sup> Pinnacle Nominees was owned and controlled by Barnes.<sup>225</sup>

Barnes and Pinnacle Nominees settled the claims against them without an admission of liability prior to the end of the trial, for an agreed payment of \$6,000,000 to Chameleon.<sup>226</sup>

At first instance, Grimaldi was found to be a de facto director of Chameleon. Importantly, Jacobs J concluded that, regardless of whether Grimaldi was a de facto director under the Corporations Act, his relationship with Chameleon in relation to the impugned transactions gave rise to fiduciary duties, which Grimaldi subsequently

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<sup>222</sup> [2010] FCA 1129 (*Chameleon*).

<sup>223</sup> *Chameleon* [2010] FCA 1129 at [1]-[2].

<sup>224</sup> *Grimaldi* (2012) 287 ALR 22 at [8].

<sup>225</sup> *Chameleon* [2010] FCA 1129 at [13].

<sup>226</sup> *Chameleon* [2010] FCA 1129 at [13].

breached.<sup>227</sup> Barnes had also breached fiduciary duties owed to Chameleon. Both Murchison and Winterfall were held liable as knowing recipients of Chameleon funds misapplied by Barnes and Grimaldi in breach duty. Murchison was also found to be a knowing assistant in relation to these breaches.

### *1 The Iron Jack Deal*

In February 2004, Winterfall negotiated the purchase a set of iron ore tenements in Western Australia (the ‘Iron Jack’ tenements) from a group of third party vendors.<sup>228</sup> Winterfall agreed to pay the vendors of the tenements via a series of instalments, but fell short of funds and became unable to complete payment of the second instalment.<sup>229</sup> A director and majority shareholder of Winterfall, Zuks, knew Grimaldi and Barnes from previous dealings and met with them in relation to the purchase of the Iron Jack tenements in about April 2004.<sup>230</sup> It was agreed at this meeting that Murchison would provide the funds necessary for Winterfall to complete the second instalment payment in return for an interest in the Iron Jack project.<sup>231</sup> Zuks negotiated an extension of time for payment of the second instalment with the Iron Jack vendors until early June 2004.<sup>232</sup> As part of the negotiated extension, Winterfall agreed that, should the June deadline not be met, the Iron Jack tenements would return to the Iron Jack vendors, and no payment made to date would be refunded.<sup>233</sup>

A Heads of Agreement was executed between Murchison and Winterfall.<sup>234</sup> Under the terms of the agreement, Murchison was to pay the \$350,000 remaining due in relation to the second instalment payment to the Iron Jack vendors, and subsequently effect a reverse takeover of Winterfall through an exchange of shares.<sup>235</sup> As part of the deal,

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<sup>227</sup> *Chameleon* [2010] FCA 1129 at [173], [690]-[691].

<sup>228</sup> *Chameleon* [2010] FCA 1129 at [354]-[356].

<sup>229</sup> *Chameleon* [2010] FCA 1129 at [357]-[358], [362].

<sup>230</sup> *Chameleon* [2010] FCA 1129 at [367].

<sup>231</sup> *Chameleon* [2010] FCA 1129 at [371].

<sup>232</sup> *Chameleon* [2010] FCA 1129 at [375].

<sup>233</sup> *Chameleon* [2010] FCA 1129 at [377].

<sup>234</sup> *Chameleon* [2010] FCA 1129 at [378].

<sup>235</sup> *Chameleon* [2010] FCA 1129 at [378]-[381].

Zuks agreed to pay an additional fee (the ‘spotter’s fee’) to Barnes and Grimaldi,<sup>236</sup> which consisted of shares in Winterfall that could later be exchanged for shares in Murchison following the completion of the reverse takeover.<sup>237</sup> The payment of the spotter’s fee was dependent upon the payment of the \$350,000 by Murchison in relation to the second of the Iron Jack instalment payments.<sup>238</sup>

In breach of the Heads of Agreement, Murchison failed to pay the \$350,000 when it became due.<sup>239</sup> As a result, Winterfall was in danger of being unable to complete the second instalment payment, and consequently of losing the \$100,000 invested in the purchase to date and the option to complete the purchase of the tenements.<sup>240</sup> Grimaldi was confident that he could secure funds for the payment and asked Zuks to wait. Zuks agreed and was able to negotiate a further extension of time with the Iron Jack vendors until 1 July 2004.<sup>241</sup>

By mid-July, Murchison had still not paid the agreed money to the Iron Jack vendors.<sup>242</sup> The vendors sent a fax to Winterfall on 22 July stating that the negotiation period had come to an end, and that they were now dealing with other offers.<sup>243</sup> Urgent discussions took place between Grimaldi and Zuks.<sup>244</sup> Grimaldi sent a fax to Zuks stating that Murchison had made available ‘via Chameleon Mining NL’ a total of \$318,000, and had a further \$32,000 plus GST of \$35,000 ready to be paid.<sup>245</sup> Zuks forwarded this fax to the Iron Jack vendors on the same day.<sup>246</sup> The vendors allowed Winterfall until 5pm the following day to present cheques for the full amount.<sup>247</sup>

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<sup>236</sup> *Chameleon* [2010] FCA 1129 at [389]-[390].

<sup>237</sup> *Chameleon* [2010] FCA 1129 at [398].

<sup>238</sup> *Chameleon* [2010] FCA 1129 at [399].

<sup>239</sup> *Chameleon* [2010] FCA 1129 at [382].

<sup>240</sup> *Chameleon* [2010] FCA 1129 at [384].

<sup>241</sup> *Grimaldi* (2012) 287 ALR 22 at [161].

<sup>242</sup> *Chameleon* [2010] FCA 1129 at [583].

<sup>243</sup> *Chameleon* [2010] FCA 1129 at [583].

<sup>244</sup> *Chameleon* [2010] FCA 1129 at [584].

<sup>245</sup> *Chameleon* [2010] FCA 1129 at [584]-[585].

<sup>246</sup> *Chameleon* [2010] FCA 1129 at [586].

<sup>247</sup> *Chameleon* [2010] FCA 1129 at [587]; *Grimaldi* (2012) 287 ALR 22 at [305].

Zuks made the payment to the Iron Jack vendors prior to the expiry of the deadline.<sup>248</sup> Included in the payment were cheque funds sourced from Chameleon's accounts to the value of \$152,750, plus \$125,090 in funds raised by Murchison through the sale of Chameleon shares received by Grimaldi as a commission in relation to the Cadetta transaction.<sup>249</sup> These transactions are outlined below.

Winterfall completed its purchase of the Iron Jack tenements and Murchison's reverse takeover of Winterfall was effected in November 2004.<sup>250</sup> Winterfall's shareholders were provided with 80 million shares and 30 million options in Murchison in exchange for their Winterfall shares.<sup>251</sup> 10 million of these shares and 12 million of the options were issued to Barnes and Grimaldi (or for their benefit) in exchange for the spotter's fee that they had received following Murchison's payment of \$350,000 to the Iron Jack vendors.<sup>252</sup>

## *2 The Cadetta Transaction*

In May 2004, Chameleon entered into a deal to purchase four mining interests known as the Cadetta tenements for an exchange of shares in Chameleon.<sup>253</sup> Grimaldi, who had been assisting Chameleon with fundraising for some time, was closely involved with the deal.<sup>254</sup> The Cadetta tenements were purchased for 8 million shares in Chameleon, with a further 5 million Chameleon shares payable to Grimaldi as a commission for introducing the Cadetta transaction to Chameleon.<sup>255</sup> Grimaldi arranged for these 5 million shares to be paid to Murchison,<sup>256</sup> and organised their sale as soon as they had

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<sup>248</sup> *Chameleon* [2010] FCA 1129 at [589].

<sup>249</sup> *Grimaldi* (2012) 287 ALR 22 at [17].

<sup>250</sup> *Chameleon* [2010] FCA 1129 at [797].

<sup>251</sup> *Grimaldi* (2012) 287 ALR 22 at [16].

<sup>252</sup> *Grimaldi* (2012) 287 ALR 22 at [16].

<sup>253</sup> *Chameleon* [2010] FCA 1129 at [41]-[49].

<sup>254</sup> *Chameleon* [2010] FCA 1129 at [42].

<sup>255</sup> *Chameleon* [2010] FCA 1129 at [48].

<sup>256</sup> *Grimaldi* (2012) 287 ALR 22 at [205].

been transferred. An amount of \$125,090 raised from the sales was then used by Murchison to assist with its payment to the Iron Jack vendors.<sup>257</sup>

### *3 The Cheques Transactions*

Chameleon only had a small amount of cash available in its account at the start of July (approximately \$4,700 on 5 July 2004).<sup>258</sup> Despite this, either or both Barnes and Grimaldi told Zuks that Chameleon would be meeting some of the payments due to the Iron Jack vendors.<sup>259</sup>

On 8 July 2004, a resolution was circulated amongst the directors of Chameleon stating that it had been resolved to pay Murchison a short-term loan in the amount of \$56,500.<sup>260</sup> Barnes drew a cheque for \$56,250 on Chameleon's account on 9 July 2004, payable to one of the Iron Jack vendors.<sup>261</sup> The cheque was initially dishonoured due to insufficient funds in Chameleon's account, but cleared when re-presented later in July.<sup>262</sup> Grimaldi, on behalf of Murchison, requested another 'loan' from Chameleon in mid-July.<sup>263</sup> Barnes subsequently drew a second cheque from Chameleon's funds for the amount of \$96,500 in favour of another Iron Jack vendor in late July.<sup>264</sup>

A total of \$152,750 (the combined value of the two cheques) was debited from Chameleon's bank account on 29 July 2004.<sup>265</sup> The only possible source of funding for the cheques was found to be from a placement that Grimaldi was organising on Chameleon's behalf for the purpose of the exploration of an unrelated gold mine.<sup>266</sup>

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<sup>257</sup> *Grimaldi* (2012) 287 ALR 22 at [206].

<sup>258</sup> *Chameleon* [2010] FCA 1129 at [560].

<sup>259</sup> *Chameleon* [2010] FCA 1129 at [561].

<sup>260</sup> *Chameleon* [2010] FCA 1129 at [562]-[564].

<sup>261</sup> *Chameleon* [2010] FCA 1129 at [567].

<sup>262</sup> *Chameleon* [2010] FCA 1129 at [569], [589].

<sup>263</sup> *Chameleon* [2010] FCA 1129 at [574].

<sup>264</sup> *Chameleon* [2010] FCA 1129 at [580]-[581].

<sup>265</sup> *Chameleon* [2010] FCA 1129 at [589].

<sup>266</sup> *Chameleon* [2010] FCA 1129 at [633].

## B *The Findings of Jacobson J*

Chameleon claimed that Grimaldi and Barnes had devised the Cadetta transaction for the improper purpose of siphoning funds from Chameleon to assist Murchison in meeting its obligations to Winterfall.<sup>267</sup> While this claim was unsuccessful, his Honour found that the commission constituted a personal benefit or gain obtained by Grimaldi by reason of his fiduciary position in relation to Chameleon.<sup>268</sup> As Grimaldi had arranged for the shares to be paid to Murchison, Murchison was found to be a knowing recipient of the Chameleon funds, and a knowing assistant in relation to Grimaldi's breach of fiduciary duty.<sup>269</sup> As the controlling mind of Murchison, Grimaldi's actual knowledge that he was not entitled to retain the commission or apply it for Murchison's benefit was attributable to Murchison.<sup>270</sup> Grimaldi's actions did not constitute a fraud on Murchison as they were at least partly of benefit to Murchison (as they assisted Murchison to meet obligations to Winterfall under the Heads of Agreement).<sup>271</sup>

His Honour found that Murchison was also a knowing recipient of the Chameleon cheque funds that had been misapplied by Barnes and Grimaldi in breach of duty.<sup>272</sup> While Chameleon had paid the funds to Winterfall and not Murchison, they had done so for Murchison's benefit. As a result, the cheques passed through Murchison's hands,<sup>273</sup> satisfying the element of receipt.<sup>274</sup> As the controlling mind of Murchison, Grimaldi's actual knowledge that the cheque funds were misapplied was imputed to Murchison.<sup>275</sup> The drawing of the cheques could not be considered to be a fraud on Murchison by Grimaldi because the transaction was partly for Murchison's benefit.<sup>276</sup>

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<sup>267</sup> *Chameleon* [2010] FCA 1129 at [533].

<sup>268</sup> *Chameleon* [2010] FCA 1129 at [543]; *Chan v Zacharia* (1984) 154 CLR 178 at 198-199.

<sup>269</sup> *Chameleon* [2010] FCA 1129 at [544].

<sup>270</sup> *Chameleon* [2010] FCA 1129 at [544].

<sup>271</sup> *Chameleon* [2010] FCA 1129 at [544], [699]-[703].

<sup>272</sup> *Chameleon* [2010] FCA 1129 at [695]-[696].

<sup>273</sup> *Chameleon* [2010] FCA 1129 at [697]; *Consul Development* (1975) 132 CLR 373 at 411 (Stephen J).

<sup>274</sup> *Chameleon* [2010] FCA 1129 at [697]; *Bell Group* (2008) 39 WAR 1 at [4663].

<sup>275</sup> *Chameleon* [2010] FCA 1129 at [699].

<sup>276</sup> *Chameleon* [2010] FCA 1129 at [700]-[702].

Murchison was also liable as a knowing assistant for assisting the dishonest and fraudulent design of Barnes and Grimaldi in relation to the receipt of the spotter's fee, which his Honour considered was an illicit commission.<sup>277</sup> Murchison possessed actual knowledge of the dishonest and fraudulent design as a result of the actual knowledge of Grimaldi.<sup>278</sup>

Finally, Murchison was liable under sections 79(a) and (c) of the Corporations Act for aiding and abetting, and being knowingly concerned in, Barnes' contraventions of sections 181 and 182 of the Corporations Act, due to Grimaldi's actual knowledge of all of the essential elements of Barnes' contraventions.<sup>279</sup>

Winterfall was found to be a knowing recipient of the Chameleon cheque funds misapplied by Barnes and Grimaldi in breach of duty. In respect of Barnes and Grimaldi's breaches of duty, Zuks was considered at the very least to have had knowledge of circumstances which would indicate the facts to an honest and reasonable man; that is, knowledge falling within category (iv) of the *Baden* scale.<sup>280</sup> Zuks' knowledge as a director of Winterfall was imputed to Winterfall. As the cheques passed through Zuks' hands and were delivered to him by the Iron Jack vendors to meet part of Winterfall's liability under the Iron Jack agreement, the element of receipt of trust property was met.<sup>281</sup>

His Honour concluded that Winterfall was also liable as an accessory under section 79 of the Corporations Act as a result of Zuks' actual knowledge of breaches by Grimaldi and Barnes of duties owed under the Act.<sup>282</sup>

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<sup>277</sup> *Chameleon* [2010] FCA 1129 at [705].

<sup>278</sup> *Chameleon* [2010] FCA 1129 at [706].

<sup>279</sup> *Chameleon* [2010] FCA 1129 at [707].

<sup>280</sup> *Chameleon* [2010] FCA 1129 at [719].

<sup>281</sup> *Chameleon* [2010] FCA 1129 at [729].

<sup>282</sup> *Chameleon* [2010] FCA 1129 at [728].



## 1 Remedies

Chameleon claimed a constructive trust or an account of profits (at its election) from Murchison in relation to Murchison's 100% shareholding in Winterfall, or alternatively over a percentage interest equivalent to the amount that the proceeds of the Chameleon cheques and Cadetta shares sale represented in relation to the total consideration provided by Winterfall for the acquisition of the Iron Jack tenements (which equated to approximately 24%).<sup>283</sup> Chameleon also claimed a constructive trust over the 10 million shares issued as the spotter's fee.<sup>284</sup> Alternatively, Chameleon claimed equitable compensation.<sup>285</sup>

His Honour concluded that the imposition of a constructive trust over Murchison's shares in Winterfall was clearly not an appropriate remedy, as the shares were neither the profit nor the property obtained by Murchison as a result of Barnes and Grimaldi's breaches.<sup>286</sup> While the nature of the benefit received by Murchison as a result of its involvement in the breaches of Barnes and Grimaldi was difficult to determine precisely, his Honour considered that Chameleon's funds had been mixed with the funds of Murchison and applied in partial discharge of Murchison's obligations towards Winterfall.<sup>287</sup> Murchison did not acquire a specific item of property as such, but instead obtained the benefit of being able to complete its transaction with Winterfall and subsequently gain an interest in the Iron Jack project.<sup>288</sup> His Honour characterised the benefit as an investment in the working capital of Winterfall in accordance with the Murchison/Winterfall Heads of Agreement.<sup>289</sup>

While Murchison did later acquire a 100% shareholding in Winterfall, the Heads of Agreement itself only provided Murchison with a right to bid for the shares, not a right

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<sup>283</sup> *Chameleon* [2010] FCA 1129 at [919]-[921].

<sup>284</sup> *Chameleon* [2010] FCA 1129 at [919].

<sup>285</sup> *Chameleon* [2010] FCA 1129 at [919].

<sup>286</sup> *Chameleon* [2010] FCA 1129 at [977]-[978]; *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41 ('*Hospital Products*') at 110; *Maguire v Makaronis* (1997) 188 CLR 449 at 468.

<sup>287</sup> *Chameleon* [2010] FCA 1129 at [927].

<sup>288</sup> *Chameleon* [2010] FCA 1129 at [927].

<sup>289</sup> *Chameleon* [2010] FCA 1129 at [997].

to purchase them. Likewise, the Heads of Agreement did not outline the consideration payable by Murchison for the shares, and there was substantial further debate between Murchison and Winterfall in relation to this over September and October of 2004.<sup>290</sup> As a result, there was an insufficient causal nexus between the acquisition of Winterfall by Murchison and the breaches of fiduciary duty, barring the imposition of a constructive trust on an application of the profit principle.<sup>291</sup> Likewise, a constructive trust could not be imposed on an application of the rules of equitable tracing, as the shares in Winterfall were not a substitute for the misapplied Chameleon funds.<sup>292</sup>

Murchison was instead required to account for profits obtained as a result of its participation in Barnes and Grimaldi's breaches of duty.<sup>293</sup> His Honour ordered an accounting of all the funds that Murchison or its subsidiaries invested in the Iron Jack project from the time that the Chameleon funds were improperly obtained, and a calculation of the net profits derived from the venture.<sup>294</sup> Chameleon was entitled to a portion of that income referable to the amount of \$277,840 (being the total funds of which it had been deprived as a result of the Cheques transaction and Cadetta transaction), as well as the repayment of that amount itself if not already received.<sup>295</sup> Murchison was not liable to account for the profits of Barnes and Grimaldi derived from the spotter's fee.<sup>296</sup>

Murchison was also ordered to compensate Chameleon under section 1317H(1) of the Corporations Act for damage suffered by Chameleon as a result of Murchison's contravention of section 79(c) of the Corporations Act.<sup>297</sup> The damage suffered was deemed to include the profits made by Murchison and Grimaldi as a result of the contraventions.<sup>298</sup> The orders made were constructed to preclude Chameleon from

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<sup>290</sup> *Chameleon* [2010] FCA 1129 at [992].

<sup>291</sup> *Chameleon* [2010] FCA 1129 at [979]-[1010].

<sup>292</sup> *Chameleon* [2010] FCA 1129 at [1011]-[1020].

<sup>293</sup> *Chameleon* [2010] FCA 1129 at [1035].

<sup>294</sup> *Chameleon* [2010] FCA 1129 at [1037].

<sup>295</sup> *Chameleon* [2010] FCA 1129 at [1038]-[1039].

<sup>296</sup> *Chameleon* [2010] FCA 1129 at [1085]-[1092].

<sup>297</sup> *Chameleon* [2010] FCA 1129 at [1101]-[1105].

<sup>298</sup> *Chameleon* [2010] FCA 1129 at [1105].

double recovery in respect of the equitable remedies granted in relation to the breaches of fiduciary duty.<sup>299</sup>

Winterfall was liable to account for the benefit received by its knowing receipt of the misapplied Chameleon cheque funds.<sup>300</sup> His Honour considered Winterfall's benefit to be the same as that received by Murchison; that is, the benefit of the investment of the cheque funds as part of a pool of working capital.<sup>301</sup> Accordingly, the account of profits was to be calculated on the same basis as for Murchison, but limited to the value of the cheques alone.<sup>302</sup>

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<sup>299</sup> *Grimaldi* (2012) 287 ALR 22 at [25].

<sup>300</sup> *Chameleon* [2010] FCA 1129 at [1098]-[1099].

<sup>301</sup> *Chameleon* [2010] FCA 1129 at [1099].

<sup>302</sup> *Chameleon* [2010] FCA 1129 at [1099].

*A Introduction*

The Full Court decision in *Grimaldi* was handed down on 21 February 2012. Their Honours Finn, Stone and Perram upheld much of Jacobson J's first instance decision. The Full Court found that his Honour's conclusions that Grimaldi was a de facto director of Chameleon and had owed and breached fiduciary duties to Chameleon in respect of the Cadetta transaction and Cheques transactions were unassailable.<sup>304</sup> Likewise, their Honours confirmed the liability of Murchison as a knowing assistant and knowing recipient of the misapplied Chameleon cheque and Cadetta shares sale funds, and the liability of Winterfall as a knowing recipient of the misapplied cheque funds.

Much of the appeal centred on the relief ordered by Jacobson J in respect of these conclusions. The Full Court confirmed that a constructive trust could not be imposed over Murchison's interest in Winterfall on the basis of Jacobson J's reasoning that the Murchison's interest in Winterfall represented neither the profit nor the property obtained by Murchison as a result of Grimaldi and Barnes' breaches of duty. In contrast, their Honours concluded that Jacobson J had erred in his characterisation of the benefit obtained by Winterfall, finding that the benefit obtained was in fact an interest in the Iron Jack tenements themselves. However, a constructive trust over a portion of Winterfall's interest in the Iron Jack tenements in favour of Chameleon was refused on discretionary grounds. While confirming Murchison and Winterfall's liability to account for profits received as a result of the misapplied Chameleon funds, their Honours overturned Jacobson J's orders in relation to the accounts for reasons discussed further below, remitting the matter back to Jacobson J for further consideration.

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<sup>303</sup> (2012) 287 ALR 22.

<sup>304</sup> *Grimaldi* (2012) 287 ALR 22 at [195].

In reaching their decision, their Honours discussed many principles relevant to the liability of third parties involved in breaches of fiduciary duty at length. The dicta and reasoning of their Honours provides valuable guidance as to the current state of Australian law in relation to third party liability.

### *B Are the Two Limbs of Barnes v Addy Distinct?*

Their Honours in *Grimaldi* noted the existence of uncertainty in relation to a distinction between the two limbs of *Barnes v Addy*, but only considered the matter insofar as a distinction between the limbs gave rise to different levels of knowledge required for knowing receipt and knowing assistance.<sup>305</sup> They considered that the conventional view in Commonwealth jurisdictions had been to treat the two limbs as distinct,<sup>306</sup> and that this view had been exaggerated by the unjust enrichment and restitution arguments in relation to knowing receipt (that is, characterising knowing receipt liability as proprietary, versus personal, a position which was rejected in Australia in *Farah*).<sup>307</sup> Despite this, the courts had still been reluctant to accept strict liability for knowing receipt.<sup>308</sup> Their Honours concluded that:

[a]s with assistance liability, recipient liability should be seen as fault based and as making the same knowledge/notice demands as in assistance cases. We need not pursue this particular matter further because the weight of authority in this country appears now to draw no distinction between the two types of liability in this respect.<sup>309</sup>

Importantly, their Honours in *Grimaldi* considered that Winterfall was liable as a knowing recipient despite no finding of dishonesty on the part of Zuks.<sup>310</sup> In contrast, dishonesty on the part of the fiduciary is required to give rise to liability for knowing assistance.<sup>311</sup>

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<sup>305</sup> *Grimaldi* (2012) 287 ALR 22 at [257].

<sup>306</sup> *Grimaldi* (2012) 287 ALR 22 at [258].

<sup>307</sup> *Grimaldi* (2012) 287 ALR 22 at [258]; *Farah* (2007) 230 CLR 89; *Citadel General Assurance Co v Lloyds Bank Canada* (1997) 152 DLR (4<sup>th</sup>) 411 ('*Citadel*'); *Royal Brunei* [1995] 2 AC 378.

<sup>308</sup> *Grimaldi* (2012) 287 ALR 22 at [258]; *Citadel* (1997) 152 DLR (4<sup>th</sup>) 411 at [51].

<sup>309</sup> *Grimaldi* (2012) 287 ALR 22 at [267].

<sup>310</sup> *Grimaldi* (2012) 287 ALR 22 at [392].

<sup>311</sup> *Bell Group* (2008) 39 WAR 1 at [4727].

It appears that the present state of Australian law continues to draw a distinction between the two limbs of *Barnes v Addy* in relation to the relevance of the state of mind of the breaching fiduciary necessary to invoke the liability. However, as shall be evident from the further discussion below, once the liability is triggered by this dishonesty, there is no further meaningful distinction between the two limbs.

### *C The Level of Knowledge Required for Knowing Receipt*

In *Grimaldi*, their Honours accepted that the liability of a third party for knowing receipt or knowing assistance is fault based, turning upon the knowledge that the third party had in relation to the breach of the fiduciary.<sup>312</sup> Each liability was considered ‘to arise as a matter of conscience not of property’.<sup>313</sup> As a result, the Full Court considered that the same level of knowledge or notice was required for knowing receipt as for knowing assistance.<sup>314</sup>

While their Honours cautioned against the application of a classification system as a formulae for problem solving,<sup>315</sup> they noted the High Court’s acceptance of the *Baden* categories in *Farah* and determined the knowledge requirement for knowing receipt in *Grimaldi* on the basis of the *Baden* classification system.<sup>316</sup> Their Honours noted that, while *Consul Development* had been determined prior to *Baden*, it had been noted by judges in Australia since *Baden* that the views of Stephen J (with whom Barwick CJ agreed) and Gibbs J in *Consul* could be considered as accepting category (iv), but not category (v) constructive knowledge as sufficient to give rise to liability for knowing receipt.<sup>317</sup> Their Honours agreed with this view.<sup>318</sup> This line of authority was consistent also with the level of knowledge required for knowing assistance as determined in

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<sup>312</sup> *Grimaldi* (2012) 287 ALR 22 at [258].

<sup>313</sup> *Grimaldi* (2012) 287 ALR 22 at [267].

<sup>314</sup> *Grimaldi* (2012) 287 ALR 22 at [267].

<sup>315</sup> *Grimaldi* (2012) 287 ALR 22 at [260].

<sup>316</sup> See *Grimaldi* (2012) 287 ALR 22 at [259]-[270].

<sup>317</sup> *Grimaldi* (2012) 287 ALR 287 22 at [268].

<sup>318</sup> *Grimaldi* (2012) 287 ALR 287 22 at [269].

*Farah*,<sup>319</sup> and thus with the view of their Honours that the same knowledge or notice requirements should apply for both knowing receipt and knowing assistance.<sup>320</sup>

Unless and until a different view is countenanced by the High Court, it now appears almost beyond doubt that the level of knowledge required to give rise to liability for knowing receipt is the same as that required for knowing assistance: levels (i)-(iv) but not level (v) of the *Baden* scale.

#### D *The Special Nature of Corporate Property*

##### 1 *Does Knowing Receipt Liability Extend to Breaches of Fiduciary Duty?*

Their Honours in *Grimaldi* considered the *Belmont Finance* position to be ‘well settled’; that is, that corporate property misapplied in breach of fiduciary duty is treated as ‘trust property’ for the purposes of *Barnes v Addy*.<sup>321</sup> The Full Court in *Grimaldi* did not address the High Court’s caution on this point in *Farah*,<sup>322</sup> instead endorsing *Belmont Finance* as authority for the principle that knowing recipient liability under *Barnes v Addy* extends to fiduciary relationships.<sup>323</sup> While uncertainty will prevail in the absence of a definitive statement by the High Court, it is submitted that their Honours’ approach in *Grimaldi* was correct.

It would indeed be an ‘odd result’<sup>324</sup> if the first limb of *Barnes v Addy* was to be strictly applied to trust property only, in circumstances where the second limb is applied more broadly to include other fiduciary relationships. If, as Dietrich and Ridge contend,<sup>325</sup> knowing receipt and knowing assistance are both fault based and necessitate the same level of knowledge, it is difficult to justify the attribution of a higher level of

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<sup>319</sup> *Farah* (2007) 236 ALR 209 at [177]-[178].

<sup>320</sup> *Grimaldi* (2012) 287 ALR 22 at [262], [267].

<sup>321</sup> *Grimaldi* (2012) 287 ALR 22 at [254], [275].

<sup>322</sup> See *Farah* (2007) 287 ALR 22 at [161]-[163]. See earlier discussion above at page 13 in relation to the High Court’s caution in *Farah*.

<sup>323</sup> *Grimaldi* (2012) 287 ALR 22 at [275].

<sup>324</sup> Atkin, above n 80, 723.

<sup>325</sup> Dietrich and Ridge, above n 20, 59-60.

wrongdoing to a person who knowingly receives property derived from a breach of trust, than to a person who knowingly receives property derived from a breach of fiduciary duty. In both instances, the deterrent function of *Barnes v Addy* liability serves to discourage a third party from exploiting the vulnerability of a beneficiary or principal that arises as a result of the trust or fiduciary relationship.<sup>326</sup> The limitation of the first limb of *Barnes v Addy* to trust property in the strict sense would create an arbitrary distinction between knowing recipients of trust property and knowing recipients of corporate property that belies justification.

## 2 Tracing Corporate Property

The process of tracing allows a claimant to assert a claim to an asset held by the defendant on the basis that this asset sufficiently represents an asset that formerly belonged to the claimant.<sup>327</sup> The claimant may trace on the ground that he or she retains a beneficial interest in property handled or received by the defendant (for example, where true trust property is transferred in breach of trust to a third party with knowledge of the breach).<sup>328</sup> It is therefore necessary to identify the original property belonging to the claimant and the nature of the claimant's interest in that property, before considering whether the property currently held by the defendant sufficiently represents that property and the related interest of the claimant.<sup>329</sup> Tracing is a process, rather than a remedy; once tracing is successfully completed, a separate inquiry arises as to what, if any rights the claimant holds in relation to the traced asset.<sup>330</sup>

The Full Court in *Grimaldi* considered that little difficulty arises when following true trust property into the hands of another, due to the 'antecedent entitlement' to the trust property held by the trust beneficiaries as a result of their beneficial ownership of the property.<sup>331</sup> Their Honours considered that the special nature of corporate property,

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<sup>326</sup> Ridge, above n 20, 460.

<sup>327</sup> G E Dal Pont and D R C Chalmers, *Equity and Trusts in Australia* (Lawbook Co, 4<sup>th</sup> ed, 2007) [39.05].

<sup>328</sup> Ibid, [39.05].

<sup>329</sup> Ibid, [39.05].

<sup>330</sup> Ibid, [39.05].

<sup>331</sup> *Grimaldi* (2012) 287 ALR 22 at [562].



however, gives rise to a ‘real difficulty’ in relation to the tracing process.<sup>332</sup> As a company is the sole legal and beneficial owner of its property, where the property is transferred to a bona fide purchaser for value without notice, both the legal and beneficial ownership in the property transfers with the property.<sup>333</sup> However, where the property is transferred in breach of fiduciary duty to a third party with knowledge of that breach, the third party becomes a ‘constructive trustee’ of the misapplied funds.<sup>334</sup> It is the knowledge of the third party of the breach of fiduciary duty that can turn it into a constructive trustee.<sup>335</sup>

According to the New South Wales Court of Appeal in *Evans v European Bank Ltd*,<sup>336</sup> it is this constructive trusteeship that provides the company with the proprietary base necessary to follow its property into the hands of the third party and trace into its substitutes.<sup>337</sup> The constructive trusteeship here is a personal liability, consistent with the use of the term by Lord Selborne in *Barnes v Addy*.<sup>338</sup>

The Full Court in *Grimaldi* accepted *Evans* as authority for the principle that the company lacks a proprietary interest in their misapplied property until the court deems the recipient of the property a constructive trustee.<sup>339</sup> Chin finds this need to impose a constructive trust for the purposes of tracing ‘baffling’.<sup>340</sup> If the company is the beneficial owner of its funds then it retains antecedent property rights in relation to its misapplied funds received by a fiduciary or third party with knowledge, regardless of the imposition or otherwise of the court of a constructive trust over the funds.<sup>341</sup> As a result, Chin considers that the proprietary base needed for tracing exists from the point of the

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<sup>332</sup> *Grimaldi* (2012) 287 ALR 22 at [563].

<sup>333</sup> Dal Pont and Chalmers, above n 327, [39.05].

<sup>334</sup> *Belmont Finance* [1980] 1 All ER 393 at 405; *Grimaldi* (2012) 287 ALR 22 at [563].

<sup>335</sup> *Grimaldi* (2012) 287 ALR 22 at [564]; *Evans v European Bank Ltd* (2004) 61 NSWLR 75 (*Evans*) at [159]-[160].

<sup>336</sup> (2004) 61 NSWLR 75.

<sup>337</sup> *Evans* (2004) 61 NSWLR 75 at [159]-[160].

<sup>338</sup> *Grimaldi* (2012) 287 ALR 22 at [564].

<sup>339</sup> *Grimaldi* (2012) 287 ALR 22 at [566].

<sup>340</sup> Chin, above n 148, 260-261.

<sup>341</sup> *Ibid*, 261.

misapplication of the funds and recovery in property does not depend on the third party recipient being deemed a constructive trustee.<sup>342</sup>

Their Honours in *Grimaldi* did not question the accuracy of *Evans*, instead turning to the question of whether:

If... a proprietary base sufficient to justify following and tracing corporate property turns critically on the court imposing a constructive trust on the property received (the company having no antecedent interest in it in the recipient's hands), the fundamental question becomes whether the court has any discretion not to do so.<sup>343</sup>

Their Honours considered that it did not appear to accord with the accepted principles of appropriate remedy and practical justice (discussed further below) for the court to be required to impose a constructive trusteeship on a third party recipient in all circumstances.<sup>344</sup> As a matter of both proper principle and binding authority, the court is not obliged to impose a constructive trust in circumstances where it is appropriate to leave the company to the personal remedies of an account of profits or equitable compensation.<sup>345</sup>

### *E The Elusive Proprietary Remedy*

#### *1 Principles Governing the Imposition of a Constructive Trust*

The Full Court in *Grimaldi* undertook a substantial analysis of the principles governing the grant of a constructive trust in relation to third party involvement in breaches of fiduciary duty.<sup>346</sup> Their Honours emphasised the discretionary nature of the constructive trust, noting a 'contemporary convergence' in constructive trust claims between the 'principle of appropriateness' (an equitable remedy must be fashioned to fit the nature of

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<sup>342</sup> *Ibid*, 261.

<sup>343</sup> *Grimaldi* (2012) 287 ALR 22 at [566].

<sup>344</sup> *Grimaldi* (2012) 287 ALR 22 at [567].

<sup>345</sup> *Grimaldi* (2012) 287 ALR 22 at [567].

<sup>346</sup> See *Grimaldi* (2012) 287 ALR 22 at [503] ff.

the case and particular facts)<sup>347</sup> and the requirement to do ‘practical justice’ (avoiding transforming the liability of the fiduciary into a vehicle for the unjust enrichment of the plaintiff).<sup>348</sup> They considered that:

in many cases and for many types of equitable wrong, the remedy that is most appropriate will self select absent unusual circumstances.<sup>349</sup>

Their Honours emphasised that this conclusion was not reflective of a lack of discretion on the part of the court, but was instead based on a ‘mixture of learning, intuition and experience’ and the type of remedy that may predictably arise from the application of a particular doctrine.<sup>350</sup> Likewise, their Honours considered that the purpose served by a particular doctrine that gives rise to a constructive trust claim may have a large bearing on the question of what is appropriate in the circumstances of a given case.<sup>351</sup>

Their Honours outlined various considerations of ‘principle and pragmatism’ that bear upon the award or refusal of a constructive trust.<sup>352</sup> They noted what they referred to as the ‘presumptive rule’ in *Hospital Products*:<sup>353</sup> that a fiduciary that has accrued a benefit by breach of duty or misuse of position is liable to account for it, and the appropriate remedy in these circumstances is a constructive trust.<sup>354</sup> Their Honours compared the situation of a third party involved in a breach of fiduciary duty, noting that a like rule in relation to the grant of a proprietary remedy has not been enunciated in relation to the benefits derived by those third parties who participate in breaches of fiduciary duty.<sup>355</sup> Their Honours considered that the reluctance of the courts to impose a constructive trust in relation to third parties may be explained by reference to the obligation that the

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<sup>347</sup> *Grimaldi* (2012) 287 ALR 22 at [503]-[505]; *Warman* (1995) 182 CLR 544 at 559.

<sup>348</sup> *Grimaldi* (2012) 287 ALR 22 at [503]-[505]; *Warman* (1995) 182 CLR 544 at 561.

<sup>349</sup> *Grimaldi* (2012) 287 ALR 22 at [503].

<sup>350</sup> *Grimaldi* (2012) 287 ALR 22 at [503].

<sup>351</sup> *Grimaldi* (2012) 287 ALR 22 at [509], eg, the deterrent principle of imposing strict standards on fiduciaries to protect the principals by nullifying temptation: *Harris v Digital Pulse Pty Ltd* (2003) 56 NSWLR 298 at [407].

<sup>352</sup> *Grimaldi* (2012) 287 ALR 22 at [510].

<sup>353</sup> *Hospital Products* (1984) 156 CLR 41.

<sup>354</sup> *Grimaldi* (2012) 287 ALR 22 at [510]; *Hospital Products* (1984) 156 CLR 41 at [108].

<sup>355</sup> *Grimaldi* (2012) 287 ALR 22 at [510].

fiduciary assumes to prefer the interests of the principal over his or her own interest and the fact that a like obligation is not assumed by the third party.<sup>356</sup>

Their Honours did not consider this lack of undertaking on the part of the third party to pose a bar to the imposition of a constructive trust in relation to knowing recipients of trust property in the strict sense, whom they considered will ordinarily be liable to hold the trust property or its traceable proceeds, plus any attributable profits, on trust for the beneficiary.<sup>357</sup> The Full Court accepted the conclusion in *Zhu v Treasurer of New South Wales*<sup>358</sup> as to the bases for this distinction:

Intervention against a third party who obtains trust property from a trustee in breach of trust is based on the need to protect the proprietary interests of the beneficiaries. Intervention against a third party who obtains some other advantage as a result of the trustee's breach of trust is based on the need to ensure that the trust receives property which, if it were to be acquired at all, should have been acquired for the trust.<sup>359</sup>

However, their Honours considered that the situation is more complicated where the trust property is not trust property in the strict sense, but instead corporate property misapplied in breach of fiduciary duty.<sup>360</sup> As discussed above,<sup>361</sup> this appears to be because their Honours considered that, unlike trust property, where the wronged beneficiary retains beneficial ownership of trust property transferred in breach of trust, and therefore holds a proprietary interest in the misapplied property sufficient to follow it into the hands of others, a wronged corporate principal lacks the necessary proprietary interest over corporate property transferred in breach of fiduciary duty unless and until the court deems the recipient of the property a constructive trustee. This suggests that the special nature of corporate property may pose a further bar to the appropriateness of the

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<sup>356</sup> *Grimaldi* (2012) 287 ALR 22 at [510].

<sup>357</sup> To the extent that such property is extant: *Grimaldi* (2012) 287 ALR 22 at [510]; *Commissioner of Taxation v Macquarie Health Corporation Ltd* (1998) 88 FCR 451 at 497-498.

<sup>358</sup> *Zhu v Treasurer of the State of New South Wales* (2004) 218 CLR 530 ('Zhu').

<sup>359</sup> *Zhu* (2004) 218 CLR 530 at [121]; *Grimaldi* (2012) 287 ALR 22 at [510].

<sup>360</sup> *Grimaldi* (2012) 287 ALR 22 at [510].

<sup>361</sup> See above at page 49, *Tracing Corporate Property*.

constructive trust as a remedy in relation to corporate property received as a result of a breach of fiduciary duty.

Their Honours noted the need to avoid thrusting parties into a continuing business relationship by imposing a constructive trust where it is clear that there is no confidence or comity between the parties.<sup>362</sup> Similarly, they considered that an account of profits may be preferable where an innocent third party may be forced into an unwanted relationship with the claimant should a constructive trust be imposed.<sup>363</sup> Also of importance is the impact of the imposition of a constructive trust to the interests of innocent third parties, even in circumstances where the plaintiff has no other useful remedy against the defendant.<sup>364</sup> Innocent third parties to be considered include not only unsecured creditors,<sup>365</sup> but also those affected because of their legitimate rights, interests or expectations in relation to the property in question,<sup>366</sup> and others generally.<sup>367</sup>

Their Honours considered that the award of a constructive trust must be a proportionate response having regard to the degree of wrongdoing of the defendant and the extent to which the benefit derived was attributable to this wrongdoing.<sup>368</sup> It must not go ‘beyond the necessities of the case’.<sup>369</sup> Ultimately, their Honours considered that proprietary relief must never be mandatory and the court must retain a discretion allowing them to refuse the imposition of a constructive trust in circumstances where a proprietary remedy is inappropriate.<sup>370</sup>

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<sup>362</sup> *Grimaldi* (2012) 287 ALR 22 at [510]; *Warman* (1995) 182 CLR 544 at 544, 564.

<sup>363</sup> *Grimaldi* (2012) 287 ALR 22 at [510].

<sup>364</sup> *Grimaldi* (2012) 287 ALR 22 at [508], [510]; *John Alexander's Clubs Pty Ltd v White City Tennis Club Ltd* (2010) 241 CLR 1 (*John Alexander's Clubs*) at [128]-[129].

<sup>365</sup> *Grimaldi* (2012) 287 ALR 22 at [510]; *Muschinski v Dodds* (1985) 160 CLR 583 at 523.

<sup>366</sup> *Grimaldi* (2012) 287 ALR 22 at [510]; *Giumelli v Giumelli* (1999) 196 CLR 101 at [49]-[50].

<sup>367</sup> *Grimaldi* (2012) 287 ALR 22 at [510]; *John Alexander's Clubs* (2010) 241 CLR 1 at [129].

<sup>368</sup> *Grimaldi* (2012) 287 ALR 22 at [510].

<sup>369</sup> *Grimaldi* (2012) 287 ALR 22 at [510]; *John Alexander's Clubs* (2010) 241 CLR 1 at [129].

<sup>370</sup> *Grimaldi* (2012) 287 ALR 22 at [511].

## *2 Was Winterfall Liable as a Constructive Trustee?*

The Full Court disagreed with Jacobson J's characterisation of the benefit received by Winterfall as a result of its knowing receipt of the Chameleon cheque funds. Jacobson J had considered that Winterfall had received the same benefit as Murchison, that being 'the benefit of the investment of the funds as part of a pool of working capital, comprising debt and equity'.<sup>371</sup> The Full Court instead found that the benefit obtained by Winterfall through the misapplied funds was in fact an interest in the Iron Jacks tenements themselves.<sup>372</sup>

In accordance with their Honours' conclusion that the grant of a proprietary remedy must remain discretionary, the Full Court rejected Chameleon's claim that it was entitled as of right to the imposition of a constructive trust on the cheques received by Winterfall, which could then be traced into the Iron Jack tenements.<sup>373</sup> Their Honours considered that, as the cheque funds were corporate property, rather than true trust property, it was necessary for the court to impose a constructive trust over the funds before they could be traced into the Iron Jack tenements.<sup>374</sup> Before the court could impose the necessary constructive trust, it was required to be satisfied that proprietary relief must be the appropriate form of relief in the circumstances.<sup>375</sup> While noting that proprietary relief may well be expected to be the appropriate relief in a knowing receipt case, such as this one, where the property received or its traceable proceeds remained wholly or partly extant, their Honours declared this to be an 'exceptional case', largely as a result of the events transpiring after Winterfall's receipt of the cheque money.<sup>376</sup>

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<sup>371</sup> *Grimaldi* (2012) 287 ALR 22 at [662].

<sup>372</sup> *Grimaldi* (2012) 287 ALR 22 at [740].

<sup>373</sup> *Grimaldi* (2012) 287 ALR 22 at [668].

<sup>374</sup> *Grimaldi* (2012) 287 ALR 22 at [669].

<sup>375</sup> *Grimaldi* (2012) 287 ALR 22 at [669].

<sup>376</sup> *Grimaldi* (2012) 287 ALR 22 at [670]; *Streeter v Western Areas Exploration Pty Ltd (No 2)* (2011) 278 ALR 291 at [682].

Their Honours identified a number of factors that together formed the basis for their conclusion that proprietary relief was inappropriate in the circumstances and would go well beyond the necessities of the case.<sup>377</sup>

Firstly, they considered that the instalment payment made with the cheque funds had to be considered in the context in which it was made; its proper complexion in this context was that it was part of the outlays made and activities engaged in or foreshadowed in anticipation of the Iron Jack mining operation (the ‘Project’), rather than simply a purchase of the Iron Jack asset.<sup>378</sup> This suggests that the characterisation of the transaction in which misapplied corporate funds are used by the knowing recipient is relevant to the consideration of whether a grant of proprietary relief may be appropriate in the circumstances.

Their Honours also considered that it was not appropriate to disregard or give diminished significance to other matters (such as Winterfall’s financial need that drove it to accept money in circumstances where it shouldn’t have) where the reason for awarding proprietary relief was not to discipline a misbehaving fiduciary.<sup>379</sup> In this sense, while the liability of a fiduciary to account for benefits obtained in breach of trust is strict, and the ‘presumptive’ rule is that the appropriate remedy is by way of constructive trust,<sup>380</sup> it appears that the remoteness of the third party may allow for greater consideration of mitigating circumstances in relation to the appropriateness or otherwise of imposing a constructive trust.<sup>381</sup>

While their Honours noted that the ‘capital base’ of Winterfall had been corrupted by the receipt of the Chameleon funds, this base had grown enormously as a result of subsequent additions of debt and equity finance contributed in good faith and by reinvested profits; Winterfall had evolved substantially since the receipt of the Chameleon funds, and *Grimaldi* was not simply a ‘case of wrongdoers continuing

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<sup>377</sup> *Grimaldi* (2012) 287 ALR 22 at [672], [681].

<sup>378</sup> *Grimaldi* (2012) 287 ALR 22 at [673].

<sup>379</sup> *Grimaldi* (2012) 287 ALR 22 at [674].

<sup>380</sup> *Grimaldi* (2012) 287 ALR 22 at [510]; *Hospital Products* (1984) 156 CLR 41 at [108].

<sup>381</sup> Chin, above n 148, 254.

knowingly to perpetuate their own wrongs to their own advantage behind a corporate form'.<sup>382</sup> Chin notes the emphasis that their Honours placed in *Grimaldi* on changes in the governance and capital base of both Winterfall and Murchison following the wrongdoing of the parties.<sup>383</sup> Considerations such as the removal of Grimaldi from Murchison's board of directors following the reverse takeover of Winterfall, the different, 'less damning' state of mind of the new directors, and changes in the capital base of the parties were relevant to the question of appropriate relief and appeared to have a mitigating influence on the choice between proprietary and personal relief.<sup>384</sup>

Also relevant was the consideration that the wrongdoing in *Grimaldi* did not involve the diversion of a corporate opportunity from Chameleon at its expense. Likewise, Winterfall did not act over time to Chameleon's detriment.<sup>385</sup> Chameleon's interests were directed primarily to gold, not the iron ore to which the Iron Jack tenements related.<sup>386</sup>

Their Honours noted that, following the misapplication of Chameleon's funds, the value of the Project had been significantly enhanced by investors, who should be properly considered innocent third parties. Expenditure to develop the Project and related capital raising since the misapplication of Chameleon's funds dwarfed the involuntary contribution of Chameleon by millions of dollars.<sup>387</sup> It was also relevant that Chameleon had not assumed any of the risk related to the Project, nor contributed to the enterprise or expertise required for the Project, including exploration and analysis costs, expenditure on infrastructure, solving of infrastructure problems, and the Project itself (which was undertaken in a climate of market volatility), all of which helped give value to the tenement rights acquired by Winterfall.<sup>388</sup>

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<sup>382</sup> *Grimaldi* (2012) 287 ALR 22 at [675].

<sup>383</sup> Chin, above n 148, 257-258.

<sup>384</sup> *Ibid*, 260-261; *Grimaldi* (2012) 287 ALR 22 at [487].

<sup>385</sup> *Grimaldi* (2012) 287 ALR 22 at [676].

<sup>386</sup> *Grimaldi* (2012) 287 ALR 22 at [676].

<sup>387</sup> *Grimaldi* (2012) 287 ALR 22 at [677].

<sup>388</sup> *Grimaldi* (2012) 287 ALR 22 at [679].



Given that the increase in value of the Iron Jack tenements had resulted primarily from the contributions, industry and risk-taking of Murchison, Winterfall and investors, their Honours considered that the award of a constructive trust in the circumstances would be a punitive measure against Winterfall and would transform Winterfall's recipient liability into a vehicle for the unjust enrichment of Chameleon.<sup>389</sup> To give Chameleon a proportionate interest in the Iron Jack tenements would also thrust the parties into a business relationship where there was unlikely to be comity or confidence between them.<sup>390</sup> The prospect of dispute, disruption and destabilisation of an established mining operation and associated infrastructure development in the circumstances was considered self-evident.<sup>391</sup>

Their Honours' conclusions highlight the difficulty that a claimant faces in establishing circumstances appropriate to the award of a proprietary remedy in relation to the benefits derived by knowing recipients and knowing assistants. As Chin notes, a right is only as valuable as the remedies.<sup>392</sup> Of no small interest in *Grimaldi* is the commercial impetus of Chameleon's claim. Chameleon, a small, start-up mining company, had funds of some \$277,840 misappropriated in breaches of fiduciary duty by Barnes and Grimaldi with no further losses by way of a diversion of corporate opportunity or otherwise.<sup>393</sup> Yet, as Jacobson J noted in his first instance decision, Chameleon's claim to a constructive trust was 'a very large one'.<sup>394</sup> As the \$660 million value of Murchison at the time of trial was considered to be almost solely attributable to Murchison's interest in the Iron Jack Project, Chameleon's claim for a constructive trust over the entirety of Murchison's shareholding in Winterfall amounted to many hundreds of millions of dollars.<sup>395</sup> Jacobson J noted that even a claim by Chameleon for a proportionate interest in the tenements (on the basis of the proportion that the misapplied Chameleon funds bore to the total consideration paid for the tenements by Winterfall) would amount to

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<sup>389</sup> *Grimaldi* (2012) 287 ALR 22 at [680].

<sup>390</sup> *Grimaldi* (2012) 287 ALR 22 at [679].

<sup>391</sup> *Grimaldi* (2012) 287 ALR 22 at [679].

<sup>392</sup> Chin, above n 148, 261.

<sup>393</sup> *Grimaldi* (2012) 287 ALR 22 at [676].

<sup>394</sup> *Chameleon* [2010] FCA 1129 at [922].

<sup>395</sup> *Chameleon* [2010] FCA 1129 at [922].

about \$160 million.<sup>396</sup> Murchison characterised Chameleon's claim as 'an egregious attempt at gold digging'.<sup>397</sup>

Their Honours in *Grimaldi* emphasised that the liability of the fiduciary or third party participant to account for benefits obtained from the relevant breach of duty must be appropriate to the circumstances of the case, and must not be 'transformed into a vehicle for the unjust enrichment of the plaintiff'.<sup>398</sup> As such, *Grimaldi* provides support for the proposition that so-called 'opportunistic' claims over a commercially valuable asset that can be linked to a breach of fiduciary duty will have limited prospects of providing a financial windfall to the claimant.

#### *F Is Third Party Liability Joint and Several?*

The Full Court noted that there are subsisting uncertainties as to whether and/or when the liabilities of knowing assistants and knowing recipients are joint and several with those of the breaching fiduciary.<sup>399</sup> Their Honours were not required to consider the question of whether third party liability in relation to the losses of the principal was joint and several, or several only.<sup>400</sup> However, they expressed the view that such liability remained several only<sup>401</sup> without further elaboration as to the reasons for their conclusion.

Their Honours supported Ridge's view of the general inappropriateness of joint and several liability of the third party for the gains of the breaching fiduciary,<sup>402</sup> noting that the liability of third parties for profits or gains arising from a breach of fiduciary duty is ordinarily several only.<sup>403</sup> The Full Court considered criticism of Canadian authority

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<sup>396</sup> *Chameleon* [2010] FCA 1129 at [922].

<sup>397</sup> *Chameleon* [2010] FCA 1129 at [923].

<sup>398</sup> *Grimaldi* (2012) 287 ALR 22 at [503]; *Warman* (1995) 182 CLR 544 at 559, 561.

<sup>399</sup> *Grimaldi* (2012) 287 ALR 22 at [553].

<sup>400</sup> *Grimaldi* (2012) 287 ALR 22 at [559].

<sup>401</sup> *Grimaldi* (2012) 287 ALR 22 at [559].

<sup>402</sup> See above at page 26, *Justifying Third Party Liability*.

<sup>403</sup> *Grimaldi* (2012) 287 ALR 22 at [557]; *Warman* (1995) 182 CLR 544 at 569.

supporting joint and several liability in ordinary cases to be justified on the basis that such liability could be considered penal.<sup>404</sup>

However, the Full Court noted two extraordinary cases in which joint and several liability may be imposed. The first is where the third party is the alter ego or ‘nominee’ of the fiduciary; in such circumstances, it is settled that the third party will be jointly and severally liable for any gains of the fiduciary.<sup>405</sup> The second case is less certain, and occurs where the fiduciary and third party act in concert to misappropriate trust property or breach fiduciary duty to secure a mutual benefit.<sup>406</sup> Neither line of extraordinary cases applied to the actions of Murchison or Winterfall in *Grimaldi*; both companies were held severally liable only for the profits derived from their involvement in Barnes and Grimaldi’s breaches of fiduciary duty.<sup>407</sup>

#### G *The Rescission Requirement*

In *Grimaldi*, Murchison and Chameleon agreed that, if in fact the cheque payments by Chameleon to Murchison constituted a loan on the running loan account between Chameleon and Murchison, the rescission requirement mandated that Chameleon could not assert equitable title to the cheque funds or to the assets into which they could be traced, or seek relief against third parties by way of tracing, unless and until Chameleon avoided the loan by seeking an order for rescission.<sup>408</sup> While the Full Court upheld Jacobson J’s finding that the misapplied Chameleon cheque funds were not loans,<sup>409</sup> they noted the ‘curious consequence’ of the rescission requirement.<sup>410</sup>

The curiosity appears to arise from the fact that, while the mere form of a transaction such as a loan or purchase cannot ‘stay the hand of equity’ for the purposes of recipient

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<sup>404</sup> *Grimaldi* (2012) 287 ALR 22 at [557].

<sup>405</sup> *Grimaldi* (2012) 287 ALR 22 at [556].

<sup>406</sup> *Grimaldi* (2012) 287 ALR 22 at [558].

<sup>407</sup> *Grimaldi* (2012) 287 ALR 22 at [742].

<sup>408</sup> *Grimaldi* (2012) 287 ALR 22 at [271], [273].

<sup>409</sup> *Grimaldi* (2012) 287 ALR 22 at [335].

<sup>410</sup> *Grimaldi* (2012) 287 ALR 22 at [276].

liability under *Barnes v Addy*,<sup>411</sup> a constructive trust cannot simply be imposed over the funds acquired by a third party who knowingly receives the fund through a contract of loan or purchase entered into in breach of fiduciary duty.<sup>412</sup> While the contract must be rescinded before proprietary relief may be granted, there is no rescission requirement where a personal remedy such as an account of profits is sought.<sup>413</sup>

The Full Court noted that the ‘understanding of the use of the constructive trust as a remedy... has evolved in recent times’,<sup>414</sup> and considered that this may well lead to a review of the rescission requirement in relation to third party knowing receipt.<sup>415</sup> In reference to the evolved understanding of the constructive trust as a remedy, their Honours cited *Bathurst City Council v PWC Properties Pty Ltd*,<sup>416</sup> where the High Court stated that:

before the court imposes a constructive trust as a remedy, it should first decide whether, having regard to the issues in the litigation, there are other means available to quell the controversy. *An equitable remedy which falls short of the imposition of a trust may assist in avoiding a result whereby the plaintiff gains a beneficial proprietary interest which gives an unfair priority over other equally deserving creditors of the defendant.*<sup>417</sup>

In situations where a wronged principal effectively avoids a transaction on the basis that it was effected in breach of fiduciary duty, the third party recipient is considered to hold the property on constructive trust for the principal. This generates a proprietary interest in favour of the principal, which may be unfair to innocent third parties, including perhaps innocent creditors of the third party in circumstances where the third party becomes insolvent.

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<sup>411</sup> *Grimaldi* (2012) 287 ALR 22 at [276]; *Robins* (2003) 175 FLR 286 at [65]-[67].

<sup>412</sup> *Grimaldi* (2012) 287 ALR 22 at [277].

<sup>413</sup> *Grimaldi* (2012) 287 ALR 22 at [277]; *Greater Pacific Investments* (1996) 39 NSWLR 143 at 153E-154.

<sup>414</sup> *Grimaldi* (2012) 287 ALR 22 at [281].

<sup>415</sup> *Grimaldi* (2012) 287 ALR 22 at [281].

<sup>416</sup> (1998) 195 CLR 566 (*‘Bathurst City Council’*).

<sup>417</sup> *Bathurst City Council* (1998) 195 CLR 566 at 585 (emphasis added).

Importantly, their Honours noted that, regardless of any prior title that a person may be able to assert over property following rescission, the key question remains whether a constructive trust is the appropriate remedy in the circumstances.<sup>418</sup> Implicit in their Honours' reasoning is that the constructive trust that arises following the effective rescission of the contract should not arise as a matter of right, but should instead be considered discretionary. This is consistent with the approach of their Honours to the question of whether the court retains a discretion to impose a constructive trust over corporate property misapplied in breaches of fiduciary duty if such a trust is necessary to provide a proprietary base to the company for the purposes of following and tracing the property. As noted above, in those circumstances their Honours concluded that, both as a matter of principle and authority, the imposition of the constructive trust is discretionary.<sup>419</sup>

Their Honours' view is also consistent with that of Gibbs CJ in *Daly*. As noted above, the Full Court of the Supreme Court of Western Australia in *Hancock* considered it to be clear from the reasoning of Gibbs CJ that a constructive trust is not automatically imposed upon money lent in circumstances that give rise to a breach of fiduciary duty following the rescission of the contract of loan.<sup>420</sup> While a constructive trust may be awarded as a discretionary remedy, such a remedy will not be granted where it is beyond what is necessary to do equity in the circumstances.<sup>421</sup>

Despite their apparent concerns that the operation of the rescission requirement may provide an unfair priority to the claimant, hence going beyond what is necessary to do equity, their Honours in *Grimaldi* endorsed the rescission requirement as it currently stands as a matter of comity with the views of the New South Wales Court of Appeal in *Robins* and the Full Court of the Western Australian Supreme Court in *Hancock*.<sup>422</sup>

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<sup>418</sup> *Grimaldi* (2012) 287 ALR 22 at [281].

<sup>419</sup> *Grimaldi* (2012) 287 ALR 22 at [567].

<sup>420</sup> *Hancock* (2000) 22 WAR 198 at [177]; *Bell Group* (2008) 39 WAR 1 at [4788].

<sup>421</sup> *Bell Group* (2008) 39 WAR 1 at [4788]; *Hancock* (2000) 22 WAR 198 at [177].

<sup>422</sup> *Grimaldi* (2012) 287 ALR 22 at [281].

## H Assessing the Profit in a Mining Venture

The Full Court in *Grimaldi* overturned Jacobson J's orders in relation to Murchison and Winterfall's liability to account for profits derived from their use of Chameleon's funds.<sup>423</sup> In the case of Winterfall, their Honours considered that Jacobson J had erred in his assessment of the benefit derived from the use of Chameleon's funds.<sup>424</sup> In the case of Murchison, their Honours considered that Jacobson J had wrongly declined to include a consideration of expected future profits in his orders,<sup>425</sup> and questions remained as to whether Murchison should be awarded a just allowance in relation to the profits earned.<sup>426</sup> The Full Court declined to provide substituted orders on the basis that the parties be afforded a chance to make further submissions as to the appropriate orders, and instead remitted the matter back to the trial judge for reconsideration.<sup>427</sup>

Their Honours comments provide a significant amount of guidance as to how profits in a mining venture may best be assessed. The fundamental principle in any account of profits is that the account must be confined to profits actually made, so as not to result in the unjust enrichment of the claimant.<sup>428</sup> In *Grimaldi*, their Honours considered that Chameleon's money had been used to establish a mining business,<sup>429</sup> bringing *Grimaldi* within the ambit of the *Docker v Somes*<sup>430</sup> line of cases.

*Docker v Somes* was concerned with the recovery of trust money improperly introduced into a trade or business.<sup>431</sup> It established the principle that, in such cases, the beneficiaries were entitled to insist upon a share of the profits made from the business, rather than interest only on the amount of trust money employed in the business.<sup>432</sup> In circumstances where the entirety of the business was attributable to the trust funds, the

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<sup>423</sup> *Grimaldi* (2012) 287 ALR 22 at [744].

<sup>424</sup> *Grimaldi* (2012) 287 ALR 22 at [740].

<sup>425</sup> *Grimaldi* (2012) 287 ALR 22 at [738].

<sup>426</sup> *Grimaldi* (2012) 287 ALR 22 at [738], [730]-[732].

<sup>427</sup> *Grimaldi* (2012) 287 ALR 22 at [743]-[744].

<sup>428</sup> *Dart Industries Inc v Décor Corporation Pty Ltd* (1993) 179 CLR 101 at 114-115; Dal Pont and Chalmers, above n 327, [34.125].

<sup>429</sup> *Grimaldi* (2012) 287 ALR 22 at [519].

<sup>430</sup> (1834) 2 My & K 655; 39 ER 1095.

<sup>431</sup> *Grimaldi* (2012) 287 ALR 22 at [519].

<sup>432</sup> *Grimaldi* (2012) 287 ALR 22 at [520].

beneficiary was entitled to the entirety of the profits.<sup>433</sup> Where the profit derived from the business was attributable in part to the skill and labour of the trustee in the development of the business, apportionment was authorised.<sup>434</sup> However, in cases where serious difficulty was encountered in tracing and apportioning the profits of the business, a fixed rate of interest was considered perhaps the more appropriate remedy.<sup>435</sup>

As an alternative to apportioning the profits of a business, the court may award a just allowance to the fiduciary.<sup>436</sup> When utilising this method, the court will ordinarily deduct an amount representing the contribution, skill and industry of the fiduciary in making the profits from the total amount of profits made, before dividing the profits between the fiduciary and beneficiary in proportion to the percentage that the trust money represented to the total capital invested.<sup>437</sup>

The Full Court in *Grimaldi* noted that modern Australian authority follows the *Docker v Somes* line of cases.<sup>438</sup> As stated by the High Court in *Warman*,<sup>439</sup> it would be inequitable to order a breaching fiduciary to account for the entirety of the profits where a portion of the profits is attributable to the fiduciary's skill, efforts, property and resources.<sup>440</sup> The onus of establishing the inequity lies with the fiduciary.<sup>441</sup>

While their Honours found the *Docker v Somes* line of cases instructive, they emphasised the relevance of the distinctive character of mining businesses in determining the profit received as a result of a breach of fiduciary duty or trust involving a mining business.<sup>442</sup> Mining businesses are inherently risky and involve time, care, attention, skill, expenditure and the investment of risk capital to develop.<sup>443</sup> The nature

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<sup>433</sup> *Docker v Somes* (1834) 2 My & K 655; 39 ER 1095 at 664-665; ER 1098.

<sup>434</sup> *Docker v Somes* (1834) 2 My & K 655; 39 ER 1095 at 666; ER 1099.

<sup>435</sup> *Docker v Somes* (1834) 2 My & K 655; 39 ER 1095 at 673; ER 1101.

<sup>436</sup> *Grimaldi* (2012) 287 ALR 22 at [529].

<sup>437</sup> *Dal Pont and Chalmers*, above n 327, [34.130]; *Grimaldi* (2012) 287 ALR 22 at [529].

<sup>438</sup> *Grimaldi* (2012) 287 ALR 22 at [528].

<sup>439</sup> *Warman* (1995) 182 CLR 544.

<sup>440</sup> *Warman* (1995) 182 CLR 544 at 561; *Grimaldi* (2012) 287 ALR 22 at [528].

<sup>441</sup> *Warman* (1995) 182 CLR 544 at 561; *Grimaldi* (2012) 287 ALR 22 at [528].

<sup>442</sup> *Grimaldi* (2012) 287 ALR 22 at [519], [537].

<sup>443</sup> *Grimaldi* (2012) 287 ALR 22 at [538]-[539].

of the mining business has a direct bearing on the attribution of profits to capital investment, expertise, exertion and the assumption of risk incurred in generating profits.<sup>444</sup>

In particular, their Honours noted the US case of *Primeau v Granfield*.<sup>445</sup> This case involved the wrongful use of money held on trust for Primeau in the development of the trustee's own gold mine. The trust money was later returned and a claim made by Primeau for an account of the benefit received by the trustee as a result of his breach of trust. Learned Hand LJ determined that Primeau's money had been used to acquire rights to explore for, extract, transport and sell gold.<sup>446</sup> His Lordship refused the remedy of a constructive trust, instead awarding an account of profits in Primeau's favour. The benefit derived from the use of the trust money, for which the trustee was accountable to Primeau, was the profits of the business proportionate to the amount that Primeau's money represented to the total consideration paid for the mining rights, after taking into account the expenditure by the trustee that 'gave those rights their value'.<sup>447</sup> His Lordship determined that Primeau was entitled to:

that proportion of the value of the ore in situ, as is represented by his contribution to the total expenses of working, plus the total rentals or royalties paid the lessor.<sup>448</sup>

Primeau was also entitled to interest on these sums, calculated from the date that his trust money was received by the trustee.<sup>449</sup> The accounting liability was a continuing one, not limited to the date of judgment.<sup>450</sup> No part of the profits made by the trustee was attributable to sources other than capital.<sup>451</sup> In other words, no allowance had been made in favour of the trustee for their skill and labour in working the gold mine.<sup>452</sup>

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<sup>444</sup> *Grimaldi* (2012) 287 ALR 22 at [540].

<sup>445</sup> 184 F 480 (SDNY 1911), the 'leading authority in US jurisprudence on constructive trusts': *Grimaldi* (2012) 287 ALR 22 at [541].

<sup>446</sup> *Grimaldi* (2012) 287 ALR 22 at [545].

<sup>447</sup> *Grimaldi* (2012) 287 ALR 22 at [545].

<sup>448</sup> *Primeau v Granfield* 184 F 480 (SDNY 1911) at 486-487; *Grimaldi* (2012) 287 ALR 22 at [544].

<sup>449</sup> *Primeau v Granfield* 184 F 480 (SDNY 1911) at 486-487.

<sup>450</sup> *Grimaldi* (2012) 287 ALR 22 at [546].

<sup>451</sup> *Grimaldi* (2012) 287 ALR 22 at [730].

<sup>452</sup> See *Grimaldi* (2012) 287 ALR 22 at [730].



Their Honours applied *Primeau v Granfield* when assessing the personal remedy to which they considered Chameleon was entitled as a result of Winterfall's use of Chameleon's funds in the acquisition of the Iron Jacks tenements.<sup>453</sup> However, their Honours entertained the possibility that a just allowance for the skill, risk-taking and exertion of Winterfall in developing the mining business may be appropriate.<sup>454</sup> They considered that Chameleon was entitled to relief from Winterfall by way of a proportionate share in the net profits from ore found, extracted, transported and marketed and sold which had been, or would be, extracted over the life of the Iron Jack Project, less the costs of finding, etc that ore and, arguably, less any such allowance as Winterfall may be allowed for its skill, risk-taking and exertion in finding, etc, the ore.<sup>455</sup> Their Honours suggested that this benefit may best be reflected in a royalty-like payment on the ore extracted.<sup>456</sup>

Their Honours also considered Murchison was required to account for profits derived from the Iron Jack Project over the life of the project, and not limited to the date of judgment.<sup>457</sup> Their Honours noted that Murchison's benefits appeared to flow from its ownership of Winterfall.<sup>458</sup> However, despite the subsidiary and parent relationship of Winterfall and Murchison following the reverse takeover, the liability of each party to account was several, with each only required to account for the benefit actually received by them as a result of the Chameleon funds misused by them, and not for any benefit derived by the other.<sup>459</sup> Likewise, any allowances to be granted in relation to either account of profits were limited to the skill (etc) of the party to whom the account related.<sup>460</sup>

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<sup>453</sup> *Grimaldi* (2012) 287 ALR 22 at [727].

<sup>454</sup> *Grimaldi* (2012) 287 ALR 22 at [743].

<sup>455</sup> *Grimaldi* (2012) 287 ALR 22 at [740].

<sup>456</sup> *Grimaldi* (2012) 287 ALR 22 at [740].

<sup>457</sup> *Grimaldi* (2012) 287 ALR 22 at [739].

<sup>458</sup> *Grimaldi* (2012) 287 ALR 22 at [741].

<sup>459</sup> *Grimaldi* (2012) 287 ALR 22 at [742].

<sup>460</sup> *Grimaldi* (2012) 287 ALR 22 at [742].

One final point requires consideration in relation to the assessment of profits derived from a mining venture. The total consideration paid by Winterfall for the Iron Jack tenements included a royalty payment to the vendors of 80 cents per tonne of ore.<sup>461</sup> Jacobson J considered that the royalty payment was irrelevant in calculating the proportion that Chameleon's misapplied funds represented to the total consideration paid for the Iron Jack tenements.<sup>462</sup> Although not in issue on appeal, their Honours noted in *obiter* that the royalty payment was in fact relevant to this consideration.<sup>463</sup> Given the prevalence of royalty-type arrangements in mining ventures, this point is an important one to bear in mind when attempting to apportion profits derived from a mining business.

### *I Cumulative Equitable and Statutory Remedies Against Third Parties*

Section 1317H of the *Corporations Act 2001* (Cth) (the 'Corporations Act') provides that a court may order a person to compensate a company where the person has contravened a civil penalty provision of the Corporations Act in relation to the company and the company has suffered damage as a result.<sup>464</sup> 'Damage' may include profits made by any person resulting from the contravention.<sup>465</sup> Section 185 of the Act provides that sections 180-184 of the Act (the statutory directors' duties provisions) operate in addition to, and not in derogation of, any general law relating to the duty or liability of a person because of their office or employment in relation to a corporation.<sup>466</sup>

As a result of the operation of section 185, where a director or officer's breach of fiduciary duty also results in a contravention of a civil penalty provision of the Corporations Act, it is open to a corporation to claim both an equitable remedy (such as an account of profits) and statutory compensation (potentially including profits) in

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<sup>461</sup> *Grimaldi* (2012) 287 ALR 22 at [735].

<sup>462</sup> *Grimaldi* (2012) 287 ALR 22 at [735].

<sup>463</sup> *Grimaldi* (2012) 287 ALR 22 at [735].

<sup>464</sup> *Corporations Act 2001* (Cth), s 1317H.

<sup>465</sup> *Corporations Act 2001* (Cth), s 1317H(2). The Full Court in *Grimaldi* determined that the court is merely empowered, rather than obliged, to include damages in an assessment of compensation: *Grimaldi* (2012) 287 ALR 22 at [631].

<sup>466</sup> *Corporations Act 2001* (Cth), s 185.

relation to the breaches.<sup>467</sup> In many cases, the profits claimed in relation to an account of profits and statutory compensation will be the same.<sup>468</sup> While the corporation is not required to elect between statutory and equitable remedies, it is prevented from double recovery in respect of the same profits.<sup>469</sup> Accordingly, section 185 is held to permit cumulative remedies.<sup>470</sup>

In *Grimaldi*, the position was less clear in relation to third parties involved in breaches of duty. Under section 79 of the Act, a third party who aids, abets, counsels, procures, induces, is knowingly concerned in, or has conspired with others to effect a contravention of the Corporations Act may be liable for involvement in another's contravention of the Act.<sup>471</sup> Section 83 of the Act imputes liability for contraventions of the Act to those deemed to be involved in the contravention under section 79.<sup>472</sup>

In his first instance decision, Jacobson J deemed Murchison to be involved in Barnes and Grimaldi's contraventions of the Corporations Act by virtue of sections 79(a) and (c) of the Act.<sup>473</sup> The Full Court upheld this finding on appeal.<sup>474</sup> As a result of his finding, Jacobson J considered that Barnes and Grimaldi's breaches of sections 181 and 182 of the Corporations Act were imputed to Murchison and a compensation order, including profits, was made against Murchison under section 1317H.<sup>475</sup> His Honour framed the orders so that the statutory compensation order operated cumulatively with the orders requiring Murchison to account for profits acquired through its participation in Barnes and Grimaldi's breaches of fiduciary duty.

Murchison challenged these orders on appeal on the basis of the formulation of section 185 of the Act. Murchison argued that, because section 185 did not explicitly deal with

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<sup>467</sup> *Grimaldi* (2012) 287 ALR 22 at [640].

<sup>468</sup> *Grimaldi* (2012) 287 ALR 22 at [641].

<sup>469</sup> *Grimaldi* (2012) 287 ALR 22 at [641]; *Re HIH Insurance; ASIC v Adler* (2002) 168 FLR 253 at [116]-[118].

<sup>470</sup> *Grimaldi* (2012) 287 ALR 22 at [641].

<sup>471</sup> *Corporations Act 2001* (Cth), s 79.

<sup>472</sup> *Corporations Act 2001* (Cth), s 83.

<sup>473</sup> *Chameleon* [2010] FCA 1129 at [707].

<sup>474</sup> *Grimaldi* (2012) 287 ALR 22 at [345].

<sup>475</sup> *Chameleon* [2010] FCA 1129 at [1105].

third parties, and no alternative provision in the Act sanctioned cumulative equitable and statutory remedies in relation to third parties, Chameleon should be required to elect between statutory compensation and an account of profits, and should not be allowed a cumulative remedy.<sup>476</sup>

The Full Court considered that the lack of explicit authorisation in the Corporations Act for cumulative statutory and general law remedies against involved third parties did not prevent such orders from being given,<sup>477</sup> and rejected Murchison's contention that, absent an express statutory provision recognising the co-existence of other remedies, the statutory and equitable liabilities were alternatives.<sup>478</sup> Their Honours noted that, while the statutory and equitable remedies may produce similar or overlapping results in given cases, it had not been suggested that they would provide identical relief in all circumstances.<sup>479</sup> Likewise, their Honours could see no reason why the policy objectives of section 185 should not apply equally to both an involved third party and breaching fiduciary.<sup>480</sup> Their Honours concluded that the statutory and equitable remedies could operate cumulatively in relation to involved third parties, subject to the preclusion of double recovery.<sup>481</sup>

It is submitted that their Honours' conclusion is correct. As their Honours noted, Murchison was liable on two distinct bases,<sup>482</sup> each of which provides its own remedy system.<sup>483</sup> No provision of the Corporations Act precludes the award of a general law remedy where a statutory remedy has been granted in these circumstances, or vice versa. While the remedies may relate to similar, if not the same, profits in many situations, there is no reason why a cumulative remedy may not be granted where there are differences between the profits in question, provided that no double recovery of profits

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<sup>476</sup> *Grimaldi* (2012) 287 ALR 22 at [645].

<sup>477</sup> *Grimaldi* (2012) 287 ALR 22 at [647].

<sup>478</sup> *Grimaldi* (2012) 287 ALR 22 at [649].

<sup>479</sup> *Grimaldi* (2012) 287 ALR 22 at [685].

<sup>480</sup> *Grimaldi* (2012) 287 ALR 22 at [649].

<sup>481</sup> *Grimaldi* (2012) 287 ALR 22 at [648].

<sup>482</sup> That is, knowing receipt and knowing assistance in equity, and as a person involved in a contravention of the Corporations Act under statute.

<sup>483</sup> *Grimaldi* (2012) 287 ALR 22 at [648].

occurs. To put a wronged principal to election between general law and statutory remedies in such circumstances may require the principal to forfeit its claim to a portion of the profit derived from the breach of duty, effectively resulting in the retention of a benefit obtained by the third party in circumstances where they have acted wrongfully both in the eyes of equity and under statute.

## VI CONCLUSION

The decision in *Grimaldi* provides further force to the argument that third party liability is a fault based, primary liability driven by equity's concern with the third party's own wrongdoing. While there remains a distinction between the two limbs of *Barnes v Addy* in the sense that dishonesty is required on the part of the fiduciary to trigger liability for knowing assistance, but not for knowing receipt, there is no further distinction in relation to the level of knowledge required of the third party or the remedies that may be awarded against the third party. For now, the English position of *Royal Brunei* has been rejected in Australia and third party liability is clearly based on what the third party knew, or had reason to know, of the breach of duty or the dishonest and fraudulent design of the fiduciary.

While we await confirmation from the High Court that the first limb of *Barnes v Addy* extends beyond breaches of trust to include other breaches of fiduciary duty, it otherwise appears all but resolved that the *Belmont Finance* characterisation of corporate property in relation to *Barnes v Addy* liability has been adopted in Australia. Unresolved questions remain, however, in relation to the special nature of corporate property in this regard, including whether the court is required to impose a constructive trust over corporate property misapplied in breach of fiduciary duty before a company will hold a sufficient proprietary interest to trace the property; and whether the rescission requirement in its current formulation should be retained in relation to third party involvement in breaches of fiduciary duty.

Perhaps most significantly, the decision in *Grimaldi* illustrates the difficulty that a company may face in obtaining a proprietary remedy in relation to company property misapplied in breach of fiduciary duty, or property derived by a third party in their own right as a result of their participation in a breach of fiduciary duty. Proprietary remedies in relation to third parties are clearly discretionary, and should not be awarded where a lesser remedy will be sufficient to do equity. The remoteness of the third party to the

principal (as compared to the close relationship between the principal and fiduciary) appears to have a significant bearing on the appropriateness or otherwise of awarding a proprietary remedy, as does the impact of a proprietary remedy upon innocent third parties.

The characterisation of the benefit flowing to the third party as a result of the breach of fiduciary duty is also significant. Where corporate property is misappropriated and used in the development of a business, the nature of the business may be relevant to both the appropriateness of a proprietary remedy, and consideration of the profits obtained as a result of the breach, including whether allowances should be made to a third party for skill, labour and risk-taking in relation to the generation of profits.

## VII EPILOGUE: THE SPECIAL LEAVE APPLICATION

On 17 August 2012, special leave was denied by the High Court in relation to Grimaldi's bid to appeal the findings made against him to the High Court.<sup>484</sup> Grimaldi's special leave application was made and denied solely on the basis of questions concerning when someone may be found to be a de facto director of a corporation under the Corporations Act and was not relevant to questions of liability in relation to third parties.

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<sup>484</sup> Transcript of Proceedings, *Grimaldi v Chameleon Mining NL* [2012] HCATrans 187 (17 August 2012).



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