27/84

SUPREME COURT OF VICTORIA — FULL COURT

INDRISIE and ANOR v GENERAL CREDITS LIMITED

Young CJ, Crockett and Nicholson JJ

13, 14 December 1983; 22 February 1984 — [1985] VicRp 20; [1985] VR 251

CONTRACT – LEASE AGREEMENT – PAYMENTS IN ARREARS – GUARANTEE CALLED UP – CROSS CLAIM BY GUARANTOR FOR DAMAGES AS A SET-OFF – WHETHER NEXUS BETWEEN CLAIM AND CROSS-CLAIM – WHETHER SET-OFF AVAILABLE WHERE NO NEXUS SHOWN – WHETHER RIGHT TO SET-OFF TRANSFERABLE TO A STRANGER – WHETHER NOTICE TO PAY VALID AND OPERATIVE.

I. controlled a company which engaged in the business of placing amusement machines at various sites. By way of a master lease agreement, the company leased the machines from the respondent, General Credits Ltd upon agreeing to pay rental and other charges. By a guarantee and indemnity, I. guaranteed payment of the company's indebtedness, and provided land owned by him as security for payment. When the payments fell into arrears, General Credits Ltd, issued a writ seeking possession of I.'s land. I. argued that as General Credits Ltd had breached the agreement in that there had been a failure to lend an additional sum certain, and that the terms of the notice to pay were inadequate, leave to enter judgment for possession of I.'s land should not be granted. A Master granted leave, and I.'s appeal to a judge was dismissed. On appeal to the Full Court—

HELD: Appeal dismissed.
(1) In order for the company to rely upon its cross-claim for unliquidated damages as an equitable set-off, there must be such a nexus between the claim and the cross-claim that the cross-claim can be said to impeach the respondents' claim.
Edward Ward & Co v McDougall **[1972] VicRp 49; [1972] VR 433; and**
Eagle Star Nominees Ltd v Merril **[1982] VicRp 57; [1982] VR 557; [1981] V Conv R 54-002, applied.**

(2) As I.'s claim was founded upon a collateral contract entirely independent of the contract in respect of which I. was liable, it did not constitute an equitable set-off.

(3) Any right to an equitable set-off would have vested in the company controlled by I. and not in I. personally. Therefore, I., as a stranger to the contract, could not rely on a right that vested in the company.

(4) As the notice sufficiently identified the debt rather than the money sum required, it was a valid and operative notice to pay.

YOUNG CJ, CROCKETT AND NICHOLSON JJ: [1] Indrisie Investments Pty Ltd ("the company") conducts throughout Australia the business of placing amusement machines at various sites. The company collects revenue from these machines and shares it with the location owner. The company is controlled by the first-named appellant, Mr Indrisie. The company financed the acquisition of machines by selling them to a finance company, General Credits Ltd, the respondent. The respondent then leased the machines back to the company. The leasing was effected by a master lease agreement. The company was obliged under the agreement to pay to the respondent rental and other charges.

By a guarantee and indemnity the appellants guaranteed to the respondent payment by the company of "each and all sums **[2]** of money interest costs expenses and damages" in which the company was then or might thereafter be indebted to the respondent "on any account whatsoever". Then, by an instrument of mortgage the appellants covenanted to pay to the respondent on demand each and all sums of money and damages in which it was then or thereafter indebted or liable or contingently indebted or liable to the (company) on any account whatsoever". The security for payment was land of which the appellants are the joint proprietors.

As at 16th August 1982, the indebtedness of the company to the respondent under the master lease for arrears of rental and interest was $337,946.86. By a notice to pay dated 20th August 1982, the respondent demanded payment by the appellants pursuant to the mortgaged

agreement, not of the specific sum then owing, but of "each and all sums of money and damages in which you are indebted or liable or contingently indebted or liable". That is to say the demand for payment was in the precise words used in the mortgage. The demand was not met. The respondent, accordingly, on the 20th September 1982, issued a writ seeking an order for possession of the land then in the possession of the appellants and which was the subject of the mortgage. Possession was sought on the ground of the appellants' default in the performance of their obligations to the respondent under the mortgage. On the 6th December 1982, on the return of a summons for final judgment, a Master granted the respondent leave to enter judgment for possession of the land. King J dismissed an appeal to him from the Master's order. The appellants now appeal from King J's order of dismissal. Before turning to the grounds of appeal reference has to be made to one further aspect in the history of the transaction.

[3] The first-named appellant in an account deposed to by him by affidavit, and which, for present purposes, must be taken as true or as possibly being established as correct, has averred that the respondent in February 1982 breached its agreement with the company. It was said that it was always agreed that the respondent would lend to the company up to $1,000,000. However, it was alleged that in late 1981 the agreement was varied so as to allow the company to borrow up to $1,500,000. The additional borrowing was to be used principally in replacing parts in machines and permitting a change-over to a more modern type of machine. The respondent then defaulted in its agreement to lend the additional $500,000. This default resulted in the company's inability satisfactorily to compete for business and to service its requirements. The consequent decline in profitability led to loss by the company and in turn to its inability to pay to the respondent the sums falling due under the master lease.

In reliance on the alleged breach by the respondent of its agreement with it, the company by a writ issued 19th August 1982, sought to restrain the respondent from taking steps to repossess amusement machines. Then, in another writ issued 26th October 1982, the company has sought the recovery from the respondent of damages for breach of contract. In these circumstances the appellants maintained that the respondent should not have had granted to it leave to enter final judgment. The two principal arguments relied on – and which are alone those that require consideration for the determination of this appeal – were that the appellants were entitled in the action to rely upon a equitable set-off and, in any event the notice to pay which was a necessary prerequisite **[4]** to the respondent's calling up the security under the mortgage was so non-specific as not to amount to a valid and operative notice to pay.

In support of the first contention it was argued that the appellants could take the benefit in the proceedings against them of any equity which the company had by virtue of the right of action accruing to it from the respondent's contractual default. Were it otherwise, so it was said, the guarantor would be placed in a worse position than the principal debtor. In particular it was said that, as the liability of the mortgagors arose only because the principal's default was in turn caused by the respondent's misconduct, that default could not be relied upon by the mortgagee to support a right of recourse by it to the mortgage security. In this connection counsel referred to a passage in Halsbury's *Laws of England* 4th ed., Vol. 20, para. 158 where it is said that "to render the surety liable the default relied upon must not be due to the creditor's misconduct". However, the misconduct there referred to is conduct that amounts to a refusal by the creditor to accept performance of the duty guaranteed. See *Rowlatt on Principal and Surety* 4th ed, p111. It has no application to a case such as the present. The Court of Appeal in New South Wales has recently held that a guarantor under a guarantee which makes him liable without more for the full indebtedness of the debtor for goods supplied cannot rely upon a cross-claim for damages which may be available to the principal debtor as against the creditor in reduction of, or as a defence to, his liability under the guarantee. *Covino v Bandag Manufacturing Pty Ltd* 30 FLR 564; [1983] 1 NSWLR 237; 4 Fam LR 65, particularly per Glass JA at pp240-241. With respect, we consider the reasoning of the Court in that case and of Isaacs J in **[5]** *Cellulose Products Pty Ltd v Truda* [1970] 92 WN (NSW) 561 on which it was based to be plainly correct.

In our opinion the company could not set up its claim for unliquidated damage as a set-off. It is not suggested that the claim amounts to a statutory or common law set-off. But it was contended for the appellants that it did constitute an equitable set-off. However reference to cases such as *Edward Ward & Co v McDougall* [1972] VicRp 49; [1972] VR 433; *British Anzani (Felixstowe) Ltd v International Marine Management (UK) Ltd* [1980] 1 QB 137 and *Eagle Star Nominees Ltd*

v Merril [1982] VicRp 57; [1982] VR 557; [1981] V Conv R 54-002 shows that, in order to rely upon a cross-claim as an equitable set-off, there must be such a nexus between the claim and cross-claim that the cross-claim can be said to impeach the plaintiff's claim. In the present case the claim for unliquidated damages is founded, not upon the transaction in respect of which the principal debtor is said to be liable, but upon a collateral contract entirely independent of that for which the respondent has the benefit of a security for due performance The appellants' claim clearly does not meet the test to be applied, namely, can the cross-claim be said to impeach the title to the respondent's legal demand?

Then, what is a no less formidable obstacle for the appellants, is the fact that any right to an equitable set-off would vest, of course, in the company. But it is not the company that seeks to rely on it but the appellants. They are strangers to the contract breach of which the company is asserting has conferred on it a claim for unliquidated damages. There is no authority to which the Court was referred in which there was acknowledged the right to any such transference of an alien claim to meet an obligation by way of equitable set-off. Nor, in our opinion, should the Court as a matter of principle **[6]** now take the step hitherto not taken of extending to a stranger to the cross-claim any right that properly should be that of the cross-claimant alone. In any event for such a step to be taken the company would have to be before the Court as a party. See *Wilson v Mitchell* [1939] 2 KB 869.

Nor, in our opinion, can the argument relating to the supposed inadequacy of the notice to pay succeed. That which the appellants were called on to pay was precisely what they had contracted to pay on demand. This is so as the notice faithfully reproduced the terms of the relevant covenant. In any event demand for payment under a mortgage is sufficient if the notice sufficiently identifies the debt of which payment is demanded. It is identification of the debt rather than the money sum which is required. *Barns v Queensland National Bank Ltd* [1906] HCA 26; [1906] 3 CLR 925; 12 ALR 238. The appeal must be dismissed.

Solicitors for the appellants: Phillips, Fox and Masel. Solicitors for the respondent: Corr and Corr.
