PRINCIPLES OF CONTRACT LAW

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PRINCIPLES OF CONTRACT LAW

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PREFACE

This book aims to provide an accessible and concise but sophisticated explanation and exploration of contract law for Australian law students. We aim to offer a clear understanding of Australian contract law while also encouraging the reader to think deeply about the law of contract from a range of different perspectives. The book also provides detailed coverage of related obligations and liabilities arising by way of equitable estoppel, restitution for unjust enrichment, misleading conduct and consumer guarantees, which are essential topics of study for students of contract law in Australia. The subject matter of the book might best be characterised, like that of Robert Hillman and Robert Summers' US casebook, as "contract and related obligations".

The book has been substantially revised throughout to take account of developments since the last edition. A number of topics have been significantly affected by consequential decisions of the High Court of Australia. The discussion of part performance has been rewritten in light of *Pipikos v Trayans* [2018] HCA 39. The restitution chapter has been extensively revised in light of *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32. The chapter on penalties has been revised to accommodate the developments in *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525. The undue influence chapter has been updated in the light of *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85. The chapter on statutory unconscionable conduct has been revised to include discussion of *ASIC v Kobelt* [2019] HCA 18.

In addition to those changes driven by developments in the law, we have revised a number of chapters in order make the discussion clearer, more comprehensive and more accessible. The estoppel chapter has been substantially rewritten to provide readers with a clear understanding of the range of different views as to the current state of promissory estoppel in Australian law. The chapter on construction has been substantially expanded to provide more detailed coverage of the courts' general approach to construction, the evidence that may be taken into account (including more detailed discussion of particular categories of extrinsic evidence), the role of contractual purposes and absurdity. In the implied terms chapter, implication for business efficacy and terms implied in law are discussed in greater detail. In the chapter on restrictions on termination, the discussions of the readiness and willingness requirement and relief against forfeiture have been expanded and made clearer. The mistake and duress chapters have been substantially rewritten and made clearer throughout.

In this edition, Andrew Robertson was responsible for chapters 1–7, 9–11, 13–14, 18–25, 30–32 and 39–42 and Jeannie Paterson was responsible for chapters 8, 12, 15–17, 26–29 and 33–38. We gratefully acknowledge the contributions of our former co-authors Peter Heffey (who contributed to the 1st edition) and Arlen Duke (who contributed to the 3rd, 4th and 5th editions). We are grateful to Elise Bant for helpful discussions of several issues and comments on draft chapters. We also express our deep thanks to Monica Stanisis and Amber Withers for their meticulous and helpful research assistance, as well as to Jake Herd, Ken Kiat, Alyssa Kim and Yi Tung. Thanks are also due to the editors at Newgen for their thorough and careful work on the manuscript. It has been a pleasure to work with Stephen Rennie, Senior Product

Developer for Thomson Reuters, who oversaw the project with great care and generously accommodated revisions late in the production process.

ANDREW ROBERTSON
JEANNIE PATERSON

Melbourne
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INTRODUCTION

PART I

CHAPTER **1**

The nature of contract

THE IDEA OF CONTRACT

[1.05] A contract is commonly defined as an agreement or set of promises that the law will enforce (ie, for breach of which the law will provide a remedy).[1] There are, however, many different ways of understanding what a contract is, and what contract law is about. This chapter explores some ideas about the nature of contract and the role of contract law. Given the range and complexity of the different approaches covered in this chapter, it is necessary to begin with an overview of the different perspectives.

First, according to the classical understanding, a contract is an expression of the joint will of parties engaged in a transaction. On this view, contractual obligations are voluntarily assumed and sharply distinguishable from obligations imposed by the law of tort. The role of contract law, according to the classical understanding, is to facilitate the freedom of the parties to create their own private law. This set of ideas, known as "classical contract theory", exerted a significant influence over the development of English contract law in the 19th century. Although these ideas have been the subject of sustained criticism over a considerable period of time, their influence can still be seen in many principles of Australian contract law and in the outcomes of contemporary Australian contract cases.

1 Coote, "The Essence of Contract – Part I" (1988) 1 *Journal of Contract Law* 91, 94–7.

The classical theory of contract was a unifying theory that attempted to capture the essence of contract in a single idea. Some contemporary scholars have offered alternative unifying theories that are related to classical theory but avoid some of its inconsistencies and deficiencies. Two prominent contemporary unifying theories of contract law are Charles Fried's theory that contractual obligation is based on promise and Randy Barnett's idea that contract is based on consent to the transfer of entitlements.

A second way of understanding contract, then, is to see it as based on the moral obligation to keep a promise. Charles Fried argues that a moral obligation arises from the making of a promise, because the promisor has invoked a convention that gives the promisee moral grounds to expect the promised performance. From this liberal individualist perspective, promise is the core of contract.

Thirdly, contract can be seen to be based on consent. Randy Barnett suggests that it is consent to a transfer of entitlements rather than promise that gives contract law its moral force. A person who manifests an intention to assume a legal obligation invokes the institution of contract and thereby incurs a moral obligation to perform that promise. The legal enforcement of a contractual promise is justified because the parties have consented to legal enforcement or have at least behaved in such a way as to indicate that they have so consented.

Fourthly, contract can be seen as a mechanism that facilitates economically efficient exchanges. Michael Trebilcock has suggested that, from an economic viewpoint, the functions of contract law are: first, to prevent opportunistic behaviour by enforcing contractual obligations; secondly, to provide a set of default rules and thus save parties the effort and expense of negotiating all of the terms of their transactions; thirdly, to fill gaps in contracts; and fourthly, to address market failures, such as misinformation and improper pressure.[2] The economic approach to contract law can be seen as another unifying theory: it attempts to explain and justify all of contract law by reference to a single idea and a single goal, namely economic efficiency.

Not all writers on contract law share the desire to explain the subject by reference to a single principle or unifying theory. Most contract scholars accept that contract law draws on a diverse range of ideas and is shaped by a number of goals, which often point in different directions. This fifth view of contract law sees it as "a rich combination of normative approaches and theories of obligation" which draws on a complex mixture of values and influences.[3] The leading exponent of this view is Robert Hillman.[4]

A sixth way of understanding contract law is to see it as a set of contradictory formal rules that serve an ideological function. That function is to mask the political and social issues underlying particular disputes and to perpetuate a legal order that protects the interests of the powerful. This understanding of contract law is associated with the Critical Legal Studies (CLS) movement.

Seventhly, contract law can be analysed from the point of view of gender. Its doctrines, its ideology and its representations of women can be seen as having negative effects on women. Contract law can also be seen as reflecting a masculine viewpoint, with its emphasis on abstract rules and its disregard of values such as co-operation and respect for others. It can

2 Trebilcock, *The Limits of Freedom of Contract* (1993), pp 15–7.

3 Hillman, *The Richness of Contract Law* (1998), pp 6–7.

4 See Hillman, *The Richness of Contract Law* (1998). See also Trakman, "Pluralism in Contract Law" (2010) 58 *Buffalo Law Review* 1031.

also be criticised for its failure to address issues of substantive gender inequality. These views can all be described as feminist perspectives on contract law.

Eighthly, contract can be viewed as a social relationship. The behaviour of parties to contracts is affected by the social relations between the parties and by the broader social context in which the contract is made. These social relations may be more important to the parties than their legal rights. Empirical evidence shows that even business people in some contexts plan transactions on the basis of trust, rather than the availability of legal sanctions, and routinely modify exchange transactions without regard to their legal rights. In many cases, this is because the relationship between the parties, which may form part of a broader web of social relations, is more important than the particular transaction. Ian Macneil and other relational contract theorists argue that contract law is primarily geared towards discrete exchange transactions. Some suggest that the principles of contract law should to a greater extent reflect the relational aspects of contracting (eg, by accepting that contractual obligations can evolve over time and that parties do not always attempt complete planning at the beginning of the relationship).

Ninthly, contract can be seen as a form of regulation. Jean Braucher points out that contract law plays a significant regulatory role in determining the validity of contracts, interpreting the language and conduct of the parties and filling substantial gaps in agreements. Hugh Collins characterises the law of contract as a particular form of regulation of markets and exchanges, which he calls "private law" regulation. The "private law of contract" gives rights to the parties themselves and allows them to enforce those rights through the courts. This private form of regulation can be contrasted with the public regulation of exchanges, through legislation that sets standards and establishes government agencies to enforce compliance with those standards.

A tenth way of understanding contract is to see it in its doctrinal context, as part of the law of obligations. The common law recognises three fundamental obligations owed by individuals to each other: the obligation to perform certain promises (the law of contract), the obligation to avoid causing harm to others in certain situations (the law of tort) and the obligation to restore certain unjust gains (the law of restitution or unjust enrichment). Alongside these legal obligations are numerous equitable and statutory obligations, which cannot be so neatly categorised. Contract law can be understood as part of a web of obligations created by the common law, equity and statute. This way of understanding contract is considered in Chapter 2.

The final section of this chapter is concerned with the internationalisation of contract law. There are many ways in which the principles of contract law in different jurisdictions are converging. There are both formal and informal moves to harmonise and standardise the principles of contract law, particularly in relation to international transactions. From a practical point of view, it is important to understand the different ways in which contract law is becoming internationalised. It is also useful to compare the approaches taken in different jurisdictions to particular contract problems. Such comparisons give us a better understanding of the nature of Australian contract law and help us to consider why a particular approach is adopted and whether it is desirable.

A final introductory point is to note the basic difficulty about theorising about "contract law" across time and across jurisdictions. Most of the literature discussed in this chapter purports to generalise about "contract", "the law of contract" or "the common law of contract" and in doing so assumes that there is an object that maintains some consistency

across time and across different jurisdictions. As Brian Bix notes, there are advantages to this: theorizing necessarily involves abstraction and generalisation, and there does appear to be a recognition among scholars that there is enough similarity and consistency to justify some general theorising.[5] We do, however, need to approach general theories with caution, bearing in mind that contract law differs in significant ways across time and across jurisdictions and that may limit the scope of application or explanatory power of particular theoretical insights.[6]

CLASSICAL CONTRACT THEORY

The philosophy underlying classical contract law

[1.10] Classical contract theory is the set of ideas and assumptions that underpinned the development of contract law in England and the United States during the 19th century. The latter half of the 19th century is often described as the classical age of English contract law. There are two reasons for this: first, because of the extensive development of contract principles that took place during that period and secondly, because the prevailing political and economic views of the time elevated contract to a position of central importance in the law.[7] Classical theory remains important to us today because significant areas of Australian contract law are still based on the classical principles developed in England in the 19th century. Moreover, the classical understanding of contract continues to influence the development of contract law in the Australian and English courts.

The law of contract that developed in the 19th century was influenced by the will theory of contract.[8] According to the will theory, a contract represents an expression of the will of the contracting parties and, for that reason, should be respected and enforced by the courts. At the heart of the will theory is the notion that a contract involves self-imposed liability. The will theory and the principle of freedom of contract were connected with economic, philosophical and political views of the late 19th century.[9] The prevailing ideology was the liberal individualist philosophy of laissez faire, and the courts developed principles of contract law that were consistent with that philosophy.[10] The parties to a contract were regarded as self-interested individuals who created their own private law through agreement. It was thought that individuals should be free to enter into whatever bargains they considered would benefit them and the courts should facilitate that freedom by enforcing whatever bargains individuals chose to make. Otherwise, the courts should interfere as little as possible.[11] Freedom of contract was the starting point for the determination of all contract law issues.[12] These ideas are reflected in the famous statement by Sir George Jessel MR in *Printing and Numerical Registering Co v Sampson* that:[13]

5 Bix, "The Promise and Problems of Universal, General Theories of Contract Law" (2017) 30 *Ratio Juris* 391, 400.

6 Bix, "The Promise and Problems of Universal, General Theories of Contract Law" (2017) 30 *Ratio Juris* 391, 400.

7 Atiyah, *An Introduction to the Law of Contract* (5th ed, 1995), p 10.

8 See Atiyah, *The Rise and Fall of Freedom of Contract* (1979), pp 405–8.

9 Atiyah, *The Rise and Fall of Freedom of Contract* (1979), Chs 1–5.

10 Atiyah, *An Introduction to the Law of Contract* (5th ed, 1995), pp 7–9.

11 Atiyah, *An Introduction to the Law of Contract* (5th ed, 1995), p 8.

12 Atiyah, *The Rise and Fall of Freedom of Contract* (1979), p 666.

13 *Printing and Numerical Registering Co v Sampson* (1875) LR 19 Eq 462, 465.

> if there is one thing which more than another public policy requires, it is that men of full age and competent understanding shall have the utmost liberty of contracting, and that their contracts when entered into freely and voluntarily shall be held sacred and shall be enforced by Courts of justice.

The political and social context in which modern contract law developed thus favoured individualism, self-reliance and the exercise of free will over government intervention and paternalism.[14] The principles of modern contract law were founded on those concepts,[15] which were encapsulated in a political theory labelled "contractualism" by Morris Cohen:

> Contractualism in the law, that is, the view that in an ideally desirable system of law all obligation would arise only out of the will of the individual contracting freely, rests not only on the will theory of contract, but also on the political doctrine that all restraint is evil and that the government is best which governs least. This in turn is connected with the classic economic optimism that there is a sort of pre-established harmony between the good of all and the pursuit by each of his own selfish economic gain.[16]

This approach had two principal effects. First, the courts were reluctant to recognise the existence of non-contractual obligations. The law of tort and restitution went largely undeveloped during the latter half of the 19th century,[17] and the courts imposed stifling constraints on the enforcement of promises that had been relied upon, but did not form part of, a bargain or exchange between the parties.[18] Hugh Collins has observed that the courts tended to perceive social relations in contractual terms. This is illustrated by the famous case of *Carlill v Carbolic Smoke Ball Co*.[19] When a manufacturer's advertisement for a device designed to prevent colds proved to be misleading, Mrs Carlill was able to obtain a remedy against the manufacturer by establishing a contract between them. A contract was found to have been made despite the fact that the parties had never communicated with each other or exchanged money or goods.[20] Collins points out that, rather than recognising the misleading advertising as a civil wrong in itself, the Court used the law of contract to discourage misleading claims in advertising and to deter the marketing of unproven pharmaceutical devices.[21]

Secondly, the principles of contract law were developed and justified by reference to an overriding concern with giving effect to the intentions of the parties. The courts "felt that they were not imposing legal rules on the parties, but were merely working out the implications of what the parties had themselves chosen to do".[22] The principles were seen as objective and

14 Atiyah, *The Rise and Fall of Freedom of Contract* (1979), esp Chs 1–2.

15 Atiyah, *The Rise and Fall of Freedom of Contract* (1979), esp Chs 13–6. Atiyah's detailed account argues that free market principles influenced the judges and filtered into the content of contract doctrine. Cf Gordley, *The Philosophical Origins of Modern Contract Doctrine* (1991), who argues that Atiyah and others have exaggerated the influence of liberal theories.

16 Cohen, "The Basis of Contract" (1933) 46 *Harvard Law Review* 553, 558.

17 Atiyah, *An Introduction to the Law of Contract* (5th ed, 1995), p 10.

18 See Robertson, "Situating Equitable Estoppel within the Law of Obligations" (1997) 19 *Sydney Law Review* 32, 33–7.

19 *Carlill v Carbolic Smoke Ball Co* [1893] 1 QB 256. See further [3.10].

20 Collins, *The Law of Contract* (4th ed, 2003), p 4.

21 Collins, *The Law of Contract* (4th ed, 2003), p 4.

22 Atiyah, *An Introduction to the Law of Contract* (5th ed, 1995), p 10.

neutral, and based on a respect for voluntary choices.[23] There could therefore be no room for any requirement of fairness in contractual exchanges or for the imposition of contractual obligations without the consent of the parties.[24]

An important factor in the development of contract as a distinct body of law was that textbooks on English contract law began to be written in the 19th century. Textbooks such as those by Chitty, Pollock and Anson played an important role in the development of the classical idea of contract law by describing in systematic form a set of abstract general principles which applied to all types of contract.[25] The textbooks helped to carve out contract as an independent body of law, which was separate from property law, the law of tort and the law of restitution.[26] Contract could therefore be seen as a branch of law that was exclusively concerned with voluntarily assumed obligations.[27] Contract was sharply distinguished from the law of tort, in which obligations were imposed on individuals. This separation was and remains artificial, since obligations are routinely imposed by the law of contract, while intention and voluntary conduct play a role in shaping obligations in tort.[28] Moreover, property, tort and restitution play an important role in the regulation of market transactions[29] and in the determination of the rights and obligations of contracting parties in particular cases.[30]

Criticism of the classical approach

[1.15] The will theory and the classical approach to contract have been comprehensively criticised. The first point is that the rights and obligations arising from a contract do not necessarily represent the will of the parties. Many problems the courts must deal with arise as a result of what the parties *have not* expressly agreed upon, rather than what they *have* agreed upon. As Morris Cohen has pointed out, litigation almost invariably reveals the absence of agreement between the parties.[31] Problems arising from miscommunication or a lack of agreement cannot be resolved by treating the agreement as an expression of the will of the parties. The courts resolve such problems by determining the rights and obligations of the parties on an objective basis.

In determining whether a contract has been formed, the courts are not concerned with whether the parties actually intended to enter into a contract, but with whether a reasonable person would believe they intended to do so, based on their words and behaviour.[32] This

23 Collins, *The Law of Contract* (4th ed, 2003), pp 6–7.

24 Collins, *The Law of Contract* (4th ed, 2003), pp 6–7.

25 Simpson, "Innovations in Nineteenth Century Contract Law" (1975) 91 *Law Quarterly Review* 242, 247; Atiyah, *The Rise and Fall of Freedom of Contract* (1979), pp 388–90.

26 Collins, *The Law of Contract* (4th ed, 2003), p 5.

27 This view remains influential; see, eg, *Transfield Shipping Inc v Mercator Shipping Inc (The Achilleas)* [2008] UKHL 48; [2009] 1 AC 61, esp [12]: "It seems to me logical to found liability for damages upon the intention of the parties (objectively ascertained) because all contractual liability is voluntarily undertaken." See also *Astley v Austrust Ltd* (1999) 197 CLR 1, 36: "Tort obligations are imposed on the parties; contractual obligations are voluntarily assumed." But cf *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [83] and [195]–[196], discussed at [10.70].

28 Atiyah, "Contracts, Promises and the Law of Obligations" (1978) 94 *Law Quarterly Review* 193, 221.

29 Collins, *The Law of Contract* (4th ed, 2003), p 6.

30 See Chapter 2 and [3.150].

31 Cohen, "The Basis of Contract" (1933) 46 *Harvard Law Review* 553, 577.

32 See Chapters 3 and 5.

approach requires the court to make policy decisions as to whether contractual obligations should be recognised in particular circumstances. Liability for breach of contract can therefore be seen as tort-like liability for negligent conduct or careless use of language, rather than as self-imposed liability that has emanated from the will of the parties.[33]

The content of a contract is also determined objectively: statements made during negotiations may form part of a contract if a reasonable bystander would think that a contractual promise was intended,[34] and unsigned written terms form part of a contract if reasonable notice of the terms was given by one party to the other.[35] The contractual terms are then interpreted according to what a reasonable person would think was meant by the language used.[36] The courts routinely imply terms to fill gaps and deal with contingencies not provided for in the contract. Other contract doctrines, such as the doctrine of frustration and the remoteness rule, require the courts to fill gaps in the contractual allocation of risk.[37] Contracting parties routinely leave it to the courts to decide what should happen in the event that one of the parties should fail to fulfil their obligations. Thus, in many respects, contract law operates in a similar way to the law of tort: the state, through the courts, imposes obligations on the parties based on norms of reasonable behaviour. Contractual obligations derived from an objective interpretation of behaviour can be seen as obligations that are imposed by the state in order to protect persons who rely on promises. This serves the broader policy goal of facilitating commercial transactions and other valuable exchanges by ensuring that individuals can rely on serious commitments made by others.

A second problem with the classical approach to contract is that it assumes that contracts are fully negotiated between the parties. Today, most written contracts are made on the basis of standard form terms which are generally not negotiable and typically not read, and the implications of which are commonly not understood by the non-drafting party.[38] The widespread use of standard forms, which began in the 19th century, undermines the idea that a contract necessarily represents a consensus between the parties. If the bargaining power in a given situation is sufficiently unequal that one party is able to impose his or her own standard terms on the other, then the resulting contract is unlikely to represent the will of both parties.[39] The classical notion of individuals freely bargaining in relation to contract terms does not take account of the dominance of standard form contracts or the unequal distribution of economic power.[40]

33 Mensch, "Freedom of Contract as Ideology" (1981) 33 *Stanford Law Review* 753, 763.

34 Subject to the parol evidence rule: see Chapter 12.

35 See Chapter 12.

36 See Chapter 13.

37 See Chapters 15 (on the doctrine of frustration) and 27 (on the remoteness rule).

38 See Kessler, "Contracts of Adhesion – Some Thoughts About Freedom of Contract" (1943) 43 *Columbia Law Review* 629; Slawson, "Standard Form Contracts and Democratic Control of Lawmaking Power" (1971) 84 *Harvard Law Review* 529; Rakoff, "Contracts of Adhesion: An Essay in Reconstruction" (1983) 96 *Harvard Law Review* 1173; Hillman and Rachlinski, "Standard-Form Contracts in the Electronic Age" (2002) 77 *New York University Law Review* 429.

39 See Robertson, "The Limits of Voluntariness in Contract" (2005) 29 *Melbourne University Law Review* 179, 187–202.

40 Dawson, "Economic Duress – An Essay in Perspective" (1947) 45 *Michigan Law Review* 253; Cohen, "The Basis of Contract" (1933) 46 *Harvard Law Review* 553.

A third problem with the notion that contract law is fundamentally concerned with individual autonomy is the role played by the state in enforcing contracts and in establishing the legal framework in which bargaining takes place. Freedom of contract is not a matter of leaving parties to do their own thing, as the philosophy of laissez faire might suggest, because the state plays a decisive role in both the enforcement and formation of contracts. A contract is only "binding" because the state, through the courts, will enforce it. Morris Cohen has observed that the role played by the state in the enforcement of contracts allows the law of contract to be viewed as a branch of public law.[41] The state also plays a decisive role in the making of a contractual bargain. In a market economy in which labour is specialised, individuals have no choice but to make contracts in order to obtain food, clothing and shelter, to acquire skills and to work.[42] Coercion is "at the heart of every bargain" because it is "inherent in each party's legally protected threat to withhold what is owned".[43] It is the right to withhold property that allows a party to force another to submit to his or her terms, provided they are no worse than the alternative.[44]

The power to bargain is founded on property rights that are conferred and enforced by the state. As Betty Mensch has explained, ownership, or the right to withhold property, is a function of legal entitlement.[45] If we can say that ownership is at the heart of every bargain and ownership is a function of the legal order, then every contract is a function of the legal order, rather than a function of the will of the parties. This conclusion demonstrates the falsity of the distinction between public and private in contract law, and the distinction between free and regulated markets.[46]

The validity of the first and second criticisms of classical contract theory set out in this section has become matters of debate in recent years. Scholars such as Charles Fried, Randy Barnett and Stephen Smith, whose work is discussed below, defend theories of contract that are based on the core classical idea that contractual obligations can in general be regarded as voluntary or self-imposed. There is also a broader movement in the contract law literature that seeks to show that there are fewer gaps in contracts than is commonly thought, and that judges play a less significant role in shaping contractual obligations than is commonly thought.[47]

PROMISE THEORY

Charles Fried

[1.20] One of the most prominent contemporary unifying theories of contract law is that proposed by Charles Fried in his book *Contract as Promise: A Theory of Contractual*

41 Cohen, "The Basis of Contract" (1933) 46 *Harvard Law Review* 553, 586.

42 Radin, "Contract Obligation and the Human Will" (1943) 43 *Columbia Law Review* 575, 580; Hale, "Bargaining, Duress, and Economic Liberty" (1943) 43 *Columbia Law Review* 603.

43 Mensch, "Freedom of Contract as Ideology" (1981) 33 *Stanford Law Review* 753, 764.

44 Hale, "Coercion and Distribution in a Supposedly Non-coercive State" (1923) 38 *Political Science Quarterly* 470, 472–3; Hale, "Bargaining, Duress, and Economic Liberty" (1943) 43 *Columbia Law Review* 603, 604.

45 Mensch, "Freedom of Contract as Ideology" (1981) 33 *Stanford Law Review* 753, 764.

46 Mensch, "Freedom of Contract as Ideology" (1981) 33 *Stanford Law Review* 753, 764.

47 See [1.22].

Obligation.[48] Fried believes that the law of contract has an underlying, unifying structure and that that structure is founded on moral principles. He argues that the moral basis of contract law is the promise principle – the principle by which people may impose on themselves obligations that previously did not exist. Contract is often defined in terms of promise and "contract as promise" is a prominent mainstream concept. Fried's basic point is that a person who makes a promise is morally bound to keep it because that person has "intentionally invoked a convention whose function it is to give grounds – moral grounds – for another to expect the promised performance".[49] A contract is, he says, first of all a promise, and a contract must be kept because a promise must be kept.

Fried's theory is essentially a restatement of the classical will theory of contract. We have seen that, according to that theory, a contract involves self-imposed duties. It is a theory that fits comfortably with the liberal individualist philosophy of allowing individuals free choice and respecting their decisions – the ideology of laissez faire. Fried's endorsement of this ideology underlies his view that judges should not interfere with contracts in order to redistribute wealth. Such redistribution should not be effected on an ad hoc basis. Rather, redistribution should be effected by the legislature through general taxation and the provision of welfare benefits.[50] On this view, presumably courts should not have the power they currently enjoy to strike down clauses, such as penalty clauses, unreasonable restraint of trade clauses and certain exemption clauses.[51] However, Fried does reject some of the extremes of the classical approach and acknowledges that there are aspects of contract law that do not rest on the promise principle. For example, when a contract is frustrated by subsequent events, he sees that there is no point in insisting that the legal consequences are somehow promise related.[52] Rather, it should be admitted that this contingency was not provided for by the contract and the courts must fill the gap by applying non-promissory principles of fairness. Fried sees no threat to the promise principle in "gap-filling" by the courts, as a gap is only filled when the parties have omitted to make a promise.

In evaluating Fried's theory, a number of issues arise. The first is that the theory does not tell us which particular promises the law should enforce. If there is a moral duty to keep promises, why are only some promises given legal force? The principal way in which the law distinguishes between legally enforceable and non-enforceable promises is through the doctrine of consideration. A promise is only enforceable under the law of contract if something is given or promised in exchange for it. Gratuitous promises are generally not enforceable. This does not accord with Fried's promise theory. He argues, however, that the concept of consideration is incoherent and inconsistently applied by the courts. Moreover, it is being undermined by developments such as the recognition of equitable or promissory estoppel, a principle of reliance-based liability which Fried sees as an attempt to "plug a

48 Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981). A second edition published in 2015 retains the original text but includes a new preface and concluding essay responding to subsequent scholarship.

49 Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), p 16.

50 Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), p 106.

51 See, respectively, Chapters 28, 41 and 13.

52 But see Morris, "Practical Reasoning and Contract as Promise: Extending Contract-based Criteria to Decide Excuse Cases" (1997) 56 *Cambridge Law Journal* 147; Langille and Ripstein, "Strictly Speaking – It Went Without Saying" (1996) 2 *Legal Theory* 63.

gap" left in the general regime of promise enforcement by the doctrine of consideration.[53] Given that the adequacy of consideration is entirely up to the contracting parties, and that even nominal consideration is sufficient, it is no doubt arguable that the law should allow individuals to make gratuitous promises that are legally binding.

But what of social and domestic promises, such as a promise to come to dinner or to help a friend fix his car? The law denies enforceability to such promises through the requirement of an intention to enter legal relations.[54] Fried accepts the need for a similar principle. He states that the promisor "must have been serious enough that subsequent legal enforcement was an aspect of what (the promisor) should have contemplated" at the time the promise was made.[55] This represents a qualification on the promise theory, since a promise is not of itself seen as sufficient to give rise to a contractual obligation.

Courts regularly interpret contracts and imply terms in them. Generally, an objective approach is taken so the actual intention of a promisor is not to the point. Does this process fit comfortably with the promise theory? Fried takes the view that the courts "flesh out" what the promisor has accepted as a contractual duty because promises "are made against a background of shared purposes, experiences and even a shared theory of the world".[56] He says "there is always some deeper, more general level of shared experience and striving to which appeal can be made in order to make the particular project mutually intelligible".[57] If this is so, then objective and subjective intention will coincide. But is Fried's rationalisation realistic, given that terms are often implied or interpreted against the will of a promisor?[58] The implication of terms and the process of interpretation can be seen as "gap-filling" by the courts.[59] The greater the extent of judicial gap-filling, the less persuasive the argument that the promise principle is dominant. On the other hand, many contracts may not receive judicial scrutiny because through careful drafting the potential gaps have already been filled by the parties themselves.

On the question of damages, Fried sees the promise principle as providing a good explanation for the awarding of expectation damages to the disappointed promisee. The principal remedy for breach of contract is an award of damages calculated to put the promisee in the position he or she would have been in had the promisor's promise been performed (expectation damages). Such a measure of damages is often compared with reliance damages (covering losses incurred in reliance on the promise) and restitutionary damages (covering the return of benefits received by the promisor). Fried makes the point that if a person makes a promise to another and fails to keep that promise, then it is only fair that the equivalent of the promised performance should be handed over.[60] Note, however, that the promisee will not always receive in damages what was promised, because in some cases the promisee will be awarded reliance damages, and in all cases the promisee is under a duty to mitigate the loss which flows from the promisor's breach. Moreover, the promise principle does not explain

53 Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), p 25.

54 See Chapter 5.

55 Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), p 38.

56 Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), p 88.

57 Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), p 88.

58 See, eg, *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, discussed in [PtV.10].

59 See Chapter 14.

60 Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), p 17.

why an award of damages, rather than specific performance, is the normal remedy available to disappointed promisees.[61]

The legal enforcement of a contractual promise necessarily restricts the autonomy of the promisor because it deprives the promisor of the ability to choose to break the promise. However, Fried contends that the legal enforcement of promises enhances, rather than restricts, individual autonomy because the existence of the contractual mechanism gives individuals the power to bind themselves. "In order that I be free as possible … it is necessary that there be a way in which I may commit myself … By doing this I can facilitate the projects of others, because I can make it possible for others to count on my future conduct".[62] As we saw, Fried is a critic of the legal requirement of consideration as that requirement restricts the ability of the individual to make a legally binding gift-promise. Once a legally binding promise is made, a promisor is not permitted a change of heart. Autonomy of the individual does not extend that far, on the Fried view, even though the promisee may not have relied on the promise in a detrimental way nor conferred any benefit on the promisor. This suggests that an absolutist morality lies at the base of Fried's promise theory.

Stephen Smith

[1.22] A promise-based understanding of contract has also been defended by Stephen Smith. Smith describes his account of contract law as "interpretive": it aims to enhance our understanding of contract law by identifying connections between different features of contract law and thereby revealing an "intelligible order" in it.[63] Smith argues the essence of contact law is best captured by promise theory, which is the idea that a contractual duty is "created by communicating an intention to undertake an obligation".[64] Contract law is therefore essentially concerned with self-imposed obligations. On this view of contract, exchanges that are truly simultaneous are not contracts because they do not involve the creation of any self-imposed obligations.

Smith differs from Fried on how best to answer arguments about the apparent lack of "fit" between contract law doctrines and the idea that contractual obligations are created by the parties through the making of promises. Smith accepts that the idea that contractual obligations are created by promises cannot explain the doctrine of consideration. But Smith notes that no other plausible theory about the nature of contractual obligation can account for the doctrine of consideration either.

Smith argues that the doctrine of consideration essentially operates as a requirement of form. By requiring a promisor to take an additional step to make a valid contract, it promotes caution and provides a means by which the parties can signal their intention to create legal obligations.[65] The doctrine of consideration "facilitates the expression and proof of contracting parties' intentions" and is therefore not inconsistent with the promise theory of contract.[66] He accepts that an objective approach to contract formation causes some discomfort for a

61 See Craswell, "Contract Law, Default Rules and the Philosophy of Promising" (1989) 88 *Michigan Law Review* 489, 517–20.

62 Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), p 13.

63 Smith, *Contract Theory* (2004), p 5.

64 Smith, *Contract Theory* (2004), p 57.

65 See further [7.05].

66 Smith, *Contract Theory* (2004), p 65.

promise theory because "promises can only be *made* intentionally – and a search for intention is necessarily subjective".[67] But Smith questions whether the courts do in fact approach the question of intention to make a contract from an objective viewpoint and claims that the literature on this point is inconclusive.[68] Moreover, he says, the objective approach can be justified on the basis that it provides the most reliable evidence that is available of a promisor's subjective intentions.

Smith argues that the objective approach to contractual *interpretation*, on the other hand, does not undermine the promissory view of contract because the *content* of a promise is always determined objectively: the content of a promise is not what the promisor intended, but what the promise itself actually meant.[69]

It was noted that Charles Fried accepted that certain contract doctrines, such as the doctrine of frustration, are instances in which the courts fill gaps in the contractual allocation of risk and therefore fall outside the promise principle. Smith, in contrast, seeks to bring these doctrines within the promise principle on the basis that the courts in these cases are not imposing a solution on the parties but are in fact interpreting and implementing the parties' intentions. Smith's argument is based on a body of recent work which seeks to show that contract doctrines that are commonly thought to be concerned with the filling of gaps in fact involve an interpretation of what was agreed by the parties.[70] This is based on the idea that contracting parties can intend things they do not mention, or even think about, during negotiations. "[A] great deal of the content of a contract therefore goes without saying."[71] Most importantly, however, this view depends on the idea that judges can identify exactly what has gone without saying; that is, what has been tacitly agreed between the parties. It depends on the notion that, by examining the nature of the contract and the context in which it was made, judges are able to identify an implicit allocation by the contracting parties of the risk in question. For Smith and others, this is what the courts do in the application of doctrines such as mistake, frustration and remoteness.

Promise theory is considered in relation to implied terms in Chapter 14 and in relation to duress in Chapter 34.

CONSENT THEORY

[1.25] Consent theory is another unifying theory of contract law. This theory has been proposed and elaborated by Randy Barnett.[72] The theory posits that contractual obligations can only be fully understood if they are seen as dependent on an underlying system of *legal entitlements*. This system of entitlements specifies the rights which people may acquire and transfer and prescribes how such acquisitions and transfers may be effected.

67 Smith, *Contract Theory* (2004), p 174.

68 This question is considered at [3.140].

69 Smith, *Contract Theory* (2004), p 62.

70 See, eg, Langille and Ripstein, "Strictly Speaking – It Went Without Saying" (1996) 2 *Legal Theory* 63; Morris, "Practical Reasoning and Contract as Promise: Extending Contract-Based Criteria to Decide Excuse Cases" (1997) 56 *Cambridge Law Journal* 147; Kramer, "Implication in Fact as an Instance of Contract Interpretation" (2004) 63 *Cambridge Law Journal* 384; Kramer, "An Agreement-Centred Approach to Remoteness and Contract Damages", in McKendrick and Cohen (eds), *Comparative Remedies for Breach of Contract* (2005), p 25.

71 Smith, *Contract Theory* (2004), p 314.

72 Barnett, "A Consent Theory of Contract" (1986) 86 *Columbia Law Review* 269.

Contract law is that part of a system of entitlements that identifies the circumstances in which entitlements are validly transferred from one person to another.[73] It concerns enforceable obligations arising from the valid transfer of *existing* entitlements, that is, those entitlements that are already vested in the parties. A transfer requires the *consent* of the rights holder, that is, consent to be legally obligated. The legal enforcement of an obligation requires moral justification, and it is consent that provides the moral justification in this instance.

One of the primary functions of an entitlements theory is to specify the boundaries within which people may operate freely in order to pursue their purposes and thereby provide the basis for co-operative activity with others. The boundaries must be ascertainable so that rights may be respected and disputes avoided. In contract law, this means that consent to the alienation of rights must be *manifested*. Without such manifestation, parties to a transaction cannot ascertain what is rightful conduct and what constitutes a commitment upon which they can rely. Whether a person has consented does not depend on that person's subjective opinion about the significance of his or her words or conduct, but rather on the meaning that would ordinarily be attached to them. Only through general reliance on objectively ascertainable assertive conduct can a system of entitlements function coherently, minimise conflicting claims and respect the interests of those who take the conduct of others at face value. Accordingly, "a consent theory specifies that a promisor incurs a contractual obligation the legal enforcement of which is morally justified by manifesting assent to legal enforcement and thereby invoking the institution of contract".[74] A promise does not itself give rise to a contractual obligation; there must be a manifest consent to legal enforcement.

Barnett does not see anything paradoxical in adhering to an objective notion of consent, even though this consent may conflict with actual or subjective intention. He points out that the objective notion of consent is based on words and conduct of people that are commonly understood to reflect their subjective assent. Moreover, a person never has direct access to another person's subjective mental state.[75] A person must learn what other people intend to communicate by evidence of their conduct and words and, in the context of contract, this must be limited to evidence available to the other party at the time of the transaction.

A consent theory, because it is based on fundamental notions of entitlements, explains why an objective manifestation of consent must prevail over a subjective intent in the (unusual) event of a conflict. Such a theory also explains exceptional cases where evidence of subjective intent will prevail.[76] For example, there may be proof of a special meaning that the parties held in common or proof that the promisee did not actually understand the ordinary meaning to be the intended meaning. In such cases, the normal boundary-defining functions of the entitlements analysis would not be served by an objective approach. The main purpose of the objective approach is to enable people to rely on the appearances created by others because the subjective intentions of others are generally inaccessible. This purpose is satisfied when a person has actual knowledge that appearances in a particular case are, in fact, deceptive.

73 Barnett's theory of contract is therefore sometimes classed as a "transfer theory"; see, eg, Smith, *Contract Theory* (2004), pp 44–5. Another prominent transfer theory of contract is that of Peter Benson, "The Unity of Contract Law" in Benson (ed), *The Theory of Contract Law* (2001), p 118.

74 Barnett, "A Consent Theory of Contract" (1986) 86 *Columbia Law Review* 269, 305.

75 See further [3.140].

76 See [3.80] and [5.05].

Barnett's view then is that the objective manifestation of consent to a transfer of alienable rights is binding:

> because of its usual connection with subjective assent (thereby protecting the reliance interest of the promisor) and because people usually have access only to the manifested intentions of others (thereby protecting the reliance interest of the promisee and others as well as the "security of transactions").[77]

Consent may be manifested formally or informally. Formal consent is manifested in a document under seal (ie, a deed). Informal consent may be manifested in various ways, such as bargained-for consideration, non-bargained-for detrimental reliance by the promisee or an unambiguous verbal commitment. Although this would go beyond the current understanding of which promises are binding (at least in Australia), Barnett believes that consent theory encourages informed action by providing a clearer criterion of enforceability that is available to the parties, namely the criterion of consent to obligation. He says that:

> A consent theory provides a focus for contemporary dissatisfaction with the doctrine of consideration, while putting into better perspective the recognised need to enforce some gratuitous commitments and to protect some acts of reliance that were not bargained for.[78]

The traditional defences to contractual liability are seen in the context of consent theory as depriving the manifestation of consent of its normal moral and therefore legal significance.[79] The objective manifestation of consent must have been "voluntary". This will not be the case if, for example, the consent was improperly coerced by the promisee (duress) or was based on misinformation for which the promisor was responsible (misrepresentation). The defence of frustration of a contract is rationalised by inferring a tacit assumption on which the consent was based that certain types of events would not occur and that the promisee should bear the risk of their occurrence.

A difficulty that must be overcome if consent is to be regarded as the basis of contractual obligation is the judicial and legislative practice of implying terms. Some implied terms are commonly understood to be imposed by the legal system for reasons of policy, rather than consented to by the parties to the contract. However, Barnett takes the view that the set of implied terms which represent a genuine imposition on the parties is much smaller than is commonly thought.[80] He distinguishes three categories of terms:[81]

1. terms that are the product of "direct consent" (express or implied-in-fact terms);
2. terms that are the product of "indirect consent" (implied-in-law default rules); and
3. terms that are imposed on the parties without any consent (implied-in-law immutable terms).

Category (1) terms are based on the parties' consent. Category (2) terms are the kind that are incorporated into the contract by the courts or legislatures unless the parties agree to oust or vary them, so a manifest assent by the parties to the contrary will displace or vary

77 Barnett, "A Consent Theory of Contract" (1986) 86 *Columbia Law Review* 269, 309–10.

78 Barnett, "A Consent Theory of Contract" (1986) 86 *Columbia Law Review* 269, 319.

79 Barnett, "A Consent Theory of Contract" (1986) 86 *Columbia Law Review* 269, 318.

80 Barnett, "The Sound of Silence: Default Rules and Contractual Consent" (1992) 78 *Virginia Law Review* 821.

81 Barnett, "The Sound of Silence: Default Rules and Contractual Consent" (1992) 78 *Virginia Law Review* 821, 827–8.

the term. Category (3) terms are mandatory and cannot be displaced by a manifest assent to the contrary. The requirement of consent to be legally bound, the basis of consent theory, necessarily implies consent to the application of *some* set of default (and immutable) rules when a gap arises in a contract. Barnett argues that in certain circumstances silence by parties in the face of category (2) default rules can constitute consent to the imposition of those *particular* default rules. He believes that default rules are often indirectly consented to by the parties who could have "contracted around" the rules but did not do so. If the parties are informed and can be counted on to know the law and to vary any default rule that did not reflect their subjective intentions, such parties by their silence have indirectly consented to the default rule. "So long as the costs of learning the content of default rules and of contracting around them are sufficiently low, silence by the parties in the face of a default rule can constitute consent to its imposition".[82] If, on the other hand, the parties are not in this situation, the default rule is only likely to reflect the parties' consent if the law has adopted a "conventionalist" default rule (ie, one that reflects the conventional or common sense understanding of the community) as this is likely to accord with the parties' subjective intentions.[83]

Another potential problem for a consent theory is that contractual obligations routinely arise from standard form contractual documents that are signed without being read. Barnett argues that a person who signs a standard form contract (or clicks "I agree" on a website displaying contractual terms) manifests an intention to be legally bound by whatever is contained in the document, even if he or she does not know what those contents are.[84] Barnett explains that a person can accept an unknown obligation because contract law facilitates the assumption of risk. A person who agrees to contractual terms without having read them is simply accepting the risk that she may regret the transaction at some later time when she learns of the content of the agreement. There is, however, an implicit limit, according to Barnett. A person who signs an unread document manifests an intention to be bound only by terms of a kind one would expect to find in such a document; accordingly, there is no manifested consent to terms that are "radically unexpected".[85]

Those who believe that subjective consent is the only "real" consent may regard Barnett's consent theory of contract as harbouring a misnomer. If consent is not real, then the resultant contractual duties appear to be imposed in much the same way as torts duties. For Barnett, however, a manifested consent can be real even when it is not accompanied by subjective assent. As he says:

> This is because the concept of consent that is at the root of contract theory is *communicated* consent, though one reason for the centrality of communicated consent is its close empirical correspondence with subjective assent.[86]

82 Barnett, "The Sound of Silence: Default Rules and Contractual Consent" (1992) 78 *Virginia Law Review* 821, 897.

83 For criticism of Barnett's analysis of default rules, see Robertson, "The Limits of Voluntariness in Contract" (2005) 29 *Melbourne University Law Review* 179, 211–3.

84 Barnett, "Consenting to Form Contracts" (2002) 71 *Fordham Law Review* 627, 635–6.

85 Barnett, "Consenting to Form Contracts" (2002) 71 *Fordham Law Review* 627, 637. For criticism of Barnett's analysis of standard form contracting, see Robertson, "The Limits of Voluntariness in Contract" (2005) 29 *Melbourne University Law Review* 179, 190–3.

86 Barnett, "The Sound of Silence: Default Rules and Contractual Consent" (1992) 78 *Virginia Law Review* 821, 859 (fn 81).

ECONOMIC ANALYSIS OF CONTRACT LAW

[1.30] Contract law can also be understood in functional terms, as an instrument of some social good. Contract law has, for example, been analysed as a mechanism for promoting the beneficial social practice of "making and keeping promises and agreements".[87] The enforcement of contracts has also been justified on the basis that it provides a peaceful mechanism for the resolution of disputes and thus serves the public interest in the maintenance of social peace.[88] By far the most influential instrumental analysis of contract law, however, understands it to be justified and shaped by the pursuit of economic efficiency.

Economic analysis has been a significant force in the field of contract law in North America in the last 30–40 years.[89] Economic analysis of law involves analysing legal rules by reference to their ability to promote efficient market outcomes. A transaction enhances economic efficiency if it results in the transfer of goods or services to a person who values them more highly. Economic analysis places a high value on voluntary exchanges. Individuals are assumed to be the persons best placed to assess their own welfare. Voluntary exchanges move resources to their most valued uses because an individual will only exchange a thing (such as money, goods or services) for another thing that he or she values more highly. This analysis assumes the individual to be a "self-interested egoist who maximises utility".[90] It is not assumed that all individuals are rational, but that the utility-maximising individual represents a "weighted average of the individuals under study in which the non-uniformities and extremes in behaviour are evened out".[91]

Economic functions of contract law

[1.35] Given its emphasis on voluntary exchanges, it is not surprising that the neo-classical economic analysis of contract law, like classical contract theory, favours a principle of freedom of contract and discourages state intervention. Nonetheless, most adherents of an economic analysis of law would accept that contract law fulfils a number of important functions in regulating voluntary exchange. Richard Posner has argued that voluntary exchanges would still take place without contract law, but the system would be much less efficient because contracting parties would need to implement costly measures to protect themselves against opportunistic behaviour.[92]

Michael Trebilcock identifies four functions of contract law in promoting economic efficiency.[93]

87 Murphy, "The Practice of Promise and Contract", in Klass, Letsas and Saprai (eds), *Philosophical Foundations of Contract Law* (2014), pp 151, 169; Murphy, "The Formality of Contractual Obligation", in Robertson and Goudkamp (eds), *Form and Substance in the Law of Obligations* (2019), p 151.

88 MacMahon, "Conflict and Contract Law" (2018) 38 *Oxford Journal of Legal Studies* 270.

89 For a recent overview and discussion, see Katz, "Economic Foundations of Contract Law", in Klass, Letsas and Saprai (eds), *Philosophical Foundations of Contract Law* (2014), p 171.

90 Veljanovski, "The Economic Approach to Law: A Critical Introduction" (1980) 7 *British Journal of Law and Society* 158, 162.

91 Veljanovski, "The Economic Approach to Law: A Critical Introduction" (1980) 7 *British Journal of Law and Society* 158, 162.

92 Posner, *Economic Analysis of Law* (9th ed, 2014), §4.1.

93 Trebilcock, *The Limits of Freedom of Contract* (1993), pp 15–7; Trebilcock, "The Value and Limits of Law and Economics", in Richardson and Hadfield (eds), *The Second Wave of Law and Economics* (1999), p 12.

Containing opportunism in non-simultaneous exchanges

[1.40] A first economic function of contract law is to contain opportunistic conduct. Where parties do not perform their contractual obligations at the same time, the party performing second may engage in opportunistic behaviour. The incentive for such conduct will occur where, after the contract is made and one party has performed, something causes the other party to regret making the commitment. The contract might, for example, prove to have been a bad deal because the market price has changed or a better opportunity has arisen. The party who has not performed may then seek to renege on the contract, despite the expectations of the other party and his or her reliance in performing. As we shall see, contract law enforces contracts by requiring a party who refuses to perform in breach of contract to pay damages to the other party and, in some cases, may order specific performance of the contract. Proponents of an economic analysis of law stress that these rules provide important protection for contracting parties against such opportunistic advantage-taking. There are also many non-legal incentives for parties to perform contracts, such as the value of a good reputation, which may in fact prove a more significant incentive for loyalty to a contract than the law.[94]

Reducing transaction costs

[1.45] A second economic function of contract law is to reduce transaction costs. Contract law reduces transaction costs by supplying *default rules*. Default rules are rules that will apply to all contracts, or to all contracts of a certain type, unless the parties have excluded their application. As we shall see, contract law recognises numerous terms that are routinely implied in certain types of contracts.[95] Moreover, many of the general rules of contract law, such as those governing termination, may be seen as default rules.[96] Default rules save the parties the expense of having to negotiate and draft provisions dealing with particular contingencies. Proponents of the economic approach argue that the default rules of contract law should encourage or facilitate efficiency-enhancing behaviour. This can be done in one of two ways. First, default rules might attempt to provide outcomes that best approximate what the parties themselves would have agreed on had they had the opportunity. Secondly, default rules can be formulated in such a way that they provide incentives or disincentives that encourage parties to behave efficiently.

Filling gaps in incomplete contracts

[1.50] A third function of contract law, which is closely related to the provision of default rules, is to fill gaps in incomplete contracts by dealing with those matters on which the parties have not expressly reached agreement. A contract may prove incomplete where the parties fail to foresee or provide for a particular contingency affecting performance of their contract. As we shall see, where a contingency for which the parties have not provided occurs, courts are in some cases prepared to imply terms in contracts on a one-off basis.[97] The doctrine of frustration, which relieves parties from their obligations where performance becomes

94 See [26.135].

95 See Chapter 14.

96 See Chapter 21.

97 See Chapter 14.

impossible or radically different from what they intended, may also be seen as a gap-filling rule.[98]

Distinguishing welfare-enhancing and welfare-reducing exchanges

[1.55] A fourth economic function of contract law is to provide excuses for non-performance. Contract law thus discourages exchanges that are inefficient because of a market failure. As we shall see, the law of contract recognises a range of factors as vitiating a contract and justifying non-performance, such as where a party has been misled, has entered into a contract on the basis of a mistake or has been subjected to illegitimate pressure to enter into a contract. These vitiating factors may be seen in economic terms as regulating cases of market failure, such as information failure[99] and lack of voluntariness.[100]

Emphasis on consequences

[1.60] Much legal analysis is confined to considering the effect of a particular rule in resolving a dispute that has occurred between the parties in a particular case. By contrast, economic analysis directs our attention to the broader consequences of a rule. Economic analysis considers the broader functions of contract law rules and analyses how well those rules fulfil their functions. Adherents of an economic analysis of law ask: what sort of incentives will the rule provide to contracting parties in the future? Economic analysis is concerned with the overall effect of the rule in either encouraging or discouraging efficient outcomes, rather than with the results in a particular case.[101]

Criticism of economic analysis

[1.65] One criticism of the economic analysis of law is that its emphasis on individual autonomy reflects an "impoverished, pre-social conception of human life".[102] As noted earlier in this chapter, adherents of an economic analysis of law presume a contracting party to be a "self-interested egoist who maximises utility".[103] By contrast, as discussed below, relational contract theorists argue that human behaviour is not merely influenced by self-interest but also by social bonds, such as those between families and communities, and also by values such as loyalty and altruism. An account of contracting behaviour that does not take account of these social influences on human behaviour will, on this view, be incomplete.

Another criticism of law and economics is that the concepts deployed are indeterminate and commonly rely on unexpressed value judgments.[104] For example, a person's decision in a particular situation will be optimal in an economic sense only if it is voluntary and informed. These are abstract concepts and there can be much argument about what they require. As Trebilcock argues, in the real world, few choices are made with perfect information or free

98 See Chapter 15.

99 See Part XIA, Chapters 31–33, "Misinformation".

100 See Part XIB, Chapters 34–38, "Abuse of Power".

101 Craswell, "Against Fuller and Perdue" (2000) 67 *University of Chicago Law Review* 99.

102 Trebilcock, *The Limits of Freedom of Contract* (1993), p 18.

103 Veljanovski, "The Economic Approach to Law: A Critical Introduction" (1980) 7 *British Journal of Law and Society* 158, 162.

104 Trebilcock, *The Limits of Freedom of Contract* (1993), p 19.

from pressures of any kind.[105] Accordingly, value judgments will be required to determine what amount of pressure should invalidate a transaction and what degree of information imperfection should be tolerated.[106]

A third criticism of economic analysis of contract law concerns its neglect of the issue of distributive justice.[107] Economic analysis focuses on the question whether an exchange is efficient, rather than on whether the allocation of resources between the parties involved was fair to begin with. Trebilcock explains that proponents of economic analysis of law assume that contracting parties have equal opportunities but ignore the fact that individuals do not "start out equal, if only because of the effects of the genetic lottery or early family circumstances, which are morally arbitrary".[108] Trebilcock gives the following example:

> Suppose a starving painter or artist agrees to sell for "a song" a book or painting he or she has been working on for years to raise a couple of dollars to buy a loaf of bread. Does this transaction meet the Pareto criterion? The answer is yes in the sense that the seller of the book or painting prefers two dollars to the book or painting and the buyer of the latter prefers it to the two dollars he agrees to pay for it. Similarly in the case of the bread transaction. Everybody seems to be better off, but we may wish we lived in a society where people did not find themselves in such desperate circumstances that they have to sell their life's work to buy a loaf of bread. The Pareto criterion provides no purchase on this problem, implying that economics has no theory of distributive justice.[109]

A fourth criticism of law and economics is that it emphasises the desirability of giving effect to parties' choices or preferences without applying any ethical criteria to the value of those preferences.[110] We may consider that some choices are not worthy of recognition. For example, we may consider that choices should not be sanctioned where they would cause harm to other people. We may also consider that some people do not have the capacity to decide what is in their own best interests, such as children or persons who are mentally incapacitated. Only value judgments can tell us what limits should be imposed on individual autonomy.

Although economic analysis continues to play a dominant role in contract law literature in the United States, Eric Posner has judged economic analysis of contract law a failure in terms of explaining contract doctrine and in terms of generating ideal contract law rules.[111] Posner notes that, despite its dominance, economic analysis has had very little influence on US contract law. Simple economic models are unhelpful because they "exclude relevant variables", while complex models are unable to justify reform because "the optimal rule depends on empirical conditions that cannot be observed".[112] The literature is becoming increasingly sophisticated as more complex models are developed but no more helpful for understanding or reforming contract law.

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105 Trebilcock, *The Limits of Freedom of Contract* (1993), p 20.

106 See generally Trebilcock, *The Limits of Freedom of Contract* (1993).

107 Trebilcock, *The Limits of Freedom of Contract* (1993), p 20.

108 Trebilcock, *The Limits of Freedom of Contract* (1993), p 20. See also Duggan, *The Economics of Consumer Protection: A Critique of the Chicago School Case against Intervention* (1982), pp 98–100.

109 Trebilcock, "The Value and Limits of Law and Economics", in Richardson and Hadfield (eds), *The Second Wave of Law and Economics* (1999), p 20.

110 Trebilcock, *The Limits of Freedom of Contract* (1993), p 21.

111 Posner, "Economic Analysis of Contract Law after Three Decades: Success or Failure?" (2003) 112 *Yale Law Journal* 829.

112 Posner, "Economic Analysis of Contract Law after Three Decades: Success or Failure?" (2003) 112 *Yale Law Journal* 829, 854.

Some proponents of economic analysis of contract law have tried to respond to some of these criticisms of the economic approach. They have tried to adopt a less dogmatic approach to the economic analysis of contract law than that which is often associated with the neo-classical approach. Scholars such as Michael Trebilcock and Gillian Hadfield have tried to combine the rigour of an economic analysis, in particular its emphasis on assessing the consequences of legal rules, with the insights of other theoretical perspectives in order to enrich those provided by an economic analysis.[113]

Economic perspectives are considered in relation to estoppel in Chapter 9, implied terms in Chapter 14, contract remedies in Chapters 26, 27, 28 and 30 and vitiating factors in Chapters 31, 34 and 39.

CRITICAL LEGAL SCHOLARSHIP

[1.70] The CLS movement has attempted to expose the ideology of contract law and the contradictions within contract doctrine.[114] CLS literature on contract law is extremely rich and diverse and draws on a number of different philosophical traditions. Broadly speaking, it involves a critique of legal formalism in contract law: the notion of contract law as a set of value-free, abstract rules that can be applied to any fact situation with predictable results. The CLS movement has sought to expose the way in which contract doctrine conceals the political choices made by judges. Contract law has been a central focus of the CLS movement, because it provides such a clear example of the formalist model and has an identifiable ideological agenda. That agenda is to support the existing economic and social order and to suppress communitarian values and collective interests.[115]

Drawing on the technique of deconstruction, some CLS writing on contract law has been concerned to expose the unquestioned assumptions and inconsistencies of contract law.[116] This begins with exposing the dualities that exist in contract law, the most important of which are: market versus community, individualism versus altruism, self versus other, form versus substance. Contract law is generally thought to favour the first of each of those poles: markets over community, individualism over altruism, self over other and form over substance. It is clear that the disfavoured poles play a role in contract law, although there are different interpretations of what that role is. Jay Feinman argues that the dichotomies between the favoured and disfavoured poles make contract law incoherent, because it relies on contradictory principles and flips from one side to another.[117] Duncan Kennedy, on the other hand, argues that the occasional forays into altruism, substance and community values (through doctrines such as estoppel, unconscionable dealing and economic duress) preserve the existing structure by pre-empting more comprehensive reform.[118] Roberto Unger also argues that the less favoured poles are used to prop up the system.[119] He argues that they are

113 Trebilcock, *The Limits of Freedom of Contract* (1993); Hadfield, "The Second Wave of Law and Economics: Learning to Surf", in Richardson and Hadfield (eds), *The Second Wave of Law and Economics* (1999), p 50ff.

114 See Hillman, *The Richness of Contract Law* (1998), Ch 10.

115 See Feinman, "The Significance of Contract Theory" (1990) 58 *Cincinnati Law Review* 1283, 1308–13.

116 A good example of this is Dalton, "An Essay in the Deconstruction of Contract Doctrine" (1985) 94 *Yale Law Journal* 997.

117 Feinman, "Critical Approaches to Contract Law" (1983) 30 *UCLA Law Review* 829, 836.

118 Kennedy, "Form and Substance in Private Law Adjudication" (1976) 89 *Harvard Law Review* 1685.

119 Unger, "The Critical Legal Studies Movement" (1983) 96 *Harvard Law Review* 561.

given effect as vague slogans, such as unconscionability and good faith, which have a very limited impact on contract law. Unger also argues that the vagueness of contract doctrine is used to confine the disfavoured poles.

Given the broad range of approaches to contract law falling within the CLS movement, attempts to criticise the entire movement may be viewed as misguided. Nevertheless, general criticisms have been made.[120] Critical Legal Scholars have been criticised for their focus on appellate cases and legal doctrine, rather than empirical evidence concerning "the social 'impact' of law or the behaviour of legal actors".[121] Robert Hillman has argued that CLS writers overstate the indeterminacy of contract doctrine. Hillman argues that contract law is sufficiently determinate that the results of most cases can be predicted.[122] Moreover, he suggests that such incoherence or malleability as exists in contract law need not necessarily be used to preserve and legitimise the status quo, but could be exploited as a means of effecting social change.[123] John Murray has gone further, suggesting that the CLS movement is "irrelevant and counterproductive" to the task of refining and enhancing legal doctrine because CLS scholars eschew doctrine and fail to offer an "alternative design" other than "an ambiguous 'communitarian' notion of a vague utopia".[124]

Some critical perspectives on the formation of contracts are provided in Chapter 3.[125]

FEMINIST ANALYSIS OF CONTRACT LAW

[1.75] Feminist analyses of the law have often concentrated on areas of the law that raise issues of specific concern to women, such as parts of criminal law, employment law and family law. Some feminists have also considered areas of the law that do not deal specifically with women but clearly affect them, such as the law of contracts. While those analysing the law from a feminist perspective generally share a concern to reveal and redress inequalities between men and women, feminist analyses of contract law reflect a range of political and theoretical perspectives.[126]

Three approaches

[1.80] It is possible to identify three different feminist approaches to contract law based on ideas of identical treatment, difference and subordination.[127] The second and third approaches involve different, rather than opposing, types of inquiry and therefore overlap.

120 For a defence of CLS writing on contract law against these criticisms, see Feinman, "The Significance of Contract Theory" (1990) 58 *Cincinnati Law Review* 1283, 1308–13.

121 Trubek, "Where the Action Is: Critical Legal Studies and Empiricism" (1984) 36 *Stanford Law Review* 575, 576.

122 Hillman, "The Crisis in Modern Contract Theory" (1988) 67 *Texas Law Review* 103, 107–10.

123 Hillman, "The Crisis in Modern Contract Theory" (1988) 67 *Texas Law Review* 103, 112.

124 Murray, "Contract Theories and the Rise of Neoformalism" (2002) 71 *Fordham Law Review* 869, 875. See also Fried, "The Ambitions of Contract as Promise" in Klass, Letsas and Saprai, *Philosophical Foundations of Contract Law* (2014), pp 17, 18–20.

125 At [3.140] and [3.150].

126 See Mulcahy (ed), *Feminist Perspectives on Contract Law* (2005).

127 See Sheehy, Background Paper, "Personal Autonomy and the Criminal Law: Emerging Issues for Women", reproduced in Graycar and Morgan, *The Hidden Gender of Law* (1990), p 40.

The identical treatment approach

[1.82] The identical treatment approach denies that there are any significant differences between women and men. Accordingly the approach "[c]alls for the elimination of legal or other distinctions between the sexes and promotes gender-neutral, strictly identical treatment of women and men".[128] The identical treatment approach has little to say about the modern law of contract, which generally does not purport to treat men and women differently.

The difference approach

[1.85] The difference approach is based on the idea that women are physically, socially, psychologically and politically different from men.[129] Substantive equality for women can only be achieved if the law takes those differences into account.[130] One version of the difference approach has been influenced by the work of Carol Gilligan.[131] Gilligan argues that, typically, men and women view life differently. Feminists influenced by Gilligan's work criticise the law as reflecting a masculine viewpoint and neglecting a feminine perspective. In relation to contract law, such feminists criticise the almost exclusive use of an abstract, rule-orientated and apparently neutral style of analysis. Feminists argue that this style of analysis relies on characteristics associated with the cultural stereotype of men.[132] A more contextualised approach to contract law would give voice to a "feminine" viewpoint.[133] Such a viewpoint might be subjective and context-specific. It might emphasise the role of values such as reliance, co-operation, respect for the other and compromise in contract law.[134] For some feminists applying a difference approach, relational contract theory[135] is seen as providing what they regard as a "feminine voice" in contract law.[136] This is because relational contract theory

128 Sheehy, Background Paper, "Personal Autonomy and the Criminal Law: Emerging Issues for Women", reproduced in Graycar and Morgan, *The Hidden Gender of Law* (1990), p 40.

129 Sheehy, Background Paper, "Personal Autonomy and the Criminal Law: Emerging Issues for Women", reproduced in Graycar and Morgan, *The Hidden Gender of Law* (1990), p 41.

130 Sheehy, Background Paper, "Personal Autonomy and the Criminal Law: Emerging Issues for Women", reproduced in Graycar and Morgan, *The Hidden Gender of Law* (1990), p 41.

131 See, eg, Gilligan, *In a Different Voice* (1982). See also Shaughnessy, "Gilligan's Travels" (1988) 7 *Law and Inequality Journal* 1, 9.

132 See, eg, Frug, "Re-Reading Contracts: A Feminist Analysis of Contracts Casebook" (1985) 34 *American University Law Review* 1065; Frug, "Rescuing Impossibility Doctrine: A Post-modern Feminist Analysis of Contract Law" (1992) 140 *University of Pennsylvania Law Review* 1029; Tilwell and Linzer, "The Flesh Coloured Band Aid" (1991) 28 *Houston Law Review* 791; Shultz, "The Gendered Curriculum: Of Contracts and Careers" (1991) 77 *Iowa Law Review* 55; Wightman, "Intimate Relationships, Relational Contract Theory, and the Reach of Contract" (2000) *Feminist Legal Studies* 93, 99–100.

133 Morgan, "Feminist Theory as Legal Theory" (1988) 16 *Melbourne University Law Review* 743, 756, discussing the work of Boyle, "Book Review" (1985) 63 *Canadian Bar Review* 427.

134 See, eg, Tilwell and Linzer, "The Flesh Coloured Band Aid" (1991) 28 *Houston Law Review* 791.

135 See [1.100]–[1.170].

136 See, eg, Threedy, "Feminists and Contract Doctrine" (1999) 32 *Indiana Law Review* 1247, 1258; Tilwell and Linzer, "The Flesh Coloured Band Aid" (1991) 28 *Houston Law Review* 791; Wightman, "Intimate Relationships, Relational Contract Theory, and the Reach of Contract" (2000) *Feminist Legal Studies* 93, 100. But cf Dow, "Law School Feminist Chic and Respect for Persons: Comments on Contract Theory and Feminism in the Flesh Coloured Band Aid" (1991) 28 *Houston Law Review* 819.

emphasises the importance of "relationships" in contract and the role of norms such as trust and co-operation.[137]

A closely related, and overlapping, approach comes from feminists influenced by postmodern literary theory. Postmodern feminism is also closely associated with the CLS movement. Some postmodern feminists focus on the dichotomies in legal discourse.[138] These scholars then explore the ways in which the dichotomies in legal discourse mirror cultural stereotypes of women and men.[139] Mary Joe Frug explains that through this process "[p]ostmodern feminists attempt to overcome the male/female opposition by accepting it and at the same time disrupting it".[140]

The difference approach might be criticised as perpetuating undesirable stereotypes about masculine and feminine characteristics.[141] Proponents might respond that by drawing attention to the gender implications of contract law doctrine and analysis, they are mounting a radical challenge to legal thought. Indeed if, as these feminists argue, contract law is premised on a masculine viewpoint, then gender reform may not merely be a case of introducing a feminine voice. Rather the entire legal system might have to be rethought. Alternatively, we might need to recognise that certain values remain outside the law.[142]

The subordination approach

[1.90] The subordination approach is associated with the work of Catherine MacKinnon.[143] This approach sees women's inequality in terms of subordination to men, rather than differences between women and men. Scholars adopting this approach evaluate particular legal practices and policies in order to "assess whether they operate to maintain women in a subordinate position".[144] If those policies and practices are justified on the basis of differences between men and women, "then the differences themselves must also be examined to ascertain whether they are consequences of social or economic oppression".[145]

Applied to contract law, the subordination approach suggests that the gender of the parties, and consequentially the power relation between them, must be taken into account in resolving contractual disputes.[146] The subordination approach makes high demands of the law in resolving disputes. It requires the law to go beyond formal legal principles to examine the reality of the power relations between the parties involved. This approach offers a radical re-envisioning of the role and function of contract law.

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137 See Mulcahy, "The Limitations of Love and Altruism", in Mulcahy (ed), *Feminist Perspectives on Contract Law* (2005), p 1.

138 See [1.70].

139 Frug, "Rescuing Impossibility Doctrine: A Post-modern Feminist Analysis of Contract Law" (1992) 140 *University of Pennsylvania Law Review* 1029, 1031.

140 Frug, "Rescuing Impossibility Doctrine: A Post-modern Feminist Analysis of Contract Law" (1992) 140 *University of Pennsylvania Law Review* 1029, 1064.

141 See Otto, "A Barren Future? Equity's Conscience and Women's Inequality" (1992) 18 *Melbourne University Law Review* 808, 812.

142 See Shaughnessy, "Gilligan's Travels" (1988) 7 *Law and Inequality Journal* 1.

143 See, eg, MacKinnon, *Feminism Unmodified* (1987).

144 Sheehy, Background Paper, "Personal Autonomy and the Criminal Law: Emerging Issues for Women", reproduced in Graycar and Morgan, *The Hidden Gender of Law* (1990), p 42.

145 Sheehy, Background Paper, "Personal Autonomy and the Criminal Law: Emerging Issues for Women", reproduced in Graycar and Morgan, *The Hidden Gender of Law* (1990), p 42.

146 Frug, "A Critical Theory of Law" (1989) 1 *Legal Education Review* 43, 56.

Feminist approaches and the "wives" special equity

[1.95] These three feminist approaches can be illustrated by considering the decision in *Garcia v National Australia Bank Ltd* (*Garcia*).[147] In that case, the High Court of Australia recognised the continued existence of a special principle protecting women who guarantee their husbands' business loans, where the woman has either been subject to undue influence by her husband or has misunderstood the effect of the guarantee.[148]

A proponent of the identical treatment approach might argue that maintaining a special equity or principle applying to wives perpetuates undesirable sexual stereotypes of women as incapable of making financial decisions or protecting their own interests. Thus, for example, Kirby J said in *Garcia*:

> For this court to accept that principle is to accord legitimacy to a discriminatory rule expressed in terms which are unduly narrow, historically and socially out of date and unfairly discriminatory against those who may be more needful of the protection of a "special equity" but who do not fit within the category of married women.[149]

Proponents of both the difference and the subordination approaches might argue that an approach based on formal equality would ignore the very real social differences and power imbalances between men and women.[150] Proponents might argue that women do not always exercise independent judgment in deciding to guarantee their husbands' business loans.[151] Thus, in *Garcia*, the High Court said:

> That Australian society and particularly the role of women in that society has changed in the last six decades is undoubted. But some things are unchanged. There is still a significant number of women in Australia in relationships which are, for many and varied reasons, marked by disparities of economic and other power between the parties.[152]

Given this social reality, Richard Haigh and Samantha Hepburn argue that the *Garcia* principle is desirable even though it relies on a stereotype because it operates to protect a vulnerable group in society.[153] They explain that the "type of analysis required in *Garcia* relies on stereotypes not to cement prejudice in place, but to critically reassess the nature of spousal guarantees and thereby balance gender ideals with practical realities".[154]

A proponent of the difference approach might argue that the special protective principle in *Garcia* is justified because, in deciding to guarantee their husbands' business borrowings, women are often influenced by factors other than their own economic interests. Wives are

147 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395.

148 The decision is discussed further in Chapter 37.

149 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395, 425.

150 See, eg, Thompson, "Feminist Relational Contract Theory: A New Model for Family Property Agreements" (2018) 45 *Journal of Law and Society* 617 and, in the broader family law context, Fehlberg, Sarmas and Morgan, "The Perils and Pitfalls of Formal Equality in Australian Family Law Reform" (2018) 46 *Federal Law Review* 367.

151 We might also note that, although numerous cases have come before the courts on this issue, there is little statistical information on the extent of the problem: see Haigh and Hepburn, "The Bank Manager Always Rings Twice: Stereotyping in Equity after Garcia" (2000) 26 *Monash University Law Review* 275, 303–4.

152 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395, 403–4.

153 Haigh and Hepburn, "The Bank Manager Always Rings Twice: Stereotyping in Equity after Garcia" (2000) 26 *Monash University Law Review* 275, 127.

154 Haigh and Hepburn, "The Bank Manager Always Rings Twice: Stereotyping in Equity after Garcia" (2000) 26 *Monash University Law Review* 275, 302.

sometimes subjected to pressure by their husbands. Even in the absence of pressure, wives may be influenced by the bonds of relationship, trust and reliance. Proponents of the difference approach might argue that legal protection is needed to ensure that the trust and reliance shown by wives is not abused or exploited. This view is reflected in the reasoning of the majority judges in *Garcia*. Their Honours explained that the rationale of the principle "is not to be found in notions based on the subservient or inferior economic position of women. Nor is it based on their vulnerability to exploitation because of their emotional involvement".[155] Instead, the majority judges said, the principle "is based on trust and confidence, in the ordinary sense of those words, between marriage partners".[156]

Proponents of the subordination approach, while not disagreeing with the special protection accorded to wives by the decision in *Garcia*, might focus on the disparities of power that may exist between husband and wife. It might be said that, because of the subordinated position of many married women, a woman's guarantee of her husband's debts cannot be presumed to have been given freely. It might be argued that the law should go beyond merely recognising the vulnerability of wives guaranteeing their husbands' debts and should strive to address that vulnerability. Thus, Dianne Otto argues that if the principle applied in *Garcia*:

> is applied paternalistically so as to protect the wife/woman because of her subordinate position, the [principle] does nothing to change her position of inequality. In effect, it operates to institutionalise her subordination by presuming that protection is necessary. On the other hand, if the [principle] arises from an acknowledgement of the socio-structural origins of women's inequality, and the legal response is directed towards altering the distribution of power that creates the relationship of influence, some broader social change may result.[157]

The *Garcia* decision treats the provision of independent advice as a panacea for some of the problems faced by women guaranteeing their husbands' debts. Proponents of the subordination approach might argue that providing independent advice is not a solution where the woman's consent to the guarantee is a result of her subordination to her husband.[158] Accordingly, measures with deeper implications for the power relationship might be required. Otto suggests that a legal response directed to altering the distribution of power might, for example, be achieved by requiring husbands (seeking to borrow on the strength of guarantees given by their wives) "to show that they have taken tangible steps to alter their position of social dominance in the relationships in question".[159]

Feminist perspectives are further considered in relation to terms in standard form contracts in Chapter 12 and in relation to third-party impropriety in Chapter 37.

CONTRACT AS SOCIAL RELATION

[1.100] Contract can also be seen as a social relationship between transacting parties, which is an inseparable part of a much broader web of social relations. A major criticism of classical

155 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395, 404.

156 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395, 404.

157 Otto, "A Barren Future? Equity's Conscience and Women's Inequality" (1992) 18 *Melbourne University Law Review* 808, 820.

158 Otto, "A Barren Future? Equity's Conscience and Women's Inequality" (1992) 18 *Melbourne University Law Review* 808, 826.

159 Otto, "A Barren Future? Equity's Conscience and Women's Inequality" (1992) 18 *Melbourne University Law Review* 808, 820.

contract theory and neo-classical economic theory is that they both assume that each contract involves a discrete, one-off exchange. Empirical study has shown that this does not always reflect the way in which people do business, and this has led to a substantial movement that focuses on the social relations between contracting parties. This approach is sometimes described as *relational contract theory*.

Empirical studies

[1.105] Interest in the relational aspect of contract began with a groundbreaking empirical study by Stewart Macaulay in the 1960s, which revealed that in certain contexts some business people pay little regard to the law of contract when they enter into business transactions, make adjustments and resolve disputes.[160] Instead of looking at the role of contract law in the courtroom, Macaulay looked at the role of contract law in business practices and the extent to which business people actually *used* contract law. Macaulay focused on the manufacturing sector in Wisconsin. His approach was to interview a large number of business people and lawyers employed by manufacturing companies and to consider the extent to which principles of contract law shaped planning, adjustment and dispute resolution amongst those involved in the industry.

Planning

[1.110] The principles of contract law are based on the assumption that contracting parties carefully plan their relationships. Lawyers and judges assume that the parties will make provision for as many future contingencies as can be foreseen.[161] Many transactions are indeed planned very carefully. Large one-off transactions tend to be extensively planned, and most companies engage in standardised planning through the use of standard forms.[162] Macaulay found, however, that parties often failed to detail their obligations properly. Expensive machinery, for example, was often ordered without agreement on performance specifications. Macaulay noted that business people often preferred to rely on a person's word or handshake, or "common honesty and decency", even when a transaction involves exposure to serious risks.[163] The desire was to keep transactions simple and avoid red tape. In most cases, buyers and sellers were simply concerned to ensure that there was agreement on the basics (quantity, specifications and price) and did not care about the "boilerplate" on the back of the forms.

Adjustment

[1.115] Exchanges are adjusted when the parties agree to modify or cancel a transaction because of changed circumstances.[164] A buyer may, for example, be allowed to cancel an order for goods because they are no longer needed, or a seller may be paid more than the contract price because of an unexpected rise in the cost of inputs. Macaulay found that all

160 Macaulay, "Non-contractual Relations in Business: A Preliminary Study" (1963) 28 *American Sociological Review* 55.

161 Macaulay, "An Empirical View of Contract" [1985] *Wisconsin Law Review* 465.

162 Macaulay, "Non-contractual Relations in Business: A Preliminary Study" (1963) 28 *American Sociological Review* 55, 57–8.

163 Macaulay, "Non-contractual Relations in Business: A Preliminary Study" (1963) 28 *American Sociological Review* 55, 58.

164 See further [4.65]-[4.105].

purchasing agents expected to be able to cancel orders, subject only to paying for major wasted expenditure, even though sellers would be legally entitled to more extensive compensation, including lost profits.[165] He found that sellers routinely accepted cancellations even though the buyer had no legally recognised excuse. One sales representative for a paper company said, "[y]ou can't ask a man to eat paper when he has no use for it".[166]

Settlement of disputes

[1.120] Macaulay's findings in relation to the settlement of disputes are perhaps the least surprising aspects of his study. Given the high cost of litigation, it is no surprise that businesspeople find other ways to resolve disputes. What is perhaps surprising is that most disputes were solved without any reference to the agreement or the parties' legal rights.[167] Macaulay found that the threat of legal sanctions ranked very low on the scale of reasons for keeping contractual promises.[168] Contractual obligations were kept in order to maintain personal relationships, business relationships and reputation in the industry. Litigation was most common *after* a relationship had been terminated or because of termination of a relationship (such as the termination of a dealer's franchise). There was then no relationship to preserve.

Conclusions and implications

[1.125] Macaulay's most important findings have been confirmed by other researchers. Other studies have shown that while large sales transactions tend to be carefully negotiated and documented,[169] businesspeople in some contexts are "neither aware of nor significantly influenced by" relevant principles of contract law.[170] Buyers and sellers are willing to adjust contract prices and modify contractual obligations in a range of circumstances.[171] It is important to note, however, that these conclusions are based on only a few small-scale studies that have focused on practices in particular industries in particular locations. We need to be cautious about drawing general conclusions.[172] If the behaviour of contracting parties in other areas of commercial life was examined, a different picture might well emerge. Corporations supplying goods and services to consumers, for example, tend to engage in

165 Macaulay, "Non-contractual Relations in Business: A Preliminary Study" (1963) 28 *American Sociological Review* 55, 61.

166 Macaulay, "Non-contractual Relations in Business: A Preliminary Study" (1963) 28 *American Sociological Review* 55, 61.

167 Macaulay, "Non-contractual Relations in Business: A Preliminary Study" (1963) 28 *American Sociological Review* 55, 61.

168 See further Charny, "Nonlegal Sanctions in Commercial Relationships" (1990) 104 *Harvard Law Review* 373.

169 Beale and Dugdale, "Contracts between Businessmen: Planning and the Use of Contractual Remedies" (1975) 2 *British Journal of Law and Society* 45, 50; Keating, "Exploring the Battle of the Forms in Action" (2000) 98 *Michigan Law Review* 2678, 2697–8.

170 Schultz, "The Firm Offer Puzzle: A Study of Business Practice in the Construction Industry" (1952) 19 *University of Chicago Law Review* 237, 283. See also Keating, "Measuring Sales Law against Sales Practice: A Reality Check" (1997) 17 *Journal of Law and Commerce* 99; Keating, "Exploring the Battle of the Forms in Action" (2000) 98 *Michigan Law Review* 2678; Beale and Dugdale, "Contracts between Businessmen: Planning and the Use of Contractual Remedies" (1975) 2 *British Journal of Law and Society* 45.

171 Weintraub, "A Survey of Contract Practice and Policy" [1992] *Wisconsin Law Review* 1, 18–24.

172 See Korobkin, "Empirical Scholarship in Contract Law: Possibilities and Pitfalls" [2002] *University of Illinois Law Review* 1033, 1051–6; Hillman, *The Richness of Contract Law* (1998), pp 244–55.

careful standardised planning through the use of standard forms[173] and may be more likely to rely on contract terms in resolving disputes.[174] If one looked at commercial banking one would also be likely to find an extremely high degree of planning (extensive articulation of the parties' obligations and provision for a wide range of future contingencies), heavy reliance on the existence of legal sanctions and frequent use of legal sanctions. Even when legal sanctions are not commonly used, they may play an important role in deterring breach and providing some assurance of performance.[175] Nevertheless, the studies by Macaulay and others in a similar vein offer two important insights. First, they draw our attention to the fact that trust and social relationships play a significant role in some contractual relations. Secondly, they show that contractual rights and obligations are not always the most important factors influencing business people planning transactions, adjusting agreements and resolving disputes.

Relational contract theory

[1.130] The empirical studies discussed at [1.05]–[1.125] suggest that parties to commercial contracts are not necessarily the hard-bargaining individuals engaged in well-planned, discrete transactions that classical contract theory and neo-classical economics may lead us to believe. Parties to commercial contracts are often engaged in long-term relationships with one another, or as part of a close-knit industry, and that has a significant impact on the way in which they deal with one another. These empirical insights have given rise to a new way of looking at contracts. Rather than viewing contracts as discrete exchanges between utility-maximising individuals, relational contract theory views contract as a more complex social interaction. Macaulay identified the need to view contracts in a different way, which took into account the relations between the parties. Ian Macneil and others have explored what it meant to look at contract from a relational perspective.[176]

The discrete-relational spectrum

[1.135] Relational analysis of contracts is based on the recognition of the fact that contractual relations are conducted within a social matrix. Exchange is only possible within a society that provides: first, a means of communication (so the parties can understand one another); secondly, a system of order (so that the parties use exchange rather than force to get what they want); thirdly, a payment mechanism; and fourthly, where some

173 Hillman, *The Richness of Contract Law* (1998), p 247.

174 Whitford, "Law and the Consumer Transaction: A Case Study of the Automobile Warranty" [1968] *Wisconsin Law Review* 1006.

175 Weintraub, "A Survey of Contract Practice and Policy" [1992] *Wisconsin Law Review* 1, 24–6.

176 Macneil's principal works on relational contract theory are: "The Many Futures of Contracts" (1974) 47 *Southern California Law Review* 691; "Contracts: Adjustment of Long-term Economic Relations under Classical, Neo-classical and Relational Contract Law" (1978) 72 *Northwestern University Law Review* 854; *The New Social Contract* (1980); "Economic Analysis of Contractual Relations: Its Shortfalls and the Need for a 'Rich Classificatory Apparatus'" (1981) 75 *Northwestern University Law Review* 1018; "Efficient Breach of Contract: Circles in the Sky" (1982) 68 *Virginia Law Review* 947; "Values in Contract: Internal and External" (1983) 78 *Northwestern University Law Review* 340; "Relational Contract: What We Do and Do Not Know" [1985] *Wisconsin Law Review* 483; "Relational Contract Theory: Challenges and Queries" (2000) 94 *Northwestern University Law Review* 877. See also Campbell (ed), *The Relational Theory of Contract: Selected Works of Ian Macneil* (2001) and Campbell, Mulcahy and Wheeler, *Changing Conceptions of Contract: Essays in Honour of Ian Macneil* (2013).

performance is to take place in the future, a mechanism for the enforcement of promises.[177] Since a contract can only be made against such a social background, all contracts are *relational*, in that they involve social relations and are embedded in a much broader social web. However, some contracts are more relational than others in that they are more deeply embedded in social relations. Macneil has suggested that there exists a spectrum of contractual behaviour, with highly relational contracts at one end and highly discrete transactions at the other.

The relational end of the spectrum

[1.140] A highly relational contract is one in which social relations play a significant role. This may be because performance of the contract is closely integrated with the parties' other activities, because the parties are relying heavily on social conventions or because the parties are involved in a long-term relationship. In a highly relational contract, the parties are less likely to be able to predict and deal with future contingencies. The more relational the exchange, the less the parties will plan the substance of the exchange and allocate risks. In these transactions, more flexibility will be required during the course of the relationship. Rather than setting out in detail their rights and obligations in relation to possible future eventualities, the parties to a highly relational contract are more likely to "plan structures and processes to govern the relation in the future".[178] Macneil notes that highly relational agreements that "contain a great deal of process planning" include collective bargaining agreements, corporate constitutions, government contracts and standardised construction contracts.[179]

Social relations may play a significant role in an exchange because the parties expect each other to behave in accordance with social customs and conventions which define their respective roles.[180] The role of medical practitioners, for example, is defined by social convention. A patient consulting a doctor about a particular medical problem would find it very difficult to spell out in advance the doctor's obligations in respect of diagnosis, treatment and referral. Instead of attempting to define the doctor's obligations in advance, the patient relies on the doctor to operate within and fulfil the doctor's socially understood role.

Social relations may also be important because the contract involves performance over a long period of time. Parties to a long-term contract, such as a contract of employment, must be flexible and co-operative in order to preserve the relationship. What the employer and employee expect of one another will inevitably change over the course of the relationship, and the parties embark on the relationship on the understanding that they will adapt to change. The parties cannot plan the entire future of the relationship but trust and rely on each other to deal with contingencies as they arise. These relational features are evident in the planning and adjustment of contracts between manufacturers and suppliers studied by Macaulay. Instead of planning for various contingencies at the outset, the parties deal with problems as they arise by adjusting their obligations and granting concessions in relation to time of performance or

177 Macneil, *The New Social Contract* (1980), p 11; Macneil, "Values in Contract: Internal and External" (1983) 78 *Northwestern University Law Review* 340, 344; Macneil, "Relational Contract Theory: Challenges and Theories" (2000) 94 *Northwestern University Law Review* 877, 884.

178 Gudel, "Relational Contract Theory and the Concept of Exchange" (1998) 46 *Buffalo Law Review* 763, 765. See Macneil, "The Many Futures of Contracts" (1974) 47 *Southern California Law Review* 691, 761–7.

179 Macneil, "The Many Futures of Contracts" (1974) 47 *Southern California Law Review* 691, 760.

180 Macneil calls this relational norm "role integrity"; see *The New Social Contract* (1980), pp 40–4, 65–6.

price. It may even be expected that one party will release the other from his or her contractual obligations altogether in order to preserve the broader relationship between the parties or one party's reputation within the industry.

The discrete end of the spectrum

[1.145] At the discrete end of the relational spectrum are transactions that are more isolated from the social context in which they are made. A relatively discrete transaction does not involve any significant co-ordination between performance of the contract and the parties' other activities, requires less flexibility and co-operation between the parties and does not draw so heavily on social conventions or understandings. A one-off exchange will usually be relatively discrete, but this will not always be the case. A single visit to a medical practitioner is likely to be highly relational, for the reasons discussed earlier in this chapter, even if the patient has not seen the doctor before and never does again.

Macneil's example of a highly discrete transaction is a motorist making a cash purchase of petrol at a service station on a highway on which the motorist rarely travels. This transaction involves the simultaneous (or almost simultaneous) exchange of goods and money and does not involve any ongoing obligations.[181] Even this transaction is deeply embedded in a broad and complex social web consisting of such things as social conventions regarding behaviour, brand loyalty (possibly involving loyalty reward schemes) and credit card or electronic payment mechanisms.[182]

An executory contract is one in which the obligations of the parties are to be performed at some time in the future. An executory contract may be relatively discrete, even if performance is to take place over a long period. In a discrete transaction, however, the parties are more likely to rely on specific planning than on co-operation or flexibility to deal with future contingencies. An executory contract involves the creation in the present of an obligation to perform an act in the future. Macneil uses the word "presentiation" to describe the process of treating the future as though it were the present. Presentiation in contract involves the parties attempting to anticipate every possible contingency which may affect the parties' performances and providing exhaustively for the consequences. You will recall that Macaulay regarded this sort of planning as "contractual" behaviour.

Contract law is premised on the assumption that parties will undertake this exercise when entering into a contract. The concept of converting the future into the present is fundamental to contract law. The assurance that the law will enforce executory promises (or promises to confer benefits in the future) allows future rights to be given a present value for the purposes of trade and credit. Elaborate planning makes a contract more discrete because it separates the transaction from the social relations between the contracting parties.

The importance of relational contracts

[1.150] Macneil argues that the needs of "a technologically complex and heavily capitalized society" cannot be satisfied by discrete transactions alone.[183] While some goods and services can be exchanged through relatively discrete transactions, greater flexibility is required for

181 Macneil, "The Many Futures of Contracts" (1974) 47 *Southern California Law Review* 691, 720–1.

182 Macneil, "Values in Contract: Internal and External" (1983) 78 *Northwestern University Law Review* 340, 344–5.

183 Macneil, "The Many Futures of Contract" (1974) *Southern California Law Review* 691, 758–66.

more complex forms of production and distribution.[184] An enterprise that cannot be completely planned from the beginning must have the capacity for "growth and change" that is provided by more relational arrangements.[185] This may explain why Macaulay found the manufacturing sector to use relational rather than "contractual" exchanges. Macneil illustrates the point by reference to the sale of wheat in the "heyday of laissez faire" in the 19th century. A sale of wheat may itself have been discrete, but there was a complex web of relationships involved in its production, including family farming partnerships, harvesting teams, milling and storage co-operatives, haulage and railroad companies and baking partnerships or companies. Each of those entities had a complex internal structure and relied on its own network of relationships, including those with financiers and employees.[186]

Consequences for contract law

[1.155] The next question is: what are the implications for contract law of these relational insights?[187] Macneil has stressed that his work is principally concerned with analysing the role of social relations in exchange transactions, rather than offering prescriptions for contract law.[188] The relational perspective does, however, suggest a deficiency in the classical approach to contract law. As we discussed earlier, classical contract law is based on the idea that parties enter into discrete exchanges, negotiate their rights and obligations fully and make provision for most of the likely contingencies in an agreement concluded at an identifiable point in time. Consequently, Gudel observes: "Contract law was and is relatively well adapted to dealing with discrete transactions. However, it was and is ill-equipped to deal with problems arising out of contract relations."[189] Macneil has observed that "transactional contract doctrines", such as the rules of offer and acceptance, are unsuited to exchanges that are not fully presentiated. He has suggested that it is possible to articulate "precise, intellectually coherent principles" which are "sufficiently open textured for effective use in the law of modern contractual relations"[190] and that these legal rules should track relational behaviour and relational norms.[191]

Catherine Mitchell has argued that relational theory justifies a stronger focus on the commercial expectations of contracting parties than English law currently allows, and less deference to contractual documents.[192] Mitchell advocates moving beyond the contextual interpretation of contractual agreements to a "fully contextual approach" to resolving

184 Gudel, "Relational Contract Theory and the Concept of Exchange" (1998) 46 *Buffalo Law Review* 763, 765.

185 Macneil, "The Many Futures of Contract" (1974) 47 *Southern California Law Review* 691, 765–6.

186 Macneil, "Relational Contract: What We Do and Do Not Know" [1985] *Wisconsin Law Review* 483, 490–1.

187 See generally Tan, "Disrupting doctrine? Revisiting the doctrinal impact of relational contract theory" (2019) 39 *Legal Studies* 98.

188 See, eg, Macneil, "Relational Contract Theory: Challenges and Theories" (2000) 94 *Northwestern University Law Review* 877, 898–9.

189 Gudel, "Relational Contract Theory and the Concept of Exchange" (1998) 46 *Buffalo Law Review* 763, 766.

190 Macneil, "Reflections on Relational Contract" (1985) in Campbell (ed), *The Relational Theory of Contract: Selected Works of Ian Macneil* (2001), p 295.

191 Macneil, "Relational Contract Theory: Challenges and Queries" (2000) 94 *Northwestern University Law Review* 877, 903. For an example of how this might be done, see Lees, "Contract, Conscience, Communitarian Conspiracies and Confucius: Normativism through the Looking Glass of Relational Contract Theory" (2001) 25 *Melbourne University Law Review* 82.

192 Mitchell, *Contract Law and Contract Practice: Bridging the Gap between Legal Reasoning and Commercial Expectation* (2013).

commercial contract disputes. Such an approach would not begin with contractual documents but with "other aspects of the contractual relationship" which "may reveal that the written documents were not that important to the parties at all and may be manifestly unreliable as a statement of their understandings about their agreement."[193] In another recent book, *Contract Law Minimalism*, Jonathan Morgan draws something close to the opposite conclusion.[194] Morgan argues that the relational perspective supports his argument that contract law should consist of minimalist, bright-line rules which can be easily understood by commercial parties and modified where necessary. Morgan's primary argument against more flexible, context-sensitive rules is that the courts lack the capacity to regulate effectively for trust and co-operation so it is better for the law to provide a set of simple, clear and unambitious optional rules which the parties can modify by express contractual provision.

The basis of contract

[1.160] Relational contract theory also has implications for unitary theories of contract law, such as promise and consent theory.[195] Relational theory contests the idea that promise is at the heart of contract. In more relational exchanges, since the parties do not plan in a comprehensive way, their promises are likely to be incomplete and so their association will be governed by relational norms.[196] Those relational norms include co-operation, compromise, flexibility and contractual solidarity.[197] A focus on promise as the basis of contract prevents us from understanding the nature of contract because it distracts attention from the important social context in which promises and express commitments are made.

Formation and contractual obligations

[1.165] For relational theorists, the classical notion of formation appears misconceived because it is based on the idea of an identifiable moment of contract formation at which the parties reach a "meeting of the minds". At the moment of formation, the contract is supposed to spring into existence, with the parties having agreed on all of their rights and obligations into the future. Both classical and contemporary contract law persistently try "to locate the entire content of the parties' agreement, and thus the entire source of their obligation to one another, in an initial moment of agreement".[198] From a relational perspective, reaching agreement on contract terms can be seen as an "incremental process" in which the parties "gather increasing information and gradually agree to more and more as they proceed".[199] Relational contract theory suggests that when committing to an exchange relationship, contracting parties "cannot specify all of the obligations and responsibilities that relation will

193 Mitchell, *Contract Law and Contract Practice* (2013), p 11.

194 Morgan, *Contract Law Minimalism: A Formalist Restatement of Commercial Contract Law* (2013).

195 Gudel, "Relational Contract Theory and the Concept of Exchange" (1998) 46 *Buffalo Law Review* 763, esp 769–86. For a defence of consent theory, see Barnett, "Conflicting Visions: A Critique of Ian Macneil's Relational Theory of Contract" (1992) 78 *Virginia Law Review* 1175.

196 Hillman, "The Crisis in Modern Contract Theory" (1988) 67 *Texas Law Review* 103, 124.

197 Macneil, "Values in Contract: Internal and External" (1983) 78 *Northwestern University Law Review* 340, 347.

198 Gudel, "Relational Contract Theory and the Concept of Exchange" (1998) 46 *Buffalo Law Review* 763, 757.

199 Macneil, "Economic Analysis of Contractual Relations: Its Shortfalls and the Need for a 'Rich Classificatory Apparatus'" (1981) 75 *Northwestern University Law Review* 1018, 1041. See also Macneil, "The Many Futures of Contract" (1974) 47 *Southern California Law Review* 691, 751.

entail".[200] Contracting parties make commitments that were not the subject of explicit promises at the time of formation. They commit themselves to doing what is necessary to "maintain the health" of the relationship and implicitly agree that the timing, manner, motivation and process of termination will be consistent with relational norms of behaviour.[201]

Two recent trends in Australian contract law may be said to reflect relational ideas.[202] First, as we will see in Chapter 3, Australian courts are increasingly willing to accept that a contract can be formed when agreement can be inferred from the conduct of the parties, even though a clear offer and acceptance cannot be identified.[203] In *Integrated Computer Services Pty Ltd v Digital Equipment Corporation (Australia) Pty Ltd*,[204] the New South Wales Court of Appeal accepted that the classical requirement of offer and acceptance was unsuited to contemporary commercial arrangements and that it may not be possible to identify all of the parties' rights and obligations by reference to the moment of formation. Referring specifically to empirical evidence as to the flexibility that is necessary to maintain ongoing business relationships, McHugh JA said:

> [I]n an ongoing relationship, it is not always easy to point to the precise moment when the legal criteria of a contract have been fulfilled … In a dynamic commercial relationship new terms will be added or will supersede older terms. It is necessary therefore to look at the whole relationship and not only at what was said and done when the relationship was first formed.[205]

A second relational trend in Australian law is the willingness of courts to recognise that contracting parties owe one another a duty to act in good faith when exercising contractual rights. In some cases, contracting parties have been held to owe an implied duty to act in good faith when exercising a power to terminate a contract.[206] In such cases, the courts look beyond the express promises made at the time of formation and require the parties to conform to broader implicit norms of behaviour. Developments such as these suggest that relational ideas may be quietly filtering into relevant aspects of contract law.

Criticism

[1.170] Some contract scholars argue that relational ideas do not have a useful role to play in the development of contract law. Michael Trebilcock has observed that relational contract theory "does not yield determinate legal principles" and that its "highly amorphous sociological inquiry" is too wide-ranging to be useful to courts in particular cases.[207] Melvin Eisenberg has argued that it is not possible to implement a set of principles governing relational contracts without developing an operational distinction between relational and discrete

200 Gudel, "Relational Contract Theory and the Concept of Exchange" (1998) 46 *Buffalo Law Review* 763, 786.

201 Gudel, "Relational Contract Theory and the Concept of Exchange" (1998) 46 *Buffalo Law Review* 763, 786. For a full explanation of relational norms, see Macneil, "Values in Contract: Internal and External" (1983) 78 *Northwestern University Law Review* 340.

202 Hillman, *The Richness of Contract Law* (1998), pp 262–3 notes that US law meets relational needs in the same way.

203 See [3.145].

204 *Integrated Computer Services Pty Ltd v Digital Equipment Corporation (Australia) Pty Ltd* (1988) 5 BPR 11,110.

205 *Integrated Computer Services Pty Ltd v Digital Equipment Corporation (Australia) Pty Ltd* (1988) 5 BPR 11,110, 11,117–11,118.

206 See Chapter 14.

207 Trebilcock, *The Limits of Freedom of Contract* (1992), pp 141–2. See also Kidwell, "A Caveat" [1985] *Wisconsin Law Review* 615.

contracts.[208] No such distinction can be developed, he suggests, because it would require us to draw an arbitrary line somewhere along the discrete/relational spectrum. If all contracts are relational to some extent, then there is no subcategory of contracts that should be governed by relational rules.[209] Accordingly, rules that take into account relational issues, such as those mentioned in the preceding section, must be either justified as general principles of contract law or rejected altogether.[210]

CONTRACT LAW AS REGULATION

[1.175] Contract law can also be understood as a means of regulating markets and exchanges. Jean Braucher has explained that "[t]he regulatory role of contract law is played out in … three normative dimensions": validity, interpretation and gap-filling.[211] First, the courts decide which exchanges should be enforced. Secondly, the courts interpret the language and conduct of the parties in order to identify the parties' rights and obligations. That process of interpretation "unavoidably involves normative choices about when obligation should arise and what its content should be".[212] Thirdly, the courts supply terms to deal with gaps and inconsistencies in the parties' agreement, "a process that constrains and in some cases replaces party control".[213] Braucher seeks to remind us that contract law plays a strong regulatory role and does not simply facilitate private ordering.

Hugh Collins sees common law contract rights as a form of state regulation.[214] This form of regulation gives rights to the parties themselves and allows them to enforce those rights through the mechanism of state sanctions provided by the courts. Collins calls this "private law regulation". Markets and exchanges can also be regulated publicly, through the legislative setting of standards enforced by a government agency, with or without the use of the courts. Public regulation occurs in some areas, such as competition law and consumer protection, often in conjunction with private law regulation.

If we see contract as a form of regulation, we can ask what form and content of legal regulation is best suited to the task of regulating markets.[215] The answer to this question will, of course, depend on what goals are to be pursued. Collins draws on economic analysis and relational contract theory to take economic efficiency, addressing market failure and the preservation of social relations to be the principal goals of contract regulation. Is the private law of contract the best means by which to pursue those goals? Collins suggests that the private law of contract has both advantages and disadvantages as a form of

208 Eisenberg, "Why There is No Law of Relational Contracts" (2000) 94 *Northwestern University Law Review* 805, 813.

209 Eisenberg, "Why There is No Law of Relational Contracts" (2000) 94 *Northwestern University Law Review* 805, 817.

210 Eisenberg, "Why There is No Law of Relational Contracts" (2000) 94 *Northwestern University Law Review* 805, 818.

211 Braucher, "Contract Versus Contractarianism: The Regulatory Role of Contract Law" (1990) 47 *Washington and Lee Law Review* 697, 712.

212 Braucher, "Contract versus Contractarianism: The Regulatory Role of Contract Law" (1990) 47 *Washington and Lee Law Review* 697, 712.

213 Braucher, "Contract versus Contractarianism: The Regulatory Role of Contract Law" (1990) 47 *Washington and Lee Law Review* 697, 712.

214 Collins, *Regulating Contracts* (1999).

215 Collins, *Regulating Contracts* (1999), pp 5–6.

regulation. The principal advantage enjoyed by private law as a regulatory system is its reflexivity or responsiveness.[216] The law of contract allows the parties themselves to set most of the standards for a transaction, modify them, monitor compliance and decide when state sanctions are necessary. In practice, the responsiveness of contract law to the needs of the parties is more limited than it might sound in theory. The common imposition of standard form contracts constrains reflexivity in standard setting, and problems of access to justice limit the ability of parties to seek sanctions.

A more fundamental problem with regulation by private, rather than by public, law is that the private law of contract tends not to look beyond the interests of the parties to a particular dispute. In this respect, contract law differs from the law of tort, which more often takes account of broader community interests. In contract cases, the focus of the courts on the interests of the contracting parties prevents the courts from taking account of the effects of the parties' conduct on third parties. Performance of contractual obligations may affect others by causing environmental damage or posing risks to safety. While a consumer may be one of hundreds or even thousands of consumers with a similar problem, contract law treats each consumer's grievance as a separate problem and fails to take account of the "collective harms" caused by the behaviour of contracting parties.[217] Public regulation is required to set and enforce standards in order to avoid undesirable externalities.

Another disadvantage of the private law of contract is its commitment to general rules that can be applied consistently to all types of transactions. The problem with this sort of generality can be seen in relation to exemption clauses in standard form contracts.[218] In a commercial contract made between parties of equal bargaining power, a clause exempting one of the parties from liability for a significant breach may be seen as a fair and efficient allocation of risk. In a contract between a large corporation and a consumer, on the other hand, a similar clause may be seen as an unfair outcome of a gross disparity of bargaining power between the parties.[219] The common law of contract fails to differentiate between the two situations and applies general rules that favour freedom of contract in each case. This failure has been addressed by consumer protection legislation.[220]

The regulatory approach to contract law is considered further in the introduction to Part VII of this book.

COMPARATIVE PERSPECTIVES

[1.180] Internationalisation is a significant force in contract law. This is manifested in a number of different ways. First, the desire to facilitate international trade has given rise to treaties such as the *United Nations Convention on Contracts for the International Sale of Goods* (known as the CISG or the Vienna Convention), which promulgates a set of standard principles governing international contracts for the sale of goods. The treaty aims to remove legal barriers to international trade by providing a set of uniform rules for international sales,

216 Collins, *Regulating Contracts* (1999), pp 62–9.

217 Collins, *Regulating Contracts* (1999), p 70, quoting Nader, "Disputing without the Force of Law" (1979) 88 *Yale Law Journal* 998, 1021.

218 Collins, *Regulating Contracts* (1999), p 77.

219 See further Chapters 12, 13 and 16.

220 See Chapters 16 and 38.

thus avoiding uncertainty resulting from differences in national laws and uncertainty as to which national law should apply to a particular transaction. Australia has ratified this treaty and legislation has been passed in all Australian States and Territories to carry it into effect.[221] The principles laid down by the convention apply to "contracts for the sale of goods between parties whose places of business are in different States: (a) when the States are Contracting States; or (b) when the rules of private international law lead to the application of the law of a Contracting State".[222] The convention expressly provides that, in its interpretation, regard is to be had to "its international character and to the need to promote uniformity in its application and the observance of good faith in international trade".[223]

Secondly, there have been significant attempts to develop regional[224] and international statements of contract law principles.[225] An important statement of international principles of contract law is provided by the *UNIDROIT Principles of International Commercial Contracts 2016* (UPICC).[226] These principles have been developed under the auspices of the International Institute for the Unification of Private Law, which is an independent inter-governmental organisation based in Rome. Its purpose is to examine ways of harmonising and co-ordinating the private law of different states and to prepare uniform rules of private law for adoption by states. The UPICC is a code of principles governing international commercial contracts, which has been developed by representatives of common law, civil law and socialist systems. The UPICC are intended to provide balanced and comprehensive rules that are ideal for international commercial transactions. They provide a model for national legislators, provide a basis for contract negotiation, can be adopted as the governing law of a particular contract (typically between parties belonging to different legal systems or speaking different languages) and are used by arbitrators and judges as a statement of internationally recognised principles.[227] The UPICC are also used as a means of interpreting, supplementing and influencing the development of domestic contract law.[228] The New Zealand Court of Appeal has referred to the principles as a "restatement of the commercial contract law of the world".[229] The principles may have a direct influence on the development of Australian

221 *Sale of Goods (Vienna Convention) Act 1987* (ACT); *Sale of Goods (Vienna Convention) Act 1986* (NSW); *Sale of Goods (Vienna Convention) Act* (NT); *Sale of Goods (Vienna Convention) Act 1986* (Qld); *Sale of Goods (Vienna Convention) Act 1986* (SA); *Sale of Goods (Vienna Convention) Act 1987* (Tas); *Goods Act 1958* (Vic); *Sale of Goods (Vienna Convention) Act 1986* (WA).

222 *United Nations Convention on Contracts for the International Sale of Goods (1980)*, Art 1(1).

223 *United Nations Convention on Contracts for the International Sale of Goods (1980)*, Art 7.

224 See the *Principles of European Contract Law*, Parts I and II (1999) and Part III (2002), produced by the Commission on European Contract Law, and von Bar and Clive, *Principles, Definitions and Model Rules of European Private Law Draft Common Frame of Reference* (2009).

225 See generally Berger, *The Creeping Codification of the New Lex Mercatoria* (2nd ed, 2010).

226 The UPICC were first published in 1994 and were revised and expanded in 2004, 2010 and 2016. See http://www.unidroit.org. A list of cases and arbitral awards citing the principles and details of relevant books and articles may be found at www.unilex.info.

227 Bonell, "UNIDROIT Principles 2004" (2004) 9 *Uniform Law Review* 5, 6–15.

228 Bonell, "UNIDROIT Principles 2004" (2004) 9 *Uniform Law Review* 5, 15–16. See also Bonell, *An International Restatement of Contract Law* (3rd ed, 2005); Bonell (ed), *A New Approach to International Commercial Contracts – The UNIDROIT Principles of International Commercial Contracts* (1999) and Bonell, "Symposium Paper: The UNIDROIT Principles of International Commercial Contracts: Achievements in Practice and Prospects for the Future" (2010) 17 *Australian International Law Journal* 177.

229 *Yoshimoto v Canterbury Golf International* [2000] NZCA 350; [2001] 1 NZLR 523, [89].

contract law. In *Hughes Aircraft Systems International v Airservices Australia*,[230] for example, Finn J cited Art 1.7 of the UPICC as evidence that the implied contractual duty of good faith has been propounded as a fundamental principle in international commercial contracts. This, along with other factors, led Finn J to the view that more open recognition of the duty is warranted in Australian contract law. Useful comparisons with the UPICC have been drawn in numerous other cases.[231]

Thirdly, Australian contract law is enriched by comparisons with approaches adopted in other jurisdictions. It is possible, for example, to point to particular contract cases in which Australian courts have been directly influenced by the principles applied in other countries.[232] Comparisons with the laws of other countries also help to provide us with a better understanding of Australian law and are drawn throughout this book. Care must be taken in relation to comparisons with the United States, because each State has its own law of contract. Since the United States Supreme Court does not hear appeals in contract law cases, there is no single court that can unify contract law in the manner of the High Court of Australia.[233] Problems of uniformity in the US are addressed to some extent by *Restatements of Law* published by the American Law Institute, which include the *Restatement of Contracts (2d)*, published in 1981. The *Restatements* are written by eminent lawyers in the relevant field and are recognised as highly authoritative secondary sources.[234] References are also made in this book to Art II of the *Uniform Commercial Code* of which deals with contracts for the sale of goods.[235] It must be noted that the *Uniform Commercial Code* has not provided the uniformity its name might suggest, because the code has been amended in different ways by State legislatures and interpreted in different ways by State courts.[236]

230 *Hughes Aircraft Systems International v Airservices Australia* (1997) 76 FCR 151, 192.

231 See also, eg, *Aiton Australia Pty Ltd v Transfield Pty Ltd* [1999] NSWSC 996; (1999) 153 FLR 236, 260–1; *Bobux Marketing Ltd v Raynor Marketing Ltd* [2001] NZCA 348, [39]; *Tan Hung Nguyen v Luxury Design Homes Pty Ltd* [2004] NSWCA 178, [705]; *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115, [108]; *Chartbrook Ltd v Persimmon Homes Ltd* [2009] UKHL 38; [2009] 1 AC 1101, [39]; *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407, [7]–[9]

232 See, eg, the influence of French law in *Banque Brussels Lambert SA v Australian National Industries Ltd* (1989) 21 NSWLR 502, 521, discussed at [5.15], and the influence of American law in *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 267–8, discussed at [16.40].

233 See Priestley, "A Guide to Comparison of Australian and United States Contract Law" (1989) 12 *University of New South Wales Law Review* 4, 5–6.

234 See Farnsworth, *Farnsworth on Contracts* (3rd ed, 2004), Vol 1, pp 32–34.

235 See generally Farnsworth, *Farnsworth on Contracts* (3rd ed, 2004), Vol 1, pp 41–59.

236 See Priestley, "A Guide to Comparison of Australian and United States Contract Law" (1989) 12 *University of New South Wales Law Review* 4, 5–9.

CHAPTER **2**

The place of contract within private law

[2.05] A useful perspective on contract law is provided by considering its place within the law of obligations and its place within the field of private law. The law of obligations is concerned with the obligations owed by individuals (including legal entities, such as corporations) to one another. The law of obligations comprises the fields of contract, tort and restitution (or unjust enrichment), along with a number of miscellaneous categories such as the equitable principles relating to fiduciaries, confidential information and estoppel. Statutes such as the *Competition and Consumer Act 2010* (Cth) (formerly the *Trade Practices Act 1974* (Cth)) are also an important source of obligations owed by individuals to one another.[1]

It is sometimes said that what distinguishes contractual obligations from other private law obligations is that the obligations owed by contracting parties are self-imposed, while other private law obligations are imposed by law.[2] As we have already seen, however, contractual obligations may be imposed on both parties by the state or by one party on the other.[3]

The expression "private law" is commonly used to describe a field of law comprising the law of obligations and the law of property.[4] The law of property can be understood as "a category of law concerned with relations between people and things".[5] In the case of both obligations and property, the relevant legal rights are "private", in that they are exclusively enforceable by the individuals who are recognised as holders of the relevant rights and who

1 See [2.70]–[2.105] and Chapters 33 and 38.
2 See, eg, Burrows, *Understanding the Law of Obligations* (1998), p 13.
3 See [1.15]–[1.25].
4 See, eg, Burrows (ed), *English Private Law* (3rd ed, 2013), which deals with the law of *persons* (family and corporations law), the law of *property* and the law of *obligations* (including contract, agency, bailment, torts and equitable wrongs and unjust enrichment) and *litigation* (insolvency, private international law, judicial remedies and civil procedure).
5 Samuel, *Law of Obligations and Legal Remedies* (2001), p 2.

may choose whether or not to enforce them. Private law is sometimes distinguished from public law, which is the body of law dealing with the relationship between individuals and the state and between states.[6] This distinction is somewhat artificial, since private law obligations exist only because they are recognised and enforced by the state through the courts. Thus "private law" has a significant public dimension.[7]

Contract commonly overlaps and intersects with other parts of the law of obligations, particularly tort, unjust enrichment, equitable doctrines (such as the duty of confidence, fiduciary duties and estoppel) and statutory obligations (such as the duty not to engage in misleading or deceptive conduct in trade or commerce). It is important to be able to identify and distinguish the different types of claim that may be available in a particular situation in order to determine the nature of the remedies available and, in some cases, to identify the claim that provides the optimal measure of relief.

TORTS

[2.10] The law of torts is concerned with actions that harm others. Torts are often described as "civil wrongs". These wrongs are "civil" as distinct from "criminal" because they are enforceable by the person wronged, rather than by the state. The law of torts provides the victim with a remedy against the perpetrator in the form of an award of damages. Torts comprise a rather miscellaneous group of anti-social acts, such as assault, battery, false imprisonment, trespass to land, conversion of goods, nuisance, defamation, deceit and negligence. From this list, it will be seen that the law of torts imposes a host of duties to avoid certain kinds of conduct which cause various kinds of harm, including physical injury, nervous shock, loss of freedom, loss of reputation, damage to or loss of property and economic loss. Generally, there is no liability without fault on the part of the perpetrator ("fault" meaning here an intention to cause the harm or carelessness in bringing it about), but there are also instances in which the law of torts imposes *strict liability*, or liability without fault.

The most significant tort from a practical point of view is the tort of *negligence*. The elements of this tort are: (1) a duty of reasonable care owed by the defendant to the plaintiff; (2) a breach of that duty and (3) a legally recognised form of damage to the plaintiff resulting from that breach. The law has imposed duties of care on a wide variety of defendants, including manufacturers, drivers of vehicles, employers, school authorities, occupiers of land, solicitors, medical practitioners and many others. The general aim of an award of damages in negligence, as in tort actions generally, is to restore the victim as far as money can to the position he or she would have been in if the tort had not been committed.

Torts committed in a contractual context

[2.15] The law of torts must often be considered in a contractual context. Consider the following situations.

6 To the list of topics covered by Feldman (ed), *English Public Law* (2nd ed, 2009), of constitution and administrative law, human rights, public law remedies and criminal law, we might add public international law and fields of regulation such as environmental law and competition law, although in some cases, these regulatory regimes also confer rights enforceable by individuals against other individuals.

7 Compare Beever, "Our Most Fundamental Rights" in Nolan and Robertson (eds), *Rights and Private Law* (2011), p 63 (arguing that private law rights exist independently of the state).

First, assume that A is induced by B's statement to enter into a contract with B and that B's statement later proves to be false. If the statement was incorporated into the contract (so that it can be said that B promised the truth of the statement in the contract), A will have an action against B for damages for breach of the contract. If the statement was not incorporated in the contract, such an action is not available. However, A may have an action for damages in *tort* – the tort of *deceit* (if B did not believe in the truth of the statement) or the tort of *negligence* (if B owed a duty of care to A and was careless in believing in the truth of the statement).

Secondly, a victim of loss may be able to sue in the tort of negligence when an existing contract provides no means of relief. Assume A purchases a product from B and is injured as a result of a defect in the product. The contractual action against B may be of no use because, for example, B is bankrupt. However, A may be able to bring an action in *negligence* against C, the manufacturer of the product, who owes a duty of care to consumers such as A.[8]

Take another example. Assume A retains solicitor B to prepare a will under which A leaves $1 million to C. When A dies C gets nothing under the will because it is invalid owing to B's carelessness in preparing it. C has no action for breach of contract against B as B's only contract was with A (ie, the contract of retainer). There is a doctrine of privity of contract which requires that only a party to a contract can sue on it.[9] But C may have action in negligence against B for breach of a duty of care owed by B to C.[10]

The point to note in both these examples is that, although B's duties in contract may be owed solely to A, an independent duty of care may be owed by B to a third party, such as C. The argument that B's duties are governed exclusively by the contract with A has been rejected by the courts.

Concurrent liability in contract and tort

[2.20] A particular incident may provide a plaintiff with actions in both contract and tort against a particular defendant. This is known as *concurrent liability*. Concurrent liability typically arises where one person (A) owes a contractual obligation to another (B) to take reasonable care in performing services for B and also owes B a duty of care in tort. If A is careless in performing the services, B may have an action for breach of contract and also an action for the tort of negligence. Hence, a taxi driver who drives carelessly and injures a passenger would be liable to that passenger in both contract and negligence. An employer who maintains an unsafe system of work may be liable in both contract and negligence to an employee injured as a result.

Needless to say, duplication of damages is not permitted in these situations, but the law does allow a choice between suing in contract and suing in tort. The plaintiff may "assert the cause of action that appears to be most advantageous".[11] The choice of one action over another may be significant given that contract and tort rules differ in areas such as the assessment of damages, remoteness of damage, the effect of the plaintiff's contributory negligence and limitation periods.

8 *Donoghue v Stevenson* [1932] AC 562.
9 See Chapter 11.
10 See, eg, *Hill v Van Erp* (1997) 188 CLR 159.
11 *Bryan v Maloney* (1995) 182 CLR 609, 622, quoting *Central Trust Co v Rafuse* [1986] 2 SCR 147, 204–5.

Tort and contract compared

[2.25] Is there any significant difference between a tort and a breach of contract?[12] They may both be described as civil wrongs and they are both creations of the common law. However, a number of possible distinctions should be noted.

Contract as self-imposed obligation

[2.27] It is often claimed that duties in contract are determined by the contracting parties themselves when they voluntarily enter into an agreement, whereas we are all bound not to commit torts whether or not we have agreed not to commit them. Ultimately, however, all duties are imposed by law in that the law recognises them as suitable for recognition.

As we saw in Chapter 1, the objective approach to contract formation means that contractual liability arises where parties behave in a certain way, regardless of their actual intentions.[13] In this sense, contractual obligations can be seen to be imposed by law on the basis of expected conformity with standards of conduct determined by the courts, in the same way as tort.[14] Moreover, as we have seen, parties to a contract often have duties imposed on them that have not been the subject of express agreement between the parties. On the other hand, duties in tort are sometimes, in a sense, self-imposed. The law of negligence recognises a duty of care in some instances where a person has assumed a responsibility to take care.[15] Whether these obligations can properly be understood as being voluntary is a matter of debate.[16]

Tort as universal duties

[2.30] It is sometimes said that by virtue of the doctrine of privity of contract, a contractual duty is only owed to the other party to the contract, whereas duties to avoid committing torts are owed to everyone. No doubt this is broadly true, and yet a duty of care, the foundation of the tort of negligence, is not owed by everyone to everyone. It is owed only by a person in a particular situation to "neighbours" (foreseeable victims) and sometimes only to just one group of people or indeed just one person. The range of potential plaintiffs in a negligence context may be quite strictly limited where the loss suffered is of a purely economic kind, such as economic loss resulting from careless financial advice. While the doctrine of privity of contract allows that contractual duties are owed only to other parties to the contract, that principle is not without some flexibility and has been substantially modified by statute in many jurisdictions.[17]

Contract as strict liability

[2.35] Another point of difference relates to culpability. Liability in contract is strict: it is not to the point that the contract breaker did not intend to break the contract or was not careless

12 See generally Swanton, "The Convergence of Tort and Contract" (1989) 12 *Sydney Law Review* 40.

13 See [1.15]–[1.25].

14 See Robertson, "On the Distinction between Contract and Tort" in Robertson (ed), *The Law of Obligations: Connections and Boundaries* (2004), pp 87–109.

15 See, eg, *Shaddock v Parramatta City Council* (1981) 150 CLR 225; *Hill v Van Erp* (1997) 188 CLR 159.

16 See Barker, Grantham and Swain (eds), *The Law of Misstatements: 50 Years on from Hedley Byrne v Heller* (2015), especially Robertson and Wang, "The Assumption of Responsibility" (ch 3) and Beever, "The Basis of the Hedley Byrne Action" (ch 4).

17 See Chapter 11.

in doing so. We noted earlier that culpability of some kind is normally relevant to establishing liability in tort and, in the case of some torts such as deceit and negligence, the very name of the tort spells a degree of culpability. Nevertheless, the standard of care in negligence is objective and may be pitched so high as to be virtually strict.

Measure of damages

[2.40] An award of compensatory damages is the primary remedy for both tort and breach of contract. The aim of such damages in both instances is to compensate for loss: to put the plaintiff in the position he or she would have been in had the contractual or tortious duty not been breached. Although it is sometimes said that the two measures of damages are different, it has been pointed out that this "is no more than a convenient way of indicating that the wrong involved and, thus, the loss occasioned by a breach of contract is of a different kind from that involved in and occasioned by the commission of a tort".[18] In contract, the wrong is the promisor's failure to perform the contractual promise. In tort, the wrong is the tortfeasor's failure to avoid harming the plaintiff or to take appropriate care of the plaintiff's interests.

The primary purposes of tort and contract are not the same. The law of torts is concerned to protect individuals from interferences that make them worse off, such as physical injury, damage to property, loss of reputation and diminution of wealth. The duties recognised by the law of tort are generally of a negative kind, prohibiting certain forms of antisocial behaviour that may harm others. Accordingly, in tort, the award of damages aims to put the victim in the position he or she would have been in had the tort not been committed – to protect the plaintiff's status quo ante interest. The law of contract, on the other hand, is concerned to ensure that the promisor improves the position of the other party by providing the promised money, property or services. The duties recognised by the law of contract are generally of a positive kind, requiring the promisor to act affirmatively in the promisee's favour. Accordingly, in contract, the award of damages aims, as we have seen, to put the promisee in the position he or she would have been in had the contract been performed – to protect the promisee's expectation interest.

This distinction between tort and contract is useful, but it is important to note that in some contract cases, damages do no more than protect a promisee from being made worse off by the contract, and in some tort cases, the plaintiff is made better off by having his or her expectation interest protected. In some cases, contractual damages protect the promisee's reliance interest by compensating the promisee for loss incurred as a result of acting in reliance on the promisor's promise.[19] Such an award restores the promisee to his or her previous position or status quo ante the contract. Similarly, damages awards in tort occasionally have the effect of fulfilling the plaintiff's expectations. For example, a solicitor making a will for a client owes a duty of care to the prospective beneficiaries (even though they are not contractually linked with the solicitor) to take care to ensure that the will is valid. If a prospective beneficiary loses his or her bequest because of the solicitor's negligence, the solicitor will be required to pay damages to the disappointed beneficiary equal to the value of the expected bequest.[20]

18 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) CLR 494, [14].

19 See Chapter 26.

20 See *Hill v Van Erp* (1997) 188 CLR 159.

UNJUST ENRICHMENT

[2.45] The law of unjust enrichment is another principal source of obligations owed by individuals to one another.[21] It is concerned with obligations to restore unjust gains. In certain circumstances, a duty will be imposed on one individual to pay a sum of money to another on the ground that otherwise the former will enjoy an unjust enrichment at the expense of the latter. Where a defendant has been unjustly enriched at the expense of the plaintiff, the plaintiff seeks *restitution*, which means the return of the benefit which has been transferred from the plaintiff to the defendant.

A claim for restitution based on unjust enrichment may take the form of a claim to recover money paid (under mistake, for example) or a claim to recover reasonable remuneration for services rendered or goods delivered (under an unenforceable contract, for example). The liability to restore unjust gains used to be described as a "quasi-contractual" obligation, because it was based on an implied contract to repay money or to pay a reasonable value for goods or services received. The implied promise was a fiction designed to provide the plaintiff with a basis for recovering an unjust gain under the constraints imposed by the medieval forms of action. It is now accepted that the obligation recognised in certain defined circumstances to restore a benefit received at the expense of another party is one that is imposed by law in order to prevent unjust enrichment.[22] That obligation is not based on an implied contract and has a different legal foundation from contractual obligations.

We have already seen that a sharp distinction cannot be drawn between contract and tort. Similarly, the law of unjust enrichment cannot be sharply distinguished from contract or tort. One type of restitutionary remedy is in a very broad sense like tort, in that the result of a successful claim is the restoration of the status quo ante (ie, the parties are returned to their earlier positions): this is the effect of recovery of money paid where there has been a total failure of consideration. Another type of restitutionary claim is closer to contract in that the result of a successful claim is the realisation of an exchange: this is the effect of recovery of a reasonable sum for services rendered or goods delivered. In such a case, the plaintiff may be better off than before the exchange, just as in contract law the promisee is made better off than before the contract by virtue of the enforcement of the contractual agreement.

In the leading restitution case of *Pavey & Matthews Pty Ltd v Paul*,[23] Mrs Paul's contractual promise to pay reasonable remuneration to builders for work on her cottage was unenforceable under a statutory provision because the contract was not in writing and signed by both parties. The builder was able to recover reasonable remuneration in restitution for the work done because Mrs Paul had requested and accepted the benefit of the work. Mrs Paul's obligation to pay was a restitutionary obligation, which was said to be imposed by law on the basis of unjust enrichment. The existence of the unenforceable contract was said to serve only to demonstrate that the services had not been performed gratuitously and to provide guidance in the determination of the amount that should be paid. Steve Hedley has argued that the restitutionary claim that was allowed in this case was indistinguishable from the contract claim that was barred by statute: "The builders had simply dressed up a contractual claim in

21 See Chapter 10.

22 See *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221.

23 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, discussed at [10.10].

the language of unjust enrichment."[24] The law of unjust enrichment is considered further in Chapter 10.

EQUITY

[2.50] Equity is also a rich source of personal obligations. The word "equity" in popular usage means, among other things, the quality of fairness or justice. While this meaning is not irrelevant for our purposes, it is important to understand that "equity" has a specialised meaning in law. It is to be compared with the *common law* and seen as a system of doctrines and remedies developed historically as a means of remedying defects in the common law. In this context, "common law" means the law developed by judges in England in the centuries following the Norman Conquest. The King's justices, in the three courts of King's Bench, Common Pleas and the Exchequer, unified the various local customs existing throughout the kingdom into a common custom: the common law. This judge-made law was ultimately the source of the basic principles of what today we call the law of contract, the law of torts and the law of restitution.

From the Middle Ages on there was much dissatisfaction with the common law system for several reasons. To take just one example, the common law courts offered a limited range of remedies: they could order the payment of damages but they could not order someone to do something or to refrain from doing something. A separate court developed, the Court of Chancery, to redress various inadequacies of the common law. It was this court that administered and developed a system of doctrines and remedies that we describe as *equitable*. For example, the Court of Chancery could exercise the power of ordering someone to perform a contract (*specific performance*) or to refrain from committing a tort or breach of contract (*injunction*). Accordingly, the word "equity" has the following specialised meaning: it is the system of doctrines and remedies developed by the Court of Chancery to rectify defects in the common law. A brief historical excursus will explain how this development occurred and its relevance to the current position in Australia. What follows is a simplified account of the development of equity.[25]

The development of equity

[2.55] In the 13th century, litigants who were dissatisfied with the injustice or inadequacy of the common law system petitioned the King to intervene in particular disputes. The petitions were dealt with by the Chancellor, as the representative of the King, and gradually a court, the Court of Chancery, was developed to hear them. In its early years, the Chancellors resolved disputes on a discretionary basis, according to what the *conscience* of the defendant required in the particular circumstances. The Chancellors usually came from an ecclesiastical background and thus exercised a spiritual authority over the litigants. After the Reformation, Chancellors with training in the common law came to be appointed and this led to the legalisation of

24 Hedley, "Unjust Enrichment: The Same Old Mistake" in Robertson (ed), *The Law of Obligations: Connections and Boundaries* (2004), pp 75, 81.

25 The following discussion draws on Heydon, Leeming and Turner, *Meagher Gummow and Lehane's Equity Doctrines and Remedies* (5th ed, 2015), ch 1; Baker, *An Introduction to English Legal History* (4th ed, 2002), ch 6 and Loughlan, "The Historical Role of the Equitable Jurisdiction" in Parkinson (ed), *The Principles of Equity* (2nd ed, 2003), ch 2.

the Court of Chancery. Cases began to be decided on the basis of precedent: decisions came to be reported and a body of equitable principles was developed. However, it was clearly inconvenient for litigants to have two sets of courts applying different principles. Moreover, the Court of Chancery eventually gained a reputation for scandalous delay and inefficiency. This sad state of affairs was memorably described by Charles Dickens in his celebrated novel Bleak House.

The Court of Chancery was abolished, and the administration of common law and equity in England and Wales was merged by the *Judicature Act*, passed in 1873. This established the Supreme Court of Judicature, which was to give effect to both common law and equitable principles, with equity prevailing in the event of conflict between the two. These reforms were soon followed in the Australian colonies, where the supreme courts were given power to administer common law and equity together, although in the Supreme Court of New South Wales, equity was administered exclusively by a separate division until 1972.[26]

Although the administration of common law and equity has been merged, the bodies of principles have not been fused. It remains important to distinguish between common law and equitable doctrines because they operate according to different principles. Equity provides different remedies from the common law. Equitable remedies (such as specific performance) are available at the discretion of the court, unlike common law remedies (such as damages for breach of contract), which are available as of right. A separate set of defences is also available in equity.

Historically, the role of equity was to remedy injustice resulting from an overly rigid common law. In the 19th century, there was a decline in this ameliorative role. Towards the end of the 20th century, however, there was an equitable revival within the law of contract, which did much to restore equity's role as the guardian of conscience. This is seen, for example, in the more frequent invocation of unconscionability as a basis for equitable relief.[27] Indeed, the prevention of unconscionable conduct may be seen today as the unifying rationale for a number of specific heads of equitable intervention.[28]

Equitable obligations

[2.60] Three equitable obligations are particularly relevant in the contractual context: the obligation not to harm others by behaving inconsistently (equitable estoppel), the obligation to act solely in the interests of those who repose special trust and confidence in us (fiduciary obligations) and the obligation not to misuse confidential information.

Equitable estoppel creates liability where promises have been relied upon. Like contract, equitable estoppel involves the enforcement of promises, but it is concerned with promises that have been relied upon rather than promises that have been bargained for. As we will see in Chapter 9, however, equitable estoppel is a distinct category of liability which differs from contract in important ways.

26 See Heydon, Leeming and Turner, *Meagher Gummow and Lehane's Equity Doctrines and Remedies* (5th ed, 2015), pp 12–23.

27 See, eg, *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387 and *Commonwealth v Verwayen* (1990) 170 CLR 394 (discussed in Chapter 9); *Taylor v Johnson* (1983) 151 CLR 422 (discussed in Chapter 31); *Commercial Bank of Australia v Amadio* (1983) 151 CLR 447 (discussed in Chapter 36).

28 See Loughlan, "The Historical Role of the Equitable Jurisdiction" and Parkinson, "The Conscience of Equity" in Parkinson (ed), *The Principles of Equity* (2nd ed, 2003), chs 1–2.

Fiduciary obligations are owed in certain situations where one person (the fiduciary) undertakes to act in the interests of a second person (the principal or beneficiary) and has the ability to exercise powers and discretions that affect the interests of the beneficiary.[29] The beneficiary reposes trust and confidence in the fiduciary and is entitled to expect that the fiduciary will act solely in the beneficiary's interests. For example, solicitors owe fiduciary obligations to their clients. Fiduciaries must not profit from their position and must ensure that their personal interests do not come into conflict with their duties to the beneficiary. The remedies for breach of fiduciary duty are sometimes restitutionary (where the fiduciary profits from the breach of duty) and sometimes compensatory (where losses are suffered by the beneficiary as a result of the breach of duty). Fiduciary duties can exist alongside contractual obligations, although it is very difficult to establish a fiduciary relationship between parties dealing at arm's length on an equal footing in a commercial transaction.[30]

Equity also enforces a duty not to misuse information that is disclosed in circumstances giving rise to an *obligation of confidence*.[31] Again the remedies for breach of confidence are sometimes restitutionary (where profits are made from misuse of the information) and sometimes compensatory (where losses result from disclosure of the information). A duty of confidence may arise, for example, between parties negotiating for a contract. If one party divulges confidential information to another during contractual negotiations which later break down, no contractual duty to pay for the information ever arises, but equity may recognise an obligation not to use the information for any purpose other than that for which it was disclosed.

Equitable doctrines and remedies in contract

[2.65] In this book, we will be concentrating on equitable doctrines and remedies that are so closely connected with contract that they are either regarded as part of contract law or are essential to understanding it. Equitable estoppel falls into this category, but the equitable doctrines relating to fiduciaries and confidential information do not. There are other aspects of equity that are crucial to a study of contract law. First, equitable remedies supplement the common law remedy of damages in the enforcement of contracts. The equitable remedies of *specific performance* and *injunction* will be granted in circumstances where the common law remedy of damages would be inadequate.[32] Secondly, a contract will be set aside or rescinded in equity where there has been some unconscionable conduct in the bargaining process, such as misrepresentation, undue influence or unconscionable dealing.[33] Thirdly, equity will rectify a written document where the parties have by mistake inaccurately recorded the terms of their agreement.[34]

29 See generally Parkinson, "Fiduciary Obligations" in Parkinson (ed), *The Principles of Equity* (2nd ed, 2003), ch 10.

30 See *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41.

31 See generally Richardson and Stuckey-Clarke, "Breach of Confidence" in Parkinson (ed), *The Principles of Equity* (2nd ed, 2003), ch 12.

32 See Chapter 30.

33 See Chapters 31–32, 34–37 and 39.

34 See Chapter 31.

STATUTORY OBLIGATIONS AND REGULATION

Statutory obligations and regulation

[2.70] A number of statutes impose obligations that affect the formation, performance and enforcement of contracts. Some statutes also regulate the content of contract terms. The statutory regime with the closest connection to contract is the *Australian Consumer Law* (ACL), which is set out in Sch 2 of the *Competition and Consumer Act 2010* (Cth) (CCA).[35]

The Australian Consumer Law

[2.75] The origin of the ACL is in the Productivity Commission's *Review of Australia's Consumer Policy Framework*, which recommended the introduction of a single national consumer law.[36] The enactment of the ACL followed an agreement by the Council of Australian Governments in October 2008 to implement the Productivity Commission's recommendation. The ACL is comprehensive consumer protection legislation which applies uniformly across Australia. It draws on the consumer protection provisions previously contained in *Trade Practices Act 1974* (Cth) (TPA), as well as other consumer protection regimes that were previously in operation in different Australian jurisdictions. The ACL regulates misleading and deceptive conduct, unconscionable conduct, unfair contract terms, consumer guarantees, product liability and unsolicited consumer agreements. The Australian Competition and Consumer Commission is given power to enforce certain provisions of the ACL, by seeking fines and remedies for affected parties. Parties who are affected are also able to seek redress by instituting legal proceedings of their own.

Legislative power to pass laws relating to consumer protection is shared between the Commonwealth and State and Territory Parliaments. To implement the ACL, the Commonwealth Parliament acted as the lead legislator. The ACL is contained in Sch 2 of the CCA. Schedule 2 applies to the extent provided for by application legislation.[37] The Commonwealth Parliament, and the Parliaments of all of the States and Territories, has passed legislation applying Sch 2 of the CCA as a law of their respective jurisdictions. As a result, corporations, unincorporated entities and individuals are all caught by the ACL under Commonwealth and/or State and Territory application laws.

Application as a law of the Commonwealth

[2.80] Part XI of the CCA provides for the application of the ACL as a law of the Commonwealth. The legislative power of the Commonwealth Parliament is limited by the Commonwealth Constitution. The CCA provides that the ACL applies to activities with respect to which the Commonwealth has constitutional power. In particular, s 131(1) of the CCA applies the ACL to the conduct of corporations.[38] Section 4 of the CCA defines "corporation" to mean a body corporate that is:

35 The CCA was until 2010 called the *Trade Practices Act 1974* (Cth); see the *Trade Practices Amendment (Australian Consumer Law) Act (No 2) 2010* (Cth), Sch 5, items 1–2.

36 Productivity Commission, *Review of Australia's Consumer Policy Framework, Inquiry Report No 45* (2008), http://www.pc.gov.au/inquiries/completed/consumer-policy/report.

37 ACL, s 1.

38 Other heads of constitutional power are invoked as a basis for applying the ACL under CCA, s 6.

- a foreign corporation (a body corporate incorporated overseas);
- a trading corporation formed within the limits of Australia (a body corporate is a trading corporation if a sufficiently significant proportion of the corporation's overall activities are trading activities);[39]
- a financial corporation formed within the limits of Australia (a body corporate that performs the function or engages in the activity of dealing in finance);[40]
- incorporated in a Territory; or
- the holding company of a trading corporation, financial corporation or body corporate incorporated in a Territory.

The ACL also applies as a law of the Commonwealth to individuals in certain circumstances.[41] This extension is achieved by reliance on other constitutional powers: the trade or commerce power, the Territories power, powers governing dealings with Commonwealth agencies and the post and telegraph power. The general result is that s 18 applies as a law of the Commonwealth to natural persons who engage in trade and commerce between Australia and places outside Australia, among the States, within a Territory, between two Territories, by way of supply of goods to the Commonwealth[42] or where "engaging in conduct" involves the use of postal or telephone services[43] or takes place in a radio or television broadcast.[44]

Section 131A of the CCA provides that with the exception of Pt 5.5 of the ACL, which is not relevant for present purposes, the Commonwealth application laws do not apply "to the supply, or possible supply, of services that are financial services, or of financial products". These types of services and products are regulated under the *Australian Securities and Investment Commission Act 2001* (Cth) (ASIC Act), which contains many, though not all,[45] of the consumer protection provisions found in the ACL. Interestingly, the State and Territory laws applying the ACL do not contain a provision equivalent to s 131A of the CCA. It is as yet uncertain whether the ACL as applied by State and Territory law could be used in respect to "the supply, or possible supply, of services that are financial services, or of financial products" or whether such an application of the ACL would be found inconsistent with the intention expressed in the CCA for these services and products to be regulated under the ASIC Act.

States and Territories

[2.85] Under the *Intergovernmental Agreement for the ACL* (2009), the States and Territories undertook to enact legislation applying the ACL as a law of their jurisdictions. Laws applying

39 *R v Judges of the Federal Court of Australia; Ex parte Western Australian National Football League* (1978) 143 CLR 190, 233.

40 *State Superannuation Board v Trade Practices Commission* (1982) 60 FLR 165, 175.

41 CCA, s 6(3), (3A).

42 CCA, s 6(2).

43 Note that sending an email has been held to constitute the use of telephone services: *Dataflow Computer Services Pty Ltd v Goodman* [1999] FCA 1625, [9].

44 CCA, s 6(3). This result is not immediately apparent from reading the version of s 6(3) that appears in the consolidated version of the legislation which, at the time of writing, refers to parts of the CCA that have been repealed and makes no mention of the ACL. However, note 2 (which can be found in the notes section of the Act, which follows Sch 2) provides that the words "Part IVA, of Divisions 1, 1A and 1AA of Part V and of Divisions 2 and 3 of Part VC" should be omitted and replaced with the words "Parts 2-1, 2-2, 3-1 (other than Division 3), 3-3, 3-4, 4-1 (other than Division 3), 4-3, 4-4 and 5-3 of the Australian Consumer Law".

45 See Chapter 16.

the provisions of the ACL to the conduct of "persons" have been enacted in all States and Territories.[46] Section 22(1)(a) of the *Acts Interpretation Act 1901* (Cth) provides that "expressions used to denote persons generally … include a body politic or corporate as well as an individual".[47] Thus, the State and Territory application laws apply directly to both individuals and corporate entities.[48]

The CCA confirms that the ACL provisions in the CCA do not exclude the operation of an application law of a participating jurisdiction to the extent that they are capable of operating concurrently.[49]

While the ACL regulates a range of different types of conduct, the provisions with most significance to the law of contract are outlined as follows.[50]

Misleading or deceptive conduct

[2.90] In the discussion of torts earlier in this chapter, we saw that a person who suffers loss through acting on a false statement might recover damages for deceit (for a dishonest statement) or negligence (for a careless statement made in breach of a duty of care). Accordingly, a person induced to enter a contract by a false statement that did not become part of the contract might nonetheless claim damages for loss suffered. A contract might also be set aside or rescinded in equity if it has been induced by a misrepresentation (restrictively defined) and various bars to relief can be avoided.

Today, however, the most important source of relief for misleading conduct (including misrepresentations) is under Pts 2-1 and 3-1 of the ACL. In particular, s 18(1) in Pt 2-1 of the ACL prohibits misleading or deceptive conduct in trade or commerce.[51] More specific prohibitions on misleading and deceptive conduct are contained in Pt 3-1 of the ACL. Persons who suffer loss as a result of contravention of these provisions have access to a wide range

46 *Fair Trading (Australian Consumer Law) Act 1992* (ACT), as amended by the *Fair Trading (Australian Consumer Law) Amendment Act 2010* (ACT); *Fair Trading Act 1987* (NSW), as amended by the *Fair Trading Amendment (Australian Consumer Law) Act 2010* (NSW); *Consumer Affairs and Fair Trading Act* (NT) as amended by the *Consumer Affairs and Fair Trading (National Uniform Legislation) Act* (NT); *Fair Trading Act 1989* (Qld) as amended by the *Fair Trading (Australian Consumer Law) Amendment Act 2010* (Qld); *Fair Trading Act 1987* (SA) as amended by the *Statutes Amendment and Repeal (Australian Consumer Law) Act 2010* (SA); *Australian Consumer Law (Tasmania) Act 2010*; *Fair Trading Act 1999* (Vic) as amended by the *Fair Trading Amendment (Australian Consumer Law) Act 2010* (Vic); *Fair Trading Act 2010* (WA).

47 The State and Territory application laws provide that the Commonwealth interpretation legislation applies to the ACL rather than the State and Territory interpretation legislation: *Fair Trading (Australian Consumer Law) Act 1992* (ACT), s 10; *Fair Trading Act 1987* (NSW), s 31; *Consumer Affairs and Fair Trading Act* (NT), s 30; *Fair Trading Act 1989* (Qld), s 19; *Fair Trading Act 1987* (SA), s 17; *Australian Consumer Law (Tasmania) Act 2010* (Tas), s 9; *Fair Trading Act 1999* (Vic), s 12; *Fair Trading Act 2010* (WA), s 23.

48 *Fair Trading (Australian Consumer Law) Act 1992* (ACT), as amended by the *Fair Trading (Australian Consumer Law) Amendment Act 2010* (ACT); *Fair Trading Act 1987* (NSW), as amended by the *Fair Trading Amendment (Australian Consumer Law) Act 2010* (NSW); *Consumer Affairs and Fair Trading Act* (NT) as amended by the *Consumer Affairs and Fair Trading (National Uniform Legislation) Act* (NT); *Fair Trading Act 1989* (Qld) as amended by the *Fair Trading (Australian Consumer Law) Amendment Act 2010* (Qld); *Fair Trading Act 1987* (SA) as amended by the *Statutes Amendment and Repeal (Australian Consumer Law) Act 2010* (SA); *Australian Consumer Law (Tasmania) Act 2010*; *Australian Consumer Law and Fair Trading Act 2012* (Vic); *Fair Trading Act 2010* (WA).

49 CCA, s 131C.

50 More information about the ACL can also be found at http://www.consumerlaw.gov.au.

51 See Chapter 33.

of remedies (including damages and rescission) under the legislation itself.[52] Provided the misleading conduct occurred in trade or commerce, applicants for relief are hampered neither by the limitations on claims for damages imposed by the law of torts (such as culpability) nor by the limitations on claims for rescission imposed by equity.

Unconscionable conduct

[2.95] Part 2-2 of the ACL prohibits certain types of unconscionable conduct in trade or commerce.[53] The courts are given power to grant a wide range of remedies, including the power to award monetary compensation and to declare contracts void, where a person suffers loss as a result of unconscionable conduct engaged in by another. These prohibitions not only are particularly important during contractual negotiations but also regulate the exercise of contractual rights, such as the power to terminate a contract.

Unfair contract terms

[2.100] Part 2-3 of the ACL regulates unfair terms in consumer contracts.[54] This part of the ACL looks to the fairness of the terms of the contract, not merely to the conduct of the parties in making, performing or enforcing the contract. The effect of an unfair term is that it is void, which means that the term is treated as if it never existed.

Consumer guarantees

[2.105] Part 3-2 of the ACL contains a regime of "consumer guarantees".[55] The consumer guarantees provide a range of minimum standards of quality that apply to the supply of goods and services to consumers. These guarantees cannot be excluded or limited by contract and take priority over any express guarantee or extended warranty that might be provided by a retailer or manufacturer. The consumer guarantees replace the contract terms that were previously implied under the TPA.

52 See Chapter 33.
53 See Chapter 38.
54 See Chapter 16.
55 See Chapter 17.

FORMATION

PART II

[PtII.05] We saw in Chapter 1 that, according to one view, contract law is essentially concerned with enforceable promises or agreements. The law distinguishes between enforceable and unenforceable promises by reference to a series of formal requirements. For an enforceable contract to come into existence, four essential requirements must be satisfied. First, the parties must reach an agreement. The requirement of agreement is often expressed in terms of offer and acceptance: one party must make an offer that is accepted by the other party. Secondly, each party must provide consideration. This means that each party must give something in return for the promises made by the other. Thirdly, it must appear objectively that the parties intend the agreement to create legal relations between them. Fourthly, the agreement must be complete and certain. Satisfaction of these four requirements shows that the parties have reached a consensus, that they have struck a bargain that involves an exchange, that they intend their actions to have legal consequences and that they have identified their respective obligations with sufficient precision. These requirements are discussed in Chapters 3–6. The circumstances in which writing is required to create an enforceable contract are then considered in Chapter 7. The issue of contractual capacity is considered in Chapter 8.

CHAPTER **3**

Agreement

OFFER AND ACCEPTANCE

[3.05] The traditional approach to establishing an agreement between two parties is to identify an offer made by one party and an acceptance of that offer by the other. Under that analysis, a contract is said to come into existence when acceptance of an offer has been communicated to the offeror.[1] This approach to contract formation by reference to offer and acceptance was developed in the 19th century. It is based on a 19th century model of contracting, in which negotiations are conducted through written correspondence, with a series of letters passing between the parties, leading ultimately to an agreement.[2] This approach is also based on a 19th century idea of contracting, in which parties can bargain freely in an unregulated market, stipulating the terms they require, reaching a concluded bargain only if there is a real consensus between them.

According to classical contract theory, the offer and acceptance formula identifies a "magic moment of formation"[3] when the parties are ad idem (of one mind) and their individual wills come together to create binding obligations. In that moment, all of the parties' contractual obligations spring into existence.[4] The rules about offer and acceptance are based on the idea that until the moment of formation the parties are under no obligation to one another and are free to withdraw from negotiations. Hugh Collins has observed that these rules "typify the formalist qualities of classical law: they are detailed, technical and mysterious, yet claim logical derivation from the idea of agreement".[5]

1 For example, *Tallerman & Co Pty Ltd v Nathan's Merchandise (Vic) Pty Ltd* (1957) 98 CLR 93, 110.
2 See Stoljar, "Offer, Promise and Agreement" (1955) 50 *Northwestern University Law Review* 445, 453–6.
3 Mensch, "Freedom of Contract as Ideology" (1981) 33 *Stanford Law Review* 753, 760.
4 See Mensch, "Freedom of Contract as Ideology" (1981) 33 *Stanford Law Review* 753, 755–6.
5 Collins, *The Law of Contract* (4th ed, 2003), p 159.

The classical approach to contract formation has been softened by developments in the law of estoppel, misleading conduct, negligent misrepresentation and unjust enrichment, which mean that parties in negotiation today clearly owe obligations to one another before the moment of formation.[6] The courts also find it difficult to fit the facts of some cases within the offer and acceptance framework. Even where the parties have clearly reached an agreement, it can be difficult to identify conduct that can be characterised as an offer on one side and conduct that can be characterised as an acceptance on the other. Many everyday transactions are entered into with little or no discussion of terms. A tram ticket may be purchased from a machine, for example, or an airline ticket over the telephone, with very few terms having been spelt out. A contract may be made with a professional person, such as a medical specialist, without even any mention of price. In cases where there is extensive discussion of terms, such as commercial agreements drafted by solicitors, there is unlikely to be a formal offer made by one party which is accepted by the other. Instead there may be a series of negotiations, which culminates in the parties simultaneously signing a written document.

Although the courts recognise its deficiencies,[7] the traditional offer and acceptance approach is routinely applied when the courts need to decide whether a contract has been formed. In order to identify whether, when or where a contract has been formed, the courts will usually seek to attach the labels "offer" and "acceptance" to particular actions, even where it seems somewhat artificial to do so.[8] As we will see, however, a contract can be established without an identifiable offer and acceptance, provided the parties have manifested mutual assent and appear to have reached a concluded bargain.[9]

OFFER

The nature of an offer

[3.10] An offer is an expression of willingness to enter into a contract on specified terms.[10] A proposal only amounts to an offer if the person making it indicates that an acceptance is invited and will conclude the agreement between the parties.[11] In *Brambles Holdings Ltd v Bathurst City Council*, Heydon JA suggested in obiter that an offer must take the form of a proposal for consideration which gives the offeree an opportunity to choose between acceptance and rejection.[12] On this view, a communication which "uses the language of command" and "peremptorily requests" the other party to adopt a particular course of action may not be regarded as an offer.[13]

It becomes important to determine whether particular conduct constitutes an offer when the party to whom it was directed purports to accept the offer and claims that a binding contract has been formed. Whether particular conduct amounts to an offer may also be

6 See [3.150].
7 See, eg, *MacRobertson Miller Airline Services v Commissioner of State Taxation (WA)* (1975) 133 CLR 125, 136.
8 See, eg, *MacRobertson Miller Airline Services v Commissioner of State Taxation (WA)* (1975) 133 CLR 125.
9 See [3.145].
10 Carter, *Contract Law in Australia* (7th ed, 2018), [3-07].
11 American Law Institute, *Restatement of Contracts (2d)* (1981), § 24; Greig and Davis, *The Law of Contract* (1987), p 254.
12 *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, 171. This point is discussed further at [3.145].
13 *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, 171.

relevant in ascertaining the terms of a contract or in determining when or where a contract has been made. The cases discussed below show that it is also sometimes necessary to determine whether particular conduct constitutes an offer for other reasons, such as determining whether a statutory offence of offering prohibited goods for sale has been committed.

In determining whether an offer has been made, the crucial issue is whether it would appear to a reasonable person in the position of the offeree that an offer was intended and that a binding agreement would be made upon acceptance. It does not matter whether the offeror in fact intended to make an offer; the court determines the offeror's intention objectively, according to outward manifestations.[14] The decision of the English Court of Appeal in the quaint old case of *Carlill v Carbolic Smoke Ball Co*[15] provides a useful illustration of the classical principles.

The defendants manufactured and sold a device called the "Carbolic Smoke Ball", which was claimed to prevent colds and influenza. They placed an advertisement in various newspapers which said that a £100 reward would be paid to any person who contracted a cold or influenza after having used the device three times daily for two weeks, in accordance with the directions supplied with each ball. The advertisement said: "£1000 is deposited with the Alliance Bank, Regent Street, shewing our sincerity in the matter". After reading the advertisement, the plaintiff purchased a smoke ball, used it for several weeks and then contracted influenza.

The defendants refused to pay the reward to the plaintiff. The plaintiff's claim that there was a contract between the parties was met with five arguments. First, the defendants argued that no promise was intended and the advertisement was a "mere puff" which meant nothing. Secondly, no offer had been made to any particular person. Thirdly, the plaintiff had not notified her acceptance of any offer. Fourthly, the agreement was uncertain because it failed to stipulate a period within which the disease must be contracted. Fifthly, the plaintiff had supplied no consideration for the defendant's promise.

The English Court of Appeal rejected these arguments and held unanimously that a contract had been formed between the plaintiff and the defendants. That contract obliged the defendants to pay £100 to the plaintiff. In relation to the first argument, the court held that the statement relating to the bank deposit made it clear that a promise was intended.[16] The court construed the advertisement objectively, according to what an ordinary person reading the document would think was intended, rather than by reference to what the defendant actually intended.[17] In relation to the second argument, the court held that the offer was made to the whole world and could be accepted by any person who performed the conditions on the faith of the advertisement.[18] Thirdly, the court held that, although acceptance of an offer must normally be notified to the offeror, the offeror may dispense with that notification. An offer that calls for performance of particular conditions may be accepted by performance of those conditions. An offer of a reward is typically this type of offer.[19] Fourthly, the court held

14 For example, *Carlill v Carbolic Smoke Ball Co* [1893] 1 QB 256; *Storer v Manchester City Council* [1974] 1 WLR 1403.

15 *Carlill v Carbolic Smoke Ball Co* [1893] 1 QB 256.

16 *Carlill v Carbolic Smoke Ball Co* [1893] 1 QB 256, 261–2, 268, 273–4.

17 *Carlill v Carbolic Smoke Ball Co* [1893] 1 QB 256, 266.

18 *Carlill v Carbolic Smoke Ball Co* [1893] 1 QB 256, 262, 268.

19 *Carlill v Carbolic Smoke Ball Co* [1893] 1 QB 256, 262–3, 269–70, 274.

that a reasonable construction must be placed on the advertisement, which made it sufficiently certain. It was possible to construe the document in three different ways, so that the reward would be paid to any person who contracted the disease during the epidemic, while the smoke ball was in use or within a reasonable time after using it.[20] Each of those possible restrictions was clearly satisfied here. Fifthly, the court held that the use of the smoke ball by the plaintiff constituted both a benefit to the defendant and a detriment to the plaintiff, either of which would have been enough to constitute good consideration for the promise.[21]

Unilateral contracts

[3.15] The contract in *Carlill v Carbolic Smoke Ball Co* was of a kind known as a "unilateral" contract. A unilateral contract is one in which the offeree accepts the offer by performing his or her side of the bargain. As the High Court has explained, "the consideration on the part of the offeree is completely executed by the doing of the very thing which constitutes acceptance of the offer".[22] The offer is accepted by performing an act, and the performance of that act is all that the contract requires of the offeree. Accordingly, by the time the contract is formed, the offeree has already performed all his or her obligations. In *Carlill v Carbolic Smoke Ball Co*, the plaintiff accepted the company's offer to pay the reward by using the smoke ball in accordance with the instructions and then contracting influenza. The offer of a reward for a lost dog is another example of a unilateral contract; the finder accepts the offer by returning the dog and thereby does all that the contract requires of him or her.

As the High Court explained in *Australian Woollen Mills Pty Ltd v Commonwealth*, the expression "unilateral contract" is a misnomer because there must necessarily be two parties to a contract.[23] A unilateral contract is only unilateral in the sense that, because one party has performed his or her obligations by the time of formation, only one party is ever under a contractual obligation. The contract can thus be distinguished from a "bilateral" contract formed by an exchange of promises. At the time of formation of a bilateral contract, the obligations of both parties remain to be performed. In other words, in a bilateral contract, the obligations of both parties are *executory* at the time of formation. In the case of a unilateral contract, the obligations of one party (the offeree) are *executed* at the time of formation, while the obligations of the other party (the offeror) are *executory*.

In *Australian Woollen Mills Pty Ltd v Commonwealth*, the plaintiff (AWM) claimed that a unilateral contract had arisen out of the Commonwealth Government's wool subsidy scheme. The scheme was introduced after the Second World War, at a time when wool was scarce. The Commonwealth subsidised purchases of wool by manufacturers of woollen products to enable those manufacturers to supply the products at low prices. In 1946, the Commonwealth announced in a series of letters to manufacturers, including AWM, that it would pay a subsidy on all wool purchased for domestic use by Australian manufacturers. AWM purchased large quantities of wool over the next two years, including purchases in April, May and June 1948 in respect of which the subsidy had not been paid. In June 1948, the Commonwealth announced that it was discontinuing the scheme but would ensure that each manufacturer would have a

20 *Carlill v Carbolic Smoke Ball Co* [1893] 1 QB 256, 266–7, 263–4, 274.

21 *Carlill v Carbolic Smoke Ball Co* [1893] 1 QB 256, 264–5, 270–1, 274–5.

22 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424, 456.

23 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424, 456.

certain amount of subsidised wool in stock on 30 June 1948. The stockpile of wool held by AWM exceeded this amount and so the Commonwealth required AWM to repay the subsidy paid on that excess. AWM repaid that amount but later sued to recover it, along with the unpaid subsidy on the April, May and June purchases.

AWM claimed that each of the announcements by the Commonwealth constituted a contractual offer to pay the subsidy in return for AWM purchasing wool for domestic consumption. Each purchase of wool was therefore said to give rise to a unilateral contract. AWM claimed that each of its purchases of wool constituted both an acceptance of the Commonwealth's offer and consideration for the promise to pay the subsidy. The High Court held that, for a unilateral contract to arise, the promise must be made *in return for* the doing of the act.[24] There must be a relation of *quid pro quo* (this for that) between the offeree's act and the offeror's promise. The court distinguished a unilateral contract from a conditional gift. If A says to B in Melbourne, "I will pay you £1000 on your arrival in Sydney", this alone does not establish the existence of a contract on B's arrival in Sydney. B must establish that the money was to be paid in return for B travelling to Sydney. The court referred to three different ways of stating this requirement, which all state essentially the same test.[25] First, the principal test is whether the "offeror" has expressly or impliedly requested the doing of the act by the "offeree". Secondly, the court can look to whether the "offeror" has stated a price which the "offeree" must pay for the promise. Thirdly, the court can ask whether the offer was made in order to induce the doing of the act.

In this case, AWM failed to establish that there was a relation of quid pro quo between the Commonwealth's promises and AWM's acts. AWM also failed to establish that, viewed objectively, the offer was intended to give rise to a contractual obligation.[26] There was, therefore, no contract between the parties, and the Commonwealth was under no obligation to pay the subsidy. On appeal, the Privy Council accepted that the Commonwealth might be said to have impliedly requested the purchase of wool by manufacturers. They said: "There may be cases where the absence of a request negatives the existence of a contract. The presence of a request does not however in itself establish a contract."[27] The Privy Council nevertheless upheld the High Court's decision on the basis that the Commonwealth's letters must be read as statements of policy and could not be regarded as offers to contract.[28]

This case demonstrates the inextricable connection between the requirements of offer and acceptance, consideration and intention to create legal relations. An offer is effective only if it identifies a valid consideration and manifests an intention to create a legal obligation. The requirement of certainty is also inherent in offer and acceptance, as *Carlill v Carbolic Smoke Ball Co* shows. An offer can lead to a binding agreement only if the offer identifies the terms of the proposed agreement with sufficient certainty.

Offers and invitations to treat

[3.20] An offer is often distinguished from an invitation to treat, which is an invitation to others to make offers or enter into negotiations. An indication by the owner of property that

24 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424, 456–7.

25 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424, 458.

26 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424, 457–8.

27 *Australian Woollen Mills Pty Ltd v Commonwealth* (1955) 93 CLR 546, 550.

28 *Australian Woollen Mills Pty Ltd v Commonwealth* (1955) 93 CLR 546.

he or she might be interested in selling at a certain price, for example, has been regarded as an invitation to treat.[29] A wine merchant's circulation of a price list has been regarded as an invitation to treat on the basis that, if it was an offer, the merchant might find himself obliged to supply unlimited quantities of wine at the listed price.[30] Whether particular conduct amounts to an offer is a question to be decided on the facts of each case[31] and there are no firm rules about whether particular types of conduct necessarily do or do not amount to an offer.[32] Nevertheless, the courts have tended to take a consistent approach to the identification of offer and acceptance in common transactions.

Shop sales

[3.25] The display of goods for sale, whether in a shop window or on the shelves of a self-service store, is ordinarily treated as an invitation to treat and not an offer.[33] In the English case *Fisher v Bell*,[34] it was held that the owner of a shop who displayed a flick-knife in a shop window had not committed the statutory offence of "offering" the knife for sale. In *Pharmaceutical Society of Great Britain v Boots Cash Chemists Ltd*,[35] it was necessary for the English Court of Appeal to determine when a sale occurred in a self-service pharmacy in order to determine whether sales took place under the supervision of a registered pharmacist. Pharmacists supervised transactions at the cash registers but did not supervise the customers' selection of goods from the shelves. The plaintiff argued that the display of goods should be regarded as an offer, which was accepted when a customer took an item from the shelf and placed it in his or her receptacle. The Court of Appeal rejected this argument on the basis that customers must be entitled to return and substitute articles they have chosen from the shelves.[36] If the customers are entitled to return articles selected from the shelves, the court reasoned, customers must be regarded as making an offer when they present the items to the cashier and are not bound until the cashier has accepted that offer.[37] Accordingly, the defendant was held to have complied with the legislative requirement that the sales be supervised. The characterisation of the display of goods as an offer is not, however, itself inconsistent with the entitlement of customers to return goods they have selected. A customer's acceptance would not be effective until communicated to the offeror, so a sale must on any interpretation take place at the checkout.[38]

In both *Fisher v Bell* and *Boots Cash Chemists*, the issue before the court did not relate to the contractual rights of the parties, but to whether a statutory offence had been committed. The English courts took a technical approach in these cases to determining whether a statutory offence had been committed. In Australia, the courts have tended to take a less technical approach to deciding whether goods have been "offered for sale" for the purpose of

29 See, eg, *Harvey v Facey* [1893] AC 552.

30 *Grainger v Gough* [1896] AC 325, 334.

31 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424, 457; *B Seppelt and Sons Ltd v Commissioner for Main Roads* (1975) 1 BPR 9147, 9151.

32 For example, *Carlill v Carbolic Smoke Ball Co* [1893] 1 QB 256.

33 See Winfield, "Some Aspects of Offer and Acceptance" (1939) 55 *Law Quarterly Review* 499, 517.

34 *Fisher v Bell* [1961] 1 QB 394.

35 *Pharmaceutical Society of Great Britain v Boots Cash Chemists Ltd* [1953] 1 QB 401.

36 *Pharmaceutical Society of Great Britain v Boots Cash Chemists Ltd* [1953] 1 QB 401, 405–6.

37 *Pharmaceutical Society of Great Britain v Boots Cash Chemists Ltd* [1953] 1 QB 401, 406, 408.

38 Greig and Davis, *The Law of Contract* (1987), p 263.

determining whether a statutory provision has been breached. In *Goodwin's of Newtown Pty Ltd v Gurrey*,[39] for example, the defendant was held to have been "offering goods for sale" in breach of the *Early Closing Act 1926* (SA), although the defendant's conduct amounted to no more than an invitation to treat. The defendant displayed television sets with marked prices and provided information to prospective purchasers. Prospective purchasers were told that the sets on display were not for sale, but an equivalent set could be purchased from the defendant at the marked price.

A similar approach has been favoured in the interpretation of the provision that was s 56(2) of the *Trade Practices Act 1974* (Cth), now s 35(2) of the ACL, which requires a corporation that has advertised goods or services for supply at a specified price to "offer such goods or services for supply" at that price for a reasonable time and in reasonable quantities. Although it was held in one case that the corporation was required to make offers to sell in the technical contractual sense,[40] most judges have favoured a non-technical approach.[41] In *Wallace v Brodribb*,[42] Spender J said that unnecessary difficulties were introduced by drawing distinctions between offers and invitations to treat and the expression "offer to supply" should be given its ordinary meaning.

Auctions

[3.30] The holding of a public auction will also usually be regarded as an invitation to treat. It is well accepted that an auctioneer does not make an offer to sell but merely invites offers from those present at the auction. Each bid constitutes an offer, and the auctioneer communicates acceptance of the final bid by the fall of the hammer.[43] This means that no contractual claim can arise if the auction is cancelled,[44] a bidder is entitled to withdraw his or her bid before it is accepted[45] and the auctioneer is not obliged to sell to the highest bidder.[46] The common law position is reflected in the Sale of Goods Acts, which provide that a sale of goods by auction is complete when the auctioneer announces its completion and, until such announcement, a bid may be retracted.[47]

The situation becomes more complicated when an auction is advertised to be held "without reserve". In *AGC (Advances) Ltd v McWhirter*,[48] it was held that an announcement that an auction was to be held without reserve did not alter the general rule. The holding of an auction without reserve did not constitute an offer and did not bind the vendor to sell to the highest bidder. The auction in that case was not advertised as being without reserve, but the

39 *Goodwin's of Newtown Pty Ltd v Gurrey* [1959] SASR 295.

40 *Reardon v Morley Ford Pty Ltd* (1980) 33 ALR 417.

41 *Attorney General for NSW v Mutual Home Loans Fund of Australia Ltd* [1971] 2 NSWLR 162, 165; *Attorney General for NSW v Australian Fixed Trusts* [1974] 1 NSWLR 110, 117; *WA Pines Pty Ltd v Registrar of Companies* [1976] WAR 149, 153; *Wallace v Brodribb* (1985) 58 ALR 737.

42 *Wallace v Brodribb* (1985) 55 ALR 737.

43 *Payne v Cave* (1789) 3 TR 148; 100 ER 502; *British Car Auctions Ltd v Wright* [1972] 1 WLR 1591, 1524; *AGC (Advances) Ltd v McWhirter* (1977) 1 BPR 9454.

44 *Harris v Nickerson* (1873) LR 8 QB 286.

45 *Payne v Cave* (1789) 3 TR 148; 100 ER 502.

46 *AGC (Advances) Ltd v McWhirter* (1977) 1 BPR 9454.

47 *Sale of Goods Act 1954* (ACT), s 60; *Sale of Goods Act 1923* (NSW), s 60; *Sale of Goods Act* (NT), s 60; *Sale of Goods Act 1896* (Qld), s 59; *Sale of Goods Act 1895* (SA), s 57; *Sale of Goods Act 1896* (Tas), s 62; *Goods Act 1958* (Vic), s 64; *Sale of Goods Act 1895* (WA), s 57.

48 *AGC (Advances) Ltd v McWhirter* (1977) 1 BPR 9454.

auctioneer announced during the auction that the "property is on the market", which was held to have the same effect.

It has been held in England that, by holding an auction without reserve, an auctioneer makes an offer to sell to the highest bidder.[49] If the highest bid is not accepted, no contract arises between the bidder and the vendor, but the bidder is able to sue the auctioneer for damages under a separate, collateral contract. This contract governs the process by which the auction is conducted. By announcing the conditions of auction, the auctioneer offers to conduct the auction in a particular way and a bidder may accept that offer by making the highest bid.[50]

Tenders

[3.35] A contract may also be formed by a tender process. Unlike an auction, a tender process involves each interested party submitting a single bid without knowing what other bids have been made. The tender process is sometimes used for the sale of commercial or residential property. It is commonly used by governments seeking to contract out the performance of government functions, such as the construction or operation of a prison. A call for written tenders will also usually constitute an invitation to treat, with each tender constituting an offer. A person calling for tenders can stipulate the basis on which the tender process will be conducted and will be bound by any conditions which he or she says will govern the tender process. In *Harvela Investments Ltd v Royal Trust Co of Canada (CI) Ltd*,[51] for example, a call for tenders was held to amount to an offer because the vendor promised to accept the highest bid.

In *Harvela Investments Ltd v Royal Trust Co of Canada (CI) Ltd*, two parties, Harvela and Outerbridge, were invited to submit written tenders for the purchase of shares. The successful tenderer would obtain control of the company. The letter sent by the vendors to the two tenderers said that "we bind ourselves to accept" the "highest offer" complying with the conditions of tender. Harvela tendered to purchase the shares for $2.175m and Outerbridge for $2.1m "or $101 000 in excess of any other offer which you may receive". The vendor accepted Outerbridge's tender, but Harvela claimed it was entitled to purchase the shares for $2.175m.

The trial judge, Peter Gibson J, held that the invitation to submit tenders amounted to an offer capable of acceptance by submission of the highest bid.[52] The Court of Appeal upheld this conclusion and it was accepted by the House of Lords. The resulting contract was said to be a unilateral contract "in the sense of a contract brought into existence by the act of one party in response to a conditional promise made by the other".[53] The fact that the invitation described the tenders as "offers" did not require the court to conclude that they were offers in law, since it was for the court to determine the character of a document.[54] The vendors' promise to accept the highest bid converted what would otherwise have been an invitation to treat into an

49 *Warlow v Harrison* (1859) 1 El & El 295; 120 ER 920; *Barry v Davies* [2000] 1 WLR 1962.

50 This reasoning was applied in *Ulbrick v Laidlaw* [1924] VLR 247. See further Carter, "Auction 'Without Reserve' – Barry v Davies" (2001) 17 *Journal of Contract Law* 69.

51 *Harvela Investments Ltd v Royal Trust Co of Canada (CI) Ltd* [1986] 1 AC 207.

52 *Harvela Investments Ltd v Royal Trust Co of Canada (CI) Ltd* [1985] 1 Ch 103, 119.

53 *Harvela Investments Ltd v Royal Trust Co of Canada (CI) Ltd* [1985] 1 Ch 103, 119.

54 *Harvela Investments Ltd v Royal Trust Co of Canada (CI) Ltd* [1985] 1 Ch 103, 119.

offer which, when the highest bid was received, completed a contract.[55] Whether this should be regarded as a contract to sell the shares or a contract to enter into an enforceable contract to sell the shares did not matter, since they amount to the same thing.[56] The principal question, then, was whether the contract had been made with Harvela or Outerbridge. This depended on whether Outerbridge's tender conformed to the requirements of the vendor's invitation. The trial judge held that there was an implied term in the invitation that excluded referential bids.[57] This meant that a contract had been made between the vendors and Harvela. Although the Court of Appeal regarded Outerbridge's tender as valid, Harvela successfully appealed to the House of Lords. The House of Lords held that the question whether the invitation allowed referential bids depended on the presumed intention of the vendors deduced from the terms of the invitation read as a whole. Those terms were inconsistent with the making of referential bids.[58]

The use of the tender process for government procurement of goods and services has come under considerable judicial scrutiny in recent years.[59] Although each case turns on its own facts, it has been held in a number of cases that governments and government instrumentalities calling for tenders have owed contractual obligations to tenderers under preliminary contracts governing the tender process.[60] These tender process contracts also impose obligations on tenderers, such as an obligation not to withdraw their tenders.[61] In *Blackpool and Fylde Aero Club Ltd v Blackpool Borough Council*,[62] the English Court of Appeal held that the Council was under an implied contractual obligation to give consideration to complying tenders. The call for tenders amounted to an offer, which was accepted by the submission of a complying tender. The Council was liable for damages under this preliminary contract when it mistakenly failed to consider the plaintiff's complying tender. In *Hughes Aircraft Systems International v Airservices Australia*,[63] Finn J found that a tender process conducted by the Civil Aviation Authority (CAA) was governed by two "process contracts". The first contract was formed by signature of a letter in which the CAA and the two tenderers committed themselves to participate in a tender process. The terms of the second contract were set out in a request for tenders, which amounted to an offer accepted by each tenderer's lodgement of a tender. The CAA was obliged to conduct the tender process in accordance with those process contracts.

Ticket cases

[3.40] In some cases, the courts are concerned to identify offer and acceptance for the purpose of determining *when*, rather than *whether*, a contract was formed between two parties. It has been necessary to decide when a contract has been formed in order to determine whether a

55 *Harvela Investments Ltd v Royal Trust Co of Canada (CI) Ltd* [1985] 1 Ch 103, 119, 133–4, 137, 149.

56 *Harvela Investments Ltd v Royal Trust Co of Canada (CI) Ltd* [1985] 1 Ch 103, 121, 133–4, quoting *Hillas & Co Ltd v Arcos* (1937) 147 LT 503, 515.

57 *Harvela Investments Ltd v Royal Trust Co of Canada (CI) Ltd* [1985] 1 Ch 103, 119.

58 *Harvela Investments Ltd v Royal Trust Co of Canada (CI) Ltd* [1987] 1 AC 207, 230–4, 225.

59 See Seddon, *Government Contracts: Federal State and Local* (6th ed, 2018), ch 7.

60 In addition to the cases mentioned below, see *Martel Building Ltd v Canada* [2000] 2 SCR 800.

61 See *Ontario v Ron Engineering & Construction Eastern Ltd* (1981) 1 SCR 111.

62 *Blackpool and Fylde Aero Club Ltd v Blackpool Borough Council* [1990] 1 WLR 1195. See Phang, "Tenders and Uncertainty" (1991) 4 *Journal of Contract Law* 46.

63 *Hughes Aircraft Systems International v Airservices Australia* (1997) 76 FLR 151, 162–87.

document is chargeable with stamp duty.[64] When a contract has been entered into between parties in different jurisdictions, it is sometimes necessary for a court to determine when and where the contract was made so that the court can decide whether it can adjudicate on the contract.[65]

It may also be important to determine when a contract has been formed in order to determine whether written conditions given by one party to another form part of the contract. If one party gives the other notice of terms after a contract has been formed, then those terms cannot form part of the contract.[66] This problem is exemplified by cases involving the issue of tickets for passenger transport. Typically a ticket containing contractual terms is issued after the fare has been paid and it might therefore be thought that the contract is formed before the ticket is issued. The courts have usually regarded the issue of the ticket as an offer which can be accepted or rejected by the passenger after the passenger has had a reasonable opportunity to consider the conditions on the ticket. The difficulty of applying the offer and acceptance model to this type of transaction is illustrated by the decision of the High Court in *MacRobertson Miller Airline Services v Commissioner of State Taxation (WA)*.[67]

The issue before the High Court was whether an airline ticket issued by MacRobertson Miller was chargeable with stamp duty as an "agreement" or a "memorandum of agreement". The airline's practice was first to quote the fare and availability of seats and then to issue a ticket in return for the fare. The ticket contained a condition, giving the airline the right to cancel a flight or cancel a booking without incurring any liability. The court held unanimously that a ticket did not record the terms of an agreement, but rather the terms of an offer which was subsequently accepted by conduct. The judges' reasons for reaching that conclusion differed.

Barwick CJ thought that the sweeping exemption clauses relieved the airline from any obligation to carry the passenger. The exemption conferred by clauses 2 and 5 "fully occupies the whole area of possible obligation, leaving no room for the existence of a contract of carriage".[68] Even apart from those express terms, however, the uncertainties of air travel precluded any promise to carry the passenger from being inferred from the issue of the ticket. Barwick CJ therefore considered that the arrangement was similar to a unilateral contract. The passenger was in effect making an offer, which could be accepted by conduct. If the airline carried the passenger, then the airline would be entitled to retain the fare as a "reward". If the passenger was not carried, the airline incurred no obligation other than to refund the fare. On that basis, there were no contractual obligations between the airline and the passenger until the airline provided the passenger with a seat on the plane.[69]

Stephen J adopted the conventional analysis in "ticket cases", which is that the ticket constitutes an offer by the airline, which is capable of acceptance or rejection by the passenger once the passenger has had a reasonable opportunity to read the conditions.[70] On

64 *MacRobertson Miller Airline Services v Commissioner of State Taxation (WA)* (1975) 133 CLR 125.

65 For example, *Oceanic Sun Line Special Shipping Company Inc v Fay* (1988) 165 CLR 197; *Brinkibon Ltd v Stahag Stahl und Stahlwarenhandelsgesellschaft mbH* [1983] 2 AC 34.

66 See [12.40].

67 *MacRobertson Miller Airline Services v Commissioner of State Taxation (WA)* (1975) 133 CLR 125.

68 *MacRobertson Miller Airline Services v Commissioner of State Taxation (WA)* (1975) 133 CLR 125, 133.

69 *MacRobertson Miller Airline Services v Commissioner of State Taxation (WA)* (1975) 133 CLR 125, 133–4.

70 *MacRobertson Miller Airline Services v Commissioner of State Taxation (WA)* (1975) 133 CLR 125, 137–40.

that basis, the ticket records the terms of an offer. Jacobs J agreed that no agreement was formed at the time the ticket was issued for the reasons advanced by both Stephen J and Barwick CJ. Jacobs J agreed with Stephen J that formation of the contract could not precede the notification of special conditions and the ticket simply recorded the terms of an offer made by an airline. He also agreed with Barwick CJ that clause 2 negatived any promise to carry which might have been implied.[71] The lack of any obligation imposed on the airline prevented the ticket from representing an enforceable agreement. Jacobs J also noted that the person who buys the ticket may not be the passenger. Where the buyer is not the passenger, then two contracts will arise. The purchase of the ticket will result in an executory agreement between the purchaser of the ticket and the airline. The issue of the ticket will also constitute an offer made to the passenger, which the passenger can accept by presenting herself or himself for travel.[72]

MacRobertson Miller Airline Services v Commissioner of State Taxation (WA) provides a good illustration of the difficulties experienced in applying the doctrine of offer and acceptance "outside the realms of commerce and conveyancing, to the everyday contractual situations which are a feature of life in modern urban communities".[73] As Stephen J noted, the contract involved sweeping restrictions on passengers' rights, passengers were not given the opportunity to negotiate the terms of the contract, and any attempt to negotiate would "in any event usually be pointless", since the carrier was willing to contract only on its standard terms.[74]

Electronic transactions

[3.41] The common law rules of offer and acceptance can be applied to electronic transactions in the same way they can be applied to other forms of communication.[75] Electronic communications raise some particular issues about the mechanics of contract formation but do not call for a fundamentally different approach.[76] Although there is no particular need for legislation dealing with offer and acceptance in electronic transactions, Electronic Transactions Acts (ETAs) have been enacted in all Australian States and Territories with the broader object of providing a regulatory framework that facilitates and promotes confidence in electronic transactions.[77] The ETAs were originally introduced pursuant to a national scheme to implement the United Nations Commission on International Trade Law (UNCITRAL) *Model Law on Electronic Commerce 1996*. The purpose of the Model Law was

71 *MacRobertson Miller Airline Services v Commissioner of State Taxation (WA)* (1975) 133 CLR 125, 148.

72 *MacRobertson Miller Airline Services v Commissioner of State Taxation (WA)* (1975) 133 CLR 125, 146.

73 *MacRobertson Miller Airline Services v Commissioner of State Taxation (WA)* (1975) 133 CLR 125, 136.

74 *MacRobertson Miller Airline Services v Commissioner of State Taxation (WA)* (1975) 133 CLR 125, 136.

75 See generally Nolan, "Offer and Acceptance in the Electronic Age" in Burrows and Peel (eds), *Contract Formation and Parties* (2010), pp 61–87 and Furmston and Tolhurst, *Contract Formation: Law and Practice* (2nd ed, 2016), pp 159-73.

76 Nolan, "Offer and Acceptance in the Electronic Age" in Burrows and Peel (eds), *Contract Formation and Parties* (2010), pp 86–7.

77 *Electronic Transactions Act 2001* (ACT), s 3; *Electronic Transactions Act 1999* (Cth), s 3; *Electronic Transactions Act 2000* (NSW), s 3; *Electronic Transactions (Northern Territory) Act*, 3; *Electronic Communications Act 2000* (SA), s 3 (facilitates and promotes "the use of electronic communications"); *Electronic Transactions (Queensland) Act 2001*, s 3; *Electronic Transactions (Victoria) Act 2000*, s 4; *Electronic Transactions Act 2011* (WA), s 3.

to remove obstacles to electronic commerce and ensure the validity of electronic transactions.[78] Since the introduction of the ETAs, the Model Law has been supplemented by the *United Nations Convention on the Use of Electronic Communications in International Contracts*.[79] The purpose of the Convention is to facilitate electronic transactions between parties located in different countries. The Convention builds on the Model Law and clarifies some of the issues and fills some of the gaps in the regime introduced by the Model Law. The Convention was not intended to alter substantive contract law rules but only to clarify some of the legal issues.[80] The ETAs have been amended in accordance with the Convention to clarify some questions about the formation of contracts by way of electronic communications. Although the Convention relates only to international contracts, the amendments to the ETAs extend the provisions of the Convention to contracts made within Australia, including personal, family and household contracts.

First, the new legislation provides that a proposal to make a contract through electronic communications which is not addressed to a particular person, but is made generally accessible to people using information systems, is to be treated as an invitation to make offers unless it clearly indicates an intention to be bound in the case of acceptance.[81] This is clearly intended to ensure that websites offering goods or services should generally be considered to be making an invitation to treat, rather than an offer, and is entirely consistent with the approach of the common law to more traditional communications in cases such as *Grainger v Gough*.[82] Secondly, the ETAs confirm that a contract formed between a natural person and an automated system, or between two automated systems, is not invalid merely on the ground that a natural person was not directly involved in the process.[83] Thirdly, and more significantly, the ETAs provide that where a natural person makes an "input error" in the course of a transaction with an automated system, and the system provides no opportunity to correct that error, then the person making the error is entitled to "withdraw the portion of the communication in which the input error was made", provided he or she does so as soon as possible after learning of the error and provided he or she has not received any material benefit from goods or services provided by the other party.[84] The ETAs specifically provide

78 UNCITRAL Secretariat, *Guide to Enactment of the UNCITRAL Model Law on Electronic Commerce* (1996), http://www.uncitral.org.

79 See Mik, "Updating the Electronic Transactions Act – Australia's Accession to the UN Convention on the Use of Electronic Communications in International Contracts 2005" (2010) 26 *Journal of Contract Law* 184.

80 Explanatory note by the UNCITRAL Secretariat on the *United Nations Convention on the Use of Electronic Communications in International Contracts*, [3]–[4]; *Explanatory Memorandum, Electronic Transactions Bill 2011* (Cth), p 3.

81 *Electronic Transactions Act 2001* (ACT), s 14B; *Electronic Transactions Act 1999* (Cth), s 15B; *Electronic Transactions Act 2000* (NSW), s 14B; *Electronic Transactions (Northern Territory) Act*, s 14B; *Electronic Communications Act 2000* (SA), s 14B; *Electronic Transactions Act 2000* (Tas), s 12B; *Electronic Transactions (Victoria) Act 2000*, s 14B; *Electronic Transactions (Queensland) Act 2001*, s 26B; *Electronic Transactions Act 2011* (WA), s 18.

82 *Grainger v Gough* [1896] AC 325. See [3.20].

83 *Electronic Transactions Act 2001* (ACT), s 14C; *Electronic Transactions Act 1999* (Cth), s 15C; *Electronic Transactions Act 2000* (NSW), s 14C; *Electronic Transactions (Northern Territory) Act*, s 14C; *Electronic Communications Act 2000* (SA), s 14C; *Electronic Transactions Act 2000* (Tas), s 12C; *Electronic Transactions (Victoria) Act 2000*, s 14C; *Electronic Transactions (Queensland) Act 2001*, s 26C; *Electronic Transactions Act 2011* (WA), s 19.

84 *Electronic Transactions Act 2001* (ACT), s 14D; *Electronic Transactions Act 1999* (Cth), s 15D; *Electronic Transactions Act 2000* (NSW), s 14D; *Electronic Transactions (Northern Territory) Act*, s 14D; *Electronic*

that the right to withdraw a portion of an electronic communication is not a right to rescind a contract. The consequences of withdrawal of the relevant portion of the communication are to be determined in accordance with applicable legal rules, but clearly in some circumstances, this will undermine the validity of the contract. If, for example, a consumer booking a ticket for air travel through a website accidentally booked a seat for travel on the wrong date, and was not given an opportunity to correct the error, the withdrawal of that portion of the communication would undermine the validity of the contract, since the withdrawn communication would have identified the subject matter of the contract.[85] Since most websites provide an opportunity to correct input errors, it seems unlikely that this provision will be widely used.

Termination of an offer

[3.45] An offer will cease to be available for acceptance when it is withdrawn by the offeror, lapses or is rejected by the offeree.

Withdrawal

General rule

[3.47] An offer may be revoked at any time before it is accepted. At common law, a promise to hold an offer open for a specified period is not binding unless the offeree has given consideration for that promise.[86] The offeror can therefore revoke the offer before the specified period for acceptance has expired, provided the offer has not been accepted in the meantime. The withdrawal of an offer is effective only when it has been actually communicated to the offeree. No exception is made for a withdrawal sent by post.[87]

In civil law systems, a promise to hold an offer open is binding: in France, an offeror who wrongfully revokes an offer will be liable in damages,[88] while in Germany, an attempt to withdraw an offer prematurely will simply be ineffective.[89] The German approach is adopted in both the *United Nations Convention on International Contracts for the Sale of Goods* (Vienna Convention) and the *UNIDROIT Principles of International Commercial Contracts 2016* (UPICC).[90] Article 16(2) of the Vienna Convention and art 2.1.4 of the UPICC both provide that an offer cannot be revoked if it states a fixed time for acceptance or otherwise indicates that it is irrevocable.

Communications Act 2000 (SA), s 14D; *Electronic Transactions Act 2000* (Tas), s 12D; *Electronic Transactions (Victoria) Act 2000*, s 14D; *Electronic Transactions (Victoria) Act 2000*, s 14D; *Electronic Transactions Act 2011* (WA), s 20.

85 See the Explanatory note by the UNCITRAL Secretariat on the *United Nations Convention on the Use of Electronic Communications in International Contracts*, [241].

86 *Dickinson v Dodds* (1876) LR 2 Ch D 463; *Goldsbrough Mort & Co v Quinn* (1910) 10 CLR 674, 678, 690. It is important to note that such a promise can give rise to an estoppel if it is relied upon: see [9.175]. To similar effect is *UNIDROIT Principles of International Commercial Contracts 2016*, art 2.1.4(2)(b).

87 *Byrne & Co v Leon Van Tienhoven & Co* (1880) LR 5 CPD 344.

88 Zweigert and Kötz, *Introduction to Comparative Law* (3rd ed, 1998), pp 359–60.

89 *Burgerliches Gesetzbuch* (BGB), § 145; Zweigert and Kötz, *Introduction to Comparative Law* (3rd ed, 1998), pp 361–2.

90 See [1.180].

Options

[3.50] A promise to hold an offer open is binding at common law if consideration has been given in return for that promise. The agreement between the parties is then described as an option. An option is an agreement between an option holder and a grantor under which the option holder is entitled to enter into a contract with the grantor on specified terms, either at a specified time or within a specified period. The option holder is then free to choose whether to exercise the option at that time or within that period. In *Goldsbrough, Mort & Co Ltd v Quinn*,[91] for example, the grantor gave the option holder an option to purchase certain land at a specified price at any time within one week of the agreement in return for the sum of five shillings paid to the grantor. The grantor's attempt to repudiate the offer before acceptance was held to be ineffective. The option holder exercised the option within the specified period and was able to force the grantor to sell the land as agreed.

There was a difference of opinion in *Goldsbrough, Mort & Co Ltd v Quinn* as to the true nature of an option. Griffith CJ and O'Connor J regarded an option to purchase a property as a contract for the sale of that property, conditional upon the option being exercised within the specified period.[92] This has been confirmed in subsequent cases as the preferred interpretation.[93] Isaacs J regarded an option as a preliminary contract to hold open an offer to sell the property, with the exercise of the option giving rise to a separate contract of sale.[94] The significance of the distinction between an irrevocable offer and a conditional contract in this case related to the remedy available to the option holder if the grantor purported to revoke the option. Griffith CJ preferred to treat the agreement as a conditional sale, which was enforceable by specific performance once the condition was satisfied. He took the view that, if regarded as an irrevocable offer, the only remedy available to the offeree in the event of revocation was damages. Isaacs J, however, held that the grantor's attempt to revoke the offer was ineffective, and so the option was successfully exercised and specific performance was available. On either view, therefore, the grantor's attempt to revoke the option was ineffective and, once the option holder had exercised the option, a contract of sale enforceable by specific performance subsisted between the parties.

In England, it has been said that an option is neither a conditional contract nor an irrevocable offer.[95] In *Spiro v Glencrown Properties Ltd*, in determining whether an option agreement satisfied the statutory requirement of a written contract for the sale of land, Hoffmann J did not find it useful or necessary to characterise the agreement as a conditional contract or an irrevocable offer. He found the analogy of the irrevocable offer useful to describe the position of the option holder and the analogy of a conditional contract useful to describe the position of the grantor of the option. An option resembles each of them but does not have all of the incidents of either. It is a legal relationship sui generis (of its own kind).[96] It cannot be regarded as a conditional contract, according to Hoffmann J, because "one generally thinks of a conditional contract as one that does not lie within the sole power of one of the parties

91 *Goldsbrough, Mort & Co Ltd v Quinn* (1910) 10 CLR 674.

92 *Goldsbrough, Mort & Co Ltd v Quinn* (1910) 10 CLR 674, 678–9, 685.

93 *Carter v Hyde* (1923) 33 CLR 115; *Laybutt v Amoco Australia Pty Ltd* (1974) 132 CLR 57, 71–6.

94 *Goldsbrough Mort & Co v Quinn* (1910) 10 CLR 674, 696. See also *Carter v Hyde* (1923) 33 CLR 115, 123.

95 *Spiro v Glencrown Properties Ltd* [1991] Ch 536.

96 *Spiro v Glencrown Properties Ltd* [1991] Ch 536, 544.

to the contract".[97] Nor can it be regarded as an irrevocable offer, since it conveys an equitable interest in land to the grantee.[98] Hoffmann J held that the option agreement satisfied the statutory requirement of writing because such a result was consistent with the intention of the legislature.[99]

Lapse

[3.55] An offer which is expressed to be available for acceptance for a particular period of time will lapse at the end of that period. If no period is stipulated, the offer will lapse after a reasonable time has passed. This can be explained either on the basis that a term can be implied that the offer lapses after a reasonable time has passed or on the basis that the court can infer rejection from the offeree's failure to accept the offer within a reasonable time.[100] What period of time is reasonable will depend on the circumstances, including the nature of the subject matter and the form in which the offer was made. A verbal offer to buy a car, for example, is likely to lapse after a short period, whereas a written offer to purchase a substantial parcel of land will be open for acceptance for a relatively longer period.

Identifying the duration of an offer will in some cases simply be a matter of determining how a reasonable person in the position of the offeree would interpret the offer. In *Bartolo v Hancock*, an offer made at the beginning of a five-day trial to settle the litigation on the basis the parties would discontinue their claims against each other and bear their own costs was interpreted, in its context, to be "a 'here and now' offer", the aim of which was "to dispose of the case then and there."[101] An attempt to accept the offer on the fifth day of the trial was unsuccessful.

There is some uncertainty as to whether an offer lapses on the death of the offeror or the offeree. In *Fong v Cilli*,[102] Blackburn J held that an offeree could not accept an offer after the offeror's death, where the offeree knew of the death before the purported acceptance. In *Smith v Woods*,[103] an offer was held to have been validly accepted after the death of the offeror by an offeree who was unaware of the offeror's death. The offer in question was an offer to compromise a dispute concerning the ownership and control of two companies. Ferguson JA held that "there is no reason why an offer should automatically be revoked upon death of the offeror. It is likely to depend upon the type of contract involved and the intention of the offeror assessed objectively."[104] Since the contract was not personal to the offeror, and there was no reason to think he would have intended the offer to lapse on his death, it remained open and was validly accepted. There are judicial statements to the effect that both the death of an offeror[105] and the death of the offeree[106] will necessarily terminate the offer, but those statements appear to be too wide.

97 *Spiro v Glencrown Properties Ltd* [1991] Ch 536, 544.

98 *Spiro v Glencrown Properties Ltd* [1991] Ch 536, 543.

99 *Spiro v Glencrown Properties Ltd* [1991] Ch 536, 546.

100 See *Farmers Mercantile Union and Chaff Mills Ltd v Coade* (1921) 30 CLR 113; *Manchester Diocesan Council v Commercial & General Investments Ltd* [1970] 1 WLR 241, 247–8.

101 *Bartolo v Hancock* [2010] SASC 305, [16].

102 *Fong v Cilli* (1968) 11 FLR 495, 498.

103 *Smith v Woods* [2014] VSC 646.

104 *Smith v Woods* [2014] VSC 646, [20].

105 *Dickinson v Dodds* (1876) 2 Ch D 463, 475; *Laybutt v Amoco Australia Pty Ltd* (1974) 132 CLR 57, 72–3.

106 *Reynolds v Atherton* (1921) 125 LT 690, 625. See further Greig and Davis, *The Law of Contract* (1987), p 344.

In the case of an option, there is at least a presumption that the death of the option holder does not prevent the option from being exercised by the option holder's personal representatives.[107] However, if the offer is personal to the option holder, then the option lapses. There seems to be no good reason why a similar presumption should not apply to the case of the death of the grantor of the option. Gibbs J has suggested that since an option is in essence a conditional contract, it can be enforced against the estate of a grantor, unlike an ordinary offer.[108]

Failure of condition and changed circumstances

[3.60] An offer may be made subject to an express or implied condition that must be fulfilled before the offer can be accepted. Alternatively, it may be made subject to an express or implied condition that it should lapse upon the happening of a certain event. In *Financings Ltd v Stimson*,[109] the defendant signed an offer to purchase a car on hire-purchase terms from a finance company, the document having been given to him by a car dealer. The document contained a clause stating that the agreement contained therein would not be binding until it had been accepted on the finance company's behalf. Before the company signed the agreement, the defendant took possession of the car, but later returned it because he was dissatisfied with the car's performance. The car was stolen from the dealer's premises and was eventually recovered in a badly damaged condition. In ignorance of this fact, the finance company then purported to accept the defendant's offer. The company sued the defendant for breach of the hire-purchase agreement. The English Court of Appeal held that the defendant's offer was subjected to an implied condition that the car should continue in the condition it was in when the offer was made and that, on the failure of that condition, the defendant's offer lapsed.

The "implied condition" approach adopted in *Financings Ltd v Stimson* is the traditional method of dealing with cases in which circumstances change between the making and acceptance of an offer but is not the only approach. In *Neilsen v Dysart Timbers Limited*, the Supreme Court of New Zealand explored the different ways of dealing with the problem of changed circumstances.[110] The offer in question was an offer to compromise or settle litigation. Dysart had obtained judgment against the Neilsen brothers for almost $315,000 under a guarantee given by the Neilsens for the debts of their company. The Neilsens disputed liability under the guarantee and applied for leave to appeal the decision against them. Three days after the leave application was heard, the Neilsens offered, through their solicitors, to pay Dysart $250,000 in full satisfaction of the judgment debt. Dysart's solicitors were asked to obtain urgent instructions from their client. Only three hours later, the parties were told by the court registrar that leave to appeal had been granted. There had been real doubt as to whether leave would be granted, and the granting of leave meant that Dysart was now faced with the costs of the appeal and the risk that it would be successful.[111] Dysart accepted the offer 42 minutes after receiving the news, but the Neilsens claimed that the offer was no longer available for acceptance. The New Zealand Supreme Court held (3-2) that the offer remained open for acceptance. The judges were agreed that a fundamental or important change of circumstances had the effect of terminating the offer but did not agree on the conceptual

107 *Carter v Hyde* (1923) 33 CLR 115, 121, 125, 132.

108 *Laybutt v Amoco Australia Pty Ltd* (1974) 132 CLR 57, 76.

109 *Financings Ltd v Stimson* [1962] 1 WLR 1184.

110 *Neilsen v Dysart Timbers Limited* [2009] NZSC 43; [2009] 3 NZLR 160.

111 *Neilsen v Dysart Timbers Limited* [2009] NZSC 43; [2009] 3 NZLR 160, [37] (Tipping and Wilson JJ).

basis for that rule or how it applied to these facts.[112] First, as in *Financings Ltd v Stimson*, a court can ask whether the offer was subject to an implied condition that it would remain open only while a particular factual state of affairs continued. Secondly, the relevant principle can be seen, like the doctrine of frustration, as a rule that an offer will lapse in the event of fundamentally changed circumstances *as a matter of law*, rather than as an implication as to the intentions of the parties.[113] Thirdly, the court can take the broader interpretive approach of asking "whether, having regard to the terms of the offer, the change of circumstances, and the subsequent 'acceptance', viewed as a whole and objectively, there is a concluded agreement".[114] The third approach could be seen as the same as the first, on the basis that "a condition that an offer lapse upon the occurrence of a particular change of circumstances should be implied into the offer only if it is objectively apparent that the willingness of the offeror to be bound by the offer has been fundamentally undermined by the change of circumstances".[115] This is consistent with the view recently expressed by the Privy Council that the implication of a term in an instrument is simply a matter of spelling out "in express words what the instrument, read against the relevant background, would reasonably be understood to mean".[116]

This implication of conditions has an important application to contracts involving more than two parties. Although each case must be decided on its own facts, a written contract signed by one party is often construed as an offer made by that party. That offer may well be subject to an implied condition that the document is ineffective until signed by all the parties to it. In *Neill v Hewens*,[117] only one of two co-vendors signed a contract of sale. The purchasers signed the agreement and later sought specific performance, even though the second vendor had not signed. The High Court held that no contract had been concluded. When one of the co-vendors signed, the presumption was that she did not intend to bind herself unless her co-vendor also signed.[118]

Rejection and counter offer

[3.65] Once an offer has been rejected, it is no longer available for acceptance.[119] A rejected offer may, however, later be revived or may form the basis of an agreement which is inferred in the absence of a valid offer and acceptance.[120] The making of a counter-offer is treated as a rejection of the original offer and will, therefore, also extinguish it.[121] The courts draw a distinction between a counter-offer and an inquiry relating to an alteration of the terms.[122]

112 McLauchlan and Bigwood, "Lapse of Offers Due to Changed Circumstances: A Contract Conversation" (2011) 27 *Journal of Contract Law* 222, 222.

113 *Neilsen v Dysart Timbers Limited* [2009] NZSC 43; [2009] 3 NZLR 160, [54]–[60] (McGrath J); [30]–[32] (Tipping and Wilson JJ).

114 *Neilsen v Dysart Timbers Limited* [2009] NZSC 43; [2009] 3 NZLR 160, [61] (McGrath J).

115 *Neilsen v Dysart Timbers Limited* [2009] NZSC 43; [2009] 3 NZLR 160, [26] (Tipping and Wilson JJ).

116 *Attorney-General of Belize v Belize Telecom Ltd* [2009] UKPC 10; [2009] 1 WLR 1988, [21].

117 *Neill v Hewens* (1953) 89 CLR 1.

118 *Neill v Hewens* (1953) 89 CLR 1, 13. As to deeds, see *Federal Commissioner of Taxation v Taylor* (1929) 42 CLR 81, 87.

119 *Tinn v Hoffman & Co* (1873) 29 LT 271, 278.

120 *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, 179. See [3.145].

121 *Harris v Jenkins* [1922] SASR 59; *Hyde v Wrench* (1840) 3 Beav 334; 49 ER 132.

122 *Stephenson, Jacques & Co v McLean* (1880) 5 QBD 346; *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153.

By requesting information, the offeror is not intending to reject the offer but only to obtain some guidance in deciding whether to accept or reject. In determining whether an agreement has been made, the courts are principally concerned to ascertain the intentions of the parties from the language and circumstances of their communications.[123] The characterisation of conduct as a counter-offer or an inquiry is really stating a conclusion about the manifested intentions of the parties. If a seller offers to sell a tonne of widgets for $1000 to a buyer, the buyer might be said to make a counter-offer if she responds by saying, "I'll give you $900". In applying this label, the court is saying that the buyer has implicitly rejected the seller's offer and the offer should therefore no longer be available for acceptance. The buyer might be said to make an inquiry or request for information if she asks whether there is some room for movement on the price. The label "inquiry" signifies that the buyer has not manifested an intention to reject and so the seller's original offer should be treated as remaining open.

Unilateral contract

[3.70] The revocation of an offer to enter into a unilateral contract raises more difficult questions. There is no difficulty if the offer is withdrawn before the offeree begins to perform. The difficulty arises where the offeree has begun to perform but has not completed the acts that constitute acceptance. If, for example, the offeror offered to pay $100,000 to the first person to swim backstroke across Bass Strait, it might seem unfair if the offer could be revoked when a swimmer was halfway across. It has been held that an offer made in exchange for the doing of an act becomes irrevocable once the act has been partly performed.[124] This principle has been justified on the basis that the offeror is subject to an implied obligation not to revoke the offer after the offeree has started to perform.[125] In a broader sense, it can be justified on the basis that an offeror has power to stipulate the terms on which his or her offer is made and can expressly reserve the right to withdraw the offer. It is more difficult for an offeree to protect himself or herself against the risk of loss once the offeree begins to perform. The notion that there is a general principle preventing revocation of offers in exchange for acts was, however, rejected by the Full Federal Court in *Mobil Oil Australia Ltd v Wellcome International Pty Ltd* (*Mobil v Wellcome*).[126]

Mobil v Wellcome involved an incentive scheme operated by Mobil to improve the performance of franchisees operating Mobil service stations. Mobil told its franchisees that it was seeking to implement a proposal whereby a franchisee who achieved certain performance targets within the "Circle of Excellence" scheme over a period of six years would be granted a nine-year renewal of his or her franchise. Mobil's representative acknowledged that there was a great deal of work to do on the proposal but made a commitment "that we will find a way to extend your tenure automatically no costs to you if you consistently achieve 90% or better in Circle of Excellence judgings".[127]

Several franchisees claimed to have spent time and money improving the operation of their retail operations in order to meet the 90% performance target. After four years, Mobil

123 Greig and Davis, *The Law of Contract* (1987), p 338.

124 *Veivers v Cordingly* [1989] 2 Qd R 278, 297–8.

125 *Daulia Ltd v Four Millbank Nominees Ltd* [1978] Ch 231, 239.

126 *Mobil Oil Australia Ltd v Wellcome International Pty Ltd* (1998) 81 FCR 475.

127 *Mobil Oil Australia Ltd v Wellcome International Pty Ltd* (1998) 81 FCR 475, 498.

unilaterally abandoned the Circle of Excellence scheme by which the franchisees' performance was judged. Wilcox J at first instance held that Mobil had made an offer to enter into a unilateral contract and was not entitled to revoke it once the franchisees had embarked on performance.[128] Since Mobil's abandonment of the scheme prevented the franchisees from completing performance, those franchisees who had achieved the 90% performance target in each year up to the time of revocation should be treated as though they had achieved the same in the remaining years. Those franchisees were, therefore, entitled to performance of the agreement to extend their franchises.

On appeal, the Full Court held that Mobil had not made an offer to the franchisees. There were numerous indications that the scheme was only at a developmental stage and what Mobil said was not in the nature of an offer.[129] The commitment to "find a way" to extend tenure was "simply too vague and uncertain to be capable of giving rise to contractual obligation".[130] Nevertheless, the court went on to address the question whether Mobil had successfully revoked any offer that had been made.

The court held that a person offering to enter into a unilateral contract may, in some circumstances, be prevented from revoking the offer by an implied ancillary contract not to revoke. Revocation in breach of such a contract would be effective, leaving the offeror liable in damages.[131] An estoppel may arise where the offeree has acted to his or her detriment on an assumption that the offer will not be revoked. The Full Court found, however, that there is no universal principle that the offeror may not revoke once the offeree embarks upon performance of the act of acceptance.[132] If there is no implied contract and no estoppel,[133] the offeror is free to revoke the offer. There is no basis for any universal principle, according to the Full Court, because the circumstances vary greatly from one unilateral contract to another. Whether it is unjust for the offeror to revoke the offer once the offeree has commenced performance may depend on whether the offeror knows the offeree has commenced performance, whether the offeree understands that incomplete performance is at his or her risk, whether the parties intended that the offeror should be at liberty to revoke the offer and whether the acts towards performance are detrimental or beneficial to the offeree.[134] In the present case, it was difficult to say when a franchisee should be taken to have "embarked upon" performance; the actions of the franchisees were of benefit to both parties and little or no detriment had been established. There was therefore no basis for an implied contract not to revoke the offer.[135] Accordingly, even if Mobil could be said to have made an offer to the franchisees, Mobil was free to revoke that offer.

The effect of *Mobil v Wellcome* is that, in general, an offer made in return for performance of an act is, like any other offer, revocable at any time. The offeror will only be prevented from revoking the offer where there is an implied contract not to revoke or an estoppel. An estoppel will arise only where the offeree is induced to adopt the assumption that the offer will not be

128 *Lyndel Nominees Pty Ltd v Mobil Oil Australia Ltd* (1997) IPR 599, 636.

129 *Mobil Oil Australia Ltd v Wellcome International Pty Ltd* (1998) 81 FCR 475, 496.

130 *Mobil Oil Australia Ltd v Wellcome International Pty Ltd* (1998) 81 FCR 475, 499–500.

131 *Mobil Oil Australia Ltd v Wellcome International Pty Ltd* (1998) 81 FCR 475, 506.

132 *Mobil Oil Australia Ltd v Wellcome International Pty Ltd* (1998) 81 FCR 475.

133 The estoppel aspects of the decision are discussed [9.50].

134 *Mobil Oil Australia Ltd v Wellcome International Pty Ltd* (1998) 81 FCR 475, 501–2.

135 See [9.50].

revoked and relies on that assumption in such a way that he or she will suffer detriment if the offer is revoked.[136]

ACCEPTANCE

Conduct constituting an acceptance

[3.75] An acceptance is an unqualified assent to the terms of an offer. An important question is whether the acceptance must result in an actual consensus between the parties or a "meeting of the minds". Where A makes an offer to B and B appears to accept, but was seriously mistaken as to what A was offering, is B bound? Whether a real meeting of the minds is required depends in theory on whether one adopts an objective or subjective approach to agreement.[137] Under a subjective approach, no contract is formed unless there was a real consensus between the parties. An objective approach, on the other hand, looks only to the external manifestations of consent, disregarding the offeree's actual state of mind. In *Taylor v Johnson*,[138] the High Court noted that, while there is a significant difference in legal technique between the subjective and objective theories, there is little difference in practice. The reason is that the subjective theory is coupled with a principle of estoppel that operates where a person conducts himself or herself in such a way that a reasonable person would believe that he or she was assenting to the terms of a contract.[139] In those circumstances, the principle of estoppel prevents the person from denying the existence of a contract. Accordingly, an offeree who behaves in such a way that a reasonable person would think he or she was accepting the offer and induces the offeror to contract with him or her on that basis will be bound under both the objective and subjective approaches.

Smith v Hughes[140] provides a useful illustration of this point. A buyer agreed to purchase a quantity of oats on the faith of a sample provided by the seller. The buyer wrongly believed the sample to be old oats, when in fact the sample and the oats supplied were new oats and were unsuitable for the buyer's purposes. Blackburn J held that there is no contract if the parties are not ad idem (of one mind) unless an estoppel prevents one of the parties from denying that he or she has agreed to the other's terms. The relevant principle is:

> If, whatever a man's real intention may be, he so conducts himself that a reasonable man would believe that he was assenting to the terms proposed by the other party, and that other party upon that belief enters into the contract with him, the man thus conducting himself would be equally bound as if he had intended to agree to the other's terms.[141]

On a subjective approach to agreement, therefore, an estoppel prevented the buyer from denying the contract because he had behaved in such a way that a reasonable person would believe he was agreeing to buy new oats. An objective approach would lead to the same result: the court would impute an agreement on the basis that there appeared to be a consensus between the parties. While *Smith v Hughes* supports the application of a subjective

136 See Chapter 9.

137 See further [1.25] and [3.140].

138 *Taylor v Johnson* (1983) 151 CLR 422, 428.

139 *Taylor v Johnson* (1983) 151 CLR 422, 428.

140 *Smith v Hughes* (1871) LR 6 QB 597, 607.

141 *Smith v Hughes* (1871) LR 6 QB 597, 607.

approach coupled with a principle of estoppel, the High Court observed in *Taylor v Johnson* that "the clear trend in the decided cases and academic writings has been to leave the objective theory in command of the field".[142] The High Court has since confirmed that "the principle of objectivity" determines "the rights and liabilities of the parties to a contract": "It is not the subjective beliefs or understandings of the parties about their rights and liabilities that govern their contractual relations. What matters is what each party by words and conduct would have led a reasonable person in the position of the other party to believe".[143] It is clear that the same objective approach governs the question whether two parties have entered into contractual relations.[144]

On that basis, an offeree will effectively accept an offer if the offeree behaves in such a way that a reasonable person would believe he or she is assenting to the terms of an offer, even if there is no real consensus between the parties.[145] There is certainly no need for a consensus as to the terms of a contract.[146] In *Fitness First (Australia) Pty Ltd v Chong*,[147] Ms Chong signed an application form to join a gym on a 12-month membership without first reading the form. She was unaware that it stipulated that she was liable to pay a $200 fee if she cancelled the membership within the first two months. A Tribunal Member held that the parties did not have "the requisite consensus ad idem" required for a valid contract, and therefore Ms Chong was not liable to pay the fee. That decision was overturned on appeal, with Harrison AsJ holding that "the Tribunal Member erred in law when he stated that a valid contract requires that the parties have the [requisite] consensus ad idem in that each fully know and understand the terms of their agreement".[148] By signing the form, Ms Chong had manifested her assent to the printed terms, and it was irrelevant that there was no true consensus ad idem between the parties.

Consciousness of the offer

[3.80] In the case of bilateral contracts formed verbally or in writing, it will usually be clear that the offeree has deliberately accepted the offer. The situation is different with unilateral contracts. If an offeree performs an act requested by an offeror without intending to accept the offer, has a contract been formed? If a person returns a lost dog and subsequently learns of the reward that had been offered by the owner, can the finder of the dog claim the reward? The answer to these questions also depends on a choice between an objective and a subjective approach. In *The Crown v Clarke*,[149] the High Court adopted a subjective approach to this particular question without abandoning the objective approach to formation generally.

142 *Taylor v Johnson* (1983) 151 CLR 422, 429.

143 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [40].

144 See *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, [25], discussed at [5.07].

145 Subject to the principles of mistake, discussed in Chapter 31.

146 See also *Shahid v Australasian College of Dermatologists* [2008] FCAFC 72; (2008) 168 FCR 46, discussed at [5.07] (where, on the basis of an objective approach, the court overturned the decision of a trial judge who had found that "there was no meeting of the minds" in relation to a particular issue).

147 *Fitness First (Australia) Pty Ltd v Chong* [2008] NSWSC 800.

148 *Fitness First (Australia) Pty Ltd v Chong* [2008] NSWSC 800, [22]. Harrison AsJ applied the principle stated in *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, discussed at [12.50].

149 *The Crown v Clarke* (1927) 40 CLR 227.

The court held that while an offeree's conduct is normally assessed by reference to external manifestations, performance of a requested act will not give rise to a unilateral contract if the evidence establishes that the offeree was not in fact acting on the faith of the offer. In other words, a unilateral contract will only arise if the offeree performs the requested acts in reliance on the offer.

The Crown v Clarke was concerned with a £1000 reward offered for information leading to the arrest and conviction of the person who murdered two police officers. Clarke and Treffene were arrested and charged with one of the murders. Clarke gave a statement which led to his own release and the arrest of a man named Coulter, and later gave evidence which led to the conviction of Treffene and Coulter. Clarke claimed the reward, but the Crown refused to pay it to him on the basis that he did not make the statement with a view to claiming the reward. Clarke admitted in evidence that, although he had seen the reward notice, he made the statement in order to clear himself of the charge of murder and not with the intention of claiming the reward. He gave no consideration to the reward until after the men were convicted.

Clarke claimed the Crown was under a contractual obligation to pay him the reward, but he was ultimately unsuccessful in establishing a contract. The High Court held that a unilateral contract will be made only where the acts required for acceptance are performed on the faith of the offer.[150] The court held unanimously that there must be a consensus of minds or wills between the parties before a contract can exist.[151] Isaacs ACJ observed that "acceptance is essential to contractual obligation, because without it there is no agreement, and in the absence of agreement, actual or imputed, there is no contract".[152] Higgins J noted that, without Clarke's admission that he not acted in reliance on the offer, a presumption might have been made that he had acted upon it, but his own evidence rebutted such a presumption.[153] Starke J treated a unilateral contract as an exception to the rule that a person's contractual intentions are normally judged from their outward expressions. The position is different, he said, in a case where communication of acceptance is dispensed with. In such a case, evidence of subjective intention can be taken into account.[154]

By requiring an actual consensus between the parties, and allowing Clarke's actual intentions to override his apparent intentions, the High Court decided the case on the basis of subjective evidence of intention. Had the court taken a purely objective approach, the court would have looked only at the outward manifestations of the parties' intentions and would have imputed an agreement on the basis of Clarke's conduct. The decision in *The Crown v Clarke* shows that the principle of estoppel described in *Smith v Hughes* does not entirely eradicate the practical consequences of the distinction between the objective and subjective approaches to agreement. Although Clarke's conduct would have led a reasonable person to believe he was assenting to the Crown's offer, the principle of estoppel described in *Smith v Hughes* could only be used against Clarke to prevent him from denying the existence of the contract. It could not be used by Clarke to prevent the Crown denying the existence of a contract.

150 *The Crown v Clarke* (1927) 40 CLR 227, 234, 241–2, 244.

151 *The Crown v Clarke* (1927) 40 CLR 227, 234, 239, 243.

152 *The Crown v Clarke* (1927) 40 CLR 227, 233.

153 *The Crown v Clarke* (1927) 40 CLR 227, 241.

154 *The Crown v Clarke* (1927) 40 CLR 227, 244.

Communication of acceptance

The general rule

[3.85] An acceptance generally has effect only when communicated to the offeror.[155] Bowen LJ suggested in *Carlill v Carbolic Smoke Ball Co*[156] that notification of acceptance is required because this establishes that the minds of the two parties have come together and formed a consensus. This rule means that a contract is formed when the offeree's acceptance is received by the offeror. In *Latec Finance Pty Ltd v Knight*,[157] Mr Knight signed a hire-purchase agreement relating to a television set. The document was expressed to operate as an offer by the hirer (Knight), which was irrevocable for a period of seven days and was not binding on the hire-purchase company until signed by the company. The company's acceptance of Knight's offer was noted on the document but was not communicated to Knight. Knight found the set unsatisfactory and returned it to the dealer before any instalments were paid. The company sought to enforce the agreement. The New South Wales Court of Appeal observed that ordinarily, a contract is not made until acceptance of an offer has been communicated.[158] An offeror, however, may expressly or impliedly dispense with the need for actual communication, and will commonly do so in one of two ways. First, the offeror may agree to treat the doing of an act as an effective acceptance. Unilateral contracts are always accepted by the doing of an act and bilateral contracts can also be formed in this way.[159] Secondly, the offeror may treat the despatch of an acceptance by a particular method as effective, whether or not the acceptance is received by the offeror.[160] The company argued that this case fell into the first category, with the act of signing the document to be treated as an effective acceptance. The court held that clear language would be required to support such a construction of the document because, if signing without notification were enough, it would give the company power to "keep the form in their office unsigned, and then play fast and loose as they pleased".[161] The language of the clause did not require this interpretation and, accordingly, there was no contract between the parties.

The postal rule

[3.90] Common law courts have long recognised an exception to the general rule stated above in cases where the acceptance is expected to be sent by post. In such cases, the acceptance is effective as soon as it is posted.[162] In England, this rule has been held to apply where the parties must have contemplated that the acceptance might be sent by post.[163] In *Tallerman & Co Pty Ltd v Nathan's Merchandise (Vic) Pty Ltd*,[164] Dixon CJ and Fullagar J appeared

155 For example, *Latec Finance Ltd v Knight* [1969] 2 NSWR 79; *Batt v Onslow* (1892) 13 LR (NSW) Eq 79.

156 *Carlill v Carbolic Smoke Ball Co* [1893] 1 QB 256.

157 *Latec Finance Ltd v Knight* [1969] 2 NSWR 79.

158 *Latec Finance Ltd v Knight* [1969] 2 NSWR 79, 81.

159 See *The Crown v Clarke* (1927) 40 CLR 227, 233–4; *Brogden v Metropolitan Railway Co* (1877) 2 App Cas 666, 691.

160 See the discussion of the postal rule below.

161 *Latec Finance Ltd v Knight* [1969] 2 NSWR 79, 81, quoting *Robophone Facilities Ltd v Blank* [1966] 1 WLR 1428, 1432.

162 *Adams v Lindsell* (1818) 1 B & A 681; 106 ER 250; *Henthorn v Fraser* [1892] 2 Ch 27.

163 *Henthorn v Fraser* [1892] 2 Ch 27.

164 *Tallerman & Co Pty Ltd v Nathan's Merchandise (Vic) Pty Ltd* (1957) 98 CLR 93.

to take a more restrictive view when they said that "a finding that a contract is completed by the posting of a letter of acceptance cannot be justified unless it is to be inferred that the offeror contemplated and intended that his offer might be accepted by the doing of that act".[165] In *Bressan v Squires*,[166] Bowen CJ in Eq considered whether Dixon CJ and Fullagar J intended to narrow the rule to cases where the offeror appeared to intend that the action of posting should have the consequence of concluding the contract. He concluded that Dixon CJ and Fullagar J must not have intended to narrow the rule because they cited in support of their formulation *Henthorn v Fraser*, a case in which the broader rule was applied.[167] When applying the principle to the facts before them, however, Dixon CJ and Fullagar J said that the necessary inference could not be drawn because solicitors were "conducting a highly contentious correspondence", and so "one would have thought that actual communication would be regarded as essential to the conclusion of agreement on anything".[168] This seemed to be an application of the narrower principle.[169]

Where the postal rule does apply, it has the effect that a contract is made when the acceptance is posted, even if it is received some time later or is lost in the post.[170] It also means that the contract is formed at the place where the acceptance is posted.

Why should posted acceptances be effective on sending, rather than on receipt? One explanation is that one of the parties must bear the risk of the acceptance being lost in the post and the courts have simply created an arbitrary rule to resolve this practical problem.[171] The rule requiring actual communication of an acceptance prejudices the offeree, who has no way of knowing whether the acceptance has reached the offeror and therefore no way of knowing whether a contract has been formed. The postal rule, on the other hand, places the offeror in a difficult position because once the acceptance is posted, the offeror is bound without knowing it. If the letter of acceptance is lost in the post, the offeror may act on the assumption that there is no contract. Since one of the parties must bear the risk, the common law courts have chosen to place the burden on the offeror. French and German law, on the other hand, burden the offeree, rather than the offeror, by unconditionally requiring communication in all cases.[172] The civil law approach has been adopted in the Vienna Convention[173] and the UPICC,[174] both of which provide that an acceptance will be effective only when the "indication of assent reaches the offeror". Greig and Davis suggest that the English courts chose the time of posting on the basis that it is the moment at which "the necessary consensus could be shown to exist".[175]

165 *Tallerman & Co Pty Ltd v Nathan's Merchandise (Vic) Pty Ltd* (1957) 98 CLR 93, 111–12.

166 *Bressan v Squires* [1974] 2 NSWLR 460.

167 *Bressan v Squires* [1974] 2 NSWLR 460, 461–2.

168 *Tallerman & Co Pty Ltd v Nathan's Merchandise (Vic) Pty Ltd* (1957) 98 CLR 93, 111–2.

169 See also *Nunin Holdings Pty Ltd v Tullamarine Estates Pty Ltd* [1994] 1 VR 74; *Wardle v Agricultural and Rural Finance Pty Ltd* [2012] NSWCA 107, [135] and *Sydney Tools Pty Ltd v Robert Bosch (Australia) Pty Ltd* [2017] NSWSC 1709 [41].

170 *Household Fire and Carriage Accident Insurance Co Ltd v Grant* (1879) LR 4 Ex D 216.

171 Peel, *Treitel's Law of Contract* (14th ed, 2015), [2-031]; Atiyah, *An Introduction to the Law of Contract* (5th ed, 1995), p 71.

172 Wheeler and Shaw, *Contract Law* (1994), p 217. See also Zweigert and Kötz, *Introduction to Comparative Law* (3rd ed, 1998), pp 356–64.

173 *United Nations Convention on International Contracts for the Sale of Goods* (1980), art 18.

174 *UNIDROIT Principles of International Commercial Contracts 2016*, art 2.1.6(2).

175 Greig and Davis, *The Law of Contract* (1987), pp 310, 314.

The rule was explained in some of the early cases on the basis that the post office is the agent of both parties and therefore receives the letter of acceptance as agent of the offeror,[176] but it has since been held that the post office is not the agent of either party.[177] More elaborate justifications for the postal rule have also been offered,[178] but no explanation is universally accepted.

Scope of the postal rule

[3.95] With the advent of electronic communications, it might have been thought that the postal rule would become an anachronism, which would have little application to modern methods of contracting. The postal rule has not, however, been confined to the post. The courts extended the postal rule to telegrams, on the basis that telegrams were given to the post office and delivered to the recipient in essentially the same way as posted letters.[179] The courts then sought to confine the postal rule, distinguishing forms of instantaneous communication. In *Entores v Miles Far Eastern Corp*,[180] the English Court of Appeal held that the postal rule should not apply to instantaneous forms of communication, such as the telephone or telex. This decision has been followed by Australian courts in relation to telephone[181] and telex communications[182] and by the House of Lords in *Brinkibon Ltd v Stahag Stahl und Stahlwarenhandelsgesellschaft mbH* (*Brinkibon*)[183] in relation to telex.

Brinkibon was concerned with a contract, made between an English buyer and an Austrian seller, for the sale of steel bars. The buyer sought to enforce the contract in the English courts and sought leave to serve a writ outside the jurisdiction. Under the Rules of the Supreme Court, leave could be granted where the litigation concerned a contract made within the jurisdiction. The contract was made by an exchange of telex messages between the buyers in London and the sellers in Vienna. After lengthy negotiations by telephone and telex, the buyers sent a telex to Vienna accepting the terms of sale offered by the sellers.

The House of Lords held that the contract was made in Vienna, where the acceptance was received. Lord Wilberforce said the general rule is that a contract is formed when acceptance is communicated to the offeror. It therefore "appears logical" that a contract should also be formed *where* acceptance is communicated to the offeror.[184] Where the postal rule applies, the acceptance is effective when and where it is placed in the hands of the post office. In the case of instantaneous communication, including telex, the general rule will usually apply. The situation may be different, according to Lord Wilberforce, where the message is sent or received through a third party, where it is sent out of office hours or is not intended to be read

176 See *Household Fire and Carriage Accident Insurance Co Ltd v Grant* (1879) LR 4 Ex D 216, 221.

177 *Henthorn v Fraser* [1892] 2 Ch 27, 33, 35–6.

178 See, eg, Evans, "The Anglo-American Mailing Rule: Some Problems of Offer and Acceptance in Contracts by Correspondence" (1966) 15 *International and Comparative Law Quarterly* 553; Gardner, "Trashing with Trollope: A Deconstruction of the Postal Rules" (1992) 12 *Oxford Journal of Legal Studies* 170.

179 *Cowan v O'Connor* (1888) 20 QBD 640; *Bruner v Moore* [1904] 1 Ch 305. See also *Leach Nominees Pty Ltd v Walter Wright Pty Ltd* [1986] WAR 244.

180 *Entores v Miles Far Eastern Corp* [1955] QB 327.

181 *Aviet v Smith and Searls Pty Ltd* (1956) 73 WN (NSW) 274; *Dewhurst (WA) and Co Pty Ltd v Cawrse* [1960] VR 278, 282; *Hampstead Meats Pty Ltd v Emerson and Yates Pty Ltd* [1967] SASR 109.

182 *Express Airways v Port Augusta Air Services* [1980] Qd R 543.

183 *Brinkibon Ltd v Stahag Stahl und Stahlwarenhandelsgesellschaft mbH* [1983] 2 AC 34.

184 *Brinkibon Ltd v Stahag Stahl und Stahlwarenhandelsgesellschaft mbH* [1983] 2 AC 34, 41.

immediately. "No universal rule can cover all such cases; they must be resolved by reference to the intentions of the parties, by sound business practice and in some cases by a judgment where the risks should lie."[185]

Lord Fraser noted that a telex sent to a large firm is not really instantaneous, since it must pass from the telex operator to the responsible person in the firm.[186] It is, however, convenient to treat it as a form of instantaneous communication for three reasons.[187] First, no difficulty or complaint has arisen from the decision in *Entores v Miles Far Eastern Corp*. Secondly, it is the responsibility of the recipient to arrange for the prompt handling of messages within his or her office. Thirdly, the sender is more likely to be aware that an attempt to send a message has been unsuccessful than the recipient is to be aware that an unsuccessful attempt has been made. Lord Brandon also thought that commercial expediency justified the postal rule, but did not justify extending it to forms of instantaneous communication such as telephone or telex.[188]

The real issue faced by the House of Lords in *Brinkibon* was whether or not an English company could sue an Austrian supplier in an English court. In order to resolve this question, the Rules of the Supreme Court required the House of Lords to decide whether the contract had been made in England. As John Wightman has observed, it is unfortunate that the technical rules of offer and acceptance are employed in cases such as *Brinkibon* to resolve jurisdictional questions.[189] This approach is also routinely followed in Australia.[190] The law of contract is not well equipped to determine where a contract has been made, since the place of formation is not relevant to the general law of contract, but only to jurisdictional questions.[191] By resolving these cases by reference to technical rules of formation, the courts cannot explicitly take account of the policy considerations relevant to the underlying issue, which involve the relative convenience and expense of the case being heard in each of the two jurisdictions. The effect of applying the technical rules of contract formation to the place of formation issue will often lead to an arbitrary result, as it did in *Brinkibon*. The contract in *Brikinbon* was concluded after lengthy communications between the two countries and it just happened that the last communication was received in Vienna. The House of Lords resolved the case by applying a technical "general rule", but left the way open for future cases to be decided differently by observing that "no universal rule can cover all such cases".[192]

Modern electronic communications

[3.100] The case law relating to communication of acceptance has inevitably lagged behind developments in communication systems.[193] Telegrams and telexes were superseded by facsimile messages, and there are now many different forms of electronic data exchange which may be used in the formation of contracts. In *Reese Bros Plastics Ltd*

185 *Brinkibon Ltd v Stahag Stahl und Stahlwarenhandelsgesellschaft mbH* [1983] 2 AC 34, 42.
186 *Brinkibon Ltd v Stahag Stahl und Stahlwarenhandelsgesellschaft mbH* [1983] 2 AC 34, 43.
187 *Brinkibon Ltd v Stahag Stahl und Stahlwarenhandelsgesellschaft mbH* [1983] 2 AC 34, 43.
188 *Brinkibon Ltd v Stahag Stahl und Stahlwarenhandelsgesellschaft mbH* [1983] 2 AC 34, 48.
189 Wightman, "Does Acceptance Matter?" in Adams (ed), *Essays for Clive Schmitthoff* (1983).
190 See, eg, *Tallerman & Co Pty Ltd v Nathan's Merchandise (Vic) Pty Ltd* (1957) 98 CLR 93.
191 Wightman, "Does Acceptance Matter?" in Adams (ed), *Essays for Clive Schmitthoff* (1983), p 145.
192 *Brinkibon Ltd v Stahag Stahl und Stahlwarenhandelsgesellschaft mbH* [1983] 2 AC 34, 42.
193 See generally Furmston and Tolhurst, *Contract Formation: Law and Practice* (2nd ed, 2016), ch 6.

v Hamon-Sobelco Australia Pty Ltd,[194] the New South Wales Court of Appeal held that a facsimile message, which is sent through telephone lines from one machine to another, should be treated as a form of instantaneous communication. Acceptances sent by facsimile are therefore governed by the general rule that an acceptance is effective only when received by the offeror. This general principle may be subject to exceptions in the circumstances discussed by Lord Wilberforce in *Brinkibon*. That is, a different principle may apply where the message is sent or received through a third party, is sent out of office hours or is not intended to be read immediately. Lord Wilberforce did not indicate what rule might apply in these situations. It could be that the postal rule should apply where an acceptance is sent or received through a third party. When a message is sent out of office hours or is not intended to be read immediately, it may be that it becomes effective some time after it is received by the offeror's machine. All such cases are likely to be resolved by reference to the presumed intention of the offeror.

The question of whether the postal rule should apply to communication over the Internet has not been authoritatively determined, although it has been suggested by way of obiter dictum that email should be treated like other forms of instantaneous communication.[195] The two forms of Internet communication most likely to be used in contracting are interactive websites and email. Communication via interactive websites is virtually instantaneous, and there seems little reason to depart from the general rule that acceptance is effective only when received. Email, on the other hand, is in some ways analogous to post, as Squires explains.[196] Once a message is sent, the sender loses control of the message as it passes through the hands of intermediaries. As a result of technical problems that may be the fault of third parties, an email message may be delayed or may never reach the addressee. A delay in transmission may also be caused by an addressee's failure to retrieve the message from an external server.

None of these features provides a compelling reason to extend the postal rule to email messages, as Squires explains.[197] Email is far quicker than the post and could fairly be described as virtually instantaneous. Although email messages pass through the hands of third parties, so too do telephone, facsimile and telex messages. Delays caused by the addressee's own failure to collect messages from a server are dealt with in legislative provisions discussed below governing the time of receipt. As with telex and facsimile messages, a person attempting to send an email is far more likely to be aware that the attempt has been unsuccessful than an intended recipient is to be aware of the fact that an attempt has been made.[198] Even if email were considered to be analogous to post, the postal rule would only apply if it were thought to have been within the contemplation of the parties that an acceptance sent by email should be effective on sending. It therefore seems likely that the general rule would be applied to electronic communication and that acceptances sent electronically would, at common law, be effective only when received by the offeror.[199]

194 *Reese Bros Plastics Ltd v Hamon-Sobelco Australia Pty Ltd* (1988) 5 BPR 11, 106.

195 *Olivaylle Pty Ltd v Flottweg AG* (No 4) [2009] FCA 522; (2009) 255 ALR 632, [25].

196 Squires, "Some Contract Issues Arising from Online Business – Consumer Agreements" (2000) 5 *Deakin Law Review* 95, 107.

197 Squires, "Some Contract Issues Arising from Online Business – Consumer Agreements" (2000) 5 *Deakin Law Review* 95, 107–10. See also Nolan, "Offer and Acceptance in the Electronic Age" in Burrows and Peel (eds), *Contract Formation and Parties* (2010), pp 61, 64–70.

198 See *Brinkibon Ltd v Stahag Stahl und Stahlwarenhandelsgesellschaft mbH* [1983] 2 AC 34, 43.

199 As indicated in *Olivaylle Pty Ltd v Flottweg AG* (No 4) [2009] FCA 522; (2009) 255 ALR 632, [25].

The Electronic Transactions Acts (ETAs) in force in all Australian jurisdictions include provisions governing "the time of dispatch" "the time of receipt" of an electronic communication "for the purposes of a law of this jurisdiction". It is not clear whether these provisions are intended to affect the law on contract formation. As Mik notes, the critical issue for contract formation is when an acceptance *becomes effective*, not when it is dispatched or received.[200] The difficulty is exacerbated by the fact that in each jurisdiction, the Part of the ETA dealing with the use of automated message systems (numbered Part 2A, except in Qld and WA) is expressed to apply to the formation of contracts,[201] while the Part dealing with the time of dispatch and receipt of electronic communications (numbered Part 2, except in Qld and WA) is not. In his new contract text, former High Court Justice Dyson Heydon assumes that the ETA provisions governing the time of receipt do apply to contract formation and thus govern the time at which an acceptance becomes effective.[202]

For the purpose of determining the time of receipt of an electronic communication, the ETAs distinguish between situations in which an electronic information system has been designated for the purpose of receiving communications and situations in which it has not. Where an electronic communication is sent to an address designated by the addressee, the time of receipt is the time that it "becomes capable of being retrieved by the addressee" at that designated address.[203] In the case of a communication sent to an address which has not been designated by the addressee, the communication is only effective once both (i) the communication "has become capable of being retrieved by the addressee" and (ii) "the addressee has become aware that the electronic communication has been sent to that address".[204] It is assumed that the communication "is capable of being retrieved by the addressee when it reaches the addressee's electronic address".[205] These provisions are subject to any agreement to the contrary. The notes to the UNCITRAL model law indicate that an information system should only be regarded as having been "designated" if it has been expressly specified for a particular purpose, such as the acceptance of an offer. The listing of an email address or facsimile number on a letterhead or

200 Mik, "The Effectiveness of Acceptances Communicated by Electronic Means, or Does the Postal Acceptance Rule Apply to Email?" (2009) 26 Journal of Contract Law 68, 72.

201 *Electronic Transactions Act 2001* (ACT), s 14A(1); *Electronic Transactions Act 1999* (Cth), s 15A(1); *Electronic Transactions Act 2000* (NSW), s 14A; *Electronic Transactions (Northern Territory) Act*, s 14A; *Electronic Communications Act 2000* (SA), s 13A; *Electronic Transactions Act 2000* (Tas), s 12A; *Electronic Transactions (Victoria) Act 2000*, s 14A; *Electronic Transactions (Queensland) Act 2001*, s 26A; *Electronic Transactions Act 2011* (WA), s 17.

202 Heydon, *Heydon on Contracts* (2019), [2.640].

203 *Electronic Transactions Act 2001* (ACT), s 13A(1); *Electronic Transactions Act 1999* (Cth), s 14A(1); *Electronic Transactions Act 2000* (NSW), s 13A(1); *Electronic Transactions (Northern Territory) Act*, s 13A(1); *Electronic Communications Act 2000* (SA), s 13A(1); *Electronic Transactions Act 2000* (Tas), s 11A(1); *Electronic Transactions (Victoria) Act 2000*, s 13A; *Electronic Transactions (Queensland) Act 2001*, s 24(1); *Electronic Transactions Act 2011* (WA), s 14(1).

204 *Electronic Transactions Act 2001* (ACT), s 13A(1); *Electronic Transactions Act 1999* (Cth), s 14A(1); *Electronic Transactions Act 2000* (NSW), s 13A(1); *Electronic Transactions (Northern Territory) Act*, s 13A(1); *Electronic Communications Act 2000* (SA), s 13A(1); *Electronic Transactions Act 2000* (Tas), s 11A(1); *Electronic Transactions (Victoria) Act 2000*, s 13A(1); *Electronic Transactions (Queensland) Act 2001*, s 24(1); *Electronic Transactions Act 2011* (WA), s 14(1).

205 *Electronic Transactions Act 2001* (ACT), s 13A(2); *Electronic Transactions Act 1999* (Cth), s 14A(2); *Electronic Transactions Act 2000* (NSW), s 13A(2); *Electronic Transactions (Northern Territory) Act*, s 13A(2); *Electronic Communications Act 2000* (SA), s 13A(2); *Electronic Transactions Act 2000* (Tas), s 11A(2); *Electronic Transactions (Victoria) Act 2000*, s 13A(2); *Electronic Transactions (Queensland) Act 2001*, s 24(2); *Electronic Transactions Act 2011* (WA), s 14(2).

similar document does not amount to a designation.[206] The effect of the ETA provisions would appear to be that an electronic message sent over the Internet to a designated address would be effective once it is received by the server operated by the recipient or a commercial server used by the recipient. The definition of "electronic communication" would also appear to cover facsimile messages,[207] which means that an acceptance sent by facsimile to a designated number would be effective once it was received by the recipient's facsimile machine.

Method of acceptance

[3.105] If an offer prescribes an exclusive method for the communication of acceptance, then only an acceptance communicated by that method will be effective.[208] An offer may, for example, say: "This offer can be accepted only by written notice posted to the following address." An offeror may also expressly or impliedly dispense with the need for communication. In the case of a unilateral contract, for example, it is the doing of the stipulated act that constitutes acceptance of the offer and the offeror implicitly dispenses with communication of acceptance.[209]

Silence as acceptance

[3.110] A contract cannot, however, be forced on the offeree by stipulating silence as the prescribed method of acceptance. In *Felthouse v Bindley*,[210] a man wrote to his nephew offering to buy a horse and said: "If I hear no more about him, I consider the horse mine at £30 15s." The nephew intended to accept the uncle's offer and instructed his auctioneer that the horse was already sold and should not be auctioned with his other stock. The auctioneer sold the horse at auction by mistake and the uncle sued the auctioneer in tort for conversion. The action was unsuccessful. No contract between uncle and nephew had been formed because the nephew had not communicated his acceptance.[211] The uncle was therefore held to have had no property in the horse at the time of the auction and no cause of action against the auctioneer. Greig and Davis have questioned this decision on the basis that the nephew had manifested his acceptance of the uncle's offer by instructing the auctioneer not to sell the horse, and the uncle had dispensed with the need for communication of acceptance. On this basis, they suggest, an action would surely have been sustainable against the uncle if he had refused to take the horse.[212]

Acceptance inferred from conduct

[3.115] In some cases, the courts will accept that an agreement has been formed even though the offeree has not effectively communicated his or her acceptance to the offeror. In *Farmers'*

206 *Guide to Enactment of the UNCITRAL Model Law on Electronic Commerce* (1996), [102], http://www.uncitral.org.

207 *Electronic Transactions Act 2001* (ACT), s 5; *Electronic Transactions Act 1999* (Cth), s 5(1); *Electronic Transactions Act 2000* (NSW), s 5(1); *Electronic Transactions (Northern Territory) Act*, s 5; *Electronic Transactions (Queensland) Act 2001*, s 6 and Sch 2; *Electronic Communications Act 2000* (SA), s 5(1); *Electronic Transactions Act 2000* (Tas), s 3; *Electronic Transactions (Victoria) Act 2000*, s 3(1); *Electronic Transactions Act 2011* (WA), s 5(1).

208 See *George Hudson Holdings Ltd v Rudder* (1973) 128 CLR 387.

209 *Carlill v Carbolic Smoke Ball Co* [1893] 1 QB 256, 269–70.

210 *Felthouse v Bindley* (1862) 11 CB (NS) 869; 142 ER 1037.

211 *Felthouse v Bindley* (1862) 142 ER 1037, 1040.

212 Greig and Davis, *The Law of Contract* (1987), p 302.

Mercantile Union and Chaff Mills Ltd v Coade,[213] the respondents applied in 1913 to buy a £25 share in the appellant company. The company did not communicate its acceptance of the offer within a reasonable time but retained the £1 paid by the respondents and entered their names on the register. The company intimated its acceptance only after a reasonable time had expired, by making calls for payment of further instalments of £5 in 1916 and 1918. The respondents ignored these calls.

Knox CJ held that an agreement to buy the share could be inferred from the respondents' inaction once they became aware that their names were on the register of shareholders.[214] Higgins J held that, although the respondents would have been entitled to reject the shares when the belated notice of acceptance was received, an agreement to take the shares must be inferred from their failure to respond.[215] An offeror in this situation is required to make a prompt choice between condoning the delay and rejecting the contract.[216] Starke J dissented on the basis that the respondents' silence could equally be regarded as a refusal to have anything to do with the company since its offer had lapsed and the matter was at an end.[217] It was for the company to establish the existence of a contract and it had failed to do this.

Acceptance by conduct also occurred in *Empirnall Holdings Pty Ltd v Machon Paull Partners Pty Ltd*.[218] Empirnall, a property developer, verbally engaged architects Machon Paull to act as project managers for a particular development. After some work was done, the architects requested a progress payment and the execution of a contract. They were told to submit the progress payment claim but that Eric Jury, a director and the major shareholder of Empirnall, "does not sign contracts". The architects nevertheless sent two copies of a contract to Empirnall and asked that one copy be signed and returned. Two weeks later, the architects wrote a letter to Empirnall that said "we are proceeding on the understanding that the conditions of the contract are accepted by you and works are being conducted in accordance with those terms and conditions". The architects continued to work and receive progress payments, but the contract was never signed. When Empirnall became insolvent, it became necessary to determine the effectiveness of a clause of the unsigned contract charging the architects' fees on the land being developed.

The New South Wales Court of Appeal accepted the principle from *Felthouse v Bindley* that an offeror cannot set up a contract by stipulating silence as the mode of acceptance.[219] Silence may, however, indicate acceptance in some circumstances. The objective theory of contract requires an objective manifestation of assent to an offer.[220] The ultimate issue, therefore, is whether a reasonable bystander would regard the offeree's conduct, including the offeree's silence, as signaling acceptance of the offer.[221] In this case, Empirnall did more than remain silent. It took the benefit of the services provided by the architects, knowing they were to

213 *Farmers' Mercantile Union and Chaff Mills Ltd v Coade* (1921) 30 CLR 113.

214 *Farmers' Mercantile Union and Chaff Mills Ltd v Coade* (1921) 30 CLR 113, 120.

215 *Farmers' Mercantile Union and Chaff Mills Ltd v Coade* (1921) 30 CLR 113, 125.

216 *Farmers' Mercantile Union and Chaff Mills Ltd v Coade* (1921) 30 CLR 113, 124.

217 *Farmers' Mercantile Union and Chaff Mills Ltd v Coade* (1921) 30 CLR 113, 131.

218 *Empirnall Holdings Pty Ltd v Machon Paull Partners Pty Ltd* (1988) 14 NSWLR 523, following *Brogden v Metropolitan Railway Co* (1877) 2 App Cas 666.

219 *Empirnall Holdings Pty Ltd v Machon Paull Partners Pty Ltd* (1988) 14 NSWLR 523, 527, 534.

220 *Empirnall Holdings Pty Ltd v Machon Paull Partners Pty Ltd* (1988) 14 NSWLR 523, 534.

221 *Empirnall Holdings Pty Ltd v Machon Paull Partners Pty Ltd* (1988) 14 NSWLR 523, 535.

be paid for in accordance with the offer and having had a reasonable opportunity to reject the offer. In those circumstances, an objective bystander would conclude that Empirnall had accepted the offer on the terms proposed. McHugh JA adopted a principle of law applied in the United States but restated it as a question of fact:

> Where an offeree with a reasonable opportunity to reject the offer of goods or services takes the benefit of them under circumstances which indicate that they were to be paid for in accordance with the offer, it is open to the tribunal of fact to hold that the offer was accepted according to its terms.[222]

Correspondence between offer and acceptance

[3.120] It is often said that an acceptance must correspond precisely with the offer. This means that the offer empowers the offeree to do no more than accept or reject the terms proposed by the offeror. If the offeree attempts to vary the terms proposed, or to add additional terms, then the purported acceptance will amount to a counter-offer, which will give rise to a contract only if it is accepted by the original offeror.[223] A particular problem arises where both parties use standard form contracts. The problem arises where two parties, such as a buyer and seller of goods, exchange inconsistent standard forms during contract negotiations and reach agreement on the principal terms without deciding whose standard form should prevail. This situation is known as the "battle of the forms".

The English approach

[3.125] The English courts have resolved the battle of the forms problem by applying the classical principles of offer and acceptance. On this approach, the sending of the last form will usually be regarded as a counter-offer, and so the "last shot" will prevail, provided the recipient of the counter-offer can be taken to have accepted the terms proposed by the other sender. *Butler Machine Tool Co Ltd v Ex-Cell-O-Corp (England) Ltd*[224] exemplifies this approach. The seller of a machine provided a price quotation on certain terms and conditions. The seller's form stipulated that orders would only be accepted subject to the terms and conditions set out in the quotation. The buyer then requested supply on its own terms and conditions, which differed in several important respects from the seller's. Attached to the buyer's form was a tear-off "acknowledgement of order" form, by which the sellers agreed to supply on the buyer's terms and conditions. The seller signed this and returned it to the buyer with a letter stipulating that the machine would be supplied in accordance with the seller's quotation. The issue was whether the seller was entitled to the benefit of a price variation provided for in the terms set out on the back of the seller's original quotation. This clause allowed the seller to increase the price of the machine where the seller's costs increased during the period of manufacture.

The trial judge found decisive the seller's stipulation that its conditions should prevail. The English Court of Appeal unanimously found for the buyer. Lawton and Bridge LJJ both

222 *Empirnall Holdings Pty Ltd v Machon Paull Partners Pty Ltd* (1988) 14 NSWLR 523, 535, citing *Laurel Race Course Inc v Regal Construction Co Inc*, 333 A 2d 319 (1975).

223 *Hyde v Wrench* (1840) 3 Beav 334; 49 ER 132; *Cullen v Bickers* (1878) 12 SALR 5. See [3.65].

224 *Butler Machine Tool Co Ltd v Ex-Cell-O-Corp (England) Ltd* [1979] 1 WLR 401. See also *British Road Services Ltd v Arthur V Crutchley & Co Ltd* [1968] 1 Lloyd's Rep 271, 281–2.

applied the traditional analysis and found that the seller's quotation constituted an offer and the buyer's order a counter-offer. The effect of the counter-offer was to "kill the original offer",[225] including the stipulation that the seller's terms prevailed. The seller accepted this counter-offer by signing and returning the tear-off slip to the buyer. The reference in the seller's letter to the original quotation was taken to refer only to the price and identity of the machine and not to the terms on the back of the quotation. Lawton LJ observed that if the seller's letter had amounted to a further counter-offer, then it could not have been said that the parties were ad idem. There would then have been no contract between the parties.

Lord Denning MR preferred to look at all of the documents passing between the parties as a whole and ascertain the terms from them. In some cases, he suggested, the terms of both parties should be construed together. If they are contradictory, "then the conflicting terms may have to be scrapped and replaced by a reasonable implication".[226] In the present case, Lord Denning found that, "as a matter of construction", the seller's acknowledgment of the buyer's order was the decisive document, since it made clear that the contract was on the buyer's terms and not the seller's.[227]

Conflict and synthesis

[3.130] The judgments in *Butler* suggest two different methods of resolving the battle of the forms: the conflict approach and the synthesis approach.[228] The conflict approach treats the exchange of terms as a battle and requires the court to determine which set of terms has prevailed. The battle will be won either by the party who fires the last shot or by the party who is most persistent in insisting that their own set of terms should prevail. The synthesis approach would require the court to build a contract from the two sets of terms. The synthesised contract would be made up of consistent terms, along with terms from one set that appeared to be accepted by the other party. Any gaps in the synthesised contract could be filled with terms implied by the court. Although Lord Denning suggested in *Butler* that the synthesis approach should be a last resort, relational analysis suggests that it should in fact provide the starting point.[229] The classical approach assumes that a set of terms is either accepted or not, and so the transaction is either on or off. This is well suited to discrete transactions but fails to allow for any complexity that may exist in the relationship between the parties.[230] Parties exchanging standard forms may implicitly be rejecting the rule requiring precise correspondence between offer and acceptance. In the business world, a party commonly will neither entirely reject nor entirely accept the terms proposed by the other party, but will be more receptive to some terms than others.[231] The synthesis approach allows the court to take account of a party's willingness to accept some terms but not others. It acknowledges that parties to a transaction often focus on, and reach agreement on, the broader issues of the "deal", without ever concerning themselves with the details of the contract.

225 *Butler Machine Tool Co Ltd v Ex-Cell-O-Corp (England) Ltd* [1979] 1 WLR 401, 406, 407.

226 *Butler Machine Tool Co Ltd v Ex-Cell-O-Corp (England) Ltd* [1979] 1 WLR 401, 405.

227 *Butler Machine Tool Co Ltd v Ex-Cell-O-Corp (England) Ltd* [1979] 1 WLR 401, 405.

228 Greig and Davis, *The Law of Contract* (1987), pp 283–92.

229 Greig and Davis, *The Law of Contract* (1987), p 288.

230 See Macneil, *The New Social Contract* (1980), pp 72–3.

231 Macneil, *The New Social Contract* (1980), p 73.

Legislative solutions

[3.135] In the United States, art 2-207 of the *Uniform Commercial Code* (US) (UCC) attempts to address the battle of the forms problem by creating an exception to the rule that acceptance must correspond precisely with the term of the offer. Article 2-207 provides that an acceptance that states additional or different terms will still be an effective acceptance. The additional terms are to be construed as proposals for additions to the contract. As between merchants, the terms become part of the contract unless the terms materially alter the offer, the offer expressly precludes the adding of terms or the offeror objects to the additional terms within a reasonable time. These provisions provide a starting point for a relational analysis because they allow a contract to be formed where a party accepts some terms but rejects others.[232]

Article 2-207(3) provides that a contract will be established where the parties by their conduct recognise the existence of a contract even though the writings of the parties do not establish a contract. The terms of the contract consist of the express terms on which the writings of the parties agree and the terms implied by the UCC. Subsection (3) ensures that a contract will be formed where the parties have agreed on the principal terms and have begun performance. As suggested by Lord Denning in *Butler*, inconsistent terms are simply dispensed with. Subsection (3) provides "a relational base on which to rely when mutual consent fails" but comes into play only when the parties have begun to perform.[233] Article 2.1.22 of the UPICC adopts a similar approach to art 2-207(3) of the UCC, without the requirement that performance has commenced, subject to one of the parties indicating either in advance or without undue delay afterwards that it does not intend to be bound by such a contract.[234]

Both the Vienna Convention[235] and the UPICC[236] allow an acceptance to include non-material modifications. Both art 19 of the Vienna Convention and art 2.1.11 of the UPICC provide that an acceptance with additional conditions is regarded as a counter-offer unless the additional terms do not materially alter the terms of the offer. Where the additions or alterations are non-material, the acceptance will be effective and the additional terms incorporated, provided the offeror does not object.

A MEETING OF THE MINDS

[3.140] Underlying many of the cases on offer and acceptance is the idea that a contract is formed only when there is a meeting of minds or a consensus ad idem between the parties. The requirement of a consensus was strongly emphasised in some of the older cases. In *Dickinson v Dodds*,[237] for example, James LJ suggested that the "existence of the same mind between the two parties … is essential in point of law to the making of [an] agreement". Whether an actual consensus, or just an appearance of consensus, is required may be said to turn on whether one adopts a subjective or objective approach to formation. It might be

232 Greig and Davis, *The Law of Contract* (1987), p 288.

233 Greig and Davis, *The Law of Contract* (1987), p 74.

234 *UNIDROIT Principles of International Commercial Contracts 2016*, art 2.1.22.

235 *United Nations Convention on International Contracts for the Sale of Goods* (1980), art 19.

236 *UNIDROIT Principles of International Commercial Contracts 2016*, art 2.1.11.

237 *Dickinson v Dodds* (1876) LR 2 Ch D 463, 473.

said that a subjective approach requires an actual consensus, whereas an objective approach looks only to the outward manifestations of the parties' intentions, so the appearance of a consensus is sufficient, even if the parties do not actually agree. As discussed at [3.75], however, the subjective approach is for practical purposes almost indistinguishable from the objective approach, because of the principle of contract by estoppel. Under either a subjective or objective approach, a person who behaves as if accepting an offer will be bound, even if there was no actual consensus.

While it might be superficially attractive to do so, it is not possible to draw a clear distinction between the subjective and objective approaches.[238] The subjective approach ultimately turns on objective criteria. In *Smith v Hughes*, the rule requiring subjective intent was met by a counter-rule imposing contractual liability where there was a false appearance of consent.[239] The court maintained that a consensus was required to form a contract but accepted that a party who appeared to consent would be estopped from denying the existence of a contract, with the same result if an actual contract had been formed. In *The Crown v Clarke*, Starke J confirmed that the law ordinarily adopts an objective approach to agreement but allowed a party's undisclosed intentions to be determinative in the "anomalous case under consideration".[240] Under the *Smith v Hughes* principle, the objective appearance of consent trumps the party's actual intentions, whereas in *The Crown v Clarke*, the party's actual intentions trumped the objective appearance of consent.

As Clare Dalton explains, the courts have tended toward objective standards for interpreting conduct in the modern cases for pragmatic reasons.[241] Assertions of private intention are unreliable and courts simply do not have access to a party's true intentions. It is not possible to escape subjective considerations, however, because subjective will is still seen as the source of contractual obligation.[242]

If the objective theory is in fact in command of the field,[243] and contractual obligation is based on objective criteria, then contract can be seen as an obligation that attaches by force of law to certain actions of the parties which normally, but may not necessarily, accompany and represent intent.[244] Contract cannot then be seen as a system of private or voluntarily assumed obligations.[245] It must be seen, like the law of tort, as a system of public obligation, in which liability is imposed on the basis of norms of reasonable behaviour. There is a fundamental inconsistency between, on the one hand, the courts' adoption of objective formation criteria and, on the other hand, the rationalisation of particular doctrines and particular decisions on the basis of whether there was or was not a consensus. Dalton argues that if contract is

238 Dalton, "An Essay in the Deconstruction of Contract Doctrine" (1985) 94 *Yale Law Journal* 997, 1039–45.

239 See [3.75].

240 *The Crown v Clarke* (1927) 40 CLR 227, 244. See [3.80].

241 Dalton, "An Essay in the Deconstruction of Contract Doctrine" (1985) 94 *Yale Law Journal* 997, 1040.

242 Dalton, "An Essay in the Deconstruction of Contract Doctrine" (1985) 94 *Yale Law Journal* 997, 1042.

243 As suggested in *Taylor v Johnson* (1983) 151 CLR 422, 429, confirmed in cases such as *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 105–10 and *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, 179, and evidenced by decisions such as *Fitness First (Australia) Pty Ltd v Chong* [2008] NSWSC 800, discussed at [3.75] and *Shahid v Australasian College of Dermatologists* [2008] FCAFC 72; (2008) 168 FCR 46, discussed at [5.07].

244 *Hotchkiss v National City Bank*, 200 F 287, 293 (1911). See Dalton, "An Essay in the Deconstruction of Contract Doctrine" (1985) 94 *Yale Law Journal* 997, 1043.

245 As it was in *Astley v Austrust Ltd* (1999) 197 CLR 1, 36.

a system of public obligation, then the courts should articulate the public concerns being addressed by the law of contract and the public values informing its operation.[246]

AGREEMENT WITHOUT OFFER AND ACCEPTANCE

[3.145] As noted at the beginning of this chapter, the identification of an offer and an acceptance remains the conventional approach to establishing the agreement element of contract formation. It has, however, been accepted in a number of cases that a contract can be established without an identifiable offer and acceptance. The Australian courts have followed their counterparts in the United States in accepting that "a manifestation of mutual assent may be made even though neither offer nor acceptance can be identified and even though the moment of formation cannot be determined".[247] In other words, "parties may drift into a contractual relationship".[248]

In *Branir Pty Ltd v Owston Nominees (No 2) Pty Ltd*, Allsop J said that "Sometimes … having discussed the commercial essentials and having put in place necessary structural matters, the parties go about their commercial business on the clear basis of some manifested mutual assent, without ensuring the exhaustive completeness of documentation".[249] In that case, the Full Court of the Federal Court applied the following principle:

> The essential question in such cases is whether the parties' conduct, including what was said and not said and including the evident commercial aims and expectations of the parties, reveals an understanding or agreement or, as sometimes expressed, a manifestation of mutual assent, which bespeaks an intention to be legally bound to the essential elements of a contract.[250]

This approach to formation was discussed and followed by Heydon JA in *Brambles Holdings Ltd v Bathurst City Council*.[251] Brambles managed a solid waste disposal depot for the Council. For some years, Brambles had received liquid waste at the depot and charged a fee to depositors, which Brambles retained. At the relevant time, this was 1.1c per litre. By a letter dated 11 September 1991, the Council informed Brambles that it had resolved to increase liquid waste disposal fees to 1.3c per litre, increasing by a further 1c each quarter up to 6c per litre. Brambles was instructed to charge the increased fees and remit the additional income to the Council. By a letter dated 3 October 1991, Brambles replied that it was not viable for Brambles to continue to provide a liquid waste disposal service at the rates it was then receiving and asked for, inter alia, an increase in its remuneration. The parties did not reach agreement on Brambles' entitlement to increased remuneration, but from October 1991, Brambles charged and retained the increased fees set out in the Council's letter, including the quarterly increases. Some years later, the Council claimed a contractual entitlement to all additional income received by Brambles from the fee increases. The Council's entitlement to recover that income depended on the existence of a contract on the terms set out in the Council's letter of 11 September 1991. The trial judge found

246 Dalton, "An Essay in the Deconstruction of Contract Doctrine" (1985) 94 *Yale Law Journal* 997, 1030, 1066.

247 *Restatement of Contracts (2d)*, §22(2), cited with approval in *Vroon BV v Foster's Brewing Group* [1994] 2 VR 32, 82–3; *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, 178.

248 *Husain v O & S Holdings (Vic) Pty Ltd* [2005] VSCA 269, [51].

249 *Branir Pty Ltd v Owston Nominees (No 2) Pty Ltd* (2001) 117 FCR 424, 525.

250 *Branir Pty Ltd v Owston Nominees (No 2) Pty Ltd* (2001) 117 FCR 424, 525.

251 *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153.

that such a contract had been formed. Brambles appealed to the New South Wales Court of Appeal.

Brambles argued, first, that no offer had been made by the Council. Heydon JA accepted that there was some question as to whether the Council's letter could properly be regarded as an offer since it used the language of command, rather than that of a proposal which could be accepted or rejected. This point was not available to Brambles, however, because it had not been pleaded or argued below.[252] Brambles' second argument was that its letter of 3 October amounted to a rejection of the Council's offer and therefore extinguished it.[253] Ipp JA held that Brambles' letter did not amount to a rejection but was "merely part of the posturing that often accompanies negotiation".[254] Heydon JA said that the notion that rejection always renders an offer incapable of acceptance is based on the erroneous assumption that the "offer and acceptance analysis must invariably be employed in reaching decisions about the formation of contracts".[255] Although the offer and acceptance formulation is "a useful tool in most circumstances" and is the "conventional" approach,[256] Heydon JA said that it is "neither sufficient to explain all cases nor necessary to explain all cases".[257] Where no offer and acceptance can be identified, it is relevant to ask whether an agreement can be inferred, whether mutual assent has been manifested and whether a reasonable person in the position of each of the parties would think there was a concluded bargain.[258]

This case was analogous to *Empirnall Holdings v Machon Paull*. Brambles took advantage of the commercial benefits being offered by the Council, knowing the basis on which the Council was prepared to allow the higher fees to be charged. This would lead a reasonable bystander to conclude that Brambles was assenting to the Council's conditions. The Council's letter and Brambles' subsequent conduct would lead reasonable persons in the positions of the parties to believe that a contract was concluded on the basis proposed by the Council.[259] Thus, a contract was made even though there was some evidence that representatives of both the Council and Brambles "believed that there was no contractual regime for liquid waste fees but that the Council had some other power to fix them".[260]

In *PRA Electrical Pty Ltd v Perseverance Exploration Pty Ltd*, the Victorian Court of Appeal held that a concluded bargain had been manifested by conduct on the basis of a tender submitted by one party to the other, even though the tender documentation included a special condition that a contract would not come into effect between the parties until a formal contractual document had been executed.[261] The parties' conduct, including acts of performance, had reached a stage where an objective observer would conclude that a contract

252 *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, 171.

253 See [3.65].

254 *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153.

255 *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, 176. Mason P (at 155) agreed with the reasons of Ipp AJA, but also agreed with Heydon JA that the case demonstrates the difficulties of "pressing too far classical theory of contract formation based upon offer and acceptance".

256 *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, 179, citing *Gibson v Manchester City Council* [1979] 1 All ER 972, 974.

257 *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, 176.

258 *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, 179.

259 *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, 179–80.

260 *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, 180.

261 *PRA Electrical Pty Ltd v Perseverance Exploration Pty Ltd* [2007] VSCA 310; (2007) 20 VR 487.

was operative between the parties on the terms set out in the documents that passed between them, but without that special condition.[262]

NON-CONTRACTUAL OBLIGATIONS

[3.150] As noted at the beginning of this chapter, the classical approach to contract formation is based on the idea of a moment of formation when enforceable contractual rights arise. Prior to that moment, the parties have no contractual obligations to one another. Once the moment of formation has arrived, however, each party becomes liable for the other party's full contractual expectation.[263] Legal obligation between transacting parties under this approach is either all or nothing. Developments in the common law, equity and statute have addressed many of the inadequacies of the classical approach. Although the moment of formation is still of great importance, it is no longer as decisive as it once was, because the modern law recognises numerous non-contractual obligations between negotiating and contracting parties. The parties will owe obligations to one another even if a contract is never formed.

Developments in the law of estoppel have facilitated the protection of pre-contractual reliance. The law of estoppel now recognises that in exceptional circumstances it may be unfair for A to withdraw from negotiations with B, if A has led B to act on the assumption that A will enter into a contract with B.[264] The law of restitution will sometimes require payment in respect of work done in anticipation of a contract that fails to materialise.[265] The law of tort recognises that in some cases negotiating parties owe each other a duty of care in the provision of information.[266] The ACL imposes numerous obligations on parties engaged in contractual negotiations.[267] The most important of these is the obligation not to engage in misleading or deceptive conduct in trade or commerce, which in some circumstances requires one negotiating party to disclose information to another.[268] That may even include an obligation on the part of A to disclose to B the fact that another commercial opportunity has arisen which reduces the likelihood that the transaction between A and B will proceed.[269] The ACL also prohibits conduct such as bait advertising,[270] which from a contractual point of view would be regarded as an invitation to treat, having no legal significance.

These developments are of great practical importance and must be borne in mind when reading the older cases. Equitable doctrines, the law of tort, the law of restitution and statutory provisions will often provide a remedy to a party who has no contractual rights. In many cases, the remedies provided by these doctrines and statutory provisions will be more limited than those provided in respect of a breach of contract because the non-contractual doctrines are not concerned to enforce promises, but to protect against harm (in the case of estoppel, tort and the statutory prohibition on misleading conduct) or restore unjust gains (in the case

262 *PRA Electrical Pty Ltd v Perseverance Exploration Pty Ltd* [2007] VSCA 310; (2007) 20 VR 487, [74]–[76].

263 Feinman, "Critical Approaches to Contract Law" (1983) 30 *UCLA Law Review* 829, 835.

264 See Chapter 9, especially [9.175].

265 See Chapter 10, especially [10.50].

266 See [32.70]–[32.80].

267 See [2.70]–[2.105].

268 See Chapter 33.

269 See [33.60], especially the discussion of *EK Nominees Pty Ltd v Woolworths Ltd* [2006] NSWSC 1172.

270 ACL, s 35.

of restitution). In addition to those practical consequences, the recognition of obligations between negotiating parties is also of philosophical significance. The development of these obligations can be seen as a move away from the classical law's individualistic model of contracting, which gave primacy to the value of self-reliance. Parties involved in contractual negotiations are no longer regarded simply as autonomous individuals who need only be concerned with the pursuit of self-interest.

It can be argued, however, that this recognition falls far short of overcoming all of the problems with the classical approach to formation. Jay Feinman has argued that similar developments in the United States have failed to overcome the inadequacies of the classical law.[271] The classical law's rigid and formalistic approach to contract formation remains largely unchanged in the modern law. Despite the flaws in the classical model, the underlying idea of freedom of contract remains enormously powerful. The abandonment of the classical model would undermine the accepted basis of contract law and require too great a leap for the common law.[272] Accordingly, we are left with a mixed image, which accepts that the courts apply social values in some areas, while insisting that the core of contract is based on private agreement.[273]

271 Feinman, "Critical Approaches to Contract Law" (1983) 30 *UCLA Law Review* 829.

272 Feinman, "Critical Approaches to Contract Law" (1983) 30 *UCLA Law Review* 829, 833.

273 Feinman, "Critical Approaches to Contract Law" (1983) 30 *UCLA Law Review* 829, 834.

CHAPTER **4**

Consideration

WHEN IS CONSIDERATION REQUIRED?

[4.05] The second essential element in the formation of a contract is consideration. The doctrine of consideration requires that something must be given in return for a promise in order to make it binding. Consideration is clearly present in most agreements and is usually taken for granted. That is because most agreements that come before the courts involve an exchange. A contract may involve an immediate exchange of things, such as an exchange of money for goods. Alternatively, a contract may involve the exchange of a thing for a promise, such as A's immediate payment of $1000 to B in return for B's promise to build a fence for A. A contract may also involve an exchange of promises, such as A's promise to pay $1000 to B in return for B's promise to build a fence for A. It is where an agreement is entirely one-sided, and a promise remains unperformed, that the issue of consideration assumes central importance. Consideration must be identified when A has made a promise to B, which B wishes to enforce, and there is some doubt as to whether B has given anything in return.

Consideration is a requirement of the enforceability of promises. If we need to know whether A's promise to B can be enforced by B, we must ask whether B (the promisee) has given consideration for that promise.[1] When a contract is made by an exchange of promises, each party's promise provides consideration to support the promise made by the other. An agreement that is not supported by consideration on both sides is sometimes said to be nudum pactum (a naked agreement), and this label carries with it the idea that the agreement is unenforceable.

1 In this chapter, the person making the promise sought to be enforced will be referred to as the *promisor* and the person seeking to enforce the promise as the *promisee*.

ORIGINS OF THE REQUIREMENT

[4.10] The requirement of consideration was originally concerned with the motivation for making a promise. In the 16th century, the legal effect of a promise depended on the "considerations" or factors motivating the making of the promise.[2] The existence of a "good consideration" for making a promise provided evidence that a promise had in fact been made and indicated that it would be just to enforce the promise. By the end of the 16th century, it was necessary to plead the motive or reason for the making of a promise on which one wanted to sue.[3] Promises came to be enforceable when the promisee had conferred some benefit on the promisor or the promisee had acted to his or her detriment in reliance on the promise.[4] Although in the latter situation detrimental reliance was induced by the promise, rather than providing a motive for it, the concept of "consideration" was twisted to include reliance.[5] In the 18th century, the fact that the promisor was under a moral obligation to the promisee was taken to be sufficient consideration for a promise.[6]

The modern doctrine of consideration took shape in the 19th century. In *Eastwood v Kenyon*,[7] the moral obligation conception of consideration was firmly rejected. During this period, the concept of "bargain" came to dominate the law of contract being shaped by textbook writers and judges. Under the influence of the bargain concept, consideration came to be seen as something of legal value given in exchange for a promise, which could be seen as the price of the promise. An all-embracing formula for consideration was developed, which united the historical recognition of "benefit" and "detriment" with the idea of an exchange adopted by consensus between the parties.[8]

THE ESSENTIAL ELEMENTS

[4.15] Consideration is something the law regards as valuable, which is given in return for a promise and can be seen as the agreed price of the promise. There are two aspects to that definition: first, the promisee must incur a detriment or confer a benefit on the promisor (the benefit/detriment requirement) and, secondly, that benefit or detriment must be given in return for the promise (the bargain requirement). The courts do not expressly set up a two-stage test covering these requirements; rather, some cases focus on the benefit/detriment aspect, while other cases focus on the bargain requirement.

The benefit/detriment requirement

[4.20] The first aspect of valuable consideration is that it must consist of a detriment to the promisee or a benefit to the promisor. In a statement which has been described as a classic definition of consideration,[9] Lush J said in *Currie v Misa*[10] that:

2 Simpson, *A History of the Common Law of Contract* (1975), p 321.
3 Greig and Davis, *The Law of Contract* (1987), p 7.
4 Greig and Davis, *The Law of Contract* (1987), p 75.
5 Simpson, *A History of the Common Law of Contract* (1975), pp 324–5.
6 *Hawkes v Saunders* (1782) 1 Cowp 289, 290, 294; 98 ER 1091, 1093.
7 *Eastwood v Kenyon* (1840) 11 Ad & El 438; 113 ER 482.
8 Greig and Davis, *The Law of Contract* (1987), pp 20–1.
9 *Beaton v McDivitt* (1987) 13 NSWLR 162, 181.
10 *Currie v Misa* (1875) LR 10 Ex 153, 162.

> A valuable consideration, in the sense of the law, may consist in some right, interest, profit, or benefit accruing to the one party, or some forbearance, detriment, loss, or responsibility, given, suffered, or undertaken by the other …

This means that the person to whom the promise is made must either confer a benefit on the promisor, or must incur a legal detriment, in the sense of giving something up or undertaking an obligation. In most cases, the consideration given in return for a promise will constitute both a benefit to the promisor and a detriment to the promisee. Assume, for example, that B wishes to enforce A's promise to pay B $1000. The consideration given by B may be the transfer of property (such as B's car), the performance of services (such as building a fence for A) or, more commonly, the making of a promise to transfer property or perform services in the future. B may also make a promise not to do something, such as a promise not to sue A in respect of a tort or breach of contract committed by A, or a promise not to trade in competition with A. In each of those examples, the consideration given by B constitutes both a detriment to B and a benefit to A.

It is important to recognise that mutual promises will provide good consideration for each other.[11] If B makes a promise in return for A's promise, this will confer a benefit on A (because A will have an enforceable legal right to have the promise performed) and will also be a detriment to B (because B will come under an obligation to perform the promise). The recognition of mutual promises involves a paradox which has vexed writers on contract law.[12] If A and B exchange promises, each promise will constitute a legal benefit to the promisee and a legal detriment to the promisor only if it is legally enforceable. Each promise will be legally enforceable only if consideration has been provided in return. But the return promise will constitute good consideration only if it is enforceable. Thus, neither promise will be binding unless consideration has been provided, but, strictly speaking, neither promise should constitute consideration unless it is binding. Since there is no doubt that the courts do recognise mutual promises as good consideration for one another, this paradox is of academic interest only.

The "bargain" requirement

[4.25] The second aspect of the doctrine of consideration is that the benefit conferred on the promisor or the detriment suffered by the promisee must be given in return for the promise. The act relied on as consideration must, in other words, be performed as the agreed price of the promise. This notion of consideration was adopted by the High Court in *Australian Woollen Mills Pty Ltd v Commonwealth*.[13] This decision illustrates the proposition that: "Consideration, offer and acceptance are an indivisible trinity, facets of one identical notion which is that of bargain."[14] The facts of the case were outlined in Chapter 3.[15] Australian Woollen Mills (AWM) attempted to enforce a series of promises made by the Commonwealth to pay subsidies on the wool purchased by Australian manufacturers. AWM claimed that, by purchasing wool, it provided consideration for the Commonwealth's promises to pay the subsidies.

11 *Perry v Anthony* [2016] NSWCA 56, [26].

12 See Coote, "The Essence of Contract – Part II" (1989) 1 *Journal of Contract Law* 183, 191–5.

13 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424.

14 Hamson, "The Reform of Consideration" (1938) 54 *Law Quarterly Review* 233, 234.

15 See [3.15].

The acts of purchasing wool satisfied the test outlined in *Currie v Misa*[16] because they constituted both a legal detriment to AWM and a benefit to the Commonwealth. The High Court held, however, that there must be a relation of quid pro quo (this for that) between the Commonwealth's promise and the acts relied on as consideration for that promise. The acts must be performed *in return for* the promise. This "bargain" aspect of consideration will be satisfied if the acts which are said to amount to consideration have been performed at the request or implied request of the person making the promise. In this case, the statements made by the Commonwealth were in the nature of policy announcements and no request to purchase wool could be implied. In the absence of such a request, it was irrelevant that AWM may have acted to their detriment in reliance on the Commonwealth's promise.[17]

On appeal, the Privy Council upheld the decision of the High Court on the basis that the letters sent by the Commonwealth contained statements of policy, rather than offers.[18] The Privy Council indicated, however, that the High Court had over-emphasised the importance of a request. The Privy Council took the view that the presence of a request will not necessarily establish a contract.[19] Although in some cases the absence of a request will negate the existence of a contract, the presence of a request to perform an act will not necessarily establish a relation of quid pro quo between the act and a promise made by the alleged offeror.

It is possible for an act to satisfy the bargain aspect of consideration, but not the benefit/detriment requirement. The facts of *Ballantyne v Phillott*[20] illustrate this. Phillott had commenced proceedings against Ballantyne, his former mistress, to recover a substantial sum of money he had lent to her. There was some evidence that Ballantyne had asserted that she had lent money to Phillott and had claimed she could sue him for defamation, although it seems doubtful that she had, or even believed she had, an enforceable claim against him on either ground.[21] At the instigation of a third party, Ballantyne and Phillott signed a written document in which Phillott agreed to discontinue the proceedings and to release all claims he may have had against her. Ballantyne relied on the agreement when Phillott later instituted fresh proceedings to recover the debt. As consideration for Phillott's promises, Ballantyne relied on a statement in the signed document that she had no right or claim against Phillott in respect of the action for debt or otherwise. The High Court held, by a majority of 2-1, that Ballantyne had not given consideration for Phillott's promises. Menzies J held that Ballantyne did not promise to give up a claim against Phillott and no promise could be implied in the circumstances. Ballantyne had done no more than to admit that she had no claim against Phillott and this does not amount to consideration.[22] On this view, even if Ballantyne's admission could be regarded as the price of Phillott's promise, the making of the admission did not constitute a detriment to Ballantyne or a benefit to Phillott. Windeyer J accepted that such an admission could be the price of a promise but found that

16 *Currie v Misa* (1875) LR 10 Ex 153.

17 Greig and Davis, *The Law of Contract* (1987), p 81. Such detrimental reliance might today be claimed to give rise to an estoppel: see Chapter 9.

18 *Australian Woollen Mills Pty Ltd v Commonwealth* (1955) 93 CLR 546, 554–5.

19 *Australian Woollen Mills Pty Ltd v Commonwealth* (1955) 93 CLR 546, 550.

20 *Ballantyne v Phillott* (1961) 105 CLR 379.

21 *Ballantyne v Phillott* (1961) 105 CLR 379, 396, 399, 390.

22 *Ballantyne v Phillott* (1961) 105 CLR 379, 397–8.

it had not been shown to be so in this case.[23] Dixon CJ dissented on the basis that, slight as the consideration was "in a legal point of view", it was something and should be regarded as sufficient.[24]

Bargains and conditional gifts

[4.30] As discussed in Chapter 3,[25] the decision in *Australian Woollen Mills Pty Ltd v Commonwealth*[26] illustrates the distinction between a contract and a conditional gift. A promise to pay someone $100 *if* they perform a certain act is a conditional gift, whereas a promise to pay $100 *in return for* performance of the act is capable of giving rise to a contract. The court used the example of a promise by A to pay B (who is in Melbourne) £1000 upon B's arrival in Sydney. No contract arises upon B's arrival in Sydney because A is simply announcing his intention to make a gift to B. The necessary relationship between the promise and the act does not exist. If, on the other hand, A had an urgent need for B's presence in Sydney and B expressed concern about the cost of travel, B's act may be regarded as consideration for A's promise. That is because it would then be possible to infer a request by A which establishes the necessary connection between A's promise and B's act.

Bargains and reliance

[4.35] It is also important to distinguish between an act performed as the agreed price of a promise and an act performed *in reliance on* a promise. An act performed in reliance on a promise will not constitute good consideration but may give rise to an estoppel. This boundary between contract and estoppel was delineated by the New South Wales Court of Appeal in *Beaton v McDivitt*.[27] This case concerned an unusual arrangement. The McDivitts expected their land to be rezoned in a way that would greatly increase the rates payable to the local council. Since they were not using all of the land, they decided to minimise the rates payable by subdividing the land into four lots. They planned to give one of those lots to a person prepared to cultivate the land using permaculture methods. An agreement was reached with Beaton that Beaton would occupy the land in question and work it rent-free. The McDivitts would transfer the land to Beaton when the rezoning and subdivision took place. Beaton took possession of the land, built a house and a road giving access to the block and farmed the block for several years. Neither the rezoning nor the subdivision eventuated. A dispute arose between the parties over a Tai Chi class held in Beaton's house, and the McDivitts ordered Beaton off the land. Beaton claimed there was a contract between the parties which entitled him to a transfer of the land in question.

At first instance,[28] Young J held that the requirement of bargained-for consideration laid down in *Australian Woollen Mills Pty Ltd v Commonwealth* was not satisfied, but there was a line of cases, starting with *Dillwyn v Llewelyn*,[29] which represented "an exception to the modern requirement that a contract should be a bargain supported by consideration in

23 *Ballantyne v Phillott* (1961) 105 CLR 379, 399–400.

24 *Ballantyne v Phillott* (1961) 105 CLR 379, 390.

25 See [3.15].

26 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424.

27 *Beaton v McDivitt* (1987) 13 NSWLR 162.

28 *Beaton v McDivitt* (1985) 13 NSWLR 134.

29 *Dillwyn v Llewelyn* (1862) 4 De G F & J 517; 45 ER 1285.

the nature of a quid pro quo".[30] Young J held that the plaintiff's reliance on the defendants' promise amounted to a consideration and gave rise to "a *Dillwyn* type contract".[31] On appeal, the New South Wales Court of Appeal refused to extend the bargain theory of consideration laid down by the High Court in *Australian Woollen Mills Pty Ltd v Commonwealth*. Kirby P[32] and McHugh JA[33] made it clear that there was no exception to the bargain concept of consideration. They said that the *Dillwyn v Llewelyn* line of cases involved the enforcement of promises by way of estoppel and not by way of contract. Kirby P found that the bargain requirement was not satisfied on the facts, since Beaton made no promise which could be regarded as a quid pro quo for a promise to transfer the land.[34] McHugh and Mahoney JJA found that Beaton had provided consideration by working the land at the McDivitts' request.[35] Beaton's performance of the requested acts therefore gave rise to a unilateral contract. Beaton was ultimately unsuccessful, however, because Mahoney JA found that the contract had been brought to an end by frustration.[36] He therefore joined Kirby P in finding against Beaton.

The decision in *Beaton v McDivitt* draws a clear line between contract and equitable estoppel. Acts performed in reliance on a promise will not constitute consideration for that promise unless those acts can be regarded as having been performed in return for the promise. A person who relies on a promise which has not been bargained for must seek a remedy in estoppel rather than contract. In the subsequent decision of the High Court in the estoppel case *Waltons Stores (Interstate) Ltd v Maher*,[37] Mason CJ and Wilson J appeared to give their approval to a strict interpretation of the *Australian Woollen Mills* decision when they suggested that it "may be doubted whether our conception of consideration is substantially broader than the bargain theory" developed in the United States.[38]

The boundary between contract and equitable estoppel is also illustrated by *Arfaras v Vosnakis*.[39] The defendant in that case promised the plaintiff (her son-in-law) that the defendant would make a particular burial plot available for the burial of the remains of her daughter and would transfer her rights in relation to the plot to the plaintiff so that his remains could in due course be buried alongside those of his late wife. The defendant's promise to transfer the plot was held to be unsupported by consideration even though the plaintiff acted on the promise, by causing his late wife's remains to be buried in the plot, and that action was contemplated and intended by the defendant. That is because there was no quid pro quo relationship between the defendant's promise to transfer the rights and the plaintiff's acts. The defendant had simply made two unconditional promises: a promise to make the plot available for the burial of the daughter's remains and a separate promise to transfer the rights. Because he acted to his detriment on the faith of the promise, however, the plaintiff was held to be entitled to a transfer of the plot on the basis of equitable estoppel.

30 *Beaton v McDivitt* (1987) 13 NSWLR 162, 170.
31 *Beaton v McDivitt* (1985) 13 NSWLR 134.
32 *Beaton v McDivitt* (1987) 13 NSWLR 162, 170.
33 *Beaton v McDivitt* (1987) 13 NSWLR 162, 182
34 *Beaton v McDivitt* (1987) 13 NSWLR 162, 170.
35 *Beaton v McDivitt* (1987) 13 NSWLR 162, 175, 183.
36 *Beaton v McDivitt* (1987) 13 NSWLR 162, 177. As to frustration, see Chapter 15.
37 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387.
38 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 402.
39 *Arfaras v Vosnakis* [2016] NSWCA 65.

The bargain requirement is sometimes overlooked in the analysis of consideration. An example of a case in which this occurred was *Atco Controls Pty Ltd (in liq) v Newtronics Pty Ltd (recs & mgrs apptd) (in liq)*.[40] Atco provided a series of annual "letters of support" to the auditors of its subsidiary (Newtronics), in which Atco confirmed that it would not to seek to recover debts owed by Newtronics to the detriment of other creditors and confirmed that it would provide sufficient funds to Newtronics to enable Newtronics to meet its trading debts. Atco's support was needed for Newtronics to remain solvent and to continue to trade, and the provision of these letters allowed Newtronics to be presented in its audited accounts as a solvent, going concern.[41] When Newtronics subsequently became insolvent, its liquidator claimed that the letters of support were evidence of a contract between Atco and Newtronics under which Atco undertook to provide financial support for Newtronics and not to call up the debt to the detriment of other creditors. Pagone J at first instance found that, by continuing to trade, Newtronics provided consideration for Atco's undertakings. This finding was overturned on appeal. The Court of Appeal held that the most that could be said was that Newtronics had continued to trade *in reliance on* Atco's undertakings. For the consideration requirement to be satisfied, Newtronics would have to show that Atco's undertakings were offered as the price or quid pro quo for the action of Newtronics in continuing to trade. "In this case, that required Newtronics to show that Atco in effect requested Newtronics to continue to trade in return for the undertaking of continued support and that Newtronics was moved by that request."[42] No such request could be implied because "Atco for all intents and purposes ran Newtronics and had no need or intention of requesting it to do anything".[43]

CONSIDERATION MUST MOVE FROM THE PROMISEE

[4.40] It is clear that consideration given in return for a promise need not move to the promisor: A may undertake a contractual obligation to B in return for a benefit conferred by B on C. A might, for example, agree to pay a reward to any person who finds and returns C's dog. If B finds and returns the dog in reliance on A's promise, B's acts will not confer a benefit on A but will constitute a legal detriment to B and will have been given in return for A's promise.

Although consideration need not move to the promisor, it is a fundamental principle that consideration must move from the promisee.[44] This requirement has led some to question whether Lush J was right to accept in *Currie v Misa*[45] that a benefit to the promisor can constitute good consideration.[46] The argument is that a benefit to the promisor cannot be

40 *Atco Controls Pty Ltd (in liq) v Newtronics Pty Ltd (recs & mgrs apptd) (in liq)* [2009] VSCA 238; (2009) 25 VR 411.

41 See *Newtronics Pty Ltd (recs & mgrs appd) (in liq) v Atco Controls Pty Ltd (in liq)* [2008] VSC 566, [9]–[12].

42 *Atco Controls Pty Ltd (in liq) v Newtronics Pty Ltd (recs & mgrs apptd) (in liq)* [2009] VSCA 238; (2009) 25 VR 411, [62].

43 *Atco Controls Pty Ltd (in liq) v Newtronics Pty Ltd (recs & mgrs apptd) (in liq)* [2009] VSCA 238; (2009) 25 VR 411, [64].

44 *Thomas v Thomas* (1842) 2 QB 851; 114 ER 330 at 859, 333–4; *Dunlop Pneumatic Tyre Co Ltd v Selfridge & Co Ltd* [1915] AC 847.

45 *Currie v Misa* (1875) LR 10 Ex 1537.

46 See Shatwell, "The Doctrine of Consideration in the Modern Law" (1954) 1 *Sydney Law Review* 289, 305–6.

treated as an alternative to detriment to the promisee in the requirement of consideration because, if the consideration moves from the promisee, it must necessarily constitute a legal detriment to the promisee. This argument appears not to be accepted by the courts, which in recent cases have clearly accepted a benefit to the promisor as an alternative to detriment to the promisee in satisfying the requirement of consideration.[47]

Where two or more parties to a contract are regarded as joint promisees, consideration may be provided by one of them on behalf of both or all of them. This principle was accepted in *Coulls v Bagot's Executor and Trustee Co Ltd*.[48] That case concerned an agreement by which Arthur Coulls gave a company the right to quarry stone from his property in return for royalties. Under the agreement, Arthur Coulls authorised the company to pay the royalties to himself and his wife Doris Coulls "as joint tenants". Property held as joint tenants passes to the surviving tenant when one of them dies. When Arthur Coulls died, a dispute arose as to whether the company was obliged to pay the royalties to Doris Coulls or to the executor of Arthur Coulls' estate.

Whether Doris Coulls was entitled to receive the royalties depended on two issues: first, whether she was a party to the agreement and, secondly, whether she had given consideration for the company's promise to pay the royalties. A majority of the court found that she was unable to enforce the agreement because she was not a party to it.[49] In their dissenting judgments, Barwick CJ and Windeyer J held that a promise made to two or more joint promisees can be supported by consideration provided by one of the promisees on behalf of all. The consideration is then regarded as moving from all of them collectively and the promise can be enforced by action taken by them jointly.[50] Taylor and Owen JJ in the majority agreed that if Doris Coulls had been a party to the contract, it would not have mattered that she personally did not provide consideration.[51]

It is important to note that a party to a contract who has not herself provided consideration will be able to enforce a promise only if she can be regarded as a joint promisee with the person who has provided consideration. In other words, it is possible to be a party to a contract in which a promise is made but still be a stranger to the consideration given in return for that promise. In *Trident General Insurance Co Ltd v McNiece Bros Pty Ltd*,[52] Mason CJ and Wilson J observed that:

> If A, B and C are parties to a contract and A promises B and C that he will pay C $1000 if B will erect a gate for him, C cannot compel A to carry out his promise, because, though a party to the contract, C is a stranger to the consideration …[53]

Whether a person is regarded as a joint promisee, and therefore as a party to consideration given by another, involves a question of interpretation.[54]

47 See [4.85]–[4.90].

48 *Coulls v Bagot's Executor and Trustee Co Ltd* (1967) 119 CLR 460.

49 See [11.15].

50 *Coulls v Bagot's Executor and Trustee Co Ltd* (1967) 119 CLR 460, 478–9, 492–3. But see Coote, "Consideration and the Joint Promisee" [1978] *Cambridge Law Journal* 301.

51 *Coulls v Bagot's Executor and Trustee Co Ltd* (1967) 119 CLR 460, 486.

52 *Trident General Insurance Co Ltd v McNiece Bros Pty Ltd* (1988) 165 CLR 107.

53 *Trident General Insurance Co Ltd v McNiece Bros Pty Ltd* (1988) 165 CLR 107, 115–16.

54 See Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [4.8].

SUFFICIENCY OF CONSIDERATION

[4.45] It is said that consideration must be sufficient but need not be adequate. The requirement of sufficiency means that consideration must be something the law regards as valuable. Provided it meets this threshold, the courts will not inquire whether the value of the consideration is equal or even proportionate to that of the promise it supports. In *Woolworths Ltd v Kelly*,[55] Kirby P explained why the courts do not generally enquire into the adequacy of consideration. First, the courts have no way of assessing the value a particular person places on the consideration he or she has contracted to receive. Secondly, any requirement of adequacy of consideration would render the enforceability of contracts uncertain. Thirdly, the courts' stance protects economic freedom, even though "[t]hat liberty extracts a price in social terms".[56] Law and economics scholars argue that the courts' refusal to consider adequacy of consideration is justified because economic efficiency is best pursued through *voluntary* exchanges.[57] The role of the courts, therefore, is simply to ensure that a bargain has been struck and an exchange made.[58]

The refusal of the courts to consider the adequacy of consideration means that a promise to give a peppercorn is good consideration for a promise to pay $1m. In practice, it means that parties can effectively avoid the requirement of consideration through the use of nominal consideration.[59] One party may, for example, undertake quite onerous obligations in return for another's promise to pay $1. In *Thomas v Thomas*,[60] for example, a woman's promise to pay £1 towards the ground rent and to keep the house in good repair was held to be good consideration for a promise by her husband's executors to give her the right to occupy the house for life.

Although inadequacy of consideration does not in itself invalidate a contract, it may be taken into account as evidence of procedural unfairness in the formation of a contract. Where a party under a special disability has received inadequate consideration, for example, this will provide evidence that the other party has unconscionably taken advantage of that disability.[61]

Discretion as to performance

[4.50] A promise will not constitute good consideration if the promisor retains an unfettered discretion as to performance. If the promisor is not bound to perform, then the promise will constitute an illusory consideration. *Placer Development Ltd v Commonwealth*[62] concerned a written agreement in which the Commonwealth promised to pay a subsidy "of an amount or at a rate determined by the Commonwealth from time to time". The High Court, by a majority of 3-2, held that the agreement imposed no obligation on the Commonwealth to pay

55 *Woolworths Ltd v Kelly* (1991) 22 NSWLR 189, 193.

56 *Woolworths Ltd v Kelly* (1991) 22 NSWLR 189, 194.

57 See Posner, *Economic Analysis of Law* (9th ed, 2014), §4.1 and §4.2 and the discussion of economic analysis of contract law at [1.30]–[1.65].

58 Posner, *Economic Analysis of Law* (9th ed, 2014), §4.2.

59 See Patterson, "An Apology for Consideration" (1958) 58 *Columbia Law Review* 929, 952–4.

60 *Thomas v Thomas* (1842) 2 QB 851; 114 ER 330. Cf Greig and Davis, *The Law of Contract* (1987), p 93.

61 See, eg, *Blomley v Ryan* (1956) 99 CLR 362, esp at 399, 406; see also [36.65].

62 *Placer Development Ltd v Commonwealth* (1969) 121 CLR 353.

any subsidy. Accordingly, the Commonwealth's promise was an illusory consideration. Kitto J expressed the applicable principle as follows:

> The general principle … is that wherever words which by themselves constitute a promise are accompanied by words showing that the promisor is to have a discretion or option as to whether he will carry out that which purports to be the promise, the result is that there is no contract on which an action can be brought at all.[63]

The minority judges found that the Commonwealth was under an obligation to determine "what the subsidy was to be, and then to pay it."[64]

The concept of illusory consideration overlaps with the concept of an illusory promise, which may render a contract uncertain. Illusory promises are considered in Chapter 6.

Past consideration

The general rule

[4.55] Past consideration is not considered sufficient consideration. This means that, subject to one exception, something given before a promise is made cannot constitute good consideration for the promise. The thing may have been given gratuitously, such as where A gives B a dog and B subsequently promises to pay A $50 for it. A cannot rely on the giving of the dog as consideration for B's promise because it is past consideration. More commonly, the past consideration rule will be invoked where, after a contractual transaction has been completed, one of the parties makes a promise which the other seeks to enforce. This is illustrated by *Roscorla v Thomas*.[65] The defendant sold the plaintiff a horse for £30. Later, at the plaintiff's request, the defendant promised that the horse was "sound and free from vice". The plaintiff sought damages for breach of contract when the horse turned out to be "very vicious, restive, ungovernable and ferocious".[66] Lord Denman CJ held that the promise was not enforceable because the plaintiff had given no consideration. Payment of the purchase price was a past consideration which did not support the later promise.

It is important to distinguish between past consideration and executed consideration. Executed consideration is something given as part of the same transaction as the promise. In the case of a unilateral contract, for example, the consideration given by the offeree has been provided or executed by the time the contract is made. Assume, for example, that A offers $50 to whoever finds and returns a lost dog, and B finds and returns the dog. The contract is made when B returns the dog. At that time, B's consideration is executed, but A's promise remains executory.

Promise to pay for past services

[4.60] An exception to the past consideration rule is made in the case of a promise to pay for past services. Where services are performed at the request of the promisor, in circumstances that raise an implication that they are to be paid for, then performance of the services by the promisee will constitute good consideration for a subsequent promise to pay for them. The performance of the services and the promise to pay for them are in effect treated as part of the

63 *Placer Development Ltd v Commonwealth* (1969) 121 CLR 353, 356.

64 *Placer Development Ltd v Commonwealth* (1969) 121 CLR 353, 363, 370–1.

65 *Roscorla v Thomas* (1842) 3 QB 234; 114 ER 496.

66 *Roscorla v Thomas* (1842) 3 QB 234, 234; 114 ER 496, 497.

same transaction. In *Ipex Software Services Pty Ltd v Hosking*,[67] for example, the respondent transferred to a corporate group a computer software business of which he was part-owner on the understanding that he would receive shares in the restructured group. That transfer was held by the Victorian Court of Appeal to constitute good consideration for a subsequent promise to transfer five per cent of the equity in the group to the respondent.

The leading early case on this point was *Lampleigh v Brathwait*.[68] Brathwait asked Lampleigh to do all he could to secure a pardon from the King for a murder Brathwait had committed. Lampleigh was unable to obtain the pardon but expended considerable effort in travelling to see the King. Brathwait afterwards promised to pay Lampleigh £100 for his services and Lampleigh sought to enforce this promise. It was held that, where services are provided at the request of a party, a later promise to pay for those services will be binding because the promise "couples itself" with the earlier request. This principle was reformulated in the 19th century to cover only situations in which there was an understanding throughout the transaction that the services were to be paid for. The leading statement of the modern principle is that of Bowen LJ in *Re Casey's Patents; Stewart v Casey*.[69] In that case, the plaintiff had worked to promote the defendant's patents and was subsequently promised a one-third share of the patents. The English Court of Appeal held that the plaintiff had provided good consideration for the plaintiff's promise. Bowen LJ said:

> Now, the fact of a past service raises an implication that at the time it was rendered it was to be paid for, and, if it was a service which was to be paid for, when you get in the subsequent document a promise to pay, that promise may be treated either as an admission which evidences or as a positive bargain which fixes the amount of that reasonable remuneration on the faith of which the service was originally rendered.[70]

The existing legal duty rule

The general rule

[4.65] Neither a promise to perform an existing legal duty, nor the performance of an existing legal duty, is regarded as sufficient consideration to support a contract. The existing legal duty rule covers promises to perform existing public duties, such as a promise to give evidence in court when the promisee is obliged by a subpoena to do so.[71] There is an obvious public interest in this aspect of the existing legal duty rule. It is important that the law of contract does not encourage public officials and those involved in the administration of justice to be influenced by promises of extra rewards for discharging their responsibilities.[72]

The existing legal duty rule is most commonly raised in relation to one-sided variations to contracts, where one party either assumes an additional obligation or agrees to release the other party from an obligation. In order to avoid confusion between the two parties involved in a one-sided contract variation, the person who promises to perform an existing

67 *Ipex Software Services Pty Ltd v Hosking* [2000] VSCA 239.

68 *Lampleigh v Brathwait* (1616) Hob 105; 80 ER 255.

69 *Re Casey's Patents; Stewart v Casey* [1892] 1 Ch 104, 115–6.

70 *Re Casey's Patents; Stewart v Casey* [1892] 1 Ch 104, 115–6.

71 *Collins v Godefroy* (1831) 1 B & Ad 950; 109 ER 1040. Cf *Glasbrook Bros Ltd v Glamorgan County Council* [1925] AC 270.

72 See Greig and Davis, *The Law of Contract* (1987), pp 101–4.

legal duty and claims the benefit of the contractual modification will be referred to in this chapter as the *beneficiary*. The party assuming an additional obligation or releasing the beneficiary from an obligation will be referred to as the *modifying party*. The rule can be illustrated as follows.

Assume that one party (the beneficiary) has agreed to build a garage and fence for another (the modifying party) for $30,000 and, after the contract has been made, the beneficiary realises that she has agreed to perform the work at a loss. She expresses some reluctance to perform, so the beneficiary and the modifying party reach an agreement that if the beneficiary builds the garage, the modifying party will pay the beneficiary an extra $5000 and will not require the beneficiary to build the fence. In return for the modifying party's promises, the beneficiary has simply promised to perform her contractual obligations. She has not agreed to do anything she was not already obliged to do. The courts will not generally enforce a promise made by the modifying party in such a situation, even though it was intended to be binding.[73] The principle was clearly stated by Mason J in *Wigan v Edwards*:[74]

> The general rule is that a promise to perform an existing duty is no consideration, at least when the promise is made by a party to a pre-existing contract, when it is made to the promisee under that contract, and it is to do no more than the promisor is bound to do under that contract.

The existing legal duty rule is sometimes referred to as the rule in *Stilk v Myrick*.[75] In that case, two sailors deserted a ship on a voyage to the Baltic. Because the captain was unable to replace the deserters, he promised the remaining crew that he would divide the deserters' wages among them if they would sail the ship back to London short-handed. The plaintiff was one of the remaining crew and he sued to recover his share. The crew were originally employed on the basis that they would "do all that they could under all the emergencies of the voyage".[76] Lord Ellenborough CJ found that the desertion of a small part of the crew was such an emergency. The remaining crew were therefore bound by the terms of their original contracts to complete the voyage short-handed. Accordingly, their agreement to sail the boat back to London was simply a promise to perform an existing obligation and did not constitute good consideration for the promise of extra payment. The captain's promise was therefore unenforceable.

In *Wigan v Edwards*,[77] Mason J noted that the existing legal duty rule is conceptually justified by the fact that a promise to perform an existing contractual duty is an illusory consideration. The promisor incurs no new burden and the promisee receives no benefit that he or she did not already enjoy. From the point of view of policy, the principle is said to discourage parties from seeking to secure additional benefits by threatening to breach their contracts.[78] The English courts seemed to regard ship owners as particularly vulnerable to extravagant demands for extra wages and, since Britain was heavily reliant on shipping, were especially concerned to protect them.[79] A case which preceded *Stilk v Myrick* and involved similar facts

73 For example, *T A Sundell & Sons Pty Ltd v Emm Yannoulatos (Overseas) Pty Ltd* (1955) 56 SR (NSW) 323.

74 *Wigan v Edwards* (1973) 1 ALR 497, 512.

75 *Stilk v Myrick* (1809) 2 Camp 317; 170 ER 1168.

76 *Stilk v Myrick* (1809) 2 Camp 317, 319; 170 ER 1168, 1169.

77 *Wigan v Edwards* (1973) 1 ALR 497, 512.

78 *Wigan v Edwards* (1973) 1 ALR 497, 594. See also *Musumeci v Winadell Pty Ltd* (1994) 34 NSWLR 723, 741.

79 Greig and Davis, *The Law of Contract* (1987), pp 108–10.

was decided on the basis of public policy, rather than the absence of consideration.[80] One report of *Stilk v Myrick* suggests that it too was decided on the basis of policy issues, rather than consideration.[81] It is clear that these policy considerations influenced the development of the existing legal duty rule.

The existing legal duty rule is regularly criticised on the basis that it does not reflect the practices of businesspeople, who routinely make one-sided variations to contracts. This is supported by empirical studies, which indicate a preparedness to modify concluded bargains where circumstances have changed.[82] Modifications are often accepted on the basis that each business deal must remain viable for both parties, so that the parties can preserve their relationship and their reputations in the business community.[83] The difficulty for lawmakers is that a one-sided variation may involve the co-operative reallocation of unforeseen risks, where the economic environment of the contract has changed, or may simply reflect one party's exploitation of another's dependency and a lack of adequate remedies for breach.[84]

It may be doubted whether the requirement of consideration provides any great protection against coercive modifications as the courts do not inquire into the adequacy of consideration. The presence of nominal consideration will render a contract modification enforceable but is entirely consistent with coercion.[85] As Santow J said in *Musumeci v Winadell Pty Ltd*: "Consideration expressed in formalistic terms of one dollar can indeed actually cloak duress rather than expose it."[86] The developing doctrine of economic duress is likely to provide a more useful weapon against coercive modifications.[87] A threat to breach a contract is regarded as illegitimate pressure and therefore capable of rendering a contract voidable on the grounds of duress.[88]

Part-payment of a debt

[4.70] A corollary of the existing legal duty rule is the principle that part-payment of a debt does not constitute good consideration for an agreement to discharge the debt. This is known as the rule in *Pinnel's Case*.[89] If a debtor owes a creditor $100 and the creditor agrees to accept $50 in satisfaction of the debt, this agreement will not be binding and the creditor will be entitled to recover the remaining $50. In paying part of the debt, the debtor is simply performing (part of) his or her legal obligation. The rule in *Pinnel's Case* was applied by the House of Lords in *Foakes v Beer*,[90] where a debtor promised to pay a

80 *Harris v Watson* (1791) Peake 102; 170 ER 94.

81 *Stilk v Myrick* (1809) 6 Esp 129; 170 ER 851.

82 See Macaulay, "Non-Contractual Relations in Business: A Preliminary Study" (1963) 28 *American Sociological Review* 55, 60–2, discussed at [1.115].

83 Macaulay, "Non-Contractual Relations in Business: A Preliminary Study" (1963) 28 *American Sociological Review* 55, 60–5; Collins, *Regulating Contracts* (1999), Ch 6, esp pp 144–5.

84 Trebilcock, *The Limits of Freedom of Contract* (1993), pp 169–70.

85 *United States v Stump Home Specialties Manufacturing Inc* (1990) 905 F 2d 1117, 1121–2, quoted in *Musumeci v Winadell Pty Ltd* (1994) 34 NSWLR 723, 742–3.

86 *Musumeci v Winadell Pty Ltd* (1994) 34 NSWLR 723, 742.

87 *Musumeci v Winadell Pty Ltd* (1994) 34 NSWLR 723, 744; *Williams v Roffey Bros & Nicholls (Contractors) Ltd* [1991] 1 QB 1, 13–4. See also Posner, *Economic Analysis of Law* (9th ed, 2014), §4.2.

88 See [34.45].

89 *Pinnel's Case* (1602) 5 Co Rep 117a; 77 ER 237.

90 *Foakes v Beer* (1884) 9 App Cas 605.

judgment debt in six-monthly instalments in return for the creditor's promise not to enforce the judgment. When the debt had been repaid in full, the creditor successfully claimed interest. The House of Lords held that, even if the creditor's promise could be construed as an agreement to forgo interest on the debt, such a promise was not supported by consideration under the rule in *Pinnel's Case*. Although the House of Lords felt that the rule was too well entrenched to be overruled,[91] its practical inconvenience was acknowledged by Lord Blackburn:

> What principally weighs with me … is my conviction that all men of business, whether merchants or tradesmen, do every day recognise and act on the ground that prompt payment of a part of their demand may be more beneficial to them than it would be to insist on their rights and enforce payment of the whole. Even where the debtor is perfectly solvent, and sure to pay at last, this often is so.[92]

The rule in *Pinnel's Case* has no application where the debtor pays before the due date or in a different form,[93] where several creditors jointly agree to forgo part of each of their debts (known as a composition),[94] where the payment is made to the creditor by a third party[95] or where the debtor gives something other than money:

> By no possibility a lesser sum can be a satisfaction to the plaintiff for a greater sum: but the gift of a horse, hawk or robe, etc, might be more beneficial to the plaintiff than the money, in respect of some circumstance, or otherwise the plaintiff would not have accepted it in satisfaction.[96]

This leads to an apparently absurd situation in which a promise to accept $999 in discharge of a $1000 debt is unenforceable for want of consideration, whereas a promise to accept $1 plus an old sandshoe in discharge of the same debt will be enforceable.[97] If nominal consideration is viewed as a formal requirement, however, the enforcement of the transaction involving the sandshoe does make sense. Such an artificial bargain must have been deliberately set up in order to make the promise binding.[98] In practice, where a creditor is prepared to accept a lesser sum in full satisfaction of a debt, the rule is commonly avoided through the use of a more conventional form, namely a deed. If the agreement is made in the form of a deed, it will be binding in the absence of consideration.[99]

Exceptions to the existing legal duty rule

[4.75] There are five situations in which the existing legal duty rule will not apply. First, the rule will not apply where the beneficiary is providing fresh consideration, such as where the beneficiary undertakes to do something more than he or she was obliged to do under the original contract. Secondly, an exception to the rule has been recognised where the beneficiary's

91 In *MWB Business Exchange Centres Ltd v Rock Advertising Ltd* [2018] UKSC 24; [2019] AC 119. Lord Sumption JSC (with whom Baroness Hale, Lord Wilson and Lord Lloyd-Jones JJSC agreed) suggested that the decision in *Foakes v Beer* was "probably ripe for re-examination".

92 *Foakes v Beer* (1884) 9 App Cas 605, 622.

93 See Greig and Davis, *The Law of Contract* (1987), pp 113–5.

94 *Couldery v Bartrum* (1881) 19 Ch D 394; *Re Pearse* [1905] VLR 446.

95 *Hirachand Punamchand v Temple* [1911] 2 KB 330.

96 *Pinnel's Case* (1602) 5 Co Rep 117a; 77 ER 237.

97 Carter, *Contract Law in Australia* (7th ed, 2018), [6-58].

98 See [4.115].

99 See [4.120].

promise to perform confers a practical benefit on the modifying party. Thirdly, the rule has been held to be inapplicable where the promise to perform an existing contractual duty is made by the beneficiary to a third party. Fourthly, a promise made by way of a bona fide compromise of a legal claim will not be covered by the rule. Fifthly, the rule will be avoided where the original contract is terminated by agreement and replaced with a new contract. These exceptions will be considered in turn.

Fresh consideration

[4.80] The existing legal duty rule applies only where, in return for the modification, the beneficiary promises to do no more than he or she promised under the original contract. If the beneficiary provides fresh consideration, by undertaking to do something more than he or she originally promised, then the existing legal duty rule can have no application.[100] *Hartley v Ponsonby*,[101] for example, was a case on similar facts to *Stilk v Myrick*[102] except that almost half the crew had deserted the ship, making it dangerous to continue. The remaining crew were under no obligation to go to sea in those conditions and therefore provided fresh consideration by agreeing to continue the voyage. The captain's promise of extra wages was therefore enforceable.

The existing legal duty rule can be avoided, if the parties are aware of it, by the beneficiary giving nominal fresh consideration in return for the promise or concession made by the modifying party. In *Stilk v Myrick*, for example, the remaining crew could have avoided the operation of the existing legal duty rule by agreeing to work longer shifts.[103] Of course, only parties who can afford and have access to legal advice can take advantage of technical exceptions such as this.

Practical benefit

[4.85] The existing legal duty rule has also been held to be inapplicable where the modifying party obtains a practical benefit from the beneficiary's promise to perform an existing obligation. This exception was first recognised by the English Court of Appeal in *Williams v Roffey Bros & Nicholls (Contractors) Ltd* (*Williams v Roffey*).[104] The defendant had contracted to refurbish a block of 27 flats. It entered into a subcontract with the plaintiff under which the plaintiff agreed to perform some carpentry work involved in the refurbishment for £20,000. Before the work was finished, the plaintiff got into financial difficulties and was concerned that he was unable to complete the work. In order to avoid the trouble and expense of finding a replacement carpenter, and to avoid incurring financial penalties under the head contract for late completion, the defendant agreed to pay the plaintiff an extra £575 for each flat completed. The plaintiff substantially completed work on eight further flats but stopped work when the promised additional sum was not paid. The defendant then engaged another carpenter to finish the work and incurred one week's time penalty on the head contract.

100 *Larkin v Girvan* (1940) 40 SR (NSW) 365, 368.

101 *Hartley v Ponsonby* (1857) 7 El & Bl 872; 119 ER 1471.

102 *Stilk v Myrick* (1809) 2 Camp 317; 170 ER 1168.

103 See Posner, *Economic Analysis of Law* (9th ed, 2014), §4.2.

104 *Williams v Roffey Bros & Nicholls (Contractors) Ltd* [1991] 1 QB 1.

The plaintiff sought to enforce the promise of extra payment but had provided no consideration other than a promise to perform his obligations under the original contract.[105] The Court of Appeal upheld the plaintiff's contractual right to recover the promised payments on the basis that he had provided consideration. The court held that the rule in *Stilk v Myrick*[106] remained good law, but an exception to the rule should be recognised where the promise to perform confers a practical benefit on the promisee. The plaintiff's promise to perform on time was of benefit to the defendant because the defendant retained the services of the plaintiff and would have been able to have the work completed without employing another carpenter. Glidewell LJ held that:

> (i) if A has entered into a contract with B to do work for, or to supply goods or services to, B in return for payment by B; and
>
> (ii) at some stage before A has completely performed his obligations under the contract B has reason to doubt whether A will, or will be able to, complete his side of the bargain; and
>
> (iii) B thereupon promises A an additional payment in return for A's promise to perform his contractual obligations on time; and
>
> (iv) as a result of giving his promise, B obtains in practice a benefit, or obviates a disbenefit; and
>
> (v) B's promise is not given as a result of economic duress or fraud on the part of A; then
>
> (vi) the benefit to B is capable of being consideration for B's promise, so that the promise will be legally binding.[107]

The *Williams v Roffey* principle has been widely criticised.[108] The main criticism is that the new principle indirectly abolishes the rule in *Stilk v Myrick* because it will always be possible to identify a practical benefit resulting from performance of a contractual obligation. In one sense, a practical benefit will be present in all cases since, absent coercion, the modifying party will only agree to a modification if there is some benefit in doing so. In another sense, the modifying agreement can never generate a real benefit for the modifying party, since that party already had a contractual right to receive any practical benefits flowing from performance. This appears to be a perfect example of situation in which "a 'rule' that appears cleanly to dispose of a fact situation is nullified by a counter-rule whose scope of application seems to be almost identical".[109] The "exception" in *Williams v Roffey* appears to cover precisely the same ground as the "general rule" in *Stilk v Myrick*.

[4.90] Two other problems with the *Williams v Roffey* principle have been identified.[110] First, the principle provides that the presence of economic duress and fraud will prevent the practical benefit from being regarded as consideration. This means that the modifying agreement will have no contractual force. As we will see in Chapters 32 and 34, however, the effect of fraud and duress is to render a contract *voidable* at the option of the party affected,

105 The plaintiff did not make an argument based on estoppel before the trial judge, so estoppel could not properly be considered by the Court of Appeal: *Williams v Roffey Bros & Nicholls (Contractors) Ltd* [1991] 1 QB 1, 13, 17–8. As to the possible application of equitable estoppel in these circumstances, see [9.215].

106 *Stilk v Myrick* (1809) 2 Camp 317; 170 ER 1168.

107 *Williams v Roffey Bros & Nicholls (Contractors) Ltd* [1991] 1 QB 1, 15–6.

108 For example, Coote, "Consideration and Benefit in Fact and in Law" (1990) 3 *Journal of Contract Law* 23; Chen-Wishart, "Consideration: Practical Benefit and the Emperor's New Clothes" in Beatson and Friedmann (eds), *Good Faith and Fault in Contract Law* (1995), p 123.

109 Kennedy, "Form and Substance in Private Law Adjudication" (1976) 89 *Harvard Law Review* 1685, 1700.

110 Carter, Phang and Poole, "Reactions to *Williams v Roffey*" (1995) 8 *Journal of Contract Law* 248.

not *void*. By bringing these vitiating factors into a principle of formation, the rule in *Williams v Roffey* changes their effect. Rather than providing a ground for rescission of the modifying agreement, the presence of these factors will prevent the agreement from being binding in the first place.[111] Secondly, the rule in *Williams v Roffey* is said to be inconsistent with the bargain theory of consideration in the way in which it identifies consideration.[112] According to the bargain theory, consideration is the thing given in exchange for a promise. What is given and accepted in return for the modifying party's promise is in fact the beneficiary's promise to perform, not the practical benefit flowing from that performance.

The principle in *Williams v Roffey* might be thought to provide an exception to the rule relating to part-payment of a debt[113] in cases where there is some practical benefit to the creditor in accepting part-payment. The English Court of Appeal has, however, refused to extend the rule in *Williams v Roffey* to the discharge of debts. In *Re Selectmove Ltd*,[114] the English Court of Appeal held that the principle in *Williams v Roffey* could not be applied to an agreement to discharge a debt in return for part payment, because that would leave the principle in *Foakes v Beer* without any application. In such a situation, according to Peter Gibson LJ, "the creditor will no doubt always see a practical benefit to himself in so doing".[115]

The rule in *Williams v Roffey* has been applied in a modified form in the Supreme Court of New South Wales. *Musumeci v Winadell Pty Ltd*[116] concerned the enforceability of a promise by a landlord to accept a reduced rental from its tenants, who were in financial difficulties. The tenants operated a fruit shop in a shopping centre and their business suffered when the landlord let a much larger shop to a member of a chain of fruit stores. In view of the tenants' difficulties, the landlord agreed to reduce the rent by one-third. After further disputation, the landlord resiled from the agreement and claimed the full amount of rent. The tenants sought to rely on the landlord's promise to accept a reduced rental, and the issue was whether they had provided consideration for that promise.

Santow J considered that the "practical benefit" exception should be accepted in Australia, with three modifications. First, modification was required to allow for the fact that this was a case in which the modifying party agreed to accept less, rather than to pay more for the beneficiary's performance. Santow J therefore extended the *Williams v Roffey* principle to cover a situation in which the modifying party makes a concession, such as accepting a reduction in the beneficiary's obligations.[117] Secondly, in order to protect against coercive modifications, Santow J considered that the practical benefit principle should apply only where the promise has not been induced by "unfair pressure".[118] Thirdly, and most importantly, Santow J refined the rule in order to meet the criticism that the practical benefit concept does not provide an

111 Carter, Phang and Poole, "Reactions to *Williams v Roffey*" (1995) 8 *Journal of Contract Law* 248, 253.

112 Carter, Phang and Poole, "Reactions to *Williams v Roffey*" (1995) 8 *Journal of Contract Law* 248, 253–4. See also Carter, *Contract Law in Australia* (7th ed, 2018), [6-48].

113 See [4.70].

114 *Re Selectmove Ltd* [1995] 1 WLR 474. See also *Collier v P & MJ Wright (Holdings) Ltd* [2007] EWCA Civ 1329; [2008] 1 WLR 643.

115 *Re Selectmove Ltd* [1995] 1 WLR 474, 481.

116 *Musumeci v Winadell Pty Ltd* (1994) 34 NSWLR 723. The correctness of the principle applied in *Musumeci* has been accepted in a number of cases, including *Tinyow v Lee* [2006] NSWCA 80, [61]. It was mentioned, with apparent approval, by Gummow and Hayne JJ in *DPP (Victoria) v Le* [2007] HCA 52, [43]; (2007) 232 CLR 562 and applied in *Hill v Forteng Pty Ltd* [2019] FCAFC 105.

117 *Musumeci v Winadell Pty Ltd* (1994) 34 NSWLR 723, 747.

118 *Musumeci v Winadell Pty Ltd* (1994) 34 NSWLR 723, 744.

adequate basis for distinguishing between cases.[119] He held that a practical benefit should only constitute good consideration if the beneficiary's performance is capable of being regarded by the modifying party as worth more than any remedy against the beneficiary.[120] In other words, performance by the beneficiary must be seen to be worth more to the modifying party than an award of damages against the beneficiary.[121] It may be doubted whether this third refinement resolves the fundamental problem with the *Williams v Roffey* principle. In theory, contract damages should reflect the value of performance, since such damages are calculated to place the innocent party in the position he or she would have occupied had the contract been performed.[122] In practice, given the uncertainties, delays and costs involved in litigation, performance will almost always be preferable to a claim for damages.

It has been held in two Canadian provinces that the doctrine of consideration should no longer be applied to contract variations, which should be enforceable provided there has been no duress or unconscionable conduct.[123] The New Zealand Court of Appeal has also accepted the force of criticism of the practical benefit exception to the existing legal duty rule and has come very close to abandoning it.[124] Although on the facts it was not necessary to decide whether the practical benefit rule should be abandoned, the Court of Appeal held that *Stilk v Myrick* "can no longer be taken to control" contract modification cases.[125] The court accepted the strength of the argument that one-sided contract modifications should be binding and "that the only principled way to such a result is to decide that consideration should not be necessary for the variation of contract".[126] The court observed that:

> The importance of consideration is as a valuable signal that the parties intend to be bound by their agreement, rather than an end in itself. Where the parties who have already made such intention clear by entering legal relations have acted upon an agreement to a variation, in the absence of policy reasons to the contrary they should be bound by their agreement.[127]

Promises made to third parties

[4.95] A promise to perform an existing contractual obligation does amount to a good consideration if it is made to a person who was not a party to the original contract.[128] The existing legal duty rule does not apply because the promisor incurs an additional legal obligation and confers an additional legal right on the new promisee. In *Pau On v Lau Yiu*

119 *Musumeci v Winadell Pty Ltd* (1994) 34 NSWLR 723, 744–7.

120 *Musumeci v Winadell Pty Ltd* (1994) 34 NSWLR 723, 745–7.

121 *Musumeci v Winadell Pty Ltd* (1994) 34 NSWLR 723, 745.

122 See Chapter 26.

123 *Nav Canada v Greater Fredericton Airport Authority Inc* (2008) 290 DLR (4th) 405; *Rosas v Toca*, 2018 BCCA 191. See also Coote, "Variations Sans Consideration" (2011) 27 *Journal of Contract Law* 185 and Harder, "One-sided Contract Modifications and the Requirement of Consideration" [2019] *Lloyd's Maritime and Commercial Law Quarterly* 138.

124 *Antons Trawling Co Ltd v Smith* [2003] 2 NZLR 23; see Coote, "Contracts and Variations: A Different Solution" (2004) 120 *Law Quarterly Review* 19 and also *Teat v Willcocks* [2013] NZCA 162; [2014] 3 NZLR 129, [54].

125 *Antons Trawling Co Ltd v Smith* [2003] 2 NZLR 23, [93].

126 *Antons Trawling Co Ltd v Smith* [2003] 2 NZLR 23, [92], citing Coote, "Consideration and Benefit in Fact and in Law" (1990) 3 *Journal of Contract Law* 23.

127 *Antons Trawling Co Ltd v Smith* [2003] 2 NZLR 23, [93], citing Coote, "Consideration and Benefit in Fact and in Law" (1990) 3 *Journal of Contract Law* 23.

128 *Scotson v Pegg* (1861) 6 H & N 295; 158 ER 121, at 299–300, 123. For a recent application, see *Ailakis v Olivera (No 2)* [2014] WASCA 127; (2014) 100 ACSR 524, [104]–[109].

Long,[129] the plaintiffs had agreed to acquire shares in a public company under a contract which required them not to sell 60 per cent of the allotted shares for 12 months. They entered into a second contract with the shareholders of the company. In return for the plaintiffs performing their obligations under the first contract, the shareholders agreed to indemnify the plaintiffs against any loss resulting from a fall in the share price during that 12-month period. When the plaintiffs sought to enforce that contract of indemnity, the Privy Council held that a promise to perform an act which the promisee is already under an existing obligation to a third party to perform will constitute good consideration. The plaintiffs had provided good consideration because the shareholders obtained the benefit of a direct obligation which they were able to enforce.[130] Moreover, the plaintiffs' entry into the main contract could not be regarded as past consideration, because the plaintiffs agreed to the restriction on selling their shares in the public company on the understanding that they would be indemnified against loss resulting from a fall in the share price.[131] The granting of the indemnity therefore fell within the exception to the past consideration rule described by Bowen LJ in *Re Casey's Patents; Stewart v Casey*.[132]

Compromise and forbearance to sue

[4.100] A promise to perform an existing legal obligation will also constitute good consideration where it is made by the beneficiary as part of a bona fide compromise of a disputed claim. This principle was applied by the High Court in *Wigan v Edwards*.[133] The Edwards entered into a contract to buy from Wigan a house that he had built. After the contract was made, the Edwards became concerned about some defects in the house. They gave Wigan a list of defects that required attention before they would consider "going into the house and finalising anything".[134] In other words, the Edwards refused to complete the transaction unless the defects were rectified. Although they had no legal right to refuse to complete the purchase, there were many defects and their claim was made honestly.[135] Faced with the Edwards' claim, Wigan signed a document agreeing to rectify the listed defects within one week and to repair any major faults in construction within five years of the purchase date. Wigan rectified some of the listed defects before the transaction was completed but did nothing after completion of the transaction to rectify the defects that remained outstanding.

The Edwards sued Wigan for damages for breach of contract. Wigan argued that the Edwards had provided no consideration for his promise to rectify the defects. All the Edwards had done in return for the promise was implicitly to agree to perform their existing legal duty to pay the purchase price and complete the transaction. The High Court held that a promise made as part of a bona fide compromise constituted an exception to the existing legal duty rule:

> An important qualification to the general principle is that a promise to do precisely what the promisor is already bound to do is a sufficient consideration, when it is given by way of a bona

129 *Pau On v Lau Yiu Long* [1980] AC 614.

130 *Pau On v Lau Yiu Long* [1980] AC 614, 631–2.

131 *Pau On v Lau Yiu Long* [1980] AC 614, 629–30.

132 *Re Casey's Patents; Stewart v Casey* [1892] 1 Ch 104; see [4.60].

133 *Wigan v Edwards* (1973) 1 ALR 497.

134 *Wigan v Edwards* (1973) 1 ALR 497, 510.

135 *Wigan v Edwards* (1973) 1 ALR 497, 513.

> fide compromise of a disputed claim, the promisor having asserted that he is not bound to perform the obligation under the pre-existing contract or that he has a cause of action under that contract.[136]

In order to fall within this exception, it was not necessary for the Edwards to establish that they had a valid legal entitlement to refuse to perform the contract. It was enough that they intimated that they did not consider themselves bound to perform and that their claim was honestly made. The requirement that the dispute must be bona fide is said to prevent parties from seeking to obtain an unfair advantage by threatening unscrupulously to withhold performance.[137]

Termination and replacement

[4.105] The existing legal duty rule will have no application where the parties have terminated their original contract and entered into a new contract. This is so even if the obligations of one party (the modifying party) are more onerous than those in the original contract and the obligations of the other (the beneficiary) are identical to those in the original contract. Since the original contract has been brought to an end, the promise made by the beneficiary is seen as a "new" promise, which provides consideration for the promises undertaken by the modifying party. The question whether a contract has been modified or replaced is potentially very important because a new contract will be supported by consideration, whereas a modification of an existing contract may not be. This exception to the existing legal duty rule will only operate where the parties intended to terminate and replace, rather than modify, their original contract.[138]

THE PURPOSE OF CONSIDERATION

Criticism of the doctrine of consideration

[4.110] The doctrine of consideration is often criticised as a "mere incumbrance" on the law of contract, which can and should be abolished.[139] Its detractors suggest that the functions of the law of consideration could be better performed by the requirement that the parties have manifested an intention to make a binding contract.[140] Many aspects of the consideration doctrine are regarded as undesirable. In 1937, the United Kingdom Law Revision Committee recommended, in vain, the abolition of the rule in *Pinnel's Case*, the existing legal duty rule, the requirement that consideration move from a promisee, the requirement that consideration be given for a promise to hold an offer open and indeed the consideration requirement itself in the case of written agreements.[141]

136 *Wigan v Edwards* (1973) 1 ALR 497, 512.

137 *Wigan v Edwards* (1973) 1 ALR 497, 512.

138 See Chapter 19.

139 Wright, "Ought the Doctrine of Consideration to Be Abolished from the Common Law?" (1936) 49 *Harvard Law Review* 1225, 1251.

140 For example, Wright, "Ought the Doctrine of Consideration to be Abolished from the Common Law" (1936) 49 *Harvard Law Review* 1225; Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), pp 35–8. But see Patterson, "An Apology for Consideration" (1958) 58 *Columbia Law Review* 929, 952–4.

141 United Kingdom Law Revision Committee, *Sixth Interim Report (Statute of Frauds and the Doctrine of Consideration)*, (1937, Cmd 5449), pp 31–2.

Charles Fried has argued that the consideration requirement is an anachronism that should be abandoned, since it operates as an unnecessary constraint on freedom of promising.[142] Allowing people to make gifts enhances individual liberty and the same can be said of allowing people to make binding promises to make gifts. According to Fried, there is no reason why the courts should not enforce a deliberate, freely made promise which is serious enough that legal enforcement must have been contemplated.

A possible failing of the bargain theory of consideration is that it excludes detrimental reliance on a promise as a basis for enforcement. A promise which is relied upon in such a way that the promisee would suffer harm in the event of breach would seem to have a better case for enforcement than one given in return for an unperformed or executory promise.[143] Yet an executory promise will constitute consideration, while detrimental reliance will not. This deficiency has, to some extent at least, been rectified through the development of equitable estoppel, which provides protection to a party who acts to his or her detriment on the faith of at least some non-contractual promises. The law of contract therefore shares the enforcement of promises with the law of equitable estoppel.[144] As we will see in Chapter 9, however, there is some doubt as to the breadth of application of equitable estoppel, and therefore, doubt as to the extent of the protection the law provides in relation to detrimental reliance on promises.

The function of consideration

[4.115] There are several possible rationales for the doctrine of consideration.[145] First, consideration can be seen as a means of distinguishing between fair and unfair transactions. Although the doctrine of consideration requires reciprocity, it does not function well as a means of ensuring fairness, since grossly inadequate consideration will suffice.[146]

Secondly, consideration may be seen as a means of assessing whether the parties intended their agreement to create legal obligations The Victorian Court of Appeal recently suggested that, although consideration and intention to create legal relations are treated as separate requirements, "the better view may be that the rules as to consideration supply the answer as to whether parties intend to enter into a legally binding bargain."[147] As the court went on to acknowledge, however, the presence of consideration is not a reliable indicator of an intention to create legal relations. Even where an agreement involves a clear exchange that satisfies the consideration requirement, the parties may expressly or impliedly signify that they do not intend to create legal relations or, alternatively, the context in which the transaction takes place may indicate that legal obligations are not intended.[148]

142 Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), pp 35–8. See [1.20].

143 Fuller and Perdue, "The Reliance Interest in Contract Damages: 1" (1936) 46 *Yale Law Journal* 52, 56.

144 See [9.170] and [9.235].

145 The doctrine has also been defended on less pragmatic grounds: Benson, "The Idea of Consideration" (2011) 61 *University of Toronto Law Journal* 241 and Chen-Wishart, "In Defence of Consideration" (2013) 13 *Oxford Commonwealth Law Journal* 209.

146 Collins, *The Law of Contract* (2nd ed, 1993), p 66. The latest edition of this book (4th ed, 2003) considers only harm prevention and wealth maximisation as potential rationales of consideration.

147 *Atco Controls Pty Ltd (in liq) v Newtronics Pty Ltd (recs & mgrs apptd) (in liq)* [2009] VSCA 238; (2009) 25 VR 411, [60], citing Shatwell, "The Doctrine of Consideration in the Modern Law" (1954) 1 *Sydney Law Review* 289, 314.

148 See further Chapter 5.

Thirdly, the doctrine of consideration might be thought to ensure that only transactions that enhance economic efficiency are enforced by the courts. But it is not true to say that the only promises worth enforcing from an economic point of view are those involving an exchange. The enforcement of gratuitous promises can also have significant economic benefits.[149]

Fourthly, the doctrine of consideration operates to limit the involvement of the state in voluntary undertakings.[150] The bargain theory of consideration provides, in effect, that the state will only involve itself in the enforcement of those voluntary undertakings that form part of an exchange.[151] The doctrine of consideration might therefore be thought desirable from a libertarian point of view because it limits the intervention of the state in the lives of its citizens.[152] It may also be thought desirable from an economic point of view because it limits the amount of litigation and therefore the cost of the judicial system. It is said that if gratuitous undertakings were actionable, the courts would be asked to enforce a significant number of promises concerning trivial matters.[153]

Fifthly, consideration can be seen as fulfilling the function of a formal requirement such as writing, a seal or notorisation, without subjecting contracting parties to the inconvenience of those requirements.[154] The presence of consideration provides evidence that a promise has in fact been made and that it was intended to be legally binding. It is said that a claim that a promise has been made in return for some consideration is less likely to be based on mistaken or perjured testimony than a claim that a gratuitous promise has been made.[155] The consideration requirement is also said to protect impulsive or inadvertent promisors, since promises for valuable consideration are less likely to have been made without proper deliberation than gratuitous promises.[156] Kirby P suggested in *Beaton v McDivitt*[157] that the policy behind the law's insistence on consideration is that people sometimes make foolish and ill-considered promises, and the law should not hold them to those promises unless they have received some quid pro quo. Consideration does not provide an ideal test of seriousness, however, since exchanges are often made without deliberation, while some gratuitous promises are made with seriousness, caution and the expectation that they will be relied upon.[158] In any event, the requirement of intention to create legal relations, discussed in Chapter 5, directly addresses the issue of seriousness.

Hugh Collins suggests that the only occasion on which consideration does resemble a formal requirement is when parties have deliberately used nominal consideration to render a promise binding. The fact that the parties have gone to the trouble of making and identifying

149 See [9.235]; Posner, *Economic Analysis of Law* (9th ed, 2014), §4.2.

150 Collins, *The Law of Contract* (2nd ed, 1993), pp 41–2.

151 Although, as we will see in Chapter 9, the state also involves itself in the enforcement of voluntary undertakings that have been relied upon.

152 Collins, *The Law of Contract* (2nd ed, 1993), p 41.

153 See *Eastwood v Kenyon* (1840) 11 Ad & El 438, 450–1; 113 ER 482, 487; Posner, *Economic Analysis of Law* (9th ed, 2014), §4.2.

154 Patterson, "An Apology for Consideration" (1958) 58 *Columbia Law Review* 929, 949–50; Collins, *The Law of Contract* (2nd ed, 1993), p 62. As to the functions of formal requirements, see [7.05].

155 Fuller, "Consideration and Form" (1941) 41 *Columbia Law Review* 799, 799.

156 Fuller, "Consideration and Form" (1941) 41 *Columbia Law Review* 799, 799; Patterson, "An Apology for Consideration" (1958) 58 *Columbia Law Review* 929.

157 *Beaton v McDivitt* (1987) 13 NSWLR 162, 169.

158 Collins, *The Law of Contract* (2nd ed, 1993), p 62.

an artificial exchange indicates that they intend to be legally bound.[159] Consideration can then be seen as a formal requirement, like the requirement of writing, which alerts parties to the fact that they are entering into a serious transaction. As Karl Llewellyn points out, the courts' acceptance of nominal consideration operates effectively as a formal requirement when the promises to be enforced are socially desirable. However, the focus of the courts on formal equivalency, rather than *actual* equivalency, in an exchange tends to obscure problems arising from a discrepancy in bargaining power between the parties.[160] Where a party in a superior bargaining position is able to extract a substantial promise from a party in an inferior bargaining position, the making of a nominal exchange may simply disguise the unfairness of the transaction.

PROMISES UNDER SEAL

[4.120] A promise which is not supported by consideration will nevertheless be enforceable at common law if it is made under seal. Dixon CJ was referring to this rule in *Ballantyne v Phillott* when he said that, if the plaintiff had overcome his prejudice against solicitors, then a seal would have been affixed to the agreement and the consideration point would not be available to him.[161] A contract under seal is commonly known as a *deed* and more rarely as a *specialty* contract. It is an agreement recorded in a particular form, which traditionally involved sealing and delivery, although the common law requirements have been modified by statute in most Australian jurisdictions.[162] The solemnity of that form is recognised by the courts as a justification for enforcing a promise in the absence of consideration. Contracts which are not under seal, and which therefore require consideration to be binding, are sometimes described as *simple* or *informal* contracts. Trebilcock notes that the institution of the seal "has been repealed by statute in about two-thirds of the American states".[163] He observes that the ability to make a gratuitous promise binding by using a seal is clearly justified on autonomy grounds but more difficult to rationalise on the basis of economic efficiency.[164] In any case, deeds are commonly used in Australia to ensure the enforceability of promises where there is some doubt as to whether consideration is being provided by the promisee, such as a guarantee or an agreement to compromise a disputed claim.

159 Collins, *The Law of Contract* (2nd ed, 1993), p 62.

160 Llewellyn, "What Price Contract – An Essay in Perspective" (1931) 40 *Yale Law Journal*, 704, 744.

161 *Ballantyne v Phillott* (1961) 105 CLR 379, 389.

162 See Seddon, *Seddon on Deeds* (2015).

163 Trebilcock, *The Limits of Freedom of Contract* (1993), p 170.

164 Trebilcock, *The Limits of Freedom of Contract* (1993), pp 170–3.

CHAPTER **5**

Intention

[5.05] The third requirement in the formation of a contract is that the parties must manifest an intention to create legal relations. There is a considerable overlap between this and the offer and acceptance requirement. As we saw in Chapter 3, a party will only be regarded as making an offer or an acceptance if that party manifests an intention to be legally bound. The requirement is also closely related to the doctrine of consideration. Whether the parties appeared to intend to create a binding agreement is relevant to the question whether a bargain has been struck and each party has "paid for" the promises made by the other. It has been argued that the doctrine of consideration provides the essential test of enforceability in the common law and it is unnecessary to make a separate inquiry as to whether the parties appeared to intend to be bound.[1] It is clear, however, that not all agreements involving valuable exchanges will be enforced. Although satisfaction of the requirement goes without saying in most cases, there is no doubt that a contract will not be made if the parties to an agreement appear not to have intended to create legal obligations.

THE OBJECTIVE APPROACH

[5.07] In accordance with the objective approach to contract formation discussed earlier,[2] the court is concerned with whether the parties manifested an intention to create legal relations and not with whether they actually intended to do so.[3] It is not open to a party to escape a contract by saying that he or she did not intend to be bound. In *Merritt v Merritt*, Lord

1 See Lucke, "The Intention to Create Legal Relations" (1970) 3 *Adelaide Law Review* 419, 419; Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [5.1]; Heydon, *Heydon on Contract* (2019), [4.30]–[4.40].

2 See [1.25], [3.75] and [3.140].

3 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 105–6.

Denning MR said that "the court does not try to discover the intention by looking into the minds of the parties. It looks at the situation in which they were placed and asks itself: Would reasonable people regard the agreement as intended to be binding?"[4] This approach was confirmed by Gaudron, McHugh, Hayne and Callinan JJ in *Ermogenous v Greek Orthodox Community of SA Inc* (*Ermogenous*):

> Although the word "intention" is used in this context, it is used in the same sense as it is used in other contractual contexts. It describes what it is that would objectively be conveyed by what was said or done, having regard to the circumstances in which those statements and actions happened. It is not a search for the uncommunicated subjective motives or intentions of the parties.[5]

In *Air Great Lakes Pty Ltd v K S Easter (Holdings) Pty Ltd* (*Air Great Lakes*),[6] Mahoney and McHugh JJA held that where a written agreement is alleged to form a contract, the court may look beyond the terms of the document to determine whether the agreement was intended to create legal relations. The court may also take into account the surrounding circumstances, including the actions and statements of the parties.[7] In *Air Great Lakes*, Mahoney JA noted the general rule that a party (A) cannot set up a subjective intention not to contract where a reasonable person in the position of the other party (B) would assume A intended to be bound. Mahoney JA suggested, however, that a subjective intention by one party (A) not to be bound *will* prevent a contract arising where that subjective intention is known to the other party (B). If, for example, A was play-acting and B knew of that, Mahoney JA suggests, a contract between them will not be formed even if the circumstances otherwise indicate an intention to be bound. This conclusion can, however, be justified on a purely objective approach, since the means by which B knew that A was play-acting will form part of the surrounding circumstances to be taken into account under the objective approach. The words, gestures or background facts (such as A's propensity for practical jokes) which revealed A's true intentions to B would be taken into account under an objective approach.[8] It is difficult to envisage a plausible situation in which A's true meaning would be understood by B, but not by a reasonable person in B's position.

The factors that are taken into account in determining whether the parties intended legal relations vary from case to case but may include "the subject-matter of the agreement, the status of the parties to it, their relationship to one another, and other surrounding circumstances".[9] The less precise the arrangement, the less likely it is that a reasonable person would consider that the parties intended it to be legally enforceable.[10] *Shahid v Australasian College of Dermatologists*[11] nicely illustrates the kinds of factors that are commonly taken into account, as well as those that are irrelevant under the objective approach. Dr Shahid made a number of unsuccessful applications to the College for a training position in dermatology. The College provided a process by which an unsuccessful applicant could, on payment of a fee, appeal against such a decision. Details of the process were set out in a training handbook published

4 *Merritt v Merritt* [1970] 1 WLR 1211, 1213.
5 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 105–6 (footnote references omitted).
6 *Air Great Lakes Pty Ltd v K S Easter (Holdings) Pty Ltd* (1985) 2 NSWLR 309.
7 *Air Great Lakes Pty Ltd v K S Easter (Holdings) Pty Ltd* (1985) 2 NSWLR 309, 332–4, 337–8.
8 See *Air Great Lakes Pty Ltd v K S Easter (Holdings) Pty Ltd* (1985) 2 NSWLR 309, 337–9.
9 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 105.
10 *Ashton v Pratt* [2015] NSWCA 12; (2015) 88 NSWLR 281, [91] and [231]–[232].
11 *Shahid v Australasian College of Dermatologists* [2008] FCAFC 72; (2008) 168 FCR 46.

by the College. Dr Shahid lodged appeals against the decisions made against her. The issue was whether each time she lodged an appeal and paid the stipulated appeal fee, Dr Shahid had entered into a contract with the College. The trial judge found that the intention to create legal relations requirement was not satisfied because, among other things, the College "regarded itself as so unfettered by any contractual concerns as to be able to substitute some other form of outcome of the appeal other than the one which would normally be anticipated, namely, the substitution of a successful appellant for the person originally selected".[12] On appeal, the Full Court held that the trial judge was wrong to have taken account of the College's "uncommunicated intentions" as to what it "regarded itself" as free to do. It was clear from the "objective state of affairs" that the outcomes available to the college were limited: they were "set out in very conventional terms in the training handbook".[13] The Full Court found that the parties did manifest an intention to create legal relations. The training program was regarded by the College as "a subject of the greatest importance" and the "handbooks were both detailed and comprehensive". The context of the transaction was "a businesslike one" involving a "weighty" subject matter; namely, a demanding professional training program which was the principal means by which the College established and maintained standards within the profession.[14] In relation to the appeals themselves, Dr Shahid paid substantial fees in return for the College's promise that there would be an appeal with certain specified characteristics. The handbook set out in a detailed and systematic manner the grounds of appeal, the process that would be followed and the powers of the appeals committee.[15] Jessup J (with whom Branson and Stone JJ agreed) said:

> Where one party makes, and the other party accepts, a money payment as consideration for a promise by the other to provide some service or to bestow some benefit, the proposition that each intended the promise to be taken seriously and to carry the conventional legal consequences does seem rather obvious. This is not a case with unusual or idiosyncratic features. Here the parties were at arm's length. Their only relationship was that constituted by the training program as a whole and by the appellant's status as a provisional trainee. That the disinterested bystander would think that the appellant would pay, and that the College would accept, a fee in the sum of $1,500 or $5,000 (plus GST in each case) without any intention that the College would, as a matter of law and not only in honour, be obliged to perform its promise seems quite improbable.

Although the conduct of the parties after the making of the agreement may be taken into account in determining whether the parties intended to be bound, conduct which does no more than indicate the subjective intentions of one of the parties is not likely to be of assistance. A helpful case on this point is *Atco Controls Pty Ltd (in liq) v Newtronics Pty Ltd (recs & mgrs apptd) (in liq)*, which was discussed in Chapter 4.[16] Atco provided a series of annual "letters of support" to its subsidiary (Newtronics) in which Atco confirmed that it would not to seek to recover debts owed by Newtronics to the detriment of other creditors and would provide sufficient funds to Newtronics to enable Newtronics to meet its trading debts.[17] These

12 *Shahid v Australasian College of Dermatologists* [2008] FCAFC 72; (2008) 168 FCR 46, [209].

13 *Shahid v Australasian College of Dermatologists* [2008] FCAFC 72; (2008) 168 FCR 46, [209].

14 *Shahid v Australasian College of Dermatologists* [2008] FCAFC 72; (2008) 168 FCR 46, [214].

15 *Shahid v Australasian College of Dermatologists* [2008] FCAFC 72; (2008) 168 FCR 46, [216].

16 See [4.35].

17 *Atco Controls Pty Ltd (in liq) v Newtronics Pty Ltd (recs & mgrs apptd) (in liq)* [2009] VSCA 238; (2009) 25 VR 411.

letters were prepared for the purposes of Newtronics' annual audit and were necessary in order for Newtronics to be presented in its accounts as a solvent, going concern.[18] The trial judge found that the letters of support were intended to be binding, even though they were not mentioned in Atco's accounts. On appeal, counsel for Atco argued that the trial judge should have taken into account the fact that Atco's accounts did not refer to any obligations in relation to the letters of support. The Court of Appeal observed that, while it is permissible to consider all of the conduct of the parties in order to determine whether a binding agreement could be inferred from that conduct, whatever was said in the accounts could amount to little more than the directors' subjective interpretation of what had occurred.[19]

> Since the existence and effect of a legally binding agreement is to be determined objectively according to what a reasonable person would take to be the intent of the parties as evidenced by their actions in the circumstances of the case, and not according to the subjective interpretations of the parties, what the Atco directors thought to be the effect of what had occurred was largely irrelevant.[20]

PRESUMPTIONS

[5.10] The intention requirement has traditionally been approached on the basis that agreements made in a commercial context are presumed to be made with an intention to create legal relations, while agreements made in other contexts are not presumed to be made with such an intention. It was even said in some cases that there was a presumption *against* an intention to create legal relations in the case of certain transactions between family members.[21] These presumptions made by the courts establish the onus of proof in relation to intention. In the case of a commercial transaction, the courts will assume that the parties intend the contract to be legally binding. The burden of disproving intention is therefore on a person denying the enforceability of such a transaction. In the case of non-commercial transactions, an intention to create legal obligations is not presumed. Accordingly, in such cases, the onus rests on the person seeking to enforce such an agreement to convince the court that the parties did manifest an intention to be bound.

In *Ermogenous v Greek Orthodox Community of SA Inc*,[22] Gaudron, McHugh, Hayne and Callinan JJ expressed the need for caution in using presumptions in relation to this aspect of contract formation. Referring to the suggestion that an intention to create legal relations should not be presumed in relation to the engagement of a minister of religion, they said: "For our part, we doubt the utility of using the language of presumptions in this context. At best, the use of that language does no more than invite attention to identifying the party who bears the onus of proof."[23]

It is not entirely clear whether their Honours meant to cast doubt on the utility of presumptions in the context of the engagement of a minister of religion or in the broader

18 See *Newtronics Pty Ltd (recs & mgrs appd) (in liq) v Atco Controls Pty Ltd (in liq)* [2008] VSC 566, [9]–[12].

19 *Atco Controls Pty Ltd (in liq) v Newtronics Pty Ltd (recs & mgrs apptd) (in liq)* [2009] VSCA 238; (2009) 25 VR 411, [44]. The Court of Appeal overturned the trial judge's decision on other grounds. See [4.35].

20 *Atco Controls Pty Ltd (in liq) v Newtronics Pty Ltd (recs & mgrs apptd) (in liq)* [2009] VSCA 238; (2009) 25 VR 411, [44].

21 For example, *Jones v Padavatton* [1969] 1 WLR 328, 332, discussed at [5.45].

22 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 105–6.

23 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 106.

context of the intention to create legal relations requirement. The tenor of the judgment suggests the latter. Their Honours expressed concern that a presumption that legal relations are not intended in a particular context could "ossify into a rule of law" that there cannot be a contract in such a context.[24] Such a proposition would, they said, distort "the proper application of basic principles of the law of contract".[25] Their Honours said that it would be wrong to formulate rules prescribing the types of cases in which an intention to create legal relations should or should not be found to exist.[26]

In light of the *Ermogenous* decision, it is suggested that the role of presumptions in relation to the intention requirement is as follows. A person who claims that a contract has been made bears the onus of establishing the elements of formation. Where the other party denies the existence of a legally binding contract, then the person alleging the existence of a contract must satisfy the court that the parties manifested an intention to create legal relations.[27] If the transaction is a commercial one, then the context will usually indicate that legal relations were intended, so the party denying the existence of a contract must convince the court that the parties did not intend to create legal relations. In other contexts, no presumption will be made.

Although there were some post-*Ermogenous* cases in which it was presumed that agreements made between people in domestic or social relationships were not intended to create legal relations,[28] the New South Wales Court of Appeal and the Full Court of the Federal Court of Australia have since held that no such presumption should be made.[29] Whether the parties have manifested an intention to create legal relations is to be considered objectively, without the use of any presumptions, although the nature of the relationship between the parties and the context in which the agreement was made remain important considerations and may even be decisive in some cases.[30]

COMMERCIAL TRANSACTIONS

Presumption of legal enforceability

[5.15] The courts have, in some cases, adopted a "strong presumption" that commercial transactions are intended to create legal obligations, which "will only be rebutted with difficulty."[31] This means that a person seeking to deny the enforceability of a commercial transaction bears a heavy onus in proving that it was not intended to be binding[32] and there are few reported cases in which a party has even attempted to discharge that onus. The reason

24 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 106.

25 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 106.

26 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 105.

27 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 106.

28 For example, *Darmanin v Cowan* [2010] NSWSC 1118, [206]–[208]; *Sion v NSW Trustee and Guardian* [2012] NSWSC 949, [71] (upheld [2013] NSWCA 337).

29 *Ashton v Pratt* [2015] NSWCA 12; (2015) 88 NSWLR 281, [73]; *Evans v Secretary, Department of Families, Housing, Community Services and Indigenous Affairs* [2012] FCAFC 81, [12]–[16].

30 *Ashton v Pratt* [2015] NSWCA 12; (2015) 88 NSWLR 281, [73]; *Evans v Secretary, Department of Families, Housing, Community Services and Indigenous Affairs* [2012] FCAFC 81, [16].

31 *Helmos Enterprises Pty Ltd v Jaylor Pty Ltd* [2005] NSWCA 235, [48].

32 *Edwards v Skyways* [1964] 1 All ER 494, 500; *Banque Brussels Lambert SA v Australian National Industries Ltd* (1989) 21 NSWLR 502, 521; *Helmos Enterprises Pty Ltd v Jaylor Pty Ltd* [2005] NSWCA 235, [48]. Cf *Gate Gourmet Australia Pty Limited (in liq) v Gate Gourmet Holding AG* [2004] NSWSC 149, [213].

for this is obvious: in most cases, there is no question that a commercial agreement was intended to have a legal effect.[33] It is unclear whether the scepticism about presumptions expressed in *Ermogenous* will affect the approach taken to commercial cases. Whether or not a presumption is made, the commercial context will usually indicate that legal relations were intended and the party denying the existence of a contract will need to show that the parties manifested an intention not to create legal relations. The question whether commercial parties intended to create legal relations has arisen in a number of cases involving letters of comfort. A letter of comfort is a document given to a financier in a situation in which a guarantee might otherwise be given. Typically a letter of comfort will be given when a bank is lending to a company which is a subsidiary of a larger company (the parent company). The bank is concerned about the subsidiary's financial strength and is reluctant to lend to the subsidiary without some assurance that the parent company will support its subsidiary. The parent company is reluctant to give a guarantee because its contingent liability under the guarantee would affect its balance sheet. The parent company therefore provides a letter of comfort, which offers some assurance to the bank without creating a clear liability. The legal status of the document may be deliberately left unclear so that both parties can proceed with the transaction. It has been said in England that, "in the search for agreed terms of a commercial transaction, business men may adopt language of deliberate equivocation in the hope that all will go well".[34]

In *Banque Brussels Lambert SA v Australian National Industries Ltd*,[35] a letter of comfort was given by Australian National Industries Ltd (ANI), a public company listed on the stock exchange, in relation to a US$5m loan facility provided by the bank to Spedley Securities Ltd (SSL). ANI held a controlling interest in Spedley's parent company, Spedley Holdings Ltd (SHL). It provided a strongly worded letter of comfort at the bank's insistence after considerable negotiations and the exchange of several drafts. In the letter, ANI consented to the making of the loan and agreed to provide the bank with 90 days' notice of any decision to dispose of its interest in SHL. The letter also said:

> We take this opportunity to confirm that it is our practice to ensure that our affiliate Spedley Securities Ltd, will at all times be in a position to meet its financial obligations as they fall due. These financial obligations include repayment of all loans made by your Bank under the arrangements mentioned in this letter.

ANI disposed of its shareholding in SHL without giving the required notice to the bank. SSL was unable to repay the debt to the bank and later went into liquidation. The bank sued ANI for damages for breach of the agreement. ANI denied liability on the basis that the parties did not manifest an intention to create legal relations. In the Supreme Court of New South Wales, Rogers CJ was influenced by the "refreshingly honest and sensible French approach to letters of comfort".[36] In French law, a letter of comfort will be regarded as a commitment to perform since the creation of a meaningless instrument in the commercial world is unthinkable.[37] Rogers CJ applied the presumption that parties to commercial agreements intend them to have legal effect:

33 *Gate Gourmet Australia Pty Limited (in liq) v Gate Gourmet Holding AG* [2004] NSWSC 149, [213].

34 *Kleinwort Benson Ltd v Malaysia Mining Corp Bhd* [1989] 1 WLR 379, 383.

35 *Banque Brussels Lambert SA v Australian National Industries Ltd* (1989) 21 NSWLR 502.

36 *Banque Brussels Lambert SA v Australian National Industries Ltd* (1989) 21 NSWLR 502, 521.

37 But compare the insights provided by empirical research such as that of Macaulay, at [1.105]–[1.125].

> There should be no room in the proper flow of commerce for some purgatory where statements made by businessmen, after hard bargaining and made to induce another business person to enter into a business transaction would, without any express statement to that effect, reside in a twilight zone of merely honourable engagement. The whole thrust of the law today is to attempt to give proper effect to commercial transactions. It is for this reason that uncertainty, a concept so much loved by lawyers, has fallen into disfavour as a tool for striking down commercial bargains. If the statements are appropriately promissory in character, courts should enforce them when they are uttered in the course of business and there is no clear indication that they are not intended to be legally enforceable.[38]

Rogers CJ held that the letter given by ANI included enforceable contractual promises to provide notice of its intention to dispose of its interest in SHL and to ensure that SSL would be in a position to repay the bank.[39] The bank was therefore entitled to damages for ANI's breaches of these promises. A similarly strongly worded letter of comfort was also held to have contractual force in a more recent case discussed at [11.23].[40] Much depends on the language used in the document, however, and there have been several cases in which less strongly worded letters have been held not to give rise to legal obligations. In *Kleinwort Benson Ltd v Malaysia Mining Corp Bhd*,[41] the English Court of Appeal held that the presumption that legal relations are intended arises only when the words used in the relevant document can be treated as a contractual promise. Where a statement made in a commercial document does not appear to have been intended as a contractual promise, the onus lies on the party alleging a contract to show that the statement was intended as a contractual promise.[42] The letter of comfort in that case could not be regarded as having been intended to contain a contractual promise.[43] Similarly, in *Commonwealth Bank of Australia v TLI Management Pty Ltd*,[44] Tadgell J of the Supreme Court of Victoria held that the letter of comfort before him contained statements of fact, rather than promises, and therefore did not give rise to an enforceable agreement. In *Australian European Finance Corporation v Sheahan*,[45] Matheson J concluded that a letter of comfort was not intended to create legal relations where the wording was not discussed in advance, there was no evidence of reliance by the lender, the letter was "clearly intended to be ambiguous" and the expressions were "vague" and "woolly".

Non-binding commercial agreements

[5.20] Since the creation of legal relations is a matter of manifested intention, it is clear that parties can, if they wish, enter into a non-binding commercial agreement. The courts will give effect to an express stipulation that an agreement is not to be legally binding. Such provisions are sometimes described as *honour clauses*, since they expressly or implicitly provide that the

38 *Banque Brussels Lambert SA v Australian National Industries Ltd* (1989) 21 NSWLR 502, 523.

39 *Banque Brussels Lambert SA v Australian National Industries Ltd* (1989) 21 NSWLR 502, 525–6.

40 *Gate Gourmet Australia Pty Limited (in liq) v Gate Gourmet Holding AG* [2004] NSWSC 149. See also *Anglican Development Fund Diocese of Bathurst v Palmer* [2015] NSWSC 1856; (2015) 336 ALR 372, where a more strongly worded letter of comfort was held to be binding.

41 *Kleinwort Benson Ltd v Malaysia Mining Corp Bhd* [1989] 1 WLR 3791.

42 *Kleinwort Benson Ltd v Malaysia Mining Corp Bhd* [1989] 1 WLR 3791.

43 *Kleinwort Benson Ltd v Malaysia Mining Corp Bhd* [1989] 1 WLR 3791, 393.

44 *Commonwealth Bank of Australia v TLI Management Pty Ltd* [1990] VR 510.

45 *Australian European Finance Corporation v Sheahan* (1993) 60 SASR 187, 206.

agreement will be binding in honour only. In *Rose & Frank Co v J R Crompton & Bros Ltd*,[46] the House of Lords recognised the effectiveness of an honour clause. The clause was contained in an agreement made between a manufacturer and a distributor, which gave the distributor the right to sell the manufacturer's product for a stipulated period. The agreement contained an "honourable pledge clause", which provided that the agreement was not entered into as a legal agreement and was not subject to legal jurisdiction, but simply recorded the parties' purpose and intention "to which they each honourably pledge themselves". The distributor sought damages for breach of contract when the manufacturer terminated the distribution agreement without giving the stipulated period of notice.

In the English Court of Appeal, Scrutton LJ said that an intention not to create legal relations may be implied from an agreement but may also be expressed by the parties. There is no reason why parties to a business agreement may not decide to "rely on each other's good faith and honour" and to exclude all outside intervention in the settlement of disputes.[47] Although the distribution agreement was held not to be binding, and the manufacturer was not obliged to accept orders from the distributor, each individual order was held to give rise to a separate contract when accepted by the manufacturer.[48]

It is important to note that it is only permissible to exclude the jurisdiction of the courts in relation to an agreement that is not binding on the parties. Where an agreement is made binding, any attempt to oust the jurisdiction of the courts is contrary to public policy and will be void.[49]

AGREEMENTS BETWEEN FAMILY MEMBERS

[5.25] It will be recalled that in *Ermogenous v Greek Orthodox Community of SA Inc*,[50] Gaudron, McHugh, Hayne and Callinan JJ expressed the concern that a presumption (that in certain situations "an intention to create legal relations is not to be presumed") might harden into a rule of law (that agreements made in such situations usually "will not give rise to legally enforceable obligations").[51] This appears to have occurred in the domestic context, where the principle that an intention to create legal relations is not to be presumed seems to have made it difficult to establish a contract between spouses, even where the agreement in question involves substantial financial matters. Since *Ermogenous*, however, agreements made in a domestic context must be considered in a different way.[52] Indeed, there is a good case for saying that family, domestic or social agreements should no longer be regarded as constituting a distinct legal category.[53] The relationship between the parties is simply one of the factors to be taken into account in determining whether the intention requirement is satisfied. Outside the commercial context, the onus is clearly on the person alleging the existence of a contract to satisfy the court that the parties manifested an intention to create legal relations. Whether

46 *Rose & Frank Co v J R Crompton & Bros Ltd* [1925] AC 445.

47 Rose & Frank Co v J R Crompton & Bros Ltd [1923] 2 KB 261, 288.

48 *Rose & Frank Co v J R Crompton & Bros Ltd* [1925] AC 445, 455.

49 See [41.110].

50 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95; see [5.10].

51 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 106.

52 See [5.10].

53 Cf Keyes and Burns, "Contract and the Family: Whither Intention?" (2002) 26 *Melbourne University Law Review* 577, esp at 580–1.

parties have manifested an intention to create legal relations must be decided on the facts of each case, taking into account all relevant circumstances. The relevant circumstances include the subject matter of the agreement and the relationship between the parties, but there is no legal rule that domestic or social agreements or agreements between spouses are not usually intended to be binding.[54] Each case must be decided on its own facts, and no presumption should be made about contractual intentions with respect to family arrangements.[55]

Financial agreements between spouses

[5.30] In *Balfour v Balfour*,[56] a married couple had been living in Ceylon where the man worked. Following a holiday in England, the woman was unable to return to Ceylon for health reasons. The man promised to pay her a living allowance of £30 per month until she could join him. The couple later agreed to remain apart and the woman sued to recover amounts due under the agreement. The English Court of Appeal held that the agreement was not intended to be enforceable. Atkin LJ noted that arrangements are often made between husband and wife involving mutual promises and consideration. "Nevertheless they are not contracts, and they are not contracts because the parties did not intend that they should be attended by legal consequences".[57] Atkin LJ said:

> The common law does not regulate the form of agreements between spouses. Their promises are not sealed with seals and sealing wax. The consideration that really obtains for them is that natural love and affection which counts for so little in these cold courts. … In respect of these promises each house is a domain into which the King's writ does not seek to run, and to which his officers do not seek to be admitted.[58]

The idea that the "King's writ does not seek to run" into the domestic domain is clearly inconsistent with the neutral approach to the intention requirement articulated by the High Court in *Ermogenous*.[59] Even if the case is now of academic interest only, that interest is considerable from the point of view of a feminist analysis of law. The decision in *Balfour v Balfour*, and the quoted passage of Atkin LJ's judgment in particular, is a striking example of the tendency of the law to draw a distinction between public and private spheres.[60] Feminists have shown that the idea of the family as a "private" sphere in which the law does not intrude is illusory. Family life is regulated by direct means, such as family and criminal law, for example, and in many other indirect ways.[61] The report into the separation of Aboriginal children from their families shows the extent of the state's reach into Aboriginal family life.[62] The family

54 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 105–6.

55 *Ashton v Pratt* [2015] NSWCA 12; (2015) 88 NSWLR 281, [73]; *Evans v Secretary, Department of Families, Housing, Community Services and Indigenous Affairs* [2012] FCAFC 81, [16].

56 *Balfour v Balfour* [1919] 2 KB 571.

57 *Balfour v Balfour* [1919] 2 KB 571, 579.

58 *Balfour v Balfour* [1919] 2 KB 571, 579.

59 Cf *Magill v Magill* [2006] HCA 51; (2006) 226 CLR 551, 614, where Heydon J referred in passing to *Balfour v Balfour* with apparent approval.

60 See, eg, Graycar and Morgan, *The Hidden Gender of Law* (2nd ed, 2002), pp 15–24; Thornton (ed), *Public and Private: Feminist Legal Debates* (1995).

61 See, eg, Olsen, "The Myth of State Intervention in the Family" (1985) 18 *Michigan Journal of Law Reform* 835.

62 Graycar and Morgan, *The Hidden Gender of Law* (2nd ed, 2002), p 20, referring to Human Rights and Equal Opportunities Commission, *Bringing Them Home: Report of the National Inquiry into the Separation of Aboriginal and Torres Strait Islander Children from their Families* (1997).

cannot, therefore, be regarded as a "private" sphere that is free of legal intervention. It is somewhat paradoxical that the sphere regarded as too private for contract law is regulated by areas of law that are more explicitly concerned with the implementation of public norms.[63]

The mapping of a private sphere that is for some purposes free of state intervention has complicated effects on those imagined to inhabit that sphere.[64] In *Balfour v Balfour*, the refusal of the court to enforce an agreement between a woman and a man on whom she was financially dependent reinforced masculine dominance of the "private" domain. But to argue that greater legal intervention in the "private" sphere would serve the interests of women is overly simplistic. For example, as Graycar and Morgan point out, the intervention of the state in the domestic lives of Aboriginal women has clearly been detrimental to them and their children.[65] Similarly, the recognition of pre- and post-nuptial financial agreements between married couples under the *Family Law Act 1975* (Cth), discussed below, may also prove disadvantageous to some women, since the procedural safeguards provided by the legislation are unlikely to overcome the problems resulting from inequality of bargaining power.[66]

Agreements between spouses who are separating

[5.35] The courts have been more willing to find an intention to create legal relations where the parties are separated or about to separate. In *Merritt v Merritt*,[67] for example, an agreement was made between a married couple after they had separated. The man signed a document in which he agreed to pay the woman £40 per month and to transfer his interest in the matrimonial home to her if she paid all charges in connection with the house until the mortgage had been repaid. The English Court of Appeal held that although domestic arrangements between spouses "living in amity" are not ordinarily intended to create legal relations, it is altogether different when the parties are separated or about to separate.[68] It may then "safely be presumed that they intend to create legal relations".[69]

Family Law Act 1975 (Cth)

[5.40] The *Family Law Act 1975* (Cth) makes specific provision for parties to marriages (Pt VIIIA) and de facto relationships (Pt VIIIAB, Div 4) to make agreements relating to their financial affairs. The provisions cover agreements relating to matters such as the distribution of property in the event of the breakdown of the marriage or relationship and agreements for the maintenance of one of the parties during or after dissolution or breakdown.[70]

63 Shultz, "The Gendered Curriculum: Of Contracts and Careers" (1991) 77 *Iowa Law Review* 55, 59–61.

64 See Orford, "Liberty, Equality, Pornography: The Bodies of Women and Human Rights Discourse" (1994) 3 *Australian Feminist Law Journal* 72.

65 Graycar and Morgan, *The Hidden Gender of Law* (2nd ed, 2002), p 20.

66 Neave, "Private Ordering in Family Law – Will Women Benefit?" in Thornton (ed), *Public and Private: Feminist Legal Debates* (1995), p 144; Graycar and Morgan, *The Hidden Gender of Law* (2nd ed, 2002), pp 111–3; Fehlberg and Smyth, "Pre-nuptial Agreements for Australia: Why Not?" (2000) 14 *Australian Journal of Family Law* 80. See also Fehlberg and Smyth, "Binding Prenuptial Agreements in Australia: The First Year" in Mulcahy (ed), *Feminist Perspectives on Contract Law* (2005), p 125.

67 *Merritt v Merritt* [1970] 1 WLR 1211.

68 [*Merritt v Merritt* 1970] 1 WLR 1211, 1213–4.

69 *Merritt v Merritt* [1970] 1 WLR 1211, 1213.

70 *Family Law Act 1975* (Cth), ss 90B, 90D, 90UB–90UD. For further discussion, see Fehlberg et al, *Australian Family Law: The Contemporary Context* (2nd ed, 2015), section 14.7.

The provisions would cover both the agreement in *Balfour v Balfour* and that in *Merritt v Merritt*. An agreement made under Pt VIIIA or Pt VIIIAB is binding on the parties if it is expressed to be made under the relevant section, is signed by both parties and includes a certificate that both parties have received independent legal advice.[71] Whether such an agreement is enforceable is to be determined in accordance with the principles of law that govern the enforceability of contracts generally.[72] Thus, the normal requirements of contractual validity must be met, including the requirement of a manifested intention to create legal relations. If the requirements mentioned above have been satisfied, however, it would seem impossible to argue that the agreement was not intended to create legal relations. In *Thorne v Kennedy*, the High Court held that the pre and post-nuptial agreements made between the parties to that case were voidable on the basis of undue influence and unconscionable dealing.[73]

Other arrangements between family members

[5.45] The restrictive approach taken in *Balfour v Balfour* has been adopted in relation to agreements between other family members. In *Jones v Padavatton*,[74] it was applied to deny enforceability to a mother's promise to pay $200 per month to her adult daughter to allow her go to England to read for the bar. All three members of the Court of Appeal adopted what Danckwerts LJ described as Atkin LJ's "magnificent exposition of the situation" in *Balfour v Balfour*.[75] A factual presumption "against" an intention to create legal relations was adopted, which was derived from "experience of human nature which shows that in such circumstances men and women usually do not intend to create legal rights and obligations".[76] The fact that the arrangement required the daughter to give up a well-paid job in Washington and move to England was not sufficient to rebut the presumption. This intended reliance by the daughter was said not to show that the parties intended their arrangement to have legal consequences, but only that the daughter was "prepared to trust her mother to honour her promise of support".[77] If a similar case arose in Australia today, the reasoning of the High Court in *Ermogenous* would require the court to approach the question of intention in relation to an agreement between family members from a more neutral starting point.[78]

An intention to create legal relations has been found in a series of cases involving promises relating to housing. In *Todd v Nichol*,[79] the defendant, a woman living in Australia,

71 *Family Law Act 1975* (Cth), ss 90B, 90D, 90G, 90UB–90UD and 90UJ. A court may declare an agreement binding even though it was made in the absence of independent legal advice if the court is satisfied that it would be unjust and inequitable if the agreement were not binding: *Family Law Act 1975* (Cth), ss 90G(1A) and 90UJ(1A).

72 *Family Law Act 1975* (Cth), ss 90KA and 90UN. The Act does, however, set out certain circumstances in which the agreement may be set aside (ss 90K and 90UM).

73 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85; see further [35.20].

74 *Jones v Padavatton* [1969] 1 WLR 328.

75 *Jones v Padavatton* [1969] 1 WLR 328, 332.

76 *Jones v Padavatton* [1969] 1 WLR 328, 332.

77 *Jones v Padavatton* [1969] 1 WLR 328, 337.

78 *Ashton v Pratt* [2015] NSWCA 12; (2015) 88 NSWLR 281, [73]. Cf *Magill v Magill* [2006] HCA 51; (2006) 226 CLR 551, 614 (where Heydon J in obiter dicta referred to with apparent approval to *Jones v Padavatton and Balfour v Balfour*) and *Smilevska v Smilevska (No 2)* [2016] NSWSC 397, [143]–[155].

79 *Todd v Nichol* [1957] SASR 72.

invited the plaintiffs, the sister and niece of the defendant's deceased husband, to move from Scotland to Australia to share her house to provide her with company. The defendant proposed the arrangement in a letter to the plaintiffs. The defendant conceded that it was "a big thing" for the plaintiffs to do and therefore promised to alter her will so that the house would be theirs until they die. The plaintiffs accepted the offer and moved to Australia. They sold their belongings in Scotland and the niece resigned her employment. When the relationship broke down, the plaintiffs sought to enforce the contract. The defendant argued that, since the agreement was between relatives, it must be presumed to have been based in trust rather than legal obligation. Mayo J observed that, since there was no explicit statement that legally enforceable obligations were intended, it was necessary to inquire whether an inference could be drawn.[80] He held that the agreement contemplated a permanent arrangement and weight had to be given to an interpretation of the agreement that did not place the plaintiffs at the whim of the defendant.[81] He therefore held that an intention to enter into a legally binding contract should be attributed to the parties.

Similar arrangements have been held to be intended to create legal obligations in other cases.[82] Although these cases involved domestic arrangements, they also involved valuable property rights. The crucial factor in each of the cases has been the degree of reliance by the plaintiff on the agreement.[83] Given the serious consequences for the party taking up an invitation, it is difficult to imagine that step being taken without a binding commitment from the other party. Even in a domestic setting, an agreement that anticipates substantial reliance by one of the parties is likely to be intended to be binding. If such an agreement does not give rise to a contract but is relied upon by one party to his or her detriment, that party may be able to obtain relief by way of estoppel.[84]

Commercial agreements between family members

[5.50] The intention requirement will easily be satisfied where a transaction between family members is essentially commercial in nature. *Roufos v Brewster*[85] concerned an arrangement between Mr and Mrs Brewster and their son-in-law, Mr Roufos. The arrangement was that Roufos would take the Brewsters' truck from Coober Pedy to Adelaide on the back of his semi-trailer so that the truck could be repaired. It was agreed that Roufos would engage a driver to drive the truck back to Coober Pedy and could send back a load of goods on the truck if he wished. The truck was damaged on the return trip and the Brewsters sought to recover damages from Roufos for breach of contract. Bray CJ held that the agreement created a legal relationship. There was evidence of "intermittent hostility" between the parties, who entered into the agreement in pursuit of their separate commercial interests. Moreover, the "whole setting of the arrangement" was "commercial, rather than social or domestic".[86]

80 *Todd v Nichol* [1957] SASR 72, 79.

81 *Todd v Nichol* [1957] SASR 72, 79–80.

82 *Wakeling v Ripley* (1951) 51 SR (NSW) 183; *Parker v Clark* [1960] 1 All ER 93.

83 *Wakeling v Ripley* (1951) 51 SR (NSW) 183, 187; *Parker v Clark* [1960] 1 All ER 93, 100–1.

84 See Chapter 9.

85 *Roufos v Brewster* (1971) 2 SASR 218.

86 *Roufos v Brewster* (1971) 2 SASR 218, 222.

NON-COMMERCIAL ARM'S-LENGTH TRANSACTIONS

[5.55] Is the presumption that legal relations are intended to be made only in relation to commercial agreements? Many transactions are entered into between individuals, neither of whom is conducting a business, in circumstances where an intention to create legal relations might be presumed. Examples include the private sale of a house or car or an agreement to employ a person in a domestic capacity, such as a housekeeper or nanny. It may be that the presumption that parties intend legal enforceability is not restricted to commercial agreements but extends to all agreements involving substantial matters entered into between individuals at arm's length.[87] But such an approach would marginalise agreements between family members.[88] It may be that in all non-commercial cases, the onus in relation to intention remains on the person asserting the existence of a contract. In *Ermogenous*, Gaudron, McHugh, Hayne and Callinan JJ accepted that, where a contract was alleged to have arisen from the engagement of a minister of religion, the onus was on the minister to "demonstrate that there was a contract" and this seemed to include the need to satisfy the court that the parties manifested an intention to create legal relations.[89] The High Court held that the South Australian Supreme Court was wrong to draw an inference that legal relations were not intended. The clergy engaged by the respondent, and similar Australian bodies were treated as employees and the industrial magistrate was held not to have erred in concluding that a contract was made.[90]

GOVERNMENT AGREEMENTS

[5.60] Whether the court will conclude that an agreement entered into by a government is intended to be binding depends in part on whether the transaction is a commercial agreement or an arrangement involving the implementation of government policy.[91] In *Australian Woollen Mills Pty Ltd v Commonwealth*,[92] the Commonwealth Government was held not to have intended to assume a legal obligation to pay the promised subsidies to manufacturers of woollen products. The absence of such an intention was indicated by four factors. First, no statutory authority was sought for the making of the payments (as one would expect if a legal obligation was being assumed).[93] Secondly, the scheme was announced by persons who had no power to commit the Crown to any expenditure.[94] Thirdly, the Commonwealth had no commercial interest in the purchases of wool but was simply dealing with a problem created by war.[95] Fourthly, the Commonwealth expressly reserved the right to vary the amount of

87 Support for such a proposition can be found in *Rose & Frank Co v J R Crompton & Bros Ltd* [1923] 2 KB 261, 293 and Hedley, "Keeping Contract in Its Place – *Balfour v Balfour* and the Enforceability of Informal Agreements" (1985) 5 *Oxford Journal of Legal Studies* 391.

88 See Keyes and Burns, "Contract and the Family: Whither Intention?" (2002) 26 *Melbourne University Law Review* 577, who argue that a distinction should not even be drawn between family and commercial agreements.

89 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 106.

90 *Ermogenous v Greek Orthodox Community of SA Inc* [2002] HCA 8; (2002) 209 CLR 95, 111–2.

91 See further Seddon, *Government Contracts: Federal, State and Local* (6th ed, 2018), [3.2]–[3.7].

92 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424, discussed at [3.15] and [4.25]. See also *South Australia v Commonwealth* (1962) 108 CLR 130, 148–9, 153, 157.

93 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424, 461.

94 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424, 461.

95 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424, 460.

the subsidy.[96] The existence of such a discretion was inconsistent with the notion that the Commonwealth intended to assume a contractual obligation. The Privy Council agreed that the scheme was administrative, rather than contractual.[97] The lack of a formal agreement and the number of uncertain factors pointed to this conclusion, and the Privy Council thought it was not remarkable that manufacturers were content to rely on the Commonwealth's statement of policy.[98]

Another example of an agreement involving the implementation of policy is *Administration of Papua New Guinea v Leahy*.[99] Leahy had sought the help of the Department of Agriculture in dealing with a tick infestation on his cattle property. It was agreed that officers of the Department would spray Leahy's cattle and implement other eradication measures, and Leahy would provide workers to assist them in mustering and handling the cattle. When the eradication work was not carried out properly, Leahy sought damages for breach of contract. The High Court held that no binding contract had been made. The Department was simply providing gratuitous assistance in the execution of its policy to eradicate ticks.[100] "The work done by the Administration was analogous to a social service which generally does not have as its basis a legal relationship of a contractual nature."[101]

The two cases discussed above can be contrasted with *Placer Developments Ltd v Commonwealth*,[102] which involved an agreement between the Commonwealth and Placer to form a timber company to operate in Papua New Guinea. Clause 14 of the agreement provided that if customs duty was paid on the importation of the timber company's products into Australia, the Commonwealth would pay to the timber company a subsidy at a rate to be determined by the Commonwealth. Placer sought to enforce the agreement. As will be discussed in Chapter 6, the majority of the court, Taylor, Owen and Kitto JJ, held that clause 14 was unenforceable as an illusory promise[103] and did not address the question of intention. The dissenting judges, Menzies and Windeyer JJ, had no doubt that the agreement was intended to create legal relations. The language was that of legal obligation,[104] the agreement had an essentially commercial character and Parliament had approved the agreement and appropriated funds to meet the obligation.[105] These factors were "enough to rescue" the agreement "from the unenforceability which a purely political arrangement has, and to give it a commercial character".[106]

PRELIMINARY AGREEMENTS

[5.65] Parties who have negotiated the principal terms of a proposed transaction may enter into a preliminary written agreement, with the intention of recording their agreement in

96 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424, 464–5.
97 *Australian Woollen Mills Pty Ltd v Commonwealth* (1955) 93 CLR 546, 555.
98 *Australian Woollen Mills Pty Ltd v Commonwealth* (1955) 93 CLR 546, 555.
99 *Administration of Papua New Guinea v Leahy* (1961) 105 CLR 6.
100 *Administration of Papua New Guinea v Leahy* (1961) 105 CLR 6, 19.
101 *Administration of Papua New Guinea v Leahy* (1961) 105 CLR 6, 11.
102 *Placer Developments Ltd v Commonwealth* (1969) 121 CLR 353.
103 *Placer Developments Ltd v Commonwealth* (1969) 121 CLR 353, 359–61, 356–7. See [6.55].
104 *Placer Developments Ltd v Commonwealth* (1969) 121 CLR 353, 363.
105 *Placer Developments Ltd v Commonwealth* (1969) 121 CLR 353, 368.
106 *Placer Developments Ltd v Commonwealth* (1969) 121 CLR 353, 368.

a more formal way at some future time. It is not uncommon in commercial transactions, for example, for the parties to record "heads of agreement" when the principal terms of a complex transaction have been agreed upon.[107] The preliminary agreement may be expressed to be "subject to contract" or "subject to preparation of a formal contract". If one of the parties wishes to withdraw from the transaction after the preliminary agreement has been signed, it will be necessary to determine whether the preliminary agreement was intended to be binding.[108] The issue is whether the parties intended to be bound immediately on the signing of the preliminary agreement or intended to defer any legal commitment until a formal contract had been made. In the determination of this issue, the court will take account of post-agreement conduct and communications, including, for example, the fact that the parties have continued their negotiations after the formation of an agreement[109] and, pointing in the opposite direction, the fact that the parties have embarked on performance.[110]

The three categories in *Masters v Cameron*

[5.70] A preliminary agreement will be binding if it appears the parties intended it to be binding. The leading case on this point is *Masters v Cameron*.[111] The parties in that case had signed a written memorandum relating to the sale of a farming property. The memorandum was signed by both parties and recorded the vendor's agreement to sell and the purchaser's agreement to buy the property for a stipulated price. The portion of the document signed by the vendor said: "This agreement is made subject to the preparation of a formal contract of sale which shall be acceptable to my solicitors on the above terms and conditions, and to the giving of possession on or about the Fifteenth Day of March 1952." Both parties behaved as though the transaction was proceeding, but no further document was signed. When the purchaser ran into financial difficulties, he refused to complete the transaction.

The High Court observed that a case such as this may fall into one of three categories.[112] First, the parties may have finalised "all the terms of their bargain" and intend to be bound immediately but propose to restate the terms in a form which is fuller or more precise, but not different in effect. Secondly, the parties may have "completely agreed upon all the terms of their bargain" and do not intend to vary those terms but "have made performance of one or more terms conditional upon the execution of a formal document".[113] Thirdly, the parties may not intend to make a binding agreement at all unless and until they execute a formal contract. In the first case, the parties are bound whether or not a formal document is ever signed; in the second, they are bound to bring the formal document into existence and in the third, they are not bound unless a formal document is signed. "Cases of the third class are not intended to have, and therefore do not have, any binding effect."[114]

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107 See, eg, *Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd* (1991) 24 NSWLR 1.

108 See, eg, *Toyota Motor Corporation Australia Ltd v Ken Morgan Motors Pty Ltd* [1994] 2 VR 106.

109 *Sagacious Procurement Pty Ltd v Symbion Health Ltd (formerly Mayne Group Ltd)* [2008] NSWCA 149, esp at [105]; *Factory 5 Pty Ltd (in liq) v State of Victoria (No 2)* [2012] FCAFC 150.

110 *RTS Flexible Systems Ltd v Molkerei Alois Müller GmbH & Co KG (UK Production)* [2010] UKSC 14, [2010] 1 WLR 753.

111 *Masters v Cameron* (1954) 91 CLR 353.

112 *Masters v Cameron* (1954) 91 CLR 353, 360.

113 *Masters v Cameron* (1954) 91 CLR 353, 360.

114 *Masters v Cameron* (1954) 91 CLR 353, 361.

The High Court held that the effect of a preliminary agreement depends on the intention disclosed by the language used by the parties.[115] The use of expressions such as "subject to contract" and "subject to formal contract" prima facie indicate that the parties have done no more than establish a basis for a future agreement, and that the preliminary agreement is not intended to be binding.[116] On the facts before the court, there was nothing to displace that presumption. The stipulation that the formal contract was to be acceptable to the vendor's solicitors indicated that it should include any terms the solicitors considered appropriate.[117] The memorandum did not, therefore, record a binding agreement. The purchaser was free to withdraw from the transaction and was entitled to a return of the deposit.

Although the *Masters v Cameron* categories are routinely relied upon, their analytical utility is limited. That is because they express possible conclusions about the question at issue rather than providing guidance in reaching that conclusion. The question to be decided is whether the parties manifested an intention to be bound by the preliminary agreement immediately upon signing. The starting point for that inquiry is the language of the agreement, but it is to be read in light of "the commercial context and surrounding circumstances" of the dealings between the parties.[118] The terms are also important: the more comprehensive an agreement, the more likely it is that the parties intend to be bound immediately. Conversely, "the more numerous and significant the areas in respect of which the parties have failed to reach agreement, the slower a court will be to conclude that they had the requisite contractual intention."[119] Subsequent conduct can be taken into account: it may, for example, be relevant that the parties continue to negotiate and do not treat the preliminary agreement as binding.[120]

A "fourth category"?

[5.75] In *Baulkham Hills Private Hospital Pty Ltd v GR Securities Pty Ltd*,[121] McLelland J suggested that, in addition to the three categories referred to in *Masters v Cameron*, the cases support the recognition of a fourth class of case in which the parties intend to be bound "immediately and exclusively" by the terms they have agreed on, "whilst expecting to make a further contract in substitution for the first contract, containing, by consent, additional terms". The existence of a fourth class has been accepted in many subsequent cases.[122] In *Anaconda Nickel Ltd v Tarmoola Australia Pty Ltd*,[123] for example, a letter signed by both parties set out the proposed terms of an agreement relating to a mineral exploration venture. The document concluded: "The above forms a heads of agreement which constitutes an agreement in itself intended to be replaced by a fuller agreement not different in substance or

115 *Masters v Cameron* (1954) 91 CLR 353, 362.

116 *Masters v Cameron* (1954) 91 CLR 353, 362–3.

117 *Masters v Cameron* (1954) 91 CLR 353, 364.

118 *Pavlovic v Universal Music Australia Pty Ltd* [2015] NSWCA 313; (2015) 90 NSWLR 605, [72].

119 *Australian Broadcasting Corporation v XIVth Commonwealth Games Ltd* (1988) 18 NSWLR 540, 548.

120 *Barrier Wharves Ltd v W Scott Fell & Co Ltd* (1908) 5 CLR 647, 669; *Australian Broadcasting Corporation v XIVth Commonwealth Games Ltd* (1988) 18 NSWLR 540, 550; *Factory 5 Pty Ltd (in liq) v State of Victoria (No 2)* [2012] FCAFC 150.

121 *Baulkham Hills Private Hospital Pty Ltd v GR Securities Pty Ltd* (1986) 40 NSWLR 622, 628, quoting *Sinclair, Scott & Co Ltd v Naughton* (1929) 43 CLR 310, 317.

122 See McLauchlan, "In Defence of the Fourth Category of Preliminary Agreements: Or Are There Only Two?" (2005) 21 *Journal of Contract Law* 286, 293–4.

123 *Anaconda Nickel Ltd v Tarmoola Australia Pty Ltd* [2000] WASCA 27; (2000) 22 WAR 101.

form." The Full Court of the Supreme Court of Western Australia (by majority) held that the heads of agreement was intended to be binding and fell within the fourth category.

Although there has been some debate as to whether the "fourth category" is really necessary,[124] the weight of authority supporting the extra category ensures that it will continue to inform analysis. The categories do not, in any case, constitute rules of law: they are not "applied as strict categories into which such cases must fall".[125] As Professor McLauchlan reminds us, it is important not to lose sight of the fact that there are really only two categories of preliminary agreement: those that are intended to be immediately binding and those that are not.[126] If a preliminary agreement is intended to be binding, then a further question arises: whether it is sufficiently complete that it is capable of constituting a binding contract. The issues of certainty and completeness are interconnected,[127] because the failure of parties to deal with matters that one would expect to see included supports the conclusion that the parties do not intend to be bound.[128] The same goes for a failure to deal effectively with significant matters that were under discussion between the parties.[129] Although similar evidence is looked at in relation to issues of intention and completeness, they are "wholly separate" issues and must be given separate treatment.[130]

The addition of further terms

[5.80] The fact that the proposed formal contract is intended to include further terms will not prevent a preliminary agreement from being binding, provided those further terms can be settled without agreement between the parties. As we will see in Chapter 6, an agreement cannot be binding if it depends on further agreement between the parties. An agreement to agree is not enforceable. In *Godecke v Kirwan*,[131] a preliminary agreement provided that the purchaser would execute a further agreement, if required, containing such other terms as the vendor's solicitors may reasonably require. The preliminary agreement was held to be binding. Gibbs J said that the court in *Masters v Cameron* had not been intending to exclude from the second class "a case in which the formal document, when executed, would include terms additional to those already expressed, provided that the additional terms did not depend on further agreement between the parties".[132] In this case, the additional terms did not depend on further agreement between the parties because they were to be determined unilaterally by the vendor's solicitors.

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124 Peden, Carter and Tolhurst, "When Three Just Isn't Enough: The Fourth Category of the 'Subject to Contract' Cases" (2004) 20 *Journal of Contract Law* 156; McLauchlan, "In Defence of the Fourth Category of Preliminary Agreements: Or Are There Only Two?" (2005) 21 *Journal of Contract Law* 286; Tolhurst, Carter and Peden, "*Masters v Cameron* – Again!" (2011) 42 *Victoria University of Wellington Law Review* 49.

125 *Pavlovic v Universal Music Australia Pty Ltd* [2015] NSWCA 313; (2015) 90 NSWLR 605, [69].

126 McLauchlan, "In Defence of the Fourth Category of Preliminary Agreements: Or Are There Only Two?" (2005) 21 *Journal of Contract Law* 286, 304–5.

127 McLauchlan, "In Defence of the Fourth Category of Preliminary Agreements: Or Are There Only Two?" (2005) 21 *Journal of Contract Law* 286, 287–8.

128 *Nationwide Produce (Holdings) Pty Ltd (in liq) v Linknarf Limited (in liq)* [2005] FCAFC 129, [42].

129 *Factory 5 Pty Ltd (in liq) v Victoria (No 2)* [2012] FCAFC 150.

130 *Helmos Enterprises Pty Ltd v Jaylor Pty Ltd* [2005] NSWCA 235, [54].

131 *Godecke v Kirwan* (1973) 129 CLR 629.

132 *Godecke v Kirwan* (1973) 129 CLR 629, 648.

CHAPTER **6**

Certainty

[6.05] The fourth requirement of contract formation is that the agreement between the parties must be certain and complete. This requirement may be said to be implicit in the requirement of agreement: an offer will only be effective if it identifies with sufficient certainty the terms of the proposed contract. Questions of certainty also overlap with the issue of intention: the more certain and comprehensive an agreement, the more likely it is that the parties intended to be legally bound by that agreement.

It is not necessary, or indeed possible, for the parties to provide for every possible contingency,[1] or to spell out their agreement in language so clear that it is susceptible of only one interpretation.[2] In the interpretation of contracts, the courts apply the maxim ut res magis valeat quam pereat (it is better for a thing to have effect than be found void)[3] and will resolve ambiguities and fill gaps in agreements to some extent.[4] Questions of certainty and completeness are therefore questions of degree. The real issue in a particular case is whether the agreement is *sufficiently* certain and *sufficiently* complete that it is capable of constituting a binding contract.

There are two reasons why that issue is often difficult to resolve. First, resolution of the issue necessarily involves a consideration of the nature of the agreement and the particular circumstances in which the agreement has been made. Abstract principles tend to be particularly unhelpful in this area.[5] Secondly, judicial attitudes differ as to the degree of certainty and completeness required. Because the courts regard contractual obligations as voluntary, the courts have traditionally been reluctant to write contracts for the parties.[6] In accordance with this approach, some judges are adamant that the courts should not resolve issues that the parties have failed to resolve.[7] Some judges regard even the filling of a gap by

1 See Part VI.
2 See Chapter 13.
3 *Hall v Busst* (1960) 104 CLR 206, 239. See also *York Air Conditioning and Refrigeration (Australasia) Pty Ltd v Commonwealth* (1949) 80 CLR 11, 26.
4 See further Parts V and VI.
5 See *Hillas and Co Ltd v Arcos Ltd* (1932) 147 LT 503, 512; [1932] All ER 494, 499.
6 See *Biotechnology Australia Pty Ltd v Pace* (1988) 15 NSWLR 130, 132–3.
7 See, eg, *Hall v Busst* (1960) 104 CLR 206, 222.

reference to what is reasonable or fair as an unwarranted interference with individual liberty.[8] Other judges are prepared to go further to uphold vague or incomplete agreements.[9] To be weighed against the notion that the courts should not make bargains for the parties is the consideration that dealings between parties should "as far as possible be treated as effective" and that the law should "not incur the reproach of being the destroyer of bargains".[10] It is generally accepted that judges today are more willing to fill gaps and resolve ambiguities than they have been in the past.[11]

The requirement that a contract be certain has three aspects:

1. The contract must be sufficiently *complete*. This means that the parties must at least reach agreement on all terms that they intended to fix by agreement, rather than have someone else set for them, and also on all matters the court cannot resolve by implication. Some interpretations of this requirement are stricter, as we will see below.
2. The agreed terms must be sufficiently *certain* and *clear* that the parties can understand their rights and obligations and the courts can enforce them.
3. The promises made by the parties must not be *illusory*. A promise made by a party is illusory if the party is given an unfettered discretion as to performance of a promise. If a party has an unfettered choice as to whether to perform a promise, then that promise cannot be said to give rise to any contractual obligation.

The effect of uncertainty, incompleteness or an illusory term in an agreement will depend essentially on whether it goes to the heart of the agreement. If it does, then the agreement cannot constitute a binding contract. There are two ways in which an agreement affected by uncertainty may be saved. First, where a particular term or part of an agreement is incomplete, uncertain or illusory, it may be possible to *sever* the offending term or part. The remainder of the agreement will then constitute a binding contract. Secondly, where an uncertain, incomplete or illusory provision has been inserted for the benefit of one of the parties, it may be possible for that party to *waive* compliance with the offending term and enforce the remainder of the contract.

COMPLETENESS

[6.10] It is often said that no binding contract can be made unless the parties have reached agreement on all of the terms, or at least all of the essential terms, of the contract.[12] Three factors must be taken into account in determining whether an omission from an agreement is fatal to contract formation. The first question is the importance or essentiality of the term. The second question is why the term has been left out: did the parties fail to reach agreement on the issue, deliberately defer agreement or simply fail to put their minds to the issue? The

8 *Biotechnology Australia Pty Ltd v Pace* (1988) 15 NSWLR 130, 133.

9 For example, *Foley v Classique Coaches Ltd* [1934] 2 KB 1; *Booker Industries Pty Ltd v Wilson Parking (Qld) Pty Ltd* (1982) 149 CLR 600, 612–7; *Upper Hunter County District Council v Australian Chilling & Freezing Co* (1968) 118 CLR 429, 436–7.

10 *Hillas & Co Ltd v Arcos Ltd* (1932) 147 LT 503, 512; [1932] All ER 494, 499.

11 See Greig and Davis, *The Law of Contract* (1987), pp 348–62.

12 For example, *Thorby v Goldberg* (1964) 112 CLR 597, 607.

third question is whether the agreement remains entirely executory or has been wholly or partly performed.

Essential terms

[6.15] As noted above, it is said that an agreement will be sufficiently complete if the parties have reached agreement on the essential terms. The label "essential term" is used in different ways for the purposes of different doctrines of contract law.[13] Here, it simply means "a term without which the contract cannot be enforced".[14] Whether a term is essential for this purpose does not depend on its importance; it is for the parties, not the courts, to decide what is important.[15] What matters is whether the court can enforce the contract in the absence of the term in question, without exceeding its role as the interpreter, rather than the author, of the contract. Whether a particular absent term will be regarded as essential depends on the nature of the contract and the circumstances of the case.[16] In an agreement for a lease, the commencement date is essential, so an agreement for lease which fails to stipulate a commencement date will not constitute a binding contract.[17] The rent to be paid is also essential, so an option to renew a lease at a rent "to be agreed" will not be binding.[18] In a contract for the sale of land, the date for completion is not regarded as essential, but the parties must reach agreement on price. There will be no contract if the parties fail to stipulate a price or an effective method or mechanism for determining a price.[19]

In a contract for the sale of goods, on the other hand, a failure to stipulate a price may not be fatal. Where an agreement for the sale of goods is silent on price, an obligation to pay a reasonable price will be imposed by the Sale of Goods Acts.[20] Menzies J suggested in *Hall v Busst*,[21] that the obligation to pay a reasonable price for goods is a restitutionary, rather than contractual, obligation, which arises only where ordered goods have been delivered and accepted and title has passed.[22] Windeyer J took the view that the obligation to pay a reasonable price would arise in the case of a wholly executory contract that was silent on price.[23] This view is more consistent with the terms of the Sale of Goods Acts and has since been preferred.[24]

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13 Compare the use of the term in relation to termination for breach, below [21.30].

14 *Thomson v White* [2006] NSWCA 350, [100]; *Ormwave Pty Ltd v Smith* [2007] NSWCA 210, [88].

15 *Pagnan SpA v Feed Products Ltd* [1987] 2 Lloyd's Rep 601, 619, adopted in numerous Australian cases, including *Anaconda Nickel Ltd v Tarmoola Australia Pty Ltd* [2000] WASCA 27; (2000) 22 WAR 101, 111; *Thomson v White* [2006] NSWCA 350, [100]; *Ormwave Pty Ltd v Smith* [2007] NSWCA 210, [88].

16 *Vroon BV v Foster's Brewing Group Ltd* [1994] 2 VR 32, 68.

17 *Harvey v Pratt* [1965] 1 WLR 1025.

18 See *Eudunda Farmers Co-operative Society Ltd v Mattiske* [1920] SALR 309; *Randazzo v Goulding* [1968] Qd R 433.

19 *Hall v Busst* (1960) 104 CLR 206, 240; *Stocks & Holdings (Constructors) Pty Ltd v Arrowsmith* (1964) 112 CLR 646, 650.

20 *Sale of Goods Act 1954* (ACT), s 13(2); *Sale of Goods Act 1923* (NSW), s 13(2); *Sale of Goods Act* (NT), s 13(2); *Sale of Goods Act 1896* (Qld), s 11(2); *Sale of Goods Act 1895* (SA), s 8(2); *Sale of Goods Act 1896* (Tas), s 13(2); *Goods Act 1958* (Vic), s 13(2); *Sale of Goods Act 1895* (WA), s 8(2).

21 *Hall v Busst* (1960) 104 CLR 206.

22 *Hall v Busst* (1960) 104 CLR 206, 234. See also at 222.

23 *Hall v Busst* (1960) 104 CLR 206, 241–2.

24 See Sutton, *Sales and Consumer Law* (4th ed, 1995), pp 159–60; *Wenning v Robinson* (1964) 64 SR (NSW) 157, 161–2, 167.

In a contract for the sale of land, the parties, the subject matter and the price are regarded as essential terms and there can be no binding contract if these details are not fixed with certainty.[25] Parties may make a valid contract, sometimes described as an "open contract", for the sale of land, dealing only with these terms, and the court will "fill in the details" by implication.[26] The court will imply obligations relating to each step necessary to complete the transaction, including an obligation to take each step within a reasonable time.[27] The court's understanding of conveyancing transactions allows it to make the necessary implications. In a "reasonably straight forward" property development joint venture, it was possible for the court to make implications as to how profits were to be calculated and how losses were to be shared.[28] Where a transaction is of a more complex and less familiar kind, such as a mining joint venture, the court may not be able to imply the necessary terms.[29] The more novel and complex an agreement is, the less likely it is that the court will feel competent to fill gaps in the agreement.[30] In *Milne v Attorney-General (Tas)*,[31] the High Court referred to certain documents which the plaintiff alleged contained the relevant terms of the contract and said:

> Those documents deal with some only of the terms which must of necessity be settled before a binding contract can exist … no contract is concluded until the parties negotiating are agreed upon all the terms of their bargain – unless the terms left outstanding are "such as the law will supply" … Here the transaction ultimately contemplated was very complex, and it is clear that the law cannot supply its terms.

The question of what is essential will depend on the facts of each particular case. In *Trollope & Colls Ltd v Atomic Power Constructions Ltd*, Megaw J suggested that the parties must "agree any term which [is], in law, essential to be agreed in order to make the contract commercially workable".[32] This point is illustrated by *Australia and New Zealand Banking Group Ltd v Frost Holdings Pty Ltd*,[33] which involved an agreement relating to an exhibition of paintings and the production of calendars featuring reproductions of those paintings. The agreement was held to be incomplete because the parties had failed to reach agreement on the design, style and content of the calendars, the quality and size of paper and the number to be supplied. Kaye J, with whom Marks and Teague JJ agreed, held that the provisions of the Sale of Goods Acts implying an obligation to pay a reasonable price can operate only where agreement has been reached on all other essential terms.[34]

Kaye J suggested in *Australia and New Zealand Banking Group Ltd v Frost Holdings Pty Ltd* that "the law does not permit a court to imply a term into a bargain between parties for

25 *Hall v Busst* (1960) 104 CLR 206, 222.

26 *Cavallari v Premier Refrigeration Co Pty Ltd* (1952) 85 CLR 20, 27.

27 *Cavallari v Premier Refrigeration Co Pty Ltd* (1952) 85 CLR 20, 27.

28 *Thomson v White* [2006] NSWCA 350, [103].

29 *Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd* (1991) 24 NSWLR 1, 38.

30 *Trawl Industries of Australia Pty Ltd v Effem Foods Pty Ltd* (1992) 27 NSWLR 326, 333–4.

31 *Milne v Attorney-General (Tas)* (1956) 95 CLR 460, 473.

32 *Trollope & Colls Ltd v Atomic Power Constructions Ltd* [1962] 1 WLR 333, 337.

33 *Australia and New Zealand Banking Group Ltd v Frost Holdings Pty Ltd* [1989] VR 695.

34 *Australia and New Zealand Banking Group Ltd v Frost Holdings Pty Ltd* [1989] VR 695, 702–3.

the purposes of making their bargain an enforceable contract".[35] Brian Coote has argued that the relevant principle cannot be "that there must be sufficient expressly agreed terms by themselves to constitute a contract before any additional terms can be implied to supplement them".[36] The threshold question is not whether the expressly agreed terms are sufficient in themselves to constitute a contract, but whether the parties have specifically agreed all the terms that only they can decide. A contract will be binding if the parties have agreed all of the terms on which they had intended that only they should agree, plus any other terms the court is incapable of supplying by implication.[37] In order to form a valid contract, the parties must, in other words, reach agreement "upon all the terms which they regarded or the law requires as essential for the formation of legally binding relations".[38] Such a principle is consistent with the result in *Australia and New Zealand Banking Group Ltd v Frost Holdings Pty Ltd*. It is also consistent with *Devani v Wells*,[39] where a real estate agent and a vendor of flats had agreed on a rate of commission to be paid to the agent but not on the event that would trigger the agent's entitlement to commission. The UK Supreme Court held that a reasonable person would understand the commission to be payable on completion of a sale of the property to a purchaser introduced by the agent and from the proceeds of sale.[40] The court would, if necessary, have held such a term to be implied.

Agreements to agree

[6.20] In most cases, it will be of no consequence whether an agreement is silent in relation to an essential term or provides that the parties will reach agreement on that term in the future. In neither case is there a binding contract: both types of agreement may be characterised as incomplete, while the second type may also be characterised as an agreement to agree, which the courts will not enforce.[41] The distinction is important, however, in a situation in which the court might otherwise have implied a term, such as an obligation to pay a reasonable price in a contract for the sale of goods.[42] The obligation to pay a reasonable price will only be inferred if the contract is silent as to price. In *May and Butcher Ltd v The King*,[43] the House of Lords held that the provision of the Sale of Goods legislation implying an obligation to pay a reasonable price has no application where the parties had deliberately deferred agreement on price. Where the parties have agreed to reach agreement on price in the future, the implication of an obligation to pay a reasonable price would be inconsistent with the expressed intention of the parties, which is to set the price themselves.

35 *Australia and New Zealand Banking Group Ltd v Frost Holdings Pty Ltd* [1989] VR 695, 702, citing dictum of Lord Roskill in the Privy Council in *Aotearoa International Ltd v Scancarriers A/S* [1985] 1 NZLR 513, 556.

36 Coote, "Contract Formation and the Implication of Terms" (1993) 6 *Journal of Contract Law* 51, 51.

37 Coote, "Contract Formation and the Implication of Terms" (1993) 6 *Journal of Contract Law* 51, 56–7.

38 *RTS Flexible Systems Ltd v Molkerei Alois Müller GmbH Co KG (UK Production)* [2010] UKSC 14; [2010] 1 WLR 753.

39 *Devani v Wells* [2019] UKSC 4; [2019] 2 WLR 617.

40 *Devani v Wells* [2019] UKSC 4; [2019] 2 WLR 617, [26]–[28].

41 For example, *Booker Industries Pty Ltd v Wilson Parking (Qld) Pty Ltd* (1982) 149 CLR 600, 604. But see McLauchlan, "Rethinking Agreements to Agree" (1998) 18 *New Zealand Universities Law Review* 77.

42 See also *Relwood Pty Ltd v Manning Homes Pty Ltd* [1990] 1 Qd R 481, 488.

43 *May and Butcher Ltd v The King* [1934] 2 KB 17n.

Executed contracts

[6.25] The courts are less likely to find an agreement incomplete if it has been wholly or partly performed.[44] Where land has been conveyed, goods delivered or services performed under an agreement, a finding that it is not binding will have more serious consequences than if it remains wholly executory. It has been said that:

> In a commercial agreement the further the parties have gone on with their contract, the more ready are the courts to imply any reasonable term so as to give effect to their intentions. When much has been done, the courts will do their best not to destroy the bargain.[45]

In *Foley v Classique Coaches Ltd*,[46] for example, the plaintiff sold land to the defendants on which they were to carry on a motor coach business. The plaintiff retained a petrol station on adjoining land. In a supplemental agreement, the defendants agreed to buy all of their supplies of petrol from the plaintiff during his lifetime "at a price to be agreed by the parties in writing and from time to time". The land was duly conveyed to the defendants, who purchased their petrol from the plaintiff for three years. The defendants then wished to acquire cheaper petrol elsewhere and claimed the agreement was not binding because no written agreement as to price had ever been made. The Court of Appeal was prepared to imply a term that the petrol was to be sold at a reasonable price. It is difficult to reconcile this case with *May and Butcher Ltd v The King*, except by reference to the fact that land had been conveyed and the parties had acted on the agreement for three years.

Machinery for settling a term

[6.30] Parties may make a valid contract that defers agreement on an essential term if they provide an effective mechanism for supplying the term in the event they fail to reach agreement. It is quite common for a commercial lease to provide an option for renewal at a rent to be agreed between the parties or, failing agreement, to be determined by a specified valuer or arbitrator.[47] A difficult question arises when the machinery specified by the parties for supplying a term fails, such as where a specified arbitrator or valuer is unable or unwilling to perform the task required of him or her by the contract. In *George v Roach*,[48] the High Court held that an agreement was ineffective when part of the purchase price was to be fixed by a nominated valuer who refused to carry out the task. This approach may be justified on the basis that it would be inconsistent with the intention of the parties for the court to set the term. The Sale of Goods legislation similarly provides that "[w]here there is an agreement to sell goods on the terms that the price is to be fixed by the valuation of a third party, and such third party cannot or does not make such valuation, the agreement is avoided".[49] In England, the courts are prepared to imply an obligation to pay a reasonable price where valuation

44 For example, *Husain v O&S Holdings (Vic) Pty Ltd* [2005] VSCA 269, [26] and [53] and *Wells v Devani* [2019] UKSC 4, [2019] 2 WLR 617, [26] and [35].

45 *F & G Sykes (Wessex) Ltd v Fine Fare Ltd* [1967] 1 Lloyd's Rep 53, 57.

46 *Foley v Classique Coaches Ltd* [1934] 2 KB 1.

47 See, eg, *Booker Industries Pty Ltd v Wilson Parking (Qld) Pty Ltd* (1982) 149 CLR 600.

48 *George v Roach* (1942) 67 CLR 253.

49 *Sale of Goods Act 1954* (ACT), s 14(1); *Sale of Goods Act 1923* (NSW), s 14(1); *Sale of Goods Act* (NT), s 14(1); *Sale of Goods Act 1896* (Qld), s 12(1); *Sale of Goods Act 1895* (SA), s 9(1); *Sale of Goods Act 1896* (Tas), s 14(1); *Goods Act 1958* (Vic), s 14(1); *Sale of Goods Act 1895* (WA), s 9(1).

machinery has failed and the specified mode of ascertaining the value of the subject matter cannot be regarded as essential.[50] Brennan J expressed support for this view by way of obiter dicta in *Booker Industries Pty Ltd v Wilson Parking (Qld) Pty Ltd*.[51]

Formula for settling a term

[6.35] Parties may also agree on a formula for settling a term or terms of their agreement, which can be applied by the court in the event of a dispute. The formula may provide a very precise means of settling the term, such as where a commercial lease specifies a mathematical formula for increases in rent to reflect movements in the Consumer Price Index. Alternatively, the parties may specify a standard, rather than a formula, such as an option to renew a lease at a "reasonable rental". The validity of the contract will then depend on whether the court regards the formula or standard as sufficiently certain.

CERTAINTY

[6.40] A contract may fail because a particular term is so vague and imprecise that the courts cannot attribute a meaning to it. The courts cannot enforce a contract if they cannot identify the obligations of the parties with some degree of precision. The courts do not take a narrow or pedantic approach to the requirement of certainty and will attribute a meaning to the language used by the parties unless it is impossible to do so.[52] As with incompleteness, uncertainty is more likely to affect a contract that remains wholly executory. Where the parties have been performing the contract without difficulty, the court will be reluctant to come to the conclusion that the contract is unintelligible.[53]

Reasonableness

[6.45] The standard of reasonableness can often be employed to provide completeness and certainty that would otherwise be lacking. A valid contract may be made for the sale of goods "at a reasonable price".[54] In other instances, the reasonableness standard will not be sufficiently certain. In *Hall v Busst*,[55] the vendor of land was given an option to repurchase it at a specified price less "a reasonable sum to cover depreciation of all buildings and other property on the land". The High Court, by a majority of 3-2, held that the clause was void for uncertainty, since there were many ways to measure depreciation, all of which could be regarded as reasonable. The majority took the view that although a sale of goods at a reasonable price was enforceable, this principle did not extend to land. Accordingly, a contract for the sale of land at a reasonable price would be void for uncertainty. In his dissenting judgment, Kitto J observed that the law has never found the standard of reasonableness too

50 *Sudbrook Trading Estate Ltd v Eggleton* [1983] AC 444.

51 *Booker Industries Pty Ltd v Wilson Parking (Qld) Pty Ltd* (1982) 149 CLR 600, 616. See also *Axelsen v O'Brien* (1949) 80 CLR 219.

52 *Upper Hunter County District Council v Australian Chilling & Freezing Co Ltd* (1968) 118 CLR 429, 436–7.

53 *York Air Conditioning and Refrigeration (Australasia) Pty Ltd v Commonwealth* (1949) 80 CLR 11, 53. See also *Hillas v Arcos* (1932) LT 503 and Lücke, "Illusory, Vague and Uncertain Contractual Terms" (1977) 6 *Adelaide Law Review* 1, 9–11.

54 *Wenning v Robinson* [1964] 64 SR (NSW) 157, 164.

55 *Hall v Busst* (1960) 104 CLR 206.

vague.[56] Windeyer J dissented for similar reasons and was also concerned that the parties had changed their position on the basis of the agreement.[57] The decision in *Hall v Busst* can be seen to reflect a more restrictive approach to questions of certainty than that which is now applied by the courts.[58]

Whitlock v Brew[59] was concerned with a contract for the sale of a large parcel of land that included a Shell petrol station. The land was sold on condition that the purchaser would grant a lease of part of the land to the Shell Company of Australia Ltd (a third party) "on such reasonable terms as commonly govern such a lease". The purchaser claimed the contract was void for uncertainty and sought to recover his deposit. There was no evidence that there were any terms for a lease that could be regarded as standard and reasonable, but, even if there were, the parties had not agreed on the vital questions of rent and the term of the lease. Taylor, Menzies and Owen JJ considered that "the expression 'upon such reasonable terms as commonly govern such a lease' [was] not, in the context in which it appears, apt to refer either to the period" of the lease or the rent payable.[60] Kitto J observed that the reference to "reasonable terms" would have been sufficiently certain had there been such a set of terms in common use, but the evidence did not establish this.[61] Accordingly, the contract was void for uncertainty. In his dissenting judgment, McTiernan J considered that the commencement date and term of the lease could be inferred from the circumstances, and the parties had expressly agreed that the rent should be reasonable.[62] McTiernan J held that, although a court might hesitate to grant specific performance, the agreement was enforceable by an action for damages.[63]

Agreements to negotiate

[6.50] It has been held in England that neither an agreement to negotiate nor an agreement to negotiate in good faith can be legally binding. In *Walford v Miles*,[64] the House of Lords held that an agreement to negotiate lacks the necessary certainty to constitute a legally enforceable obligation. The case concerned the enforceability of a "lock out" agreement, which required a proposed seller of shares not to deal with any other potential buyer, with a view to concluding an agreement with the other party to the lock out agreement. The House of Lords held that the agreement was unenforceable because no duration was specified. A central issue was whether the uncertainty as to duration could be resolved by implying a duty to negotiate in good faith. The House of Lords held that no such duty could be imposed. Lord Ackner said that "a bare agreement to negotiate has no legal content" because negotiating parties are free to withdraw at any time.[65] A duty to negotiate in good faith was said to be "unworkable in

56 *Hall v Busst* (1960) 104 CLR 206, 226.
57 *Hall v Busst* (1960) 104 CLR 206, 238–9.
58 See *Booker Industries Pty Ltd v Wilson Parking (Qld) Pty Ltd* (1982) 149 CLR 600, esp at 616.
59 *Whitlock v Brew* (1968) 118 CLR 445.
60 *Whitlock v Brew* (1968) 118 CLR 445, 460.
61 *Whitlock v Brew* (1968) 118 CLR 445, 456.
62 *Whitlock v Brew* (1968) 118 CLR 445, 454–5.
63 *Whitlock v Brew* (1968) 118 CLR 445, 455.
64 *Walford v Miles* [1992] 2 AC 128.
65 *Walford v Miles* [1992] 2 AC 128, 138.

practice" and "inherently repugnant to the adversarial position of the parties when involved in negotiations".[66]

In *Petromec Inc v Petroleo Brasileiro SA*, Longmore LJ observed that:

> The traditional objections to enforcing an obligation to negotiate in good faith are (1) that the obligation is an agreement to agree and thus too uncertain to enforce, (2) that it is difficult, if not impossible, to say whether, if negotiations are brought to an end, the termination is brought about in good or in bad faith, and (3) that, since it can never be known whether good faith negotiations would have produced an agreement at all or what the terms of any agreement would have been if it would have been reached, it is impossible to assess any loss caused by breach of the obligation.[67]

The refusal to recognise an agreement to negotiate in good faith has been criticised.[68] It has been argued that if parties have agreed to negotiate in good faith, the law should respect their intentions.[69] An agreement to negotiate is not an agreement to agree; it does not oblige the parties to reach agreement but merely to make good faith efforts to reach agreement. If the parties make a good faith effort to reach agreement,[70] but cannot agree, they are free to withdraw from the negotiations.

In one Australian case, a promise in a memorandum of understanding to "use reasonable endearvours to negotiate" a gas supply agreement and to "work in good faith" to progress the agreement was held to be insufficiently certain to be enforceable.[71] Australian courts have, however, been willing to recognise the enforceability of a contractual duty to negotiate in good faith in particular contexts. In *Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd*,[72] a majority of the New South Wales Court of Appeal accepted that a promise to negotiate in good faith may, in particular circumstances, be enforceable. The court was concerned with a heads of agreement relating to a proposed mining joint venture. The agreement provided that the parties would "proceed in good faith to consult together upon the formulation of a more comprehensive and detailed Joint Venture Agreement". Given the complexity of the proposed joint venture, the importance of the outstanding issues and the absence of machinery for resolving outstanding differences, the relevant provision was too vague and uncertain to be enforceable.[73] Kirby P, with whom Waddell A-JA agreed, accepted that "a promise to negotiate in good faith will be enforceable, depending upon its precise terms … so long as the promise is clear and part of an undoubted agreement between the parties".[74]

It is arguable that the court in *Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd* should not have been concerned about the completeness of the heads of agreement in setting out the

66 *Walford v Miles* [1992] 2 AC 128, 138.

67 *Petromec Inc v Petroleo Brasileiro SA* [2005] EWCA Civ 891, [116]. See also *Barbudev v Eurocom Cable Management Bulgaria EOOD* [2011] EWHC 1560 (Comm), [97], quoting Peel, "Agreements to Negotiate in Good Faith" in Burrows and Peel (eds), *Contract Formation and Parties* (2010), 37, p 50.

68 See Paterson, "The Contract to Negotiate in Good Faith: Recognition and Enforcement" (1996) 10 *Journal of Contract Law* 120.

69 See also *Petromec Inc v Petroleo Brasileiro SA* [2005] EWCA Civ 891, [121].

70 As to which, see Paterson, "The Contract to Negotiate in Good Faith: Recognition and Enforcement" (1996) 10 *Journal of Contract Law* 120, 132–8.

71 *Baldwin v Icon Energy Ltd* [2015] QSC 12; [2016] 1 Qd R 397.

72 *Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd* (1991) 24 NSWLR 1.

73 *Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd* (1991) 24 NSWLR 1, 27

74 *Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd* (1991) 24 NSWLR 1, 26.

terms of the joint venture.[75] The court was not being asked to give effect to that agreement as a final contract relating to the joint venture. As noted above, an agreement to negotiate only requires the parties to negotiate towards a final agreement. The role of the court in enforcing such an agreement is to assess whether or not the parties have negotiated in good faith. The adoption of this approach would not have changed the result of the case, since Kirby P found that if there was an enforceable agreement to negotiate in good faith, it had not been breached.[76]

In *Aiton Australia Pty Ltd v Transfield*,[77] Einstein J regarded promises to negotiate and mediate in good faith to resolve disputes arising under an agreement as sufficiently certain to be enforceable. Clause 28 of a construction contract set out a dispute resolution procedure, which included obligations to negotiate and mediate in good faith. Einstein J held that clause 28 would have been sufficiently certain to be enforceable had the parties provided for payment of the mediator's costs.[78] More recently, in *United Group Rail Services Limited v Rail Corporation New South Wales*, the New South Wales Court of Appeal reviewed the authorities and upheld the validity of a clearly worded dispute resolution clause which included an agreement to "meet and undertake genuine and good faith negotiations with a view to resolving the dispute".[79] The court confirmed that such a promise does not prevent the parties from acting self-interestedly, but simply requires "an honest and genuine commitment … to the process of negotiation for the designated purpose".[80] The parties must bring to the negotiations a genuine belief about their rights and obligations under the agreement and must negotiate by reference to those beliefs:

> These are not empty obligations; nor do they represent empty rhetoric. An honest and genuine approach to settling a contractual dispute, giving fidelity to the existing bargain, does constrain a party. The constraint arises from the bargain the parties have willingly entered into. It requires the honest and genuine assessment of rights and obligations and it requires that a party negotiate by reference to such. A party, for instance, may well not be entitled to threaten a future breach of contract in order to bargain for a lower settlement sum than it genuinely recognises as due. That would not, in all likelihood, reflect a fidelity to the bargain. A party would not be entitled to pretend to negotiate, having decided not to settle what is recognised to be a good claim, in order to drive the other party into an expensive arbitration that it believes the other party cannot afford.[81]

ILLUSORY PROMISES

[6.55] A promise will be illusory if the promisor has an unfettered discretion in relation to performance. A promise to offer a renewed lease to a tenant is illusory if it leaves the terms and

75 Paterson, "The Contract to Negotiate in Good Faith: Recognition and Enforcement" (1996) 10 *Journal of Contract Law* 120, 130.

76 *Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd* (1991) 24 NSWLR 1, 28–31.

77 *Aiton Australia Pty Ltd v Transfield* [1999] NSWSC 996; (1999) 153 FLR 236.

78 *Aiton Australia Pty Ltd v Transfield* [1999] NSWSC 996; (1999) 153 FLR 236, 271.

79 *United Group Rail Services Limited v Rail Corporation New South Wales* [2009] NSWCA 177; (2009) 74 NSWLR 618.

80 *United Group Rail Services Limited v Rail Corporation New South Wales* [2009] NSWCA 177; (2009) 74 NSWLR 618, [71].

81 *United Group Rail Services Limited v Rail Corporation New South Wales* [2009] NSWCA 177; (2009) 74 NSWLR 618, [72]–[73].

conditions, including rent, to the offeror.[82] In *Placer Development Ltd v Commonwealth*,[83] an agreement was made between Placer and the Commonwealth for the formation of a timber company to operate in Papua New Guinea. As noted in Chapter 5,[84] Clause 14 of the agreement provided that if customs duty was paid on the importation of the timber company's products into Australia, the Commonwealth would pay to the timber company a subsidy at a rate to be determined by the Commonwealth, but not exceeding the amount of customs duty paid. The High Court held, by a majority of 3-2, that the promise was unenforceable. Kitto J said:

> The general principle … is that wherever words which by themselves constitute a promise are accompanied by words showing that the promisor is to have a discretion or option as to whether he will carry out that which purports to be the promise, the result is that there is no contract on which an action can be brought at all.[85]

It followed that the Commonwealth's promise to pay an unspecified sum of money was illusory, since the Commonwealth was expressly given a discretion to determine the amount to be paid.[86]

In their dissenting judgments, Menzies and Windeyer JJ were more reluctant to come to the conclusion that a contractual promise should have no legal effect and were able to identify an enforceable promise by the Commonwealth.[87] Menzies and Windeyer JJ held that the Commonwealth was under an enforceable obligation to determine the amount of the subsidy to be paid and to pay that amount.[88] Its only discretion was in relation to the amount payable. Windeyer J observed that where an agreement produces an obligation to pay an unspecified sum of money, it can normally be said that an obligation to pay a reasonable sum was intended and that can be determined by the court.[89] In this case, however, the reasonableness of a subsidy could not be determined by objective criteria, so the court could not determine the amount of the subsidy if the Commonwealth failed to do so.[90] Nevertheless, the Commonwealth remained under an obligation that could be enforced by an action for damages and perhaps specific performance.[91]

A promise may also be rendered illusory by an exemption clause which is so sweeping in its effect that it effectively deprives the promise of any force. In *MacRobertson Miller Airline Services v Commissioner of State Taxation*,[92] discussed in Chapter 3,[93] clauses set out in an airline ticket gave the airline the right to cancel a flight or cancel a booking without incurring

82 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* [2016] HCA 26; (2016) 260 CLR 1, [198]–[200] (Nettle J); contra Gageler J at [62]–[64] and Gordon J at [265] (promise to make an "offer" not rendered illusory by discretion as to terms).

83 *Placer Development Ltd v Commonwealth* (1969) 121 CLR 353.

84 See [5.60].

85 *Placer Development Ltd v Commonwealth* (1969) 121 CLR 353, 356. See also *Thorby v Goldberg* (1964) 112 CLR 597, 605.

86 *Placer Development Ltd v Commonwealth* (1969) 121 CLR 353, 359–60.

87 The dissenting judgment of Hope JA in *Biotechnology Australia Pty Ltd v Pace* (1988) 15 NSWLR 130, 143–7 reflects a similar approach.

88 *Placer Development Ltd v Commonwealth* (1969) 121 CLR 353, 364–5, 370–4.

89 *Placer Development Ltd v Commonwealth* (1969) 121 CLR 353, 371.

90 *Placer Development Ltd v Commonwealth* (1969) 121 CLR 353, 371–2.

91 *Placer Development Ltd v Commonwealth* (1969) 121 CLR 353, 372.

92 *MacRobertson Miller Airline Services v Commissioner of State Taxation* (1975) 133 CLR 125.

93 See [3.40].

any liability. These clauses rendered illusory any implied promise the airline might have made to carry the passenger.[94] Barwick CJ found that the clauses occupied "the whole area of possible obligation" and left no room for the existence of a contract.[95] Similarly, Jacobs J held that the clauses made nugatory any promise to carry that might have been implied.[96]

A contemporary example of an illusory promise is a "discretionary risk product" of the kind analysed in *Evans v Davantage Group Pty Ltd*.[97] The applicant in that case, who represented a class of approximately 27,000 people in similar positions, had purchased a used car for approximately $17,000. For an additional sum of almost $2000, the applicant entered into a warranty agreement with the respondent, which traded as National Warranty Company (NWC). Under that warranty agreement, NWC promised to reimburse the applicant for the cost of rectifying certain mechanical failures in certain circumstances "up to" certain specified limits. Crucially, clause 11 included the following:

> The Warranty is a discretionary risk product. This means that you are entitled to have your claim for assistance heard, but that NWC is not obliged to pay all claims that come within the terms and conditions of the Warranty. You are entitled to have NWC decide whether or not to pay the entire claim or to make a contribution to your claim.

Beach J held that the promises made by NWC under the warranty agreement were illusory. Clause 11 carved out "the whole area of possible performance of any possible payment obligation". A promise by NWC to consider each claim and exercise its discretion "in a fair or just way" did not create any obligation because, in the context of clause 11, it was "obscure and uncertain", "devoid of any content" and did not supply "objectively identifiable criteria" by reference to which the rights of the parties could be worked out.[98]

The primary effect of a promise being illusory is that the promise will not itself be enforceable. The broader effect of an illusory promise on a contract can be analysed in two ways. First, as noted in Chapter 4,[99] an illusory promise will not constitute good consideration for a counter-promise made by another party. Accordingly, if one party makes only illusory promises, then the entire contract will fail for want of consideration. Secondly, a contract containing an illusory promise may be regarded as incomplete. The entire contract will be regarded as illusory where an essential term has been left to be determined by one of the parties.[100] An agreement for the sale of land, for example, will not be binding if it leaves the price to be determined by the buyer or the seller.[101]

[6.60] A contract will not be regarded as illusory if important matters are left to be determined by a third party or if subsidiary matters are left to be determined by one of the parties.

94 But note that Barwick CJ held that no such promise would be implied in any case, having regard to the well-known uncertainties of air travel: *MacRobertson Miller Airline Services v Commissioner of State Taxation* (1975) 133 CLR 125, 133–135.

95 *MacRobertson Miller Airline Services v Commissioner of State Taxation* (1975) 133 CLR 125, 133.

96 *MacRobertson Miller Airline Services v Commissioner of State Taxation* (1975) 133 CLR 125, 148.

97 *Evans v Davantage Group Pty Ltd* [2019] FCA 884.

98 *Evans v Davantage Group Pty Ltd* [2019] FCA 884, [96], citing *Upper Hunter County District Council v Australian Chilling & Freezing Co Ltd* (1968) 118 CLR 429, 437.

99 See [4.50].

100 *Godecke v Kirwan* (1973) 129 CLR 629, 646–7.

101 *Battie v Fine* [1925] VLR 363; *Godecke v Kirwan* (1973) 129 CLR 629, 646–7. Cf *Powell v Jones* [1968] SASR 394.

In *Godecke v Kirwan*,[102] an offer to purchase land was made in the form of a document which set out the principal terms of the transaction. Clause 6 provided that the purchasers would, if required by the vendor, sign a further agreement to be prepared by the vendor's solicitors "containing the foregoing and such other covenants and conditions as they may reasonably require". The document was countersigned by the vendor by way of acceptance. The High Court held that the agreement recorded in the document was binding. Clause 6 did not require further agreement between the parties but allowed the vendor's solicitors to add terms unilaterally.[103] It is well accepted that a contract can leave even essential terms to be determined by a third party and that the power can be left to the solicitor acting for one of the parties.[104] Walsh J, with whom Mason J agreed, accepted that a binding contract could leave a matter to be determined by one of the parties.[105] In this case, the vendor's solicitors could only add terms that were consistent with those set out in the offer and were reasonable in an objective sense.[106] The court could determine whether any terms they sought to add were reasonable according to objective criteria.[107]

The fact that a contractual provision leaves to one of the parties "a latitude of choice as to the manner in which agreed stipulations shall be carried into effect" does not render the provision illusory.[108] It has also been held that a discretion conferred on one of the parties will not render that party's promises illusory if the discretion relates to the fulfilment of a condition on which performance of the contract depends or if the discretion is to be exercised according to objective criteria. A "subject to finance" clause in a contract for the sale of land will usually fulfil both those criteria and will not, therefore, render the purchaser's promises illusory.

In *Meehan v Jones*,[109] a contract for the sale of land was made subject to the purchaser "receiving approval for finance on satisfactory terms and conditions". The vendor argued that the contract was void for uncertainty because the language of the clause was meaningless, conferred a discretion on the purchaser as to whether to perform, and left a vital matter to be determined by the purchaser. The High Court held that the clause required finance to be satisfactory to the purchaser. The purchaser was required to act honestly, and perhaps also reasonably, in deciding whether finance was satisfactory.[110] Since the court could assess the purchaser's fulfilment of the standards of honesty and reasonableness, the purchaser's obligation was enforceable. Mason J held that the existence of this obligation meant the purchaser did not have a discretion as to whether he would carry out his side of the bargain.[111] Gibbs CJ held that a contract is illusory where one of the parties is given a discretion as to whether to perform the contract but not where one of the parties has a discretion in relation to the fulfilment of a condition on which the contract depends.[112] The agreement is then

102 *Godecke v Kirwan* (1973) 129 CLR 629.
103 *Godecke v Kirwan* (1973) 129 CLR 629, 645.
104 *Godecke v Kirwan* (1973) 129 CLR 629, 645.
105 *Godecke v Kirwan* (1973) 129 CLR 629, 642.
106 *Godecke v Kirwan* (1973) 129 CLR 629, 642.
107 *Godecke v Kirwan* (1973) 129 CLR 629, 642–3.
108 *Thorby v Goldberg* (1964) 112 CLR 597, 605.
109 *Meehan v Jones* (1982) 149 CLR 571.
110 As to the nature of the purchaser's obligation, see below [20.35].
111 *Meehan v Jones* (1982) 149 CLR 571, 589–90.
112 *Meehan v Jones* (1982) 149 CLR 571, 581.

analogous to an option, which can usually be regarded as a contract which is conditional on the grantee giving notice of exercise of the option.[113]

SEVERANCE

[6.65] Whether an incomplete, uncertain or illusory provision will invalidate the entire agreement depends on the essentiality of the term and the intention of the parties disclosed by the agreement.[114] If the incomplete, uncertain or illusory provision is essential, then the contract must fail. If the relevant provision is not essential, the crucial question is whether the court can infer an intention that the agreement should be valid in the absence of the relevant provision. If such an intention can be inferred, then the offending provision can be severed, leaving the remainder of the agreement enforceable. In *Fitzgerald v Masters*,[115] a contract for the sale of a half-interest in a farm set out the essential terms but included a clause which purported to incorporate the "usual conditions of sale in use or approved by the Real Estate Institute of New South Wales relating to sales by private contract of lands held under the Crown Lands Act". This clause was meaningless because there were no such terms. The High Court held that it was severable from the rest of the contract because the clause was merely an appendage to the agreement. It was clear that the parties intended their agreement to subsist even if the clause should fail to incorporate any additional conditions.[116] In *Whitlock v Brew*,[117] on the other hand, the High Court held that the uncertain clause obliging the purchaser to grant a lease to the Shell Co could not be severed. Kitto J said:

> It is therefore clear on the face of the document that the parties had no intention of agreeing upon a sale which would entitle the purchaser to vacant possession without having to grant any lease to the Shell Co.; and it follows that to treat the "contract" as binding though shorn of condition 5 would be to turn the sale into a different sort of sale from that which the parties contemplated. Courts are of course anxious to hold the parties to what they have agreed upon, but there can be no justification for holding them to something they have not agreed upon.[118]

WAIVER

[6.70] It may also be possible for an uncertain, incomplete or illusory provision in a contract to be waived by the party for whose benefit that clause was inserted. Where performance of a contract is subject to fulfilment of a condition which has not been fulfilled, there is no doubt that the party for whose benefit that condition was inserted can waive fulfilment of the condition and enforce the contract.[119] Where a contract for the sale of a house is made subject to the purchaser obtaining finance from a particular lender, for example, the purchaser may choose to proceed with the transaction even if finance has not been obtained from that lender. The question then arises whether it is possible for one party to waive the benefit of an

113 See above [3.50].

114 *Life Insurance Co of Australia Ltd v Phillips* (1925) 36 CLR 60, 72; *Whitlock v Brew* (1968) 118 CLR 445, 461.

115 *Fitzgerald v Masters* (1956) 95 CLR 420.

116 *Fitzgerald v Masters* (1956) 95 CLR 420, 427–8, 438.

117 *Whitlock v Brew* (1968) 118 CLR 445.

118 *Whitlock v Brew* (1968) 118 CLR 445, 457.

119 See [20.55].

uncertain or illusory term of the contract made by the other party. In *Grime v Bartholomew*,[120] the Supreme Court of New South Wales held that a party cannot waive an uncertain clause that is essential to the contract because the uncertainty means the parties failed to reach an agreement at all. Since there is no contract, no right of waiver can arise. In *Bradford v Zahra*,[121] on the other hand, a purchaser successfully waived the benefit of an uncertain "subject to finance" clause and thereby "removed" the uncertainty. It may also be possible to waive the benefit of a failed machinery provision, provided it is entirely for the benefit of one party and is not essential to the operation of the agreement.[122]

120 *Grime v Bartholomew* [1972] 2 NSWLR 827.

121 *Bradford v Zahra* [1977] Qd R 24.

122 See *George v Roach* (1942) 67 CLR 253.

CHAPTER **7**

Formalities

[7.05] The common law does not require a contract to be in any particular form.[1] A verbal agreement is enforceable at common law, and its existence can be established by oral testimony. There are many statutes that prescribe formal requirements for contracts of particular types, principally for the protection of consumers. Many different types of contract are affected, and they include contracts involving the provision of consumer credit, the sale of motor vehicles, residential tenancies, door-to-door sales and building contracts. The consequences of a failure to comply with these formal requirements vary from statute to statute, but they include penalties, such as fines, as well as civil consequences, such as non-enforceability of the agreement or parts of the agreement.

Requirements as to the form of contracts are said to serve several purposes.[2] First, they provide reliable evidence of the fact that a contract has been made and allow its terms to be identified more easily. Secondly, they promote caution, by drawing the attention of the parties to the potentially serious consequences of the agreement. Thirdly, they protect vulnerable parties, by forcing stronger parties to set out the terms they wish to impose in a form that makes the terms more likely to be understood, and harsh or important terms more likely to be noticed by the vulnerable party. Fourthly, they have a channelling function, helping to identify particular types of transactions and to mark them as enforceable or unenforceable. A legal form such as that prescribed by the *Statute of Frauds* can be used by the parties to express the seriousness of their intentions and can deliberately be avoided by parties seeking to indicate that they do not yet intend to be bound.[3] Despite those worthy objectives, the circumstances

1 *Beckham v Drake* (1841) 9 M & W 79, 92–3; 152 ER 35, 40–1.
2 Fuller, "Consideration and Form" (1941) 41 *Columbia Law Review* 799, 800–4; Peel, *The Law of Contract* (14th ed, 2015), [5-002].
3 Fuller, "Consideration and Form" (1941) 41 *Columbia Law Review* 799, 801–2.

and ways in which formal requirements have been imposed have been the subject of trenchant criticism, as we shall see in this chapter.

THE STATUTE OF FRAUDS

[7.10] The formal requirements that have sparked the most litigation are those that originated in a 1677 English statute known as the *Statute of Frauds*. The *Statute of Frauds* provided that no action could be brought on contracts of particular types unless the agreement or some memorandum or note of the agreement was in writing and signed. The legislation was designed to prevent fraudulent claims being made on the basis of false evidence. It was passed at a time of great social and political upheaval, when the rules of evidence prevented a person from testifying in litigation to which they were a party.[4] A plaintiff could pay a witness to give false testimony that a verbal agreement had been made with the defendant, and the defendant could not give evidence to deny it. The purpose of the statute, as stated in its preamble, was "the prevention of many fraudulent practices which are commonly endeavoured to be upheld by perjury and subornation of perjury".

The types of contracts affected by the *Statute of Frauds* included contracts of guarantee, contracts made in consideration of marriage, contracts for the sale of an interest in land, contracts not to be performed within the space of one year from the making of the contract and contracts for the sale of goods for a price of £10 or more. It is not easy to see why the drafters of the statute selected these particular types of contracts.[5] The English Law Revision Committee has observed that they seem to have been "arbitrarily selected and to exhibit no relevant common quality".[6]

The *Statute of Frauds* has been widely criticised.[7] A considerable amount of case law has been generated by the Statute, and Lord Wright has said that these cases are "all devoted to construing badly drawn and ill planned sections of a statute which was an extemporaneous excrescence on the common law".[8] In some cases, the legislation produces rather than avoids injustice, since it facilitates the avoidance of contracts which have in fact been made but do not comply with its requirements. This has led the courts to give the legislation a narrow operation and to develop exceptions that seem inconsistent with the language of the provisions. It has been said of the *Statute of Frauds* that had it "been always carried into execution according to the letter, it would have done ten times more mischief than it has done good, by protecting, rather than preventing, frauds".[9] Not all judges take such a critical view of the statute, and some are inclined to confine the exceptions on the basis that the statute and successor provisions still play an important role. In *Perpetual Executors & Trustees Association of Australia Ltd v Russell*,[10] for example, Evatt J insisted that a contract rendered unenforceable by the statute could not be relied upon as a defence:

4 Holdsworth, *History of English Law* (1924), Vol VI, pp 379–97.
5 Hening, "The Original Drafts of the Statute of Frauds and Their Authors" (1913) 61 *University of Pennsylvania Law Review* 283.
6 United Kingdom, Law Revision Committee, *Sixth Interim Report*, Cmd 5449 (1937).
7 See United Kingdom, Law Revision Committee, *Sixth Interim Report*, Cmd 5449 (1937).
8 Wright, *Legal Essays and Addresses* (1939), p 226.
9 *Simon v Metivier* (1766) 1 Wm Bl 599, 601; 96 ER 347, 348.
10 *Perpetual Executors & Trustees Association of Australia Ltd v Russell* (1931) 45 CLR 146, 157.

> The *Statute of Frauds* has been made the target of many an attack. Some of these attacks are unjustified. Its clear object was to reject oral testimony in certain cases deemed to be of public importance. Times have changed, but, in spite of the criticisms, modern legislatures show a strong disinclination to remove the safeguards of the Statute. If a defendant can set up by parol an agreement within the mischief aimed at, a door is open for further evasion of the Statute.

The *Statute of Frauds* has been modified or repealed and partly re-enacted in all Australian States and Territories. Some *Statute of Frauds* provisions remain in force in each State and Territories, but they are far from uniform. Legislation in all States and Territories affects contracts for the sale of an interest in land.[11] In some jurisdictions, contracts of guarantee,[12] agreements made in consideration of marriage,[13] agreements not to be performed within the space of one year[14] and contracts for the sale of goods over a certain price[15] remain affected.[16]

In Victoria, for example, s 126 of the *Instruments Act 1958* provides that:

> An action must not be brought to charge a person upon a special promise to answer for the debt, default or miscarriage of another person or upon a contract for the sale or other disposition of an interest in land unless the agreement on which the action is brought, or a memorandum or note of the agreement, is in writing signed by the person to be charged or by a person lawfully authorised in writing by that person to sign such an agreement, memorandum or note.

Contracts of guarantee

[7.15] One category of contract covered by the *Statute of Frauds* was a "special promise to answer for the debt, default or miscarriages of another person". This expression has long been held to cover a guarantee, but not an indemnity.[17] A *guarantee* is a promise to pay another person's debt if that person defaults. The debtor's obligation is primary, and the guarantor's is secondary. An *indemnity*, on the other hand, involves a primary obligation. An indemnity is a promise to keep another person free from harm or to ensure that the person suffers no loss arising out of particular circumstances. An indemnity given in connection with a loan is a promise to ensure that the creditor suffers no loss arising out of the transaction with the debtor. Apart from the *Statute of Frauds*, the practical importance of the distinction is that the obligation under a guarantee is contingent upon the existence of the debtor's obligation, while an indemnity is not. If the debtor's obligation is unenforceable or is discharged for any reason, then a guarantee of that obligation will automatically be discharged. A promise to indemnify the creditor against loss resulting from the transaction with the debtor will remain enforceable even if the creditor's rights against the debtor are not.

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11 *Civil Law (Property) Act 2006* (ACT), s 204; *Conveyancing Act 1919* (NSW), s 54A; *Law of Property Act* (NT), s 62; *Property Law Act 1974* (Qld), s 59; *Law of Property Act 1936* (SA), s 26(1); *Conveyancing and Law of Property Act 1884* (Tas), s 36(1); *Mercantile Law Act 1935* (Tas), s 6; *Instruments Act 1958* (Vic), s 126; *Law Reform (Statute of Frauds) Act 1962* (WA), s 2; *Statute of Frauds 1677* (UK), s 4.

12 *Law of Property Act* (NT), s 58; *Mercantile Law Act 1935* (Tas), s 6; *Property Law Act 1974* (Qld), s 56; *Instruments Act 1958* (Vic), s 126(1); *Law Reform (Statute of Frauds) Act 1962* (WA), s 2; *Statute of Frauds 1677* (UK), s 4.

13 *Mercantile Law Act 1935* (Tas), s 6.

14 *Mercantile Law Act 1935* (Tas), s 6.

15 *Sale of Goods Act 1896* (Tas), s 9; *Sale of Goods Act 1895* (WA), s 4.

16 Contracts involving a special promise by an executor or administrator to answer damages out of his or her own estate also remain affected in Tasmania: *Mercantile Law Act 1935*, s 6.

17 *Yeoman Credit Ltd v Latter* [1961] 1 WLR 828.

There is no obvious reason for requiring writing in the case of guarantees but not indemnities. An indemnity is a more onerous obligation than a guarantee, and there is no reason to think that false claims relating to guarantees are more likely than false claims relating to indemnities. It has also been held that a guarantee given as an incidental part of a larger transaction will not be caught by the statute. On this basis, verbal guarantees given by *del credere* agents (ie, agents who, in return for extra commission, guarantee the obligations of contracting parties introduced to the principal) have been enforced.[18] The courts have also been prepared to enforce guarantees given by persons seeking to have property in which they are interested freed from an incumbrance.[19] Also exempted have been transactions in which a person makes his or her property available as security for another person's debts without undertaking any personal liability.[20] While it might be argued that fraudulent claims are less likely in these situations, it is difficult to reconcile their exclusion with the wording of the statute. Commentators have suggested that, given the scope of the exceptions to this part of the statute and the fine distinctions involved in applying them, the requirement of writing for guarantees should be abandoned in those jurisdictions that retain it.[21]

Contracts dealing with an interest in land

[7.20] The most important *Statute of Frauds* provisions are those affecting contracts involving dealings in land. Expressions such as "contract for the sale or other disposition of an interest in land" used in the legislation cover not only contracts for the sale of land but also other dealings in interests in land, such as leases and mortgages. An option to purchase or acquire an interest in land is also covered,[22] as is an agreement to transfer land to be acquired in the future.[23] A contract to declare a trust is regarded as a contract for the sale or disposition of an interest in land, even though it involves the creation of a new interest in the land, rather than the conveyance of an existing interest.[24] There is a wealth of case law on what amounts to an "interest in land" for the purpose of the statute.[25]

THE FORMALITIES REQUIRED

[7.25] The *Statute of Frauds* and successor legislation provide that an action shall not be brought on a contract of a particular type unless the agreement, or a memorandum or note of the agreement, is in writing and signed by the party to be charged on the contract. The statute contemplates reliance on two different types of document. First, where the contract is

18 *Anthoness v Melbourne Malting and Brewing Co* (1888) 14 VLR 916, 931.

19 *Fitzgerald v Dressler* (1859) 7 CB (NS) 374; 141 ER 861. See also *Marginson v Ian Potter & Co* (1976) 136 CLR 161; *Williams v Leper* (1766) 3 Burr 1886; 97 ER 1152. A may, eg, buy goods from B which are held by X as security for a debt owed by B to X. A may induce X to deliver the goods to her by promising to pay B's debt if B defaults. It may be said that A's promise is not within the statute because her main object is to protect her property, rather than to answer for B's debt.

20 *Harvey v Edwards Dunlop and Co Ltd* (1927) 39 CLR 302, 311–2.

21 See, eg, Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [16.9]–[16.19]; Peel, *The Law of Contract* (14th ed, 2015), [5-018].

22 *Jeffrey v Anderson* [1914] St R Q 66; *Mainline Investments Pty Ltd v Davlon Pty Ltd* [1969] 2 NSWR 392.

23 *Riches v Hogben* [1986] 1 Qd R 315.

24 *Khoury v Khouri* [2006] NSWCA 184; (2006) 66 NSWLR 241.

25 See Greig and Davis, *The Law of Contract* (1987), pp 683–92.

made in writing, the plaintiff[26] may rely on the written contract. Secondly, where the contract is made verbally, the plaintiff may rely on a memorandum or note of the agreement, that is, a document that provides evidence of the existence of the verbal agreement. Most of the case law is concerned with the second type of document. A document need not be created as a memorandum of the contract in order to satisfy the statute. Documents such as receipts and letters are commonly relied upon.

Five principal issues arise in determining whether a particular document or documents satisfy the statute: first, the amount of detail a document must contain in order to be regarded as a "memorandum or note" of a contract; secondly, when a document must come into existence in order to satisfy the statute; thirdly, when separate documents can be read or joined together to satisfy the statute; fourthly, when a document is taken to be "signed" for the purpose of the statute; and fifthly, whether a document in electronic form can satisfy the statute.

Contents of memorandum or note

[7.30] A memorandum or note must contain all of the terms,[27] or at least all of the essential terms,[28] of the contract other than those the law will imply. This means that the parties, the subject matter and the consideration[29] must be identified in the document, along with any other essential provisions such as the terms of payment.[30] In *Pirie v Saunders*,[31] a solicitor's notes of instructions to prepare a draft lease were held to be inadequate because, among other things, they contemplated that special conditions relating to certain matters would be formulated at a later time. A document that omits reference to a particular term may be relied upon if the term is exclusively for the benefit of the plaintiff, since the plaintiff may then waive the benefit of the term.[32]

A party may be described in the document, rather than named, provided the description is sufficient to identify the party.[33] Thus, a reference to the "owner" of a particular property will be sufficient. Similarly, the subject matter may be described in general terms, provided it points to some particular property. Even expressions such as "my house" have been found to be acceptable, with oral evidence being admitted to identify the house in question.[34] A document will, however, be inadequate if it says only that "part of" a particular property is being sold, without identifying which part.[35]

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26 The person seeking to enforce the contract will be referred to in this chapter as the *plaintiff* and the person against whom the contract is sought to be enforced (ie, the party to be charged on the contract) as the *defendant*.

27 *Sinclair, Scott & Co Ltd v Naughton* (1929) 43 CLR 310, 318–9.

28 *Harvey v Edwards Dunlop & Co Ltd* (1927) 39 CLR 302, 307.

29 Except in the case of guarantees: *Law of Property Act* (NT), s 58(2); *Property Law Act 1974* (Qld), s 56(2); *Mercantile Law Act 1935* (Tas), s 12; *Instruments Act 1958* (Vic), s 129; *Mercantile Law Amendment Act 1856* (Imp), s 3, adopted in Western Australia by *Imperial Acts Adopting Ordinance 1867*, 31 Vict No 8.

30 *Corcoran v O'Rourke* (1888) 14 VLR 889; *Sinclair, Scott & Co Ltd v Naughton* (1929) 43 CLR 310, 318–9.

31 *Pirie v Saunders* (1961) 104 CLR 149, 155–6.

32 See *Bastard v McCallum* [1924] VLR 9, 27.

33 See *Tooth & Co Ltd v Bryen (No 2)* (1922) 22 SR (NSW) 541, 549; *Di Biase v Rezek* [1971] 1 NSWLR 735, 742–3; *Rosser v Austral Wine and Spirit Co Pty Ltd* [1980] VR 313, 316–8.

34 See *Cowley v Watts* (1853) 22 LJ Ch 591.

35 *Pirie v Saunders* (1961) 104 CLR 149, 155.

Time of creation of memorandum or note

[7.35] A memorandum must generally come into existence after the contract has been made. Any document made earlier cannot establish that a contract was made but only indicate a probability that a contract would be made.[36] An exception is made in the case of a written offer made by the defendant, which is subsequently accepted verbally by the plaintiff.[37] This exception has been explained on the basis that, once the offer is accepted, the document setting out the terms of the offer can be regarded as an agreement in writing, rather than just a memorandum or note of an oral agreement.[38] In *Pirie v Saunders*,[39] the High Court refused to extend this exception to a solicitor's notes recording verbal instructions to prepare a draft lease. Those notes could not be recognised as a memorandum or note of a concluded agreement, because the parties may have intended that no binding contract be made until the formal document was executed. A written offer, on the other hand, does record terms on which the offeror is prepared to be bound immediately upon acceptance.

Joinder of documents

[7.40] It is often necessary to rely on more than one document to satisfy the statutory requirements. It may be, for example, that some of the terms of a transaction are set out in one document, such as a letter, while other terms and the defendant's signature are set out in another document, such as a reply to that letter. The acceptance of two documents as together constituting a memorandum or note of a contract is known as joinder of documents. The courts will allow joinder of documents that are physically connected, such as a letter and the envelope in which it was posted.[40] Where there has been no physical connection between two documents, the documents may be joined by a reference in one document to the other. Some difficulty arises in determining how specific that reference must be.

In *Thomson v McInnes*,[41] the High Court held insufficient a document that acknowledged a sum "being a deposit and first part purchase money for 320 acres of land in the Parish of Broadwater". The court held that these words could not be construed as a reference to other documents passing between the parties that provided particulars of the agreement. Griffith CJ held that the reference in the signed document "must be to some other document as such, and not merely to some transaction or event in the course of which another document may or may not have been written".[42] It is necessary, he said, to find some words that are capable of referring to another document, rather than to a transaction or event. The language of the receipt was not capable of referring to another document. A less stringent approach may have been approved by Knox CJ, Gavan Duffy J and Starke J in *Harvey v Edwards Dunlop and Co Ltd*,[43] when they adopted the following principle:

36 *Haydon v McLeod* (1901) 27 VLR 395, 402.

37 *Heppingstone v Stewart* (1901) 12 CLR 126; *Wight v Haberdan Pty Ltd* [1984] 2 NSWLR 280.

38 *Haydon v McLeod* (1901) 27 VLR 395, 406; *O'Young v Walter Reid & Co Ltd* (1932) 47 CLR 497, 513. But cf *Heppingstone v Stewart* (1901) 12 CLR 126, 136; *Pirie v Saunders* (1961) 104 CLR 149, 154.

39 *Pirie v Saunders* (1961) 104 CLR 149, 155.

40 *Pearce v Gardner* [1897] 1 QB 688.

41 *Thomson v McInnes* (1911) 12 CLR 562.

42 *Thomson v McInnes* (1911) 12 CLR 562, 569.

43 *Harvey v Edwards Dunlop and Co Ltd* (1927) 39 CLR 302.

> If you can spell out of the document a reference in it to some other transaction, you are at liberty to give evidence as to what that other transaction is, and, if that other transaction contains all the terms in writing, then you get a sufficient memorandum within the statute by reading the two together.[44]

In *Tonitto v Bassal*,[45] the Bassals (the vendors) granted an option to purchase land to the Tonittos (the purchasers). A written option agreement was signed by the purchasers, but not by the vendors. That agreement provided that the option could be exercised by delivering a signed contract of sale in a certain form, together with a cheque for the deposit. The purchasers purported to exercise the option by giving a notice to the vendors, together with a cheque for the deposit, but without the signed contract of sale. The vendors' solicitors responded by letter saying that they did not regard "the option" as properly exercised because the purchasers had not complied with the mode of exercise stipulated in "the option agreement". The purchasers sought specific performance, relying on the letter from the vendors' solicitors, together with the option agreement as together forming a memorandum or note that satisfied the relevant statutory requirement. Bryson J held at first instance that the documents could not be read together since the letter did not specifically mention the option document. On that basis, neither document could be regarded as a sufficient memorandum of the contract. The New South Wales Court of Appeal held that if the words used in one document were capable of referring to another, but it was not clear whether they did, then oral evidence could be admitted to resolve the doubt.[46] In this case, references in the letter to the option and option agreement were capable of referring to the option document. The letter therefore incorporated the terms of the option and provided a sufficient memorandum or note to satisfy the statutory requirement.

Signature

[7.45] The *Statute of Frauds* and successor provisions all require that the document in question be signed by the party to be charged or by her or his authorised agent. Only in Victoria must the agent be authorised in writing.[47] Since the statute requires only that the document be signed by or on behalf of the party to be charged, an agreement will often be enforceable at law against only one of the parties. The courts do not require reciprocity of action and will allow a plaintiff who has not signed a document evidencing an agreement to enforce the agreement against a defendant who has signed such a document.[48]

The courts have taken a very liberal approach to the requirement of signature. Where the name of the party to be charged appears on the relevant document, that will be regarded as a signature, provided the document has been "authenticated" or recognised by that party as the final record of the contract.[49] This is known as the *authenticated signature fiction*. The principle does not apply to a printed name in a document to which the parties intend to affix

44 *Harvey v Edwards Dunlop and Co Ltd* (1927) 39 CLR 302, 307, quoting *Stokes v Whicher* [1920] 1 Ch 411, 418. See *Elias v George Sahely & Co* [1983] 1 AC 646, 655 to similar effect.

45 *Tonitto v Bassal* (1992) 28 NSWLR 564.

46 *Tonitto v Bassal* (1992) 28 NSWLR 564, 572–3, applying *Long v Millar* (1879) 4 CPD 450.

47 *Instruments Act 1958* (Vic), s 126(1).

48 *Heppingstone v Stewart* (1910) 12 CLR 126.

49 *Schneider v Norris* (1814) 2 M & S 286; 105 ER 388; *Neill v Hewens* (1953) 89 CLR 1. For a recent application of the principle, see *Konstantinidis v Baloglow* [2000] NSWSC 1229.

their handwritten signatures.[50] In *Pirie v Saunders*,[51] the High Court rejected the conclusion of the Full Court that the defendant could be said to have recognised his solicitor's notes of instructions to prepare a draft lease as a record of a prior agreement with the plaintiff and thereby "authenticated" his signature. The court held that the principle can "have no application to any document which is not in some way or other recognisable as a note or memorandum of a concluded agreement".[52] The solicitor's notes were not capable of being recognised as such a note. Moreover, given the character of the document and the fact that it had not been established that the defendant knew what the solicitor was writing down, the defendant could not be said to have recognised the document as a record of the agreement.[53]

Documents in electronic form

[7.50] Electronic Transactions Acts (ETAs) in force in all Australian States and Territories provide that, for the purposes of a law of the relevant jurisdiction, "a transaction is not invalid" because it took place wholly or partly by means of one or more electronic communications.[54] In Victoria, s 126 of the *Instruments Act 1958* specifically provides that its requirements "may be met in accordance with the *Electronic Transactions (Victoria) Act 2000*".[55] In other States and Territories, it seems that the relevant ETA provision is intended to allow electronic communications to satisfy the *Statute of Frauds* provisions. The choice of language may be regarded as unfortunate, however, because it is well accepted that non-compliance with the *Statute of Frauds* provisions does not render a contract invalid, but simply unenforceable.[56] Any doubt as to whether the ETAs were intended to cover the *Statute of Frauds* provisions may be resolved by reference to the stated object of the legislation, which is "to provide a regulatory framework that", among other things, "facilitates the use of electronic transactions".[57]

The ETAs also provide that where a law requires a person's signature, that requirement is taken to have been met if an appropriately reliable method has been used to identify the person and indicate the person's intention, and the person consents to the requirement being met by that method.[58] In email correspondence, a person's email address may adequately identify

50 *Farrelly v Hircock* [1971] Qd R 341, 356.

51 *Pirie v Saunders* (1961) 104 CLR 149.

52 *Pirie v Saunders* (1961) 104 CLR 149, 154.

53 *Pirie v Saunders* (1961) 104 CLR 149, 155.

54 *Electronic Transactions Act 2001* (ACT), s 7; *Electronic Transactions Act 1999* (Cth), s 8; *Electronic Transactions Act 2000* (NSW), s 7; *Electronic Transactions (Northern Territory) Act*, s 7; *Electronic Transactions (Queensland) Act 2001*, s 8; *Electronic Communications Act 2000* (SA), s 7 (and see *Electronic Transactions Regulations 2017* (SA), reg 5); *Electronic Transactions Act 2000* (Tas), s 5; *Electronic Transactions (Victoria) Act 2000*, s 7; *Electronic Transactions Act 2011* (WA), s 8.

55 *Instruments Act 1958* (Vic), s 126(2).

56 See [7.55] and Greig and Davis, *The Law of Contract* (1987), pp 715–6.

57 *Electronic Transactions Act 2001* (ACT), s 3; *Electronic Transactions Act 1999* (Cth), s 3; *Electronic Transactions Act 2000* (NSW), s 3; *Electronic Transactions (Northern Territory) Act*, s 3; *Electronic Transactions (Queensland) Act 2001*, s 3; *Electronic Communications Act 2000* (SA), s 3; *Electronic Transactions (Victoria) Act 2000*, s 4; *Electronic Transactions Act 2011* (WA), s 3.

58 *Electronic Transactions Act 2001* (ACT), s 9; *Electronic Transactions Act 1999* (Cth), s 10; *Electronic Transactions Act 2000* (NSW), s 9; *Electronic Transactions (Northern Territory) Act*, s 9; *Electronic Transactions (Queensland) Act 2001*, s 14; *Electronic Communications Act 2000* (SA), s 9; *Electronic Transactions Act 2000* (Tas), s 7; *Electronic Transactions (Victoria) Act 2000*, s 9; *Electronic Transactions Act 2011* (WA), s 10.

them.[59] Given the liberal approach the courts have taken in relation to what constitutes a "signature",[60] an electronic indication of approval or consent to contract terms may be regarded as a signature even without resorting to the provisions of the ETAs.

THE CONSEQUENCES OF NON-COMPLIANCE

[7.55] The *Statute of Frauds* and successor provisions do not make contracts void for non-compliance but simply provide that no action shall be taken to enforce them.[61] Although the contract itself is unenforceable, the dealings between the parties may still give rise to enforceable rights. First, it may be possible to rely on the contract as a defence in some circumstances. Secondly, specific performance of the contract may be available under the doctrine of part performance. Thirdly, the circumstances may give rise to a constructive trust or equitable estoppel, which will not be affected by the relevant statutory provision. Fourthly, any benefits conferred on one party by the other under the unenforceable contract may be the subject of a claim in restitution. Fifthly, where only part of the agreement is unenforceable, it may be possible to sever that part of the agreement, leaving the remainder enforceable.

Reliance on the contract as a defence

[7.60] The extent to which an unenforceable contract can be relied on to provide a defence is a controversial question. Since affected contracts are not void, and the statutes provide only that no action shall be brought on them, the courts have allowed unenforceable contracts to be relied upon in some cases to establish a defence.[62] In *Thomas v Brown*,[63] for example, a vendor who remained willing to proceed with a verbal contract for the sale of land successfully relied on that contract as a defence to an action by the purchaser to recover money paid as a deposit.[64]

Dictum in *Perpetual Executors and Trustees Association of Australia Ltd v Russell*[65] suggests a more restrictive approach.[66] The plaintiffs in that case sought possession of land from the defendant, who was in possession pursuant to a verbal contract to purchase the land. The trial judge dismissed the plaintiffs' action on the basis that the *Statute of Frauds* did not prevent the defendant from relying on the contract as a defence.[67] The High Court overturned

59 *Bullhead Pty Ltd v Brickmakers Place Pty Ltd* [2017] VSC 206, [170] (not disturbed on appeal: [2018] VSCA 316).

60 See [7.45].

61 *Leroux v Brown* (1852) 12 CB 801; 138 ER 1119; *Maddison v Alderson* (1883) 8 App Cas 467, 474. Note that the position is different in the United Kingdom in relation to contracts for the sale of land. The *Law of Property (Miscellaneous Provisions) Act 1989* (c 34), s 2(1) provides that: "A contract for the sale or other disposition of an interest in land can only be made in writing and only by incorporating all the terms which the parties have expressly agreed in one document or, where contracts are exchanged, in each".

62 *Miles v New Zealand Alford Estate Co* (1886) 32 Ch D 266; *Head v Kelk* (1963) 63 SR (NSW) 340.

63 *Thomas v Brown* (1876) 1 QBD 714.

64 Where the vendor is unwilling to proceed, the purchaser can recover the money on the basis of a total failure of consideration: see *Noske Bros Pty Ltd v Leys* [1930] SASR 43, 45.

65 *Perpetual Executors and Trustees Association of Australia Ltd v Russell* (1931) 45 CLR 146.

66 But see *Head v Kelk* (1963) 63 SR (NSW) 340, 348.

67 The decision may be explained on a narrower basis. See Williams, "Availability by Way of Defence of Contracts Not Complying with the Statute of Frauds" (1934) 50 *Law Quarterly Review* 532; *Take Harvest Ltd v Liu* [1993] AC 552, 570.

the decision, observing that "it may safely be said that neither at law nor in equity can a claim unenforceable by action because of the Statute be enforced by counterclaim or defence".[68] The Privy Council has suggested that the High Court "went a little too far" with this statement.[69] The Privy Council said the question a court must decide is "whether the party who relies on the oral agreement is in substance seeking to enforce it", regardless of whether the agreement is raised by way of "claim, defence, counterclaim or otherwise".[70]

Part performance

[7.65] Equity has long recognised that the *Statute of Frauds* is capable of facilitating fraud, as well as preventing it. Where one of the parties has wholly or partly performed his or her obligations under a contract, it may be fraudulent or unconscionable for the other party to rely on the statute. Courts of equity will therefore grant specific performance of verbal contracts falling within the statute if they have been partly performed. Although the doctrine of part performance is difficult to reconcile with the wording of the *Statute of Frauds* itself, it is expressly preserved in most Australian jurisdictions.[71] The doctrine is justified on the basis that a court granting specific performance is not enforcing the contract but instead is charging the defendant "upon the equities" arising from the acts performed by the plaintiff in execution of the contract.[72]

Only equitable relief can be awarded to give effect to the "equity" created by part performance of an unenforceable contract.[73] This means that the only remedies available are specific performance or equitable damages in lieu of specific performance.[74] The doctrine of part performance does not provide a basis for an award of damages at common law. Accordingly, where part performance is established, but equitable relief is not available in the circumstances of the case,[75] the plaintiff will be left without a remedy.

Acts establishing the existence of a contract

[7.70] The doctrine of part performance operates only where the plaintiff has performed some acts that establish the existence of a contract between the parties relating to the land. In *Maddison v Alderson*, Lord Selborne LC held that "the acts relied upon as part performance must be unequivocally, and in their own nature, referable to some such agreement as that alleged".[76] In that case, a woman had been induced to act as a housekeeper without wages

68 *Perpetual Executors and Trustees Association of Australia Ltd v Russell* (1931) 45 CLR 146, 153.

69 *Take Harvest Ltd v Liu* [1993] AC 552, 549.

70 *Take Harvest Ltd v Liu* [1993] AC 552, 569.

71 *Civil Law (Property) Act 2006* (ACT), s 204(2)(c); *Conveyancing Act 1919* (NSW), s 54A(2); *Law of Property Act* (NT), s 5(c); *Property Law Act 1974* (Qld), s 6(d); *Law of Property Act 1936* (SA), s 26(2); *Conveyancing and Law of Property Act 1884* (Tas), s 36(2); *Property Law Act 1969* (WA), s 36(d). Note that the doctrine of part performance has been abolished in the United Kingdom by the *Law of Property (Miscellaneous Provisions) Act 1989* (c 34), s 2(8). See *Yaxley v Gotts* [2000] Ch 162, 171–2.

72 *McBride v Sandland* (1918) 25 CLR 69, 77; *JC Williamson Ltd v Lukey and Mulholland* (1931) 45 CLR 282, 300, 309.

73 *JC Williamson Ltd v Lukey and Mulholland* (1931) 45 CLR 282, 297.

74 See Chapter 30. As to whether an injunction could be granted, see *JC Williamson Ltd v Lukey and Mulholland* (1931) 45 CLR 282, 293–4, 301, 310, 318.

75 As to the availability of equitable relief, see Chapter 30.

76 *Maddison v Alderson* (1883) 8 App Cas 467, 479.

for many years on condition that her employer would make a will leaving her a life interest in a farm property. He did sign such a will before he died, but it was not properly attested and was therefore invalid. The House of Lords held her performance of housekeeping duties to be insufficient to establish part performance of the agreement, since they did not necessarily point to the existence of a contract, "much less of a contract concerning her master's land".[77] Lord O'Hagan said that the plaintiff "might unquestionably have remained with her master in the enjoyment of some present comforts and the expectation of some future provision, though no such contract had been ever dreamt of".[78]

More liberal tests have been proposed, most notably by the House of Lords in *Steadman v Steadman*,[79] but the High Court affirmed the strict *Maddison v Alderson* test in *Pipikos v Trayans*.[80] In that case, Pipikos claimed that his brother and sister-in-law agreed to sell him a half-interest in certain land they owned, with the purchase price to be paid partly by Pipokos funding his brother and sister-in-law's contribution to the purchase of another property and partly by way of a cash payment Pipikos claimed to have made to them. The High Court unanimously rejected Pipikos's argument that a more relaxed test should be applied, holding that both principle and High Court authority supported the retention of the strict test.[81] Kiefel CJ, Bell, Gageler and Keane JJ held that the basis of the part performance doctrine is that the court enforces the "equities arising from partial performance" rather than rights arising from the contract itself.[82] The acts relied upon must therefore show that the parties are "in the midst of an uncompleted contract for the sale or other disposition of an interest in land".[83]

> In a case where the parties are found, as a matter of fact, to be in that position, equity requires that the transaction be completed notwithstanding the objection of the defendant that the contract itself cannot be enforced by reason of non compliance with the Statute of Frauds. The requirement for unequivocal referability is essential to Lord Selborne's thesis that the court is not enforcing the contract – that would be contrary to the Statute of Frauds – but the equities generated by its partial performance. It is only where the acts of part performance are inherently and unequivocally referable to such a contract that it cannot be objected that, in truth, and contrary to the legislation, it is the parol contract that is being enforced.[84]

On the facts of *Pipikos v Trayans*, the payments made by Pipikos were clearly not unequivocally referable to a contract for the sale or disposition of an interest in land. As the trial judge observed, the acts were equally consistent with, for example, a contract of loan or some agreement involving unequal contributions to the real estate investment partnership.[85]

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77 *Maddison v Alderson* (1888) 8 App Cas 467, 480–1.

78 *Maddison v Alderson* (1888) 8 App Cas 467, 486. If these facts occurred in Australia today, the plaintiff might be able to obtain a remedy on the basis of equitable estoppel; see [7.85] and [9.185].

79 *Steadman v Steadman* [1976] AC 536, approving the decision of the English Court of Appeal in *Kingswood Estate Co Ltd v Anderson* [1963] 2 QB 169.

80 *Pipikos v Trayans* [2018] HCA 39.

81 *Pipikos v Trayans* [2018] HCA 39, [80] (Kiefel CJ, Bell, Gageler and Keane JJ), [121] (Nettle and Gordon JJ), [157]–[159] (Edelman J). One of the authorities relied upon was *Cooney v Burns* (1922) 30 CLR 216, discussed at [7.70].

82 *Pipikos v Trayans* [2018] HCA 39, [49]; cf [138]–[145], [151] (Edelman J).

83 *Pipikos v Trayans* [2018] HCA 39, [50].

84 *Pipikos v Trayans* [2018] HCA 39, [52].

85 *Pipikos v Trayans* [2018] HCA 39, [28].

Preparatory acts not sufficient

[7.75] Actions taken in preparation for performance of a contract will not allow a plaintiff to invoke the doctrine of part performance. Clearly acts done before an oral agreement is concluded cannot qualify.[86] But even where a verbal agreement has been made, preparatory actions will not be sufficient. In *Cooney v Burns*,[87] an agreement was made for the sale of a hotel operating from leased premises. The purchaser's solicitors prepared an assignment of the lease and made application for a transfer of the hotel licence, while the purchaser took an inventory of the chattels to be included in the sale. The High Court, by a majority of 4-1, held that these preparatory acts were insufficient to establish part performance.

Performance of obligations not required

[7.80] The doctrine of part performance does not require that the plaintiff has performed obligations under the contract, but only that the plaintiff has taken some action under the contract.[88] In *Regent v Millett*,[89] the plaintiffs, a married couple, sought specific performance of a contract to purchase a house property from the woman's parents. Although the plaintiffs were not required by the contract to take possession of the property, they had done so and had carried out repairs and renovations and paid mortgage instalments. The High Court rejected the defendants' argument that the acts of part performance must have been done in compliance with a requirement of the contract. If this were necessary, Gibbs J said, the utility of the doctrine of part performance "would be reduced to vanishing point".[90] Part performance may be established by acts done "pursuant to the contract", even where they are not required by the contract.[91]

Constructive trust and equitable estoppel

[7.85] The circumstances surrounding a verbal contract for the sale of land, even if insufficient to invoke the part performance doctrine, may give rise to a "common intention" constructive trust.[92] In *Ogilvie v Ryan*,[93] for example, Ogilvie proposed to Ryan that if she moved into his house and looked after him for the rest of his life, the house would be hers for as long as she lived. On that basis, Ryan moved into Ogilvie's house, performed nursing and housekeeping services for him, and spent money on repairs and improvements to the house. When Ogilvie died without mentioning Ryan in his will, Ogilvie's son, who was the executor of his estate, sought to evict Ryan. Holland J held that Ryan's actions were not unequivocally referable to a contract for an interest in the property since they could be explained on the basis of love and affection and an expectation that she was to be rewarded in some other way.[94] Ryan did succeed, however, in establishing a constructive trust that entitled her to occupy the property

86 *Hamblin v Marjoram* (1878) 12 SALR 62; *Sheppard v Warner* (1895) 1 ALR 168.

87 *Cooney v Burns* (1922) 30 CLR 216.

88 Despite earlier authority to the contrary, such as *Scott v White* [1938] VLR 188.

89 *Regent v Millett* (1976) 133 CLR 679.

90 *Regent v Millett* (1976) 133 CLR 679, 683.

91 *Regent v Millett* (1976) 133 CLR 679, 683.

92 See Harris, "The Doctrine of Part Performance and the Constructive Trust" (1993) 11 *Australian Bar Review* 27.

93 *Ogilvie v Ryan* [1976] 2 NSWLR 504.

94 *Ogilvie v Ryan* [1976] 2 NSWLR 504, 524.

for the remainder of her life. That constructive trust was based on the fact that the parties had a common intention that the defendant should be entitled to occupy the house for the rest of her life, and the defendant had conferred benefits on the deceased in the course of their joint occupation of the property and on the faith of that common intention.[95] It was therefore fraudulent or unconscionable for the Ogilvie or his executor to make a claim for possession based on the legal title.

An equitable estoppel may also arise where the plaintiff has acted to his or her detriment on the faith of an expectation induced by the defendant:

1. that the plaintiff will be granted an interest in land under a verbal contract;[96]
2. that the parties will enter into a written contract;[97] or
3. that the statute will not be relied upon.[98]

A plaintiff relying on equitable estoppel in these circumstances is not suing on the basis of any contract between the parties but is seeking to enforce an equity arising out of the circumstances by way of estoppel.[99] The *Statute of Frauds* and similar provisions do not prevent the enforcement of such an equity.[100] Similarly, it is well established that the *Statute of Frauds* and similar provisions do not inhibit the declaration of a constructive trust.[101] A court declaring a constructive trust is not enforcing the verbal contract, but recognising the plaintiff's beneficial interest in the property.

Restitution

[7.90] Where one of the parties to an unenforceable verbal contract has paid money or transferred goods to the other party or has performed services for that party, an action to recover the money or a reasonable sum for the goods or services may be available in restitution.[102] The leading case is *Pavey and Matthews Pty Ltd v Paul*,[103] which is discussed in detail in Chapter 10. In some cases, the relevant legislation will bar restitutionary claims, as well as claims on the contract.[104]

Severance

[7.95] If a contract contains several promises – some of which are required to be in writing and some of which are not – it may be possible to sever the promises required to be in writing.

95 *Ogilvie v Ryan* [1976] 2 NSWLR 504, 518–9.

96 *Riches v Hogben* [1986] 1 Qd R 315. Whether equitable estoppel can operate in this situation is now a matter of controversy: see [9.185].

97 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387.

98 *Collin v Holden* [1989] VR 510. See further Chapter 9.

99 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 433. See further [9.35].

100 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387. On the distinction between part performance and equitable estoppel, see *Pipikos v Trayans* [2018] HCA 39, [58]–[65] (Kiefel CJ, Bell, Gageler and Keane JJ); cf [96] (Nettle and Gordon JJ).

101 *Ogilvie v Ryan* [1976] 2 NSWLR 504, 519.

102 An action in debt may also be available: see Cooper, "The Statute of Frauds and Actions in Restitution and Debt" (1989) 19 *Western Australian Law Review* 56.

103 *Pavey and Matthews Pty Ltd v Paul* (1987) 162 CLR 221.

104 See [10.85].

If it is possible to sever the unenforceable parts of the contract, the remainder of the contract will be enforceable. The promises sought to be enforced must be independent of, and not "implicated with", the unenforceable promises.[105] They must be supported by an independent consideration or an identifiable part of a divisible consideration.[106]

VARIATION AND TERMINATION

[7.100] The courts draw an unsatisfactory distinction between variation and termination of contracts required to be in writing. An oral agreement terminating the contract will be effective, but an oral variation will not.[107] This means that, in a particular case, it may be of great importance to determine whether a written contract covered by the *Statute of Frauds* has been varied by a subsequent verbal agreement, or terminated and replaced.[108] In neither case will the new arrangements be enforceable. In the first case, the variation will be ineffective so that the contract will remain enforceable on its original terms; in the second, the contract will have been effectively terminated, but the new verbal contract will be unenforceable.

105 *Hodgson v Johnson* (1858) EB & E 685, 690; 120 ER 666.

106 *Horton v Jones* (1935) 53 CLR 475, 485; *Collin v Holden* [1989] VR 510, 512–3.

107 *Tallerman & Co Pty Ltd v Nathan's Merchandise (Victoria) Pty Ltd* (1956) 98 CLR 93, 112–3, 122–4, 143–4.

108 As to which, see [19.30].

CHAPTER **8**

Capacity

[8.05] A contract made with a person who lacks contractual capacity may not be legally binding, but rather able to be set aside at the option of the person who lacks capacity or, more commonly, their representatives. There are a number of classes of person who lack contractual capacity: people who are minors or underage, people with mental impairments and people who are intoxicated. Historically, married women lacked the capacity to enter into contracts. This situation has now been altered by legislation and is not discussed in this chapter.[1] A corporation has the capacity of a natural person, although in some cases, there may be limits on the power of the corporation to engage in certain activities. The capacity of corporations is also not discussed in this chapter.[2]

Typically contracts for essential items, called "necessaries", cannot be avoided. The consequences of a contract being made with a person who lacks legal capacity vary between jurisdictions and are governed by a combination of common law and statute, which are discussed in this chapter.

1 See Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [17.58]–[17.66].
2 See Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [17.67]–[17.71].

The reason for making contracts voidable in certain instances where one party lacks relevant capacity is to protect people in the relevant categories. People without the requisite legal capacity may not have been able to assess whether those contracts were in their own best interests. As we shall see in Part XI, there are a number of other factors that are considered to undermine the integrity of contractual consent, such as misrepresentation or duress, and also make a contract voidable.

MINORS

[8.10] In all jurisdictions in Australia, 18 is the age of "majority", or full legal capacity.[3] Persons under that age are described as either *infants* or *minors* (minors is the more modern term). The law relating to contracts with minors is somewhat technical and uncertain. The common law rules are not always consistent and have been overlaid with legislation. Although the legislation varies between the States and Territories, the main distinctions in this area are between contracts that are:

1. binding on the minor, namely contracts for *necessaries*;
2. binding unless repudiated (*voidable*);
3. only binding if *ratified*; and
4. of no effect (*void under statute*).

These issues are discussed below. The position in New South Wales is discussed separately because in that jurisdiction, there is comprehensive legislation dealing with contracts with minors.

BINDING CONTRACTS

Necessaries

[8.15] A first category of contracts made by minors are contracts for necessaries. Under common law, contracts for the supply of "necessary" goods and services are binding on infants and minors. In the case of goods, Sale of Goods legislation in jurisdictions other than New South Wales provides that "where necessaries are sold and delivered to a minor … he [or she] must pay a reasonable price therefor".[4] This legislation means that while a minor will be bound by a contract for necessary goods, he or she will only be bound to pay a reasonable price for those goods. The obligation of a minor or other person lacking capacity to contract to pay for necessaries has no application in circumstances where the supplier had not intended that the recipient should pay for the goods and services.[5]

The category of "necessaries" clearly includes food and drink necessary to maintain life. The category also extends beyond such items. Sale of Goods legislation provides that the term

3 *Age of Majority Act 1974* (ACT), s 5; *Minors (Property and Contracts) Act 1970* (NSW), ss 8–9; *Age of Majority Act* (NT), s 4; *Law Reform Act 1995* (Qld), s 17; *Age of Majority (Reduction) Act 1971* (SA), s 3; *Age of Majority Act 1973* (Tas), s 3; *Age of Majority Act 1977* (Vic), s 3; *Age of Majority Act 1972* (WA), s 5.

4 *Goods Act 1958* (Vic), s 7. See similarly: *Sale of Goods Act 1954* (ACT), s 7; *Sale of Goods Act* (NT), s 7; *Sale of Goods Act 1896* (Qld), s 5; *Sale of Goods Act 1895* (SA), s 2; *Sale of Goods Act 1896* (Tas), s 7; *Sale of Goods Act 1895* (WA), s 2.

5 *Aster Healthcare v Shafi* [2014] EWCA Civ 1350, [19].

"necessaries" means "goods suitable to the condition in life of such minor … and to his [or her] actual requirements at the time of the sale and delivery".[6] The common law has taken a similar approach. Thus, in assessing whether goods or services are necessaries, courts will consider the actual circumstances of the minor and the things that are suitable to the life of the minor in the context of those circumstances. The difficulty is that, of the relatively few cases on the question of what necessaries are, most were decided in or before the 19th century and raise different issues than might be faced today. Nonetheless, some of the cases give guidance on issues of contemporary relevance. One such issue is whether a motor vehicle is a necessary. A motor vehicle was held not to be a necessary in *Re Mundy*[7] and *Alliance Acceptance Co Ltd v Hinton*.[8] By contrast, in *Mercantile Credit v Spinks*,[9] a car was a necessary for a minor employed as a salesman. Services that have been found necessaries include the services of a lawyer,[10] medical services,[11] and instruction in a career.[12] Minors are also bound by contracts of apprenticeship and of employment.[13]

For goods or services to be necessaries, the minor must not be adequately supplied with the goods or services at the time of the contract. In *Scarborough v Sturzaker*,[14] the minor used his bicycle to travel the 12 miles distance between his home and his place of employment. The minor bought a new bicycle from the plaintiff. The old bicycle was given to the plaintiff in part-payment. The minor then refused to pay for the new bicycle and the plaintiff sued. McIntyre J in the Supreme Court of Tasmania allowed an action by the seller to recover the price of the bicycle. In the circumstances the bicycle was a necessary. Given the old bicycle had been given in part-payment of the new bicycle, the minor was not already sufficiently supplied with the item.

In *Bojczak v Gregorcewicz*,[15] the plaintiff paid the fare for the 18-year-old defendant (a minor) to come from Poland to Australia. The defendant promised to repay the amount but failed to do so. In an action to enforce the promise, the plaintiff argued that the contract was binding as one for necessaries. This plaintiff argued that the contract gave the defendant the opportunity to leave hard conditions in a communist country and to start a new life in Australia. The Supreme Court of South Australia held that the contract was not for necessaries. Ross J accepted the findings of the magistrate that the defendant did not come to Australia for the purpose of "providing herself with a means of self support, for she already had a job in Poland which was by Polish standards a satisfactory one".[16] Nor had the defendant come to Australia for the purpose of obtaining instruction. The fact the contract was beneficial to the defendant did not make it one for necessaries.

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6 *Goods Act 1958* (Vic), s 7. See similarly: *Sale of Goods Act 1954* (ACT), s 7; *Sale of Goods Act* (NT), s 7; *Sale of Goods Act 1896* (Qld), s 5; *Sale of Goods Act 1895* (SA), s 2; *Sale of Goods Act 1896* (Tas), s 7; *Sale of Goods Act 1895* (WA), s 2.

7 *Re Mundy* (1963) 19 ABC 165, 168–9.

8 *Alliance Acceptance Co Ltd v Hinton* (1964) 1 DCR (NSW) 5, 7.

9 *Mercantile Credit v Spinks* [1968] QWN 32.

10 *Helps v Clayton* (1964) 17 CB (NS) 553; 144 ER 222.

11 *Huggins v Wiseman* (1960) Carth 110; 90 ER 669.

12 *Blennerhassett's Institute of Accountancy Pty Ltd v Gairns* (1938) 55 WN (NSW) 89; *Minister for Education v Oxwell* [1966] WAR 39, 45. See also *McLaughlin v Darcy* (1918) 18 SR (NSW) 585.

13 See, eg, *Gadd v Thompson* [1911] 1 KB 304; *Bromley v Smith* [1909] 2 KB 235.

14 *Scarborough v Sturzaker* (1905) 1 Tas LR 117.

15 *Bojczak v Gregorcewicz* [1961] SASR 128.

16 *Bojczak v Gregorcewicz* [1961] SASR 128, 134.

A contract for necessaries will not be binding on the minor if it is harsh or oppressive[17] because such contracts cannot be regarded as benefiting the minor. In *De Francesco v Barnum*,[18] an apprenticeship deed bound the 14-year-old minor as an apprentice to the plaintiff for seven years for the purpose of being taught stage dancing. The minor agreed not to marry during the apprenticeship and not to accept professional engagements without the permission of the plaintiff. The plaintiff did not bind himself to provide the minor with engagements or to maintain her while unemployed. The pay for the minor under the agreement was not generous. The plaintiff could terminate the contract if, after a fair trial, the minor was found unfit for stage dancing. The plaintiff sued the defendant for the tort of inducing the minor away from her employment. Fry J held that the provisions of the deed were of an "extraordinary and an unusual character, which throw, or appear to throw, an inordinate power into the hands of the master without any correlative obligation on the part of the master".[19] Such a contract was not for the benefit of the minor and hence not binding on her.

Contract or restitution?

[8.20] Different views have been expressed about the basis for a minor's liability for necessaries.[20] One view is that the minor is liable in contract;[21] the other view is that the minor is liable on the basis of unjust enrichment.[22] In relation to goods, Sale of Goods legislation seems to support the second view, providing that a minor must pay a reasonable price for necessaries "sold and delivered".[23] Payment of a reasonable price is a restitutionary remedy consistent with the claim being based on unjust enrichment. If a minor was liable in contract, the contract price would be payable.

Another factor supporting liability based on unjust enrichment is that executory contracts (ie, contracts which have yet to be performed) for the supply of necessary goods have generally not been enforceable.[24] There can only be an obligation to make restitution for necessary services where the goods have actually been delivered. The situation is somewhat different for services. Contracts for necessary services have been held to be enforceable against a minor even where executory.[25] This suggests that the basis for liability for necessities may be contract. However, it is difficult to find a convincing reason for distinguishing between goods and services in this context.

17 See, eg, *Mercantile Union Guarantee Corp Ltd v Ball* [1937] 2 KB 498; *Alliance Acceptance Co Ltd v Hinton* (1964) 1 DCR (NSW) 5.

18 *De Francesco v Barnum* (1890) 45 ChD 430.

19 *De Francesco v Barnum* (1890) 45 ChD 430, 442.

20 See further Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [17.8]; Carter, *Contract Law in Australia* (7th ed, 2018), [15].

21 *Nash v Ingham* [1908] 2 KB 1, 11–3.

22 *Nash v Ingham* [1908] 2 KB 1, 8–9; *Re J* [1909] 1 Ch 574, 577; *Pontypridd Union v Drew* [1927] 1 KB 214, 220. On unjust enrichment and restitution, see below, Chapter 10.

23 *Goods Act 1958* (Vic), s 7. Similarly: *Sale of Goods Act 1954* (ACT), s 7; *Sale of Goods Act* (NT), s 7; *Sale of Goods Act 1896* (Qld), s 5; *Sale of Goods Act 1895* (SA), s 2; *Sale of Goods Act 1896* (Tas), s 7; *Sale of Goods Act 1895* (WA), s 2.

24 See Winfield, "Necessaries under the Sale of Goods Act 1893" (1942) 58 *Law Quarterly Review* 83.

25 See, eg, *Roberts v Gray* [1913] 1 KB 520; *McLaughlin v Darcy* (1918) 18 SR (NSW) 585.

CONTRACTS BINDING UNLESS REPUDIATED

[8.25] A second category of contracts made by minors are those that are binding unless repudiated by the minor during minority or within a reasonable time of reaching the age of majority. Such contracts are described as being *voidable* at the option of the minor. Repudiation may be found in words or conduct by the minor disclaiming the contract. There is some authority that a repudiation made while a minor will not be binding and may be revoked on the minor attaining majority.[26]

The category of contracts that are binding on a minor unless repudiated primarily covers contracts under which the minor acquires an interest in a subject matter of a permanent nature to which continuous obligations are attached. Thus, the category includes contracts under which the minor acquires a leasehold interest in land,[27] contracts under which the minor purchases shares from a company which are not fully paid up[28] and contracts of partnership.[29] It is uncertain whether contracts for the sale or purchase of property by a minor are also binding unless repudiated or require ratification.[30] However, in the case of Torrens system land, once the transfer is registered, a minor cannot repudiate in instances where the purchaser was not aware that the vendor was a minor.[31]

Consequences of a minor repudiating

[8.30] If a minor repudiates a contract in this category, he or she will not be liable for obligations arising in the future. While the position with respect to obligations which have already accrued is not entirely clear,[32] there is authority that the minor will be bound by such obligations.[33] For example, if a minor repudiates a lease, he or she will be liable for rent accruing up to the time of repudiation, but not after that time.[34]

Money paid by the minor under a repudiated contract will be recoverable only if there has been a total failure of consideration, in the sense that the minor received none of the bargained-for benefit under the contract.[35] In *Steinberg v Scala (Leeds) Ltd*,[36] the minor applied for shares in the defendant company and paid for the amount due on allotment. The shares were allotted to her. The minor did not receive any dividends from the shares. Eighteen months after allotment she repudiated the contract and asked for repayment of the money paid by her to the company. The Court of Appeal held that the minor was unable to recover. The minor had received the shares, which was the consideration for which her money had been paid. Therefore, there was no total failure of consideration.[37]

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26 See, eg, *North Western Railway Co v M'Michael* (1850) 5 Ex 114; 155 ER 49, 127 (Ex), 55 (ER); *Sellin v Scott* (1901) 1 SR (NSW) Eq 64, 67.

27 *Davies v Beynon-Harris* (1931) 47 TLR 424.

28 *North Western Railway Co v M'Michael* (1850) 5 Ex 114; 155 ER 49.

29 *Lowell & Christmas v Beauchamp* [1894] AC 607, 611.

30 See further Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [17.18].

31 *Percy v Youngman* (1941) VLR 275.

32 See Carter, *Contract Law in Australia* (7th ed, 2018), [15-20].

33 *Norman Baker Pty Ltd (in liq) v Baker* (1978) 3 ACLR 856, 859–60.

34 *Davies v Benyon-Harris* (1931) 47 TLR 424.

35 On total failure of consideration, see also [10.25].

36 *Steinberg v Scala (Leeds) Ltd* [1923] 2 Ch 452.

37 *Rain v Fullerton* (1900) 21 LR (NSW) Eq 311; *Thurston v Nottingham Permanent Building Society* [1902] 1 Ch 1, affirmed [1903] AC 6; *Re Willmott* (1948) St R Qd 256.

A minor will be entitled to recover any land he or she has transferred on repudiating a contract.[38] Where goods have been transferred by a minor, they may only be recovered if the minor has not received any of the promised consideration for the transaction.[39]

In South Australia, these rules are varied by s 7 of the *Minors' Contracts (Miscellaneous Provisions) Act 1979* (SA), which provides that where property has passed to another person under a contract subsequently voided on grounds of minority, the court may order restitution of the property on such terms and conditions as the courts considers just. Such an order may be made even if the minor has received some benefit under the contract or if any other party has partly performed his or her obligations under the contract.

A guarantor of a contract with a minor will not be liable if the minor repudiates the principal contract.[40] This position has been changed by legislation in New South Wales,[41] South Australia,[42] and Tasmania.[43]

CONTRACTS REQUIRING RATIFICATION

[8.35] The third category of contracts made by minors is contracts that are not binding on the minor unless ratified. Subject to statute, this class contains all contracts not in one of the other classes already discussed. This means that no action can be taken to enforce the contract against a minor unless and until the contract is ratified by the minor. At common law, no formal act of ratification is required; ratification may be inferred from the minor continuing to perform the contract on reaching the age of majority.[44] Statute has modified the common law in some jurisdictions by removing the right to ratify some contracts and/or by requiring ratification to be in writing.

Northern Territory and Western Australia

[8.40] In Western Australia and the Northern Territory, the *Statute of Frauds (Amendment) Act 1828* (UK) (*Lord Tenterden's Act*) applies in its original form as imperial legislation. Section 6 of *Lord Tenterden's Act* provides:

> No action shall be maintained whereby to charge any person upon any promise made after full age to pay any debt contracted during infancy, or upon any ratification after full age of any promise or simple contract made during infancy, unless such promise or ratification shall be made by some writing signed by the person to be charged therewith.

Thus, ratification in these jurisdictions must be in writing and signed by the minor against whom the contract is to be enforced. The better view is that the legislation does not apply to contracts binding on the minor in the absence of ratification.[45]

38 See, eg, *Rain v Fullarton* (1900) 21 LR (NSW) Eq 311.

39 See, eg, *Pearce v Brain* [1929] 2 KB 310.

40 *Land & Homes (WA) Ltd v Roe* (1936) 39 WALR 27. See also Carter, *Contract Law in Australia* (7th ed, 2018), [15-25]; Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [17.36].

41 *Minors (Property and Contracts) Act 1970* (NSW), s 47.

42 *Minors Contracts (Miscellaneous Provisions) Act 1979* (SA), s 5.

43 *Minors Contracts Act 1988* (Tas), s 4.

44 *Williams v Moor* (1843) 11 M&W 256; 152 ER 798.

45 Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [17.26].

Lord Tenterden's Act distinguishes between a new promise made by a minor on reaching majority and ratification of a contract made by a minor. The former type of promise does not require ratification unless it relates to a debt contracted by the promisor while still a minor.

Australian Capital Territory

[8.45] In the Australian Capital Territory, s 15 of the *Mercantile Law Act 1962* (ACT) is based on *Lord Tenterden's Act*. Section 15 requires ratification to be in writing and signed by the minor against whom the contract is to be enforced. Section 15 also provides that any promise "made after full age to pay any debt contracted during infancy" must be in writing and signed by the minor.

Queensland

[8.50] The common law rules with respect to the ratification of minors' contracts apply in Queensland.

Tasmania

[8.55] The common law rules apply in Tasmania, except in relation to guarantees.[46]

South Australia

[8.60] In South Australia, s 4 of the *Minors Contracts (Miscellaneous Provisions) Act 1979* (SA) provides that ratification of an otherwise unenforceable minor's contract must be in writing.[47]

Victoria

[8.65] In Victoria, s 50 of the *Supreme Court Act 1986* (Vic) provides that no proceeding can be brought to enforce a promise made after attaining majority to pay a debt contracted during minority or on a ratification made on attaining majority of a promise or contract made during minority. Like *Lord Tenterden's Act*, this legislation distinguishes between ratification of a contract made by a minor and a new promise, supported by fresh consideration, made by a minor on reaching majority. A new promise supported by consideration and in the same form as a promise made during minority will be enforceable except in relation to a debt. By contrast, a ratification of a promise made during minority will not be enforceable.[48] As discussed below, in Victoria, legislation makes a number of types of contracts with minors void.

Consequences of non-ratification

[8.70] Contracts with minors which require ratification are not binding on the minor until and unless ratified. Accordingly, a minor will not be bound by any obligations under the

46 See [8.30].

47 It is uncertain whether the provision supplements or impliedly repeals the relevant provisions of *Statute of Frauds (Amendment) Act 1828* (UK): Carter, *Contract Law in Australia* (7th ed, 2018), [15-18]; Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [17.25] n 101.

48 *Ditcham v Worrell* (1880) 5 CPD 410; [1874-80] All ER 1324; *Watson v Campbell (No 2)* [1920] VLR 347; *Vickery's Motors Pty Ltd v Tarrant* [1924] VLR 195.

contract unless and until it is ratified. The minor may, however, sue the other party to the contract for damages for breach. The minor will not be able to obtain an order for specific performance on the ground of lack of mutuality; that is, such an order would not be given to the other party to enforce the contract against the minor.[49] The principles concerning the recovery of property and money are the same as those discussed above in relation to the category of contracts binding unless repudiated.

VOID CONTRACTS

Victoria

[8.75] Section 49 of the *Supreme Court Act 1986* (Vic) makes void contracts with minors for the repayment of money lent or to be lent and contracts for the payment of goods supplied or to be supplied other than necessities and accounts stated (ie, an admission by the minor that a sum certain is due from the minor to another person). A loan of money cannot be ratified after the minor attains majority.

Section 51 of the *Supreme Court Act 1986* (Vic) provides that if a minor has contracted a loan and agrees after attaining majority to repay it, "that agreement and any instrument relating to it" is void. It is also provided that a bona fide holder for value of a negotiable instrument can recover from the minor. If this occurs, the minor may recover the sum from the person to whom the minor gave the instrument.

Consequences of a contract being void

[8.80] A *void* contract will usually have no legal effect. However, contracts with minors declared void by legislation are not treated in this way. The common view is that contracts declared void by legislation should be treated in the same way as contracts not binding unless ratified.[50] Thus, for example, the contract may be enforced by the minor. Property in goods may pass to a minor.[51] Where a loan to a minor is rendered void, the guarantee will also not be enforceable.[52] This rule has been changed in some jurisdictions.[53]

TORT LIABILITY

[8.85] Minors may be liable in tort. However, a minor will not be liable for a tort where that would amount to indirect enforcement of a contract.[54] For example, a minor who fraudulently

49 *Flight v Bolland* (1828) 4 Russ 298; 38 ER 817; [1824-34] All ER Rep 372; *Boyd v Ryan* (1947) 48 SR (NSW) 163. On specific performance generally, see further below, Chapter 30.

50 Carter, *Contract Law in Australia* (7th ed, 2018), [15-18]; Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [17.34]. See also *Woolf v Associated Finance Pty Ltd* [1956] VLR 51.

51 *Hall v Wells* [1962] Tas SR 122.

52 *Coutts & Co v Browne Lecky* [1947] KB 104.

53 See in particular *Minors (Property and Contracts) Act 1970* (NSW), s 47; *Minors Contracts (Miscellaneous Provisions) Act 1979* (SA), s 5; *Minors Contracts Act 1988* (Tas), s 4. See also the discussion of credit legislation in Carter, *Contract Law in Australia* (7th ed, 2018), [15-25]; Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [17.36].

54 The rule is different in New South Wales: see [8.110].

misrepresents his or her age in entering into a contract will not be liable in deceit.[55] Equity may require a minor to disgorge property obtained by fraud, provided that property is still in the possession of the minor.[56]

NEW SOUTH WALES

[8.90] In New South Wales, the *Minors (Property and Contracts) Act 1970* (NSW) provides a comprehensive code dealing with the law relating to minors. A contract that is not within the statutory provisions is not binding on the minor.[57]

Presumptively binding contracts

[8.95] Section 6(1) defines a "civil act" to include a contract and a number of specified acts connected with a contract. Section 19 makes presumptively binding on the minor a civil act that is for the benefit of the minor at the time of his or her participation.[58] Under s 6(3), a presumptively binding civil act is binding on the minor as if the minor "were not under the disability of infancy" at the time of his or her participation in the act. The civil act may be challenged on the basis of any of the established factors vitiating contractual consent, such as mistake or misrepresentation. Section 18 also allows the actual capacity of the minor to be taken into account in determining whether a civil act is binding, providing:

> [t]his Part does not make presumptively binding on a minor a civil act in which the minor participates, or appears to participate, while lacking, by reason of youth, the understanding necessary for his or her participation in the civil act.

Grant of capacity

[8.100] Under s 26, the Supreme Court may grant the minor capacity to participate in any civil act where such an order will be for the benefit of the minor. A civil act authorised by a grant of capacity will be presumptively binding on the minor.

Under s 27, a local court may by order, on application by a minor, approve a contract proposed to be made by a minor or a disposition of property proposed to be made by or to a minor. The order must be for the benefit of the minor. Such a contract is then presumptively binding on the minor.

Affirmation and repudiation

[8.105] Under s 30, a civil act may be affirmed by a minor after he or she attains the age of 18 years or by a court where the affirmation is for the benefit of the minor. The affirmed civil act will then be presumptively binding on the minor. Under s 39, a minor may not enforce against any other party a civil act that is not presumptively binding on the minor. Under s 30(5), an affirmation of a civil act by a minor may be by words, written or spoken, or by

55 *R Leslie Ltd v Sheill* [1914] 3 KB 607.

56 See further Carter, *Contract Law in Australia* (7th ed, 2018), [15-22]; Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [17.42].

57 *Minors (Property and Contracts) Act 1970* (NSW), s 17.

58 See also specific transactions stated to be presumptively binding in ss 22, 23 and 24 and s 20, dealing with dispositions of property. *Minors (Property and Contracts) Act 1970* (NSW).

conduct, and need not be communicated to any person. A court may affirm a contract to a minor's benefit where it appears to the court that the affirmation is for the benefit of the minor.

Under s 31, a minor may repudiate a civil act at any time during his or her minority or afterwards but before the minor attains the age of 19 years. A repudiation of a civil act will not have effect if "it appears that, at the time of the repudiation, the civil act is for the benefit of the minor". Section 33 provides that a repudiation of a civil act will only have effect if notice is served on the relevant person and is in writing and signed by the person making the repudiation or by the person's agent. Under s 38, a contract that is not otherwise conclusively binding will become so if not repudiated by the time the minor attains the age of 19 years. Under s 34, a court may also repudiate a civil act on behalf of a minor at any time during his or her minority, but not if it appears to the court that the civil act is for the benefit of the minor.

Under s 37, where a civil act is repudiated, a court may, on the application of any person interested in the civil act, make orders adjusting the rights arising out of the civil act. However, where on such an application:

> it appears to the court that any party to the civil act was induced to participate in the civil act by a misrepresentation made by a minor participant in the civil act, being a fraudulent misrepresentation as to the age of the minor participant or as to any other matter affecting the capacity of the minor participant to participate in the civil act, the court may confirm the civil act and anything done under the civil act.

Liability for tort

[8.110] Under s 48, where a person under the age of 21 years is guilty of a tort, the person is answerable for the tort whether or not "(a) the tort is connected with a contract, or (b) the cause of action for the tort is in substance a cause of action in contract".

MENTAL INCAPACITY AND INTOXICATION

Mental incapacity

[8.115] A contract made with a person with a mental impairment, which prevents that person from making an informed decision about whether to enter into that contract, may be voidable at the option of that person. Examples of such impairments include intellectual disability, dementia, acquired brain injury or a mental illness. While mental incapacity is a ground for setting aside a contract, it should not be used as a reason for assuming all people with cognitive disabilities or mental impairments lack legal, decision-making capacity in all circumstances. The *Convention on the Rights of Persons with Disabilities* is premised on the autonomy and decision-making agency of people with disabilities, which requires support for decision-making rather than presumptive denials of capacity.[59]

A person seeking to set aside a contract on grounds of mental impairment must show two things, relating to his or her own understanding and the knowledge of the other party.

59 Australian Law Reform Commission, Equality, Capacity and Disability in Commonwealth Laws, Report No 124 (2014) Ch 2. See also Maker, Arstein-Kerslake, McSherry, Paterson, Brophy, "Ensuring Equality for Persons with Cognitive Disabilities in Consumer Contracting: An International Human Rights Law Perspective" (2018) 19 *Melbourne Journal of International Law* 178.

First, to set a contract aside on grounds of a lack of mental capacity, the person alleging incapacity, or his or her representative, must show that he or she was incapable of understanding the contract in question at the time it was made, having regard to the circumstances. Mental capacity for this purpose is usually defined by reference to the statement of Dixon CJ, Kitto and Taylor JJ in *Gibbons v Wright*, referring to "such soundness of mind as to be capable of understanding the general nature of what he is doing by his participation".[60] Mental capacity for this purpose is assessed:

> relative to the particular transaction which is being effected by means of the instrument, and may be described as the capacity to understand the nature of that transaction when it is explained.[61]

Secondly, to set a contract aside on grounds of a lack of mental capacity, the person seeking to have the contract set aside must prove that the other party to the contract knew,[62] or potentially ought to have known, of the impairment. In England, there is support for the view that constructive knowledge is sufficient.[63] In Australia, the question is unsettled,[64] with support for the position that actual knowledge is needed,[65] and also some case law supporting constructive knowledge being sufficient.[66] A contract made with a person lacking mental capacity may also, in some cases, be challenged on grounds of non est factum[67] and unconscionable dealing.[68]

In *Lampropoulos v Kolnik*,[69] the parties entered into a "Memorandum of Understanding" that gave the plaintiff, an estate agent, an option to purchase a house from an elderly man, who was suffering from some form of impaired cognitive capacity, potentially dementia. The Court set the contract aside on grounds that the elderly man lacked mental capacity and that the plaintiff knew of the man's reduced mental capacity.[70] This knowledge could be inferred from a number of factors, primarily the age of the man, the fact that the man was prepared to enter into an agreement to sell his house at a significant undervalue, and from the general disorder of his home.[71] The transaction was also able to be avoided on grounds of unconscionable conduct.

A person lacking mental capacity will be obliged to pay for necessaries supplied to him or her, or his or her spouse. Under Sale of Goods legislation, a person lacking mental capacity to contract will only be required to pay a reasonable, as opposed to the contractual, price for

60 *Gibbons v Wright* (1954) 91 CLR 423, 437.

61 *Gibbons v Wright* (1954) 91 CLR 423, 438.

62 *Molton v Camroux* (1848) 2 Exch 487; 154 ER 584, affirmed (1849) 4 Ex 17; 154 ER 1107; *Gibbons v Wright* (1954) 91 CLR 423, 441.

63 *Dunhill v Burgin* [2014] UKSC 18, [25]. See also Varney, "Redefining Contractual Capacity? The UN Convention on the Rights of Persons with Disabilities and the Incapacity Defence in English Contract Law" (2017) 37 *Legal Studies* 493.

64 *Hanna v Raoul* [2018] NSWCA 201, [51].

65 *Public Trustee (WA) v Brumar Nominees Pty Ltd* [2012] WASC 161; *Macura v Sarasevic* [2019] NSWSC 1409, [226]. Also Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [17.53].

66 *Lampropoulos v Kolnik* [2010] WASC 193, [350].

67 See Chapter 31. See also *Ford v Perpetual Trustees Victoria Ltd* [2009] NSWCA 186; (2009) 75 NSWLR 42.

68 See Part XIB: Abuse of Power.

69 *Lampropoulos v Kolnik* [2010] WASC 193.

70 *Lampropoulos v Kolnik* [2010] WASC 193, [362].

71 *Lampropoulos v Kolnik* [2010] WASC 193, [363]–[387].

necessaries.[72] Legislation in each jurisdiction also provides for courts and certain officials to manage the affairs of a person who lacks the mental capacity for this task.[73]

In *Aster Healthcare v Shafi*,[74] a local authority with responsibility for aged care placed an elderly man with dementia in a private care home. The authority then, on finding the elderly man had resources, directed the care home to seek payment from him. After the man died, the care home sought payment from his estate, relying on a statutory form of the obligation of those lacking capacity to pay a reasonable sum for necessaries. The English Court of Appeal upheld the decision of the first instance judge rejecting this claim.[75] The principle did not allow a supplier to "recover payment for the supply of necessaries to a person under a mental incapacity in circumstances in which he never intended that person to make that payment".[76]

Intoxication

[8.120] The capacity of an intoxicated person to make a contract is the same as that of a person who lacks mental capacity.[77]

72 *Goods Act 1958* (Vic), s 7. Similarly: *Sale of Goods Act 1954* (ACT), s 7(2); *Sale of Goods Act 1923* (NSW), s 7; *Sale of Goods Act* (NT), s 7(2); *Sale of Goods Act 1896* (Qld), s 5(2); *Sale of Goods Act 1895* (SA), s 2(1); *Sale of Goods Act 1896* (Tas), s 7(1); *Sale of Goods Act 1895* (WA), s 2(1).

73 See further Carter, *Contract Law in Australia* (7th ed, 2018), [15-44].

74 *Aster Healthcare v Shafi* [2014] EWCA Civ 1350.

75 *Aster Healthcare v Shafi* [2014] EWCA Civ 1350, [34].

76 *Aster Healthcare v Shafi* [2014] EWCA Civ 1350, [19].

77 See further Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [17.56].

DETRIMENTAL RELIANCE AND UNJUST ENRICHMENT

PART III

[PtIII.05] This part of the book deals with two important non-contractual obligations that arise in contractual contexts: first, the obligation to avoid causing harm to others through inconsistent conduct (estoppel) and, secondly, the obligation to restore unjust gains made at the expense of others (restitution).

The principles of estoppel operate in a range of situations to supplement the law of contract by preventing harm arising from detrimental reliance by one party on inconsistent conduct of another. The law of estoppel prevents or compensates certain harm which is not compensable under ordinary contract principles (such as the expenditure of money in reliance on a non-contractual promise). The law of restitution also supplements the law of contract in a range of situations by facilitating the recovery of certain unjust enrichments (such as money paid under a mistake or services performed under an unenforceable contract) which are not recoverable under ordinary contractual principles.

CHAPTER **9**

Estoppel

[9.05] We noted in Chapter 4 that detrimental reliance on a promise does not constitute consideration and therefore does not provide a basis for enforcing the promise within the law of contract. Assume, for example, that A promises to give certain land to B. B gives nothing in return for that promise but relies on the promise by building on the land. A then refuses to transfer the land to B. If the promise is not enforced, B will suffer detriment as a result of having built on the land in reliance on A's promise. There is no contract between A and B because B has given no consideration for A's promise. The building of the house does not

satisfy the "bargain" requirement because it is not given *in return for* the land. The law of contract fails to protect B against harm suffered as a result of reliance on A's promise. B must therefore look to the principles of estoppel for protection against the detriment that B would suffer if A fails to transfer the land.

The principles of estoppel operate where non-contractual promises and representations have been relied upon. Where B relies to her detriment on an assumption induced by A's conduct, the principles of estoppel may prevent A from acting inconsistently with that assumption, at least without taking steps to ensure that B does not suffer harm as a result of her reliance on the assumption. The law of misrepresentation and misleading or deceptive conduct, discussed in Chapters 32 and 33, is also concerned with loss resulting from reliance on representations, but protects against loss resulting from *the representation being untrue*, rather than from *inconsistent conduct* on the part of the person making the representation.

As we will see in this chapter, the principles of estoppel play a very important role in the contractual context. In some situations, the principles of estoppel provide, or help to provide, a basis for relief where none is provided by the law of contract. In other situations, the principles of estoppel prevent one party from enforcing contractual rights against another.

THE NATURE OF ESTOPPEL BY CONDUCT

[9.10] The principles of estoppel by conduct are concerned with inconsistent conduct by one party that causes or threatens to cause harm to another as a result of the second party's reliance on that conduct. An estoppel may arise where one person (the inducing party) induces another person (the relying party) to adopt and act upon an assumption of fact (estoppel by representation) or an assumption as to the future conduct of the inducing party (equitable estoppel). If the inducing party and the relying party have negotiated the terms of a contract, for example, an estoppel by representation may arise if the inducing party induces the relying party to believe that the inducing party *has* signed the contract. This is an assumption of existing fact. An equitable estoppel may arise if the inducing party induces the relying party to believe that the inducing party *will* sign the contract. This is an assumption relating to the future conduct of the inducing party.

An estoppel will only arise where the relying party has acted on the assumption in such a way that he or she will suffer detriment if the inducing party acts inconsistently with the assumption. In the above example, the relying party might act to his or her detriment by incurring expenditure in preparation for performance of the contract in the belief that the inducing party has signed or will sign the contract. That expenditure will be wasted if the inducing party disappoints the assumption by denying that the contract has been signed or by refusing to sign the contract.

The effect of an estoppel by representation is to prevent the inducing party from denying the truth of the assumption in litigation between the parties. The rights of the parties are then determined by reference to the assumed state of affairs, rather than the true state of affairs. In the above example, the rights of the parties will be determined on the basis that the contract has been signed. Although the contract has not been signed, the relying party can enforce the contract as though it had been signed. The effect of an equitable estoppel is to prevent the inducing party from acting inconsistently with the assumption without taking steps to ensure that the departure does not cause harm to the relying party. Those steps might include compensating the relying party for any financial loss resulting from reliance on the assumption or giving the relying party reasonable notice of the inducing party's intention to

depart from the assumption, so that the relying party can resume his or her original position. If the inducing party acts inconsistently with the assumption without taking any such steps, then the court must fashion relief by which to give effect to the estoppel.

The word "estoppel" comes from the old French word "estoupail", meaning a bung or stopper.[1] Estoppel by representation is an older form of estoppel, and its operation is consistent with the origin of the word. The estoppel stops up the mouth of the inducing party, preventing him or her from pleading the truth. The stopper metaphor is not apt to describe the operation of equitable estoppel, however, because the effect of the estoppel is not to "stop up" the inducing party's mouth, but either to prevent the inducing party from enforcing its legal rights or to create new rights against the inducing party which the court must satisfy by granting an appropriate remedy. From the point of view of contract law, equitable estoppel is far more important than estoppel by representation because it operates alongside contract as a source of rights that can arise from promises, such as a promise to convey land or a promise not to enforce existing contractual rights.

ESTOPPEL BY REPRESENTATION AND EQUITABLE ESTOPPEL

[9.15] Judges and scholars use a bewildering range of expressions to describe different types of estoppel. Unfortunately, the names are not used consistently. The most important distinction is between *estoppel by representation* and *equitable estoppel*. Before we consider the differences between estoppel by representation and equitable estoppel, it is important to note some common features. First, both estoppels by representation and equitable estoppels are founded on assumptions induced by the conduct of another person. They can therefore collectively be referred to as *estoppel by conduct*. Secondly, both are essentially concerned to prevent detriment resulting from action taken on the faith of the assumption if the assumption is not adhered to. Detrimental reliance is an essential element of each. Thirdly, both estoppel by representation and equitable estoppel operate only where it is unjust or unconscionable to depart from the assumption.

Estoppel by representation

[9.20] The expression "estoppel by representation" is usually used to describe the following principle, which is also sometimes called *common law estoppel*.[2] Where one person (the inducing party) leads another (the relying party) to adopt an assumption of fact, and the relying party acts on that assumption in such a way that the relying party will suffer detriment if the inducing party subsequently denies that it is true, the inducing party is "estopped" from denying the truth of the representation.

Assume, for example, that a builder has negotiated the terms of a building contract with a customer, with the parties intending to be bound only when a written contract has been signed. The builder prepares a written contract, signs it and sends it to the customer. The customer telephones the builder and tells the builder that the customer has signed the contract. On the faith of that assurance, the builder purchases materials for the job and rejects other offers of work during the relevant period. The customer has induced the builder to adopt an

1 "estoppel, n." *Oxford English Dictionary Online*, Oxford University Press, http://www.oed.com (accessed 13 August 2019).

2 See, eg, *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 397–8, 458–9.

assumption of fact (that the customer has signed the contract). That assumption has been relied upon by the builder (by purchasing materials and refusing other work) such that the builder will suffer detriment if the purchaser now denies having signed the contract. The customer is therefore "estopped" from denying that she has signed the contract. The effect of the estoppel is that the rights of the parties are determined on the basis of the *assumed* state of affairs. The estoppel prevents the customer from denying that she has signed the written contract and thus provides a foundation for the builder to sue in contract.

Estoppel by representation is relatively rare because it can only operate where a person seeks to assert rights that are inconsistent with the fact represented. It is far less common for a person to behave inconsistently with an assumed fact than it is for a person to behave inconsistently with an assumption about his or her future conduct.

Equitable estoppel

[9.25] *Equitable estoppel* encompasses promissory estoppel and proprietary estoppel.[3] *Proprietary estoppel* operates where the relying party acts to his or her detriment on the faith of an assumption that the relying party has or will be granted an interest in land.[4] *Promissory estoppel* is now commonly used to describe any application of equitable estoppel that does not relate to an interest in land. Prior to the decision of the High Court in *Waltons Stores (Interstate) Ltd v Maher* (*Waltons Stores v Maher*),[5] the expression "promissory estoppel" was used to describe a narrower principle that operated only in relation to a promise not to enforce contractual or other legal rights.[6] Since the High Court has accepted that promissory estoppel and proprietary estoppel are manifestations of a single principle,[7] the expression "equitable estoppel" is commonly used to describe that principle and the expressions "promissory" and "proprietary" estoppel have, until recently, been used less frequently.

The nature and scope of promissory and proprietary estoppel have long been controversial questions. Unfortunately, the controversy in relation to promissory estoppel has become particularly acute in Australian law in recent years. Most significantly, the New South Wales Court of Appeal has in a series of decisions insisted that promissory and proprietary estoppel remain entirely separate doctrines, and that promissory estoppel can only act as a restraint on rights. That view is difficult to reconcile with the decision of the High Court in *Waltons Stores v Maher* and is inconsistent with what has been understood by most Australian courts to be the law since that landmark decision. It is also inconsistent with the outcomes of numerous other cases decided in the last thirty years.[8]

The divergence of views as to the state of equitable estoppel in Australian law is illustrated by the judgments in the High Court in *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd*.[9] Although the justices of the High Court were agreed that no doctrine of estoppel was

3 Parkinson, "Estoppel", in Parkinson (ed), *The Principles of Equity* (2nd ed, 2003), [711].

4 Proprietary estoppel encompasses estoppel by encouragement (which operates where the owner of land encourages the relying party to build on the land) and estoppel by acquiescence (which operates where the owner of land knowingly allows the relying party to build on the land).

5 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387.

6 See [9.35].

7 See *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387; *Commonwealth v Verwayen* (1990) 170 CLR 394; *Giumelli v Giumelli* [1999] HCA 10; (1999) 196 CLR 101, discussed later in this chapter.

8 See further below [9.150]–[9.165] and Robertson, "Three Models of Promissory Estoppel" (2013) 7 *Journal of Equity* 226.

9 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* [2016] HCA 26; (2016) 260 CLR 1.

applicable on the facts, Keane J and Nettle J expressed different understandings of the state of equitable estoppel. Keane J expressed the view that promissory and proprietary estoppel were "separate categories", which "serve a common purpose" (namely, protecting against detriment flowing from a change of position if the assumption that led to it is deserted), but allow for different approaches to the level of certainty required in the founding assumption.[10] Nettle J, on the other hand, took the view that proprietary estoppel arising from a promise of land was a form of promissory estoppel, and, since a single foundational principle underlay all forms of equitable estoppel there could, as a matter of principle, be no difference between them as to the level of certainty required.[11]

It is important to bear in mind that the nature and scope of promissory estoppel and the existence of a unified doctrine of equitable estoppel are unsettled questions, and that support for strikingly divergent views can be found in the case law. Particular attention should be paid to [9.150]–[9.165], where the different views as to the current state of the law are explained.

A BRIEF HISTORY OF ESTOPPEL BY CONDUCT

Fact and future conduct

[9.30] It is difficult to understand the current principles of estoppel without knowing something of the history of estoppel by conduct. The forerunner of all estoppels by conduct is the principle of estoppel by representation of fact. Although the principle of estoppel by representation of fact originated in the Court of Chancery,[12] it came to be applied in the common law courts[13] and is sometimes referred to as common law estoppel. Estoppels by representation of fact occasionally arise in the contractual context, such as in the situation mentioned at [9.20], where an inducing party leads a relying party to believe that she has signed a contract, when in fact she has not. Of far greater importance to contract law are estoppels arising from promises to do something in the future. A relying party might, for example, be induced to act on an assumption that the inducing party:

- will enter into a contract with the relying party at some time in the future;
- will transfer land, pay money, or provide another benefit to the relying party; or
- will not enforce certain contractual rights against the relying party (eg, a landlord's promise to accept a reduced rent from a tenant).

Up until the middle of the 19th century, the Court of Chancery would order a representor to "make good" a representation as to future conduct that was intended to, and did in fact, induce reliance.[14] The principle that was applied was analogous to estoppel by representation of fact: where a representor made a promise which was relied upon, then the representor was required to "make good" the promise if a failure to fulfil it would cause harm to the

10 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* [2016] HCA 26; (2016) 260 CLR 1, [139]–[141].

11 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* [2016] HCA 26; (2016) 260 CLR 1, [215]–[217].

12 *Franklin v Manufacturers Mutual Insurance Ltd* (1935) 36 SR (NSW) 76, 80; see also *Legione v Hateley* (1983) 152 CLR 406, 430.

13 See, eg, *Jorden v Money* (1854) 5 HLC 185; 10 ER 868, 881.

14 See, eg, *Hobbs v Norton* (1682) 1 Vern 136; 23 ER 370; *Wankford v Fotherley* (1694) 2 Freem 201; 22 ER 1159 and the discussion in Robertson, "Revolutions and Counterrevolutions in Equitable Estoppel" in Worthington, Robertson and Virgo (eds), *Revolution and Evolution in Private Law* (2018) 161.

relying party as a result of his or her reliance. A series of decisions in the second half of the 19th century brought this line of cases to an end.[15] These decisions were influenced by classical contract theory and a concern to ensure the sanctity of bargains and to promote ideals of self-reliance.[16] The most significant decision was *Jorden v Money*,[17] in which a majority of the House of Lords held that a promise or representation as to future conduct could only be binding by way of contract. Estoppel at common law and in equity was limited to representations of existing fact.

The rule in *Jorden v Money* was applied strictly by the common law courts and continues to limit the scope of estoppel at common law to representations or assumptions of fact.[18] In equity, however, two exceptions to the rule in *Jorden v Money* developed. The first was a set of principles which have more recently come to be known as proprietary estoppel, which operated where an owner of land led a relying party to assume that the relying party had or would be granted an interest in that land.[19] If the relying party acted to his or her detriment on the faith of that assumption, then the inducing party would be required to make good the assumption or compensate the relying party. The second was the principle of promissory estoppel, which operated where one party to a contract led a second party to believe that certain contractual rights would not be enforced. Where the second party had changed his or her position on the faith of that assumption, the first would not be allowed to enforce those rights.[20]

From *High Trees* to *Waltons Stores*

[9.35] In *Central London Property Trust Ltd v High Trees House Ltd* (*High Trees*),[21] Denning J creatively interpreted a series of earlier cases to establish a broad principle of law. This principle later became known as promissory estoppel. It operated where a person made a promise which was intended to affect the legal relations between the parties, was intended to be acted upon and was in fact acted upon. The principle did not provide a cause of action for damages for breach of the promise but operated to prevent the inducing party from acting inconsistently with the promise. If a landlord promised to accept a reduced rent from a tenant and the tenant acted on that promise, promissory estoppel would prevent the landlord from claiming the amount of rent foregone. After the *High Trees* case, it was thought that a promissory estoppel could arise only where the parties were in a pre-existing legal relationship and could operate only as a defence, preventing the enforcement of rights which the inducing party had promised not to enforce. The English courts were reluctant to allow promissory estoppel to be used for the positive enforcement of a promise, fearing that the enforcement

15 See further Robertson, "Situating Equitable Estoppel within the Law of Obligations" (1997) 19 *Sydney Law Review* 32, 33–7.

16 See [1.10] and Metzger and Phillips, "The Emergence of Promissory Estoppel as an Independent Theory of Recovery" (1983) 35 *Rutgers Law Review* 472.

17 *Jorden v Money* (1854) 5 HLC 185; 10 ER 868.

18 Although estoppel by convention (discussed at [9.200]) can arise from an assumption concerning the legal rights of the parties, this is regarded by some as a common law doctrine.

19 See McFarlane, *The Law of Proprietary Estoppel* (2014).

20 *Hughes v Metropolitan Railway Co* (1877) 2 App Cas 439; *Birmingham and District Land Co v London and North Western Railway Co* (1888) 40 Ch D 268.

21 *Central London Property Trust Ltd v High Trees House Ltd* [1947] 1 KB 130.

of relied-upon promises would undermine the doctrine of consideration and thus the law of contract.

Both the principles of proprietary estoppel[22] and promissory estoppel[23] came to be applied in the Australian courts. In *Waltons Stores v Maher*,[24] the High Court recognised a unity of principle between promissory and proprietary estoppel and recognised that they are manifestations of a broader principle of equitable estoppel.[25] It was said that the common thread that links promissory and proprietary estoppel together is the principle that equity will come to the relief of a plaintiff who has acted to his or her detriment on the basis of an assumption induced by the defendant's conduct.[26]

Waltons Stores negotiated to lease land from Mr and Mrs Maher on terms that required the Mahers to demolish a building on their land and construct a new building to Waltons' specifications. Time was short and the terms of the lease needed to be finalised quickly so that the Mahers could complete the construction work by the date stipulated by Waltons. The Mahers were concerned to ensure that there were no problems with the lease before they demolished a new brick part of the old building. When negotiations were essentially complete, Waltons' solicitors sent to the Mahers' solicitors a copy of the lease which incorporated some final amendments requested by the Mahers. Waltons' solicitors told the Mahers' solicitors that they would let them know the next day if Waltons disagreed with any of the amendments. The Mahers heard no more from Waltons' solicitors on this issue. The lease was signed by the Mahers and returned to Waltons on 11 November "by way of exchange". Waltons then instructed its solicitors to "go slow" on the transaction, pending a review of its retailing strategy. Waltons became aware in December that the Mahers had begun to demolish the existing building, but still delayed signing. On 19 January, when the construction of the new building was 40 per cent complete, Waltons' solicitors informed the Mahers' solicitors that Waltons did not intend to proceed with the lease.

No contract existed between the parties because Waltons had not executed the lease. Deane and Gaudron JJ found that the Mahers had acted on the assumption that exchange *had* taken place and a binding agreement for lease had been made.[27] This was an assumption of existing fact which, when relied upon, established an estoppel by representation (also referred to as a common law estoppel or an estoppel in pais). The effect of that estoppel was to prevent Waltons from denying that they had signed the lease. The rights of the parties were therefore determined on the basis that Waltons had signed the lease.[28] Mason CJ, Wilson and Brennan JJ preferred the conclusion that the Mahers had acted on the assumption that Waltons *would* complete the transaction.[29] This was an assumption as to Waltons' future conduct, which could only give rise to a promissory or equitable estoppel.

22 See, eg, *Hamilton v Geraghty* (1901) 1 SR (NSW) (Eq) 81; *Raffaele v Raffaele* [1962] WAR 29; *Jackson v Crosby (No 2)* (1979) 21 SASR 280; *Cameron v Murdoch* [1983] WAR 321; *Riches v Hogben* [1986] Qd R 315.

23 See, eg, *Je Maintiendrai Pty Ltd v Quaglia* (1980) 26 SASR 101.

24 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387.

25 See *Silovi Pty Ltd v Barbaro* (1988) 13 NSWLR 466, 472.

26 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 404.

27 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 442, 465.

28 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 445, 465.

29 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 398, 431.

Mason CJ and Wilson J accepted that a promissory estoppel could arise between parties involved in pre-contractual negotiations and could be used to support a cause of action in contract. Here, they said Waltons' inaction encouraged the Mahers to continue to act on the assumption that the completion of the transaction was merely a formality.[30] In view of the urgency of the transaction and Waltons' knowledge that the Mahers had commenced work on the assumption that exchange was a mere formality, Waltons was not "entitled to stand by in silence".[31] It was unconscionable for Waltons to act (or refrain from acting) as it did and Waltons was estopped from retreating from its implied promise to complete the contract.[32] Brennan J recognised that equitable estoppel could operate as an independent source of rights where one person led another to believe that a particular legal relationship existed or would exist between them.[33] If the proper inference from the facts was that the Mahers had been led to believe that a contract would come into existence, then Waltons' unconscionable conduct raised an equity in favour of the Mahers, which the Court had to satisfy by granting appropriate relief.[34] The appropriate relief was to treat Waltons as though it had signed and exchanged the lease.

The decision in *Waltons Stores v Maher* was a significant development in Australian contract law because it involved a departure from the classical idea that a promise creates a legal obligation only when consideration has been given in return for the promise and a contract has been formed. The decision greatly expanded the range of situations in which liability could result from reliance on non-contractual promises.

THE ELEMENTS OF EQUITABLE ESTOPPEL

[9.40] Universal agreement has not been reached on the elements necessary to establish an equitable estoppel. It is possible to make a list of the basic elements, but there are some important issues that remain unsettled. The lists of elements proposed by Brennan J in *Waltons Stores v Maher*[35] and Priestley JA in *Silovi Pty Ltd v Barbaro*[36] are commonly quoted and applied, but neither can be regarded as a definitive statement. The statement of Priestley JA is very broad and does not direct attention to all of the issues that have arisen in the cases. The statement of Brennan J is not broad enough to accommodate all the decisions and all the approaches adopted by other judges in the leading High Court cases. It has been authoritatively stated that they should not be applied in a mechanical fashion.[37] Nevertheless, Brennan J's statement provides a convenient and well-accepted framework and starting point for considering the relevant issues. Two additional elements – reasonableness and unconscionability – have been required in numerous other judgments and also need to be considered.

30 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 407.

31 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 407.

32 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 407–8.

33 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 428–33.

34 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 431–3.

35 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 428–9.

36 *Silovi Pty Ltd v Barbaro* (1988) 13 NSWLR 466, 472. The list was refined by Priestley JA in *Austotel Pty Ltd v Franklin Selfserve Pty Ltd* (1989) 16 NSWLR 582, 615–6.

37 *Doueihi v Construction Technologies Australia Pty Ltd* [2016] NSWCA 105; (2016) 92 NSWLR 247, [166].

Assumption

[9.45] The first of Brennan J's list of elements is that the relying party must have assumed that a particular legal relationship existed or would exist between the relying party and the inducing party, and that the inducing party would not be free to withdraw from that relationship.[38]

The need to distinguish assumptions of fact

[9.47] The first point to note about the assumption element is that the nature of the assumption will determine whether it is capable of giving rise to an estoppel by representation or an equitable estoppel. Estoppel by representation can only arise from an assumption of fact, whereas equitable estoppel can arise from an assumption relating to an existing or future legal relationship or, as we will see below, an assumption that the inducing party will act in a particular way in the future. The facts of *Waltons Stores v Maher*, considered at [9.40], illustrate this distinction. Deane and Gaudron JJ held that Waltons had led the Mahers to believe that Waltons *had* completed the exchange. This was an assumption of fact which, when relied upon, gave rise to an estoppel by representation. Mason CJ, Wilson J and Brennan J, on the other hand, found that the Mahers had been led to believe that Waltons *would* complete the exchange. Since this was an assumption as to Waltons' future conduct, it could only give rise to an equitable estoppel. As noted at [9.30], the principle that an estoppel can arise at common law only from an assumption of existing fact, and not an assumption as to the future conduct of the inducing party, is known as the rule in *Jorden v Money*.[39]

Must the assumption relate to a legal relationship?

[9.50] In *Waltons Stores v Maher*,[40] Brennan J held that it was necessary for a plaintiff to prove that he or she assumed that *a particular legal relationship* existed or would exist between the plaintiff and the defendant, and the defendant would not be free to withdraw from that relationship.[41] This suggests that an equitable estoppel cannot arise where one person assumes that another person will behave in a particular way in the future (ie, confer a benefit on the relying party) outside the context of a legal relationship.[42]

The first point to note about this limitation imposed by Brennan J is that it clearly does not apply where the inducing party leads the relying party to assume that the inducing party will transfer an interest in land to the relying party.[43] The law is clear that such an assumption can give rise to an equitable estoppel of a kind that has been called *proprietary estoppel* or *estoppel by encouragement*. This form of equitable estoppel was well established before *Waltons Stores v Maher* [44] and has been applied in High Court decisions since.[45] An equitable

38 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 428.

39 *Jorden v Money* (1854) 5 HLC 185; 10 ER 868.

40 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387.

41 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 428.

42 See *Misner v Australian Capital Territory* (2000) 146 ACTR 1, [38].

43 *Doueihi v Construction Technologies Australia Pty Ltd* [2016] NSWCA 105; (2016) 92 NSWLR 247, [153]–[170].

44 For example, *Dillwyn v Llewelyn* (1862) 4 De GF & J 517; 45 ER 1285.

45 *Giumelli v Giumelli* [1999] HCA 10; (1999) 196 CLR 101; *Sidhu v Van Dyke* [2014] HCA 19; (2014) 251 CLR 505.

estoppel has also been held to arise from a promise to transfer contractual rights which "did not consist of, or grant, any interest in land".[46]

The second point to note is that – outside the proprietary estoppel context – Brennan J's restriction has been accepted in some cases and rejected in others. It has been observed that the restriction was not supported by Mason CJ and Wilson in *Waltons Stores v Maher*,[47] although their discussion of the scope of the principle was somewhat opaque.[48] In *Austotel Pty Ltd v Franklins Selfserve Pty Ltd*,[49] Priestley JA offered a broader statement of the assumption element of equitable estoppel. He said that an equitable estoppel could operate in relation to "an assumption that *a contract will come into existence* or *a promise be performed* or *an interest granted* to the plaintiff by the defendant".[50] The first possibility (a contract will come into existence) covers the facts of *Waltons Stores v Maher*. The third (an interest granted) covers proprietary estoppel by encouragement. That leaves the fundamentally important question whether an equitable estoppel can arise in Priestley JA's second situation, that is, from an assumption that a promise will be performed. If, for example, A promises to pay B $5000 next week, B's assumption relates simply to A's future behaviour (ie, that the money will be paid) and not to any existing or expected legal relationship. Can a promise of that kind give rise to an equitable estoppel?

One line of cases has answered that question in the negative.[51] The fact that an assumption has not related to an existing or future legal relationship has in some cases been fatal to an equitable estoppel claim.[52] In other cases, such as *Mobil Oil Australia Ltd v Wellcome International Pty Ltd*,[53] the expectation of an interest in land is taken to constitute a limited exception to the rule stated by Brennan J. As discussed in Chapter 3,[54] *Mobil v Wellcome* concerned an incentive scheme operated by the Mobil Oil company for its franchisees. The franchisees were told that Mobil was looking for a way to ensure that any franchisee who met certain performance targets over a period of six years would be granted a renewal of his or her franchise without charge. On the faith of that representation, the franchisees claimed that they spent time and money improving their retail operations in order to meet the performance targets. After four years, Mobil unilaterally abandoned the incentive scheme. The franchisees argued that an equitable estoppel arose, which required Mobil to adhere to the assumption that it would grant the extended tenure. Wilcox J held at first instance that, although the franchisees incurred some additional costs in attempting to achieve their targets, the detriment suffered by them was not sufficient to justify holding Mobil to its promise. On appeal, the Full Federal Court held that the assumption adopted by the franchisees was not capable of giving rise to an equitable estoppel. The Court held that "it is a necessary element of the principle that

46 Arfaras v Vosnakis [2016] NSWCA 65, [80].

47 *Doueihi v Construction Technologies Australia Pty Ltd* [2016] NSWCA 105; (2016) 92 NSWLR 247, [56], [166].

48 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 406.

49 *Austotel Pty Ltd v Franklins Selfserve Pty Ltd* (1989) 16 NSWLR 582.

50 *Austotel Pty Ltd v Franklins Selfserve Pty Ltd* (1989) 16 NSWLR 582, 610 (emphasis added).

51 See further [9.160]. An equitable estoppel in this situation is also ruled out by the "restraint on rights" line of cases discussed at [9.155].

52 For example, *Settlement Group Pty Ltd v Purcell Partners Pty Ltd* [2013] VSCA 370.

53 *Mobil Oil Australia Ltd v Wellcome International Pty Ltd* (1998) 81 FCR 475. The decision has also been reported as *Mobil Oil Australia Ltd v Lyndel Nominees Pty Ltd* (1998) 153 ALR 198.

54 See [3.70].

the defendant has created or encouraged an assumption that 'a particular legal relationship' or 'an interest' would arise or be granted".[55] The generalised commitment given by Mobil to "find a way" to implement a "tenure for achievement" scheme was held not to be capable of giving rise to an equitable estoppel, because it could not give rise to an expectation of a particular legal relationship coming into existence or an interest being granted. The "elements and details of the legal relationship" were said to be lacking.[56]

A second line of cases provides a positive answer to the question whether an equitable can arise from an assumption relating to the future conduct of the inducing party, which does not involve a legal relationship or the grant of an interest in land.[57] In *W v G*,[58] for example, the plaintiff and the defendant in that case lived together in a lesbian relationship for more than eight years. Some years into the relationship, the plaintiff told the defendant that she wished to have children. The defendant agreed to share responsibility for the welfare of the children with the plaintiff and assisted the plaintiff in a course of artificial insemination, as a result of which the plaintiff ultimately bore two children. The plaintiff and the defendant later separated and the plaintiff sought compensation by way of equitable estoppel for the loss of the promised financial support. Hodgson J found that the defendant created or encouraged in the plaintiff an assumption that "the defendant would act with the plaintiff as parents of the two children and would assist and contribute to the raising of these children for so long as was necessary".[59] He held that the plaintiff relied on that assumption in deciding to have each of the children and that the defendant knew or intended that the plaintiff would do so. Accordingly, Hodgson J held that the plaintiff was entitled to relief on the basis of equitable estoppel.[60] The assumption made by the plaintiff did not relate to any existing or expected legal relationship between the parties, but only that the defendant would behave in a particular way in the future.

Another example is *Gray v National Crime Authority*,[61] where the promisees acted to their detriment in reliance on a promise that they would be protected from financial disadvantage if they entered a witness protection program. And in *Chanrich Properties Pty Ltd v Baulkham Hills Shire Council*,[62] an equitable estoppel arose where a developer proceeded with a subdivision on the faith of an assumption induced by the council that it would, in accordance with its then practice, pay compensation at market value for land dedicated as public reserve. Hodgson CJ in Eq said:

55 *Mobil Oil Australia Ltd v Wellcome International Pty Ltd* (1998) 81 FCR 475, 513. The reference to "an interest" being granted is a recognition of the proprietary estoppel cases, which do not necessarily involve an assumption that a legal relationship will arise between the parties.

56 *Mobil Oil Australia Ltd v Wellcome International Pty Ltd* (1998) 81 FCR 475, 515.

57 For more detailed discussion of this issue and more cases, see Robertson, "Three Models of Promissory Estoppel" (2013) 7 *Journal of Equity* 226, 239–45.

58 *W v G* (1996) 20 Fam LR 49. See also *Lee Gleeson Pty Ltd v Sterling Estates Pty Ltd* (1991) 23 NSWLR 571; *Chanrich Properties Pty Ltd v Baulkham Hills Shire Council* [2001] NSWSC 229.

59 *W v G* (1996) 20 Fam LR 49, 66.

60 The actual relief granted was an order that the defendant pay the sum of $151,125 into an interest-bearing account, which was then to be used to buy annuities for each child, providing monthly payments until the child reached 18 years of age.

61 *Gray v National Crime Authority* [2003] NSWSC 111 (the availability of equitable estoppel in these circumstances was not challenged on appeal: *Australian Crime Commission v Gray* [2003] NSWCA 318).

62 *Chanrich Properties Pty Ltd v Baulkham Hills Shire Council* [2001] NSWSC 229.

> On the basis of my analysis of *The Commonwealth v Verwayen* the fact that the expectation was not one as to the existence of a legal relationship capable of strict classification as contractual, fiduciary, proprietary etc is not a reason to deny the plaintiff relief based on estoppel.[63]

In summary, Brennan J's assumption element is clearly stated too narrowly, but how wide it should be is a controversial question. It must at least be broadened to accommodate assumptions relating to the grant or transfer of interests in land. The controversial question is whether the existing state of the law requires it to be broadened further to accommodate assumptions relating to any future conduct of the inducing party. If equitable estoppel cannot be founded on an assumption that a non-proprietary benefit will be conferred on the relying party outside the context of a legal relationship, then cases such as those discussed above were wrongly decided.

Inducement

The nature of the requirement

[9.55] The second element necessary to establish an estoppel is that "the defendant has induced the plaintiff to adopt that assumption or expectation".[64] In many cases, the assumption will be induced by an express representation or promise by the inducing party, but it is clear that an express representation or promise is not required. In *Waltons Stores v Maher*, for example, it was Waltons' inaction that induced the Mahers to continue to act on the basis of the assumption they had made.[65] Waltons' silence was said to have induced Mr Maher to continue in the assumption that Waltons "was already bound" or "would execute and deliver the original deed as a matter of obligation".[66]

Must an unequivocal promise or representation be made?

[9.60] It has been held in some cases that an estoppel can only arise from a clear or unequivocal "promise" or "representation" made by the inducing party. This requirement was applied by Mason and Deane JJ in *Legione v Hateley*.[67] The case concerned a contract for the sale of land. The purchasers failed to pay the purchase price on the due date. The vendors then served a notice of intention to rescind the agreement if the purchase was not completed by 10 August. On 9 August, the purchasers' solicitor telephoned the vendors' solicitors and informed Miss Williams, the secretary dealing with the matter, that the purchasers would be able to complete the purchase on 17 August. Miss Williams responded that she thought that would be all right but would have to get instructions. As a consequence of that assurance, the purchasers did not make any further attempts to obtain finance in time to complete the purchase before the notice of rescission expired. The purchasers' attempt to tender the purchase price on 15 August was rejected, and the purchasers sought specific performance of the contract. The relevant issue for the court was whether an estoppel arose which prevented

63 *The Commonwealth v Verwayen* [2001] NSWSC 229, [99]. See also *Antov v Bokan* [2018] NSWSC 1474, [487].

64 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 428–9 (Brennan J). The burden of proving inducement was considered by the High Court in *Sidhu v Van Dyke* [2014] HCA 19; (2014) 251 CLR 505 and is discussed at [9.132].

65 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 407.

66 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 430 (Brennan J).

67 *Legione v Hateley* (1983) 152 CLR 406. See also *Low v Bouverie* [1891] 3 Ch 82.

the vendors from insisting on the deadline and thus treating the contract as rescinded on 11 August.

Gibbs CJ and Murphy J held that an estoppel would arise if it could be established that Miss Williams, by saying she would get instructions, had induced the purchasers' solicitors to believe that the vendors' right to rescind the contract would be kept in abeyance until instructions were obtained.[68] Gibbs CJ and Murphy J found that such a belief had been induced by Miss Williams' conduct and the purchasers had altered their position on the faith of that belief by failing to tender the purchase moneys, which were available on 9 August.[69] Accordingly, they would have held that the vendors were estopped from treating the contract as rescinded.[70] Mason and Deane JJ held that a promissory estoppel could result only from a clear representation as to the future conduct of the person making the representation.[71] They found that Miss Williams did not, by her words or conduct, make a clear and unequivocal representation to the effect that the purchasers could disregard the time fixed by the notice of rescission.[72] Accordingly, no estoppel arose against the vendors, despite the finding that the purchasers had acted to their detriment on the faith of Miss Williams' representation.[73] The fifth member of the Court, Brennan J, held that the vendors' solicitors had no actual or implied authority to vary the effect of the notice of intention to rescind and thus could not extend the time for completion. Since the purchasers' solicitors must be taken to have known of the limit of Miss Williams' authority, no promise or representation that the time for completion was to be extended could be inferred from Miss Williams' conduct.[74] The finding that no estoppel arose thus commanded a majority.

The requirement of a clear promise or representation is one of several ways of limiting the availability of equitable estoppel to cases in which liability is warranted. In *Legione v Hateley*, for example, it could have been said that it was not reasonable for the purchasers to have assumed from the language used by Miss Williams that the time for completion was to be extended.[75] The High Court judgments since *Legione v Hateley* have tended to focus on the requirement of an "induced assumption", rather than a promise or representation that is necessary to establish an estoppel.[76] In *Waltons Stores v Maher*,[77] no express promise or representation was made, but it was clearly reasonable for the Mahers to adopt the relevant assumption and to act as they did. Branson J observed in *Murphy v Overton Investments Pty Ltd*,[78] that since *Waltons Stores v Maher* and *Commonwealth v Verwayen*,[79] the "now preferred approach" is to ask whether the relying party was induced to adopt an assumption as to the future conduct of the inducing party, rather than to ask whether a promise or representation

68 *Legione v Hateley* (1983) 152 CLR 406, 421.

69 *Legione v Hateley* (1983) 152 CLR 406, 422.

70 *Legione v Hateley* (1983) 152 CLR 406, 423.

71 *Legione v Hateley* (1983) 152 CLR 406, 438.

72 *Legione v Hateley* (1983) 152 CLR 406, 440.

73 *Legione v Hateley* (1983) 152 CLR 406, 438.

74 *Legione v Hateley* (1983) 152 CLR 406, 453–5.

75 *Legione v Hateley* (1983) 152 CLR 406, 422.

76 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 397–9, 407, 413, 428–9, 442, 458–63; *Commonwealth v Verwayen* (1990) 170 CLR 394, 413–7, 444–9, 453–60, 500–2, cf 423–30.

77 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387.

78 *Murphy v Overton Investments Pty Ltd* [2001] FCA 500; (2001) 112 FCR 182.

79 *Commonwealth v Verwayen* (1990) 170 CLR 394.

has been made.[80] Although a clear promise or representation may not be a requirement in itself, the nature of the inducing conduct remains an important factor for the court to consider in determining whether reliance was reasonable.[81] In *Galaxidis v Galaxidis*,[82] the New South Wales Court of Appeal held that a representation that was insufficiently precise to give rise to a contract could (and did in that case) found a promissory estoppel, provided it was reasonable for the relying party to interpret and rely upon it in the way they did.[83]

The authorities on this point were reviewed at length in *Westpac Banking Corporation v The Bell Group Ltd (No 3)*[84] by Drummond AJA, who came to the conclusion that it is essential to distinguish in this respect between promissory and proprietary estoppel because a clear representation or promise is required for promissory estoppel but not proprietary estoppel. As noted above, a similar view was expressed in *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* by Keane J, who held that promissory estoppel requires a clear and unequivocal representation.[85] French CJ and Kiefel and Bell JJ in the same case synthesized the "clear and unequivocal representation requirement" with the reasonableness requirement, concluding that the words by which the assumption was induced "must be capable of misleading a reasonable person in the way that the person relying on the estoppel claims he or she has been misled".[86]

Detrimental reliance

The nature of the requirement

[9.65] The third element in the establishment of an estoppel is detrimental reliance. There are two aspects to this, as Brennan J made clear in *Waltons Stores v Maher*. First, the relying party must act or abstain from acting in reliance on the assumption (Brennan J's element 3), and secondly, it is necessary that such action or inaction will result in detriment to the relying party if the assumption is not fulfilled (Brennan J's element 5). The detrimental reliance requirement lies at the heart of estoppel by representation, as Dixon J made clear in *Thompson v Palmer* when he said that "the very foundation of the estoppel is the change of position to the prejudice of the party relying upon it".[87] It also lies at the heart of equitable estoppel.

It is important to distinguish here between two different types of detriment that arise in estoppel cases: expectation loss and reliance loss.[88] Expectation loss is simply the loss

80 *Murphy v Overton Investments Pty Ltd* [2001] FCA 500; (2001) 112 FCR 182, 202.

81 See *Thorner v Major* [2009] UKHL 18; [2009] 1 WLR 776 (discussed by McFarlane and Robertson, "Apocalypse Averted: Proprietary Estoppel in the House of Lords" (2009) 125 *Law Quarterly Review* 535).

82 *Galaxidis v Galaxidis* [2004] NSWCA 111.

83 *Galaxidis v Galaxidis* [2004] NSWCA 111, [93]; see also *Australian Crime Commission v Gray* [2003] NSWCA 318, [179]–[208]; *Flinn v Flinn* [1999] 3 VR 712; *Wright v Hamilton Island Enterprises Ltd* [2003] QCA 36, [87]; *Australian Goldfields NL (in liq) v North Australian Diamonds NL* [2009] WASCA 98; (2009) 40 WAR 191, [195]–[204]; *Evans v Evans* [2011] NSWCA 92, [121]–[127].

84 *Westpac Banking Corporation v The Bell Group Ltd (No 3)* [2012] WASCA 157; (2012) 44 WAR 1, [1744]–[1768].

85 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* [2016] HCA 26; (2016) 260 CLR 1, [142]–[143].

86 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* [2016] HCA 26; (2016) 260 CLR 1, [35], citing *Low v Bouverie* [1891] 3 Ch 82, 113 (an estoppel by representation case).

87 *Thompson v Palmer* (1933) 49 CLR 507, 549.

88 These types of loss equate to the expectation interest and reliance interest in contract damages identified by Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936) 46 *Yale Law Journal* 52 and 373. See [9.115] and Chapter 26.

of the benefit the relying party assumed she had or expected to receive. Reliance loss is loss suffered as a result of the relying party's reliance on the relevant assumption when the inducing party acts inconsistently with the assumption. Assume that A thinks B needs a holiday, tells B to book an overseas trip and promises to give her $5000 the following week to enable her to pay for it. In reliance on that promise, B books a trip and pays $1000 of her own money to a travel agent as a non-refundable deposit. A breaches the promise and B loses the deposit, having no more money of her own to pay for the balance. B's expectation loss is $5000, since that is the benefit she expected to receive from A. Her reliance loss is $1000, since that is the amount of the expenditure she incurred in reliance on the promise, which was lost when the promise was breached. In *Waltons Stores v Maher*,[89] the Mahers' expectation loss was the rent they expected Waltons to pay during the term of the anticipated lease. Their reliance loss was the wasted expenditure incurred in demolishing the existing building and partially constructing the building required by Waltons, along with any diminution in the value of their land as a result of the demolition. Expectation loss will always result from the breach of a promise to confer a valuable benefit, but reliance loss will arise only where the relying party has taken some action or inaction on the faith of the promise which proves detrimental when the promise is breached. The detriment (whether actual or potential) that is necessary to found an estoppel by representation or an equitable estoppel is reliance loss.

The stringency of the detrimental reliance requirement is a distinguishing feature of Australian law on estoppel by representation and equitable estoppel. In its early judgments on estoppel by representation, the High Court placed great emphasis on the detrimental reliance requirement and applied it strictly.[90] The relying party's detrimental reliance is essential to the establishment of an estoppel because it is that detrimental change of position that makes it unjust or unconscionable for the inducing party to depart from the assumption.[91] In England, it has been held that detriment is not essential to the establishment of a promissory estoppel; it is enough if the relying party has "acted on the belief induced by the other party".[92] This approach has been rejected in Australia[93] and the element of detriment confirmed as essential to promissory estoppel.[94]

Types of detrimental reliance

[9.70] Detrimental reliance takes many different forms. It often involves the wasted expenditure of money, such as expenditure on improvements to the inducing party's land[95]

89 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387.

90 *Thompson v Palmer* (1933) 49 CLR 507; *Grundt v Great Boulder Pty Gold Mines Ltd* (1937) 59 CLR 641; *Donaldson v Freeson* (1934) 51 CLR 598.

91 *Newbon v City Mutual Life Assurance Society Ltd* (1953) 52 CLR 723, 734–5; *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 401.

92 *WJ Alan Ltd v El Nasr Export and Import Co* [1972] 2 QB 189, 213–4, quoting *Tool Metal Manufacturing Co Ltd v Tungsten Electric Co Ltd* [1955] 1 WLR 761, 799. See further Cooke, *The Modern Law of Estoppel* (2000), pp 100–3; Robertson, "The Form and Substance of Equitable Estoppel" in Robertson and Goudkamp (eds), *Form and Substance in the Law of Obligations* (2019) 249, 255–9.

93 *Je Maintiendrai Pty Ltd v Quaglia* (1980) 26 SASR 101; *Gollin & Co Ltd v Consolidated Fertilizer Sales Pty Ltd* [1982] Qd R 435.

94 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387; *Commonwealth v Verwayen* (1990) 170 CLR 394.

95 For example, *Dillwyn v Llewelyn* (1862) 4 De GF & J 517; 45 ER 1285; *Re Whitehead* [1948] NZLR 1066; *Hamilton v Geraghty* (1901) 1 SR (NSW) 81.

or expenditure in preparation for a contract with the inducing party.[96] The relying party may expend time and energy in the performance of services for the inducing party, such as domestic services[97] or building work.[98] Inactivity can also be detrimental where it results in the loss of an opportunity to obtain a benefit or avoid a loss. A relying party may, for example, fail to exercise a contractual right, such as an option to renew a lease,[99] or may fail to commence litigation during the statutory limitation period.[100] Consenting to the adjournment of litigation can prove detrimental to the relying party,[101] as can commencing or continuing litigation.[102] Inactivity will not, of course, be regarded as detrimental when there is nothing the relying party could have done to improve its position.[103]

It is not possible to provide a comprehensive catalogue of the different types of detrimental action and the cases continue to produce unexpected examples. In *W v G*,[104] for example, the relying party conceived and bore two children on the faith of the inducing party's promise to assist with and contribute to their upbringing. In *Commonwealth v Verwayen*,[105] the relying party continued litigation relating to a traumatic incident on the basis of an assumption that the Commonwealth would not take advantage of certain defences available to it. In doing so, he was found to have suffered increased stress, anxiety and ill-health.[106] In *Gray v National Crime Authority*,[107] the plaintiffs entered the defendant's witness protection program (and were thereby "severed from their lawful means of livelihood") on the faith of assurances that the defendant would make good any financial disadvantage that resulted. In *Arfaras v Vosnakis*,[108] the plaintiff caused his late wife's body to be interred in a double burial plot controlled by his mother-in-law, the defendant. He did so on the understanding that the defendant would transfer her rights in relation to the plot to the plaintiff so that his remains could in due course be buried alongside those of his wife. When the defendant changed her mind, the plaintiff was faced with the prospect of exhuming his wife's remains in order to fulfil his wish to be buried with her. An equitable estoppel required the defendant to transfer the burial plot licence to the plaintiff.

The relying party's circumstances

[9.75] Whether particular action is detrimental may depend on the situation of the relying party, as is shown by *Je Maintiendrai Pty Ltd v Quaglia*.[109] The issue in that case was whether an estoppel arose from a landlord's gratuitous promise to accept a reduced amount of rent

96 For example, *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387.

97 For example, *Public Trustee v Wadley* (1997) 7 Tas R 35.

98 For example, *Jackson v Crosby (No 2)* (1979) 21 SASR 280.

99 *S & E Promotions Pty Ltd v Tobin Brothers Pty Ltd* (1994) 122 ALR 637.

100 *Morris v FAI General Insurance Company Ltd* (1995) 8 ANZ Insurance Cases 61-258; *Re Lindsay v Smith* [2001] QCA 229.

101 *Collin v Holden* [1989] VR 510.

102 *Commonwealth v Verwayen* (1990) 170 CLR 394; *Commonwealth v Clark* [1994] 2 VR 333.

103 *Thompson v Palmer* (1933) 49 CLR 507, 521, 527–8, 548–9, 559.

104 *W v G* (1996) 20 Fam LR 49.

105 *Commonwealth v Verwayen* (1990) 170 CLR 394.

106 *Commonwealth v Verwayen* (1990) 170 CLR 394, 448–9 (Deane J), 462 (Dawson J).

107 *Gray v National Crime Authority* [2003] NSWSC 111, [251].

108 *Arfaras v Vosnakis* [2016] NSWCA 65.

109 *Je Maintiendrai Pty Ltd v Quaglia* (1980) 26 SASR 101.

from the tenants. The tenants rented a shop in the landlord's shopping centre in which they conducted a hairdressing business. The landlord agreed to a rent reduction because of financial difficulties faced by the tenants and because the landlord was experiencing difficulties in filling vacant shops in the shopping centre. The landlord accepted the reduced rent for a period of 18 months until the tenants sought to leave the premises, at which time the landlord demanded the amount unpaid.

The Full Court of the South Australian Supreme Court by majority upheld the decision of the trial judge that promissory estoppel prevented the landlord from claiming the unpaid portion of the rent. The Full Court held unanimously that a promissory estoppel could only arise if the promisor had altered his or her position on the faith of the promise and would thereby suffer detriment if the promisor was subsequently allowed to assert his or her strict legal rights.[110] While acknowledging that the evidence as to detriment was sparse, King CJ and White J accepted the finding of the trial judge that, in view of their financial position, it would be a detriment to the tenants to be forced to pay the arrears in a lump sum.[111] More controversially, White J also referred to the fact that, in reliance on the landlord's promise, the tenants remained in the premises and gave up other choices open to them, such as abandoning the shop and taking their chances "about being sued for breach of contract".[112] Cox J dissented on the basis that, although it was possible to speculate about detriment the tenants might have suffered, the tenants had not discharged the burden of establishing affirmatively that they had acted to their detriment on the faith of the assumption.[113]

Crucial to the decision in *Je Maintiendrai* was the principle that detriment must be assessed at the time the inducing party seeks to resile from the relevant assumption.[114] Until the landlord attempted to resile from the assumption that the full rent was not payable, the tenants actually obtained a benefit in paying a reduced amount of rent. That benefit would have become a detriment if the landlord had been able to claim the unpaid amount, however, because it was clearly easier for impecunious persons, such as the tenants, to make small periodical payments than to pay a lump sum.[115] Presumably no estoppel would have arisen had the tenants been wealthy persons for whom payment of the unpaid rent in a lump sum would have presented no difficulty. That is, unless the wealthy tenants had, on the faith of the promised rent reduction, incurred expenditure which they would not otherwise have incurred.

Material detriment

[9.85] It is said that the detriment suffered or to be suffered by the relying party as a result of reliance on the relevant assumption must be material,[116] significant[117] or substantial.[118]

110 *Je Maintiendrai Pty Ltd v Quaglia* (1980) 26 SASR 101, 105–6, 113–5, 117.

111 *Je Maintiendrai Pty Ltd v Quaglia* (1980) 26 SASR 101, 107, 115–6.

112 *Je Maintiendrai Pty Ltd v Quaglia* (1980) 26 SASR 101, 115. But see further [9.215].

113 *Je Maintiendrai Pty Ltd v Quaglia* (1980) 26 SASR 101, 120–1.

114 *Je Maintiendrai Pty Ltd v Quaglia* (1980) 26 SASR 101, 114–5, 117. Where the inducing party has not sought to resile from the assumption, the court will need to assess the detriment that would arise if the inducing party attempted to resile.

115 *Je Maintiendrai Pty Ltd v Quaglia* (1980) 26 SASR 101, 106–7.

116 *Thompson v Palmer* (1933) 49 CLR 507, 547; *Newbon v City Mutual Life Assurance Society Ltd* (1953) 52 CLR 723, 734; *Chin v Miller* (1981) 37 ALR 171; *Territory Insurance Office v Adlington* (1992) 109 FLR 124, 136.

117 *Commonwealth v Verwayen* (1990) 170 CLR 394, 444.

118 *Je Maintiendrai Pty Ltd v Quaglia* (1980) 26 SASR 101, 117.

This requirement is exemplified by the decision of the New South Wales Court of Appeal in *Hawker Pacific Pty Ltd v Helicopter Charter Pty Ltd*.[119] In that case, the inducing party led the relying party to believe that the inducing party would pay a certain sum of money to the relying party in settlement of a disputed claim. On the faith of that assumption, employees of the relying party made a number of trips to the inducing party's premises to collect a cheque in payment of the sum due. The Court of Appeal held that no equitable estoppel arose in part because the detriment resulting from these "fruitless visits" did not "constitute a material or significant disadvantage or detriment sufficient to support an estoppel".[120]

As Handley JA observed in that case, a clear distinction can be drawn between the valuable consideration required to support a contract and the material detriment required for an estoppel.[121] The loss of a single peppercorn is sufficient detriment to constitute valuable consideration but is not sufficient detriment to establish an estoppel. The distinction is justified on the basis that to constitute consideration, the peppercorn must have been accepted as the price of a bargain. It is the bargain, rather than the detriment, that forms the basis of contractual obligation and the promise breaker has at least a theoretical choice as to whether to accept it. Since estoppels lack the elements of acceptance and mutuality, the detriment itself plays a crucial role in justifying the imposition of obligation and must therefore be substantial.

It is important to note that neither the common law nor the equitable principles of estoppel require that detriment has actually been suffered by the relying party at the time the estoppel is sought to be established. The prospect of detriment is sufficient in each case. Where the inducing party has acted inconsistently with the assumption, the relying party may have suffered some detriment, but the detriment may be ongoing. The notion of prospective detriment is particularly important in a case where the inducing party has not yet departed from the assumption in question but has simply threatened to do so. Unless the inducing party has actually departed from the assumption, the relying party will not have suffered any detriment.[122] Accordingly, the relevant question in many cases is whether the relying party *would* suffer detriment if the inducing party were allowed to do so. It must be noted, however, that a mere conjectural or speculative possibility of detriment is not sufficient to establish an estoppel.[123]

Knowledge of reliance or intention to induce reliance

[9.87] The fourth of Brennan J's elements of equitable estoppel is a requirement that the inducing party knew that the relying party was acting on the assumption or intended him or her to do so. This element was crucial in *Waltons Stores v Maher* itself, where the relevant assumption was induced by silence. Brennan J said:

> In the present case the question is whether Waltons, knowing that Mr Maher was labouring under the belief that Waltons was bound to the contract, was under a duty to correct that belief. The evidence was capable of supporting an inference that Waltons knew the belief under which

119 *Hawker Pacific Pty Ltd v Helicopter Charter Pty Ltd* (1991) 22 NSWLR 298.

120 *Hawker Pacific Pty Ltd v Helicopter Charter Pty Ltd* (1991) 22 NSWLR 298, 308, see also 305.

121 *Hawker Pacific Pty Ltd v Helicopter Charter Pty Ltd* (1991) 22 NSWLR 298, 308.

122 *Commonwealth v Clark* [1994] 2 VR 333, 369–81.

123 *Territory Insurance Office v Adlington* (1992) 2 NTLR 55.

> Mr Maher was labouring when Waltons became aware that Mr Maher was doing the work specified in the deed. Waltons deliberately refrained from correcting what Waltons must have regarded as an erroneous belief.[124]

Knowledge of reliance or an intention to induce reliance may not be required in all cases. Mason CJ and Wilson J suggested in *Waltons Stores v Maher* that the unconscionable conduct that grounds equitable estoppel may be found in the creation of an assumption that a promise will be performed together with knowledge that the other party relied to his or her detriment. Alternatively, they suggested, it might be found in a reasonable expectation on the part of a promisor that his or her promise will induce detrimental reliance. Their alternative formulation was based on the US doctrine of promissory estoppel, which is described in the Second Restatement of Contacts, s 90 as follows:

> (1) A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise. The remedy granted for breach may be limited as justice requires.[125]

It may be that knowledge of reliance or an intention to induce reliance is only required in cases in which the assumption is induced by silence. Liability in equitable estoppel has the effect of attributing to the inducing party legal responsibility for the detriment suffered by the relying party. There must be some conduct on the part of the inducing party that justifies that attribution of responsibility. Where no express promise has been made, some other factor must make it unconscionable or unjust for the inducing party to act inconsistently with the assumption. Where an assumption is induced by silence, it may be necessary to show that the inducing party either intended reliance or knew of the acts of reliance and refrained from correcting or warning the relying party.[126] In other cases, it has been held to be sufficient that the inducing party "ought to have known" that the relying party would act on the assumption.[127]

Departure or threatened departure

[9.90] Brennan J's sixth and final element of an equitable estoppel claim is that the inducing party "has failed to act to avoid [the] detriment whether by fulfilling the assumption or expectation or otherwise".[128] In most cases, an estoppel claim will not arise unless the inducing party has departed or threatened to depart from the assumption. It is sometimes said that the relying party has nothing to complain about unless the inducing party seeks to breach the promise or deny the truth of the assumption.[129] It is the inducing party's departure or threatened departure from the assumption which is said to constitute unconscionable conduct. On that basis, it has been held that:

124 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 428.

125 American Law Institute, *Restatement of Contracts 2d* (1981), § 90.

126 See Robertson, "Knowledge and Unconscionability in a Unified Estoppel" (1998) 24 *Monash University Law Review* 115.

127 *New Zealand Pelt Export Company Ltd v Trade Indemnity New Zealand Ltd* [2004] VSCA 163, [98]–[99].

128 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 429.

129 For example, *Thompson v Palmer* (1933) 49 CLR 507, 547.

> An equitable estoppel cannot arise until there has been an unjust or unconscionable departure or threat to depart from the assumption adopted and acted upon by the party seeking to assert the estoppel.[130]

There have, however, been several cases in which equitable estoppels have been held to arise without any attempt by the inducing party to depart from the assumption. In these cases, the estoppel has been held to take effect once an assumption has been induced and reasonably relied upon.[131] The inducing party is then under an obligation not to act inconsistently with it without taking steps to ensure that the departure does not cause harm to the relying party.

Reasonableness

[9.95] Just as all promises cannot be enforced by the law of contract, it is clear that not all inconsistent conduct that causes harm through detrimental reliance can give rise to an equitable estoppel or estoppel by representation. It is necessary to limit the circumstances in which an inducing party will be held responsible for such loss resulting from reliance on assumptions induced by his or her conduct. Two mechanisms have been used in the cases to limit the scope of operation of equitable estoppel: first, a requirement that the relying party's reliance must be reasonable and, secondly, a requirement that the inducing party's departure from the relevant assumption must be unconscionable. Although the two requirements perform much the same function, they do so from different perspectives. The reasonableness requirement is principally concerned with whether the relying party is deserving of protection, while the unconscionability requirement is essentially concerned with whether the relying party deserves blame. Both limits, however, necessarily require the court to allocate risk and responsibility and to make a judgment about what are acceptable standards of behaviour, both for those engaging in conduct which might be relied upon and for those relying on the conduct of others.[132]

The reasonableness requirement involves two related questions: first, whether the relying party acted reasonably in adopting the relevant assumption and, secondly, whether the relying party acted reasonably in taking the detrimental action that he or she took on the faith of the assumption.[133] Authority for the reasonableness requirement is provided by *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd*, which also illustrates the first aspect.[134] In that case, tenants operating restaurants in the Crown Casino complex entered into five-year leases on terms that required the tenants to undertake costly refurbishments. During negotiations, the tenants expressed concern about the cost of the refurbishments and asked

130 *Ashton Mining Ltd v Commissioner of Taxation* [2000] FCA 590; (2000) 44 ATR 249, [50]; see also Spencer, Bower and Turner, *The Law Relating to Estoppel by Representation* (3rd ed, 1977), p 110.

131 *Kintominas v Secretary, Department of Social Security* (1991) 30 FCR 475; *Sarkis v Deputy Commissioner of Taxation* [2005] VSCA 67; *Secretary, Department of Family and Community Services v Wall* [2006] FCA 863; *Repatriation Commission v Tsourounakis* [2007] FCAFC 29; (2007) 158 FCR 214. See also *McNab v Graham* [2017] VSCA 352; (2017) 53 VR 311 and discussion in Robertson, "Estoppels and Rights-Creating Events: Beyond Wrongs and Promises" in Neyers, Bronaugh and Pitel (eds), *Exploring Contract Law* (2009), pp 199–224.

132 See further Robertson, "Reasonable Reliance in Estoppel by Conduct" (2000) 23(2) *University of New South Wales Law Journal* 87, 94–7.

133 *Standard Chartered Bank Aust Ltd v Bank of China* (1991) 23 NSWLR 164, 180–1; [2001] FCA 500; (2001) 112 FCR 182, 202.

134 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* [2016] HCA 26; (2016) 260 CLR 1. See also *Thorner v Major* [2009] UKHL 18; [2009] 1 WLR 776.

for a longer term. The landlord was unwilling to offer a longer term but told the tenants that they would be "looked after at renewal time". The tenants claimed to have entered into the leases on the assumption that, after the initial term, they would be offered new leases on the same terms and conditions. French CJ and Keifel and Bell JJ held that the landlord's statement that the tenants would be "looked after at renewal time" was "not capable of conveying to a reasonable person that the tenants would be offered a further lease".[135] Keane J reached the same conclusion.[136]

Another example is *Murphy v Overton Investments Pty Ltd*.[137] In that case, the operator of a retirement village gave prospective tenants an estimate of the maintenance expenses for which they would be liable on "present budget figures". A majority of the Full Federal Court held that if the tenants assumed that this estimate took into account all expenditure likely to be incurred in future budget periods, it was "unreasonable for them to have done so".[138] In the life of a retirement village, new types of expenditure would be likely to arise as buildings aged, public authorities imposed different requirements and management practices changed.

Unconscionable conduct

[9.100] It is commonly said that equitable estoppel is essentially concerned with the prevention of unconscionable conduct. In some cases, unconscionable conduct is referred to as a justification for granting relief in estoppel cases; the courts grant relief because it is unconscionable to depart from an assumption which one has induced another to adopt and detrimentally rely upon.[139] Unconscionability is then seen as "the underlying principle informing the elements of estoppel, rather than a discrete ingredient which is additional to those elements".[140] Unconscionable conduct might also be understood as the conclusion that will be drawn if the elements discussed above have been satisfied, and the basis on which the granting of a remedy is justified.

In other cases, unconscionable conduct has been taken to be a positive requirement in itself (ie, an additional element that the relying party must establish). In *Forbes v Australian Yachting Federation Inc*,[141] for example, Santow J held that "it is an essential requirement of the principle of [equitable] estoppel, that the conduct of the parties sought to be estopped must properly be characterised as unconscionable". In *Silovi Pty Ltd v Barbaro*,[142] Priestley JA held that, for an estoppel to operate, there must be an induced assumption "and reliance on that by the plaintiff, in circumstances where departure from the assumption by the defendant would be unconscionable".

135 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* [2016] HCA 26; (2016) 260 CLR 1, [35].

136 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* [2016] HCA 26; (2016) 260 CLR 1, [160]

137 *Murphy v Overton Investments Pty Ltd* [2001] FCA 500; (2001) 112 FCR 182.

138 *Murphy v Overton Investments Pty Ltd* [2001] FCA 500; (2001) 112 FCR 182, 201. On appeal, the High Court recognised that the tenants had established a cause of action in respect of misleading or deceptive conduct: see [33.125].

139 For example, *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 419; (1990) 170 CLR 394, 407. See also Cooke, *The Modern Law of Estoppel* (2000), pp 84–8.

140 *Anaconda Nickel Ltd v Edensor Nominees Pty Ltd* [2004] VSCA 167, [40].

141 *Forbes v Australian Yachting Federation Inc* (1996) 131 FLR 241, 287.

142 *Silovi Pty Ltd v Barbaro* (1988) 13 NSWLR 466, 472. See also *Austotel Pty Ltd v Franklins Selfserve Pty Ltd* (1989) 16 NSWLR 582, 610.

If unconscionability is seen as a separate requirement, then it clearly involves a broad inquiry and a judgment that takes into account all the circumstances of the case. Deane J said in *Commonwealth v Verwayen*[143] that the inquiry as to unconscionability relates to the conduct of the inducing party in all the circumstances and focuses on the role of the inducing party in inducing the adoption of the assumption. The inducing party's knowledge of the relying party's assumption and any intention to induce reliance are also clearly relevant, particularly where the assumption has been induced by silence on the part of the inducing party.[144] It is recognised that whether it was reasonable for the relying party to adopt and act upon the assumption is central to the question of unconscionability.[145] It has been said that it cannot be unconscionable for the inducing party to deny responsibility for detriment sustained as a result of unreasonable reliance.[146] Deane J said in *Commonwealth v Verwayen* that:

> Ultimately, however, the question whether departure from the assumption would be unconscionable must be resolved not by reference to some preconceived formula framed to serve as a universal yardstick but by reference to all the circumstances of the case, including the reasonableness of the conduct of the other party in acting upon the assumption and the nature and extent of the detriment which he would sustain by acting upon the assumption if departure from the assumed state of affairs were permitted.[147]

THE EFFECT OF AN ESTOPPEL

Estoppel by representation

[9.105] To understand the effect of an estoppel, we need to go back to the origin of the word in the plug or stopper metaphor.[148] Estoppel by representation operates in a manner that is consistent with that origin. Where a representation of fact is relied upon by a relying party, the effect of the estoppel is to stop up the mouth of the inducing party and prevent the inducing party from asserting facts contrary to his or her own representation.[149] The rights of the parties are then determined by reference to the represented or assumed state of affairs. An estoppel by representation of fact can be used defensively, where an action which would otherwise be available to the plaintiff is not available on the assumed state of affairs. In *Avon County Council v Howlett*,[150] for example, the plaintiff paid money to the defendant by mistake and would have been entitled to recover it in restitution. An estoppel arose because the plaintiff represented to the defendant that he was entitled to the money in question and the

143 *Commonwealth v Verwayen* (1990) 170 CLR 394, 444; see also *Australian Crime Commission v Gray* [2003] NSWCA 318, [200]–[208].

144 *Commonwealth v Verwayen* (1990) 170 CLR 394, 444–5. See [9.87].

145 See *Doueihi v Construction Technologies Australia Pty Ltd* [2016] NSWCA 105; (2016) 92 NSWLR 247, [80] and [202]–[216] and *Australian Securities Commission v Marlborough Gold Mines Ltd* (1993) 177 CLR 485, 506.

146 *Galaxidis v Galaxidis* [2004] NSWCA 111, [94].

147 *Commonwealth v Verwayen* (1990) 170 CLR 394, 445. For an attempt to describe the various criteria relevant to a broad unconscionability test, see Spence, *Protecting Reliance – The Emergent Doctrine of Promissory Estoppel* (1999), pp 59–66.

148 See [9.10].

149 Spencer, Bower and Turner, *The Law Relating to Estoppel by Representation* (3rd ed, 1977), p 112, cited with approval in *Avon County Council v Howlett* [1983] 1 WLR 605, 622.

150 *Avon County Council v Howlett* [1983] 1 WLR 605. See further [10.120].

defendant spent the money in reliance on that representation. The effect of the plaintiff being held to the assumed state of affairs was that no action was available.

An estoppel by representation can also be used aggressively, to establish a state of affairs in which a cause of action exists, where that cause of action would not be available on the true state of affairs.[151] In *Waltons Stores v Maher*,[152] for example, Gaudron J, like the trial judge and the Court of Appeal below, held that an estoppel arose at common law which prevented the defendant from denying that it had entered into an agreement with the plaintiffs. The rights of the parties were, therefore, determined on the basis of the assumed state of affairs, and the plaintiffs were able to maintain an action on an agreement which would not otherwise have been enforceable.

Equitable estoppel

Satisfying the "equity"

[9.110] It is often said that a party is "estopped" from doing something by way of equitable estoppel, but it is more accurate to say that the effect of establishing an equitable estoppel is to raise an "equity" in favour of the relying party. The word "equity" in this context means an entitlement to some equitable relief, the determination of which is within the court's discretion. The "equity" raised by estoppel is said to be an undefined equity, since the relying party cannot assert a right to a particular remedy but must persuade the court to fashion a remedy to suit the facts of the particular case.[153] The discretion exercised by a court in this context is a principled one, which is exercised according to well-established criteria.

Like estoppel by representation, promissory estoppel has traditionally had a preclusionary operation; where a person promised that contractual rights would not be enforced, and that promise was relied upon by the promisee, the effect of the estoppel was to prevent the promisor from asserting those rights, either temporarily or permanently.[154] Thus, in *Je Maintiendrai v Quaglia*, the landlord was held to be "estopped from claiming the alleged arrears of rent".[155] The operation of proprietary estoppel has been more flexible, and courts of equity have exercised a wide discretion in giving effect to the equity raised by that doctrine. The courts have usually exercised that discretion by requiring the inducing party to perform the relevant promise or to act in accordance with the relevant representation.[156] In *Dillwyn v Llewelyn*,[157]

151 Other prominent cases in which common law estoppel has been used to establish a cause of action include *Seton, Laing, & Co v Lafone* (1887) 19 QBD 68 (conversion) and *Laws Holdings Pty Ltd v Short* (1972) 46 ALJR 563 (debt).

152 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 463–4.

153 Neave and Weinberg, "The Nature and Function of Equities" (Pt 1) (1978) 6 *University of Tasmania Law Review* 24, 27.

154 See, eg, *Hughes v Metropolitan Railway Co* (1877) 2 App Cas 439; *Birmingham and District Land Co v London and North Western Railway Co* (1888) 40 Ch D 268; *Central London Property Trust Ltd v High Trees House Ltd* [1947] 1 KB 130; *Motor Oil Hellas (Corinth) Refineries SA v Shipping Corporation of India Ltd* [1990] 1 Lloyd's Rep 391, 399; see also Spencer, Bower and Turner, *The Law Relating to Estoppel by Representation* (3rd ed, 1977), pp 395–400; Peel, *Treitel's Law of Contract* (14th ed, 2015), 3-077–3-092.

155 *Je Maintiendrai v Quaglia* (1980) 26 SASR 101, 116.

156 See Robertson, "Satisfying the Minimum Equity: Equitable Estoppel Remedies after Verwayen" (1996) 20 *Melbourne University Law Review* 805, 809-20 and "The Reliance Basis of Proprietary Estoppel Remedies" (2008) 72 *The Conveyancer and Property Lawyer* 295.

157 *Dillwyn v Llewelyn* (1862) 4 De GF & J 517; 45 ER 1285.

for example, an estoppel arose when the plaintiff built a house on land promised to him by his father. The effect of the estoppel was to render the promise enforceable. The son's expenditure "created a binding obligation" on the father to transfer the land to the son.[158] There have, however, been some proprietary estoppel cases in which the courts have granted relief that has had the effect of compensating the relying party for loss suffered as a result of their reliance, without fulfilling his or her expectations.[159] In *The Unity Joint Stock Banking Association v King*,[160] for example, the estoppel was held to create a lien in favour of the relying parties for the amount of their expenditure on the land promised to them.

The recognition in *Waltons Stores v Maher*[161] of a unity of principle between promissory and proprietary estoppel has led – in many but not all cases – to the discretionary approach that is followed in proprietary estoppel cases being applied to all cases of equitable estoppel.[162] The effect of any equitable estoppel on this view is to raise an equity in favour of the relying party which the courts must satisfy. The courts are now quite consistent in their approach to determining the appropriate remedy to give effect to an estoppel or "satisfy the equity" raised by the estoppel. An attempt will be made at [9.135] to summarise the current approach.[163] Before doing so, it is necessary to identify some of the key concepts and consider the reasoning in the three most important High Court decisions on this point.

The reliance interest and the expectation interest

[9.115] Although the courts do not usually use this language, it is helpful to analyse estoppel remedies by reference to the two "interests" the relying party has.[164] First, the relying party has an interest in protection from harm resulting from his or her reliance on the relevant promise or representation. The most direct means of protecting the relying party's reliance interest is to order the inducing party to pay monetary compensation for the detriment suffered by the relying party in reliance on the relevant assumption.[165] The court can also protect the reliance interest by granting a lien or charge over the inducing party's property to the value of expenditure incurred by the relying party in reliance on the relevant assumption.[166] Although the reliance interest plays an important role in the determination of estoppel relief,

158 *Dillwyn v Llewelyn* (1862) 4 De GF & J; 45 ER 1285, 1287.

159 For example, *Re Whitehead* [1949] NZLR 1066; *Hussey v Palmer* [1972] 1 WLR 1286; *Morris v Morris* [1982] 1 NSWLR 61 and the cases discussed at [9.135].

160 *The Unity Joint Stock Banking Association v King* (1858) 25 Beav 72; 53 ER 563.

161 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387.

162 As discussed at [9.150]–[9.165], some judges deny this development and insist that promissory estoppel still has a purely defensive operation; compare *Saleh v Romanous* [2010] NSWCA 274; (2010) 79 NSWLR 453, discussed at [9.210] with *ACN 074 971 109 (as trustee for the Argot Unit Trust) v The National Mutual Life Association of Australasia Limited* [2008] VSCA 247; (2008) 21 VR 351, discussed at [9.135] and *Anaconda Nickel Ltd v Edensor Nominees Pty Ltd* [2004] VSCA 167, discussed at [9.195].

163 See [9.135].

164 These labels refer to the reliance interest and expectation interest in contract damages identified by Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936) 46 *Yale Law Journal* 52 and 373.

165 As proposed in *Commonwealth v Verwayen* (1990) 170 CLR 394, 431, 504 and granted in cases such as *Public Trustee v Wadley* (1997) 7 Tas R 35, *Young v Lalic* [2006] NSWSC 18; *EK Nominees Pty Ltd v Woolworths Ltd* [2006] NSWSC 1172; *Powell v Benney* [2007] EWCA Civ 1283; *ACN 074 971 109 Pty Ltd (as Trustee for the Argot Unit Trust) v The National Mutual Life Association of Australasia* [2008] VSCA 247; (2008) 21 VR 351; and *Ryan v Ryan* [2016] TASSC 4.

166 See, eg, the proprietary estoppel cases *The Unity Joint Stock Mutual Banking Association v King* (1858) 25 Beav 72; 53 ER 563, *Morris v Morris* [1982] 1 NSWLR 61 and *McGuane v Welch* [2008] EWCA Civ 785.

the compensation of harm resulting from reliance is not the usual remedy granted in estoppel cases, for reasons discussed at [9.135].

The second interest the relying party has is in receiving the benefit that he or she expected to receive or was led to believe that he or she had. The expectation interest is protected when the court orders specific performance, or payment of damages in lieu of specific performance, of an unexecuted agreement which the inducing party promised would be executed.[167] It is also protected where the court refuses to allow the inducing party to depart from a representation as to future conduct,[168] orders the inducing party to transfer to the relying party a promised interest in land,[169] or orders the inducing party to pay monetary compensation to the relying party calculated to put the relying party in the position he or she would be in if the assumption was fulfilled (eg, the value of a promised interest in land).[170]

The expectation and reliance interests are usually overlapping, in that protection of the expectation interest will usually also protect the reliance interest. The fulfilment of the relying party's expectations ensures that no detriment is suffered as a result of his or her reliance, because the relying party receives the benefits that he or she was counting on receiving.[171] Indeed, as Fuller and Perdue have observed in the contractual context, the value of the expectancy offers "the measure of damages most likely to reimburse the plaintiff for the (often very numerous and difficult to prove) individual acts and forbearances which make up his total reliance on the contract".[172]

As we will see, both the expectation interest and the reliance interest play an important role in the determination of estoppel remedies. The relying party has a prima facie entitlement to have the relevant assumption made good, but this will be displaced if to do so would be disproportionate to the harm that would be suffered by the relying party if the inducing party were allowed to depart from the assumption.

Development of the current approach

Waltons Stores v Maher

[9.120] The current approach to equitable estoppel remedies has its origins in the judgment of Scarman LJ in *Crabb v Arun District Council*.[173] Scarman LJ said that once an equity is established by way of estoppel, the court should determine the extent of the equity and then the relief appropriate to satisfy the equity. He went on to identify "the *minimum equity* to do justice to the plaintiff" in the circumstances of the case.[174] In *Waltons Stores v Maher*,[175]

167 See, eg, *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387.

168 See, eg, *Commonwealth v Verwayen* (1990) 170 CLR 394, where the inducing party was prevented from pleading defences which the relying party was led to believe would not be pleaded.

169 See, eg, *Dillwyn v Llewelyn* (1862) 4 De GF & J 517; 45 ER 1285, where the inducing party was ordered to transfer to the relying party the land which the relying party was led to believe would be transferred to him.

170 See, eg, *Giumelli v Giumelli* [1999] HCA 10; (1999) 196 CLR 101.

171 There are, however, rare cases such as *Baker v Baker* (1993) 25 HLR 408, in which the relying party's detrimental reliance (giving up rented accommodation and contributing £33,950 towards the defendants' purchase of a house) was of greater value than his expectancy (that he would have a right to reside in a room in the defendants' house rent-free for the rest of his life).

172 Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936) 46 *Yale Law Journal* 52, 60.

173 *Crabb v Arun District Council* [1976] 1 Ch 179.

174 *Crabb v Arun District Council* [1976] 1 Ch 179, 198 (emphasis added).

175 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 426–7.

Brennan J interpreted the "minimum equity" raised by equitable estoppel as the minimum necessary to prevent detriment being suffered by the relying party as a result of his or her reliance. Essential to this approach to relief is the notion that equitable estoppel operates as a source of legal obligation, rather than operating, like estoppel by representation, as a means of establishing a state of affairs by reference to which the legal rights of the parties are to be established. This approach to relief is founded on the idea that the object of equitable estoppel is to prevent detriment flowing from reliance on promises, rather than to enforce those promises, and relief is determined accordingly.

The remedy granted in *Waltons Stores v Maher* was equitable damages in lieu of specific performance of the lease the Mahers assumed Waltons had signed or would sign. The effect of the estoppel was essentially preclusionary: the estoppel effectively prevented Waltons from denying the existence of contractual rights which the Mahers were induced to believe they had or would have.[176] This result necessarily followed from the application by Deane and Gaudron JJ of the principle of estoppel by representation of fact; the rights of the parties were determined on the basis of the state of affairs represented by Waltons. The other three judges, applying equitable estoppel, exercised a discretion in giving effect to the estoppel. Mason CJ and Wilson J approved Scarman LJ's "minimum equity" approach to relief but did not discuss how best to satisfy the equity arising in favour of the Mahers. They held that Waltons was "estopped in all the circumstances from retreating from its implied promise to complete the contract".[177] Brennan J found that the equity raised against Waltons was to be satisfied by treating Waltons "as though it had done what it induced Mr Maher to expect that it would do, namely by treating Waltons as though it had executed and delivered the original lease".[178]

Commonwealth v Verwayen

[9.125] The remedial effects of equitable estoppel received detailed attention in *Commonwealth v Verwayen*.[179] All members of the court recognized the flexibility of the remedy, although the relief ultimately granted was to prevent the Commonwealth from behaving inconsistently with the assumption that they had led Mr Verwayen to adopt and rely upon. The case was complicated by the fact that Gaudron and Toohey JJ decided the case on the basis of waiver, rather than estoppel, and held that the Commonwealth had irrevocably waived its right to take advantage of the relevant defences. The other members of the majority, Deane and Dawson JJ, held that the estoppel that arose against the Commonwealth was to be satisfied by fulfilling Verwayen's assumption and preventing the Commonwealth from pleading the defences. Mason CJ, Brennan J and McHugh J all emphasised the principle that the remedy should go no further than is necessary to prevent detriment.[180]

Giumelli v Giumelli

[9.130] The remedial consequences of equitable estoppel were again considered by the High Court in *Giumelli v Giumelli*.[181] Robert Giumelli and his parents were partners in a family

176 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 408, cf 431–3.

177 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 408.

178 *Commonwealth v Verwayen* (1990) 170 CLR 394, 445–6.

179 *Commonwealth v Verwayen* (1990) 170 CLR 394.

180 *Commonwealth v Verwayen* (1990) 170 CLR 394, 413, 441–3, 501, 504.

181 *Giumelli v Giumelli* [1999] HCA 10; (1999) 196 CLR 101.

orchard business. Robert lived in a house he had built on one of the properties used by the partnership, which was owned by his parents. Robert's parents promised him that if he stayed on the property, it would be subdivided and a portion including the house and an orchard (the "promised lot") would be transferred to him. On the faith of that promise, Robert gave up an opportunity to pursue a different career and continued to work the property. The relationship between Robert and his parents broke down when he married a woman of whom his parents disapproved and his parents refused to transfer the property. The Full Court found that the parents held the property on trust to convey the promised lot to Robert.

The parents appealed to the High Court on the basis that the Full Court should not have granted relief that went beyond the reversal of detriment. The High Court did not accept the appellants' argument that the judgments in *Commonwealth v Verwayen* required more limited relief to be granted. The court held that the judgments in *Commonwealth v Verwayen* did not foreclose the granting of a remedy such as that made by the Full Court. This cannot be doubted, since all of the judgments in *Commonwealth v Verwayen* emphasised the flexibility of the remedy. In a joint judgment in *Giumelli v Giumelli*, Gleeson CJ, McHugh, Gummow and Callinan JJ referred with approval to the statement of Deane J in *Commonwealth v Verwayen* that the relying party has a prima facie entitlement to relief based on the assumed state of affairs which will be qualified if that would "exceed what could be justified by the requirements of conscientious conduct and would be unjust to the estopped party".[182] Although the High Court evidently did not consider that the remedy exceeded what could be justified by the requirements of conscientious conduct, the court did find that, in the circumstances of the case, monetary relief was more appropriate. The court held that the parents should pay Robert a sum of money calculated by reference to the value of the promised lot. The court thus substituted expectation relief in monetary form for expectation relief in specie (in its own form, rather than its equivalent). In other words, the *measure* of the relief was determined by the value of the interest that Robert expected to receive, but the *form* of the remedy was compensation, rather than the land itself.

Sidhu v Van Dyke

[9.132] The High Court again considered the remedial effect of equitable estoppel in *Sidhu v Van Dyke*.[183] A married couple (the Sidhus) owned a rural property and lived in the main homestead. They let a cottage on the property to Mrs Sidhu's brother (Svenson) and his wife (Van Dyke), where Svenson and Van Dyke lived with their newborn son. Mr Sidhu and Van Dyke later embarked on a sexual relationship, in the course of which Sidhu promised Van Dyke that he would subdivide the property and transfer the cottage to her so that she would have somewhere to raise her son. When Van Dyke and Svenson separated, Sidhu told Van Dyke that she did not need a property settlement from Svenson because she had the cottage. Van Dyke did not seek a property settlement. She also spent time and effort maintaining and improving the cottage and the Sidhus' land and refrained from seeking full-time employment for several years. Although approval for a subdivision was granted by the local council, the land was not subdivided and the cottage was later destroyed in a fire. The relationship between Sidhu and Van Dyke broke down, and Mr and Mrs Sidhu

182 *Giumelli v Giumelli* [1999] HCA 10; (1999) 196 CLR 101, 123–4, quoting Deane J in (1990) 170 CLR 394, 442–3.

183 *Sidhu v Van Dyke* [2014] HCA 19; (2014) 251 CLR 505.

refused to convey any land to Van Dyke. Van Dyke sought relief on the basis of equitable or proprietary estoppel.

The crucial questions were whether Van Dyke had detrimentally relied on Sidhu's promises and, if she had, what was the appropriate quantum of relief. The Court of Appeal held that inducement could be inferred from the circumstances, so the burden of proof shifted to the defendant to show that the defendant did not rely on the promises. The High Court held that this was incorrect. The burden of proof at all times remains on the person claiming the benefit of an estoppel. "Reliance is a fact to be found; it is not to be imputed on the basis of evidence which falls short of proof of the fact".[184] Here, Van Dyke had "made out a compelling case of detrimental reliance": she gave evidence that she had relied on the Sidhu's promises and those promises "were objectively likely to have a significant effect upon the decision-making of a person in the respondent's position".[185] For Van Dyke to discharge her onus, it was not necessary that Sidhu's conduct was the sole inducement for her to take the detrimental action she took but was enough that it "played a part".[186] The High Court upheld the award of compensation based on the value of the promised land. It was said that the detriment here "involves life changing decisions with irreversible consequences…beyond the measure of money" and so, "as in *Giumelli v Giumelli*, justice between the parties will not be done by a remedy the value of which falls short of holding the appellant to his promises".[187]

Pipikos v Trayans

[9.133] The most recent statements from the High Court on the remedial effect of equitable estoppel were made in *Pipikos v Tryans*, a part performance case discussed at [7.70]. Kiefel CJ, Bell, Gageler and Keane JJ distinguished part performance from equitable estoppel on the basis that equitable estoppel is not concerned with the enforcement of promises, but the prevention of detriment resulting from reliance, and the remedy is moulded according to what is necessary to prevent that detriment.[188]

The current approach

[9.135] Since the *Giumelli v Giumelli*[189] decision, the approach to determining relief in equitable estoppel cases has become reasonably well settled and consistent.[190] The starting point in giving effect to an equity raised by estoppel is that the relying party has a prima facie entitlement to have the relied-upon assumption made good.[191] This is not always expressed in terms of a prima facie entitlement, but the courts almost invariably start from a position

184 *Sidhu v Van Dyke* [2014] HCA 19; (2014) 251 CLR 505, [58].

185 *Sidhu v Van Dyke* [2014] HCA 19; (2014) 251 CLR 505, [67]–[68].

186 *Sidhu v Van Dyke* [2014] HCA 19; (2014) 251 CLR 505, [71].

187 *Sidhu v Van Dyke* [2014] HCA 19; (2014) 251 CLR 505, [84]–[85], quoting *Donis v Donis* [2007] VSCA 89; (2007) 19 VR 577, 588–9.

188 *Pipikos v Trayans* [2018] HCA 39, [58]–[61].

189 *Giumelli v Giumelli* [1999] HCA 10; (1999) 196 CLR 101.

190 The discussion in this section draws heavily on Robertson, "The Reliance Basis of Proprietary Estoppel Remedies" (2008) 72 *Conveyancer and Property Lawyer* 295, esp at 297.

191 The Victorian Court of Appeal has expressed the view that this prima facie entitlement operates only in proprietary estoppel cases, which require a different approach from promissory estoppel cases: *Fifteenth Eestin Nominees Pty Ltd v Rosenberg* [2009] VSCA 112; (2009) 24 VR 155, [271], although this seems to be inconsistent with what was said in *Anaconda Nickel Ltd v Edensor Nominees Pty Ltd* [2004] VSCA 167, [44] (Buchanan JA; Eames JA and Coldrey AJA agreeing).

that the relevant representation should be adhered to or the promise fulfilled. There are two different reasons why that prima facie entitlement might give way to some other form or measure of relief.

The first consideration is pragmatic: it may be impossible, impractical or inappropriate in the circumstances to fulfil the relying party's expectations. That may be because the claimant's expectations are indefinite, the assumption related to property which the inducing party has since disposed of, a clean break between the parties is required or enforcement of the assumption would cause hardship to a third party. In *Giumelli v Giumelli*, for example, it was not appropriate to require the parents to give Robert the interest in land he expected to receive because Robert's brother, Stephen, had improved the property and now lived there with his family.

The second consideration is one of principle or justice between the parties: this is the minimum equity principle or proportionality requirement. Where the value of the expected benefit is disproportionate to the harm that has been or would be suffered by the claimant as a result of his or her reliance on the relevant assumption, then it is said that fulfilment of the claimant's expectations would be "inequitably harsh" or "unjust to the estopped party" or "would exceed what could be justified by the requirements of conscientious conduct".[192] In these circumstances, the court must grant the relief that is the minimum necessary to ensure that the relying party suffers no harm as a result of his or her reliance.

In *Delaforce v Simpson-Cook*, Handley AJA (with whom Allsop P and Giles JA agreed) suggested that, since *Giumelli*, the minimum equity principle "is probably no longer the law in this country".[193] Handley AJA did acknowledge, however, that the remedy must not be disproportionate to the detriment, and the approach adopted by Handley AJA in that case is consistent with that described in this section. The Victorian Court of Appeal has interpreted the effect of *Giumelli* as follows:

> It is true that in *Giumelli v Giumelli*,[194] Gleeson CJ and McHugh, Gummow and Callinan JJ said that *Verwayen* did not foreclose as a matter of doctrine relief making good the assumption in an appropriate case. But nothing which their Honours said in *Giumelli* suggests that there was any change from the view expressed in *Verwayen* that the doctrine of equitable estoppel enables a court to do what is required to avoid detriment to the party who has been induced to act upon an assumed state of affairs, and thus that that the relief required in a given case may be less than making good the assumption.[195]

Although the minimum equity principle or proportionality requirement is explicitly considered by judges in most cases in which an equitable estoppel is established,[196] in the great majority of cases the effect of the estoppel is that the inducing party is required to make good the assumption that has been relied upon. The reason for this is that it is usually not possible to

192 *Commonwealth v Verwayen* (1990) 170 CLR 394, 443 and 445–6 (Deane J), adopted in *Giumelli v Giumelli* [1999] HCA 10; (1999) 196 CLR 101, 123–4 (Gleeson CJ, McHugh, Gummow and Callinan JJ).

193 *Delaforce v Simpson-Cook* [2010] NSWCA 84; (2010) 78 NSWLR 483, [59]. See also *Hobsons Bay City Council v Gibbon* [2011] VSC 140; (2011) 32 VR 168.

194 *Giumelli v Giumelli* [1999] HCA 10; (1999) 196 CLR 101, 125 [50].

195 *ACN 074 971 109 (as trustee for the Argot Unit Trust) v The National Mutual Life Association of Australasia Limited* [2008] VSCA 247, (2008) 21 VR 351, [169].

196 See Robertson, "The Reliance Basis of Proprietary Estoppel Remedies" (2008) 72 *Conveyancer and Property Lawyer* 295, 298, fn 14 and accompanying text.

quantify the detriment with any precision.[197] Where the detriment cannot be quantified, the only way to ensure that the relying party does not suffer loss as a result of his or her reliance is by requiring the inducing party to perform the promise or adhere to the representation. As McHugh J said in *Commonwealth v Verwayen*: "Often the only way to prevent the promisee suffering detriment will be to enforce the promise".[198] In some cases, for example, the detriment results from the performance of unpaid domestic services (such as caring for an elderly relative) in the expectation of receiving an interest in land. Although there was one prominent case in which the relying party was compensated for the services at the market rate,[199] the courts are usually unwilling to place a financial value on the relying party's labour and lost opportunities.[200] In *Donis v Donis*,[201] the detrimental reliance included "life changing decisions of a personal nature", namely marrying, having children and abandoning a teaching career in the expectation of receiving an interest in land. Nettle JA held that the detriment was "beyond the measure of money" and could "only be accounted for by substantial fulfilment of the assumption on which the [relying party's] actions were based".[202] In commercial cases, the detriment commonly consists of the loss of a commercial opportunity which cannot be quantified. In these cases, too, requiring the inducing party to make good the assumption is often the only way to satisfy the equity.[203]

The minimum equity principle plays an important role in at least three situations. First, where the detriment can accurately be quantified and is clearly disproportionate to the value of the expected benefit, a compensatory remedy will be granted.[204] In *ACN 074 971 109 Pty Ltd (as Trustee for the Argot Unit Trust) v The National Mutual Life Association of Australasia* (*Argot Unit Trust*) case, investors were promised that they would be able to switch between two different kinds of investment portfolios in a way that would have allowed them to earn arbitrage profits of $1.44 billion over the life of the investments.[205] When the inducing party resiled from the promise, it was required to pay compensation of $37 million for the investors' reliance losses, which consisted of the cost of borrowing, management fees and alternative investment opportunities foregone. The award was upheld on appeal. The Court of Appeal confirmed that relief should be "no more than was necessary to avoid detriment" and held that the requirements of good conscience did not require the inducing party to adhere to

197 Robertson, "The Reliance Basis of Proprietary Estoppel Remedies" (2008) 72 *Conveyancer and Property Lawyer* 295; Robertson, "Satisfying the Minimum Equity: Equitable Estoppel Remedies after Verwayen" (1996) 20 *Melbourne University Law Review* 805; Robertson, "Reliance and Expectation in Estoppel Remedies" (1998) 18 *Legal Studies* 360.

198 *Commonwealth v Verwayen* (1990) 170 CLR 394.

199 *Public Trustee v Wadley* (1997) 7 Tas R 35.

200 See, eg, *Jennings v Rice* [2002] EWCA 159 and the discussion in Robertson, "The Reliance Basis of Proprietary Estoppel Remedies" (2008) 72 *Conveyancer and Property Lawyer* 295, 305–9.

201 *Donis v Donis* [2007] VSCA 89; (2007) 19 VR 577, [34].

202 *Donis v Donis* [2007] VSCA 89; (2007) 19 VR 577, [34].

203 See, eg, *Anaconda Nickel Ltd v Edensor Nominees Pty Ltd* [2004] VSCA 167, discussed at [9.195].

204 For an example of this, see *Repatriation Commission v Tsourounakis* [2007] FCAFC 29; (2007) 158 FCR 214, discussed in Robertson, "The Reliance Basis of Proprietary Estoppel Remedies" (2008) 72 *Conveyancer and Property Lawyer* 295, 310–2. See also *Pegela Pty Ltd v National Mutual Life Association of Australasia Ltd* [2006] VSC 507, [952] and *Petronijevic v Milojkovic* [2014] NSWSC 1337.

205 *ACN 074 971 109 Pty Ltd (as Trustee for the Argot Unit Trust) v The National Mutual Life Association of Australasia* [2008] VSCA 247; (2008) 21 VR 351.

the promise or pay compensation for the expectation loss of $1.44 billion.[206] Another example is *Young v Lalic*,[207] where the relying party contributed $50,000 towards the construction of a house on land owned by her prospective mother-in-law in the expectation of an interest in land worth some $400,000. The marriage foundered after a short time and the detriment consisted solely of the financial contribution. Brereton J held that it would be disproportionate to grant the relying party the expected interest in the property and her equity was satisfied by a charge for the amount of her contribution, plus interest.[208]

Secondly, even where the detriment resulting from reliance cannot be quantified, the court may decide that it is disproportionate to the expected benefit. In *Jennings v Rice*,[209] the relying party worked unremunerated for some years nursing the elderly inducing party in the expectation of receiving property worth over £400,000. The proportionality principle required that he be awarded compensation in the sum of £200,000. In cases such as this, it is necessary to take a "broad brush" approach to the determination of the remedy that is necessary to satisfy the equity.[210] The minimum equity principle also comes into play when harm can be prevented by some other means. In *Sullivan v Sullivan*,[211] the relying party had given up subsidised public accommodation for which she waited seven years on the faith of her brother and sister-in-law's promise of a home for life.[212] The effect of the estoppel was to allow the claimant to remain in the promised house for a further seven years in order to give her an opportunity to return to public housing. The inducing party's right to possession of the property was effectively suspended for that period in order to allow the relying party an opportunity to resume her original position.

A UNIFIED ESTOPPEL

[9.145] There have been attempts by members of the High Court to rationalise this area of the law by unifying the common law and equitable doctrines of estoppel by conduct. Deane J in *Waltons Stores v Maher*,[213] *Foran v Wight*[214] and *Commonwealth v Verwayen*,[215] and Mason CJ in *Commonwealth v Verwayen*,[216] recognised and applied unified principles of estoppel by conduct operating both at common law and in equity. Although Mason CJ and Deane J both recognised the unification of common law and equitable principles of estoppel by conduct, the unified principles they applied were different. The unified doctrine recognised by Deane J was based on common law estoppel and essentially extended the application of

206 *ACN 074 971 109 (as trustee for the Argot Unit Trust) v The National Mutual Life Association of Australasia Limited* [2008] VSCA 247; (2008) 21 VR 351, [169].

207 *Young v Lalic* [2006] NSWSC 18.

208 See also *Powell v Benney* [2007] EWCA Civ 1283 (compensation of £20,000 awarded to claimants who incurred minor expenditure in the expectation of receiving properties worth £280,000) and *McGuane v Welch* [2008] EWCA Civ 785.

209 *Jennings v Rice* [2002] EWCA 159.

210 A "broad brush … assessment" was also upheld by the Victorian Court of Appeal in *Donis v Donis* [2007] VSCA 89; (2007) 19 VR 577, [24].

211 *Sullivan v Sullivan* [2006] NSWCA 312.

212 *Sullivan v Sullivan* [2006] NSWCA 312.

213 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 451.

214 *Foran v Wight* (1989) 168 CLR 385, 435.

215 *Commonwealth v Verwayen* (1990) 170 CLR 394, 440.

216 *Commonwealth v Verwayen* (1990) 170 CLR 394, 413.

common law estoppel to assumptions relating to the future conduct of the inducing party. That doctrine would provide a prima facie right to relief based on the assumed state of affairs, which would be qualified where such a remedy would be unjust to the inducing party.[217] The unified doctrine recognised by Mason CJ, on the other hand, was based on the modern doctrine of equitable estoppel and essentially involved the extension of that doctrine to assumptions of existing fact. The doctrine proposed by Mason CJ would raise an equity in favour of the relying party, which would be satisfied by doing no more than is necessary to prevent detriment resulting from the relying party's reliance.[218]

The view that the doctrines of estoppel by conduct should be treated as unified in any form has not been accepted by a majority of the High Court. Three members of the High Court in *Commonwealth v Verwayen* proceeded on the basis that common law and equitable estoppel remained separate doctrines,[219] while, at most, three members of the court accepted the unification of those doctrines.[220] Accordingly, it is well accepted that the common law and equitable doctrines of estoppel by conduct remain separate doctrines.[221] If the status quo is to be challenged – which presently seems unlikely – the challenge may come from an estoppel by representation of fact case involving a significant disproportion between the relying party's reliance loss and expectation loss.[222]

THE CURRENT STATE OF PROMISSORY ESTOPPEL

[9.150] As noted above, there is a significant difference of opinion as to the current state of promissory estoppel and equitable estoppel in Australian law. The disagreement essentially relates to the effect of the High Court's decision in *Waltons Stores v Maher* on Australian law. Three different views have emerged: first, that promissory estoppel remains a purely defensive doctrine (as it does in English law); secondly, that promissory estoppel can arise from a promise to enter into a legal relationship and, thirdly, that promissory estoppel can arise from a promise to confer a benefit of any kind on the relying party and operates as an independent source of rights or a cause of action.

Promissory estoppel as a restraint on rights

[9.155] In English law, promissory estoppel remains the essentially defensive doctrine described by Denning J in the *High Trees* case.[223] It does not provide a cause of action where the inducing party promises to confer a benefit on the relying party, such as a promise to pay money or provide financial support, and the relying party acts to her detriment on the faith

217 *Commonwealth v Verwayen* (1990) 170 CLR 394, 445–6.

218 *Commonwealth v Verwayen* (1990) 170 CLR 394, 415–17.

219 *Commonwealth v Verwayen* (1990) 170 CLR 394, 428–9, 453–4, 500–1.

220 *Commonwealth v Verwayen* (1990) 170 CLR 394, 413, 487.

221 See, eg, *MK & JA Roche Pty Ltd v Metro Edgley Pty Ltd* [2005] NSWCA 39, [71].

222 As to whether unification is appropriate or desirable, compare Bryan, "Unifying Estoppel Doctrine: The Argument for Heresy" (2013) 7 *Journal of Equity* 209 and Bant and Bryan, "Fact, Future and Fiction: Risk and Reasonable Reliance in Estoppel" (2015) 35 *Oxford Journal of Legal Studies* 427, with Hudson, "The True Purpose of Estoppel by Representation" (2015) 32 *Journal of Contract Law* 275 and Hudson, "The Price of Coherence in Estoppels" (2017) 39 *Sydney Law Review* 1.

223 See [9.35].

of that promise.[224] In a series of cases, the New South Wales Court of Appeal has taken the view that, despite *Waltons Stores v Maher*, Australian law is essentially the same as English law on this point. The court has maintained that promissory and proprietary estoppel remain entirely separate principles, that promissory estoppel is negative in substance and it can only operate to prevent a person from enforcing a legal or equitable right. On this view, proprietary estoppel provides a cause of action but promissory estoppel does not: the latter can only arise from a promise not to enforce a right. This understanding of promissory estoppel in contemporary Australian law was first outlined by KR Handley in his 2006 book *Estoppel by Conduct and Election*.[225] It was then applied by Handley AJA in *Saleh v Romanous*,[226] where the restrictive nature of the principle was directly relevant to the decision. That view of the law has been reiterated in subsequent decisions.[227] More recently, Bathurst JA observed that:

> These decisions are to the effect that a promissory estoppel only operates as a restraint on the enforcement of rights and, unlike a proprietary estoppel, must be negative in substance; that is, it will only apply to assumptions or expectations that existing or future rights will be suspended or extinguished rather than created.[228]

The idea that promissory estoppel can only operate defensively as a restraint on rights in Australian law would seem to be plainly inconsistent with *Waltons Stores v Maher*. In that case, a majority of the High Court held that a promissory or equitable estoppel arose from the Mahers' reliance on an assumption induced by Waltons that it would sign and exchange a lease on terms that had been negotiated. The binding authority of *Waltons Stores v Maher* as a promissory estoppel case could be avoided if it could be understood as a decision on proprietary estoppel, with the unusual feature of the case being that the estoppel was asserted by the land owner against a person who had promised to take an interest in the land by way of lease.[229] This explanation is, however, very difficult to reconcile with the judgments of Brennan J and Mason CJ and Wilson J in that case.[230]

The restraint on rights view of promissory estoppel has been described by one judge as controversial.[231] A Master of the Supreme Court of Western Australia considered it "doubtful" and refused to strike out a statement of claim which attempted to set up positive rights.[232] The New South Wales Court of Appeal discussed the issue at length in *Ashton v Pratt* but did not need to resolve it in order to decide that case. Bathurst JA (with whom McColl and Meagher JJA agreed) noted that "there is significant dicta contrary to this limitation on promissory estoppel".[233] He also noted, however, that in two recent cases, the House

224 *Combe v Combe* [1951] 2 KB 215.

225 Now in its second edition: Handley, *Estoppel by Conduct and Election* (2nd ed, 2016).

226 *Saleh v Romanous* [2010] NSWCA 274; (2010) 79 NSWLR 453 (Giles JA and Sackville AJA agreed with Handley AJA).

227 *DHJPM Pty Ltd v Blackthorn Resources Ltd* [2011] NSWCA 348; (2011) 83 NSWLR 728, [93]–[94]; *Hammond v JP Morgan Trust Australia Ltd* [2012] NSWCA 295, [26].

228 *Ashton v Pratt* [2015] NSWCA 12; (2015) 88 NSWLR 281, [102].

229 Handley, *Estoppel by Conduct and Election* (2nd ed, 2016), [11-032]. See also *DHJPM Pty Ltd v Blackthorn Resources Ltd* [2011] NSWCA 348; (2011) 83 NSWLR 728, [122].

230 See Robertson, "Three Models of Promissory Estoppel" (2013) 7 *Journal of Equity* 226, 231–3.

231 *Construction Technologies Australia Pty Ltd v Doueihi* [2014] NSWSC 1717, [130] (White J).

232 *Character Design Pty Ltd v Kohlen* [2013] WASC 112, [16] (Sanderson M).

233 *Ashton v Pratt* [2015] NSWCA 12; (2015) 88 NSWLR 281, [138].

of Lords had maintained a distinction between promissory and proprietary estoppel "in a manner which appears consistent with statements in this court in *Saleh* and *DHJPM*".[234] This contrasts with the widely held view that Australian law has deviated significantly from English law in this area.[235]

The idea that promissory estoppel can only operate defensively as a restraint on rights is clearly inconsistent with the outcomes of a number of cases discussed in this chapter and the reasoning in many more. Since *Waltons Stores v Maher*, the Full Court and Court of Appeal of the Supreme Court of Victoria have, in numerous cases, applied a broad doctrine of equitable estoppel which can operate positively and create new rights to which the court must give effect through the granting of discretionary relief "moulded to meet the justice of the case".[236] In the *Argot Unit Trust* case, for example, an equitable estoppel arose where investors were induced to assume that they would be allowed to switch between two different kinds of investment in a way that would allow them to make arbitrage profits. When the inducing party sought to act inconsistently with that assumption, an equitable estoppel arose and justified an award of compensation for the investors' reliance losses. Unfortunately, none of the inconsistent Victorian cases, nor any of the inconsistent judgments of the Supreme Court of New South Wales,[237] have been cited by the New South Wales Court of Appeal in its discussions of the restraint on rights limitation.

The legal relationship model of promissory estoppel

[9.160] A second view of promissory estoppel is that it is not merely a defensive doctrine but can be used where a person leads another to assume that a particular legal relationship exists or will exist between them. This view finds support in the first of the elements that Brennan J said in *Waltons Stores v Maher* must be established to make out an equitable estoppel. On this view, promissory estoppel does not provide a cause of action or independent source of rights but may provide the foundation of a cause of action if A has promised to enter into a legal relationship with B in which B would have an cause of action against A under "ordinary principles".[238] This view is consistent with the outcome of *Waltons Stores v Maher* itself (where the relying party was, in effect, able to enforce the unsigned contract). As discussed above, however, there have been numerous cases in which promissory or equitable estoppel has arisen from an assumption that does not involve a particular legal relationship.[239] In those cases, promissory estoppel has operated as a cause of action in its own right.

234 *Ashton v Pratt* [2015] NSWCA 12; (2015) 88 NSWLR 281, [137], citing *Cobbe v Yeoman's Row Management Ltd* [2008] UKHL 55; [2008] 1 WLR 1752; *Thorner v Major* [2009] UKHL 18; [2009] 1 WLR 776.

235 See, eg Peel, *Treitel's Law of Contract* (14th ed, 2015), [3-093].

236 *Anaconda Nickel Ltd v Edensor Nominees Pty Ltd* [2004] VSCA 16, [44]. See also *Metropolitan Transit Authority v Waverley Transit Pty Ltd* [1991] 1 VR 181; *Commonwealth v Clark* [1994] 2 VR 333; *Fifteenth Eestin Nominees Pty Ltd v Rosenberg* [2009] VSCA 112; (2009) 24 VR 155.

237 For example, *W v G* (1996) 20 Fam LR 49; *Lee Gleeson Pty Ltd v Sterling Estates Pty Ltd* (1991) 23 NSWLR 571; *Chanrich Properties Pty Ltd v Baulkham Hills Shire Council* [2001] NSWSC 229; *EK Nominees Pty Ltd v Woolworths Ltd* [2006] NSWSC 1172.

238 *Commonwealth v Verwayen* (1990) 170 CLR 394, 445 (Deane J). See also, eg, *CPB Contractors Pty Ltd v Rizzani De Eccher Australia Pty Ltd* [2017] NSWSC 1798, [341].

239 Above [9.50] and *Arfaras v Vosnakis* [2016] NSWCA 65, discussed at [9.70].

Promissory estoppel as an independent source of rights

[9.165] A third view of promissory estoppel is that it can potentially arise from a promise to confer a benefit of any kind, including, for example, a promise to pay money to another. On this view, promissory estoppel operates as a cause of action or independent source of liability to which the court gives effect by way of relief "moulded to meet the justice of the case".[240] There is no doubt that proprietary or equitable estoppel will provide a cause of action where a person relies on an assumption that the inducing party will transfer or grant an interest in land to the relying party.[241] If promissory estoppel can provide a cause of action when a person relies on a promise of a benefit of some other kind, and generates a remedy which is shaped by the same considerations as proprietary estoppel, then there is no substantial distinction between promissory and proprietary estoppel. Rather, there is a unified and substantive doctrine of equitable estoppel, the scope of application of which is not limited to any particular types of fact situations. The widespread use of the label "equitable estoppel" in the Australian case law since *Waltons Stores v Maher* reflects the widespread acceptance of the existence of a unified equitable doctrine.

Since the decisions of the High Court in *Waltons Stores v Maher*[242] and *Commonwealth v Verwayen* identified the unity of principle between proprietary and promissory estoppel, it is difficult to argue that one should provide a cause of action, while the other should not. Brennan J recognised this in *Waltons Stores v Maher*, when he said that:

> Unless the cases of proprietary estoppel are attributed to a different equity from that which explains the cases of promissory estoppel, the enforcement of promises to create new proprietary rights cannot be reconciled with a limitation on the enforcement of other promises … It does not accord with principle to hold that equity, in seeking to avoid detriment occasioned by unconscionable conduct, can give relief in some cases but not in others.[243]

Subsequent cases show that equitable estoppel is being accepted as a cause of action in cases outside the proprietary estoppel context. A clear example is the case of *W v G*,[244] which was discussed earlier in the chapter.[245] The decision of Hodgson J in that case can only be supported on the basis that equitable estoppel provides a cause of action in non-proprietary contexts. The estoppel upheld by Hodgson J resulted in the enforcement of the defendant's promise to assist the plaintiff in raising the children and cannot be seen as supporting any other cause of action. Another example is *Yarrabee Chicken Company Pty Ltd v Steggles Ltd*.[246] Steggles, a chicken processing company, contracted with growers to rear chickens on its behalf in return for a fee. The arrangement was that Steggles would deliver batches of chicks

240 *Anaconda Nickel Ltd v Edensor Nominees Pty Ltd* [2004] VSCA 167; (2004) 50 ACSR 679, [44]. A strong example of a remedy moulded to meet the justice of the case is the *Argot Unit Trust* case, discussed at [9.135].

241 *Giumelli v Giumelli* [1999] HCA 10; (1999) 196 CLR 101; *Sidhu v Van Dyke* [2014] HCA 19; (2014) 251 CLR 505.

242 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387.

243 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 426. See also McFarlane and Sales, "Promises, Detriment and Liability: Lessons from Proprietary Estoppel" (2015) 131 *Law Quarterly Review* 610, 621–5.

244 *W v G* (1996) 20 Fam LR 49.

245 See [9.50]. See also *Lee Gleeson Pty Ltd v Sterling Estates Pty Ltd* (1991) 23 NSWLR 571; *News Corporation Ltd v Lenfest Communications Inc* (1996) 21 ASCR 553; *Chanrich Properties Pty Ltd v Baulkham Hills Shire Council* [2001] NSWSC 229; *Gray v National Crime Authority* [2003] NSWSC 111, esp at [251], discussed at [9.70].

246 *Yarrabee Chicken Company Pty Ltd v Steggles Ltd* [2010] FCA 394.

to growers who would rear them under agreed conditions so that they could be collected by Steggles approximately 45 days later for processing. Steggles entered into standard form contracts with growers which required Steggles to deliver batches of chicks to growers but did not specify a minimum number of batches of chicks per year or a minimum density of birds per square metre of shed space. In order to induce two growers to increase their rearing capacity by building more "tunnel ventilated sheds", Steggles promised each of them that it would supply them with six batches of chicks per year for the duration of the contract at a stocking density of 19.5 birds per square metre. In reliance on those promises and with Steggles' encouragement, the growers borrowed substantial sums of money and built new tunnel ventilated sheds. Steggles then failed to supply the promised number of batches at the promised stocking density. Jagot J held that equitable estoppel "is enforceable as a cause of action in its own right" and did so in this case.[247] The only way to ensure that the growers did not suffer detriment as a result of their reliance was to hold Steggles to its promises by way of "a declaration and, if necessary, an order requiring Steggles to supply birds" as promised for the duration of the contract.[248] The estoppel did not have the effect of varying the terms of the contract but provided an independently enforceable right to the promised supply of birds.

ESTOPPEL AND CONTRACT

[9.170] The principle of equitable estoppel is not seen by the courts as a contractual form of obligation.[249] In the development of equitable estoppel, the High Court of Australia has been careful to ensure that the recognition of a substantive doctrine of equitable estoppel does not upset the balance and structure of the law of obligations by undermining the law of contract. In *Giumelli v Giumelli*,[250] the appellants argued that it was important to limit the remedy provided by equitable estoppel in order to ensure that the doctrine did not undermine the doctrine of consideration by directly enforcing non-contractual promises. The High Court rejected this argument, adopting three explanations given in previous cases as to why, even without a strict reliance-based approach to relief, equitable estoppel does not undermine the law of contract. First, the fact that the court exercises discretion in the granting of relief allays any fear that the doctrine of consideration is being undermined.[251] While establishing a breach of contract gives the plaintiff a legal entitlement to compensatory damages, establishing an equitable estoppel simply raises an equity in favour of the relying party. The court exercises a broad discretion in fashioning relief to give effect to that equity. Secondly, while the obligation in contract derives from the promise, it is the expectation generated by the promise that attracts the operation of estoppel.[252] In other words, equitable estoppel is concerned with the assumption adopted by the relying party, rather than the promise made by the inducing party. Thirdly, the obligation in estoppel cases does not arise from the existence of an unperformed

247 *Yarrabee Chicken Company Pty Ltd v Steggles Ltd* [2010] FCA 394, [135].

248 *Yarrabee Chicken Company Pty Ltd v Steggles Ltd* [2010] FCA 394, [170].

249 See, eg, *Pipikos v Trayans* [2018] HCA 39, [58]–[65].

250 *Giumelli v Giumelli* [1999] HCA 10; (1999) 196 CLR 101, 120.

251 *Giumelli v Giumelli* [1999] HCA 10; (1999) 196 CLR 101, 121, quoting *Commonwealth v Verwayen* (1990) 170 CLR 394, 454.

252 *Giumelli v Giumelli* [1999] HCA 10; (1999) 196 CLR 101, 121, quoting *Riches v Hogben* [1985] 2 Qd R 292, 301.

promise but from the conduct of the relying party in acting upon the expectation. It is the relying party's detrimental reliance that is fundamental to establishing an estoppel.

The High Court therefore sees equitable estoppel as a form of obligation which exists alongside contract but which is distinguishable from contract in the determination of questions of liability and remedy. Because equitable estoppel, like contract, can arise from a promise, it is very often pleaded as an alternative to contract. Both common law and equitable principles of estoppel play an important role in the law of contract, and it is very important to be aware of the principal points at which they intersect with contract law.

Formation

[9.175] The principles of estoppel can play a role in negotiations to enter into a contract. An equitable estoppel may arise if an offeror leads the offeree to believe that the offer will not be revoked and the offeree acts to his or her detriment in reliance on that assumption.[253] A similar principle is recognised in both the *United Nations Convention on International Contracts for the Sale of Goods* (Vienna Convention) and the *UNIDROIT Principles of International Commercial Contracts 2016* (UPICC).[254] Article 16(2) of the Vienna Convention and art 2.1.4(2) of the UPICC provide that an offer cannot be revoked if it was reasonable for the offeree to rely on the offer as being irrevocable and the offeree has acted in reliance on the offer. Under Australian law, an equitable estoppel will not necessarily make the offer irrevocable; it will raise an equity against the offeror which may be satisfied by the granting of some other relief.[255]

Waltons Stores v Maher[256] established that where a relying party acts on the assumption that a contract *has* been signed, estoppel by representation may prevent the inducing party from denying that a contract exists. Where a relying party acts on the assumption that a contract *will* be signed, the relying party may be able to obtain relief by way of equitable estoppel. Again, the effect of the estoppel will be to raise an equity in favour of the relying party and the court may give effect to the equity by enforcing the anticipated contract.

Although it is clearly possible to establish an estoppel in the context of pre-contractual negotiations, the cases since *Waltons Stores v Maher* have shown that it is very difficult to do so. There are two reasons for this. First, in most cases, parties negotiating to enter into a contract should reasonably expect that they cannot safely rely on the transaction proceeding until a contract has been formally concluded.[257] Thus, it is extremely difficult to establish an estoppel in the course of negotiations that are expressly made "subject to contract".[258] The second reason is that the courts are reluctant to find an estoppel arising unless all the terms of the contract have been settled.[259] The circumstances in *Waltons Stores v Maher* were unusual because the terms of the contract had been settled, immediate commencement of the

253 See *Mobil Oil Australia Ltd v Wellcome International Pty Ltd* (1998) 81 FCR 475, discussed at [3.70] and [9.50].

254 See [1.180].

255 See [9.110].

256 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387.

257 See *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 405–6.

258 Cf *Attorney-General of Hong Kong v Humphreys Estate (Queen's Gardens) Ltd* [1987] AC 114 with *EK Nominees Pty Ltd v Woolworths Ltd* [2006] NSWSC 1172, discussed later in this section and at [33.60]. See also *Yeoman's Row Management Ltd v Cobbe* [2008] UKHL 55; [2008] 1 WLR 1752 (estoppel claim unsuccessful where claimant relied on an incomplete preliminary agreement which was understood by the parties not to be binding).

259 See *Yeoman's Row Management Ltd v Cobbe* [2008] UKHL 55; [2008] 1 WLR 1752.

building works was required and Waltons knew the Mahers were acting on the assumption that Waltons had executed or would execute the contract.

The facts of *Waltons Stores v Maher* can be contrasted with those of *Austotel Pty Ltd v Franklins Selfserve Pty Ltd*.[260] Austotel was negotiating to lease premises to Franklins for use as a supermarket. Franklins had issued a letter setting out the terms on which it was prepared to lease the premises but had refused to finalise the terms of a lease on the basis that the finalisation of other leases was more urgent. The parties later agreed to a 9 per cent increase in the area to be let to Franklins but did not negotiate the additional rental to be paid for this area. In the meantime, the store was being built to Franklins' specifications, and Franklins incurred substantial liabilities to third parties in preparation for fitting out the store. Before the terms of the contract were finalised, Austotel sought to withdraw from the transaction. Franklins claimed Austotel was bound, either on the basis of contract or estoppel.

At first instance, Needham J found that no binding contract had been formed because the parties had failed to agree on the amount of rent to be paid or a mechanism for calculating the rental. He found that an estoppel arose against Austotel which entitled Franklins to a lease of the premises at a rental to be fixed by reference to expert valuation. The Court of Appeal, by a majority of 2-1, overturned that decision. Kirby P held that the parties' failure to agree on the rental to be paid stood in the way of an estoppel being established. The parties, who were substantial enterprises involved in a commercial transaction, failed to reach agreement on a crucial element of the transaction and were each deliberately refusing to commit themselves. In those circumstances, it was not unconscionable for one of the parties to withdraw from the transaction. Rogers A-JA noted evidence that Franklins was deliberately refraining from discussing the question of rent in the hope of obtaining the extra area without paying any additional rent. It would, he said, be inappropriate for the court to complete the agreement by settling a term that at least one party had deliberately left open.

Where negotiating parties have reached a preliminary "in-principle" agreement, an important question is whether an estoppel can be established on the basis of an assumption that the other party *will* proceed with the transaction or whether it is necessary to assume that the other party is *legally bound* to proceed.[261] In *EK Nominees Pty Ltd v Woolworths Ltd* (*EK Nominees*),[262] White J held that it was unconscionable for Woolworths not to proceed with an agreement for lease, even though EK Nominees did not believe that Woolworths was bound to enter into a lease and understood that they were free to withdraw.[263] With Woolworths' encouragement, EK Nominees had proceeded with costly preparatory work for a retail and residential development on the faith of an in-principle agreement that Woolworths would enter into a lease as the anchor tenant for the development. While work on the development proceeded, Woolworths entered into negotiations with the owner of a better site nearby and ultimately decided to lease premises at that site instead. It was unconscionable for Woolworths to withdraw from the agreement with EK Nominees because, among other things, Woolworths had not only encouraged EK Nominees to proceed with the development but had threatened

260 *Austotel Pty Ltd v Franklins Selfserve Pty Ltd* (1989) 16 NSWLR 582.

261 On this question, see also *Construction Technologies Australia Pty Ltd v Doueihi* [2014] NSWSC 1717, [132]–[229] (affirmed on appeal: *Doueihi v Construction Technologies Australia Pty Ltd* [2016] NSWCA 105; (2016) 92 NSWLR 247) and Silink, "Equitable Estoppel in 'Subject to Contract' Negotiations" (2011) 5 *Journal of Equity* 252.

262 *EK Nominees Pty Ltd v Woolworths Ltd* [2006] NSWSC 1172.

263 *EK Nominees Pty Ltd v Woolworths Ltd* [2006] NSWSC 1172. The facts are discussed in more detail at [33.60].

to hold EK Nominees responsible for Woolworths' costs and loss of profits if EK Nominees did not take all the necessary preliminary steps.[264] It could be said that Woolworths induced EK Nominees to act on the assumption that Woolworths would negotiate in good faith and will not withdraw from the negotiations for any reason other than a genuine failure to reach agreement on terms.[265]

On the question raised at the beginning of the previous paragraph, the opposite conclusion was reached by Lord Walker in *Yeoman's Row Management Ltd v Cobbe*.[266] In that case, a property developer undertook considerable effort and expense to obtain planning permission for a property on the faith of an oral agreement with the owner that he would buy the property at an agreed price if that permission was granted. Although the main commercial terms were agreed, the agreement was incomplete in significant respects and was understood to be binding in honour only. No estoppel arose, even though the land owner had encouraged the developer to undertake the work and had simply demanded a higher price when the planning permission had been granted. The House of Lords held that the developer had taken the risk that the necessary formal agreement might not be concluded.[267] In the *EK Nominees* case, on the other hand, White J held that, while EK Nominees had taken the risk that the parties might not reach agreement, it had not taken the risk of Woolworths abandoning the project for its own reasons.[268]

DHJPM Pty Ltd v Blackthorn Resources Ltd[269] supports the view that a party to negotiations must induce an assumption that it is irrevocably bound to proceed before an equitable estoppel can arise. DHJPM leased and fitted out office space with the intention that some of the space would be occupied by other companies, who would share a receptionist, boardroom and other facilities. AIM gave an express commitment to take a specified part of the space, and on the faith of that commitment, DHJPM entered into an agreement for the head lease and a contract to fit out the premises. Ensuing negotiations between the parties' solicitors revealed the lack of agreement between AIM and DHJPM on the essential terms of the transaction, including basic questions such as whether AIM was to be granted a sub-lease or a licence. AIM refused to proceed and DHJPM sought compensation by way of equitable estoppel. The primary judge held that AIM had induced in DHJPM an assumption that was capable of supporting an equitable estoppel, but no estoppel arose because, inter alia, it was not unreasonable for AIM to refuse to enter into an agreement on the terms proposed. The Court of Appeal upheld the conclusion that no estoppel arose but considered the assumption induced by AIM's conduct to be incapable of supporting an equitable estoppel. Meagher JA (with whom Macfarlan JA agreed) held that it was not enough that AIM had induced an assumption in DHJPM that the parties would negotiate in good faith or that a sublease would be entered into. An equitable estoppel could not arise because "AIM did not encourage an expectation that it had 'bound' itself irrevocably to enter into a sublease".[270]

264 *EK Nominees Pty Ltd v Woolworths Ltd* [2006] NSWSC 1172, [268].

265 See Robertson, "Three Models of Promissory Estoppel" (2013) 7 *Journal of Equity* 226, 243.

266 *Yeoman's Row Management Ltd v Cobbe* [2008] UKHL 55; [2008] 1 WLR 1752, [65]–[67].

267 Cobbe nevertheless succeeded on a restitutionary claim to recover his expenses and reasonable fee for his work: *Yeoman's Row Management Ltd v Cobbe* [2008] UKHL 55; [2008] 1 WLR 1752, [40]–[45].

268 *EK Nominees Pty Ltd v Woolworths Ltd* [2006] NSWSC 1172, [260]. See also the discussion of this issue in the restitution context, [10.50].

269 *DHJPM Pty Ltd v Blackthorn Resources Ltd* [2011] NSWCA 348; (2011) 83 NSWLR 728.

270 *DHJPM Pty Ltd v Blackthorn Resources Ltd* [2011] NSWCA 348; (2011) 83 NSWLR 728, [68].

Privity

[9.180] Another situation in which an estoppel can arise is where a contractual claim is barred by the privity rule, which is discussed in Chapter 11. A person who is not a party to a contract but who has been led to believe that they are a party or will receive a benefit under a contract may be able to establish an estoppel if they have acted to their detriment on the faith of the assumption.[271] It has also been held that an inducing party who is not a party to a contract will be liable where they have induced a relying party to act to their detriment on the faith of an assumption that the inducing party will abide by the terms of the contract.[272]

Formalities

[9.185] Equitable estoppel may also provide relief where a contract is unenforceable because it fails to comply with formal requirements laid down by statute, such as the requirement of writing for sale of land contracts.[273] Where a party has acted to his or her detriment on the faith of an expectation that a written contract will come into existence, that party may be able to obtain relief by way of equitable estoppel.[274] The statutory requirements of writing do not affect the operation of estoppel because the action is brought on the equity raised by the estoppel and not on the contract itself.[275]

In some circumstances, equitable estoppel may provide an alternative to the enforcement of the contract through the doctrine of part performance.[276] It has been held in some cases that detrimental reliance on the verbal contract itself will not be enough to establish an estoppel and "something more" is required to establish an estoppel, such as a promise to perform the oral contract or a promise not to rely on the statutory requirement of writing.[277] That view has been criticised.[278] There is support in the case law for a broader view, which is that an estoppel can arise from reliance on the assumptions induced by the making of the unenforceable oral agreement, without the need for "something more".[279]

Contract variations

[9.190] The principles of estoppel can operate where one party induces another to believe that a contract has been or will be varied or to believe that a term of the contract will not be enforced. Variations made before formation of the contract raise different issues from those made after formation.

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271 *Trident General Insurance Co Ltd v McNiece Bros Pty Ltd* (1988) 165 CLR 107, 140.

272 *Weir v Hoylevans Pty Ltd* [2001] WASCA 23.

273 See Chapter 7.

274 *Collin v Holden* [1989] VR 510.

275 *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 433.

276 See [7.65]–[7.85].

277 *Actionstrength Ltd v International Glass Engineering In GI En SpA* [2003] 2 AC 541; *Powercell Pty Ltd v Cuzeno Pty Ltd* [2004] NSWCA 51; *Tipperary Developments Pty Ltd v Western Australia* [2009] WASCA 126; (2009) 38 WAR 488, [21]–[24] (Wheeler JA). See also *Yeoman's Row Management Ltd v Cobbe* [2008] UKHL 55; [2008] 1 WLR 1752, [29].

278 Robertson, "The Statute of Frauds, Equitable Estoppel and the Need for 'Something More'" (2003) 19 *Journal of Contract Law* 173.

279 *Riches v Hogben* [1985] 2 Qd R 292; *Tipperary Developments Pty Ltd v Western Australia* [2009] WASCA 126; (2009) 38 WAR 488, [130]–[146] (McLure JA, with whom Newnes JA agreed).

Pre-contractual variations

[9.195] It occasionally happens that parties will enter into a written contract on the understanding that a particular term will be interpreted in a particular way or will not be strictly enforced. The party who stands to benefit from that variation will enter into the contract on the faith of that understanding and will suffer detriment if the other party is able to enforce the contract on its written terms.

A good example of the operation of promissory or equitable estoppel in this situation is provided by *Anaconda Nickel Ltd v Edensor Nominees Pty Ltd*.[280] The parties entered into a contract for the sale of shares in a mining company, Centaur. Clause 4.1(a) of the contract provided that completion was subjected to the buyer conducing a due diligence investigation of Centaur's assets and liabilities and being satisfied with the results of that investigation. On the day fixed for completion, the buyer requested a six-month extension but promised that the transaction would be completed. In a telephone conversation, the buyer's representative said: "I give you my word that I'm going to settle. I give you my word Joseph…I need a six-month extension…You can trust me. We've known each other for many years and I have never let you down". The parties signed a letter that confirmed the extension and certain other new terms but expressly provided that completion remained subject to cl 4.1(a) of the original agreement. On the faith of the buyer's promise to complete the purchase, the seller transferred board control of Centaur to the buyer. The seller also lost the opportunity to "preserve and exploit Centaur's nickel and gold prospects" and to deal with other potential buyers of the shares. Centaur's financial position deteriorated during the six-month period and the buyer refused to complete the purchase, relying on cl 4.1(a). A promissory estoppel arose because the buyer had induced the belief that it would not invoke its rights under cl 4.1(a) and the seller had acted to its detriment on that belief. Holding the buyer to its promise to complete the purchase was "the minimum equity to do justice to the plaintiff".[281]

Estoppel by convention

[9.200] The principle of estoppel by convention is sometimes relied upon in relation to pre-contractual variations. Estoppel by convention operates where parties to an agreement have adopted a particular state of affairs as the basis of their agreement or relations. The estoppel holds the parties to the agreed or assumed state of affairs for the purposes of the transaction or relationship in question. The estoppel may operate by virtue of an express term of a contract, where the parties have expressly agreed that they will take certain facts to be true or, more commonly, the parties may be precluded merely on the basis of a common assumption which has been adopted as to the basis of the contract.[282] Detrimental reliance by the person claiming the benefit of an estoppel by convention has not always been clearly identified in earlier cases, but it is now consistently held to be an essential element of establishing an estoppel by convention.[283] In *Con-Stan Industries Pty Ltd v Norwich Winterthur Insurance*

280 *Anaconda Nickel Ltd v Edensor Nominees Pty Ltd* [2004] VSCA 167.

281 *Anaconda Nickel Ltd v Edensor Nominees Pty Ltd* [2004] VSCA 167, [44], quoting *Crabb v Arun DC* [1976] Ch 179, 198.

282 Spencer, Bower and Turner, *The Law Relating to Estoppel by Representation* (3rd ed, 1977), pp 158–9.

283 *MK & JA Roche Pty Ltd v Metro Edgley Pty Ltd* [2005] NSWCA 39, [72]; *Ryledar Pty Ltd v Euphoric Pty Ltd* [2007] NSWCA 65; (2007) 69 NSWLR 603, [200]–[202]; *Shiu Shing Sze Tu v Lowe* [2014] NSWCA 462, [447].

(Australia) Ltd (*Con-Stan*) [284], the High Court held that an estoppel by convention must be based on an assumption of fact and could not arise from an assumption as to the legal effect of the parties' conduct. In that case, a company paid insurance premiums to their insurance broker, who went into insolvent liquidation without passing the premiums on to the insurer. The company claimed, against the insurer, an estoppel by convention to the effect that the broker alone would be liable to the insurer for the premiums. The High Court held that the claim failed: first, because the evidence did not establish any such convention and, secondly, because the assumption asserted was not an assumption of fact, but concerned the legal effect of the parties' conduct.[285] In *Eslea Holdings Ltd v Butts*, a majority of the New South Wales Court of Appeal held that, since the evidentiary basis of the estoppel was not made out in the *Con-Stan* case, the High Court's statement about the need for an assumption of fact was not an alternative ground for the decision but was instead an obiter dictum which was, in fact, inconsistent with the authorities cited.[286] It is now well accepted that an estoppel by convention can arise from an assumption as to the legal rights of the parties or the effect of a document.[287]

In *Whittet v State Bank of New South Wales*[288] estoppel by convention was held to operate in relation to a pre-contractual variation. Mrs Whittet gave a mortgage to the bank to secure repayment of her husband's business overdraft. The transaction was entered into on the assumption that the mortgage would secure repayment of $100,000 plus interest on that sum. Before the mortgage was signed, Mrs Whittet's solicitor received verbal assurances from the bank to that effect. The mortgage was in fact an "all moneys" mortgage, which was expressed to secure repayment of all of Mr Whittet's debts to the bank without any limit. Rolfe J held that an estoppel by convention arose which prevented the bank from recovering more than the amount which the parties understood to be secured by the mortgage. It is possible to construe the assumption adopted by Mrs Whittet as an assumption of fact (that the terms of the mortgage did in fact limit the amount secured), as an assumption as to the legal effect of the mortgage (that its legal effect was to secure only $100,000) or as an assumption as to the future conduct of the bank (that it would enforce the mortgage only to the extent of $100,000). It is therefore possible to justify the application of both estoppels by convention and equitable estoppel in such situations.

There is some controversy as to whether the parol evidence rule (discussed at [9.205]) prevents an estoppel by convention arising from pre-contractual negotiations which culminate in a written contract. In *Johnson Matthey Ltd v AC Rochester Overseas Corp*,[289] McLelland J held that it could not, but that view was rejected by Rolfe J in *Whittet v State Bank of New*

284 *Con-Stan Industries Pty Ltd v Norwich Winterthur Insurance (Australia) Ltd* (1986) 160 CLR 226, 244–5.

285 *Con-Stan Industries Pty Ltd v Norwich Winterthur Insurance (Australia) Ltd* (1986) 160 CLR 226, 244–5.

286 *Eslea Holdings Ltd v Butts* (1986) 6 NSWLR 175, 186. Cf Bennett, "Equitable Estoppels and Related Estoppels" (1987) 61 *Australian Law Journal* 540, 549–51 and Derham, "Estoppel by Convention – Part II" (1997) 71 *Australian Law Journal* 976, 982.

287 The authorities are collected in *Mineralogy Pty Ltd v Sino Iron Pty Ltd (No 6)* [2015] FCA 825, [759].

288 *Whittet v State Bank of New South Wales* (1991) 24 NSWLR 146.

289 *Johnson Matthey Ltd v AC Rochester Overseas Corp* (1990) 23 NSWLR 190, 195–6. See also *Skywest Aviation Pty Ltd v Commonwealth* (1995) 126 FLR 61, 104–5; *Australian Co-operative Foods v Norco* [1999] NSWSC 274; (1999) 46 NSWLR 267, 279. See also *State Rail Authority of New South Wales v Heath Outdoor Pty Ltd* (1986) 7 NSWLR 170, 195–6.

South Wales.[290] This question has been discussed in a number of cases since, but not resolved. The answer may depend on whether estoppel by convention operates at common law or in equity.[291] As a common law doctrine, the parol evidence rule is generally thought not to restrict the application of equitable principles.[292] Although estoppel by convention originated at common law, there are indications that it has "moved house" and now operates as an equitable principle.[293]

The parol evidence rule

[9.205] An important issue relating to pre-contractual variations is whether the parol evidence rule prevents an estoppel from being established. The parol evidence rule is a principle that operates where parties have signed a contractual document which appears to provide a complete record of their agreement. The rule prevents the admission or consideration of evidence that subtracts from, adds to, varies or contradicts the terms of the written document.[294] The scope of the parol evidence rule remains a matter of some debate and the courts are divided on the question whether extrinsic evidence should be admitted for the purpose of establishing an estoppel by convention or an equitable estoppel.

The parol evidence rule is justified on three bases. First, all discussion of terms during the negotiation stage should be treated as superseded by a written agreement that appears to be final and complete. Secondly, a written agreement that appears to be final and complete should be accorded special status so that parties can regard it as secure and certain. Thirdly, an investigation into what the parties have agreed or intended during negotiations is often time-consuming and inconclusive. Some judges have said that these considerations justify the exclusion of evidence to establish an estoppel, as well as evidence relating to the contractual terms. Accordingly, they have said that evidence of pre-contractual negotiations will not be admitted for the purpose of establishing an estoppel.[295] On the other hand, it has been said that it is unconscionable for a party to insist on her or his strict legal rights if another party has given those rights on the faith of an assurance that they will only be exercised in a particular way.[296] In *Saleh v Romanous*, which is discussed at [9.210], the New South Wales Court of Appeal held that equitable doctrines such as promissory estoppel operate to "trump" legal rights, including those protected by the parol evidence rule.[297] Promissory estoppel operates like other "equitable restraints on the enforcement of contractual rights based on pre-contractual conduct" such as equitable fraud, innocent misrepresentation and mistake.[298]

290 *Whittet v State Bank of New South Wales* (1991) 24 NSWLR 146, 151–4.

291 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [34], [577].

292 *Ryledar Pty Ltd v Euphoric Pty Ltd* [2007] NSWCA 65; (2007) 69 NSWLR 603, [204]–[214]; *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [34], [577].

293 Cooke, *The Modern Law of Estoppel* (2000), p 31, quoted with approval in *Tim Barr Pty Ltd v Narui Gold Coast Pty Ltd* [2010] NSWSC 29, [335].

294 See Chapter 12.

295 *Johnson Matthey Ltd v AC Rochester Overseas Corp* (1990) 23 NSWLR 190, 195–6; *Skywest Aviation Pty Ltd v Commonwealth* (1995) 126 FLR 61, 104–5; *Australian Co-operative Foods v Norco* [1999] NSWSC 274; (1999) 46 NSWLR 267, 279. See also *State Rail Authority of New South Wales v Heath Outdoor Pty Ltd* (1986) 7 NSWLR 170, 195–6.

296 *State Rail Authority of New South Wales v Heath Outdoor Pty Ltd* (1986) 7 NSWLR 170, 193.

297 *Saleh v Romanous* [2010] NSWCA 274; (2010) 79 NSWLR 453, [68].

298 *Saleh v Romanous* [2010] NSWCA 274; (2010) 79 NSWLR 453, [56].

Accordingly, the parol evidence rule cannot prevent the operation of promissory estoppel in relation to pre-contractual promises.

Entire agreement clauses

[9.210] It is common for "entire agreement" or "merger" clauses to be included in both standard-form written contracts and specially drafted agreements used in commercial transactions.[299] An entire agreement clause typically provides that the written contractual document constitutes the entire agreement between the parties and neither party has relied on any additional promises or representations made by the other. Such clauses attempt not only to invoke the parol evidence rule but also to exclude claims (such as for misrepresentation) that would not be excluded by the parol evidence rule.[300]

It has been accepted in several cases that an entire agreement clause will itself give rise to an estoppel by convention that will prevent the relying party from claiming the benefit of an estoppel that might otherwise have arisen from the pre-contractual negotiations.[301] On this view, the relying party, who has entered into the contract on the basis of a promise made by the inducing party, is estopped by the entire agreement clause from claiming the benefit of an estoppel against the inducing party. On the other hand, it is difficult to see why "a remedy of equity based on unconscionability" should be defeated by an entire agreement clause, particularly when the relying party has been induced by the inducing party's conduct to enter into the agreement containing the clause.[302] It is said that "equity would not permit an entire agreement clause to stultify the operation of its doctrines".[303] The weight of recent authority now seems to favour this second view.[304]

The second approach was followed by the New South Wales Court of Appeal in *Saleh v Romanous*.[305] Romanous entered into a contract to buy land from Saleh on the assumption that Saleh's brother Edmond, who owned the adjoining land, would participate with Romanous in a joint venture to develop the two properties. Before the contract was made, Saleh said to Romanous "I'm taking responsibility for Eddie. If Eddie does not want to build you don't have to buy and you'll get your money back". Romanous was unable to negotiate a joint venture with Edmond, so he terminated the contract and sought to recover the deposit. The trial judge held that promissory estoppel prevented Saleh from enforcing the contract of sale. The Court of Appeal confirmed that promissory estoppel could operate despite the fact that the contract of sale included an entire agreement clause. The Court of Appeal held – controversially, as discussed at [9.155] – that promissory estoppel could only operate defensively and therefore

299 Note that an entire agreement clause in a consumer or small business contract could be considered an unfair term, particularly if one-sided: see Chapter 16.

300 See Seddon, "Can Contract Trump Estoppel?" (2003) 77 *Australian Law Journal* 126, 129.

301 *Johnson Matthey Ltd v AC Rochester Overseas Corp* (1990) 23 NSWLR 190, 196; *Skywest Aviation Pty Ltd v Commonwealth* (1995) 126 FLR 61, 104–5; *Australian Co-operative Foods v Norco* [1999] NSWSC 274; (1999) 46 NSWLR 267, 279; *CG Mal Pty Ltd v Sanyo Office Machines Pty Ltd* [2001] NSWSC 445, [49]–[55]. Einstein J concluded in *Chint Australasia Pty Limited v Cosmoluce Pty Limited* [2008] NSWSC 635, [138], that the balance of authority favoured this view, but the balance of authority has since tipped in the other direction.

302 *Branir Pty Ltd v Owston Nominees (No 2) Pty Ltd* (2001) 117 FCR 424, 544. This view is also favoured by Seddon, "Can Contract Trump Estoppel?" (2003) 77 *Australian Law Journal* 126.

303 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [554].

304 *Franklins v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603 and *Saleh v Romanous* [2010] NSWCA 274; (2010) 79 NSWLR 453.

305 *Saleh v Romanous* [2010] NSWCA 274; (2010) 79 NSWLR 453.

did not provide a basis on which the deposit could be recovered.[306] Since the promissory estoppel prevented Saleh from enforcing the contract, however, Romanous was entitled to an order for repayment of the deposit under s 55(2A) of the *Conveyancing Act 1919* (NSW), which gives the court power to order the repayment of any deposit.

Post-contractual variations

[9.215] The traditional application of promissory estoppel is in relation to a one-sided agreement varying the terms of an existing contract. An estoppel may arise where A has a contract with B and A either undertakes an additional obligation to B or agrees to release B from a contractual obligation, apparently receiving nothing in return.[307] Where A seeks to resile from that promise, the question arises whether B can enforce it by way of contract or estoppel. In determining whether the variation is enforceable in contract, the vital question is whether A has received consideration from B.[308] The crucial issue in establishing an estoppel is whether B has acted on A's promise in such a way that he or she will suffer detriment if A does not adhere to the promise. The classic instance is a promise by a landlord to accept a reduced rental, which is later breached by the landlord suing the tenant to recover the difference between the original rent and the reduced amount. In *Je Maintiendrai Pty Ltd v Quaglia*, promissory estoppel was successfully relied upon by tenants as a defence to such a claim by the landlord.[309]

An important question for the operation of equitable estoppel in this context is whether the relying party (B in the above example) can be said to have suffered a detriment in losing the opportunity to breach the contract. It has been said that the relying party could claim that he or she would have been better off had he or she breached the contract and paid damages to A, rather than continuing to perform the contract on the basis of its original terms.[310] This raises the question whether the performance of a contractual obligation can be regarded as a detrimental action. It is difficult to see how performance of a contract could be regarded as detrimental, because a party does not have a choice as to whether to perform his or her contractual obligations. A party to a contract is under a legal duty to perform and is not entitled to breach the contract, even on offering to pay damages.[311] Windeyer J said in *Coulls v Bagot's Executor & Trustee Co Ltd*:

> It is, I think, a faulty analysis of legal obligations to say that the law treats a promisor as having a right to elect either to perform his promise or pay damages. Rather … the promisee has "a legal right to the performance of the contract".[312]

306 *Saleh v Romanous* [2010] NSWCA 274; (2010) 79 NSWLR 453, [73]–[81]. On the effect of promissory estoppel, compare *Anaconda Nickel Ltd v Edensor Nominees Pty Ltd* [2004] VSCA 167, discussed at [9.195], which was not cited in *Saleh v Romanous*.

307 For recent examples, see *GEC Marconi Systems Pty Ltd v BHP Information Technology Pty Ltd* (2003) 128 FCR 1; *New Zealand Pelt Export Company Ltd v Trade Indemnity New Zealand Ltd* [2004] VSCA 163.

308 See [4.65]–[4.105].

309 *Je Maintiendrai Pty Ltd v Quaglia* (1980) 26 SASR 101, discussed at [9.75].

310 *Je Maintiendrai Pty Ltd v Quaglia* (1980) 26 SASR 101, 115–6; Spence, *Protecting Reliance – The Emergent Doctrine of Equitable Estoppel* (1999), p 135.

311 *South Wales Miners' Federation v Glamorgan Coal Co Ltd* [1905] AC 239, 253.

312 *Coulls v Bagot's Executor & Trustee Co Ltd* (1967) 19 CLR 460, 504, quoting Lord Erskine in *Alley v Deschamps* (1806) 13 Ves Jun 225; 33 ER 278, 279. See also *Placer Developments Ltd v Commonwealth* (1969) 121 CLR 353, *Zhu v Treasurer of NSW* [2004] HCA 56; (2004) 218 CLR 530, [128] and *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [13].

A contracting party cannot, therefore, claim to have suffered detriment simply by reason of having performed a contractual obligation and having thereby lost the opportunity to breach the contract. If this view is right, then equitable estoppel will not provide a remedy in a contract variation case unless B has taken some action on the faith of A's promise, other than mere performance of B's contractual obligations, which would operate to B's detriment if the promise was not kept.

Estoppel as an alternative to contract

[9.220] The next issue is whether a plaintiff can choose to sue in equitable estoppel, rather than contract, where the plaintiff has relied on and given valuable consideration for a promise. In the United States it is said that promissory estoppel is sometimes asserted in lieu of a traditional contract claim in cases where bargain consideration has been given.[313] It is clear that, under Australian law, an equitable estoppel cannot arise from reliance on an enforceable contractual promise. If a promisee has given consideration for and relied on the promise, then there is a contract and no equitable estoppel. There are two reasons for this. First, a plaintiff who has enforceable contractual rights arising from a promise could not be regarded as having suffered detriment as a result of his reliance on that promise. Secondly, since equity acts only to supplement the common law, if the common law provides a remedy to the promisee through contract, there is no reason for equity to intervene.[314] The proper order of analysis, then, is to ask first whether a promise forms part of an enforceable contract.[315] If it does, then the plaintiff's only remedy is in contract. It is only where the promise does not form part of an enforceable contract equitable estoppel can be considered.

Termination of contracts

[9.225] We have seen in the context of contract variations that a contractual right may be lost by way of estoppel or its exercise restricted. Where the holder of a contractual right (A) leads B to act on the assumption that the right will not be exercised, then A cannot exercise that right in such a way as to cause detriment to B. That principle is capable of operating in relation to any contractual right or power, including an entitlement to terminate a contract. A's right to terminate the contract may arise as a result of a breach by B or as a result of the non-fulfilment of a condition set out in the contract. In either case, where A induces B to assume that A will not exercise the right to terminate and B acts to his or her detriment on the faith of that assumption, equitable estoppel will restrict the exercise by A of that right to terminate.[316]

313 Farber and Matheson, "Beyond Promissory Estoppel: Contract Law and the Invisible Handshake" (1985) 52 *University of Chicago Law Review* 903, 908; Pham, "The Waning of Promissory Estoppel" (1994) 79 *Cornell Law Review* 1263, 1267–8.

314 *Riches v Hogben* [1985] 2 Qd R 292, 301, in a passage quoted by the High Court in *Giumelli v Giumelli* [1999] HCA 10; (1999) 196 CLR 101, 121.

315 *PRA Electrical Pty Ltd v Perseverance Exploration Pty Ltd* [2007] VSCA 310, (2007) 20 VR 487, [54]–[55].

316 As to an estoppel relating to termination for breach, see *Legione v Hateley* (1983) 152 CLR 406, and as to estoppel relating to termination for non-fulfilment of a condition, see *Willing v Baker* (1992) 58 SASR 357. See also *Foran v Wight* (1989) 168 CLR 385, discussed at [25.25].

Estoppel by representation and misrepresentation

[9.230] It is important to distinguish the principle of estoppel by representation from the principles relating to misrepresentation and the statutory prohibition on misleading or deceptive conduct.[317] Where a misrepresentation of fact has been made and relied upon, there is sometimes confusion as to which of these principles applies. The fundamental distinction is that the estoppel by representation is concerned only with detriment resulting from inconsistent conduct and not with detriment resulting from the falsity of the representation. Where a misrepresentation has been made, then estoppel by representation will only protect against detriment that results from the combination of reliance by the relying party and an attempt by the inducing party to behave inconsistently with the representation.[318] Assume, for example, that A represents to B that a car B is buying is a 1960 model, whereas in fact, it is a less valuable 1963 model. If B buys the car on the faith of that representation, then B will not be entitled to relief against A by way of estoppel because A has not attempted to deny the truth of the assumption or to act inconsistently with it. B must look to the law of misrepresentation or misleading conduct for relief. B has suffered loss because B has relied on a representation which is untrue. If, on the other hand, A had falsely represented to B that the car was not owned by A and then sought to assert his or her ownership after B had bought the car from a third party, then A's inconsistent conduct would give rise to an estoppel by representation. Here, any detriment B would suffer would result from A's inconsistent conduct in first denying ownership and then asserting it.

WHY PROTECT RELIANCE?

[9.235] Why should the courts protect reliance by one party on an assumption induced by another? Several explanations have been advanced. The High Court has articulated a concern to redress unconscionable conduct. The courts intervene in estoppel cases because it is unconscionable for a inducing party to act inconsistently with an assumption that he or she has induced the relying party to adopt and rely upon.[319] It can, however, be argued that it is the promise, rather than the unconscionable departure that is crucial. In the United States, it has been argued that the principle of promissory estoppel is based on a concern to enforce serious promises.[320] On this view, the requirement of detrimental reliance serves only to identify serious promises and distinguish them from promises not warranting enforcement. Stephen Smith has also argued that "the best overall explanation" of the English doctrine of promissory estoppel is that it is a promissory doctrine which can be seen as resting on the same foundations as contractual obligations.[321] Smith notes that this conclusion "relies in part on moral arguments".[322] The courts' strong preference for granting expectation relief might suggest that the courts are essentially concerned in estoppel cases with the enforcement

317 See Chapters 32 and 33.

318 See *Murphy v Overton Investments Pty Ltd* [2001] FCA 500; (2001) 112 FCR 182, [63] and [70].

319 See, eg, *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387, 405, 419; *Commonwealth v Verwayen* (1990) 170 CLR 394, 407, 428–9.

320 Yorio and Thel, "The Promissory Basis of Section 90" (1991) 101 *Yale Law Journal* 111.

321 Smith, *Contract Theory* (2004), p 244. See also Atiyah and Smith, *Atiyah's Introduction to the Law of Contract* (6th ed, 2005), p 127.

322 Smith, *Contract Theory* (2004), p 244.

of promises. Against the promise-based view of equitable estoppel, however, it has been argued that equitable estoppels commonly arise without the making of any promise or commitment, and detrimental reliance is a fundamental requirement which does more than simply identify serious promises. Moreover, while the cases in which expectation-based relief have been granted can be explained according to a reliance theory (on the basis that where detriment cannot be quantified, there is no other way to protect against harm), the promise-based understanding of estoppel cannot account for those cases in which the remedy has been restricted to compensation for reliance loss.[323]

A third explanation is that the principles of estoppel by conduct are essentially concerned with protecting against harm. The particular type of harm against which estoppel by representation and equitable estoppel protects is the harm resulting from reliance on the conduct of others, when those others act inconsistently. The strict requirement of detrimental reliance provides support for this theory. On this understanding, the principles of estoppel can be justified on the basis that social values require parties who induce assumptions in others and reliance on those assumptions to take responsibility for harm caused by their inconsistent conduct.[324] While some see equitable estoppel as an equitable wrong that is analogous to tort,[325] others argue that estoppel is fundamentally different from tort because rights arise by way of estoppel from conduct of the parties that precedes the commission of any wrongful conduct. If rights arise by way of estoppel from a series of events consisting of the inducement of an assumption and (potentially detrimental) action in reliance on that assumption, then equitable estoppel is not part of the law of wrongs but is a sui generis source of rights and obligations.[326]

Economic analysis suggests that equitable or promissory estoppel provides a useful deterrent to the harm caused by detrimental reliance on promises.[327] The protection provided by a doctrine of promissory or equitable estoppel also encourages efficient reliance on promises, as Goetz and Scott explain.[328] A promise gives the promisee a valuable piece of information about the future. If the promisee acts on the promise and the promise is fulfilled, then the promisee's early reliance may be beneficial to one or both parties. Equitable estoppel is justified because it encourages beneficial reliance on promises by providing protection against the harm that can result from reliance. Legal principles that reduce the reliability of promises may discourage detrimental reliance but will do so at the cost of an equal reduction in beneficial reliance.

Whatever the rationale of equitable estoppel, there is no doubt that it supplements the doctrine of consideration in the enforcement of promises. The bargain theory of consideration confines contractual liability to a narrow range, protecting reliance only on those promises for which the promisee has bargained and paid. By protecting reliance on non-bargain promises,

323 Robertson, "Estoppels and Rights-Creating Events: Beyond Wrongs and Promises" in Neyers, Bronaugh and Pitel (eds), *Exploring Contract Law* (2009), 199, pp 211–24.

324 See Robertson, "The Form and Substance of Equitable Estoppel" in Robertson and Goudkamp (eds), *Form and Substance in the Law of Obligations* (2019) 249, 253–4.

325 See, eg, Benson, "The Unity of Contract Law" in Benson (ed), *The Theory of Contract Law: New Essays* (2001), pp 118, 177.

326 Robertson, "Estoppels and Rights-Creating Events: Beyond Wrongs and Promises" in Neyers, Bronaugh and Pitel (eds), *Exploring Contract Law* (2009), pp 199–224.

327 Posner, *Economic Analysis of Law* (9th ed, 2014), §4.1.

328 Goetz and Scott, "Enforcing Promises: An Examination of the Basis of Contract" (1980) 89 *Yale Law Journal* 1261.

equitable estoppel can be seen as providing a necessary corrective to the constraints of the bargain theory of consideration.

HOW SHOULD RELIANCE BE PROTECTED?

Promise, unconscionability and reliance

[9.240] The three theories underlying the principles of equitable estoppel, based on unconscionable conduct, promise and reliance, also provide guidance as to the way in which equitable estoppel should operate. If equitable estoppel is based on protecting against unconscionable conduct, then the central issue in each case is whether the inducing party's departure from the relevant assumption can be regarded as unconscionable.[329] If equitable estoppel is essentially concerned with enforcing promises, then the promise itself, rather than the reliance, should govern questions of liability and remedy. On this view, the doctrine should be subsumed by the law of contract through the relaxation of the doctrine of consideration.[330] If protecting against harm is the central concern, then issues of liability and remedy should revolve around the relying party's reasonable detrimental reliance. As currently conceived and applied by the Australian courts, equitable estoppel can be said to draw on each of these philosophies. A concern to prevent unconscionable conduct underlies the doctrine, while detrimental reliance provides the litmus test for the determination of liability and the remedial effect of equitable estoppel is, in most cases, the enforcement of a promise.

Economic efficiency

[9.245] In the United States, the goal of economic efficiency has been used by several commentators to provide guidance as to the way in which promissory estoppel should operate.[331] Some have argued that economic efficiency justifies only the enforcement of promises that further economic activity.[332] Others have argued that liability should be imposed on the party who is best placed to ensure that reliance occurs at the optimum time, in order to balance the benefits of early planning against the pitfalls of relying too early.[333] This, it is said, is likely to be the party with the greater bargaining power.

The remedy provided by promissory or equitable estoppel is also thought to have significant consequences for economic efficiency. Trebilcock has argued that an expectation measure of damages would be efficient because it would encourage promisors to disclose the circumstances that may affect their willingness to fulfil their promises.[334] Goetz and Scott, on the other hand,

329 See Spence, *Protecting Reliance – The Emergent Doctrine of Equitable Estoppel* (1999), pp 55–66. Cf Robertson, "Situating Estoppel within the Law of Obligations" (1997) 19 *Sydney Law Review* 32, 52–5.

330 Atiyah, *An Introduction to the Law of Contract* (5th ed, 1995), pp 137–41. Cf McFarlane, "Equitable Estoppel as a Cause of Action" in Degeling, Edelman and Goudkamp (eds), *Contract in Commercial Law* (2016) 143, 369–75.

331 See Robertson, "The Failure of Economic Analysis of Promissory Estoppel" (1999) 15 *Journal of Contract Law* 69.

332 Farber and Mattheson, "Beyond Promissory Estoppel" (1985) 52 *University of Chicago Law Review* 903.

333 Katz, "When Should an Offer Stick? The Economics of Promissory Estoppel in Preliminary Negotiations" (1996) 105 *Yale Law Journal* 1249.

334 Trebilcock, *The Limits of Freedom of Contract* (1993), pp 175–9.

suggest that even compensating reliance loss may be excessive.[335] They argue that if relying parties are overcompensated, this will encourage over-investment in reliance on promises, since it would provide a form of insurance against breach. Too limited a remedy, on the other hand, would discourage reliance and deprive society of the benefits of reliance. Goetz and Scott therefore propose a damages formula that would encourage an optimal level of reliance. The optimum remedy would, they argue, need to be something less than the relying party's full reliance loss.

Each of these proposals for an efficient doctrine of promissory or equitable estoppel rests on a series of assumptions.[336] First, the proposals assume that the goal of the law should be to encourage efficient behaviour, regardless of the consequences for parties in particular cases. Secondly, they assume that economic analysis can provide clear guidance as to which rule is most efficient. Thirdly, they assume that promissory estoppel can encourage efficient behaviour by providing incentives and disincentives. This, in turn, assumes that most people will know and understand the relevant legal rules and will act rationally in response to those rules.

335 Goetz and Scott, "Enforcing Promises: An Examination of the Basis of Contract" (1980) 89 *Yale Law Journal* 1261.

336 See Robertson, "The Failure of Economic Analysis of Promissory Estoppel" (1999) 15 *Journal of Contract Law* 69, 73–5, 78–80.

CHAPTER **10**

Restitution

INTRODUCTION

[10.05] This chapter is concerned with restitution for unjust enrichment. It is necessary to begin by distinguishing between *restitution* (which describes the *type of remedy* with which we are concerned) and *unjust enrichment* (which describes the *source of the obligation* with which we are concerned). The law of restitution is concerned with the recovery of gains made at the expense of others. A restitutionary obligation is an obligation to restore a gain which has been received at the expense of another person. A restitutionary remedy is one that reverses a transfer of value from the plaintiff to the defendant.[1] Restitutionary remedies are sometimes granted as a response to wrongs, such as a breach of contract.[2] We are not concerned here with restitution for wrongs. In the cases discussed in this chapter, restitutionary remedies are granted as a response to unjust enrichment. In these cases, unjust enrichment is the source of the obligation in question. Claims based on unjust enrichment constitute a distinct subset of the law of restitution.

Contracting parties almost invariably confer benefits on one another, but the resulting enrichment is not unjust because the recipient has a legal right to receive those benefits, having paid or promised to pay an agreed price for them. An employee enriches his or her employer through the performance of services, but these services are paid for in the form of wages or a salary. The buyer of a house enriches the seller by paying the purchase price, but receives

1 See Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), Ch 3 (arguing that, while restitution of value is the most common type of restitutionary remedy made to prevent unjust enrichment, orders for restitution of other things such as rights are sometimes made).

2 See further at [10.140].

the property in return. If return performance is not provided, there is usually an action for damages for breach of contract. In some cases, however, parties confer on one another benefits that are not governed by enforceable contractual rights. That may be because no valid contract ever comes into existence between the parties. Work may, for example, be done on the basis of an agreement which is void for uncertainty. Or a valid contract may come into existence, but subsequently be terminated. For example, a buyer may pay money to a supplier for machinery which cannot be delivered because of the outbreak of war.[3] In these cases, the recipient of the money or services is under no contractual obligation to reciprocate, and so the payer or provider of services may need to look to the law of restitution for unjust enrichment for a legal remedy.

Although the courts have been allowing restitutionary claims for hundreds of years, the law of restitution has only recently been recognised as a subject in its own right.[4] The scope and structure of the subject, and the role and scope of the concept of unjust enrichment, remain matters of controversy.[5] Most books devoted to the subject now explain and rationalise the types of claims considered in this chapter on the basis of a concern to prevent unjust enrichment.[6] In *Roxburgh v Rothmans of Pall Mall Australia Ltd*, Gummow J warned against the use of "top-down reasoning" from "any all-embracing theory" in this area.[7] He emphasised the fact that the law of restitution, like equity, developed "as a series of innovations" to fill gaps in the law and to avoid unjust results in specific cases.[8] Gummow J's warning was echoed by Gageler J and by Nettle, Gordon and Edelman JJ in *Mann v Paterson Constructions Pty Ltd*.[9] Although there are differences of opinion as to its scope and conceptual structure, there is no doubt that the law of restitution for unjust enrichment is a distinct and important branch of the law of obligations. Restitutionary obligations arising from unjust enrichment play an important gap-filling role in the contractual context and contract law cannot properly be understood without a basic understanding of those obligations.

The courts have recognised for some time that restitution for unjust enrichment is a branch of the law of obligations that is separate from contract and tort.[10] It is sometimes said that the law of unjust enrichment is subsidiary to the law of contract.[11] One illustration of this is that a restitutionary obligation to pay for services will not generally arise where there

3 The contract is then terminated by frustration: see [10.80] and Chapter 15.

4 The first English textbook on the subject, Goff and Jones, *The Law of Restitution*, was published in 1966 and the first Australian text, Mason and Carter, *Restitution Law in Australia*, in 1995. The American Law Institute published its first *Restatement of Restitution* in 1937.

5 For an overview of various competing theories, see Burrows, *The Law of Restitution* (3rd ed, 2011), Ch 2.

6 See, eg, Birks, *Unjust Enrichment* (2nd ed, 2005); Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), Ch 2; Mitchell, Mitchell and Watterson, *Goff and Jones: The Law of Unjust Enrichment* (9th ed, 2016), Ch 1; Burrows, *A Restatement of the English Law of Unjust Enrichment* (2012).

7 *Roxburgh v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516, 544–5.

8 *Roxburgh v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516, 545, quoting Laycock, "The Scope and Significance of Restitution" (1989) 67 *Texas Law Review* 1277, 1278.

9 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [79]–[81] (Gageler J), [199] (Nettle, Gordon and Edelman JJ).

10 See *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1942] AC 32, 62.

11 Grantham and Rickett, "On the Subsidiarity of Unjust Enrichment" (2001) 117 *Law Quarterly Review* 273; *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [14]–[18] (justifying a minority view). See further at [10.40] and [10.60].

is an enforceable contract governing the right to remuneration for those services.[12] More broadly, it means that a court must, in determining any restitutionary claim, consider how the restitutionary claim fits with any contractual arrangements between the parties and also any relevant contractual arrangements between the parties to the restitutionary claim and others.[13] Restitutionary obligations must not alter the rights and obligations that have been established by contract or redistribute risks that have been allocated by contract.[14]

FROM QUASI-CONTRACT TO UNJUST ENRICHMENT

[10.10] The two restitutionary claims that most commonly arise in the contractual context are the claim to recover money paid to another party (sometimes called an action for *money had and received*) and the claim to recover reasonable remuneration for services performed (sometimes called an action for a *quantum meruit* – the amount earned). These two actions, along with the claim to recover a reasonable price for goods delivered (*quantum valebant*–the amount they are worth),[15] were previously known as "quasi-contractual" actions because they were based on an implied or fictional contract.[16] They developed at a time when a legal claim needed to be brought within one of the recognised writs or "forms of action" and no writ was available to make a restitutionary claim. The courts adopted the fiction of an "implied contract" in order to allow a plaintiff seeking to recover money or the reasonable value of services or goods to issue a recognised writ such as indebitatus assumpsit. So, if one person paid money to another under a mistake, the law would "imply" a promise by the recipient to repay the money in order to provide the payer with a basis for recovery. Even claims with respect to goods or services were enforced by writ of debt on the basis of a fictional promise to pay a sum representing the value of the goods or services.[17] The forms of action were abolished in the 19th century. More recently, the courts have recognised that the basis of these claims is not an implied contract, but an obligation imposed by law in order to prevent unjust enrichment. These claims are now known as restitutionary claims, or claims based on unjust enrichment, rather than "quasi-contractual" claims. In Australia, the decisive step was taken in *Pavey & Matthews Pty Ltd v Paul*.[18]

Pavey and Matthew Pty Ltd (the builders) entered into a verbal contract with Mrs Paul to carry out building work renovating Mrs Paul's cottage. Mrs Paul agreed to pay the builders "a reasonable remuneration for that work, calculated by reference to prevailing rates of payment in the building industry". The builders completed the work and it was accepted by Mrs Paul. The builders claimed that $62,945.50 was a reasonable sum for the work, but Mrs Paul paid only $36,000. The verbal contract was unenforceable under s 45 of the *Builders Licensing Act 1971* (NSW), which provided that a contract under which a licensed builder undertakes

12 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 256. See further at [10.45] and cf *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, discussed at [10.65].

13 *Lumbers v W Cook Builders Pty Ltd (in liq)* [2008] HCA 27; (2008) 232 CLR 635, [79]; see also *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, discussed at [10.65].

14 *Lumbers v W Cook Builders Pty Ltd (in liq)* [2008] HCA 27; (2008) 232 CLR 635, [79] and [126]; *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, esp at [205].

15 The singular form is quantum valebat, the plural, quantum valebant.

16 See Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), pp 9–15.

17 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [182].

18 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221.

to carry out building work is not enforceable against the other party unless the contract is in writing, signed by both parties and sufficiently describes the work. The builders sued to recover $26,945.50 on the basis of a quantum meruit. The builders were successful at first instance, but the New South Wales Court of Appeal held that the builders' claim was barred by the statute since it involved enforcement of the oral contract.

The High Court held (4-1) that the builders were entitled to succeed. Mason, Wilson and Deane JJ held that the builders were entitled to recover in restitution reasonable remuneration for the work they had done, which had been accepted by Mrs Paul. A person who accepts services performed under an unenforceable contract is obliged by law to pay a reasonable remuneration for those services.[19] Although that obligation was formerly seen as arising from an "implied" contractual promise to pay, it should now be recognised as an obligation imposed by law. The idea that this restitutionary obligation arose from an implied contract should, Deane J said, "be recognised as but a reflection of the influence of discarded fictions, buried forms of action and the conventional conviction that, if a common law claim could not properly be framed in tort, it must necessarily be dressed in the language of contract".[20] The basis of the builders' claim was an obligation imposed by law to make restitution. This was not a claim to enforce the oral agreement, and so it was not precluded by the statute.[21] Although "proof of the oral contract may be an indispensable element in the plaintiff's success", the builder relied on the contract only to show that the benefits were not intended as a gift and had not been paid for.[22] If there had been an enforceable agreement between the parties governing the builders' right to compensation for the work, the law would not impose a restitutionary obligation.[23]

The effect of *Pavey & Matthews Pty Ltd v Paul* is that the old "quasi-contractual" actions are now seen as obligations imposed by law in order to prevent unjust enrichment.[24] Deane J cautioned that the recognition of restitution as the basis of the relevant actions "is not to assert a judicial discretion to do whatever idiosyncratic notions of what is fair and just might dictate".[25] He said that the circumstances in which the law imposes an obligation to make restitution for benefits received under an unenforceable agreement are set out in the cases and scholarly writings and are not likely to be greatly affected by the recognition that restitution or unjust enrichment is the basis of the obligation.[26] The High Court has repeatedly emphasised that unjust enrichment is not a legal principle that can be directly applied to the facts of particular cases.[27] Its function is simply taxonomical; it identifies and unites particular

19 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 227, 255–7. Brennan J dissented on the basis that a restitutionary or a quasi-contractual obligation could not be imposed while there is a subsisting contract covering the same subject matter. He said (at 237–8) that the "subsisting contract is the source and charter of the rights and obligations of the parties" and "the imposed obligation would be either inconsistent with the contract or it would duplicate the contractual obligation".

20 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 256.

21 See further at [10.85].

22 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 227–8.

23 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 256.

24 This has also been recognised in Canada (*Delgman v Guaranty Trust Co of Canada* [1954] SCR 725) and in England (*Lipkin Gorman v Karpanale Ltd* [1991] AC 70).

25 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 256.

26 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 256.

27 *Lumbers v W Cook Builders Pty Ltd (in liq)* [2008] HCA 27; (2008) 232 CLR 635, [85] (Gummow, Hayne, Crennan and Kiefel JJ); *Friend v Brooker* [2009] HCA 21; (2009) 239 CLR 129, [7] (French CJ, Gummow,

categories of cases in which the law allows parties to recover benefits retained by others.[28] Nevertheless, it is an important unifying concept, as Deane J made clear in *Pavey & Matthews Pty Ltd v Paul*:

> That is not to deny the importance of the concept of unjust enrichment in the law of this country. It constitutes a unifying legal concept which explains why the law recognizes, in a variety of distinct categories of case, an obligation on the part of a defendant to make fair and just restitution for a benefit derived at the expense of a plaintiff and which assists in the determination, by the ordinary processes of legal reasoning, of the question whether the law should, in justice, recognize such an obligation in a new or developing category of case.[29]

The High Court thus recognised in *Pavey & Matthews v Paul* that the quantum meruit action to recover reasonable remuneration for services was based on unjust enrichment. Soon after, in *Australia and New Zealand Banking Group Ltd v Westpac Banking Corporation*, the High Court held that an action to recover money paid under a mistake of fact rested on the same foundation:

> The basis of the common law action of money had and received for recovery of an amount paid under fundamental mistake of fact should now be recognised as lying not in implied contract but in restitution or unjust enrichment.[30]

Although the money claims and the services claims examined in this chapter have both been held to be restitutionary causes of action which aim to prevent unjust enrichment, they operate by reference to different criteria. Although both are common law causes of action, the action for money had and received has been infused with equitable principles while the quantum meruit action has not.[31] The reason for this is historical. In the foundational case of *Moses v Macferlan*, Lord Mansfield explained that the gist of the action to recover "money paid by mistake; or upon a consideration which happens to fail" or under duress is "that the defendant, upon the circumstances of the case, is obliged by the ties of natural justice and equity to refund the money."[32] We are, therefore, concerned in the money cases with a common law cause of action that is informed by equitable principles.[33] The core question in such cases is said to be whether retention of the payment is unconscionable.[34]

THE UNJUST ENRICHMENT FRAMEWORK

[10.15] A leading English treatise identified three essential elements that underlie the principle of unjust enrichment:

Hayne and Bell JJ); *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd* [2014] HCA 14; (2014) 253 CLR 560, [78] (Hayne, Crennan, Kiefel, Bell and Keane JJ).

28 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [30] (French CJ, Crennan and Kiefel JJ).

29 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 256–7.

30 *Australia and New Zealand Banking Group Ltd v Westpac Banking Corporation* (1987) 164 CLR 662, 673.

31 *Peet v Richmond* [2011] VSCA 343; (2011) 33 VR 465, [126] (Nettle JA, with whom Neave JA and Judd AJA agreed). Cf *Lumbers v W Cook Builders Pty Ltd (in liq)* [2008] HCA 27; (2008) 232 CLR 635, [55] (where retaining the benefit of work done at the recipient's request was also said to be "unconscionable").

32 *Moses v Macferlan* (1760) 2 Burr 1005; 97 ER 676, 681.

33 This influence of equity is extensively discussed in *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd* [2014] HCA 14; (2014) 253 CLR 560.

34 *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd* [2014] HCA 14; (2014) 253 CLR 560, [65]–[76].

1. the defendant must have been *enriched* by the receipt of a benefit;
2. the benefit must have been gained *at the claimant's expense*; and
3. it would be *unjust* to allow the defendant to retain the benefit.[35]

This abstract formulation is commonly recited in restitution textbooks and scholarly writings as a basis for assessing those restitutionary claims that are based on unjust enrichment,[36] often combined with a fourth element that no defence is available to the defendant.[37] In English law, those four questions provide a framework through which unjust enrichment claims of all kinds are assessed. In *Benedetti v Sawiris*,[38] for example, Lord Clark JSC said:

> It is now well established that a court must first ask itself four questions when faced with a claim for unjust enrichment as follows. (1) Has the defendant been enriched? (2) Was the enrichment at the claimant's expense? (3) Was the enrichment unjust? (4) Are there any defences available to the defendant?

In *Investment Trust Companies v Revenue and Customs Commissioners*,[39] the UK Supreme Court cautioned that these four questions do not dispense with the need for careful analysis or the consideration of relevant authorities, which date back centuries. They "are no more than broad headings for ease of exposition".[40]

> They are intended to ensure a structured approach to the analysis of unjust enrichment, by identifying the essential elements in broad terms. If they are not separately considered and answered, there is a risk that courts will resort to an unstructured approach driven by perceptions of fairness, with consequent uncertainty and unpredictability. At the same time, the questions are not themselves legal tests, but are signposts towards areas of inquiry involving a number of distinct legal requirements. In particular, the words "at the expense of" do not express a legal test; and a test cannot be derived by exegesis of those words, as if they were the words of a statute.[41]

The formulation is sometimes used by Australian courts,[42] but recent Australian decisions tend to do so with great caution.[43] There are three reasons for this. First, the High Court of Australia has firmly rejected the idea that restitutionary claims can be analysed by direct

35 Jones, *Goff and Jones' Law of Restitution* (7th ed, 2007), 1-106. The current edition takes a different approach to the subject and describes the formula somewhat differently: see Mitchell, Mitchell and Watterson, *Goff and Jones: The Law of Unjust Enrichment* (9th ed, 2016), 1-09.

36 Most writers regard restitution for wrongs, discussed at [10.140], as falling outside this framework.

37 See, eg, Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 8.

38 *Benedetti v Sawiris* [2013] UKSC 50; [2014] AC 938, [10] (Lord Clark, with whom Lord Kerr and Lord Wilson agreed).

39 *Investment Trust Companies v Revenue and Customs Commissioners* [2017] UKSC 29; [2018] AC 275, [40]–[42] (Lord Reed, with whom Lord Neuberger, Lord Mance, Lord Carnwarth and Lord Hodge agreed).

40 *Investment Trust Companies v Revenue and Customs Commissioners* [2017] UKSC 29; [2018] AC 275, [41].

41 *Investment Trust Companies v Revenue and Customs Commissioners* [2017] UKSC 29; [2018] AC 275, [41]. See also *Swynson Ltd v Lowick Rose Llp (formerly Hurst Morrison Thomson Llp) (in liq)* [2017] UKSC 32; [2018] AC 313, [22]: "English law does not have a universal theory to explain all the cases in which restitution is available. It recognises a number of discrete factual situations in which enrichment is treated as vitiated by some unjust factor."

42 See, eg, *Hollis v Atherton Shire Council* [2003] QSC 147, [10]; *Spangaro v Corporate Investment Australia Funds Management Ltd* [2003] FCA 1025, [48].

43 See, eg, *Vasco Investment Managers Pty Ltd v Morgan Stanley Australia Pty Ltd* [2014] VSC 455, [352]–[356]; *Lampson (Australia) Pty Ltd v Fortescue Metals Group Ltd (No 3)* [2014] WASC 162, [50]–[51].

reference to an abstract framework or principle.[44] The High Court insists that restitutionary claims must be approached by reference to specific principles, rather than a general formula covering all restitutionary claims. In *Roxborough v Rothmans of Pall Mall Australia Ltd* (*Roxborough v Rothmans*),[45] Gummow J emphasised the disparate nature of restitutionary claims and cautioned against the use of an "all-embracing theory of restitutionary rights and remedies founded upon a notion of unjust enrichment". Gummow J's warnings against "top-down reasoning" and the analysis of restitution cases at a high level of abstraction were reiterated by Gummow, Hayne, Crennan and Kiefel JJ in *Lumbers v W Cook Builders Pty Ltd (in liq)*.[46] Direct application of the unjust enrichment framework has been held to be an error of law[47] and contrary to binding authority.[48] In *Mann v Paterson Constructions Pty Ltd*, however, Nettle, Gordon and Edelman JJ suggested that the four questions may serve a useful purpose.[49] Provided the usual common law techniques of incremental development and reasoning by analogy are applied, the four questions may be used within the process of development and refinement of the law in order to structure understanding and analysis.[50]

The second reason to be cautious is that the list of abstract criteria can give the impression that there is a generalised right to restitution for unjust enrichment. The High Court has repeatedly said that there is no general right to restitution for unjust enrichment. Rather, unjust enrichment simply provides a "unifying concept" which explains why the courts order restitution in particular situations.[51] Whether an enrichment is unjust does not depend on a general evaluation of whether it is fair for the recipient to retain the benefits that have been conferred on him or her. Under Australian law, "restitution arises in recognised categories of case and is not necessarily available whenever, and to the extent that, a defendant is enriched at the plaintiff's expense in circumstances that render the enrichment unjust."[52] Recovery in restitution "depends on the existence of a qualifying or vitiating factor" which is recognised in law as making the enrichment unjust.[53] In the contractual context, unjust enrichment most commonly arises from the payment of money and the performance of services. The unjust factors that most commonly provide the basis for restitutionary claims in the contractual context are mistake, failure of consideration and compulsion or duress in the case of payments of money, and request, free acceptance or failure of consideration in relation to services. Each of those bases for restitutionary claims will be considered in turn.

The third reason to be cautious is that the direct application of a broad principle of unjust enrichment may point to an erroneous outcome, as some cases have shown. As we will

44 Most recently in *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [80], [199] and [212]–[213].

45 *Roxburgh v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516, 544.

46 *Lumbers v W Cook Builders Pty Ltd (in liq)* [2008] HCA 27; (2008) 232 CLR 635, [75]–[79].

47 *Henderson's Automotive Technologies Pty Ltd (in liq) v Flaton Management Pty Ltd* [2011] VSCA 167; (2011) 32 VR 539, [52]–[53], [62]–[67].

48 *Southage Pty Ltd v Vescovi* [2015] VSCA 117, [49].

49 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [213].

50 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [213].

51 For example, *Lumbers v W Cook Builders Pty Ltd (in liq)* [2008] HCA 27; (2008) 232 CLR 635, [85]; *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [199].

52 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [213] (Nettle, Gordon and Edelman JJ).

53 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353, 379; *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* [2007] HCA 22; (2007) 230 CLR 89, [151].

see, a restitutionary claim will not necessarily fail where the defendant's enrichment does not come at the ultimate expense of the plaintiff; the fact that the plaintiff has passed on the cost to others is no answer to the claim.[54] Similarly, it is incorrect to attempt to assess whether a defendant has a valid change of position defence to a restitutionary claim by looking to the extent to which the defendant has been disenriched by events following the receipt of a payment.[55] Moreover, a restitutionary award with respect to services will not be determined by direct reference to the "enrichment" of the defendant and may deviate significantly from it.[56]

For those reasons, this chapter does not approach the subject by reference to a general formula for assessing claims for restitution based on unjust enrichment. Instead, it considers the particular circumstances in which such claims may arise in the contractual context and focuses on the principles that are applicable to claims made in each context.

INEFFECTIVE TRANSACTIONS

[10.20] The most common restitutionary claims in the contractual context arise where money (such as a deposit) is paid or services are rendered pursuant to a transaction that turns out to be ineffective. The transaction may be ineffective, for example, because the parties anticipate the formation of a contract that never materialises or because a contract is void for illegality, is frustrated or is terminated for breach.[57] The fact that benefits have been conferred under a contract that is or has become ineffective or unenforceable does not, of itself, provide a basis for restitution. Where money has been paid under an ineffective contract, it is recoverable if the money was paid for a consideration or purpose that has totally failed. The relevant basis for restitution is *failure of consideration*.

Where services are performed under ineffective contracts, restitutionary obligations to pay reasonable remuneration have been held to arise from a *request* that the work be done, from *free acceptance* of the work or from a total failure of consideration. Historically, services cases have not been assessed on the basis of failure of consideration. In England, the House of Lords has recognised that a restitutionary claim with respect to services provided under an ineffective transaction (such as a contract that fails to materialise) may be made on the basis of a failure of consideration.[58] Influential commentators have argued that this approach should also be adopted in Australia.[59] In *Mann v Paterson Constructions Pty Ltd*,[60] members of the High Court for the first time recognised failure of consideration (or failure of basis) as the foundation of a restitutionary obligation with respect to services. As will be discussed below, failure of consideration seems certain to play a more significant role in services cases in the future.

54 *Roxborough v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516, discussed at [10.35].

55 *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd* [2014] HCA 14; (2014) 253 CLR 560, discussed at [10.115].

56 See [10.49].

57 See further at [10.50]–[10.90].

58 *Cobbe v Yeoman's Row Management Ltd* [2008] UKHL 55; [2018] 1 WLR 1752, [43]–[44].

59 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), Ch 11.

60 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [168]–[169] (Nettle, Gordon and Edelman JJ).

Failure of consideration

Consideration: performance, purpose or basis

[10.25] There are four important points to note about the requirement of total failure of consideration. The first is that the word "consideration" is used in a different sense here from the contract formation context, where the giving of a valuable promise is good consideration. Where restitution is sought with respect to money paid or services rendered under a contract, the issue is not whether a return promise was given by the payee, but whether the payee's promise was fulfilled.[61] In the restitutionary context, "it is the performance of the defendant's promise, not the promise itself, which is the relevant consideration".[62] Moreover, and more importantly, the concept of failure of consideration is not limited to cases in which the defendant has failed to perform a contractual obligation. It extends to situations in which there has been a failure of the *purpose* for which money has been paid or services provided.

"There will be a 'failure of consideration' where a payment has been made for a purpose that is not fulfilled (including an unpromised future event), or in contemplation of a state of affairs which does not materialise."[63] In *Martin v Andrews*,[64] for example, money paid to a witness to defray his travelling expenses was recoverable when the case was settled before trial. Although Lord Campbell CJ said that the *consideration* had failed,[65] there was no failure of contractual performance. Rather, there was a failure of the *purpose* for which the money was paid. This ground of restitution is therefore more accurately called *failure of basis* (on which a payment is made or services provided) rather than *failure of consideration*,[66] and there are signs of a shift towards that more apt terminology.[67] Whether it is called failure of consideration or failure of basis, it occurs where "the state of affairs contemplated as the basis or reason for the payment [or services] has failed to materialise or, if it did exist, has failed to sustain itself."[68]

In order to make out this ground of restitution, a plaintiff must show that a payment was made or services provided on a particular basis or for a particular purpose. If the plaintiff is unable to establish the purpose of a payment, the claim will not succeed even if the court is convinced the payment was not made as a gift. In *Alexiadis v Zirpiadis*,[69] the court disbelieved both parties as to the purpose of the payment and drew the inference that the payment was made for an undisclosed illegal purpose such as funding the cultivation of cannabis. The award of restitution at first instance was overturned on appeal because the plaintiff, having

61 *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32, 48.

62 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 351.

63 *Spangaro v Corporate Investment Australia Funds Management Ltd* [2003] FCA 1025, [51].

64 *Martin v Andrews* (1876) 7 El & Bl 1; 119 ER 1148, quoted with approval in *Roxborough v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516, 555–6, discussed at [10.35].

65 *Martin v Andrews* (1876) 7 El & Bl 1; 119 ER 1148, 1149.

66 Mitchell, Mitchell and Watterson, *Goff and Jones: The Law of Unjust Enrichment* (9th ed, 2016), 13-01.

67 *Barnes v Eastenders Cash & Carry Plc* [2014] UKSC 26; [2015] AC 1, [105]–[106]; *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [77]–[81] (Gageler J).

68 Birks, *An Introduction to the Law of Restitution* (1989), p 223, quoted with approval in *Barnes v Eastenders Cash & Carry Plc* [2014] UKSC 26; [2015] AC 1, [107]–[108] and *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [189] (Nettle, Gordon and Edelman JJ).

69 *Alexiadis v Zirpiadis* [2013] SASCFC 64.

failed to establish the purpose of the payment, had failed to prove an essential element of a restitutionary claim based on a total failure of consideration.

The need for a "total" failure

[10.30] The second point is that recovery is possible only if the failure of consideration is total. Restitutionary relief is not available if the claimant has received some of what he or she bargained for. Where a person has paid money for a consideration which has partially failed, the courts will not allow restitution of a proportion of the sum paid. Against the apparent strictness of the rule, however, three things must be noted. First, as will be seen below, restitution can be granted where a severable part of the consideration has totally failed and the payment in question can be apportioned between the failed part and the effective part of the consideration. Secondly, Mason J suggested in *Baltic Shipping Co v Dillon*[70] that the "total failure" rule precludes restitution only if the claimant has received and retained "any *substantial part* of the benefit expected under the contract". Thirdly, the High Court has indicated that the "total failure" rule may not preclude restitution "in a case where counter-restitution is relatively simple".[71] In other words, the claimant may be able to seek restitution if he or she can easily account for and return the benefits he or she has received.

In *Baltic Shipping Co v Dillon*, a passenger on a cruise ship sought recovery of the fare when the cruise ship sank on the tenth day of a 14-day cruise as a result of the breach of the carrier's duty to take reasonable care.[72] The carrier (Baltic) refunded part of the fare. The trial judge held that the passenger (Mrs Dillon) was entitled to recover the balance of the fare because any benefits Mrs Dillon obtained were "entirely negated by the catastrophe".[73] The High Court held that she was not entitled to recover any part of the fare in restitution because she had received a substantial part of the "bargained-for benefit".[74] Because Mrs Dillon had received the benefit of "the accommodation, the sustenance, the entertainment and the transport involved in the first eight clear days of the fourteen-day cruise", the failure of consideration was partial, rather than total.[75] Although the "catastrophe of the shipwreck … undoubtedly outweighed the benefits" Mrs Dillon had received in the first eight days, it did not alter the fact that those benefits "had been provided, accepted and enjoyed".[76]

Deane and Dawson JJ regarded as significant the fact that this was a pleasure cruise, rather than a contract for transportation. They observed that under a contract for air transportation from Sydney to London, the consideration would "at least prima facie, wholly fail" if the aircraft were forced to return to Sydney "after dinner and the inflight film".[77] The relevant question is not whether the claimant has received *any benefits* from performance of the contract, but whether he or she has received any part of *the benefit he*

70 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 350 (emphasis added).

71 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353, 383.

72 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344.

73 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 393.

74 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 351.

75 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 353, 377–9, 386.

76 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 379.

77 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 377, 378.

or she contracted to receive. The most famous illustration of this principle is *Rowland v Divall*.[78] The buyer of a car, which later turned out to have been stolen, sought to recover the purchase price when the car was seized by the police and returned to its true owner. The English Court of Appeal held that the consideration had totally failed because the buyer did not receive title to the car, even though the buyer (a dealer) and the person to whom he had sold it between them had the use of the car for four months before it was located by the police and returned to its true owner.

Severable consideration and the apportionment of payments

[10.35] The third point is that it is possible to recover a part of a sum paid if the amount claimed can be attributed to a distinct and severable part of the consideration, and that part of the consideration has failed. In *Roxborough v Rothmans*,[79] tobacco retailers purchased tobacco products from a wholesaler on terms that required them to pay the wholesale price of the products plus a "tobacco licence fee", which was thought to be payable to the New South Wales Government and was separately identified in invoices issued by the respondent. The legislation imposing the licence fee was declared unconstitutional by the High Court.[80] The retailers then sought to recover from the wholesaler the amounts they had paid to the wholesaler as "tobacco licence fees", but which the wholesaler was not required to pay to the revenue authorities as a result of the High Court's decision. Although there may have been a mistake as to the validity of the statute, the payments were not recoverable on the basis of mistake because any such mistake did not *cause* the payment. Rather, the payment was caused by the existence of a binding contractual obligation to pay the money.[81] The retailers were, however, entitled to recover on the basis that there had "been a failure of a distinct and severable part of the consideration".[82] Gummow J said that it was unconscionable for the wholesaler to retain the payments given "the failure to sustain itself of the state of affairs contemplated as a basis for the payments".[83] Where the consideration for a payment is "entire and indivisible", the law will not apportion it, but here the payments made by the retailers could be "broken up".[84] It was clear that "the sum designated in respect of the licence fee" was paid to fund the payment of the invalid tax.[85] The wholesaler argued unsuccessfully that its enrichment was not at the expense of the retailers. The retailers were held to be entitled to recover from the wholesaler even though the retailers had passed on the relevant cost to their customers and would therefore obtain a windfall. The retailers had paid "the amounts

78 *Rowland v Divall* [1923] 2 KB 500. See also *Rover International Ltd v Cannon Film Sales Ltd (No 3)* [1989] 3 All ER 423.

79 *Roxburgh v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516.

80 In *Ha v New South Wales* (1997) 189 CLR 465, the High Court of Australia held that the *Business Franchise Licences (Tobacco) Act 1987* (NSW) imposed an excise duty and was therefore invalid under s 90 of the Constitution.

81 *Roxburgh v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516, 562.

82 *Roxburgh v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516, 528 (Gleeson CJ, Gaudron and Hayne JJ). The same conclusion was reached by Gummow J (558) and Callinan J (589); Kirby J dissented on the basis that the failure of consideration was partial (577–9).

83 *Roxburgh v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516, 557.

84 *Roxburgh v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516, 557–8.

85 *Roxburgh v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516, 558.

referable to the tax" from their own money and it was unconscionable for the wholesaler to withhold repayment even if the retailers were not "ultimately left impoverished to that extent".[86]

The apportionment principle also applies where restitution is sought with respect to services. In *Mann v Paterson Constructions Pty Ltd*,[87] a construction contract required the owners to pay a fixed price for building work in accordance with a Progress Payments Table, which set out the amount to be paid to the builder on completion of each specified stage of construction. The contract was wrongfully repudiated by the owners before the work was complete and was terminated by the builder on the basis of that repudiation. The builder had been paid for some of the work done under the contract but remained unpaid: (i) for work done in respect of completed stages (for which there was an accrued right to payment under the contract), and (ii) for work done in respect of uncompleted stages (for which a right to payment under the contract had not yet accrued). Nettle, Gordon and Edelman JJ noted that in the case of fixed-price service contracts that are "infinitely divisible" (ie, the party doing the work is entitled to be paid for any part of the work), there will be no failure of consideration because there will be an accrued right to payment for *any work* done.[88] Where an obligation is "entire" (ie, no payment is due until *all of the work* is complete), then there will be a total failure of consideration if the contract is terminated for breach by the other party before the work is complete.[89] If the contract is "divisible into several entire stages", then the party doing the work will have an accrued contractual right to payment for the stages that are complete, and there will be a total failure of consideration in relation to stages that are incomplete.[90] Whether a contract can be understood to contain "divisible obligations of performance" is a matter of interpretation, but where a building contract is divided into stages, with payment due at the end of each stage, it will usually be interpreted in that way.[91]

Recovery under a subsisting contract

[10.40] The fourth point to note about failure of consideration is that in exceptional circumstances, money can be recovered on the basis of a failure of consideration even though the contract under which it was paid remains valid and on foot (ie, not terminated). *Roxborough v Rothmans*[92] stands as authority for this. Prior to *Roxborough v Rothmans*, many took the view that a restitutionary claim to recover benefits conferred under a contract could only succeed if the contract was void or unenforceable or had been terminated or rescinded. This point was unsuccessfully argued by the wholesaler in *Roxborough v Rothmans*.[93] The High Court's decision has been criticised on the basis that a restitutionary claim in relation to a benefit conferred under a contract should not be allowed unless the contract has been terminated, and this requirement should be overlooked only in exceptional circumstances

86 *Roxburgh v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516, 528.
87 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32.
88 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [172].
89 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [173].
90 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [174].
91 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [176].
92 *Roxburgh v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516.
93 *Roxburgh v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516, 588.

where it is clear that allowing the claim "would not subvert the contractual allocation of risk".[94] Beatson and Virgo suggest that the need for a contract to be terminated or rescinded before restitutionary remedies are available is based on the "fundamental principle" that the law of restitution is subordinate to the law of contract.[95] Michael Bryan has argued, however, that when a restitutionary claim is made in a contractual context, the important question is not whether the contract has been terminated, but "whether an order of restitution, if granted, would be inconsistent with the contractual allocation of risk agreed between the parties".[96] The crucial point was that the contract in *Roxborough v Rothmans* had not allocated this particular risk, and so it was clear that the law of restitution was fulfilling its gap-filling or auxiliary role:[97]

> In *Roxborough* it could hardly be claimed that the contract allocated the risk that the tobacco licensing scheme might turn out to be unconstitutional. This was "a gap in the contractual allocation" which allowed room for "applying the principle of unjust enrichment", even if the contract was still operative.[98]

Services

[10.45] Where services are provided under an ineffective contract, a claim to recover a reasonable sum (quantum meruit) has been held to be available where the services have been requested, freely accepted or provided for a consideration that totally fails. In *Liebe v Molloy*,[99] Griffith CJ (delivering the judgment of the High Court) said:

> When a man does work for another without any express contract relating to the matter, an implied contract arises to pay for it at its fair value. Such an implication of course arises from an *express request* to do made under such circumstances as to exclude the idea that the work was covered by a written contract. So it would arise from the owner *standing by and seeing the work done* by the other party, *knowing that the other party, in this case the contractor, was doing the work in the belief that he would be paid for it as extra work*.

It is not clear whether the references to "an implied contract" in this passage were intended to refer to a contract implied in fact, or a restitutionary obligation, which at the time was commonly said to be based on an "implied contract" but is now understood to be imposed by law to prevent unjust enrichment.[100] Assuming the latter, the statement of Griffith CJ clearly identifies two alternative bases for a quantum meruit claim arising from work done under an ineffective contract.

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94 Beatson and Virgo, "Contract, Unjust Enrichment and Unconscionability" (2002) 118 *Law Quarterly Review* 352, 356.

95 Beatson and Virgo, "Contract, Unjust Enrichment and Unconscionability" (2002) 118 *Law Quarterly Review* 352, 356.

96 Bryan, "Rescission, Restitution and Contractual Ordering: The Role of Plaintiff Election" in Robertson (ed), *The Law of Obligations: Connections and Boundaries* (2004), p 72.

97 Gummow J observed that the action in *Roxborough v Rothmans* "may be illustrative of the gap-filling and auxiliary role of restitutionary remedies": *Roxburgh v Rothmans of Pall Mall Australia Ltd* [2001] HCA 68; (2001) 208 CLR 516, 545.

98 Bryan and Ellinghaus, "Fault Lines in the Law of Obligations" (2000) 22 *Sydney Law Review* 636, 663 (quoting Beatson, "Restitution and Contract: Non-Cumul?" (2000) 1 *Theoretical Inquiries in Law* 83, 94).

99 *Liebe v Molloy* (1906) 4 CLR 347, 354 (emphasis added).

100 *Lampson (Australia) Pty Ltd v Fortescue Metals Group Ltd (No 3)* [2014] WASC 162, [62]–[71].

Free acceptance

[10.46] In *Pavey & Matthews Pty Ltd v Paul*, Mrs Paul's obligation to make restitution was said to have arisen from "her acceptance of the work without paying the agreed remuneration".[101] Acceptance alone is clearly not enough to generate a restitutionary obligation, however. The principle of "free acceptance" requires that the services were not provided gratuitously and that the recipient must have had a reasonable opportunity to reject the services. In *Brenner v First Artists Management Pty Ltd*, Byrne J set out the elements necessary to establish free acceptance of the benefit of the services. Byrne J said that acceptance of the benefit of services will generate a restitutionary obligation to pay reasonable remuneration where:

1. "there is no subsisting enforceable contract between the parties for the performance of the services";[102]
2. a reasonable person in the position of the recipient would have realised that the person providing the services expected them to be paid for; and
3. the recipient accepted the services having had a reasonable opportunity to reject them.[103]

The second and third elements will be satisfied where services are provided under an ineffective contract "or pursuant to a request made in the course of a normal commercial relationship with a person whose business it is to provide those services for reward".[104]

Request

[10.47] Although it seemed for some time to have been subsumed by the free acceptance principle, the idea of request as a distinct basis for a restitutionary claim with respect to services has a long history. It was revived by the High Court in *Lumbers v W Cook Builders Pty Ltd (in liq)*.[105] W Cook & Sons Pty Ltd (Sons) orally agreed to build a house for the Lumbers. The work of the builder mostly involved employing and supervising sub-contractors. It was agreed that the Lumbers would pay the costs incurred by Sons plus a supervision fee, although the amount of the fee was never determined. Following a corporate reorganisation, and without the knowledge of Lumbers, all of the building work that was being done by Sons was taken over by a related company, W Cook Builders Pty Ltd (Builders). From then on, the work on the Lumbers' house was undertaken by or on behalf of Builders, but Sons continued to invoice the Lumbers for the work and passed on the amounts received to Builders. Three years after the house was completed, Builders went into liquidation. Although Sons made no further claim against the Lumbers, the liquidator of Builders claimed that Builders had been underpaid for the work on the Lumbers' house. The liquidator of Builders sought to recover from the Lumbers the difference between the total amount paid by the Lumbers and an amount that represented reasonable remuneration for the work done by Builders (ie, the cost of the building works plus a reasonable fee for supervision).

101 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 228.

102 *Brenner v First Artists Management Pty Ltd* [1993] 2 VR 221, 257.

103 *Brenner v First Artists Management Pty Ltd* [1993] 2 VR 221, 260; *Damberg v Damberg* (2001) 52 NSWLR 492, 528–30.

104 *Brenner v First Artists Management Pty Ltd* [1993] 2 VR 221, 260.

105 *Lumbers v W Cook Builders Pty Ltd (in liq)* [2008] HCA 27; (2008) 232 CLR 635.

The trial judge found that the difference was more than $260,000. There was no adequate explanation as to why this amount was not claimed by Sons. The liquidator failed at first instance. Since the contract between the Lumbers and Sons remained in force, and was not assigned to Builders, Builders was held to have undertaken the work on the Lumbers' house as a subcontractor for Sons. The trial judge in the District Court therefore held that Builders had no rights against the Lumbers. On appeal, the Full Court of the South Australian Supreme Court held (2-1) that Builders could recover in restitution against the Lumbers. The Lumbers had incontrovertibly benefited from the work done by Builders and freely accepted that benefit, even though they did not know it was being provided by Builders.

The High Court overturned the decision of the Supreme Court and held that Builders had no rights against the Lumbers. The Lumbers' contractual obligations were to Sons, and Builders' contractual rights were against Sons. If an unpaid subcontractor was allowed to proceed in restitution against the principal, that would have the effect of upsetting contractually allocated risks and redistributing contractually allocated rights and obligations. Moreover, Gleeson CJ held that Lumbers made no request to Builders for the services provided, nor did Lumbers freely accept them or acquiesce to Builders providing those services since "Lumbers were unaware of the existence or role of Builders".[106] Gummow, Hayne, Crennan and Kiefel JJ held that Builders had no restitutionary claim against Lumbers because "it can point to no request by the Lumbers directed to Builders that Builders do any work it did or pay any money it did".[107] Their Honours referred to the nine factors identified in *Angelopoulos v Sabatino* as relevant to a quantum meruit claim based on free acceptance (which included matters such as whether the plaintiffs intended to provide their services gratuitously, whether the recipient should reasonably have understood that the services were to be paid for and whether the services were provided on the basis that they were to be paid for only if an event came to pass, such as a contract being made).[108] Gummow, Hayne, Crennan and Kiefel JJ said of these factors:

> And if Builders did work or paid money at the Lumbers' request, it would follow that it would be neither necessary nor appropriate to consider any of the other eight factors identified in *Angelopoulos* in deciding whether Builders could recover a fair price for the work it had done and the amount it had paid for and at the request of the Lumbers. To the extent that *Angelopoulos* is understood as requiring separate or additional consideration of those other factors, where a plaintiff seeks to recover a fair price for work done at the defendant's request, or the amount the plaintiff has paid for the defendant at the defendant's request, *Angelopoulos* is wrong and should not be followed.[109]

106 *Lumbers v W Cook Builders Pty Ltd (in liq)* [2008] HCA 27; (2008) 232 CLR 635, [49]–[53].

107 *Lumbers v W Cook Builders Pty Ltd (in liq)* [2008] HCA 27; (2008) 232 CLR 635, [126].

108 The nine factors mentioned in *Angelopoulos v Sabatino* (1995) 65 SASR 1, 12 were: 1. whether the plaintiffs intended to provide their services gratuitously; 2. whether the plaintiff acted "entire at its own initiative" or at the request of the defendant; 3. whether the plaintiffs provided their services on the basis that payment was to be made only if a certain event came to pass (and took the risk that the event may not occur); 4. whether the work was done on a basis from which the plaintiff chose to depart; 5. whether the defendant benefited from the plaintiff's work; 6. whether the benefit was conferred at the expense of the plaintiff; 7. whether the defendant approved of or agreed to the plaintiff doing the work they did; 8. whether the defendant should reasonably have known that the plaintiff expected the work to be paid for and 9. whether some factor (such as a change of position by the defendant) makes it unjust to require the defendant to make restitution.

109 *Lumbers v W Cook Builders Pty Ltd (in liq)* [2008] HCA 27; (2008) 232 CLR 635, [90].

Gummow, Hayne, Crennan and Kiefel JJ held that where services have been requested by the defendant, the request and the doing of the work are enough to establish a restitutionary claim.[110] They said that:

> At once it should be pointed out that, if Builders did whatever work it did and paid whatever money it paid at the Lumbers' request, Builders' claim for a reasonable price for the work and for the money it paid would fall neatly within long-established principles. It would matter not at all whether the request was made expressly, or its making was to be implied from the actions of the parties in the circumstances of the case. Builders would have an action for work and labour done or money paid for and at the request of the Lumbers.[111]

Two significant issues arise from the recognition in *Lumbers v Cook* that an express or implied request provides an independent basis for an obligation to pay for services that have been performed. The first is whether the presence of a request really can, as Gummow, Hayne, Crennan and Kiefel JJ suggested, render irrelevant all of the factors considered in the free acceptance cases. In order to determine whether a person who has performed services outside a contractual relationship is entitled to restitution, it cannot be enough simply to ask whether the person receiving the services requested them. Surely, it is necessary to consider the circumstances in which the request was made, including at least some of the factors that Gummow, Hayne, Crennan and Kiefel JJ characterised as "neither necessary nor appropriate to consider", such as: whether the defendant had a reasonable expectation that the services were to be provided gratuitously (or, conversely, should reasonably have known that the plaintiff expected the work to be paid for); and whether the plaintiffs were providing their services on the basis that payment was to be made only if a certain event came to pass (and took the risk that the event may not occur). Services are regularly requested in situations in which there is no expectation of payment unless a particular event comes to pass. Consider, for example, a request made to a travel agent to investigate the availability of flights and make tentative bookings. The travel agent does not expect to be paid unless a firm booking is made, and the presence of a request would not render that factor irrelevant or inappropriate to consider if the travel agent were to make a quantum meruit claim against a customer.

In *Vasco Investment Managers Pty Ltd v Morgan Stanley Australia Pty Ltd*,[112] Vickery J upheld a restitutionary claim with respect to services that were requested. His Honour specifically considered whether the defendant should have understood that the plaintiff expected to be paid for the services.[113] Vickery J held that this requirement was satisfied because the services were provided in the course of a normal commercial relationship by a company that was in the business of providing services for reward.[114] In contrast, the Queensland Court of Appeal has held that, after *Lumbers v Cook*, the necessary elements of the relevant cause of action and the only matters that should be pleaded and considered are that the plaintiff has performed work and that it has done so at the request of the defendant.[115]

The second issue is whether request was intended to provide the exclusive basis for restitutionary claims with respect to services or whether free acceptance continues to operate

110 *Lumbers v W Cook Builders Pty Ltd (in liq)* [2008] HCA 27; (2008) 232 CLR 635, [89].

111 *Lumbers v W Cook Builders Pty Ltd (in liq)* [2008] HCA 27; (2008) 232 CLR 635, [89].

112 *Vasco Investment Managers Pty Ltd v Morgan Stanley Australia Pty Ltd* [2014] VSC 455.

113 *Vasco Investment Managers Pty Ltd v Morgan Stanley Australia Pty Ltd* [2014] VSC 455, [370]–[373].

114 *Vasco Investment Managers Pty Ltd v Morgan Stanley Australia Pty Ltd* [2014] VSC 455, [370].

115 *Sunwater Ltd v Drake Coal Pty Ltd* [2016] QCA 255; [2017] 2 Qd R 109, [41].

as an alternative basis for such claims. In other words, can free acceptance establish a claim where neither an express nor an implied request can be established? This issue arose in *Lampson (Australia) Pty Ltd v Fortescue Metals Group Ltd (No 3)*.[116] The defendant in that case sought to have a free acceptance claim struck out on the basis that, after *Lumbers v Cook*, Australian law does not recognise a restitutionary claim based on free acceptance. Edelman J refused to strike out the pleading. He accepted that the status of the free acceptance principle was unclear after *Lumbers v Cook* but noted that there was no express rejection of the principle in that case, and that one would expect the High Court to discuss its own decision in *Liebe v Molloy* before denying the existence of free acceptance as the basis for a claim.[117] In *Vasco Investment Managers Pty Ltd v Morgan Stanley Australia Pty Ltd*,[118] Vickery J treated free acceptance and request as separate classes of case in which "[t]he law may impose an obligation to make restitution on a quantum meruit basis."[119]

Failure of consideration

[10.48] In terms of the unjust enrichment framework outlined above,[120] the identification of either a request for or free acceptance of services serves two functions. First, it establishes that the defendant has received something which is of *benefit* to him or her (rather than something which he or she may not value) and that the defendant has therefore been *enriched*. Secondly, it provides a basis for saying that the retention of that benefit or enrichment is *unjust*. If one approaches a services claim on the basis of the unjust enrichment framework, then whether the services have been requested or freely accepted is clearly relevant to the question of enrichment. But there is strong scholarly support for the view that the relevant "unjust factor" is not the presence of a request or free acceptance, but failure of consideration.[121] Edelman and Bant argue that failure of consideration, as the relevant unjust factor, provides the most satisfactory basis for determining services claims.[122] They argue that cases such as *Pavey & Matthews Pty Ltd v Paul* and *Brenner v First Artists Management Pty Ltd*[123] are better understood as having succeeded on the ground that the services were provided in return for a consideration that totally failed.[124] In England, the House of Lords has accepted failure of consideration as the basis of a restitutionary claim with respect to services.[125]

In *Mann v Paterson Constructions Pty Ltd*, three members of the High Court also accepted failure of consideration or failure of basis as the foundation of a restitutionary claim with respect to services. As discussed at [10.35], a construction contract was validly terminated by the builder on the basis of a wrongful repudiation by the owner. The builder remained unpaid in respect of work done in relation to uncompleted stages of the building project and

116 *Lampson (Australia) Pty Ltd v Fortescue Metals Group Ltd (No 3)* [2014] WASC 162.

117 *Lampson (Australia) Pty Ltd v Fortescue Metals Group Ltd (No 3)* [2014] WASC 162, [80]–[86].

118 *Vasco Investment Managers Pty Ltd v Morgan Stanley Australia Pty Ltd* [2014] VSC 455.

119 *Vasco Investment Managers Pty Ltd v Morgan Stanley Australia Pty Ltd* [2014] VSC 455, [339].

120 See [10.15].

121 Burrows, *A Restatement of the English Law of Restitution* (2012) (no mention of request or free acceptance as unjust factors); Mitchell, Mitchell and Watterson, *Goff and Jones: The Law of Unjust Enrichment* (9th ed, 2016), Ch 13–7 (failure of basis and free acceptance treated as alternatives).

122 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), Ch 11.

123 *Brenner v First Artists Management Pty Ltd* [1993] 2 VR 221, discussed at [10.55].

124 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), 271–2 and 324–8.

125 *Cobbe v Yeoman's Row Management Ltd* [2008] UKHL 55; [2018] 1 WLR 1752, [43]–[44].

sought restitution with respect to that work. Three members of the High Court held that a restitutionary claim was available on the ground of failure of consideration, which Gageler J noted has been renamed as "failure of basis".[126] The services were rendered by the builder "on a 'basis' that 'has failed to sustain itself' in the events that have occurred".[127] Nettle, Gordon and Edelman JJ held that the factor giving rise to an obligation to make restitution was "a total failure of consideration, or a total failure of a severable part of the consideration" and that "[i]n this context, consideration means the matter considered in forming the decision to do the act".[128] In a building contract divided into stages, with payment due at the end of each stage, "there will be a total failure of consideration in respect of [any incomplete] stages due to the failure of the builder's right to complete the performance and earn the price."[129]

In light of:

(a) the doubt cast by Gummow, Hayne, Crennan and Kiefel JJ in *Lumbers v Cook* on free acceptance as a basis for restitutionary claims with respect to services;

(b) the manifest inadequacy of "request" as an alternative (as outlined at [10.47] above);

(c) the strong support in the scholarly literature for treating failure of consideration or failure of basis as the operative unjust factor in (most) services cases; and

(d) the recognition by three members of the High Court in *Mann v Paterson Constructions Pty Ltd* of failure of consideration or failure of basis as the foundation of a quantum meruit claim,

failure of consideration or failure of basis seems almost certain to be treated as the operative unjust factor in cases falling within this category in the future.

Valuing services

[10.49] An obvious complication of claims relating to services is the difficulty of valuation. In most cases, the services are valued at the market rate for the work done and the materials supplied, rather than by reference to a discernable increase in the defendant's wealth. This tendency provides powerful ammunition for those who deny that any coherent principle of "unjust enrichment" underlies this part of the law of restitution. Steve Hedley asks: "Why is the defendant liable for the *reasonable price*, and not for the amount by which he is actually better off, whether this is less or more than the reasonable price?"[130] Hedley's answer is that, while we can say that "speaking in very loose and general terms" the law of restitution is concerned with "the recovery of benefits unjustly retained",[131] the idea that law of restitution is concerned with reversing unjust enrichments made at the plaintiff's expense is an over-simplification.[132]

In determining the amount to be paid for services that have been requested or freely accepted, then, the court is concerned primarily with the market rate for the services, not the cost to the plaintiff of providing them or the extent to which they have increased the

126 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [78].

127 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [78].

128 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [168].

129 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [176].

130 Hedley, "Unjust Enrichment as the Basis of Restitution – An Overworked Concept" (1985) 5 *Legal Studies* 56, 62.

131 Hedley, "Unjust Enrichment as the Basis of Restitution – An Overworked Concept" (1985) 5 *Legal Studies* 56, 56.

132 Hedley, "'Unjust Enrichment': The Same Old Mistake" in Robertson (ed), *The Law of Obligations: Connections and Boundaries* (2004), p 75.

defendant's wealth. The award can, therefore, include a margin for profit and overheads.[133] The court can have regard to the rate of remuneration that is common in the industry, taking into account the standing of the plaintiff in the profession or industry, and also the difficulty of the work and creativity involved.[134] The court can use an hourly rate or make a global assessment.[135] Where remuneration is typically paid on a commission basis for services of the relevant kind, the court can take into account the commission that might have been earned.[136] In some cases, it is unjust to require payment of reasonable remuneration, such as where work is "unsolicited but accepted" and reasonable remuneration "would far exceed the enhanced value of the property".[137] In those cases, it is necessary to look to the extent to which the value of the defendant's property has been increased by the work done by the plaintiff. Other factors may need to be taken into account in determining the amount of compensation that is "fair and just" in the circumstances.[138] In *Pavey & Matthews Pty Ltd v Paul*, for example, Deane J noted that if Mrs Paul had sustained "an identifiable real detriment" as a result of the builder's failure to satisfy the legislative requirements that would need to be taken into account.[139]

Another difficult question is the role of the contract price in setting the amount of the restitutionary remedy where services have been provided under a contract. It is clear that the contract price at least provides evidence of the amount that should be regarded as reasonable remuneration for the work.[140] Where the contract is *void*, the contract price does not operate as a limit on the restitutionary claim.[141] Where the contract is *unenforceable*, but has been fully performed on one side, Deane J suggested in *Pavey & Matthews Pty Ltd v Paul*[142] that the contract price will provide a ceiling on the amount that the defendant can be ordered to pay. In *Mann v Paterson Constructions Pty Ltd*, the High Court held that, where a contract has been *terminated for breach*, the contract price will generally operate as an upper limit on the amount recoverable by the aggrieved party. For the reasons discussed at [10.70], Gageler J said the contract price will always operate as a ceiling on the amount recoverable. Nettle, Gordon and Edelman JJ held that it will usually do so.[143] Their Honours observed that, for work done up to the point of termination of a contract, the contract price was the basis on which the work was done. The contract price also reflects the parties' agreed allocation of risk, and "[t]ermination of the contract provides no reason to disrespect that allocation."[144] The governing role of the contract price – which involves a clear departure from a concern with the

133 *Sopov v Kane Constructions Pty Ltd (No 2)* [2009] VSCA 141; (2009) 24 VR 510, [34]–[37].

134 *Brenner v First Artists Management Pty Ltd* [1993] 2 VR 221, 263.

135 *Brenner v First Artists Management Pty Ltd* [1993] 2 VR 221, 264.

136 *Brenner v First Artists Management Pty Ltd* [1993] 2 VR 221, 264–72. See also *Andrew Shelton & Co Pty Ltd v Alpha Healthcare Ltd* [2002] 5 VR 577, 608–9; *Upjay Pty Ltd v MJK Pty Ltd* [2001] SASC 62; (2001) 79 SASR 32, 47–50.

137 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 263.

138 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 263.

139 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 264.

140 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 257; *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 278; *Upjay Pty Ltd v MJK Pty Ltd* [2001] SASC 62; (2001) 79 SASR 32, 48–9; *Sopov v Kane Constructions Pty Ltd* (No 2) [2009] VSCA 141; (2009) 24 VR 510.

141 *Rover International Ltd v Cannon Film Sales Ltd (No 3)* [1989] 3 All ER 423.

142 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 257.

143 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [215].

144 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [205].

"enrichment" of the defendant – is another telling indication of the fact that the prevention of unjust enrichment does not operate as a definitive legal principle in Australian law.[145]

Types of ineffective transactions

Anticipated contracts that fail to materialise

[10.50] A restitutionary claim may arise where money is paid or work is done in the expectation that a contract will be made between the parties. If the contract is not concluded, the recipient of the money or the services will be under no contractual obligation to reciprocate and so the payer or provider of services must look to the law of restitution for recompense on the basis of a total failure of consideration (or possibly request or free acceptance in the case of services).

In *William Lacey (Hounslow) Ltd v Davis*,[146] a builder tendered to reconstruct a war-damaged building for Davis. The builder was told that his tender was the lowest and was led to believe that he would be contracted to undertake the building work. At Davis' request, the builder undertook considerable work preparing a revised estimate and supplying other information for the War Damage Commission, which resulted in the War Damage Commission approving additional payments to assist with the rebuilding. Davis then told the builder that he was going to employ another builder to do the work and, in fact, soon sold the premises without the building work being done. Barry J held that no contract was ever formed between the parties, but the work done by the builder went far beyond what a builder normally performs gratuitously when tendering for work. The work was done on the basis that it was to be paid for under a contract which both parties believed would be made. Since Davis requested the work and took the benefit of it, the builder was entitled to recover a reasonable sum for the work done.[147]

Goff and Jones note that Davis may have received an economic benefit from the work in the form of a higher price for the building, but this was not central to the decision. The defendant was deemed to have benefited from the plaintiff's services because the defendant requested them.[148] As to the unjust factor that provided the foundation for the restitutionary claim, Goff and Jones suggest that the case is best understood on the basis of free acceptance: "The defendant had not only benefited at the plaintiff's expense but had requested the performance of the services with knowledge that plaintiff did not intend to render the services gratuitously."[149] Edelman and Bant explain the case as an instance of failure of consideration since the work "had been done on the basis that a contract would eventuate."[150]

It is well accepted that a restitutionary claim for pre-contractual work will fail where the plaintiff has taken the risk that the work will go unremunerated if agreement is not reached

145 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [212]–[213].

146 *William Lacey (Hounslow) Ltd v Davis* [1957] 1 WLR 932. See also *British Steel Corp v Cleveland Bridge and Engineering Co Ltd* [1984] 1 All ER 504; McKendrick, "Work Done in Anticipation of a Contract which does not Materialise" in Cornish et al (eds) *Restitution: Past, Present and Future* (1998), p 163.

147 Jones, *Goff and Jones' Law of Restitution* (7th ed, 2007), 26-009. The current edition treats the decision as a failure of basis case, rather than a free acceptance case: Mitchell, Mitchell and Watterson, *Goff and Jones: The Law of Unjust Enrichment* (9th ed, 2016), Ch 16.

148 Jones, *Goff and Jones' Law of Restitution* (7th ed, 2007), 26-008.

149 Jones, *Goff and Jones' Law of Restitution* (7th ed, 2007), 26-009.

150 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 260.

and has undertaken the work in the mere hope that a contract will be made.[151] Where a person is invited to submit a tender for a particular contract, for example, it is usually understood that any work done in preparing the tender will go unremunerated if the tender is unsuccessful.[152] Similarly, where negotiations are expressly made "subject to contract", it is likely to be found that any work undertaken by the parties in anticipation of the contract is done at their own risk, and therefore, no restitutionary claim will be available if the other party withdraws from the negotiations.[153] It can be difficult to discern whether the person doing the work has accepted the risk that the contract may not materialise.[154]

Restitutionary claims have been successful in some cases against defendants who have withdrawn from contractual negotiations because they have changed their minds about proceeding with the transaction. In these cases, it is said that the party incurring expenditure may have taken the risk of the transaction going off because of a failure of the parties to reach agreement but has not taken the risk of the defendant simply changing his or her mind about the proposed transaction.[155] Restitution has been held to be available where the defendant:

> Unilaterally decides to abandon the project, not for any reason associated with bona fide disagreement concerning the terms of the contract to be entered into, but for reasons which, however valid, pertain only to his own position and do not relate at all to that of the other party.[156]

The other elements of a restitutionary claim must of course also be satisfied.

Agreements void for uncertainty

[10.55] A restitutionary claim may also be available in relation to money paid or services rendered under a contract that is void for uncertainty. In *Brenner v First Artists' Management Pty Ltd*,[157] the plaintiffs were engaged to provide management services to Daryl Braithwaite, a former pop star who was seeking to revive his career.[158] The arrangements as to the plaintiffs' responsibilities and their entitlement to commission were too uncertain to give rise to any enforceable contracts. For some months, the plaintiffs provided services, which contributed to the production of a recording and the making of arrangements for Braithwaite's comeback. The relationship deteriorated and the management arrangements were terminated by the defendant, but the album was subsequently released and Braithwaite's comeback was successful. Byrne J held that the defendant was under a restitutionary obligation to pay for such of the services as were provided in circumstances where a reasonable person would realise that the plaintiffs expected them to be paid for. He held that the plaintiffs' entitlement

151 Jones, *Goff and Jones' Law of Restitution* (7th ed, 2007), 26-013.

152 *Brenner v First Artists' Management Pty Ltd* [1993] 2 VR 221, 259.

153 *Regalian Properties plc v London Dockland Development Corp* [1995] 1 WLR 212. See also the analogous estoppel case *Attorney-General of Hong Kong v Humphreys Estate (Queen's Gardens) Ltd* [1987] AC 114.

154 See, eg, *Independent Grocers' Co-operative Ltd v Noble Lowndes Superannuation Consultants Ltd* (1993) 60 SASR 525.

155 *Sabemo Pty Ltd v North Sydney Municipal Council* [1977] 2 NSWLR 880; *Leading Edge Events Australia Pty Ltd v Te Kanawa* [2007] NSWSC 228. See also the analogous estoppel case *EK Nominees Pty Ltd v Woolworths Ltd* [2006] NSWSC 1172, discussed at [9.175].

156 *Sabemo Pty Ltd v North Sydney Municipal Council* [1977] 2 NSWLR 880, 903.

157 *Brenner v First Artists Management Pty Ltd* [1993] 2 VR 221.

158 *Brenner v First Artists Management Pty Ltd* [1993] 2 VR 221, 230.

to restitution did not depend on proof that their work had resulted in an economic benefit to the defendant. When one person requests another to do something, the law assumes that the person making the request "sees some benefit in its performance, however wrong this view may be on an objective basis".[159] Byrne J concluded that "in a case where the services were requested and accepted, the law will not stop to enquire whether they were, on any other basis, of benefit to the party requesting and accepting them".[160] In order to determine whether the enrichment was unjust, Byrne J applied the test for free acceptance set out above.[161] Fenner and Brenner were professional artists' managers who provided their services "pursuant to a request accompanied by a discussion as to the mode of payment".[162] Braithwaite was therefore unjustly enriched by the receipt of the services and was obliged to make restitution for the benefit he had received. Byrne J assessed the value of the services on an hourly rate and tested the reasonableness of these amounts by comparing them with the amounts that might have been earned on a commission basis.

Failure of a condition of formation or performance

[10.60] Contracting parties may agree that either the formation of the contract or the obligation to perform it shall be conditional on an event occurring (such as the parties entering into a more formal contract or the purchaser obtaining finance to complete the purchase).[163] If it is a condition of formation, then no contract will arise if the event does not occur. If it is a condition of performance, then one or both parties may terminate the contract if the event does not occur. It is quite common for a deposit to be paid under a contract that is subject to a condition of performance. If the stipulated condition is not fulfilled and the contract is terminated, then the deposit is recoverable in restitution on the basis of total failure of consideration. In *George v Roach*,[164] the parties made a contract for the sale of a business, with part of the purchase price to be determined by a valuation made by a man named Mr Solomon. A deposit of £100 was paid on signing, and a further £1000 was later paid under the terms of the agreement. Mr Solomon refused to provide the valuation. The valuation was held to be a condition precedent to formation of the contract. Accordingly, the agreement was ineffective and the £1100 paid by the purchaser was recoverable as money paid for a consideration that had failed.

Termination for breach

[10.65] As we will see in Chapter 21, some breaches of contract provide the aggrieved party with the right to terminate the contract at his or her option. A repudiation of the contract by one party will also provide a basis for termination of the contract by the other party, as we will see in Chapter 22. If the aggrieved party elects to terminate, this has the effect of terminating the contract as to the future only. Rights and obligations already accrued are not discharged. This means that the parties may enforce any accrued contractual rights to

159 *Brenner v First Artists Management Pty Ltd* [1993] 2 VR 221, 258.

160 *Brenner v First Artists Management Pty Ltd* [1993] 2 VR 221, 258–9.

161 See [10.45].

162 *Brenner v First Artists Management Pty Ltd* [1993] 2 VR 221, 260.

163 See Chapter 20.

164 *George v Roach* (1942) 67 CLR 253.

payment, and the aggrieved party may claim damages for loss suffered as a result of the breach of contract.[165]

Restitution for the aggrieved party

[10.70] As an alternative to claiming damages for breach of contract, the aggrieved party may claim a restitutionary remedy in respect of money paid or goods or services provided under the contract.[166] If, for example, money is paid in advance under a contract for the supply of goods or services, and the payer receives none of the goods or services contracted for, then the payer could recover the money in restitution on the basis that it has been paid for a consideration that has totally failed. Alternatively, the payer could claim damages for breach of contract on the basis that the other party has breached a contractual obligation to provide the goods or services.

In *Mann v Paterson Constructions Pty Ltd*, the High Court (by a majority of 4-3) confirmed that a restitutionary action is available to an aggrieved party as an alternative to contract damages where a contract has been terminated for breach. Kiefel CJ, Bell and Keane JJ dissented on this issue. Their Honours held that, although it has long been accepted that following termination for breach the aggrieved party can chose between contract damages and a restitutionary remedy with respect to services, that line of authority was based on the "rescission fallacy".[167] That is, it was based on the misconception that termination for breach renders a contract void from the beginning, rather than prospectively from the date of termination. Moreover, Kiefel CJ, Bell and Keane JJ held that to allow a restitutionary claim as an alternative to contract damages would "subvert the contractual allocation of risk"[168] and would be inconsistent with the "gap-filling and auxiliary role of restitutionary remedies".[169] The majority of the court (Gageler J and Nettle, Gordon and Edelman JJ) held that allowing a restitutionary remedy does not upset any contractual allocation of risk. That is because an award of damages for breach of contract is not "a product of the agreement", but arises "by operation of law".[170] Gageler J noted that there are procedural advantages in seeking restitution rather than damages for breach of contract, and observed that overlapping causes of action and remedies are commonplace in the common law system.[171] The availability of restitution as an alternative to contract damages in this situation "has grown up over centuries", is "widely accepted and applied in kindred jurisdictions" and is too well-established to be abrogated by judicial decision in the interests of neatness and perceived theoretical order.[172]

Gageler J observed in *Mann v Paterson Constructions Pty Ltd* that a potential problem with allowing a restitutionary claim to a party who terminates a contract for breach is that, if the value of services is determined without reference to the contract, it could create an incentive

165 On the effect of termination for breach, see also *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32.

166 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32.

167 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [7], quoting *Sopov v Kane Constructions Pty Ltd (No 2)* [2009] VSCA 141; (2009) 24 VR 510, [10].

168 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [21].

169 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [22].

170 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [195] (Nettle, Gordon and Edelman JJ), and to similar effect [83] (Gageler J).

171 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [86]–[87], [84], and to similar effect [197]–[198] (Nettle, Gordon and Edelman JJ).

172 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [199] (Nettle, Gordon and Edelman JJ).

to terminate in certain situations.[173] This would occur where a contract has been underpriced, so the party doing the work will make a loss if performance is completed.[174] It would also occur where the contract price is disproportionately weighted towards the early stages of a contract.[175] Once the more profitable stages have been completed, and a right to those higher payments has accrued, the contractor is better off terminating than performing. This creates an incentive on one side "to search out and seize upon conduct able to be characterised as a repudiation" and, on the other side, to do everything necessary to avoid default, including overperforming and taking excessive precautions.[176] The common law must, Gageler J said, address this "problem of distorted contractual incentives":[177]

> The common law rule should accordingly be that the amount recoverable on a non-contractual *quantum meruit* as remuneration for services rendered in performance of a contract prior to its termination by acceptance of a repudiation cannot exceed that portion of the contract price as is attributable to those services.[178]

Nettle, Gordon and Edelman JJ similarly held that the amount of restitution recoverable on a quantum meruit "should prima facie not exceed a fair value calculated in accordance with the contract price or an appropriate part of the contract price", but left open the possibility of a restitutionary award that exceeds the contract price where it would be "unconscionable to confine the plaintiff to the contractual measure."[179] One possible example of this is where continuing breaches by the defendant have caused a cost overrun and thereby rendered the contract unprofitable for the plaintiff.[180] Because Kiefel CJ, Bell and Keane JJ held that no restitutionary claim is available in these circumstances, it was unnecessary for them to consider whether the contract price operated as a ceiling on the amount recoverable in restitution.[181]

A final point to note is that the aggrieved party cannot recover both restitution and damages. The reason for this is that restitution removes the basis on which the payer is entitled to call for damages. In *Baltic Shipping Co v Dillon*,[182] the High Court held that Mrs Dillon was not entitled to recover both damages and restitution of her fare because she would then receive both the equivalent of contractual performance (by way of damages) and the amount paid in return for such performance (by way of restitution).

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173 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [88]–[89]

174 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [88].

175 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [88].

176 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [89].

177 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [90]; cf [52] (Kiefel CJ, Bell and Keane JJ).

178 [102]. Gageler J held that, to the extent that they allowed recovery in excess of the contract price, *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, *Iezzi Constructions Pty Ltd v Watkins Pacific (Qld) Pty Ltd* [1995] 2 Qd R 350 and *Sopov v Kane Constructions Pty Ltd [No 2]* (2009) 24 VR 510 were wrongly decided.

179 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [215]–[216]. The reasons for this were discussed at [10.49].

180 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [216]. Their Honours noted at [217] that there was no suggestion that there were any circumstances in the case before the court that warranted "departure from the prima facie position that a claimant should not achieve a better result by way of restitution than under the contract."

181 *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32, [4].

182 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, see [10.30].

Restitution for the party in breach

[10.75] Whether the party in breach can recover reasonable remuneration for services appears to depend on whether, in the circumstances, the services can be said to have been freely accepted. In *Sumpter v Hedges*,[183] a builder agreed to construct two houses and stables for a lump sum but ran out of money and abandoned the work before it was completed. The owner finished the buildings, using materials left on the site by the builder. The builder was unable to recover reasonable remuneration for the work done but was able to recover in respect of materials left on the building site and used by the owner in completing the building. The distinction is justifiable on the basis that the owner had no choice but to accept the work (and thus could not be said to have freely accepted it) but could have rejected the materials.[184] Collins LJ said that a person who has abandoned performance of a contract may recover on a quantum meruit for work done provided the circumstances are "such as to give an option to the defendant to take or not to take the benefit of the work done".[185] Where work is done on land, the owner of the land has no choice but to take the benefit of the work. Here, the defendant was "not bound to keep unfinished a building which in its incomplete state would be a nuisance on his land".[186]

The decision of the High Court in *Steele v Tardiani*[187] provides support for this focus on the issue of free acceptance where a party in breach seeks restitution, although here the contract was not terminated for breach. The plaintiffs contracted with the defendant to cut timber for firewood into lengths of a certain diameter at a certain price per ton. The plaintiffs were not employed to cut any particular amount of timber, and the contract could be terminated by either party at any time. Before leaving the defendant's employment, the plaintiffs cut a quantity of timber, mostly into lengths exceeding the required diameter. The trial judge held that the defendant was liable to pay the contract price for timber cut to the required dimensions and was liable to pay a fair price for the cutting of the remainder of the wood. The High Court upheld the conclusions of the trial judge. Simply using or selling the firewood was not enough to create a liability to pay for the work because the defendant had no choice but to use his wood; he could not be expected to let it rot on the ground.[188] But here the defendant took the benefit of the work by allowing the plaintiffs to continue splitting the timber into non-complying lengths, allowing them to leave his employment without insisting that they split the firewood to reduce its diameter and then subsequently disposing of the wood.[189] He was therefore obliged to pay reasonable remuneration for the work.

Whether the party in breach can recover payments other than a deposit made for a consideration that has totally failed is a matter of some controversy. Peter Birks and Andrew Burrows argue that a party in breach can recover payments for which consideration has

183 *Sumpter v Hedges* [1898] 1 QB 673.

184 Jones, *Goff and Jones' Law of Restitution* (7th ed, 2007), 20-047; Birks, *An Introduction to the Law of Restitution* (rev ed 1995), p 239. Cf Stevens and McFarlane, "In Defence of Sumpter v Hedges" (2002) 118 *Law Quarterly Review* 569.

185 *Sumpter v Hedges* [1898] 1 QB 673, 676.

186 *Sumpter v Hedges* [1898] 1 QB 673, 676.

187 *Steele v Tardiani* (1946) 72 CLR 386.

188 *Steele v Tardiani* (1946) 72 CLR 386, 394.

189 *Steele v Tardiani* (1946) 72 CLR 386, 403–5.

totally failed.[190] IM Jackman, on the other hand, argues that "there is ample authority to the effect that the party in breach cannot claim restitution of money paid on a total failure of consideration".[191] It is clear that a deposit paid by the party in breach may not be recovered. Since a deposit is paid as an earnest of performance, it could not be said that the consideration has failed where the contract is terminated as a result of the payer's breach.[192] It is therefore crucial for a party seeking recovery of a deposit to establish that the contract did not come to an end as a result of his or her default. In *Foran v Wight*,[193] for example, a majority of the High Court held that the sale of land contract in question had been validly terminated by the purchasers as a result of a breach by the vendors. The purchasers were therefore entitled to recover the deposit in restitution "as money paid for a consideration that had totally failed".[194] The New South Wales Court of Appeal[195] and Mason CJ in his dissenting judgment in the High Court[196] reached the conclusion that the contract had come to an end as a result of the purchasers' default and held, accordingly, that the purchasers were not entitled to recover the deposit.

Frustrated contracts

[10.80] Frustration of a contract occurs where, after the contract is made, a supervening event renders performance impossible or radically different from what the parties originally intended.[197] The effect of frustration is to terminate the contract automatically from the date the frustrating event occurs.[198] This commonly leaves a contracting party who has conferred benefits on another with no contractual right to require a return performance by the other party. In some jurisdictions, claims in relation to work done or money paid under a frustrated contract are governed by legislation.[199] In other jurisdictions, the only basis for recovering money paid or the value of work done under the contract is under the law of restitution. Money paid under a frustrated contract may be recovered if the consideration has totally failed. A reasonable sum may be recovered for services that have been requested or accepted.

A restitutionary claim arising out of a frustrated contract becomes more complicated if the plaintiff has performed only part of the work required by the contract. A restitutionary claim relating to services will not be available if the contract expressly or impliedly allocates to the plaintiff the risk of incomplete performance. In *Cutter v Powell*,[200] a sailor (Cutter) was employed to act as second mate on a ship sailing from Jamaica to Liverpool under a letter of engagement providing that he would be paid "the sum of thirty guineas, provided

190 Birks, *An Introduction to the Law of Restitution* (rev ed, 1995), pp 234–8; Burrows, *The Law of Restitution* (3rd ed, 2011), p 353.

191 Jackman, *The Varieties of the Law of Restitution* (2nd ed, 2017), p 91.

192 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 352: "There can, of course, be no [total failure of consideration] when the plaintiff's unwillingness or refusal to perform the contract on his or her part is the cause of the defendant's non-performance."

193 *Foran v Wight* (1989) 168 CLR 385.

194 *Foran v Wight* (1989) 168 CLR 385, 432, 438.

195 *Wight v Foran* (1987) 11 NSWLR 470.

196 *Foran v Wight* (1989) 168 CLR 385, 413.

197 See Chapter 15.

198 See [15.100].

199 See [15.130]–[15.150].

200 *Cutter v Powell* (1795) 6 TR 320; 101 ER 573.

he proceeds, continues and does his duty as second mate in the said ship from hence to the port of Liverpool". Cutter died approximately three-quarters of the way through the journey. Cutter's estate was unable to recover on a quantum meruit since the contract terms clearly placed the risk of non-completion on Cutter. Sailors were normally paid on a monthly basis at a much lower rate. The contract here provided that Cutter would be given a larger than normal payment "if the whole duty were performed and nothing unless the whole of that duty were performed: it was a kind of insurance".[201] This case has been treated as authority for a principle that restitution for work done under an entire contract[202] will not be available if the contract is frustrated before the performance is complete.[203] The better view, however, is that the "entire contract" doctrine precludes only a claim *for the contract price*. If the contract is frustrated before performance is completed, a claim to recover reasonable remuneration *in restitution* is possible, provided the contract does not allocate the risk of incomplete performance to the plaintiff.[204] As to whether restitutionary relief is available, it will also depend on proof that the defendant has requested or freely accepted the services.

The leading case on restitution for benefits conferred under a frustrated contract is *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd*.[205] That case involved a contract under which an English company agreed to manufacture and deliver certain machinery to a Polish company. The buyer paid £1000 towards the purchase price shortly after the contract was made. Some weeks later, the contract was frustrated by the outbreak of the World War II; because Germany had invaded Poland and Great Britain had declared war on Germany, it was not possible to perform the contract. The buyer sought recovery of the £1000. The seller refused to return it because it had begun manufacturing the machinery. The House of Lords held that, in the absence of a contract term dealing with the matter, the money was recoverable. The buyer's claim was not on the contract itself, but a claim to "to get the money back, on the ground that the consideration for it has totally failed". The law provides a remedy in restitution "to the party who has not got that for which he bargained".[206] It did not matter that the seller was not at fault. Nor did it matter that the seller had provided valuable consideration in the contract formation sense by promising to manufacture the machinery. Nor did it matter that the seller had incurred expenditure in carrying out the contract. The payment was recoverable because the buyer had not received the performance for which it was made, which was the delivery of the machinery.

Unenforceable contracts

[10.85] A claim in restitution may be made in respect of money paid or services rendered under a contract that is rendered unenforceable by legislation such as the *Statute of Frauds*,[207]

201 *Cutter v Powell* (1795) 6 TR 320; 101 ER 573, 576.

202 An entire contract is one that requires a party to perform his or her obligations in full before he or she will be entitled to payment: see further at [29.15].

203 For example, *Appleby v Myers* (1867) LR 2 CP 651.

204 Jones, *Goff and Jones' Law of Restitution* (7th ed, 2007), 20-004 to 20-006; Mason, Carter and Tolhurst, *Mason & Carter's Restitution Law in Australia* (3rd ed, 2016), [933] and [1231].

205 *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32, see further at [15.110].

206 *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32, 46 (Viscount Simons LC used the expression "quasi-contract" rather than "restitution").

207 See Chapter 7.

provided the restitutionary claim is not barred by the legislation. In *Pavey & Matthews Pty Ltd v Paul*,[208] a restitutionary claim was allowed in respect of work done under a contract which was unenforceable under legislation.[209] Section 45 of the *Builders Licensing Act 1971* (NSW) provided that a contract by which a licensed builder agrees to carry out building work was "not enforceable against the other party" unless it was in writing and signed. A crucial issue for the High Court was whether a restitutionary claim amounted to "enforcement" of the contract. The court answered this question by reference to the purpose of s 45. Mason and Wilson JJ considered that the purpose of s 45 was either to protect the building owner against spurious claims by builders or to ensure both precision in house-building contracts and that they are covered by insurance arrangements. Allowing a restitutionary claim in respect of work which had been completed and accepted by the building owner did not undermine those purposes.[210] In *Sutton v Zullo Enterprises Pty Ltd*,[211] on the other hand, the relevant legislation provided that a person carrying out building work without a licence "is not entitled to any monetary or other consideration for doing so". The Queensland Court of Appeal held that this provision precluded a restitutionary claim being made in respect of such work.[212]

Illegal contracts

[10.90] As we will see in Chapters 40–41, some contracts are unenforceable because they are expressly or impliedly prohibited by statute, while others are unenforceable because they infringe a recognised principle of public policy. In some circumstances, a restitutionary claim may be available to a party who has made a payment or performed services under a contract that is unenforceable because of illegality. Illegality has been mentioned, alongside mistake and duress, as a vitiating factor that may enliven a restitutionary action.[213] Often, however, illegality will also provide a defence to a restitutionary claim, as discussed at [10.110].

MISTAKE

[10.95] Money paid by one contracting party to another may be recovered where it was paid under a mistake of fact or law, in circumstances where the mistake can be regarded as the cause of the payment. In *Kelly v Solari*,[214] for example, payment was made on the basis of a mistake that a contract existed. An insurer paid benefits under a life insurance policy having forgotten that the policy had lapsed for non-payment of the premiums. The insurer failed at first instance. The Court of Exchequer ordered a new trial on the basis that the recipient of money paid under a mistake of fact is obliged to repay it, however careless the payer might have been. The payment is not recoverable, though, if "it is intentionally paid, without reference to the truth or falsehood of the fact, the plaintiff meaning to waive all inquiry into

208 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221.

209 See [10.10].

210 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 228–30, 262. Cf Brennan J at 244.

211 *Sutton v Zullo Enterprises Pty Ltd* [2000] 2 Qd R 196.

212 The legislation in question provided that an unregistered person "must not carry out … building work" so the contract in question here was *illegal* rather than merely *unenforceable*.

213 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353, 379; *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [101].

214 *Kelly v Solari* (1841) 9 M&W 54; 152 ER 24.

it, and that the person receiving shall have the money at all events, whether the fact be true or false".[215]

David Securities Pty Ltd v Commonwealth Bank of Australia Ltd[216] involved a claim to recover money paid under a void contractual provision. David Securities borrowed money from the Commonwealth Bank through its Singapore branch. The loan agreement included a "grossing up" provision in cl 8(b), which required the borrower to pay to the bank any additional amounts necessary to meet any tax obligations and ensure that the bank would receive the full amount of interest payable under the loan agreement. David Securities paid additional sums to the bank in accordance with cl 8(b), without knowing that s 261 of the *Income Tax Assessment Act 1936* (Cth) rendered void any provision in a mortgage or collateral agreement requiring the mortgagor to pay income tax on the interest paid under the mortgage. David Securities sought to recover the amounts paid to the bank under cl 8(b) on the basis that they had been paid under a mistake. The Federal Court of Australia held that no action was available to recover money paid under a mistake of law. The High Court held that the cases applying this principle were based on weak foundations and should no longer be followed. The court noted that the rule denying recovery of money paid under a mistake of fact had been thoroughly criticized by judges and scholars. Moreover, the distinction between mistake of law and mistake of fact was unsustainable in light of the recognition of the principle of unjust enrichment in *Pavey & Matthews Pty Ltd v Paul*.[217] Mason CJ, Deane, Toohey, Gaudron and McHugh JJ said:

> If the ground for ordering recovery is that the defendant has been unjustly enriched, there is no justification for drawing distinctions on the basis of how the enrichment was gained, except in so far as the manner of gaining the enrichment bears upon the justice of the case.[218]

The court in *David Securities v Commonwealth Bank* rejected suggestions that the mistake must in some way be "fundamental" or that the claimant must establish "unjustness" in addition to the mistake. The fact that a payment was made under a mistake of fact or law makes its retention unjust and "is sufficient to give rise to a prima facie obligation on the part of the [recipient] to make restitution".[219] It was necessary for the High Court to remit the matter to the trial judge to make some additional determinations of fact. Because the trial judge had dismissed the claim on the basis that payments made under a mistake of law were not recoverable, two relevant factual questions had not been determined. First, it was necessary to consider whether the mistake was causative, that is, whether the borrowers had paid the additional amounts *because* of their mistaken belief that the loan agreement required them to make the payments. Secondly, the High Court held that a defence was potentially available to the bank if the bank could show that it had detrimentally changed its position on the faith of the payments. The bank might, for example, have exercised a contractual right to demand earlier repayment of the loan, and thereby reduced its withholding tax liability, had it known it was obliged to repay the amounts received under cl 8(b).[220]

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215 *Kelly v Solari* (1841) 9 M&W 54; 152 ER 24, 26.

216 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353.

217 *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221.

218 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353, 375; see also at 455, 459.

219 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353, 379.

220 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353, 386. See further at [10.115].

DURESS OR COMPULSION

[10.100] A restitutionary claim is available in respect of benefits conferred under duress, or compulsion as it was called in the older cases. There is a clear parallel between an award of restitution for benefits conferred under duress and setting aside a contract made under duress.[221] Indeed, rescission of a contract for duress can be seen as an instance of restitution for unjust enrichment.[222] A person who procures a contract by applying improper pressure to another person may be seen to have been unjustly enriched through the acquisition of the contractual rights. That enrichment is reversed through the remedy of rescission: the contract is set aside and the parties are restored to their original positions.

In *Smith v William Charlick Ltd*, Isaacs J said:

> "Compulsion" in relation to a payment of which refund is sought, and whether it is also variously called "coercion", "extortion," "exaction," or "force," includes every species of duress or conduct analogous to duress, actual or threatened, exerted by or on behalf of the payee and applied to the person or the property or any right of the person who pays or, in some cases, of a person related to or in affinity with him. Such compulsion is a legal wrong, and the law provides a remedy by raising a fictional promise to repay.[223]

This statement recognises three different types of pressure that will justify a restitutionary claim: (a) a threat to cause harm to a person; (b) a threat to cause harm to property and (c) a threat to infringe a person's legal rights. These categories coincide with the categories of duress that will justify rescission of a contract,[224] with the third category covering what is now sometimes called *economic duress*. The modern cases suggest that duress is not limited to these categories and any "illegitimate" pressure may amount to duress.[225] McHugh JA said in *Crescendo Management Pty Ltd v Westpac Banking Corporation* that: "Pressure will be illegitimate if it consists of unlawful threats or amounts to unconscionable conduct."[226]

A threat not to enter into a contract will not usually be regarded as illegitimate pressure. In *Smith v William Charlick Ltd*, the Wheat Harvest Board (a statutory monopolist) demanded that a miller pay a surcharge on wheat that the miller had purchased previously and stockpiled. The Board had no right to demand the payment but did so because the price of wheat had risen and the Board thought the miller should pay the extra amount that would then have been payable to buy the stockpiled wheat. The miller initially refused to pay but capitulated when the Board threatened to withhold further supplies. The High Court held that the payment was not recoverable. The miller made the payment with full knowledge of the facts and the legal rights of the parties "in order to induce the Board to do that which it was under no legal obligation to do".[227] Isaacs J said:

221 See *Hawker Pacific Pty Ltd v Helicopter Charter Pty Ltd* (1991) 22 NSWLR 298, 302, 306.

222 Cf Tamblyn, "Separating Rescission and Restitution" (2016) 33 *Journal of Contract Law* 135.

223 *Smith v William Charlick Ltd* (1924) 34 CLR 38, 56.

224 See Chapter 34.

225 *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 NSWLR 40, 45–6. See further Mitchell, Mitchell and Watterson, *Goff and Jones: The Law of Unjust Enrichment* (9th ed, 2016), Ch 10 and Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), Ch 9.

226 *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 NSWLR 40, 46.

227 *Smith v William Charlick Ltd* (1924) 34 CLR 38, 51.

> It is plain that a mere abstention from selling goods to a man except on condition of his making a stated payment cannot, in the absence of some special relation, answer the description of "compulsion", however serious his situation arising from other circumstances may be.[228]

Birks suggests that the case might be decided differently today.[229] It could be argued that the pressure applied by the Board was illegitimate or unconscionable because the Board had improperly exploited its monopoly power.

A threat to breach a contract generally will be regarded as illegitimate pressure. In *TA Sundell & Sons Pty Ltd v Emm Yannoulatos (Overseas) Pty Ltd*,[230] a sum paid in response to a threat to breach a contract was held to be recoverable. The parties entered into a contract for the sale of galvanized iron at £109 per ton, with payment to be made by letter of credit. After the contract was made the seller demanded a price increase on the basis of "fantastic rises in the price of zinc". The buyer did not accept that the seller had the right to increase the price but urgently required the iron for building work. The buyer therefore increased the letter of credit but insisted that it was doing so without prejudice to its rights. After the iron was delivered, and payment made to the seller under the letter of credit, the buyer sought to recover from the seller the difference between the contract price and the price paid. The court held that any promise by the buyer to pay the higher price did not give rise to a contract of variation because of a lack of consideration.[231] It was held that the buyer provided the additional funds under a threat that the iron would not be delivered if it failed to do so. This "threat to refrain from performing a contractual duty" was sufficient compulsion to justify recovery of the payment.[232]

DEFENCES

[10.105] In *Moses v Macfarlan*, Lord Mansfield said that in an action for money had and received, a defendant "may defend himself by every thing which shews that the plaintiff, ex æquo & bono, is not intitled to the whole of his demand, or to any part of it".[233] In *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd*, French CJ embraced this open-ended statement, and with it the idea that it is not possible to make a comprehensive statement of all possible defences to restitutionary claims.[234] The number and scope of available defences remain matters of considerable debate and uncertainty. A good illustration of a case in which no recognised defence was available but where it was nevertheless unjust to require restitution is *Ford v Perpetual Trustees Victoria Ltd*.[235] Mr Ford was intellectually impaired and illiterate. Mr Ford's son took advantage of his father's condition by arranging the purchase in his father's name of a cleaning business which the son planned to operate entirely for his own benefit. The

228 *Smith v William Charlick Ltd* (1924) 34 CLR 38, 56.

229 Birks, *An Introduction to the Law of Restitution* (rev ed, 1989), p 178; cf Mason, Carter and Tolhurst, *Mason & Carter's Restitution Law in Australia* (3rd ed, 2016), [516].

230 *TA Sundell & Sons Pty Ltd v Emm Yannoulatos (Overseas) Pty Ltd* [1956] SR (NSW) 323.

231 Compare the cases discussed at [4.85].

232 *TA Sundell & Sons Pty Ltd v Emm Yannoulatos (Overseas) Pty Ltd* [1956] SR (NSW) 323, 326–8.

233 *Moses v Macfarlan* (1760) 2 Burr 1005; 97 ER 676, 679 ("ex aequo et bono" means according to equity and good conscience, or, what is fair and just).

234 *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd* [2014] HCA 14; (2014) 253 CLR 560, [5]–[6].

235 *Ford v Perpetual Trustees Victoria Ltd* [2009] NSWCA 186; (2009) 75 NSWLR 42.

son also arranged a loan in his father's name to finance the purchase. The bulk of the loan money was paid by the lender to the vendors of the business in satisfaction of the purchase price. Although the relevant documents were signed by Mr Ford, he did not understand them. When the business failed, the lender sought to recover the loan from Mr Ford. The trial judge held that the loan agreement was void under the non est factum doctrine,[236] but Mr Ford was liable to make restitution because the loan money was paid under the mistaken assumption that the loan agreement was valid, and the payment enriched Mr Ford because it was used to discharge his liability to the vendors of the business. An appeal was allowed. The Court of Appeal held that the fact that the money was paid under a mistake gave rise to a prima facie right to recovery but did not end the inquiry as to whether justice required that Mr Ford repay the amount of the loan. Although the lender's payment to the vendors of the business benefited Mr Ford in a technical sense by discharging his obligation to the vendors under the purchase contract, "in no real or substantive sense did he receive and retain benefits such that it would be unjust for him not to repay the loan".[237]

Illegality

[10.110] As noted at [10.90], a restitutionary claim may be available to a party who has made a payment or performed services under a contract that is void or unenforceable because of illegality. Illegality may, however, also provide a defence to a restitutionary claim. Whether a restitutionary claim will be barred by illegality depends on whether allowing it would undermine the coherence of the law or stultify the purpose of the prohibition. That was the principle applied by the High Court in *Equuscorp Pty Ltd v Haxton*.[238] That case concerned an action to recover money lent pursuant to a failed investment scheme. Investors purchased interests in a blueberry farming business under a scheme that promised immediate tax deductions, as well as future profits and capital growth. The investors' participation in the scheme was funded by loans provided by a company associated with the promoter of the scheme. When the scheme failed, the lender assigned its rights against the investors to Equuscorp. The loan agreements were held to be unenforceable because they were made in furtherance of an illegal purpose. It was unlawful under the Companies Codes to offer such investments without registering a prospectus providing prescribed information about the investments, and no prospectus was registered. The policy of the legislation was to protect potential investors by ensuring that sufficient information was provided to allow them to make informed decisions.

The question for the High Court was whether the amount lent could be recovered from the investors as money paid for a consideration that has totally failed. This was held to be a question of public policy. It depended on whether allowing the restitutionary claim would undermine the coherence of the law or stultify the statutory purpose.[239] In other words, the question was whether granting restitution would defeat or frustrate the policy of the statute.[240]

236 See [31.90].

237 *Ford v Perpetual Trustees Victoria Ltd* [2009] NSWCA 186; (2009) 75 NSWLR 42, [127].

238 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498.

239 Cf *Patel v Mirza* [2016] UKSC 42; [2017] AC 467, esp at [120].

240 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [38], [104] (quoting American Law Institute, *Third Restatement on Restitution and Unjust Enrichment* (2011), §32(2)), [111].

Here, the lender (Rural) was "not an arms' length financier" but was "part of the closely related group of companies that were involved in the promotion of the schemes".[241] By making the investments more attractive, the loans furthered the illegal purpose of offering "prescribed interests" to investors without the protection of a prospectus. Moreover, restitution was sought in this case from members of the class of persons whom the legislation was intended to protect, namely investors.[242]

> The respondents were not in pari delicto with Rural. The failure of consideration invoked by Equuscorp was the product of Rural's own conduct in offering the loan agreements in furtherance of an illegal purpose. This is a clear case in which the coherence of the law, and the avoidance of stultification of the statutory purpose by the common law, lead to the conclusion that Rural did not have a right to claim recovery of money advanced under the loan agreements as money had and received. There was therefore no right to claim such relief available for assignment to Equuscorp.[243]

Equuscorp Pty Ltd v Haxton can be contrasted with *Patel v Mirza*,[244] in which the Supreme Court of the United Kingdom held that money paid for an illegal purpose was recoverable despite the illegality. The plaintiff paid £620,000 to the defendant for the purpose of engaging in insider trading in shares, which is prohibited by statute. The defendant did not receive the information that was expected to affect the price of the shares in question, so the scheme was not carried into effect. The plaintiff sought to recover the money on the basis of failure of consideration. As discussed at [42.80], the Supreme Court sat as a panel of nine judges in *Patel v Mirza* in order to review the law relating to the illegality defence, which was widely considered to be in an unsatisfactory state. A majority of the Supreme Court supported the adoption of a broad, policy-based approach. The Court held that the plaintiff should not be denied restitution on the basis that the money had been paid for an illegal purpose. The essential concern in illegality cases, Lord Toulson said, is whether allowing recovery would render the law incoherent and "self-defeating, condoning illegality by giving with the left hand what it takes with the right hand."[245] The crucial question in a given case was therefore whether it would be harmful to the public interest (focused on the integrity of the legal system and possibly also public morality) to allow recovery. The answer to that question required consideration of the purpose of the prohibition, whether that purpose would be enhanced by denying the claim, whether denial of the claim would be a proportionate response to the illegality, and any other public policy that would be affected by denying the claim.[246] It was held that denying the claim would not advance the purpose of the statutory prohibition on insider trading and would not be a "just and proportionate response to the illegality."[247]

241 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [45].

242 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [45], [108]–[109].

243 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [45].

244 *Patel v Mirza* [2016] UKSC 42; [2017] AC 467.

245 *Patel v Mirza* [2016] UKSC 42; [2017] AC 467, [99] and [120] (Lord Toulson, with whom Baroness Hale, Lord Kerr, Lord Wilson and Lord Hodge agreed).

246 *Patel v Mirza* [2016] UKSC 42; [2017] AC 467, [120]

247 *Patel v Mirza* [2016] UKSC 42; [2017] AC 467, [115] and [121].

Change of position

[10.115] A second defence to a restitutionary claim operates where the defendant has detrimentally changed his or her position in good faith in reliance on the payment.[248] This defence operates pro tanto (to an extent): the defendant's obligation to make restitution is reduced only to the extent of the detriment suffered by the defendant as a result of his or her change of position. Assume, for example, that A credits $1000 to B's bank account by mistake and B, honestly believing the money is hers and that she now has some money to spare, gives $400 to a charity. As a result of B's change of position, she is obliged to repay only $600 to A. In *David Securities v Commonwealth Bank*, the High Court observed that if payments made under mistake of law are to be prima facie recoverable, then "a defence of change of position is necessary to ensure that enrichment of the recipient of the payment is prevented only in the circumstances where it would be unjust".[249] The High Court suggested in *David Securities v Commonwealth Bank* that the change of position must involve some "expenditure or financial commitment which can be ascribed to the mistaken payment" and this does not include spending the money "on ordinary living expenses".[250] In that case, the borrower of money paid amounts to the lending bank on the mistaken assumption that the borrower was required to do so under the terms of the loan agreement.[251] In fact, the relevant provision of the loan agreement was rendered void by statute. The bank argued that it might have terminated the agreement earlier had it known the payments were recoverable by the borrower. The bank had "rolled over" or renewed the loan a number of times when it was not bound to do so. The High Court held that there was insufficient evidence before the court to establish the defence and remitted the matter to the trial judge to determine whether the bank had changed its position on the faith of the payments.

The requirement that the change of position must be made "on the faith of" the payment carries with it the notion that the defendant must have acted on the assumption that he or she was entitled to the payment. Edelman and Bant note that the way the defence was framed by the High Court in as *David Securities* limits it to changes of position instigated by the defendant in reliance on the payment.[252] It has been accepted in England that the defence should be available where the defendant's position has changed in such a way as to make it detrimental to have to make restitution, but without any reliance by the defendant, such as where the money has been stolen from the defendant.[253] Gageler J indicated in *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd* that an intervening theft may not provide a defence,[254] but the matter has not been fully considered by an Australian court and there is scholarly support for the adoption of the English approach.[255]

248 This defence also operates pursuant to legislation in Western Australia: *Property Law Act 1969*, s 125(1) in relation to claims to recover money paid under a mistake. See further Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), pp 359–62.

249 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353, 385.

250 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353, 385–6.

251 See [10.95].

252 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), 339–40.

253 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), 340–1.

254 *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd* [2014] HCA 14; (2014) 253 CLR 560, [142].

255 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), 340–1.

It is well accepted that, in order to establish the defence, the change of position must have been made "in good faith".[256] Good faith requires that the defendant had some reason to believe that he or she was entitled to the payment or, in the case of an intermediary such as a bank, some reason to believe that it was entitled to deal with the payment.[257] A recipient who parts with money knowing the payment was made under a mistake cannot take advantage of the defence.[258] A recipient who has reason to believe that "the payment may have been made under a mistake, but cannot be sure" may be found not to have acted in good faith if he or she fails to make inquiries before changing his or her position.[259] It has been held in Victoria that a recipient who willfully or recklessly failed to make the inquiries that a reasonable person would make in the circumstances was not acting in good faith and was not entitled to rely on the change of position defence.[260]

The change of position that is required to establish the defence is closely analogous to the detrimental reliance required for estoppel, though here of course the assumption that is acted upon has not been induced by the other party. In *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd*, the High Court recognised that a change of position must be detrimental but need not involve "expenditure or financial commitment".[261] TCP was in financial difficulties and owed money to Hills and Bosch. AFSL was induced by fraud on the part of TCP to make payments to Hills and Bosch to purchase equipment which AFSL intended to lease to TCP. In fact, the equipment did not exist and the documentation was forged. Hills and Bosch received the payments in good faith, treated TCP's indebtedness as extinguished, ceased recovery action and began to trade with TCP. TCP later became insolvent and went into liquidation. After discovering the fraud, AFSL sought to recover the money paid to Hills and Bosch on the basis that it had been paid under a mistake of fact. Hills and Bosch claimed to have changed their positions on the faith of the payments. AFSL argued that Hills and Bosch suffered no detriment as a result of their changes of position because the debts were in any case irrecoverable due to TCP's insolvency. The High Court held that the change of position defence operates where it is inequitable or unconscionable to require the recipient of a mistaken payment to repay it. Detriment resulting from the change of position is required, but as in estoppel, "detriment is not a narrow or technical concept" and a quantifiable financial detriment is not required.[262] "[U]nder Australian law a mathematical assessment of enduring economic benefit does not determine the availability of restitutionary remedies."[263] Here, discharging the debts and continuing to trade with TCP would place Hills and Bosch in

256 *David Securities v Commonwealth Bank* (1992) 175 CLR 353, 379–80.

257 *Perpetual Trustees Australia Ltd v Heperu Pty Ltd* [2009] NSWCA 84; (2009) 76 NSWLR 195, [139]: "a payee must know more than the fact of mere receipt. It must have information that entitles it (on the basis of the information) to deal with the receipt."

258 *Niru Battery Manufacturing Co v Milestone Trading Ltd* [2003] EWCACiv 1446; [2004] QB 985, [164] (quoting and approving Moore-Bick J at first instance: [2002] EWHC 1425 (Comm), [135]).

259 *Niru Battery Manufacturing Co v Milestone Trading Ltd* [2003] EWCACiv 1446; [2004] QB 985, [164] (quoting and approving Moore-Bick J at first instance: [2002] EWHC 1425 (Comm), [135]).

260 *Sino Iron Pty Ltd v Worldwide Wagering Pty Ltd* [2017] VSC 101; (2017) 52 VR 664.

261 *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd* [2014] HCA 14; (2014) 253 CLR 560, [82].

262 *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd* [2014] HCA 14; (2014) 253 CLR 560, [25], [88], [150].

263 *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd* [2014] HCA 14; (2014) 253 CLR 560, [84].

a disadvantageous position if they were to be required to repay the money, and this made it inequitable to require repayment.[264]

The scope of application of the change of position defence is unclear.[265] While change of position certainly operates as a defence to a claim to recover money paid under a mistake, it is not clear what other restitutionary claims it may affect. If change of position can operate as a defence to a claim based on total failure of consideration, then this would significantly affect the outcome of a case such as *Fibrosa v Fairbairn*.[266] Edelman and Bant argue that, while a change of position is "a general defence to claims in unjust enrichment", the good faith requirement will be difficult to satisfy in cases other than those involving mistaken payments.[267] A person who procures a payment through duress will almost always have knowledge of the circumstances rendering the enrichment unjust, so any change of position will not be made in good faith.[268] In most failure of consideration cases, the defendant will know the enrichment was conferred conditionally and will not, in good faith, be able to treat it as if it were not.[269]

In *Lumbers v W Cook Builders Pty Ltd*,[270] a change of position was one of the factors that were said to be "neither necessary nor appropriate to consider" in relation to a claim with respect to money paid or services provided at the request of another. On that basis, the Queensland Court of Appeal has held that an attempt to plead a change of position in a defence to a claim with respect to work done at the request of the defendant should be struck out.[271] Philippides JA said that, since the various restitutionary actions are distinct causes of action with distinct elements and defences, "principles relevant to the right of action for money had and received are not able to be transplanted to the right of action for work done at the request of another".[272]

Estoppel

[10.120] Like change of position, estoppel is concerned with detrimental reliance. The difference is that change of position is concerned with detrimental reliance on the faith of the relevant payment, while estoppel is concerned with detrimental reliance on the faith of an assumption induced by the payer's conduct.[273] In *Avon County Council v Howlett*,[274] the Council sought to recover payments of £1007 mistakenly made to its employee. When the employee queried the payments, he was led to believe that he was entitled to treat the money as his own. In reliance on that representation, the employee spent some of the

264 *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd* [2014] HCA 14; (2014) 253 CLR 560, [95]–[96].

265 See Bant, *The Defence of Change of Position* (2009), Ch 7.

266 *Fibrosa v Fairbairn* [1943] AC 32, discussed above [10.80]. See Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 353.

267 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 353.

268 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 352.

269 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 353.

270 *Lumbers v W Cook Builders Pty Ltd (in liq)* [2008] HCA 27; (2008) 232 CLR 635, [88]–[90].

271 *Sunwater Ltd v Drake Coal Pty Ltd* [2016] QCA 255; [2017] 2 Qd R 109.

272 *Sunwater Ltd v Drake Coal Pty Ltd* [2016] QCA 255; [2017] 2 Qd R 109, [19].

273 See Chapter 9.

274 *Avon County Council v Howlett* [1983] 1 WLR 605, discussed at [9.105].

money on things he would not otherwise have bought and omitted to claim social security payments to which he would have been entitled had he not been receiving the mistaken payments. The trial judge held that the Council's restitutionary claim was barred to the extent of the employee's expenditure and lost social security payments (totalling £546). The English Court of Appeal held that estoppel by representation could not operate pro tanto (ie, to an extent). It operated as a complete defence to the Council's claim because its effect was "simply to preclude the representor from averring facts contrary to his own representation".[275]

The defence of estoppel by representation does not sit entirely comfortably with the change of position defence. Some fact situations will attract the operation of both defences and they can yield different results. If the facts of *Avon County Council v Howlett* occurred in Australia today, the employee could rely on a change of position defence to bar the claim only to the extent of his detriment but could rely on common law estoppel to bar the claim entirely. In an English case, the conflict was resolved by refusing to allow the defendant to rely on estoppel. The court held that "it would be unconscionable, or clearly inequitable, to allow the defendant to keep the whole of the overpayment of £172,451 when his detriment is limited to £9662 of that amount".[276] A further complication in Australia is that if the payee relied on *equitable estoppel*, rather than estoppel by representation (perhaps on the basis of a representation by the payer that it would not enforce its right to payment), the court would exercise a discretion in determining the appropriate remedy to give effect to the estoppel and could well exercise that discretion by barring the restitutionary claim only to the extent of the expenditure.[277]

In *TRA Global Pty Ltd v Kebakoska*, it was held that the change of position defence has not displaced estoppel by representation, and the latter "persists as a potential separate defence to a claim for restitution of money paid out by mistake".[278] An employer made a redundancy payment to an employee under the mistaken belief that it was under a legal obligation to do so.[279] The employee was told, wrongly, that the redundancy payment was made in accordance with a particular Federal Award. The employee subsequently disclosed the payment when making an application to the relevant government agency for unemployment benefits and was denied those benefits in consequence of having received the payment. The employer later sought to recover the payment. Because the employee had changed her position on the faith of the payment, the defence of change of position was held to be available to the extent of the unemployment benefits foregone. Osborn J held that the defence of estoppel by representation was also available on the facts and operated as a complete defence, as it did in *Avon County Council v Howlett*, and not pro-tanto. The availability of the change of position defence did not prevent the employee from relying on the more effective defence of estoppel by representation.

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275 *Avon County Council v Howlett* [1983] 1 WLR 605, 622.

276 *Scottish Equitable plc v Derby* [2000] 3 All ER 793, 806, criticized by Mitchell, "Unjust Enrichment" in Burrows (ed), *English Private Law* (2nd ed, 2007), [18.268]. See also Bryan, "Mistaken Payments and the Law of Unjust Enrichment" (1993) 15 *Sydney Law Review* 461, 487–90.

277 See [9.110]–[9.140].

278 *TRA Global Pty Ltd v Kebakoska* [2011] VSC 480, [78]. See also *National Westminster Bank v Somer International Ltd* [2001] EWCA 970; [2002] QB 1286.

279 *TRA Global Pty Ltd v Kebakoska* [2011] VSC 480.

Voluntary settlement of an honest claim

[10.125] Another defence to a claim to recover money paid under a mistake of law is that the plaintiff paid the money voluntarily, in settlement of an honest claim. The rationale of this defence is that sometimes payments are made without a full understanding of the respective legal rights of the parties in order to finalise a claim. In *David Securities v Commonwealth Bank*,[280] the majority of the High Court justified the "mistake of law" principle on the basis that the denial of restitution in an earlier case[281] could be attributed to a principle that payments made in voluntary settlement of an honest claim were irrecoverable. Their Honours said:

> The payment is voluntary or there is an election if the plaintiff chooses to make the payment even though he or she believes a particular law or contractual provision requiring the payment is, or may be, invalid, or is not concerned to query whether payment is legally required; he or she is prepared to assume the validity of the obligation, or is prepared to make the payment irrespective of the validity or invalidity of the obligation, rather than contest the claim for payment. We use the term "voluntary" therefore to refer to a payment made in satisfaction of an honest claim, rather than a payment not made under any form of compulsion or undue influence.[282]

The voluntary payment defence cannot be invoked against a person who makes a payment in total ignorance of the fact that the sum may not be payable. If the defence did operate in these circumstances, then it would overwhelm the right to restitution of money paid under a mistake of law.[283] The defence is limited to situations in which the payer has made a decision to pay, irrespective of whether he or she is liable to pay or not. The approach the courts have taken is consistent with Michael Bryan's suggestion that recovery should be denied only when the payer can be said to have *assumed the risk* of invalidity of the charge.[284] In *Hollis v Atherton Shire Council*,[285] Jones J took the view that choice is the essential element of the defence and therefore rejected an argument that the defence can apply wherever the payer is not concerned to query the payment. This narrow interpretation of the defence is also consistent with the decision in *Riessen v State of South Australia*.[286] The plaintiff in that case sought to recover a speeding fine, which she claimed to have paid under a mistake as to the validity of the "school speed zones" scheme under which she was fined. Martin J held that the scheme was valid and there was no right to restitution. He said that any restitutionary claim was, in any case, defeated by the defence of voluntary settlement. The plaintiff was aware that the legality of the "school speed zones" scheme under which she was fined was being challenged by others but decided to pay the fine rather than challenge its validity "because she thought she was not likely to win and it could have been expensive".[287] She chose to pay the fine "after considering her options and making a calculated decision on pragmatic grounds".[288]

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280 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353, 372–6.

281 *South Australian Cold Stores Ltd v Electricity Trust of South Australia* (1957) 98 CLR 65.

282 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353, 373–4 (Mason CJ, Deane, Toohey, Gaudron and McHugh JJ). Brennan J took a different approach (at 396–400).

283 Bryan, "Mistaken Payments and the Law of Unjust Enrichment" (1993) 15 *Sydney Law Review* 461, 481–2. A similar point was made in *Hookway v Racing Victoria Ltd* [2005] VSCA 310; (2005) 13 VR 444, 457.

284 Bryan, "Mistaken Payments and the Law of Unjust Enrichment" (1993) 15 *Sydney Law Review* 461, 483.

285 *Hollis v Atherton Shire Council* [2003] QSC 147, [23].

286 *Riessen v State of South Australia* [2001] SASC 71; (2001) 79 SASR 82.

287 *Riessen v State of South Australia* [2001] SASC 71; (2001) 79 SASR 82, 89.

288 *Riessen v State of South Australia* [2001] SASC 71; (2001) 79 SASR 82, 90.

A similar approach was taken by the Victorian Court of Appeal in *Hookway v Racing Victoria Ltd*.[289] Following a horse race, a stewards' inquiry was conducted as to whether a prohibited substance had been administered to the winner (Mistegic). When the stewards disqualified the winning horse, Racing Victoria paid out the prize money to Mr Hookway, the owner of the horse that ran second (Windigo). At the time the payment was made, the relevant officer of Racing Victoria (Mr Chung) was unaware that recent changes to the local rules of racing provided a right of appeal against the stewards' disqualification decision. The owners of Mistegic successfully appealed against its disqualification. Racing Victoria then sought to recover the overpayment made to Hookway. The Court of Appeal held that the money had been paid under a mistake of law. The defence of voluntary payment was not applicable here, even though Hookway made no demand for payment and Chung made a free and deliberate choice to pay, without any external pressure.[290] Ormiston J held that a person who makes a payment in ignorance of the basis of invalidity of their liability cannot be treated as having made the payment voluntarily.[291] The defence of voluntary payment operates only where a person makes a conscious decision to make the payment regardless of whether he or she is under a legal obligation to pay.

The making of a protest at the time money is paid will provide evidence that the payment is not being made in voluntary settlement of the claim, but is not conclusive:

> A protest at the time of payment may of course "afford some evidence, when accompanied by other circumstances, that the payment was not voluntarily made to end the matter"… But there is no magic in a protest; for a protest may accompany a voluntary payment or be absent from one compelled. … Moreover the word protest is itself equivocal. It may mean the serious assertion of a right or it may mean no more than a statement that payment is grudgingly made.[292]

Good consideration

[10.130] Where money is paid under a mistake it may be a defence to say that the plaintiff has received good consideration for the payment. In *David Securities v Commonwealth Bank*,[293] the bank relied on this defence, arguing that the borrowers had received good consideration for the payments they made because the bank would have charged a higher rate of interest had it known that the amounts in question were not payable. "By not being charged this higher interest, the appellants have received consideration for the bargain."[294] The High Court accepted that good consideration is a defence but held that it was not made out here. In order to make out this defence, the bank would need to show that the borrowers received consideration "for the payments under cl 8(b)", which the bank was not able to do.[295] The loan agreement clearly separated out the payments to be made by the borrowers under cl 8(b) from the interest payments the borrowers were required to make. The bank had therefore

289 *Hookway v Racing Victoria Ltd* [2005] VSCA 310; (2005) 13 VR 444.

290 See *Hookway v Racing Victoria Ltd* [2005] VSCA 310; (2005) 13 VR 444, 451.

291 *Hookway v Racing Victoria Ltd* [2005] VSCA 310; (2005) 13 VR 444, 463.

292 *Mason v The State of New South Wales* (1959) 102 CLR 108, 143, quoting *Maskell v Horner* [1915] 3 KB 106, 120.

293 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353.

294 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353, 380.

295 *David Securities Pty Ltd v Commonwealth Bank of Australia Ltd* (1992) 175 CLR 353, 383.

failed to establish that the borrowers had received any consideration for the amounts payable under cl 8(b).

The defence was made out in *Ovidio Carrideo Nominees Pty Ltd v The Dog Depot Pty Ltd*.[296] The tenant of retail premises sought to recover certain rental payments it had made to its landlord. The *Retail Tenancies Reform Act 1998* (Vic) required the landlord to provide a disclosure statement to the tenant at least seven days before the tenant entered into the lease. The legislation provided that if the disclosure statement was not provided before the lease was entered into, then the tenant was entitled to withhold rent until after the statement had been given, and the tenant was not liable to pay the rent attributable to the period before the statement was given. The landlord neglected to provide the statement until more than two years after the lease was entered into. The tenant sought to recover the amount of the rental payments it had made during that period as money paid under a mistake of law. The landlord conceded that the tenant had a prima facie right to recover the payments, since the tenant made the payments in ignorance of its right to withhold them. The Victorian Court of Appeal held, however, that the landlord had a good defence to the restitutionary claim. The tenant had received good consideration for the payments, in the form of exclusive possession of the demised premises, which it had occupied and used for its business purposes throughout the period in question.[297]

RESTITUTION FOR WRONGS (INCLUDING BREACH OF CONTRACT)

[10.140] Most commentators see the law of restitution as divided into two distinct branches, the first being "autonomous actions in unjust enrichment" and the second "restitution for wrongs". The first branch consists of claims that are based solely on unjust enrichment: the "action is autonomous because it is not dependent upon proof of the elements of some other cause of action; rather the availability of relief is premised exclusively upon unjust enrichment".[298] In cases involving autonomous claims, the restitutionary remedy is said to be a legal response to the unjust enrichment itself, not a legal response to a wrong, such as a breach of contract or a tort.[299] The recovery of money paid under mistake, under compulsion or for a consideration that has totally failed are all examples of autonomous claims, as is the recovery of reasonable remuneration for services that have been requested or freely accepted. The second branch of the law of restitution consists of "restitution for wrongs", that is, restitutionary remedies granted in respect of other causes of action (such as breach of contract or breach of fiduciary duty). Here, the concept of unjust enrichment is "purely remedial because it plays no part" in establishing the plaintiff's cause of action or entitlement to a remedy but operates only to shape the remedy that is granted.[300] Most restitution scholars

296 *Ovidio Carrideo Nominees Pty Ltd v The Dog Depot Pty Ltd* [2006] VSCA 6. See also *Adrenaline Pty Ltd v Bathurst Regional Council* [2015] NSWCA 123, [78]–[86].

297 *Ovidio Carrideo Nominees Pty Ltd v The Dog Depot Pty Ltd* [2006] VSCA 6, [21], [33], [57]. The Court of Appeal held that the tenant's claim to recover the rent was also defeated by the landlord's counter-restitutionary claim against the tenant for use and occupation of the demised premises: [22], [49].

298 McInnes, "The Canadian Principle of Unjust Enrichment: Comparative Insights into the Law of Restitution" (1999) 37 *Alberta Law Review* 1, 23.

299 McInnes, "The Canadian Principle of Unjust Enrichment: Comparative Insights into the Law of Restitution" (1999) 37 *Alberta Law Review* 1, 23–31.

300 McInnes, "The Canadian Principle of Unjust Enrichment: Comparative Insights into the Law of Restitution" (1999) 37 *Alberta Law Review* 1, 24.

draw a sharp distinction between autonomous claims and restitution for wrongs and argue that restitution for wrongs is not part of the law of unjust enrichment.[301]

Contract damages are ordinarily assessed by reference to the loss suffered by the aggrieved party, rather than the gain made by the contract breaker.[302] In exceptional cases in some jurisdictions, a party breaching a contract is required to account for the profits derived as a result of the breach.[303] This remedy is known as an *account of profits* or *restitutionary damages*. The remedy is restitutionary in the sense that it has the effect of reversing a gain made by the defendant, but the gain made by the defendant is not necessarily made at the expense of (by subtraction from) the plaintiff. The defendant is often "giving up" a gain made as a result of the "wrong" of breach of contract rather than "giving back" an enrichment gained at the plaintiff's expense. Some suggest that damages awards requiring the "giving up" rather than "giving back" of a gain are more accurately described as awards of "disgorgement damages", rather than "restitutionary damages".[304] *Restitutionary damages* involve "giving back" a gain made at the expense of the plaintiff, while *disgorgement damages* involve "giving up" a gain made as result of a wrong, but not at the plaintiff's expense. Both restitutionary damages and disgorgement damages awarded for breach of contract are granted as a response to the wrong of breach of contract and are distinguishable from the autonomous claims based on unjust enrichment which have been considered in this chapter.

301 Notably Birks, *Unjust Enrichment* (2nd ed, 2005).

302 See Chapter 26.

303 For example, *Attorney General v Blake* [2001] 1 AC 268, discussed at [26.100].

304 For example, Edelman, "The Meaning of Damages: Common Law and Equity" in Robertson (ed), *The Law of Obligations: Connections and Boundaries* (2004), pp 31, 41–4; Edelman, *Gain Based Damages* (2002).

PARTIES

PART IV

CHAPTER **11**

Privity

[11.05] A person who is not a party to a contract can neither enforce the contract nor incur any obligations under it. This is known as the doctrine of privity of contract. Although the privity rule was once described as one of the fundamental principles in the laws of England,[1] it has been roundly criticised, is subject to significant exceptions, can be circumvented in numerous ways and has been substantially abrogated in numerous jurisdictions. The privity rule is distinct from the requirement discussed in Chapter 4 that consideration must move from the promisee. In order to sue on a promise, the plaintiff must not only have given consideration in return for that promise but must also be a *promisee*. The plaintiff must, in other words, be a party to the contract.

BENEFITS

[11.10] The privity doctrine principally operates to prevent non-parties from enforcing contractual promises that benefit them. A contract might benefit a third party by way of a positive or a negative stipulation. First, one of the parties might undertake a positive obligation

1 *Dunlop Pneumatic Tyre Co Ltd v Selfridge Co Ltd* [1915] AC 847.

to confer a benefit on the third party. A might, for example, enter into a contract with B under which A agrees to pay money to C in return for B's provision of services to A. B might enter into such an arrangement in order to settle a debt owing to C or because C is a relative of B's or is a company related to B. Secondly, a contract between A and B might confer a benefit on C in the form of a negative stipulation. For example, A (the owner of land) might engage B (a builder) to perform building work for A on the understanding that B will subcontract some carpentry work to C. The contract between A and B might then stipulate that A will not sue B or C in respect of any negligence committed in the course of the building work.

The privity doctrine does not prevent contracting parties from conferring a benefit on a third party, but simply prevents the third party from enforcing the contract. In the first of the examples above, if B performs the agreed services, C could not sue A to recover the money A has agreed to pay to C. B, a party to the contract, may enforce the contract but, as we will see, the remedies available to B may not be adequate to ensure that C obtains the benefit of A's promise. In the second example, if A sues C in respect of negligent work, C could not rely on the contract as a defence.

Coulls v Bagot's

[11.15] The privity rule was applied by the High Court in *Coulls v Bagot's Executor and Trustee Co Ltd*.[2] The case concerned an agreement by which Arthur Coulls granted to a company the right to quarry stone from his property in return for the payment of certain royalties. The agreement was headed "Agreement between Arthur Leopold Coulls and O'Neil Construction Proprietary Limited" but was signed by Arthur Coulls and his wife Doris Coulls, as well as L O'Neil on behalf of the company. After stipulating the royalties payable, the agreement provided that Arthur Coulls "authorised" the company to pay all moneys connected with the agreement to Doris Coulls and himself "as joint tenants". When Arthur Coulls died, his executor sought directions from the court as to whether the company was entitled or bound to pay the royalties to Doris Coulls. A majority of the High Court held that the company owed no contractual obligation to Doris Coulls because she was not a party to the agreement.[3] The principal indication of this was that the contract expressly purported to be made between Arthur Coulls and the company.[4] Moreover, the company made no express promise to pay royalties to Doris Coulls and it was not possible to imply such a promise.[5] The fact that Doris Coulls had signed the agreement did not make her a party. The authorisation clause took effect as a revocable mandate to the company to pay the royalties to Arthur and Doris Coulls, and that mandate lapsed on the death of Arthur Coulls.

Barwick CJ and Windeyer J dissented, considering that Doris Coulls should be regarded as a party to the agreement.[6] Barwick CJ held that Doris Coulls's signature of the agreement was explicable only on the basis that she was intended to be a party to the agreement. On that view, the company's promise to pay royalties was made to Mr and Mrs Coulls jointly, with the intention that the royalties would be paid to them jointly while they both lived and thereafter

2 *Coulls v Bagot's Executor and Trustee Co Ltd* (1967) 119 CLR 460. See also *Wilson v Darling Island Stevedoring and Lighterage Co Ltd* (1956) 95 CLR 43.
3 Cf Greig and Davis, *The Law of Contract* (1987), p 1032.
4 *Coulls v Bagot's Executor and Trustee Co Ltd* (1967) 119 CLR 460, 482–3, 486.
5 *Coulls v Bagot's Executor and Trustee Co Ltd* (1967) 119 CLR 460, 487.
6 *Coulls v Bagot's Executor and Trustee Co Ltd* (1967) 119 CLR 460, 476, 490–3.

to the survivor. Thus, according to the minority judges, following the death of Arthur Coulls, Doris Coulls was solely entitled to enforce the contract.

Trident v McNiece

[11.20] The ability of a third party to enforce a contractual promise was closely scrutinised by the High Court in *Trident General Insurance Co Ltd v McNiece Bros Pty Ltd*.[7] McNiece Bros Pty Ltd (McNiece) sought to take the benefit of an insurance contract made between Trident and Blue Circle Southern Cement Ltd (Blue Circle). McNiece was the principal contractor for construction work at a plant owned by Blue Circle. Under Blue Circle's contract of insurance with Trident General Insurance Co Ltd (Trident), Trident agreed to indemnify "The Assured" against liability in respect of injury to non-employees. The contract defined "The Assured" to mean Blue Circle, all of its related companies and all contractors and suppliers. In 1979, Hammond, a crane driver working under the direction of McNiece but employed by another company, sued McNiece for damages in respect of personal injuries. McNiece sought indemnity from Trident under the terms of the insurance contract made with Blue Circle. Trident argued that McNiece had no right to sue on that contract since it was not a party to it and gave no consideration.

After these events occurred, the *Insurance Contracts Act 1984* (Cth) was passed by the Commonwealth Parliament. On the recommendation of the Australian Law Reform Commission, this Act specifically provides that a person who is covered by a general insurance policy can recover from the insurer notwithstanding that he or she is not a party to the contract.[8] The Act does not apply to a contract of insurance made before its commencement, such as that between Trident and Blue Circle.[9] McNiece therefore had to rely on common law principles.

The trial judge held that McNiece was entitled to enforce the contract because it had been made by Blue Circle as McNiece's agent.[10] The New South Wales Court of Appeal did not agree that Blue Circle had contracted as the agent of McNiece, but upheld the decision on the basis that an exception to the privity rule should be recognised in the case of insurance contracts. Commercial convenience and practice demanded it, and the common law should "proceed in parallel fashion with statutory reforms" such as s 48 of the *Insurance Contracts Act 1984* (Cth). McNiece also succeeded in the High Court, by 5-2, though the judges deciding in McNiece's favour gave different reasons for Trident's liability.

Mason CJ and Wilson J noted that both the privity rule and the rule that only a party who has provided consideration for a promise can enforce it[11] "have been under siege throughout the common law world".[12] These rules have been criticised on substantial grounds, they are not accepted in most American states, they have been eroded by statute and they have the capacity to cause injustice.[13] Mason CJ and Wilson J considered that the High Court had a responsibility to reform unjust rules, even when they are well entrenched:

7 *Trident v McNiece* (1988) 165 CLR 107.
8 *Insurance Contracts Act 1984* (Cth), s 48.
9 *Insurance Contracts Act 1984* (Cth), s 4(1).
10 See [11.35].
11 See [4.40].
12 *Trident v McNiece* (1988) 165 CLR 107, 116.
13 *Trident v McNiece* (1988) 165 CLR 107, 116–23.

> Regardless of the layers of sediment which may have accumulated, we consider that it is the responsibility of this court to reconsider in appropriate cases common law rules which operate unsatisfactorily and unjustly.[14]

Their Honours even went so far as to suggest a way in which the law relating to contracts to benefit third parties could be modified:

> A simple departure from the traditional rules would lead to third party enforceability of such a contract, subject to the preservation of a contracting party's right to rescind or vary, in the absence of reliance by the third party to his detriment, and to the availability in an action by the third party of defences against a contracting party.[15]

Ultimately, however, Mason CJ and Wilson J limited themselves to the question "whether the old rules apply to a policy of insurance"[16] and found that they did not. If "the old rules" did apply to insurance contracts, Mason CJ and Wilson J said, they would cause injustice because the likelihood of reliance on insurance policies by third parties is so great. Third parties such as McNiece order their affairs and refrain from making their own arrangements in the knowledge that another person has insured against a particular risk.[17]

For similar reasons, Toohey J found that neither the privity rule nor the rule requiring consideration to move from the promisee should prevent enforcement of a contract of insurance by a third party in these circumstances. According to Toohey J, the "insurance exception" to the privity rule should only apply where it may be expected that the third party would order his or her affairs by reference to the insurance policy.[18] It has, however, been suggested in subsequent cases that the distinction between the rule formulated by Mason CJ and Wilson J on the one hand and the rule formulated by Toohey J on the other may be "illusory".[19]

Gaudron J found for McNiece on the basis that a promisor who accepts consideration for a promise to benefit a third party is unjustly enriched at the expense of the third party if the promise is not fulfilled. In order to prevent unjust enrichment, Gaudron J said, the third party is entitled to enforce an obligation imposed by law, which will ordinarily correspond with the contractual obligation.[20] Gaudron J's reasoning has been "extensively" and "properly" criticised and has been held not to represent the law in Australia.[21] As we saw in Chapter 10, unjust enrichment is not a freestanding principle of general application. Even if it was, any enrichment of the promisor (Trident) is at the expense of the party who provided the consideration (Blue Circle), not the promisee (McNiece). Allowing the promisee to enforcing the contract would not reverse any transfer of value.

Deane J held that the terms of the contract in question indicated that Blue Circle held its rights against Trident on trust for non-party beneficiaries, including McNiece. He would have

14 *Trident v McNiece* (1988) 165 CLR 107, 123. See, to similar effect, *Fraser River Pile & Dredge Ltd v Can-Drive Services Ltd* [1999] 3 SCR 108, [27].

15 *Trident v McNiece* (1988) 165 CLR 107, 123.

16 *Trident v McNiece* (1988) 165 CLR 107, 123.

17 *Trident v McNiece* (1988) 165 CLR 107, 123–4.

18 *Trident v McNiece* (1988) 165 CLR 107, 172.

19 See *Rail Corporation of New South Wales v Fluor Australia Pty Ltd* [2008] NSWSC 1348, [171]–[177].

20 *Trident v McNiece* (1988) 165 CLR 107, 176–7.

21 *Benson v Rational Entertainment Enterprises Ltd* [2018] NSWCA 111, [117]–[124]. See also *Rail Corporation of New South Wales v Fluor Australia Pty Ltd* [2008] NSWSC 1348, [186].

given McNiece leave to plead a trust and to join Blue Circle as a party to the action so that any such trust could be enforced.[22]

Brennan and Dawson JJ dissented entirely from the conclusion that McNiece should be entitled to enforce the contract. Brennan J held that there was no basis in policy or logic for any special principle allowing third parties to enforce contracts of insurance.[23] Nor was there any basis for overruling the doctrine of privity; his Honour held that any injustices caused by the rule could be overcome by developments in the law of trusts, estoppel and damages.[24] Dawson J held that the doctrine of privity was "inescapable having regard to the place which promise occupies in our law of contract".[25] The hardship caused by the rule can be alleviated by a generous approach to inferring that the promisee holds rights under the contract on trust for the third party.[26] Like Brennan J, Dawson J considered that there was no conceptual basis for exempting only contracts of insurance from the privity doctrine. Not only was the doctrine of privity too well entrenched to be overturned, but this would require the resolution of numerous difficult issues of policy which it would be inappropriate for a court to resolve.[27]

[11.23] In subsequent cases, Australian courts have generally resisted the temptation to widen by analogy the exception recognised by Mason CJ and Wilson and Toohey JJ.[28] In *Gate Gourmet Australia Pty Ltd (in liq) v Gate Gourmet Holding Ag*, however, Einstein J was willing to take the "relatively modest incremental step" of extending the principle to a contract of indemnity in the form of a letter of comfort.[29] A subsidiary company (in liquidation) sought to enforce a promise of financial support issued by its ultimate parent company to its immediate holding company. The letter had been provided to satisfy an auditing requirement. Under the "Letter of Support", the parent promised to provide the financial support necessary to enable the holding company "and its controlled entities" (which included the plaintiff subsidiary) to meet their financial obligations as they fell due. Einstein J held that the subsidiary company was a party to the contract but also held that, if that conclusion was incorrect, the subsidiary company could nevertheless enforce the promise. The exception to the privity rule recognised by Mason CJ and Wilson and Toohey JJ in *Trident General Insurance Co Ltd v McNiece Bros Pty Ltd* could be extended because of the similarities between contracts of insurance and contracts of indemnity, and because the parties had a common intention that the subsidiary company would obtain the benefit of the promises contained in the letter and it had ordered its affairs accordingly.[30] Alternatively, Einstein J held that the holding company held the benefit of the parent company's promise on trust for the subsidiary.[31]

The Supreme Court of Canada has recognized the injustice of the privity rule and has developed a "principled exception" of general application. The exception applies whenever

22 See [11.40].

23 *Trident v McNiece* (1988) 165 CLR 107, 125–8.

24 *Trident v McNiece* (1988) 165 CLR 107, 139–40.

25 *Trident v McNiece* (1988) 165 CLR 107, 155.

26 *Trident v McNiece* (1988) 165 CLR 107, 156.

27 *Trident v McNiece* (1988) 165 CLR 107, 162. See [11.85].

28 *Mizzi v Reliance Financial Services Pty Ltd* [2007] NSWSC 37, [71]; *Silver v Dome Resources NL* (2007) 62 ACSR 539, 567. For a novel application of the "Trident exception" see *Merrell Associates Ltd v HL (Qld) Nominees Pty Ltd* [2010] SASC 155.

29 *Picwoods Pty Ltd v Panagopoulos* [2004] NSWSC 149, [255].

30 *Picwoods Pty Ltd v Panagopoulos* [2004] NSWSC 149, [254]–[255].

31 *Picwoods Pty Ltd v Panagopoulos* [2004] NSWSC 149, [256].

(a) the parties to a contract intended to extend the benefit in question to the third party seeking to rely on the contractual provisions, and (b) the activities performed by the third party seeking to rely on the contractual provision are the very activities contemplated as coming within the scope of the contract.[32] In *London Drugs Ltd v Kuehne & Nagel International Ltd*, employees of a warehouse company negligently damaged goods belonging to their employer's customer. When the customer sued them for damages, the employees were held to be entitled to take advantage of a limitation of liability clause in the contract between the employer and the customer.

BURDENS

[11.25] The privity doctrine also prevents a contract from imposing a legal burden on a third party. A contract between a manufacturer of goods (A) and a wholesaler (B) cannot restrict the terms on which the goods may be sold by a retailer (C) who purchases the goods from the wholesaler.[33] The contract between A and B cannot impose obligations on C. The principal exception to this is a restrictive covenant affecting land, which can bind subsequent owners of the land.[34] Such a covenant creates an equity, which will bind subsequent owners of the land who acquire their interest with notice of the covenant. The subsequent owners are bound by "privity of estate", rather than privity of contract. The leading case on this principle is *Tulk v Moxhay*,[35] in which the plaintiff owned land in Leicester Square and several houses around the square. The plaintiff sold the land in the square to Elms, who covenanted for himself, his heirs and assigns not to build on the land. The defendant purchased the land with knowledge of the covenant after it had passed through the hands of several intervening owners. Since the defendant acquired his interest with notice of the restrictive covenant, he was bound by the plaintiff's equity and the plaintiff was able to obtain an injunction to prevent the defendant from building on the land in breach of the covenant. The principle applied in *Tulk v Moxhay* applies only to restrictive covenants and not to positive covenants, such as a promise to keep an adjoining house in good repair.[36] In Australia, the principle has been modified by statute and is subject to certain restrictions.[37]

NON-APPLICATION OF THE PRIVITY RULE

[11.30] There are two circumstances in which it may be possible to show that a party not directly involved in acts of contract formation is nevertheless a party to the contract. These are:

1. where one of the parties who is involved acts as agent for the non-involved party; and

32 *London Drugs Ltd v Kuehne & Nagel International Ltd* [1992] 3 SCR 299; *Fraser River Pile & Dredge Ltd v Can-Drive Services Ltd* [1999] 3 SCR 108

33 *Taddy and Co v Sterious and Co* [1904] 1 Ch 354. A restriction relating to the minimum price at which the goods can be resold will infringe the prohibition against resale price maintenance contained in s 48 of the *Competition and Consumer Act 2010* (Cth).

34 Another exception arises in the case of contracts of bailment. The terms of a contract of bailment will in some circumstances be binding on a sub-bailee who is not a party to that contract: *The Pioneer Container* [1994] 2 AC 324.

35 *Tulk v Moxhay* (1848) 2 Ph 774; 41 ER 1143.

36 *Rhone v Stephens* [1994] 2 AC 310.

37 See Bradbrook and Neave, *Easements and Restrictive Covenants in Australia* (3rd ed, 2011).

2. where one of the involved parties transfers contractual benefits to the non-involved party by way of an assignment or novation of the contract.

In such circumstances, the non-involved party is in fact a party to the contract and, thus, the privity rule has no application.

Agency

[11.35] The privity rule does not apply if a person promised a benefit under a contract can show that one of the parties involved in the contractual negotiations entered into the contract as his or her agent. An agent is a person who has power to enter into a contract on behalf of another person (the principal). If A, acting as an agent of C, makes a contract with B, then C is a party to that contract. Agency relationships can be created expressly or by implication. To establish the existence of an agency relationship, it is necessary to show that the principal expressly or impliedly consented to the agent acting on his or her behalf so as to effect the principal's relations with third parties.[38] In *Pola v Commonwealth Bank of Australia*, Sundberg J said:

> In general, no formality is necessary for the appointment of an agent to act on behalf of his principal … It is only necessary that the principal and agent consent to that relationship … The existence of agency may often be established from the words of the parties and the circumstances of the particular case, and may be implied from prior habits or from a course of dealing between the parties where the agent has repeatedly been permitted to perform similar acts in the past … If the facts fairly disclose that one party is acting for or representing another by the latter's authority, the agency exists … Thus the consent of the principal may be implied where he places another in such a situation that a reasonable man would understand the other to have the principal's authority to act on his behalf, or where the principal's words or conduct, coming to the knowledge of the agent, are such as to lead to the reasonable inference that he is authorising the agent to act for him.[39]

In addition to establishing that an agency relationship exists, it will also be necessary to show that, with respect to the particular transaction under consideration, the agent was purporting to act on behalf of the principal and not solely on his or her own behalf.[40] Ratification refers to the adoption or confirmation of a contract which was entered into by an agent who did not have prior authority from the principal. Ratification has commonly been relied upon to avoid the application of the privity rule in relation to limitation of liability clauses in contracts of carriage. Contracts for the carriage of goods commonly contain a clause exempting or limiting liability for loss or damage to the goods. Such clauses typically extend the exclusion or limitation of liability to cover employees, agents and sub-contractors of the carrier, such as stevedores engaged to load and unload the goods. These clauses are sometimes referred to as *Himalaya clauses*.[41] Although clauses of this type can have the effect of saving "grossly negligent people from the normal consequences of their negligence", the courts have exhibited what has been called a "curious, and seemingly irresistible" anxiety to give effect to them.[42] One explanation is that a limitation of liability clause which protects the carrier and its sub-contractors and

38 See *CAN 007 528 207 Pty Ltd v Bird Cameron* (2005) 91 SASR 570, 592–7.

39 *Pola v Commonwealth Bank of Australia* (Sundberg J, 19 December 1997, unreported), 12.

40 *Picwoods Pty Ltd v Panagopoulos* [2004] NSWSC 978, [84]–[85].

41 After *Adler v Dickson (The Himalaya)* [1955] 1 QB 158.

42 *Wilson v Darling Island Stevedoring and Lighterage Co Ltd* (1956) 95 CLR 43, 71.

employees in many cases gives effect to a commercial understanding that the owner of the goods is expected to make their own insurance arrangements. Allowing the owner of the goods to sue a sub-contractor or employee for negligence may have the effect of upsetting the agreed allocation or risk and circumventing the insurance arrangements the parties have put in place.[43]

In order to determine whether a stevedore is entitled, on the basis of agency, to take advantage of an exemption clause contained in a contract of carriage made between a carrier and the owner of goods, courts apply the four-stage test laid down by Lord Reid in *Scruttons Ltd v Midland Silicones Ltd*.[44] Lord Reid suggested that a stevedore is entitled to the benefit of an exemption clause if:

1. the bill of lading (which sets out the terms of the contract of carriage) makes it clear that the stevedore was intended to be protected;
2. the bill of lading makes it clear that the carrier was contracting as agent for the stevedore as well as on its own behalf;
3. either the carrier was authorised to make the contract on behalf of the stevedore or the stevedore subsequently ratified the carrier's actions; and
4. the stevedore provided consideration to the promisor.

The High Court and the Privy Council found that these requirements were met in *Port Jackson Stevedoring Pty Ltd v Salmond & Spraggon (Aust) Pty Ltd (The New York Star)*.[45] That case involved a consignment of razor blades shipped from Canada to Australia. The carrier issued a bill of lading to the consignor of the goods, the terms of which were expressly accepted by the consignee. The bill of lading imposed a 1-year time bar on proceedings in respect of loss or damage to the goods. Clause 2 of the bill of lading was a Himalaya clause, extending the benefit of that limitation to servants, agents and independent contractors employed by the carrier. The appellant stevedore was 49 per cent owned by the carrier, commonly acted as its stevedore and was aware of the terms of the bill of lading. The goods were unloaded by the stevedore and placed in its storage shed, from which 33 of the 37 cartons in the consignment were stolen. The consignee sued the stevedore for damages in tort, outside the stipulated time period. The High Court, by a majority of 3-2, held that the stevedore was entitled to the protection of clause 17 but, by a majority of 4-1, held that the stevedore's actions were not covered by the clause. On appeal, the Privy Council held that the stevedore was entitled to rely on the clause as a bar to the consignee's claim.

The consignee conceded that the first two of Lord Reid's requirements were satisfied. In the High Court, Barwick CJ held that the third element was satisfied because the carrier had acted with the authority of the stevedore as its agent in contracting for the stevedore's

43 See *London Drugs Ltd v Kuehne & Nagel International Ltd* [1992] 3 SCR 299, 443–446.

44 *Scruttons Ltd v Midland Silicones Ltd* [1962] AC 446.

45 *Port Jackson Stevedoring Pty Ltd v Salmond & Spraggon (Aust) Pty Ltd (The New York Star)* (1978) 139 CLR 231 (HC); (1980) 144 CLR 300 (PC). The Privy Council found the requirements satisfied in an earlier case: *New Zealand Shipping Co Ltd v AM Satterthwaite & Co Ltd (The Eurymedon)* [1975] AC 154. The principle has since been applied by the Supreme Court of Canada: *ITO – International Terminal Operators Ltd v Miida Electronics Inc* [1986] 1 SCR 752.

protection.[46] The stevedore provided consideration by unloading the goods. Mason and Jacobs JJ, on the other hand, treated the protective provisions of the bill of lading as an offer made by the consignee to the stevedore through its agent, the carrier. The stevedore accepted that offer and provided consideration for it by unloading the goods with knowledge of the offer and in reliance on it. On this view, the circumstances gave rise to a unilateral contract between the consignee and the stevedore, rather than a bilateral contract made through the agency of the carrier.[47]

Stephen and Murphy JJ dissented. Stephen J held that the terms of the bill of lading did not support a unilateral contract but could only be construed as a contract "having immediate effect as binding both parties".[48] At the time the agreement was made, the stevedore provided no consideration to support such a contract. The subsequent unloading of the goods could not operate as consideration for the earlier promise.[49] Stephen J also noted that the conclusion that the stevedore was entitled to the benefit of the clause may be inconsistent with the public interest. While fleet-owning nations might wish to protect carriers as fully as possible, the interest of countries that are reliant on ships for import and export trade is to the contrary. Australian courts have no reason to accord any "benevolent interpretation" to carriers' exemption clauses.[50] Moreover, Stephen J was concerned that the use of such clauses divorced the power of control over goods from liability for the consequences of irresponsibility or a lack of effective supervision. Consignees bear the consequences of any carelessness in the form of increased insurance premiums, but have no power to control the employees of the stevedores. If the stevedores can escape liability, they have no incentive to exercise effective control and supervision over their employees.[51] Murphy J agreed, noting that the carriage of goods and the overseas stevedoring industry were so enmeshed by restrictive practices that Australian importers have no real freedom in their arrangements. It was therefore a distortion to regard those arrangements as contractual.[52]

On the other hand, it has been argued that the decision in *The New York Star case* "makes eminent commercial sense".[53] Mark Tedeschi argues that the risk of loss should fall on the owner of the goods, since the owner is best placed to insure against loss. The owner knows the nature and true value of the goods and can insure the goods for the entire journey, rather than each person handling the goods having to effect insurance for the period in which they are in control. Freight rates may be lower than they would be if stevedores had to insure against, or take responsibility for, loss or damage to the goods.

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46 *Port Jackson Stevedoring Pty Ltd v Salmond & Spraggon (Aust) Pty Ltd (The New York Star)* (1978) 139 CLR 231, 243.

47 As to unilateral contracts, see [3.15]. The unilateral contract analysis had earlier been employed by the Privy Council in *New Zealand Shipping Co Ltd v AM Satterthwaite & Co Ltd (The Eurymedon)* [1975] AC 154.

48 *Port Jackson Stevedoring Pty Ltd v Salmond & Spraggon (Aust) Pty Ltd (The New York Star)* (1978) 139 CLR 231, 257.

49 *Port Jackson Stevedoring Pty Ltd v Salmond & Spraggon (Aust) Pty Ltd (The New York Star)* (1978) 139 CLR 231, 257–8.

50 *Port Jackson Stevedoring Pty Ltd v Salmond & Spraggon (Aust) Pty Ltd (The New York Star)* (1978) 139 CLR 231, 259.

51 *Port Jackson Stevedoring Pty Ltd v Salmond & Spraggon (Aust) Pty Ltd (The New York Star)* (1978) 139 CLR 231, 258.

52 *Port Jackson Stevedoring Pty Ltd v Salmond & Spraggon (Aust) Pty Ltd (The New York Star)* (1978) 139 CLR 231, 285.

53 Tedeschi, "Consideration, Privity and Exemption Clauses" (1981) 55 *Australian Law Journal* 876, 879.

The principle applied in *The New York Star case* has been applied in subsequent cases involving the carriage of goods by road[54] and even, in Canada, to the liability of a race official to a contestant.[55] There is no reason why the four requirements articulated by Lord Reid in *Scruttons Ltd v Midland Silicones Ltd* could not be expressed in broader terms, to cover any contractual promise to confer a benefit on a party who is not directly involved in the making of an agreement. It could be said that where:

1. a contract makes it clear that a benefit is to be conferred on a beneficiary;
2. the contract makes it clear that the promisee is acting as agent of the beneficiary;
3. the promisee was authorised to enter into the contract on the beneficiary's behalf (or the contract was subsequently ratified); and
4. the beneficiary provided consideration for the promise,

the beneficiary is a party to the contract and is entitled to enforce it.

Although some view the agency approach as a useful means of circumventing the privity rule,[56] others are less enthusiastic.[57] It is an artificial means of avoiding the doctrine of privity and its application sometimes requires a distortion of the principles of contract formation. In *Celthene Pty Ltd v WKJ Hauliers Pty Ltd*,[58] for example, Yeldham J accepted that a driver provided consideration even though at the time of performance he had not been aware of the existence of the relevant clause.[59]

Assignment and novation

[11.37] A person who is not originally a party to a contract can acquire rights under it by way of assignment. The assignment of contractual rights is a complex area of law which can only briefly be sketched here.[60] An assignment involves the transfer to a third party (the *assignee*) of some or all of the *contractual rights* held by a contractual party (the *assignor*) against another (the *obligor*). The doctrine of privity does not prevent the assignee from enforcing the contractual rights that have been assigned because the rights have been transferred from the assignor to the assignee. A contractual right will be be assignable without the consent of the person by whom the duty is owed (the *obligor*) if the identity of the person to whom the duty is owed makes no difference to the obligor.[61] A contractual right is not assignable without the obligor's consent if, in view of its subject matter and the nature of the contract, it is personal "in the sense that the identity of the contractual obligee is material to the contractual relationship itself … or to the contractual performance to be

54 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* (2004) 219 CLR 165.

55 *Dyck v Manitoba Snowmobile Association Inc* (1981) 5 WWR 97.

56 Lücke, "Exclusion Clauses and Freedom of Contract: Judicial and Legislative Reactions" (1977) 51 *Australian Law Journal* 532.

57 See, eg, *Carrington Slipways Pty Ltd v Patrick Operations Pty Ltd* (1991) 24 NSWLR 745, 747, 754; Malcolm, "The Negligent Pilot and the Himalaya Clause: A Saga of Disagreement" (1993) 67 *Australian Law Journal* 14.

58 *Celthene Pty Ltd v WKJ Hauliers Pty Ltd* [1981] 1 NSWLR 606.

59 Cf *The Crown v Clarke* (1927) 40 CLR 227, discussed at [3.80] and see Cavanagh, "The Ultimate Exclusion Clause" (1985) 59 *Australian Law Journal* 67.

60 See, eg, Tolhurst, *The Assignment of Contractual Rights* (2nd ed, 2016) and Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), Ch 8.

61 *Tolhurst v Associated Portland Cement Manufacturers* (1900) Ltd [1902] 2 KB 660, 668.

rendered".[62] The terms of a contract may permit the assignment of rights not otherwise assignable or may prohibit the assignment of rights that otherwise would be assignable.[63]

While contractual *rights* can in some circumstances be assigned without the consent of the other contracting party, contractual *obligations* cannot.[64] A third party may, however, be substituted for one of the original contracting parties by a process known as novation.[65] Novation involves the substitution of a new contract between one of the original parties and a substituted party in place of the original contract. This is normally effected by way of an agreement between the original parties and the substituted party, although the original contract may authorise a party to substitute another party in its place without the need for further agreement.[66] The effect of novation is that the contractual relationship between the original parties is brought to an end and privity of contract is then established between the remaining original party and the substituted party.

CIRCUMVENTING THE PRIVITY RULE

[11.38] There are several ways in which the privity rule may be circumvented by a person seeking to take the benefit of a contract in which he or she is not named as a party. In the following discussion, the person making a contractual promise to benefit a third party is referred to as the *promisor*, the other party to the contract as the *promisee* and the third party seeking to enforce the contract as the *beneficiary*. The main circumstances under which the privity rule may be of circumvented are:

1. The promisee may hold rights under the contract on trust for the beneficiary.
2. The beneficiary may be entitled to assert an estoppel against the promisor.
3. The beneficiary may be entitled to claim damages for misleading or deceptive conduct.
4. The beneficiary may be entitled to claim damages in tort.

Trust

[11.40] All but one of the judgments in *Trident v McNiece*[67] pointed to the trust as a means of alleviating some of the injustice occasioned by the application of the privity rule. A contractual right is a form of property (a chose in action) which, like any other form of property, can be held by a trustee on trust for a beneficiary. Where A (the promisor), in a contract with B (the promisee), makes a promise to confer a benefit on C (the beneficiary), the court may discern an intention on the part of B to hold on trust for C the contractual right to enforce that promise. Where such an intention can be discerned, this does not make the beneficiary a party to the

62 *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* (2006) 149 FCR 395, [32].

63 *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* (2006) 149 FCR 395, [32]. See also *Leveraged Equities Ltd v Goodridge* [2011] FCAFC 3; (2011) 191 FCR 71, [363] and Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [8.8].

64 *Tolhurst v Associated Portland Cement Manufacturers (1900) Ltd* [1902] 2 KB 660, 668.

65 *Olsson v Dyson* (1969) 120 CLR 365, 388. For a discussion of the distinction between assignment and novation, see *Ashton v Australian Cruising Yacht Co Pty Ltd* [2005] WASC 192, [61]–[63],

66 *Leveraged Equities Ltd v Goodridge* [2011] FCAFC 3; (2011) 191 FCR 71, [299]–[317].

67 *Trident v McNiece* (1988) 165 CLR 107, 120–1, 135, 140–1, 146–55, 167, 170. See generally Wright, "Trusts Involving Enforceable Promises" (1996) 70 *Australian Law Journal* 911.

contract; rather, it creates an obligation on the part of the promisee to enforce the promise on behalf of the beneficiary. The beneficiary can indirectly enforce the promise by compelling the promisee/trustee to enforce it. In practice, this means that the beneficiary can sue the promisor, provided the promisee/trustee is joined as a defendant.[68]

The difficult question relating to the use of the trust is when the courts will be prepared to imply or infer an intention to create a trust. In some cases, courts have insisted on a clear expression of intention to create a trust and have been unwilling to infer such an intention. In others, the courts have been prepared to infer a trust from the fact that a contract was made for the benefit of a third party.[69] It has been said that uncertainty as to when a trust will be implied or inferred makes the trust an inadequate means of redressing the injustice caused by the privity and consideration rules.[70]

The approach that should be taken to inferring an intention to create a trust of a contractual right was discussed in *Trident v McNiece*. Deane J in that case said:

> [T]he requisite intention should be inferred if it clearly appears that it was the intention of the promisee that the third party should himself be entitled to insist on performance of the promise and receipt of the benefit and if trust is, in the circumstances, the appropriate legal mechanism for giving effect to that intention. A fortiori, equity's requirement of an intention to create a trust will be at least prima facie satisfied if the terms of the contract expressly or impliedly manifest that intention as the joint intention of both promisor and promisee.[71]

Deane J therefore treated intention to create a trust as a question of construction of the contract in its context.[72] Although the intention to create a trust will commonly be a joint intention, it is important to note that it is sufficient if it is the promisee's intention alone.[73] Whether a trust arises depends entirely on the intention of the promisee is the settlor of any trust that is created.[74] Deane J observed that a trust of a contractual promise will more readily be discerned in some classes of contract than in others. In a contract of liability insurance, it is clearly intended that each assured should be entitled to insist on performance of the insurer's promise to indemnify him or her. In legal terms, this can be construed as an intention that the relevant contractual right should be held on trust for the assured in question.[75] Since there was nothing to negate such an intention, Deane J concluded that Blue Circle held the benefit of Trident's promise to indemnify McNiece on trust for McNiece. Accordingly, his Honour would have given McNiece leave to join Blue Circle as a party to the action so that this trust could be enforced.

Since the case had not been pleaded or argued on the basis of trust, there was no need for the other members of the court to decide whether Blue Circle held rights against Trident on

68 See *Trident v McNiece* (1988) 165 CLR 107, 135.

69 *Trident v McNiece* (1988) 165 CLR 107, 120–1. See also *Wilson v Darling Island Stevedoring and Lighterage Co Ltd* (1956) 95 CLR 43, 71.

70 *Trident v McNiece* (1988) 165 CLR 107, 121, citing Corbin, "Contracts for the Benefit of Third Persons" (1930) 46 *Law Quarterly Review* 12.

71 *Trident v McNiece* (1988) 165 CLR 107, 147.

72 *Trident v McNiece* (1988) 165 CLR 107, 148.

73 *Trident v McNiece* (1988) 165 CLR 107, 149. This was also emphasised by Mason CJ and Wilson J at 121. See also *Gate Gourmet Australia Pty Limited (in liq) v Gate Gourmet Holding Ag* [2004] NSWSC 149, [261].

74 *Mizzi v Reliance Financial Services Pty Ltd* [2007] NSWSC 37, [72].

75 *Trident v McNiece* (1988) 165 CLR 107, 149.

trust for McNiece. Nevertheless, Mason CJ and Wilson J did attempt to resolve the uncertainty as to when a trust of a contractual right in favour of a third party will be recognised:

> This apparent uncertainty should be resolved by stating that the courts will recognise the existence of a trust when it appears from the language of the parties, construed in its context, including the matrix of circumstances, that the parties so intended. We are speaking of express trusts, the existence of which depends on intention. In divining intention from the language which the parties have employed the courts may look to the nature of the transaction and the circumstances, including commercial necessity, in order to infer or impute intention …[76]

Estoppel

Equitable estoppel

[11.45] The doctrine of equitable estoppel is another means by which equity may alleviate some of the injustice arising from the application of the privity rule. Equitable estoppel will prevent injustice arising from a party relying to his or her detriment on an expected benefit or entitlement arising from a contract to which he or she is not a party. Where a beneficiary has been induced by a promisor to assume that he or she will receive a benefit under a contract with a promisee, and the beneficiary has relied on that assumption in such a way that he or she will suffer a detriment if it is not fulfilled, then the beneficiary may be entitled to assert an estoppel against the promisor.[77] If, for example, McNiece had been led by Trident to believe that it would have the benefit of indemnity cover under Blue Circle's insurance policy with Trident and, on the faith of that belief, had omitted to obtain its own insurance cover, McNiece might have been entitled to "claim the benefit of the policy by way of estoppel".[78]

The doctrine of equitable estoppel also makes it possible for a person to incur a burden under a contract to which he or she is not a party. As noted in Chapter 9, a person who is not a party to a contract may be liable where he or she induces a relying party to act on the faith of an assumption that the inducing party will abide by the terms of the contract.[79]

Estoppel by convention

[11.47] The doctrine of estoppel by convention, which operates where parties have adopted a particular state of affairs as the basis of their relations,[80] may prevent a person who is not a party to a contract under ordinary principles from denying that he or she is a party.[81] It has also been suggested that estoppel by convention can be used by a beneficiary to enforce a promise made for his or her benefit provided the beneficiary can show that the promisee, promisor and beneficiary shared an assumption that the beneficiary would receive a benefit under the contract and the beneficiary has relied on that assumption to his or her detriment.[82]

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76 *Trident v McNiece* (1988) 165 CLR 107, 121.

77 See Chapter 9.

78 See *Trident v McNiece* (1988) 165 CLR 107, 140, 145.

79 *Weir v Hoylevans Pty Ltd* [2001] WASCA 23.

80 See [9.200].

81 See, eg, *Whitehouse v BHP Steel Ltd* [2004] NSWCA 428.

82 Neyers, "Explaining the Principled Exception to Privity of Contract" (2007) 52 *McGill Law Journal* 757, 780, 787.

Torts

[11.50] In some circumstances, a beneficiary who has no contractual rights will be able to enforce an equivalent obligation imposed on the promisor by the law of torts.[83] This will be the case where the contractual duty in question is a duty to take care to avoid harm to the beneficiary, and there is a relationship of proximity between the promisor and the beneficiary which gives rise to a duty of care under the law of negligence. In *Hill v Van Erp*,[84] Mrs Hill was a solicitor retained by Mrs Currey to prepare her will, which included a disposition in favour of Mrs Van Erp. Hill failed to ensure that the will was properly attested, as a result of which the disposition in favour of Van Erp failed. Hill owed a contractual duty of care to Currey. Although Van Erp was not a party to that contract, she would have benefited from it had it been properly performed.[85] Van Erp therefore sued in tort. The High Court accepted that, in the circumstances, Hill owed Van Erp a duty of care and Van Erp was entitled to damages for breach of that duty. The law of tort operated in that case to vindicate fulfilment of Hill's contractual obligation to Currey, which would otherwise have sounded only in ineffective legal remedies.[86]

Misleading or deceptive conduct

[11.55] The making of a contractual promise will, in some circumstances, constitute misleading or deceptive conduct. Section 18 of the *Australian Consumer Law* (Cth)[87] prohibits misleading or deceptive conduct in trade or commerce. A person who suffers loss as a result of such conduct is entitled to recover damages from the person who engages in the conduct.[88]

Where the making of a contractual promise contravenes the statutory prohibition against misleading or deceptive conduct, and a person who is not a party to the contract (the beneficiary) suffers loss as a result of reliance on the promise, then the beneficiary will be entitled to damages. In such a case, the beneficiary is not seeking to enforce the contract but is simply asserting a statutory right to damages. Where the promise in question relates to the future conduct of the promisor, and the beneficiary suffers loss as a result of a failure to fulfil that promise, then there may well be an overlap between equitable estoppel and the beneficiary's statutory rights. Where the contractual promise is a warranty that a particular fact is true,[89] there will generally be no estoppel because the harm suffered by the beneficiary will not result from any inconsistent conduct on the part of the promisor, but rather from the falsity of the warranty.[90]

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83 See Fleming, "Tort in a Contractual Matrix" (1995) 33 *Osgoode Hall Law Journal* 661.

84 *Hill v Van Erp* (1997) 188 CLR 159. See also *White v Jones* [1995] 2 AC 207; *Bryan v Maloney* (1995) 182 CLR 609 and Bell and Jocic, "Negligence Claims by Subsequent Building Owners: Did the Life of Bryan End Too Soon?" (2017) 41 *Melbourne University Law Review* 1.

85 *Hill v Van Erp* (1997) 188 CLR 159, 233.

86 *Hill v Van Erp* (1997) 188 CLR 159, 233.

87 See [2.80].

88 See Chapter 33.

89 As in *Accounting Systems 2000 (Developments) Pty Ltd v CCH Australia Ltd* (1993) 42 FCR 470, discussed later in this section.

90 See [9.230].

In *Accounting Systems 2000 (Developments) Pty Ltd v CCH Australia Ltd*,[91] CCH recovered damages under the *Trade Practices Act 1974* (Cth) in respect of loss suffered as a result of reliance on a promise made in a contract to which CCH was not a party. The contract in question was between AS2000 and Castle Douglas Pty Ltd, by which AS2000 assigned copyright in a computer program to Castle Douglas. By clause 3.1 of that contract, AS2000 warranted that it was entitled to assign the copyright to Castle Douglas and that there was no claim or potential claim against AS2000 for breach of copyright. In fact, the program in question infringed the copyright of a fourth party, who had a claim against AS2000 for breach of copyright. CCH entered into certain other contracts, including a licence agreement with Castle Douglas, in reliance on the contractual warranties made by AS2000 to Castle Douglas. CCH sued AS2000 for damages under the *Trade Practices Act 1974* (Cth). The trial judge found that the making of the warranties constituted misleading or deceptive conduct. This finding was upheld by the Full Federal Court. CCH suffered loss as a result of that misleading conduct and was therefore entitled to relief, notwithstanding "that the misleading conduct is found in the making of a contractual provision, and the complainant does not have contractual privity with the defendant".[92]

Domestic building warranties

[11.57] Most Australian jurisdictions provide protection to purchasers of domestic buildings against defects by implying certain warranties into building contracts (eg, that the work will be carried out with care and skill) and then providing that a subsequent owner of the building can sue for breach of any of the warranties "as if that person was a party to the contract."[93]

REMEDIES AVAILABLE TO THE PROMISEE

[11.60] If a promisee is willing to sue a promisor to enforce a contractual promise to confer a benefit on a third party, the remedies available may not be sufficient to ensure that the third party obtains the promised benefit. In some cases, substantial damages will be available, and in others, specific performance will be decreed. There are, however, some situations in which specific performance will be unavailable and there is doubt as to when the promisee will be entitled to recover substantial damages.

Damages

[11.65] Whether the promisee can recover substantial damages is a vexed question.[94] The purpose of contract damages is to compensate the plaintiff for loss caused by a breach of contract.[95] Where A breaches a promise made to B to confer a benefit on C, it can be said

91 *Accounting Systems 2000 (Developments) Pty Ltd v CCH Australia Ltd* (1993) 42 FCR 470.

92 *Accounting Systems 2000 (Developments) Pty Ltd v CCH Australia Ltd* (1993) 42 FCR 470, 506.

93 *Domestic Building Contracts Act* 1995 (Vic), s 9. To similar effect are: *Building Act 2004* (ACT), s 88(3); *Home Building Act* 1989 (NSW), s 18D; *Queensland Building and Construction Commission Act 1991* (Qld), Sch 1B, s 27; *Building Work Contractors Act* 1995 (SA), s 32(3); *Residential Building Work Contracts and Dispute Resolution Act 2016* (Tas), 31. Cf *Building Act 1993* (NT), Pt 5A, Div 2 (consumer guarantees rather than contractual warranties).

94 *Trident v McNiece* (1988) 165 CLR 107, 118.

95 See Chapter 26.

that B will not normally suffer any loss. It is C who has lost the promised benefit and this will only cause loss to B if B has a particular interest in A's performance, such as where payment by A would have discharged a debt owed by B to C. The orthodox view, therefore, is that if non-performance of the promise causes no particular harm to the promisee, then the promisee will only be entitled to nominal damages.[96] Where the promisee holds the relevant contractual rights on trust for the third-party beneficiary, then it seems that the promisee can recover all that the third party could have recovered if the contract had been made with the third party.[97]

In England, the courts have recognised some exceptions to the general rule stated earlier in this section. English courts have recognised certain situations in which a promisee is entitled to damages in respect of the loss suffered by the third party.[98] The general rule itself was cast into doubt by the English Court of Appeal in *Jackson v Horizon Holidays Ltd*.[99] The Court of Appeal appeared to apply a general principle that a promisee can recover substantial damages in respect of loss suffered by a third-party beneficiary as a result of a breach of contract, even where the promisee did not hold the contractual rights on trust for the third party. In that case, Horizon contracted with Jackson to provide a holiday for Jackson and his family. Jackson sued for damages after the accommodation fell far short of the promised standard. In the English Court of Appeal, Lord Denning MR, with whom Orr LJ agreed, held that where a contract is made for the benefit of a third party, the promisee is entitled to recover damages in respect of the loss suffered by the third party, even where the promisee is not a trustee.[100] Jackson was therefore entitled to recover for the "expense … discomfort, vexation and upset" suffered by the other members of his family.[101] Dicta of the House of Lords in *Woodar Investment Development Ltd v Wimpey Construction (UK) Ltd*[102] indicate that Lord Denning went too far in saying that damages will always be recoverable in respect of loss suffered by a third-party beneficiary. Such damages may only be recoverable in respect of contracts of a particular type, where third parties stand to gain indirectly by performance[103] or where there may be a presumption that the promisee himself or herself suffered a loss as a result of the deprivation of the third parties.[104]

96 *Trident v McNiece* (1988) 165 CLR 107, 118, 158; *Beswick v Beswick* [1968] AC 58; *White v Jones* [1995] 2 AC 207.

97 *Coulls v Bagot's Executor and Trustee Co Ltd* (1967) 119 CLR 460, 501; *Trident v McNiece* (1988) 165 CLR 107, 118.

98 Exceptions have been recognised in relation to contracts for the carriage of goods being sold to a third party (*Dunlop v Lambert* (1839) 6 Cl & F 600; 7 ER 824) or, more broadly, contracts concerning goods which it is contemplated may be transferred to a third party before the breach occurs (*The Albazero* [1977] AC 774, 847) and building contracts in which it is foreseeable that land will be transferred to a third party (*Linden Gardens Trust Ltd v Leneston Sludge Disposals Ltd* and *St Martin's Property Corporation v Sir Robert McAlpine Ltd* [1994] 1 AC 85). See also *Darlington Borough Council v Wiltshier Northern Ltd* [1995] 1 WLR 68 and *Alfred McAlpine Construction Ltd v Panatown Ltd* [2001] 1 AC 518, noted later in this section. For a useful discussion of the decisions leading up to the last, see Treitel, "Damages in Respect of a Third Party's Loss" (1998) 114 *Law Quarterly Review* 527.

99 *Jackson v Horizon Holidays Ltd* [1975] 3 All ER 92.

100 *Jackson v Horizon Holidays Ltd* [1975] 3 All ER 92, 95–6.

101 *Jackson v Horizon Holidays Ltd* [1975] 3 All ER 92, 96.

102 *Woodar Investment Development Ltd v Wimpey Construction (UK) Ltd* [1980] 1 WLR 277, 283, 297, 300.

103 *Woodar Investment Development Ltd v Wimpey Construction (UK) Ltd* [1980] 1 WLR 277, 283, 297.

104 *Woodar Investment Development Ltd v Wimpey Construction (UK) Ltd* [1980] 1 WLR 277, 300.

More recently, in *Alfred McAlpine Construction Limited v Panatown Ltd*,[105] the House of Lords held, by a majority of 3-2, that where a direct remedy is available to the third-party beneficiary against the promisor (as, in this case, under another contract), then the promisee is entitled to only nominal damages. The correctness of *Jackson v Horizon Holidays Ltd* was not considered. The dissenting judges, Lord Goff and Lord Millett, held that the promisee could be seen as suffering a loss as a result of not receiving the bargain for which it had contracted. The promisee was therefore entitled to substantial damages to protect its "performance interest", that is, its interest in the performance of contractual obligations owed to it.[106] This approach would justify the result in *Jackson v Horizon Holidays Ltd*, but on a different basis.

In *Trident v McNiece*, Mason CJ and Wilson J doubted the basis of the decision in *Jackson v Horizon Holidays Ltd* and described its uncertain status as a "telling indictment against the law as it presently stands".[107] Brennan J also noted the uncertainty and suggested that a development of the damages rules would be a more appropriate means to redress any injustice caused by the privity rule than accepting a third party's right to sue.[108]

Specific performance

[11.70] Specific performance is a particularly useful remedy for the enforcement of a promise made for the benefit of a third party. The remedy can be sought by the promisee and, if granted, will result in the third party obtaining the promised benefit. Specific performance will only be granted where damages are inadequate, but it is accepted that damages will be an inadequate remedy for breach of a promise to confer a benefit on a third party, even where the promise is simply to pay money.[109] There are, however, many situations in which the remedy of specific performance will be unavailable or unsuitable. For example, the courts will not decree specific performance where the contract involves the performance of personal services, the supervision of the court would be required to enforce the decree or the decree would be futile.[110] In cases where performance is required at a particular time or defective performance has been tendered, such as in *Jackson v Horizon Holidays Ltd*,[111] specific performance is not a suitable remedy. Moreover, specific performance will only be available where the promisee is willing or obliged by a trust to sue on behalf of the third party.[112]

105 *Alfred McAlpine Construction Limited v Panatown Ltd* [2001] 1 AC 518.

106 *Alfred McAlpine Construction Ltd v Panatown Ltd* [2001] 1 AC 518, 553, 590, adopting a principle articulated by Lord Griffith in *Linden Gardens Trust Ltd v Leneston Sludge Disposals Ltd* and *St Martins Property Corporation Ltd v Sir Robert McAlpine Ltd* [1994] 1 AC 85, 96–8, which has received considerable support in the academic literature. See further Coote, "The Performance Interest, Panatown, and the Problem of Loss" (2001) 117 *Law Quarterly Review* 81.

107 *Trident v McNiece* (1988) 165 CLR 107, 119.

108 *Trident v McNiece* (1988) 165 CLR 107, 139.

109 *Coulls v Bagot's Executor and Trustee Co Ltd* (1967) 119 CLR 460, 478, 503; *Trident v McNiece* (1988) 165 CLR 107, 119, 138, 158; *Beswick v Beswick* [1968] AC 58.

110 See [30.80].

111 *Jackson v Horizon Holidays Ltd* [1975] 3 All ER 92.

112 *Trident v McNiece* (1988) 165 CLR 107, 120.

REASONS FOR ABOLISHING THE PRIVITY DOCTRINE

[11.75] As Mason CJ and Wilson J noted in *Trident v McNiece*,[113] numerous criticisms have been directed at the doctrine of privity and there is much substance in these criticisms. The arguments in favour of reforming the privity rule were considered by the English Law Commission[114] and were neatly summarised in an article by Law Commissioner Burrows.[115] Those arguments are as follows:

1. The privity rule thwarts the intentions of contracting parties. Even where the promisor and promisee unambiguously manifest an intention that the third party should obtain the right to enforce the promise, the privity rule prevents the courts from giving effect to that intention. The privity rule therefore operates as a constraint on freedom of contract.
2. The privity rule may cause injustice to the third party, by denying a benefit that the third party reasonably expects to receive and by denying a right the third party might reasonably expect to have. Where the third party relies to his or her detriment on the contractual promise, injustice may be avoided by the availability of equitable estoppel.
3. The privity rule prevents a person (the third party) who has suffered a loss through non-fulfilment of the promise from suing, while allowing a person (the promisee) who may have suffered no loss to sue. The limited effectiveness of the remedies available to the promisee in respect of a breach of a promise to benefit a third party may also be regarded as a source of injustice.
4. Even where substantial damages or specific performance may be granted, the availability of these remedies is dependent upon the promisee's willingness and ability to sue.
5. The fact that plaintiffs have resorted to a wide range of common law and statutory means of circumventing the privity rule suggests that the rule is unjust. It is unlikely that the various means of circumventing the rule will have resolved all injustices.
6. The range of exceptions makes the law complex, artificial and uncertain.
7. Those few jurisdictions that do not recognise third-party rights arising by way of contract should do so in the interests of harmonisation. The notion that a third party can acquire enforceable rights under a contract is recognised in civil law systems.[116] The German Civil Code, for example, provides that a contract can stipulate for performance to a third party, with the effect that "the third party directly acquires the right to demand performance".[117] Even within the common law world, the privity doctrine is increasingly being abandoned. The privity doctrine has gradually been abrogated throughout the United States through legislative and judicial development. The right of third parties to enforce contracts made for their benefit is recognised by the *Restatement of Contracts* (2d)

113 *Trident v McNiece* (1988) 165 CLR 107, 118.

114 *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Com No 242, 1996).

115 Burrows, "Reforming Privity of Contract: Law Commission Report No 242" [1996] *Lloyd's Maritime and Commercial Law Quarterly* 467, 468–71.

116 Burrows, "Reforming Privity of Contract: Law Commission Report No 242" [1996] *Lloyd's Maritime and Commercial Law Quarterly* 467, 470.

117 *Bürgerliches Gesetzbuch*, §328(1).

(US) ss 302-15.[118] Legislation in New Zealand, New Brunswick, England, Queensland, the Northern Territory and Western Australia allows third parties to sue on contracts made for their benefit.[119] In Canada, the privity rule is being undermined through the development of "principled exceptions", although thus far the Supreme Court has stopped short of a wholesale abolition of the doctrine.[120]

8. The injustice and inconvenience of the rule has long been recognised by judges and academics.[121] Numerous law reform bodies, beginning with the English Law Revision Committee in 1937,[122] have advocated reform.

9. The privity rule causes difficulty in particular situations for parties to commercial contracts who wish to confer benefits on third parties. It would be more convenient if contracts could create enforceable third-party rights.

REASONS FOR RETAINING THE PRIVITY DOCTRINE

[11.80] The arguments for reforming the privity rule set out at [11.75] are not universally accepted.[123] The retention of the privity doctrine has been justified on the basis of the practical and theoretical considerations set out at [11.85]-[11.90].

Practical considerations

[11.85] Mason CJ and Wilson J pointed in *Trident v McNiece*[124] to three practical policy considerations sometimes invoked to justify the privity and consideration rules. First, if both the promisee and the third party can enforce a promise to benefit the third party, double recovery from the promisor is possible. This risk can, however, be avoided by requiring joinder of all parties in the first action[125] or by creating special rules to prevent double recovery.[126] Secondly, the privity doctrine protects a promisor from exposure to liability to a large number of potential plaintiffs. A contractual promise made to a government, for example, may be intended to benefit a class of persons.[127] Thirdly, and most significantly, the entitlement of a third party to enforce a contract might constrain the freedom of action of the promisor and promisee. The privity rule ensures that, whatever benefits are promised to third parties, the promisee is free to rescind the contract, modify it by agreement with the promisor or

118 See Farnsworth, *Farnsworth on Contracts* (1990), Ch 10. The landmark cases were *Lawrence v Fox*, 20 NY 268 (1859) and *Chate, Hall & Stewart v SCA Services Inc*, 392 NE 2d 1045 (1979).

119 See [11.95]–[11.120].

120 See *London Drugs Ltd v Kuehne & Nagel International Ltd* [1992] 3 SCR 299; *Fraser River Pile & Dredge Ltd v Can-Drive Services Ltd* [1999] 3 SCR 108.

121 See the references cited by Burrows, "Reforming Privity of Contract: Law Commission Report No 242" [1996] *Lloyd's Maritime and Commercial Law Quarterly* 467, 468–71.

122 United Kingdom Law Revision Committee, Sixth Interim Report, *Statute of Frauds and the Doctrine of Consideration* (1937, Cmd 5449).

123 Stevens, "The Contracts (Rights of Third Parties) Act 1999" (2004) 120 *Law Quarterly Review* 292 challenges each of them.

124 *Trident v McNiece* (1988) 165 CLR 107.

125 *Trident v McNiece* (1988) 165 CLR 107, 121; see also *Property Law Act 1969* (WA), s 11(2)(b).

126 As does the *Contracts (Rights of Third Parties) Act 1999* (UK), s 5.

127 *Trident v McNiece* (1988) 165 CLR 107, 122.

compromise or assign his or her contractual rights.[128] Modification of the privity rule requires a balancing of the interests of the third party with those of the promisee.

In *Trident v McNiece*, Brennan and Dawson JJ cited the difficulties encountered in developing a set of rules to deal with these issues as a reason to retain the privity rule.[129] Brennan J said:

> The difficulties encountered in propounding a set of rules to condition the proposed exception to the doctrine of privity demonstrate the undesirability of endeavouring now overthrow the doctrine in whole or (what might be more confusing) in part.[130]

Theoretical considerations

[11.90] In a series of articles, Kincaid has argued that it is not unjust to deny third parties the right to sue on contracts made for their benefit and it is in fact unjust to allow them to do so.[131] Kincaid argues that the essence of contract is bargain, involving promise and exchange. His conception of contract is one in which obligations are privately assumed, not imposed by the law.[132] A third party who is promised a benefit under a contract has not participated in the bargain or exchange and has not paid a price for the promise. Accordingly, there is no relationship between the promisor and the third party that justifies the recognition of an obligation. Contract law, according to Kincaid, should be concerned with balancing the private interests of the parties and not giving effect to public interests. The recognition of third-party rights gives public interests priority over private interests. Whether contract is, or should be, exclusively concerned with the enforcement of bargains, the balancing of private rights and the enforcement of assumed, rather than imposed obligations is, of course, a matter of great debate.[133]

Kincaid also argues that the justifications advanced by the English Law Commission do not stand up to close scrutiny. The three principal justifications are giving effect to the parties' intentions, fulfilling the third-party beneficiary's reasonable expectations and protecting the third-party beneficiary's reliance on the promise. The intention to benefit a third party does not of itself justify the imposition of an obligation. Obligation in contract is not based on intention alone, Kincaid suggests, but on bargain. If the third party's reliance is the justification for imposing liability on the promisor, then Kincaid says the promisor's liability must lie outside contract and must be limited to rectifying the harm caused by reliance, rather than having the effect of realising the third party's expectations.

STATUTORY MODIFICATION OF THE PRIVITY DOCTRINE

[11.95] The privity rule has been modified by statute in several jurisdictions, but the modifications have been far from uniform. Burrows has identified five issues that need to be

128 *Trident v McNiece* (1988) 165 CLR 107, 122.

129 *Trident v McNiece* (1988) 165 CLR 107, 138, 162.

130 *Trident v McNiece* (1988) 165 CLR 107, 138.

131 Kincaid, "Third Parties: Rationalising a Right to Sue" [1989] *Cambridge Law Journal* 243; "The Trident Insurance Case: Death of Contract" (1989) 2 *Journal of Contract Law* 160; "Privity and the Essence of Contract" (1989) 12 *University of New South Wales Law Journal* 59; "The UK Law Commission's Privity Proposals and Contract Theory" (1994) 8 *Journal of Contract Law* 51; "Privity and Private Justice in Contract" (1997) 12 *Journal of Contract Law* 47; "Privity Reform in England" (2000) 116 *Law Quarterly Review* 43.

132 Kincaid, "Privity and Private Justice in Contract" (1997) 12 *Journal of Contract Law* 47, 57.

133 See Chapter 1.

resolved if third parties are to be given the right to enforce contracts.[134] These issues have been resolved in different ways in different jurisdictions.

The test of enforceability

[11.100] The first issue is when a third party will acquire a right to enforce a contract. Should it arise whenever the contracting parties intend a third party to benefit from a contract? Should it depend on the contracting parties intending that the third party should be able to sue? Should the right arise only when the third party has expressly accepted the benefit of the contract?[135]

Under the Western Australian legislation, the contract must expressly purport to confer a benefit directly on the third party.[136] The *Insurance Contracts Act 1984* (Cth) requires only that the third party be specified or referred to as a person to whom the cover extends.[137] The Queensland and Northern Territory legislation requires that the promise "appears to be intended to create a duty enforceable by a beneficiary"[138] and that the beneficiary accept the promise.[139] In *Trident v McNiece*,[140] Mason CJ and Wilson J noted that the parties are unlikely to turn their attention to the question of enforcement, so the ascertainment of this intention is likely to be fraught with problems. The English legislation allows a third party to enforce a term if the contract expressly provides that he or she may or if it simply confers a benefit on him or her, provided the parties did not appear to intend that the third party should have no right of enforcement.[141]

Variation and rescission

[11.105] The second issue is the extent to which the promisee should retain the right to vary, rescind or terminate the contract. Under the Queensland legislation, the promisor and promisee may, prior to acceptance by the third-party beneficiary, vary or discharge the contract without the beneficiary's consent.[142] Once the beneficiary has communicated his or her acceptance of the contract to the promisor, the beneficiary's consent is required to vary or discharge the promise.[143] The Western Australian legislation allows cancellation or modification by the

134 Burrows, "Reforming Privity of Contract: Law Commission Report No 242" [1996] *Lloyd's Maritime and Commercial Law Quarterly* 467, 471–81.

135 See *Trident v McNiece* (1988) 165 CLR 107, 122–3.

136 *Property Law Act 1969* (WA), s 11(2). See *Westralian Farmers' Co-operative Ltd v Southern Meat Packers Ltd* [1981] WAR 241; *Visic v State Government Insurance Co Ltd* (1990) 3 WAR 122.

137 *Insurance Contracts Act 1984* (Cth), s 48.

138 *Property Law Act 1974* (Qld), s 55(6); *Law of Property Act* (NT), s 56(6). See *Northern Sandblasting Pty Ltd v Harris* (1997) 188 CLR 313. The Northern Territory provision is almost identical to that in Queensland.

139 *Property Law Act 1974* (Qld), s 55(1); *Law of Property Act* (NT), s 56(1). See *Hyatt Australia Ltd v LTCB Australia Ltd* [1996] 1 Qd R 260.

140 *Trident v McNiece* (1988) 165 CLR 107, 123.

141 *Contracts (Rights of Third Parties) Act 1999* (UK), s 1. The *Contract and Commercial Law Act* 2017 (NZ), s 13 contains a similar proviso. For explanation of the operation of the English legislation, see Burrows, "The Contracts (Rights of Third Parties) Act 1999 and its Implications for Commercial Contracts" [2000] *Lloyd's Maritime and Commercial Law Quarterly* 540 and Beale, "A Review of the Contracts (Rights of Third Parties) Act 1999" in Burrows and Peel (eds), *Contract Formation and Parties* (2010), 225.

142 *Property Law Act 1974* (Qld), s 55(2). See also *Law of Property Act* (NT), s 56(2). Cf *Fraser River Pile & Dredge Ltd v Can-Drive Services Ltd* [1999] 3 SCR 108, [36].

143 *Property Law Act 1974* (Qld), s 55(3)(d); *Law of Property Act* (NT), s 56(3)(d).

parties at any time prior to adoption of the contract by the third-party beneficiary. In England, the parties lose their right to rescind or vary the contract if the third party communicates assent to the term or relies on the term, where the promisor knows of or should reasonably expect reliance.[144] The New Zealand legislation also limits the parties' capacity to vary or discharge the contract if the beneficiary has materially altered his or her position in reliance on the promise or obtains judgment on the promise.[145]

Defences, set-offs and counterclaims

[11.110] The third issue is whether the promisor should be entitled to raise against the third party any defences, counterclaims or set-offs available against the promisee. Under the Western Australian legislation, any defences that would have been available to the promisor had the third party been named as a party is available.[146] The *Insurance Contracts Act 1984* (Cth) similarly provides that any defences that would be available against the promisee are available against the third party.[147] In Queensland, any matter that would in other proceedings render a promise void, voidable or unenforceable or operate as a defence has the same effect in proceedings brought under the section.[148] The English legislation makes more comprehensive provision to ensure that any defence, set-off or counterclaim that would have been available against the promisee is available against the third party.[149]

Promisee's right to sue

[11.115] The fourth issue is whether the promisee should retain the right to sue, in addition to the third party. The Western Australian legislation requires each party named in the contract to be joined as a party to the action instituted by the third party.[150] This prevents double recovery by ensuring that the resulting decision is binding on all parties.[151] The English legislation expressly preserves the promisee's right to sue and avoids double recovery by giving the court discretion to deduct any amount the promisor has paid to the promisee from the award to the third party.[152] The Queensland legislation is silent on this issue.

Preservation of the third party's other rights

[11.120] The final issue is whether the other rights available to the third party, such as by way of estoppel or trust, should be preserved. The English legislation specifically preserves any rights or remedies available to a third party.[153] The Queensland, Northern Territory and Western Australian provisions are silent on this issue, but there is nothing to suggest that the statutory right granted to the third party would affect any other rights he or she might have.

144 *Contracts (Rights of Third Parties) Act 1999* (UK), s 2.
145 *Contract and Commercial Law Act* 2017 (NZ), ss 14–16.
146 *Property Law Act 1969* (WA), s 11(2)(a).
147 *Insurance Contracts Act 1984* (Cth), s 48(3).
148 *Property Law Act 1974* (Qld), s 55(4). See also *Law of Property Act* (NT), s 56(4).
149 *Contracts (Rights of Third Parties) Act 1999* (UK), s 3.
150 *Property Law Act 1969* (WA), s 11(2)(b).
151 *Trident v McNiece* (1988) 165 CLR 107, 121.
152 *Contracts (Rights of Third Parties) Act 1999* (UK), s 5.
153 *Contracts (Rights of Third Parties) Act 1999* (UK), s 7.

EXPRESS TERMS

PART V

Disputes over terms

[PtV.05] The rights and obligations of the parties to a contract are determined primarily by the terms of that contract. Disputes over the existence, meaning and content of the terms arise where, in the course of performing the contract, the parties disagree on what one or other of them is required or entitled to do. One party may allege that the other party has not performed his or her side of the bargain. The other party may argue that he or she was not under any obligation of the kind alleged, either because the parties did not agree on a term imposing such an obligation or because the term in dispute does not mean what the dissatisfied party contends.

There are potentially five matters to consider in attempting to resolve disputes about the terms of a contract. First, it will be necessary to identify the express terms of the contract agreed by the parties, an issue discussed in Chapter 12. Secondly, the terms must be construed to determine their meaning and legal effect, or, in other words, whether the terms apply to resolve the dispute in question. Contract construction is discussed in Chapter 13. Thirdly, in both identifying the terms of the contract and in construing their meaning, it may be necessary to consider the admissibility of extrinsic evidence (ie, the evidence outside the written contract itself). The application of the rule that applies to determine this issue, known as the parol evidence rule, is also discussed in Chapters 12 and 13. Fourthly, if the express terms of the contract prove silent on the issue in dispute, it must be determined whether there is a gap in the terms into which the court may imply a term dealing with the issue in dispute. Gap-filling terms are discussed in Part VI. Fifthly, it may be necessary to consider the effect of statute on the parties' contractual rights and obligations. Statutory regulation of consumer contracts is considered in Chapters 16 and 17.

The objective approach

[PtV.10] In identifying the terms of the contract and in construing those terms the courts sometimes express a concern to give effect to the "common intentions" or "presumed intentions" of the parties.[1] However, in this context, courts do not refer to the private or subjective intentions of the parties. Rather, the modern law of contract favours an objective approach.[2] The objective approach, combined

1 For example, *Fitzgerald v Masters* (1956) 95 CLR 420, 426; *Australian Broadcasting Commission v Australasian Performing Rights Association Ltd* (1973) 129 CLR 99, 101; *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41, 61–62.

2 See, for example, *Life Insurance Co of Australia Ltd v Phillips* (1925) 36 CLR 60; *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 352, 401;

with the parol evidence rule,[3] means that the subjective beliefs of the parties about the scope and meaning of their contract are generally irrelevant.[4] References to "intention" in contract law usually mean "the intention which reasonable persons would have had if placed in the situation of the parties".[5]

The justification for the objective approach relates to its role in protecting the security of bargains.[6] One party to a contract may not share the other party's private thoughts about the content or meaning of that contract. Each party can be expected to have adopted a reasonable interpretation of what the other party said or did. Adopting an objective approach means that both parties can rely on a reasonable interpretation of their contract, rather than risking the contract being set aside on grounds of a lack of subjective consensus between them. From an economic perspective, it may also be argued that the objective approach protects the security of the bargain in an efficient manner.[7] The objective approach puts the onus on each party to clarify any intentions that would not be suggested by a reasonable interpretation of the contract. In the absence of an objective approach, the other party would need to take steps to clarify the subjective intentions of the first party. It will usually be easier for the first party to clarify its own intentions than for the other party to have to inquire into those intentions. Attempting to ascertain the actual intentions of the parties would also be time-consuming and expensive for a court.[8]

In most cases, the subjective intentions of the parties will coincide with the intentions that a reasonable person would attribute to them. But in making a contract, the parties necessarily subject themselves to the court's objective interpretation of their rights and obligations and thus to the possibility that the court will not give effect to the contract the parties privately intended to make. This possibility is starkly illustrated by the decision in *Brambles Holdings Ltd v Bathurst City Council*.[9]

The case concerned the interpretation of a series of contracts under which Brambles managed a waste disposal depot on behalf of the council. One of the questions for the court was whether liquid waste fell within the expression "general commercial waste" used in a contract made on 12 July 1990. Both the trial judge and the New South Wales Court of Appeal held that, on an objective interpretation, "general commercial waste" did include liquid waste. Evidence of a mutual belief that the contract did not regulate the charging of fees for liquid waste was held to be irrelevant and inadmissible. That evidence included correspondence in January and February 1990 in which the parties made an arrangement regarding liquid waste that was inconsistent with the July 1990 contract. It included post-contractual conduct relating to liquid waste that was consistent with the January/February arrangement and

Taylor v Johnson (1983) 151 CLR 422; *Pacific Carriers Ltd v BNP Paribas* [2004] HCA 35; (2004) 218 CLR 451; *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [40].

3 See Chapter 14.

4 See, for example, *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153; *Pacific Carriers Ltd v BNP Paribas* [2004] HCA 52; (2004) 218 CLR, [22].

5 *Reardon Smith Line v Hansen-Tangen* [1976] 1 WLR 989, 996; *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41, 62; *Equuscorp Pty Ltd v Glengallan Investments Pty Ltd* [2004] HCA 55; (2004) 218 CLR 471, [34].

6 See Mason and Gageler, "The Contract" in Finn (ed), *Essays on Contract* (1987), p 4. Also *Equuscorp Pty Ltd v Glengallan Investments Pty Ltd* [2004] HCA 55; (2004) 218 CLR 471, [35].

7 See Posner, *Economic Analysis of Law* (9th ed, 2014) § 4.3.

8 See *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 352.

9 [2001] NSWCA 61; (2001) 53 NSWLR 153.

inconsistent with the fee structure set up in the July contract. Finally, it included testimony from the relevant officers of each of the contracting parties indicating that they believed the July contract did not relate to liquid waste.[10]

Ipp AJA held that the parties were "wrong" in their understanding of the meaning of the agreement. Ipp AJA observed that "the parties (wrongly in my view) believed that the July 1990 contract … did not regulate the charging of fees for liquid wastes".[11] Referring to the trial judge's interpretation of the July 1990 contract, Heydon JA noted that:

> There is some evidence that in 1990 and 1991 both the Council and the defendant did not share his conclusions, but in the absence of any argument for a decree of rectification or for an estoppel by convention the actual opinions of the parties are irrelevant.[12]

The objective approach to identifying and interpreting the terms of a contract causes difficulties for any theory of contract based on the will or consent of the parties themselves, such as classical contract theory and promise or consent theories.[13] The objective approach appears to disregard what the parties themselves actually thought they were consenting to or promising. In other words, as illustrated in *Brambles Holdings Ltd v Bathurst City Council*,[14] the objective approach may have the consequence of separating contractual obligations from the will of the parties.[15] Similar difficulties are raised when a court is prepared to imply terms into a contract. The challenge to contract theories posed by the objective approach is discussed further in Chapter 14.

10 [2001] NSWCA 61; (2001) 53 NSWLR 153, [133]–[136].

11 [2001] NSWCA 61; (2001) 53 NSWLR 153, [147].

12 [2001] NSWCA 61; (2001) 53 NSWLR 153, [46].

13 See Chapter 1.

14 [2001] NSWCA 61; (2001) 53 NSWLR 153.

15 For criticism of this approach McLauchlan, "The New Law of Contract Interpretation" [2000] *New Zealand University Law Review* 147, 166–7.

CHAPTER **12**

Identifying the express terms

TERMS AND THE COMMUNICATIONS OF THE PARTIES

[12.05] In simple cases, the terms of a contract will be those proposed by the offeror and accepted by the offeree.[1] In more complex cases, the rules of offer and acceptance may not prove an easy way of identifying the terms of the contract. For example, where there has been protracted correspondence or long, drawn out negotiations, it may be unclear which proposed terms or negotiating statements were intended to bind the parties.

In significant transactions, contracting parties will usually record the terms of their agreement in a formal, written document, which is signed by the parties and which then embodies the "contract" between them. In such cases, the terms of the contract will be those contained in the contractual document. However, except where required by statute, the terms of a contract do not need to be recorded in a formal written contract. The terms of a contract may be found in any of the communications through which the contract was made, such as through email correspondence, letters or telephone conversations. The terms of a contract may also be incorporated through a notice or sign displayed at a trader's premises or website. It is also possible to have a contract that is partly oral and partly written, in which case the

1 See Chapter 3.

terms of the contract will be those contained in any written document and supplemented by oral promises.

This chapter discusses the ways in which courts identify the terms of a contract. It considers the significance of a signed contractual document, the possibility of terms being incorporated into a contract through notice and the incorporation of terms through a course of dealings between the parties. The chapter then considers the rules for determining when statements made during negotiations amount to contractual terms and, in cases where there is a written contract, the rule of evidence governing the admissibility of oral and other extrinsic evidence of terms other than those contained in the written document, known as the "parol evidence rule".

WRITTEN TERMS AND THE EFFECT OF SIGNATURE

The rule in *L'Estrange v F Graucob Ltd*

[12.10] The general rule is that a person who signs a contractual document will be bound by the terms in that document, regardless of whether he or she has read or understood those terms.[2] This rule is often referred to as the rule in *L'Estrange v Graucob*.[3] In *L'Estrange v F Graucob Ltd*[4] Ms L'Estrange, the plaintiff, purchased a cigarette vending machine from the defendant, F Graucob Ltd. The plaintiff signed a form headed "Sales Agreement", which contained printed terms of sale. When the machine was delivered, it did not work satisfactorily. The plaintiff brought an action for damages for breach of an implied warranty that the machine was reasonably fit for the purposes for which it was required. The defendant relied upon the following clause in the sales agreement:

> The agreement contains all the terms and conditions under which I agree to purchase the machine specified above and any express or implied condition, statement, or warranty, statutory or otherwise not stated herein is hereby excluded.

The trial judge gave judgment for the plaintiff. The trial judge held that there had been a breach of the implied warranty and that, when she had signed the form, the plaintiff had no knowledge of its contents except for the price, instalments and the arrangements for installing the machine. The trial judge held that the typeface used in the form was unreasonably small and that the defendant did not do what was reasonably sufficient to give the plaintiff notice of the terms contained in it. The Divisional Court allowed an appeal by the defendant. The Divisional Court held that "the plaintiff, having put her signature to the document and not having been induced to do so by any fraud or misrepresentation, cannot be heard to say that she is not bound by the terms of the document because she has not read them".[5]

The rule in *L'Estrange v Graucob* is well established in Australian law.[6] In *Toll (FGCT) Pty v Alphapharm Pty Ltd*, the High Court stated that:

> The general rule, which applies in the present case, is that where there is no suggested vitiating element, and no claim for equitable or statutory relief, a person who signs a document which

2 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [57].
3 *L'Estrange v F Graucob Ltd* [1934] 2 KB 394.
4 *L'Estrange v F Graucob Ltd* [1934] 2 KB 394.
5 *L'Estrange v F Graucob Ltd* [1934] 2 KB 394, 404.
6 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [46].

> is known by that person to contain contractual terms, and to affect legal relations, is bound by those terms, and it is immaterial that the person has not read the document.[7]

The legal significance of signature is widely recognised in the general community and is certainly well established in the business community. Thus, the act of signing a contractual document is generally seen in law and in practice as representing a willingness to be bound to the terms contained in the document. As explained by the High Court of Australia in *Toll (FGCT) Pty v Alphapharm Pty Ltd*:

> [T]o sign a document known and intended to affect legal relations is an act which itself ordinarily conveys a representation to a reasonable reader of the document. The representation is that the person who signs either has read and approved the contents of the document or is willing to take the chance of being bound by those contents … whatever they might be.[8]

Circumstances in which the effect of signature may be avoided

[12.12] There are a number of circumstances where signature will not apply to bind parties to a written document containing terms.[9] In *Toll (FGCT) Pty v Alphapharm Pty Ltd*, the High Court recognised that the rule making signature binding assumes:

> [T]he absence of any grounds, such as a plea of non est factum, which at common law would render the contract void and of any grounds, such as misrepresentation, which might attract equitable relief, or which might elicit curial dispensation under a statutory regime.[10]

Misrepresentation

[12.15] The signature rule in *L'Estrange v Graucob* will not apply where the contents of the document being signed have been misrepresented, where the plea of non est factum[11] would apply, or where there are equitable grounds for setting aside the contract.[12]

In *Curtis v Chemical Cleaning and Dyeing Co*[13] Curtis took a white satin wedding dress to the defendant for cleaning. The defendant's shop assistant handed Curtis a paper headed "Receipt" which she was asked to sign. Before doing so, Curtis asked why her signature was required and was told that it was because the defendant would not accept liability for certain specified risks, including the risk of damage to the beads and sequins with which the dress was trimmed. Curtis then signed the "Receipt". In fact, the paper contained a term excluding the defendant from liability for any damage "howsoever arising". When the dress was returned, there was a stain on it. Curtis claimed damages. The English Court of Appeal considered that the defendant was not able to rely on the exemption clause to exclude its liability for the damage. The defendant's assistant had misrepresented the breadth of the exemption clause in the document and, as a result, the clause did not become part of the contract.[14]

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7 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [57].
8 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [45].
9 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [57].
10 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [49].
11 See Chapter 32.
12 *Toll (FGCT) Pty v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [57]. See further Part XI of this book.
13 *Curtis v Chemical Cleaning and Dyeing Co* [1951] 1 KB 805.
14 *Curtis v Chemical Cleaning and Dyeing Co* [1951] 1 KB 805, 809–10.

Where one party has been misled about the nature or extent of contractual terms, such as *Curtis v Chemical Cleaning and Dyeing Co*,[15] the rule in *L'Estrange v Graucob* does not apply and the term in question is not binding on the parties. In such circumstances, the misled party may also seek to be released from the contract on the basis of misrepresentation or on the basis of the legislative prohibitions on misleading or deceptive conduct.[16]

In *Toll (FGCT) Pty v Alphapharm Pty Ltd*, the High Court left open the possibility that the presence of unusual terms in a signed contractual document might amount to a misrepresentation so as to render those terms non-binding.[17] The case concerned an exclusion clause relating to the terms of transport of goods that was contained in a signed document headed "Application for Credit". The party affected argued that the term was unusual in this type of contract and should not be binding in the absence of notice of the term being given to it before signing. The argument was rejected by the High Court. The Court noted that the document "invited" the person signing to read the terms it contained.[18] The High Court did not consider the term in question unusual in the contract in question.[19] The High Court also strongly affirmed the general rule that signature is binding regardless of whether the party signing had read the relevant terms.

The High Court also acknowledged a role for misrepresentation as an exception to the signature rule. The Court stated that there "may be cases where the circumstances in which a document is presented for signature, or the presence in it of unusual terms, could involve a misrepresentation".[20] Given the Court's strong affirmation of the signature rule, the scope for arguing that the signature rule does not apply in a particular case to bind a party signing a contract containing unusual terms on the basis of misrepresentation must be very narrow and viable only in extraordinary circumstances.[21] The High Court itself suggested that there would have to be some element of "concealment" for this kind of argument to succeed.[22]

Non-contractual documents

[12.20] The rule in *L'Estrange v Graucob* applies where a person signs a "contractual document", that is, a document known to contain contract terms and intended to affect legal relations.[23] The rule will not apply where the document in question could not reasonably be considered a contractual document. As recognised by the High Court in *Toll (FGCT) Pty v Alphapharm Pty Ltd*,[24] if a document, or the circumstances in which a document is presented for signature, are such as to mislead the person signing as to the significance of that conduct, the contractual effect of signature will be negated.[25] Accordingly, a person will not be bound

15 *Curtis v Chemical Cleaning and Dyeing Co* [1951] 1 KB 805.

16 See Chapter 33.

17 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [63].

18 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [39], [52].

19 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [64].

20 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [63].

21 See [12.15].

22 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [64].

23 *Toll (FGCT) Pty v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [57].

24 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165.

25 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [63]. For a possible example see *Le Mans Grand Prix Circuits Pty Ltd v Iliadis* [1998] 4 VR 661.

by signing a document that reasonably appears merely to be a timesheet,[26] or a receipt or voucher.[27]

For example, in *Curtis v Chemical Cleaning and Dyeing Co*,[28] discussed at [12.15], Denning LJ suggested that even if the assistant had not misrepresented the extent of the clause, Curtis might not have been bound by the exemption clause. Denning LJ considered that Curtis might reasonably have understood the document only to be a receipt to be presented when collecting the dress and not to contain contractual terms.[29]

Criticisms of the rule

[12.25] Spencer suggests that English courts' approach to signature may have been based on a concern about allowing parties to escape the apparent assumption of contractual obligation by claiming they were unaware of the terms.[30] In *Blay v Pollard & Morris*, Scrutton LJ said:[31]

> It would be very dangerous to allow a man over the age of legal infancy to escape from the legal effect of a document he has, after reading it, signed, in the absence of any express misrepresentation by the other party of that legal effect.

The courts' practice of strictly applying the signature rule has nonetheless been subject to robust criticism.[32] The rule takes the objective fact of a party's signature as indicating his or her acceptance of the terms in the signed document, without considering the reality of whether that party was aware of the terms or understood their impact. While well-resourced commercial entities can be expected to ensure that they are adequately informed about the obligations they are assuming under a signed contract, the experience of other contracting parties may be quite different. Other kinds of contracting parties, such as consumers or small business owners, may sign contracts without reading the terms due to pressures of time. As in *L'Estrange v F Graucob Ltd*, the terms may be difficult to read or involve unfamiliar legal concepts. If they read the contract, such parties may not have the skills needed to assess the impact of the terms or the effect of the risks allocated to them. Studies in behavioural economics suggest that individual contracting parties typically find it difficult to assess future risk, and instead tend to base decisions on a few key or salient factors, such as price and quality rather than the fine print details at the back of a contract.[33]

These considerations raise real doubts as to whether signature can be equated with consent for the purposes of inferring agreement to the terms of a written signed contract. Consent

26 *Grogan v Robin Meredith Plant Hire* [1996] CLC 1127.

27 *Chapleton v Barry Urban District Council* [1940] 1 KB 532.

28 *Curtis v Chemical Cleaning and Dyeing Co* [1951] 1 KB 805.

29 *Curtis v Chemical Cleaning and Dyeing Co* [1951] 1 KB 805, 809. See also *DJ Hill & Co Pty Ltd v Walter H Wright Pty Ltd* [1971] VR 749.

30 Spencer, "Signature, Consent, and the Rule in L'Estrange v Graucob" (1973) 32(1) *Cambridge Law Journal* 104, 122.

31 *Blay v Pollard & Morris* [1930] 1 KB 628, 633.

32 See, eg, Chapman, "Common Law, Contract and Consent: Signature and Objectivity" (1989) 49 *Northern Ireland Legal Quarterly* 363, 364–5.

33 On the insights of behavioural economics see further Korobkin, "Bounded Rationality, Standard Form Contracts, and Unconscionability" (2003) 70 *University of Chicago Law Review* 1203; Ramsay, *Consumer Law and Policy* (2nd ed, Hart Publishing, Oxford, 2007), pp 73–4.

in this sense is formal rather than substantive.[34] As we shall see, where there are terms that purport to be part of a contract that is not signed, the courts require reasonable notice of those terms to have been given to the party to be bound.[35] Legislation protecting consumers entering into standard form contracts from unfair terms is discussed in Part VII of this book.

A feminist perspective

[12.30] Frug has analysed the rule regarding signature from a feminist perspective.[36] She discusses *Allied Van Lines Inc v Bratton*[37] which involved facts somewhat similar to *L'Estrange v F Graucob Ltd*[38] and *Curtis v Chemical Cleaning and Dyeing Co*.[39] In *Allied Van Lines v Bratton*[40] two female householders brought actions against a national moving company after their household goods were destroyed in transit. Both women challenged provisions in a standard form contract that limited the moving company's liability for loss and damage. The women argued that these provisions should not bind them because, although they had signed the forms containing the alleged terms of the contract, they had not read the provisions. The Court rejected the argument of one of the women, Mrs Bratton, on the ground that signature was sufficient to bind her to the agreement. The Court accepted the argument of the other woman, Mrs McKnab, on the ground that Mrs McKnab had asked questions about the amount of insurance coverage available under the contract and had been given incorrect information in response.

Frug argues that gender-related ideas are "implicated" in the Court's approach. Frug argues that the Court in *Allied Van Lines v Bratton*[41] adopted a self-reliant view of personhood. Under this view, Mrs Bratton was passive with respect to her own rights under the contract. She did not read or ask questions about the document she signed. In contrast, Mrs McKnab was active in protecting her rights, alerting the agent to her desire for maximum insurance.[42] Frug then explains the relevance of gender to these characterisations of the two women's conduct as follows:[43]

> The court in [Allied Van Lines] protects Mrs McKnab's "masculine" attempt to be autonomous, aggressive, and self-reliant, and the court denies Mrs Bratton relief because she didn't try to conduct her affairs in a similarly "masculine" way. If traditional readers implicitly recognise Mrs McKnab's conduct as masculine and Mrs Bratton's conduct as feminine, accepting Allied will be as natural as the superiority of "male" traits sometimes seems.

Frug argues that the insights provided by some types of feminism challenge this traditional analysis. Frug notes that at trial, Mrs Bratton testified that she did not read the document

34 See Chen-Wishart, "Contractual Mistake, Intention in Formation and Vitiation: The Oxymoron of Smith v Hughes" in Neyers, Bronaugh and Pitel (eds), *Exploring Contract Law* (Hart Publishing, Oxford, 2009) 352.

35 See [12.45]–[12.75].

36 Frug, *Postmodern Legal Feminism* (1992).

37 351 So 2d 344 (Fla, 1977).

38 *L'Estrange v F Graucob Ltd* [1934] 2 KB 394.

39 *Curtis v Chemical Cleaning and Dyeing Co* [1951] 1 KB 805.

40 351 So 2d 344 (Fla, 1977).

41 351 So 2d 344 (Fla, 1977).

42 Frug, *Postmodern Legal Feminism* (1992), pp 96–8.

43 Frug, *Postmodern Legal Feminism* (1992), p 98.

because "the house was really cold; and the men were tired. They were in a hurry to get out". Frug argues that although some people might ignore the workers' discomfort, Mrs Bratton could not.[44] Frug argues that this conduct was consistent with characteristics commonly associated with women:

> Women are socialised to consider and value others' feelings above their own, and Mrs Bratton simply acted like a woman in this situation. Because feminist readers are sympathetic to characteristics commonly associated with women, the court's refusal to evaluate the substantive content of Mrs Bratton's standardised contract will not seem like a neutral judgment to these readers but a preference for male rather than female personality traits.[45]

Moreover, Frug argues that the Court's analysis ignored the power imbalance in the parties' relationship. The agent exercised power over Mrs Bratton through his control and familiarity with the standard form contract and through his status as a man. Requiring Mrs Bratton to inform herself about the contents of the document required her to challenge these forms of power.[46]

Frug suggests that the Court's approach to the case might have been quite different had the Court been sympathetic to issues of gender and "valued feminine as well as masculine personality traits".[47] Frug argues that the Court could have analysed the contract by reference to a co-operative, rather than an adversarial, model.[48] Under such an approach:

> The court could have considered whether Mrs Bratton's agent should have extended more sensitivity and compassion to her by understanding her sympathy for him and his men, by informing her about the insurance option, and by preventing her from signing without indicating the level of coverage she wanted.[49]

INCORPORATION OF TERMS BY NOTICE

[12.35] A business that does not rely on a signed contract in its dealings with customers may instead attempt to incorporate the terms it wants to govern the transaction through the device of notice. Adequate notice given before the contract is made makes those terms binding on both parties, even though no contractual document has been signed. Notice is typically given either through delivering a document containing the terms or displaying a notice containing the terms.[50] For example, the owner of a car park may seek to include in the contract with his or her customers terms which are contained on a ticket provided on entry into the car park or which are displayed on a board at the entrance to the car park.

Whether delivered or displayed terms are incorporated into a contract will depend on two, interrelated issues: first, whether the displayed or delivered terms were made available to the party to be bound by those terms before the contract was formed; and second, whether reasonable steps were taken to bring those terms to the notice of the party to be bound.

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44 Frug, *Postmodern Legal Feminism* (1992), pp 99–100.

45 Frug, *Postmodern Legal Feminism* (1992), p 100.

46 Frug, *Postmodern Legal Feminism* (1992), p 101.

47 Frug, *Postmodern Legal Feminism* (1992), p 100.

48 Frug, *Postmodern Legal Feminism* (1992), p 101.

49 Frug, *Postmodern Legal Feminism* (1992), p 100.

50 In many cases, the terms in question will include exemption clauses but the principles discussed apply generally.

The time at which the terms are available

[12.40] For delivered or displayed terms to be incorporated into a contract, the terms must be made available to the party to be bound before the contract is made. Only terms that have been made available in a timely manner can be incorporated into the contract.[51]

The principle is illustrated in *Oceanic Sun Line Special Shipping Co Inc v Fay*.[52] In this case, a resident of Queensland made a booking in New South Wales for a cruise of the Greek islands. Upon paying the fare, the passenger was given an "exchange order" which stated that it would be exchanged for a ticket upon boarding the cruise ship. When issued, the ticket contained a condition that the courts of Greece would have exclusive jurisdiction in any action against the owner. The passenger was injured on the cruise and sued the owner for negligence in the Supreme Court of New South Wales. The High Court held that the contract for the cruise had been made when the cruise was booked.[53] Accordingly, the conditions on the ticket issued later, when the passenger arrived in Greece, could not form part of the contract.[54]

In *eBay International AG v Creative Festival Entertainment Pty Ltd*,[55] the tickets to a music event, the Big Day Out, issued after the contract was concluded contained a term that was not displayed on the Ticketmaster webpage used by consumers to purchase tickets. Rares J held that this term was misleading; it conveyed the impression of binding consumers when it was not, in fact, incorporated into the contract for the sale of tickets.

Knowledge or notice

[12.45] The second requirement for delivered or displayed terms to be incorporated into a contract is that the party to be bound must either have actual knowledge of the terms or have been given reasonable notice of those terms.[56]

Knowledge

[12.50] A party who knows that a delivered document or a sign displayed before or at the time the contract was made contains contractual terms will be bound by those terms.[57] This will be so regardless of whether or not the party to be bound has actually read the terms.

Reasonable notice of contractual documents

[12.55] Courts have suggested that if a delivered or displayed document is one that a reasonable person would expect to contain the terms of a contract, the mere presentation of the document will be sufficient notice of the terms in that document to ensure that they are binding.[58] For example, it has been suggested that a party entering into a contract for the carriage of goods by sea will normally be bound by the conditions contained in a bill

51 *Oceanic Sun Line Special Shipping Co Inc v Fay* (1988) 165 CLR 197.

52 *Oceanic Sun Line Special Shipping Co Inc v Fay* (1988) 165 CLR 197.

53 *Oceanic Sun Line Special Shipping Co Inc v Fay* (1988) 165 CLR 197, 206, 227, 256, 261.

54 *Oceanic Sun Line Special Shipping Co Inc v Fay* (1988) 165 CLR 197, 207, 228, 256, 261.

55 *eBay International AG v Creative Festival Entertainment Pty Ltd* [2006] FCA 1768; (2006) 170 FCR 450.

56 *Thornton v Shoe Lane Parking Ltd* [1971] 2 QB 163, 170; *Baltic Shipping Co v Dillon (The Mikhail Lermontov)* (1991) 22 NSWLR 1, 8, 24–5 (appealed against to the High Court on other issues: *Baltic Shipping Co v Dillon* (1993) 176 CLR 344).

57 *Parker v South Eastern Railway Co* (1877) 2 CPD 416, 423. See, eg, *Ange v First East Auction Holdings Pty Ltd* [2011] VSCA 335.

58 See further Greig and Davis, *The Law of Contract* (Law Book Co, 1987), pp 613–15.

of lading even if he or she has not read the bill of lading, or did not actually know that it contained contractual terms. The bill of lading is the standard contractual document used in such transactions. As Mellish LJ explained in *Parker v South Eastern Railway Co*:

> [In] the great majority of cases persons shipping goods do know that the bill of lading contains the terms of the contract of carriage; and the shipowner, or the master delivering the bill or lading, is entitled to assume that the person shipping the goods has that knowledge. It is, however, quite possible to suppose that a person who is neither a man of business nor a lawyer might on some particular occasion ship goods without the least knowledge of what a bill of lading was, but in my opinion such a person must bear the consequences of his own exceptional ignorance, it being plainly impossible that business could be carried on if every person who delivers a bill of lading had to stop to explain what a bill of lading was.[59]

Reasonable notice of non-contractual documents

[12.60] Where delivered or displayed terms are not contained in a document that is an obvious or well-understood contractual document, the party seeking to incorporate the terms must take reasonable steps to bring those terms to the notice of the party to be bound. In *Causer v Brown*[60] Mr Causer took his wife's dress to the defendants for dry cleaning. When it was collected, the dress was found to have been damaged. The defendants sought to avoid liability by relying on an exclusion clause printed on a docket handed to Mr Causer when he left the dress at the defendants' shop. Herring CJ in the Supreme Court of Victoria held that the defendants were not entitled to rely on the clause. His Honour said that the docket handed to Mr Causer:[61]

> Was one that might reasonably be understood to be only a voucher for the customer to produce when collecting the goods, and not understood to contain conditions exempting the defendants from their common law liability.

Accordingly, the defendants should have drawn Mr Causer's attention to the existence of the exemption clause.

What amounts to reasonable notice?

[12.65] The reasonable notice required to incorporate delivered or displayed terms into a contract will depend on the circumstances of the particular case. The general principle is that the notice must be in such a form that it is likely to come to the attention of the party to be bound. In *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd* Bingham LJ summarised the effect of the English decisions as follows:

> The tendency of the English authorities has, I think, been to look at the nature of the transaction in question and the character of the parties to it; to consider what notice the party alleged to be bound was given of the particular condition said to bind him; and to resolve whether in all the circumstances it is fair to hold him bound by the condition in question.[62]

Thornton v Shoe Lane Parking Ltd[63] concerned whether a clause exempting the operator of a car park from liability for injury to customers was effective in achieving that result.

59 *Parker v South Eastern Railway Co* (1877) 2 CPD 416, 422.

60 *Causer v Brown* [1952] VLR 1.

61 *Causer v Brown* [1952] VLR 1, 6.

62 *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd* [1989] 2 QB 433, 445.

63 *Thornton v Shoe Lane Parking Ltd* [1971] 2 QB 163.

When the customer in question had entered the car park, he had been issued with a ticket showing the time he entered the car park. The ticket also stated in small print: "[t]his ticket is issued subject to the conditions of issue as displayed on the premises." The conditions were displayed inside the car park and were not visible either from the entrance or the place where the ticket was issued. The English Court of Appeal held that the customer was not bound by the exemption clause. The customer did not know that the ticket was issued subject to the exempting condition, and the operator of the car park had not done what was reasonable to give him notice of it.

Reference to terms that are not readily available

[12.70] In some cases, one party seeking to incorporate terms might advise the other party that the contract is made subject to terms contained in another document; in circumstances where that document is not immediately available to the party to be bound. Typically, this approach has not been sufficient to satisfy the requirement of reasonable notice so as to incorporate the terms into the contract.[64] In *Thornton v Shoe Lane Parking Ltd*[65] the notice relied on by a car park operator referred to terms that customers could not read without getting out of their cars and going into the car park to find the sign containing the terms. These terms were, unsurprisingly, not binding on the customers. No adequate notice of the terms was provided before the contract was made. In *Baltic Shipping Co v Dillon (The Mikhail Lermontov)*[66] the fact that terms contained in a ticket were, prior to the issue of the ticket, available to passengers at the offices of the provider of the cruise "scarcely amounted to a sufficient compliance with the appellant's responsibility to bring unusual conditions at least to the notice of passengers … before they would be bound by them".[67]

Unusual terms

[12.75] Where the terms sought to be incorporated into a contract are unusual or unexpected in the context of the transaction, the party seeking to incorporate those terms must make extra efforts in giving notice of those terms. The notice must be such as will "fairly and reasonably" bring the terms to the attention of the party to be bound.[68] In *J Spurling Ltd v Bradshaw*, Denning LJ commented: "[c]lauses which I have seen would need to be printed in red ink on the face of the document with a red hand pointing to it before the notice could be held to be sufficient."[69] In other words, the prominence of the notice of displayed or delivered terms must be proportionate to the unusual nature of the term.

64 For circumstances where the terms in the other document were available to the party to be bound and could be incorporated by reference, see eg, *Ange v First East Auction Holdings Pty Ltd* [2011] VSCA 335.

65 *Thornton v Shoe Lane Parking Ltd* [1971] 2 QB 163.

66 (1991) 22 NSWLR.

67 *Baltic Shipping Co v Dillon (The Mikhail Lermontov)* (1991) 22 NSWLR 1, 24. See also *eBay International AG v Creative Festival Entertainment Pty Ltd* [2006] FCA 1768; (2006) 170 FCR 450, [52]. Cf *New South Wales Lotteries Corporation Pty Ltd v Kuzmanovski* [2011] FCAFC 106; (2011) 195 FCR 234.

68 *Thornton v Shoe Lane Parking Ltd* [1971] 2 QB 163, 169, 172, 174; *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd* [1989] 2 QB 433, 445; *Baltic Shipping Co v Dillon (The Mikhail Lermontov)* (1991) 22 NSWLR 1, 8, 24 (appealed against to the High Court on other issues: *Baltic Shipping Co v Dillon* (1993) 176 CLR 344); *Livingstone v Roskilly* [1992] 3 NZLR 230, 237. See also *Maxitherm Boilers Pty Ltd v Pacific Dunlop Ltd* [1998] 4 VR 559, 569.

69 *J Spurling Ltd v Bradshaw* [1956] 1 WLR 461, 466.

In *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd*,[70] Interfoto, which ran a library of photographic transparencies, sent to Stiletto, on request, 47 transparencies. Included in the bag with the transparencies was a delivery note setting out the date of dispatch and of return. At the bottom of the note was the heading "Conditions", printed in fairly prominent capitals, and under this heading was set out nine conditions. One of these conditions provided that the transparencies must be returned within 14 days and that a holding fee of £5 per day would be charged for each transparency retained for longer than the 14-day period. Stiletto retained the transparencies for an additional two weeks and was charged a fee of £3783.50. This fee was substantially larger than was usual.[71]

The English Court of Appeal held that Stiletto was not liable to pay the fee. Bingham LJ referred to the civil law principle that in carrying out contracts, parties should act in good faith.[72] Bingham LJ stated that good faith did not simply mean that the parties should not deceive one another; the effect of the duty was "perhaps most aptly conveyed by such metaphorical colloquialisms as 'playing fair', 'coming clean' or 'putting one's cards face upwards on the table' ".[73] Bingham LJ considered that in the present case, it might have been held that Interfoto was under a "duty in all fairness to draw [Stiletto's] attention to the high price payable if the transparencies were not returned in time".[74] However, Bingham LJ noted that English law had not committed itself to such an overriding principle as good faith, responding to issues of unfairness in a more piecemeal fashion.[75]

Analysing the case in terms of traditional doctrine, Bingham LJ and Dillon LJ held that the contract was not made until Stiletto opened the bag containing the photographs.[76] Once the delivery note was taken out, Stiletto would have recognised it as a document reasonably likely to contain contractual terms and would have seen the terms printed on the document. While those terms that were commonly encountered in the business of the parties would have been incorporated into the contract,[77] their Lordships considered that Interfoto did not do what was reasonably necessary to draw the clause in question, which was "unreasonable and extortionate", to the attention of Stiletto.[78]

Concern with sufficiency of the notice of unusual terms was also shown by the New South Wales Court of Appeal in *Baltic Shipping Co v Dillon (The Mikhail Lermontov)*.[79] In this case, the plaintiff paid a deposit for a holiday cruise. Ten days later, the plaintiff received a booking form that stated that a contract of carriage with the shipping company pursuant to the booking was made "only at the time of issuing of tickets". The form said that the contract of carriage would be subject to the conditions printed on the tickets, which were available at the office of the shipping company. The plaintiff paid the full fare and received the ticket two weeks prior to the commencement of the cruise. The conditions printed on the ticket included

70 *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd* [1989] 2 QB 433.

71 *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd* [1989] 2 QB 433, 445.

72 *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd* [1989] 2 QB 433, 439. On good faith, see also Chapter 14.

73 *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd* [1989] 2 QB 433, 439.

74 *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd* [1989] 2 QB 433, 439.

75 *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd* [1989] 2 QB 433, 439.

76 *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd* [1989] 2 QB 433, 445.

77 *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd* [1989] 2 QB 433, 445.

78 *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd* [1989] 2 QB 433, 445.

79 *Baltic Shipping Co v Dillon (The Mikhail Lermontov)* (1991) 22 NSWLR 1.

conditions limiting the liability of the shipping company undertaking the cruise for personal injury and damage to personal effects. During the cruise, the ship sank and the plaintiff sought damages for the losses she had suffered as a result.

The New South Wales Court of Appeal held that the plaintiff was not bound by the conditions purporting to limit the shipping company's liability. The Court accepted the statement in the booking form that the contract of carriage was made at the time of the issue of the ticket to the plaintiff. For the conditions printed on the ticket to have been incorporated in the contract, the passenger must have been given notice of those conditions. Until the plaintiff received the ticket, the only information she had been given about the conditions of carriage was what was contained in the booking form. Gleeson CJ stated that the information contained in the booking form may have been sufficient notice of many of the conditions on the ticket.[80] However, both Gleeson CJ and Kirby J considered that the mere availability of the conditions at the company's office was inadequate notice of the term, when those terms were likely to be unusual or unexpected in the kind of transaction in question, such as those significantly limiting the company's liability.[81]

Contrast with signed contracts

[12.80] As already discussed, signature renders the terms in a signed contractual document presumptively binding on the signing party.[82] In *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd*[83] the High Court reaffirmed the significance of signature in committing contracting parties to the terms contained in a signed contractual document. The Court considered the question of notice would only be relevant in such cases where there was an issue such as misrepresentation, which might displace signature as binding the parties to the contract. The Court explained that:

> If there is a claim of misrepresentation, or non est factum, or if there is an issue as to whether a document was intended to affect legal relations or whether, on the other hand, it was tendered as a mere memorandum of a pre-existing contract, or a receipt, or if there is a claim for equitable or statutory relief, then even in the case of a signed document it may be material to know whether a person who has signed it was given sufficient notice of its contents. The general rule, which applies in the present case, is that where there is no suggested vitiating element, and no claim for equitable or statutory relief, a person who signs a document which is known by that person to contain contractual terms, and to affect legal relations, is bound by those terms, and it is immaterial that the person has not read the document.[84]

The Court dismissed the role of notice as a standard requirement for incorporating terms in a signed contract, with the comment that:

> When an attempt is made to introduce the concept of sufficient notice into the field of signed contracts, there is a danger of subverting fundamental principle based on sound legal policy.[85]

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80 *Baltic Shipping Co v Dillon (The Mikhail Lermontov)* (1991) 22 NSWLR 1, 8–9.

81 *Baltic Shipping Co v Dillon (The Mikhail Lermontov)* (1991) 22 NSWLR 1, 8–9, 24–5. For a case where notice of terms available from a company office was sufficient, see *O'Brien v MGN Ltd* [2001] EWCA Civ 1279.

82 See [12.10].

83 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [54]. Cf Chapman, "Common Law, Contract and Consent: Signature and Objectivity" (1989) 49 *Northern Ireland Legal Quarterly* 363 and in Canada see *Tilden Rent-A-Car Co v Clendenning* (1978) 18 OR (2d) 601.

84 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; [2004] 219 CLR 165, [57].

85 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [54].

Identifying the terms in electronic contracts

[12.85] Many contracts are now made in electronic form, such as by email or over the internet.[86] Clearly, a person purchasing goods or services over the internet is unlikely to have signed a contractual document in a physical sense. Most contracts made online are either "clickwrap" contracts, where the purchaser will have been required to click on a dialogue box that states that the purchaser agrees to the terms of the contract prepared by the seller before proceeding with the transaction, or "browsewrap" contracts, where the purchaser is given notice of the seller's standard terms through a hypertext link displayed on the web page used to purchase the goods.

The act of clicking "I accept" on a website will usually have the same effect as signature in incorporating the terms proposed by the trader into the contract between the parties. Electronic Transactions Acts in force in all Australian States and Territories provide that where a law requires a person's signature, that requirement is taken to have been met if an appropriately reliable method has been used to identify the person and show their intention in relation to the information communicated.[87] A purchaser's act of "clicking", in circumstances where it is stated that this conduct amounts to acceptance of the seller's terms, will usually signal an intention to accept those terms, in the same manner as signature on a hard copy contractual document is taken to indicate consent to the terms contained in that document. Clicking "I accept" may not amount to signature and acceptance of the seller's terms in circumstances where the purchaser would reasonably have understood that act to be performing a different function, for example, as signalling agreement to the specified purchase price, quantity of goods or delivery details,[88] or as authorising the downloading of software.[89] Where an online contract is not signed, a seller seeking to incorporate standard terms into its contracts with purchasers will have to provide reasonable notice of those terms, as discussed earlier in this section.

There is also increased interest in "smart" contracts.[90] These are not traditional text based contracts found on the internet and made online. Smart contracts involve self-executing or automated performance. The terms may be recorded in format, digital or code. Nontheless, determining the terms on which these contracts are made still involves the application of the established principles discussed above to the circumstances of the transaction in question.

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86 See further Macdonald, "Incorporation of Standard Terms in Website Contracting: Clicking 'I Agree' " (2011) 27 *Journal of Contract Law* 198; Paterson, "Consumer Contracting in the Age of the Digital Natives" (2011) 27 *Journal of Contract Law* 152.

87 *Electronic Transactions Act 2001* (ACT), s 9; *Electronic Transactions Act 1999* (Cth), s 10; *Electronic Transactions Act 2000* (NSW), s 9; *Electronic Transactions (Northern Territory) Act* (NT), s 9; *Electronic Transactions (Queensland) Act 2001* (Qld), s 14; *Electronic Communications Act 2000* (SA), s 9; *Electronic Transactions Act 2000* (Tas), s 7; *Electronic Transactions (Victoria) Act 2000* (Vic), s 9; *Electronic Transactions Act 2011* (WA), s 10. See discussion of these acts at [3.100].

88 Sneddon, "Legislating to Facilitate Electronic Signatures and Records: Exceptions, Standards and the Impact of the Statute Book" (1998) 21 *University of New South Wales Law Journal* 334, 368.

89 *Specht v Netscape Communications* 306 F 3d 17 (2nd Cir, 2002).

90 See further Mik, "Smart Contracts: Terminology, Technical Limitations and Real World Complexity" (2017) 9 *Law, Innovation & Technology* 2; Ryan, "Smart Contract Relations in e-Commerce: Legal Implications of Exchanges Conducted on the Blockchain" (2017) 7 *Technology Innovation Management Review* 14.

INCORPORATION OF TERMS BY A COURSE OF DEALINGS

[12.90] Where parties have had a history of dealings, contractual terms introduced in earlier transactions may be incorporated into a subsequent contract even though the ordinary requirements for the incorporation of terms have not been met in relation to that subsequent contract.[91] The justification for such incorporation will be that the party to be bound has, by continuing to deal with the party seeking to impose contractual terms, evidenced a willingness to be bound by the terms.[92]

In *Balmain New Ferry Co Ltd v Robertson*,[93] a ferry company used a private wharf in the course of their business of running a steam ferry from the City of Sydney to Balmain. On the wharf were two turnstiles. Passengers entering or leaving the wharf paid one penny to the officer at the turnstiles. There was a notice board near the turnstiles on which was printed the words: "[n]otice. A fare of one penny must be paid on entering or leaving the wharf. No exception will be made to this rule, whether the passenger has travelled by the ferry or not."

Robertson paid the fare and stepped onto the wharf. Having missed the ferry he wanted to catch, Robertson sought to leave the wharf and was asked to pay another penny. Robertson refused. The High Court held that Robertson was bound by a term of the contract requiring the payment of one penny to leave the wharf. The Court considered that having travelled on many occasions on the company's ferries and paid his fare, Robertson must have known of the terms upon which the ferry company conducted its business.[94]

Requirement for regularity and uniformity

[12.95] For terms to be incorporated by a course of dealings, that course of dealings must have been regular[95] and uniform.[96] The document relied upon in previous transactions must also reasonably be considered a contractual document,[97] rather than having the appearance of a mere receipt or docket.[98]

In *DJ Hill & Co Pty Ltd v Walter H Wright Pty Ltd*,[99] the defendant agreed by telephone to carry some machinery for the plaintiff. The machinery was damaged in transit, and the plaintiff sued for damages. The defendant sought to rely on a clause excluding liability for loss or damage. The clause was contained in a document that had been presented to employees of the plaintiff for signature on previous occasions when machinery had been delivered. There was evidence that some of the plaintiff's employees were aware of the fact that the document

91 See generally Swanton, "Incorporation of Contractual Terms by a Course of Dealing" (1989) 1 *Journal of Contract Law* 223.

92 *Henry Kendall & Sons v William Lillico & Sons Ltd* [1969] 2 AC 31, 104–5, 113; *Chattis Nominees Pty Ltd v Norman Ross Homeworks Pty Ltd* (1992) 28 NSWLR 338, 343.

93 *Balmain New Ferry Co Ltd v Robertson* (1906) 4 CLR 379.

94 *Balmain New Ferry Co Ltd v Robertson* (1906) 4 CLR 379, 391; *Chattis Nominees Pty Ltd v Norman Ross Homeworks Pty Ltd* (1992) 28 NSWLR 338, 343.

95 See, eg, *Henry Kendall & Sons v William Lillico & Sons Ltd* [1969] 2 AC 31; *Chattis Nominees Pty Ltd v Norman Ross Homeworks Pty Ltd* (1992) 28 NSWLR 338, 343.

96 See *McCutcheon v David MacBrayne Ltd* [1964] 1 WLR 125; *Henry Kendall & Sons v William Lillico & Sons Ltd* [1969] 2 AC 31, 104, 115.

97 See *La Rosa v Nudrill Pty Ltd* [2013] WASCA 18.

98 *DJ Hill & Co Pty Ltd v Walter H Wright Pty Ltd* [1971] VR 749.

99 *DJ Hill & Co Pty Ltd v Walter H Wright Pty Ltd* [1971] VR 749.

contained terms relating to the carriage of the machinery, but not that any employee had ever read or knew of the content of the terms.[100]

The Full Court of the Supreme Court of Victoria held that, in the absence of actual knowledge by the plaintiff, the defendant was not entitled to rely on the exclusion clause in the document. The Court considered that the document presented on previous occasions could not incorporate terms into the contract between the parties. The document was presented for signature after the contract had been performed. Accordingly, the plaintiff might reasonably have regarded it as merely an acknowledgment of the delivery of the goods, and not as a contractual document.[101]

The decision in *DJ Hill & Co Pty Ltd v Walter H Wright Pty Ltd*[102] has been criticised.[103] It can be argued that when there is a course of dealings using the document in question, the time at which a document is received in any individual transaction should not be determinative of its contractual status. Frequent use of a document, which might otherwise reasonably be considered contractual, should be able to overcome any timing problems. In *Eggleston v Marley Engineers Pty Ltd*,[104] Hogarth J in the Supreme Court of South Australia considered that documents of the type in question should be classified as contractual, but nonetheless felt constrained to follow the authority of *DJ Hill & Co Pty Ltd v Walter H Wright Pty Ltd*.

STATEMENTS MADE DURING NEGOTIATIONS

[12.100] Parties negotiating a contract may make a great many statements about matters relating to their proposed agreement. These statements may form the basis of the parties' oral contract. Alternatively, particularly where a significant transaction is involved, the parties may record their agreement in a written contractual document that contains some, but perhaps not all, of the statements made during negotiations. After producing a draft written contract, the parties might have further discussions about how they will perform the contract or additional obligations. For example, the parties might agree that a certain term will not be enforced except in specified circumstances or discuss additional features that the goods to be sold will hold.

If a statement made in negotiations proves false, the legal status of that statement may prove to be an issue of great significance. The status of the statement will determine whether the party to whom it was made can seek a remedy for losses incurred as a result of the false statement in tort, contract or under legislation. If the statement was a term of the contract, sometimes called a *warranty*, and proves false, there will be a remedy for breach of contract. If the statement was not a term of the contract, sometimes described as a *mere representation*, and proves false, a contractual remedy for breach will not be available. In some cases, relief may be sought under the law relating to misrepresentation and misleading and deceptive

100 *DJ Hill & Co Pty Ltd v Walter H Wright Pty Ltd* [1971] VR 749, 752.

101 *DJ Hill & Co Pty Ltd v Walter H Wright Pty Ltd* [1971] VR 749, 753–4. See also *Rinaldi and Patroni Pty Ltd v Precision Mouldings Pty Ltd* [1986] WAR 131; cf *Garden City Transport v National Manufactured Products No 2 Ltd* (1995) 65 SASR 109.

102 *DJ Hill & Co Pty Ltd v Walter H Wright Pty Ltd* (1979) 21 SASR 51, 65.

103 For criticism of the decision, see Greig and Davis, *The Law of Contract* (Law Book Co, 1987), pp 577–9.

104 *DJ Hill & Co Pty Ltd v Walter H Wright Pty Ltd* (1979) 21 SASR 51.

conduct.[105] Estoppel may prove relevant in some cases.[106] In other cases, a statutory remedy may be available.[107]

In this part of the chapter, we will consider the principles for determining whether a statement made by the parties when negotiating their contract is a term of that contract. There are two issues to consider: the effect of the parol evidence rule and whether the statement was intended by the parties to be a term of the contract. Initially, however, we need to consider the effect of the contractual provisions that seek to exclude pre-contractual statements having any contractual effect.

Entire agreement clauses

[12.105] Parties who have entered into a written contract may attempt to ensure that any pre-contractual statements are not treated as contractual terms by including in their contract a *merger* or *entire agreement* clause. An entire agreement clause is a term stating that the written document contains the "entire agreement" of the parties and that no other "extrinsic" statements are to be treated as incorporated into that contract. As explained by Lightman J in *Inntrepreneur Pub Co v East Crown*:[108]

> The purpose of an entire agreement clause is to preclude a party to a written agreement from threshing through the undergrowth and finding in the course of negotiations some (chance) remark or statement (often long forgotten or difficult to recall or explain) on which to found a claim such as the present to the existence of a collateral warranty. The entire agreement clause obviates the occasion for any such search and the peril to the contracting parties posed by the need which may arise in its absence to conduct such a search. For such a clause constitutes a binding agreement between the parties that the full contractual terms are to be found in the document containing the clause and not elsewhere, and that accordingly any promises or assurances made in the course of the negotiations (which in the absence of such a clause might have effect as a collateral warranty) shall have no contractual force, save insofar as they are reflected and given effect in that document.

The effect of an entire agreement clause depends on the words actually used. However, in Australia, entire agreement clauses will usually be taken as conclusive. Under this approach, an entire agreement clause expresses the parties agreement that the written contract represents the entire agreement between the parties and that any statements made in negotiations or other extrinsic material do not form part of that written contract.[109] Thus, for example, in *Franklins Pty Ltd v Metcash Trading Ltd*, Campbell JA held that a "reasonable observer would conclude" from the entire agreement clause that the parties did not intend earlier correspondence to influence the meaning of the concluded contract.[110]

Entire agreement clauses may not be effective in precluding other types of legal liability from arising; for instance, from statements or representations made in negotiations. In Australia,

105 See Chapters 32 and 33.

106 See Chapter 9.

107 See Chapter 17.

108 *Inntrepreneur Pub Co v East Crown* [2000] 2 Lloyd's Rep 611, [7].

109 See, eg, *Hope v RCA Photophone of Australia Pty Ltd* (1937) 59 CLR 348, 357, 363, 365, 368; *Boston Commercial Services v GE Capital Finance Australasia Pty Ltd* [2006] FCA 1352; (2006) 236 ALR 720, [84]. For a different view, see McLauchlan, "The Entire Agreement Clause: Conclusive or a Question of Weight?" (2012) 128 *Law Quarterly Review* 521.

110 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [342]. See also Mitchell, "Entire Agreement Clauses: Contracting Out of Contextualism" (2006) 22 *Journal of Contract Law* 222.

contrary to the view expressed in *Inntrepreneur Pub Co v East Crown*[111] above, it has been suggested that entire agreement clauses may not be effective to preclude the parties from establishing a collateral contract.[112] Entire agreement clauses may not be effective to exclude evidence relevant to establishing an estoppel.[113] Such clauses will also not necessarily preclude the implication of terms.[114] Entire agreement clauses in standard form consumer contracts may be void as unfair terms under the Australian Consumer Law.[115]

THE PAROL EVIDENCE RULE

[12.110] Where a contract is oral, in identifying the terms of that contract, a court may consider all relevant evidence, including, for example, what was said when the parties were making their contract and the nature of the industry in which the parties were contracting. Where the parties have recorded their agreement in writing, the evidence that is admissible for the purpose of identifying and interpreting the terms of a contract is more limited. The *parol evidence rule* limits "extrinsic" evidence, meaning evidence outside the written contract, that may be brought to add to, or vary, the terms of that written contract. The classic explanation of the parol evidence rule is that given by Denman CJ in *Goss v Lord Nugent*:[116]

> [I]f there be a contract which has been reduced into writing, verbal evidence is not allowed to be given of what passed between the parties, either before the written document was made, or during the time that it was in a state of preparation, so as to add to or subtract from, or in any manner to vary or qualify the written contract.

The parol evidence rule is usually considered to have two parts:

1. First, the rule prevents extrinsic evidence being given to add to, vary or contradict the terms of a contract as they appear in a written document.
2. Second, the rule limits the evidence that can be given to explain the meaning of the terms of a written contract.

The first part of the parol evidence rule prevents extrinsic evidence being given to add to, vary or contradict the terms of a contract as they appear in a written document. The rule therefore limits the extrinsic evidence that may be given in identifying the terms of the contract. The second part of the rule applies to the use of extrinsic evidence in interpreting a contract and will be discussed in Chapter 13.

The extrinsic evidence excluded

[12.115] The parol evidence rule will exclude any evidence outside or extrinsic to the written contract made by the parties from being used to explain the scope of the contract or the meaning of its terms. Thus, for example, the rule will exclude evidence of oral statements

111 *Inntrepreneur Pub Co v East Crown* [2000] 2 Lloyd's Rep 611, [7].

112 *McMahon v National Foods Milk Ltd* [2009] VSCA 153; (2009) 25 VR 251, [38]. See also Peden and Carter, Peden and Carter, "Entire Agreement – and Similar – Clauses" (2006) 22 *Journal of Contract Law* 1.

113 See *Saleh v Romanous* [2010] NSWCA 274; (2010) 79 NSWLR 453, discussed at [9.210].

114 *Hart v MacDonald* (1910) 10 CLR 417, 430. See also [14.10].

115 See Chapter 16.

116 *Goss v Lord Nugent* (1833) 5 B & Ad 58, 64–5; 110 ER 713, 715–16. See also *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 347.

made by the parties when negotiating their contract and written material, such as letters or memoranda relating to the negotiations or earlier drafts of the written record of the contract.[117]

Can extrinsic evidence be used to determine whether a contract is wholly in writing?

[12.120] The parol evidence rule only applies to exclude extrinsic evidence of terms supplementing a written contract where that contract is wholly in writing.[118] The rule will not apply to exclude extrinsic evidence relevant to identifying the terms of a contract that is only partly in writing. A party who seeks to incorporate into a written contract terms based on oral statements made during negotiations will accordingly attempt to argue that the contract was only partly in writing. Conversely, the party who wants to exclude such statements will argue that the contract was entirely in writing. In choosing between these arguments, the extrinsic evidence of what was said during negotiations may often be extremely relevant.

There are two approaches to the use of extrinsic evidence in assessing whether a written contractual document is entirely in writing:

1. The stricter approach accords primacy to a written document that appears on its face to be the complete record of the parties' contract.[119] Under this approach, extrinsic evidence will not be admissible to add to, vary or contradict the terms contained in the written document. This approach is based on a view that parties who have recorded their contract in writing should be presumed to have intended the written document to embody or *integrate* the whole of their agreement.[120] On this view, correspondence entered into and statements made prior to the written document being made are no longer relevant to the parties' agreement, either having been integrated into the written document or rejected by the parties. This approach provides parties with certainty with respect to the scope of contracts in writing.[121] It also reduces the time and costs of litigation by confining the inquiry of courts into the terms of a contract to those contained in the written document.[122]
2. The more flexible approach to the use of extrinsic evidence in determining whether a contract is wholly or only partly in writing puts greater emphasis on ascertaining the presumed intentions of the parties. Under this approach, the parol evidence rule has no application until it is determined that the parties intended the written document to contain all of the terms of their contract.[123] Accordingly, extrinsic evidence will be

117 See, eg, *Harris v Sydney Glass & Tile Co* (1904) 2 CLR 227, 237.

118 *Hoyt's Pty Ltd v Spencer* (1919) 27 CLR 133, 143; *Hope v RCA Photophone of Australia Pty Ltd* (1937) 59 CLR 348, 357.

119 See, eg, *LG Thorne & Co Pty Ltd v Thomas Borthwick & Sons (Australasia) Ltd* (1956) SR (NSW) 81, 88; *Gordon v Macgregor* (1908) 8 CLR 316, 320; *Hoyt's Pty Ltd v Spencer* (1919) 27 CLR 133, 143.

120 See also *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 352; *B and B Constructions (Australia) Pty Ltd v Brian A Cheeseman and Associates Pty Ltd* (1994) 35 NSWLR 227, 234, 243.

121 *Hope v RCA Photophone of Australia Pty Ltd* (1937) 59 CLR 348, 357.

122 *B and B Constructions (Australia) Pty Ltd v Brian A Cheeseman and Associates Pty Ltd* (1994) 35 NSWLR 227, 234; *Equuscorp Pty Ltd v Glengallan Investments Pty Ltd* [2004] HCA 55; (2004) 218 CLR 471, [35].

123 *Life Insurance Co of Australia Ltd v Phillips* (1925) 36 CLR 60, 71; *Maybury v Atlantic Union Oil Co Ltd* (1953) 89 CLR 507, 517; *Spunwill Pty Ltd v BAB Pty Ltd* (1994) 36 NSWLR 290, 299; *Branir Pty Ltd v Owston Nominees*

> admitted to establish whether the parties intended the document to be an exclusive record of their agreement or whether the parties intended the written document to be supplemented or varied by promissory statements made during negotiations or other extrinsic material. If the Court concludes that the parties intended the second option, then it will consider the nature of the extrinsic evidence submitted to determine if in fact that material does contain additional terms.

Parties who have gone to the effort of preparing a written record of their contract commonly have intended that written contractual document to be the complete expression of their agreement. However, the relationship of contracting parties may not always be confined within such parameters. In some cases, parties may have prepared a written document to formalise their relationship, but would also have expected subsequent discussions about that document to be binding on them.[124] The more flexible approach to the role of the parol evidence rule in identifying the terms of a contract allows a court to consider the possibility of oral terms adding to, varying or contradicting the written document, even if the Court eventually concludes that the written document does embody the whole of the parties' agreement.

It might also be noted that the second approach renders the parol evidence rule, in its application to identifying the terms of the contract, a circular inquiry. As the English Law Reform Commission explained:[125]

> [W]hen it is proved or admitted that the parties to a contract intended that all the express terms of their agreements should be recorded in a particular document or documents, evidence will be inadmissible (because irrelevant) if it is tendered only for the purpose of adding to, varying, subtracting from or contradicting the express terms of that contract.

The High Court has not yet conclusively determined which of these two approaches to the parol evidence rule should be taken in identifying the terms of a contract.[126] In a number of decisions, State courts have indicated a preference for the more flexible approach, stating that "the parol evidence rule applies only to contracts that are wholly in writing, and thus has no scope to operate until it has first been ascertained that the contract is wholly in writing".[127]

Circumstances where the parol evidence rule has no application

[12.125] Even where a contract is wholly in writing, there are a number of circumstances in which extrinsic evidence adding to or varying the terms of the contract may be admitted. Although these circumstances are commonly described as exceptions to the parol evidence rule, they more accurately represent situations in which the parol evidence rule has no application.

(No 2) Pty Ltd (2001) 117 FCR 424, 508–9 [288]–[293] (Allsop J); *Nicolazzo v Harb* [2009] VSCA 79; (2009) 22 VR 220, 234–5 [88]–[90]; *Mainieri v Cirillo* [2014] VSCA 227; (2014) 47 VR 127, [13].

124 See Hadfield, "Problematic Relations: Franchising and the Law of Incomplete Contracts" (1990) 42 *Stanford Law Review* 927, 957, 979–80.

125 The Law Commission, *The Law of Contract, The Parol Evidence Rule* (Cmnd 9700, 1986), [2.7].

126 Although dealing with an argument that a contract was partly oral and partly in writing, the question was not addressed in *Equuscorp Pty Ltd v Glengallan Investments Pty Ltd* [2004] HCA 55; (2004) 218 CLR 471.

127 *Masterton Homes Pty Ltd v Palm Assets Pty Ltd* [2009] NSWCA 234, [90]. See also *State Rail Authority of New South Wales v Heath Outdoor Pty Ltd* (1986) 7 NSWLR 170, 191; *Nemeth v Bayswater Road Pty Ltd* [1988] 2 Qd R 406, 414; *NSW Cancer Council v Sarfaty* (1992) 28 NSWLR 68, 76–7; *County Securities Pty Ltd v Challenger Group Holdings Pty Ltd* [2008] NSWCA 193, [8]; *Nicolazzo v Harb* [2009] VSCA 79; (2009) 22 VR 220, [90]; *Skyrise Consultants Pty Ltd v Metroland Funds Management Ltd* [2011] NSWCA 406, [13].

Collateral contract

[12.130] The parol evidence rule has no application where the parties have entered into a collateral contract, discussed at [12.195].

Estoppel

[12.135] Courts are divided on whether extrinsic evidence should be admitted for the purpose of establishing an estoppel. This issue is discussed further in Chapter 9.[128]

Rectification

[12.140] Courts have an equitable power to rectify a contract in writing where a mistake is made in recording the parties' agreement. Rectification is discussed in Chapter 31.

Contract subject to a condition precedent

[12.145] Extrinsic evidence will be admitted for the purpose of establishing that a written contract is subject to a contingent condition that must be satisfied before the contract will become effective.[129] Extrinsic evidence may also be admitted to show that the parties did not intend to make a binding contract.[130]

The true consideration

[12.150] In certain circumstances, extrinsic evidence is admissible to prove the real consideration under a contract. In *Pao On v Lau Yiu Long*, the Privy Council explained that:[131]

> Extrinsic evidence is admissible to prove the real consideration where (a) no consideration, or a nominal consideration, is expressed in the instrument, or (b) the expressed consideration is in general terms or ambiguously stated, or (c) a substantial consideration is stated, but an additional consideration exists. The additional consideration must not, however, be inconsistent with the terms of the written instrument. Extrinsic evidence is also admissible to prove the illegality of the consideration.

Implied terms

[12.155] The better view is that a court may have regard to extrinsic evidence when considering whether or not a term should be implied in a contract.[132] As noted at [12.110], the parol evidence rule applies in identifying the terms of a contract, and in construing a contract. Neither aspect applies to the implication of a term, which is a process that gives effect to what is already implicit in the contract.[133]

The parol evidence rule and electronic contracts

[12.160] The authors of the English contract text *Chitty on Contracts* suggest that where the terms of a contract are recorded electronically, but are capable of being retrieved and

128 See [9.205].

129 *Pym v Campbell* (1856) 6 El & Bl 370; 119 ER 903; *Life Insurance Co of Australia Ltd v Phillips* (1925) 36 CLR 60, 71. On contingent conditions, see Chapter 20.

130 *Air Great Lakes Pty Ltd v K S Easter (Holdings) Pty Ltd* (1985) 2 NSWLR 309, 333–4.

131 *Pao On v Lau Yiu Long* [1980] AC 614, 631.

132 See *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 347–53. But cf *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 402. On implied terms, see Chapter 14.

133 See *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 347.

converted to a readable form, the terms should be treated as being in writing for the purpose of the parol evidence rule.[134] The rule might, for example, apply to a contract for the purchase of goods made over the internet. The seller of the goods may display on its website the terms on which the goods will be supplied and the consumer might indicate his or her acceptance of those terms by clicking on a dialogue box marked "I accept these terms". In such a case, if the authors of *Chitty on Contracts* are correct, the contract will be in writing. This would mean that a consumer who argues that the terms displayed on the website were supplemented by other terms, such as promises made by the seller over the telephone or in email correspondence, will have to contend with the parol evidence rule in bringing evidence of that extrinsic material before a court.

WHEN IS A STATEMENT A TERM OF THE CONTRACT?

[12.165] Assuming any difficulties with the parol evidence rule are overcome, a party seeking to show that a statement made in negotiations forms a term of the parties' contract must next establish that the statement was intended to be contractually binding.

For an oral, or other form of extrinsic, statement to constitute a term of a written contract, as opposed to being a mere representation, the statement must have been intended by the party making it to be a promise and to form part of the written contract. Intention is judged objectively. The court will assess whether or not a person in the circumstances of the parties would reasonably have considered the statement to be a contractual promise.[135] As Lord Denning explained in *Oscar Chess Ltd v Williams*:[136]

> The question whether a warranty was intended depends on the conduct of the parties, on their words and behaviour, rather than on their thoughts. If an intelligent bystander would reasonably infer that a warranty was intended, that will suffice.

The answer will depend on the particular circumstances of the case in question, although the decided cases identify a number of factors that may prove relevant in making this determination.[137]

The existence of a formal written contract

[12.170] Where the parties have recorded their agreement in a formal; written, contractual document, this fact will usually suggest that any statements made by the parties during negotiations and not included in the written contractual document were not intended to be part of the final contract. If the parties had intended those statements to form part of their contract, then they would presumably have included those statements in the written contractual document. The very purpose of the written document will have been to record the mutually agreed obligations from the earlier discussions. This inference will be even stronger where the alleged oral terms are inconsistent with those contained in the written contract.[138]

134 Chitty, *Chitty on Contracts* (33rd ed, 2018), [13-046], citing *Derby & Co Ltd v Weldon (No 9)* [1991] 1 WLR 652.

135 See, eg, *Oscar Chess Ltd v Williams* [1957] 1 WLR 370, 375; *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41, 61.

136 *Oscar Chess Ltd v Williams* [1957] 1 WLR 370, 375.

137 See also *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41.

138 *Equuscorp Pty Ltd v Glengallan Investments Pty Ltd* [2004] HCA 55; (2004) 218 CLR 471, [33]; *Skyrise Consultants Pty Ltd v Metroland Funds Management Ltd* [2011] NSWCA 406, [14].

In a dispute about which of the two sets of terms should prevail, priority must logically be given to the subsequent written record.

In *Equuscorp Pty Ltd v Glengallan Investments Pty Ltd*[139] the parties had executed a written loan contract. The borrowers subsequently argued that the transaction was governed by an earlier oral agreement made on different terms. The argument was dismissed by the High Court of Australia.[140] In reaching this conclusion, the Court was highly influenced by the fact that the parties had executed a formal written contract and that the alleged oral terms contradicted those in the written contract. The Court considered that in these circumstances, the execution of the formal written contract discharged any prior oral agreement. The Court stated:

> The conclusion that the respondents are bound by the written loan agreements may leave open the possibility that an earlier consensus reached by the parties was in each case a collateral agreement (made in consideration of the parties later executing the written agreement), but that has never been the respondents' case. In another case it may leave open the possibility that the contract is partly oral and partly in writing. But that cannot be so here. The oral limited recourse terms alleged by the respondents contradict the terms of the written loan agreement. If there was an earlier, oral, consensus, it was discharged and the parties' agreement recorded in the writing they executed.[141]

Another scenario in which it might be argued that a written contract is supplemented by oral or other extrinsic statements is where a standard form contract prepared by one of the parties is qualified by statements made in subsequent negotiations between the parties. However, as in the case of statements made prior to drafting a written contract, this line of argument can be met with the objection that, if the statements were so important to the parties that they were intended to be binding, why were they not included as an amendment to the written contract before it was executed by the parties. Such a failure might suggest that the oral statement was not, in fact, intended to qualify the written contract.

State Rail Authority of New South Wales v Heath Outdoor Pty Ltd[142] concerned a contract entered into between Heath Outdoor and the State Rail Authority to place advertising on the property of the State Rail Authority. The written contract granted the State Rail Authority the power to terminate the contracts at any time, with one month's written notice. Heath Outdoor then contracted with a cigarette manufacturer to display cigarette advertising on the hoardings for a period of five years. Following a government decision to phase out cigarette advertising on government property, the State Rail Authority exercised its right to terminate the contract with Heath Outdoor. Heath Outdoor argued that the right to terminate in the written contract had been qualified by statements, made before the contract was signed, by an officer of the State Rail Authority to the effect that the right to terminate would only be exercised by the State Rail Authority in exceptional circumstances and would not affect the contract with Heath Outdoor. The officer also stated that it would be difficult for him to have the standard form contract changed. McHugh JA, with whom Kirby P and Glass JA agreed, held that while the parol evidence rule did not exclude the Court from considering evidence relating to the oral conversations for the purpose of assessing the nature of the contract, the

139 *Equuscorp Pty Ltd v Glengallan Investments Pty Ltd* [2004] HCA 55; (2004) 218 CLR 471.

140 *Equuscorp Pty Ltd v Glengallan Investments Pty Ltd* [2004] HCA 55; (2004) 218 CLR 471, [33].

141 *Equuscorp Pty Ltd v Glengallan Investments Pty Ltd* [2004] HCA 55; (2004) 218 CLR 471, [33].

142 *State Rail Authority of New South Wales v Heath Outdoor Pty Ltd* (1986) 7 NSWLR 170.

submission that the contract was partly oral and partly in writing should be rejected. The written contract conferred an unfettered right to terminate the contract with Heath Outdoor. The officer of the State Rail Authority made it plain that he had no authority to change any condition of the written contract.[143]

Importance of the statement

[12.175] A statement that was highly significant or important to one party's decision to enter into the transaction is more likely to be regarded as a promise than a statement of lesser significance. In *Van den Esschert v Chappell*[144] the purchaser of a house, before signing the written contract of sale, asked the vendor whether or not the house had any white ants. The vendor assured the purchaser that there were none. The Full Court of the Supreme Court of Western Australia held that the statement was a term of the contract. Wolff CJ explained:

> I would think that on the purchase of a house in this country an inquiry regarding the presence of white ants was most important: when (as in this case) the prospective purchaser immediately before signing a contract makes a specific request to be informed about that matter and gets an affirmative answer such as the purchaser got in this case it was intended to be made a part and parcel of the contract and was to be regarded as a term.[145]

The words used

[12.180] A statement made in the course of negotiating a contract is more likely to be a promise where the party making it uses words suggesting promissory intent. Examples of such words are, obviously, "promise" and also words of strong undertaking such as "agree", "guarantee" or "warrant". Conversely, where the party making the statement uses words that indicate he or she is merely expressing an opinion or a hypothesis, the statement is more likely to be a mere representation. Examples might be expressions such as "I estimate" or "I guess".

In *JJ Savage & Sons Pty Ltd v Blakney*,[146] the purchaser of a motor boat sued in respect of a statement made by the seller in a letter that the "estimated speed" of the boat was 15 miles per hour. The written record of the contract did not contain any reference to the boat's capacity to achieve any particular speed. The High Court concluded that the statement about the speed of the boat was not a promise, but a mere representation. The words used indicated "an expression of opinion" only.[147]

The relative expertise of the parties

[12.185] The relative knowledge or expertise of the parties may be relevant in assessing whether a statement was made as a promise or as a mere representation. A statement made by a party with expertise to a person who is inexperienced is more likely to be promissory than a statement made by a party known to be inexperienced.

In *Oscar Chess Ltd v Williams*[148] Williams had offered his mother's car to a car dealer as part payment for a new car. Williams described the car as a 1948 model, the date shown in the

143 *State Rail Authority of New South Wales v Heath Outdoor Pty Ltd* (1986) 7 NSWLR 170, 191.

144 *Van den Esschert v Chappell* [1960] WAR 114.

145 *Van den Esschert v Chappell* [1960] WAR 114, 116. See also *Couchman v Hill* [1947] KB 554.

146 *JJ Savage & Sons Pty Ltd v Blakney* (1970) 119 CLR 435.

147 *JJ Savage & Sons Pty Ltd v Blakney* (1970) 119 CLR 435, 442.

148 *Oscar Chess Ltd v Williams* [1957] 1 WLR 370.

car's registration book. The car dealer paid Williams £290 for the car. It turned out that the car was a 1939 model and only worth £175. The car dealer claimed damages representing the difference in value of £115, on the ground that it was a term of the contract that the car was a 1948 model. The claim was rejected by the English Court of Appeal. It should have been obvious to the car dealer that Williams had no personal knowledge of the year the car was made and was relying on the date in the registration book.[149]

In *Smythe v Thomas*[150] statements by a seller of an airplane listed on eBay that the plane would be capable of being flown from Albury to South Australia, and would have a current airworthiness certificate on completion of the 100-hour inspection, were promissory in nature. Rein AJ said:

> The statements were matters upon which the [seller] alone had the relevant information and would in my view objectively be regarded as important by a purchaser, particularly where it was intended to fly the aircraft from Albury to South Australia.[151]

Other doctrines giving effect to statements made in negotiations

[12.190] Even if an oral statement made in negotiations does not form a term of the written contract agreed between the parties, there are a number of doctrines that may give legal effect to that statement.

Collateral contracts

[12.195] A *collateral contract* is the name given to the contract made when one party makes a promise, connected to, but independent of, a main contract and, as consideration for that promise, the other party agrees to enter into the main contract.[152] For example, consider a case where a buyer of property signs a formal written contract of sale that says nothing about drains after the seller makes a verbal promise that the drains on the property are in good order. If the drains are not in good order and the buyer wishes to sue the seller for breach of the oral promise, the buyer will be confronted by the parol evidence rule. The buyer may avoid the operation of the rule by showing that the written document was not intended to comprise all of the terms of the contract but is partly oral and partly in writing. Alternatively, the buyer may avoid the rule by showing that there were two separate contracts. One will be the main contract, the contract of sale. The other will be a collateral contract, consisting of the seller's promise that the drains are in good order, given in return for the buyer's entry into the main contract.[153]

For a pre-contractual oral statement to take effect as collateral contract, the statement must be "promissory and not merely representational",[154] intended to induce entry into the contract,[155] and consistent with the terms of the main contract.[156]

149 *Oscar Chess Ltd v Williams* [1957] 1 WLR 370, 376, 378. See also *Ellul v Oakes* (1972) 3 SASR 377, 381–2; *Dick Bentley Productions Ltd v Harold Smith (Motors) Ltd* [1965] 1 WLR 623.

150 *Smythe v Thomas* [2007] NSWSC 844; (2007) 71 NSWLR 537.

151 *Smythe v Thomas* [2007] NSWSC 844; (2007) 71 NSWLR 537, [61].

152 See *Heilbut Symons & Co v Buckleton* [1913] AC 30, 47.

153 See also *De Lassalle v Guildford* [1901] 2 KB 215, esp 222.

154 *JJ Savage & Sons Pty Ltd v Blakney* (1970) 119 CLR 435, 442; *Gates v City Mutual Life Assurance Society Ltd* (1986) 160 CLR 1, 5, 11.

155 *JJ Savage & Sons Pty Ltd v Blakney* (1970) 119 CLR 435, 441–3.

156 *Hoyt's Pty Ltd v Spencer* (1919) 27 CLR 133, 139, 147; *Maybury v Atlantic Union Oil Co Ltd* (1953) 89 CLR 507, 517; *Gates v City Mutual Life Assurance Society Ltd* (1986) 160 CLR 1, 5, 11; *Adicho v Dankeith Homes*

A promissory statement

[12.197] For a representation made in the course of negotiations to be binding as an agreement that is collateral to the main agreement, it must be concluded that the parties intended the representation to be contractually binding.[157] As already discussed at [12.165], the test is an objective one that considers what a reasonable person in the position of the parties would have understood them to have intended.[158]

In *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd*[159] the owner of a casino and entertainment complex entered into two leases for restaurant premises with commercial tenants. Each lease was for five years with no option to renew. The leases required the tenant to complete a major refurbishment of the premises as part of the lease. A representative of the landlord said to the tenants that if they spent money to achieve the refurbishment of the premises to a high standard, the tenants would be "looked after at renewal time". At the expiry of the five-year term, the landlord gave notice tenants requiring the tenants to vacate the premises. The tenants argued that the landlord's representations amounted to a collateral contract to offer a renewal of the leases for a further five years.

This argument was rejected by the High Court (French CJ, Kiefel, Bell, Keane and Nettle JJ, Gageler and Gordon JJ dissenting). The majority considered that the statement that the tenants would be "looked after at renewal time" did not amount to a contractual promise.[160] The statement was no more than "vaguely encouraging".[161] Further, any agreement was illusory and unenforceable because the terms of the renewed leases were not agreed to, but were at the discretion of the landlord.[162]

Consistency

[12.199] As already noted, the parol evidence rule does not apply to preclude evidence of a statement forming a collateral contract.[163] However, the requirement that a collateral contract must be consistent with the main contract means that the collateral contract has a relatively narrow operation as a means of giving contractual force to an oral representation varying a contract in writing.[164]

The requirement of consistency is known as the rule in *Hoyt's Pty Ltd v Spencer*.[165] In this case, a written lease provided that the lessor might, at any time, terminate the lease "by giving the lessee at least four weeks" written notice of his intention to do so. The lessor later gave notice to terminate the lease. The lessee alleged that in consideration of his taking the lease, the lessor agreed not to give such notice except in certain circumstances. The High Court held that

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Pty Ltd [2012] NSWCA 316, [26]. In England, there is contrary authority on this issue: *City and Westminster Properties (1934) Ltd v Mudd* [1959] Ch 129.

157 *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41, 61–2.

158 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* (2016) 260 CLR 1, [22].

159 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* (2016) 260 CLR 1.

160 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* (2016) 260 CLR 1, [28], [196].

161 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* (2016) 260 CLR 1, [23], quoting Hargrave J in the Supreme Court of Victoria.

162 *Crown Melbourne Ltd v Cosmopolitan Hotel (Vic) Pty Ltd* (2016) 260 CLR 1, [31], [132], [199].

163 See [12.130].

164 See criticism of the requirement in Seddon, "A Plea for the Reform of the Rule in Hoyt's Pty Ltd v Spencer" (1978) 52 *Australian Law Journal* 372.

165 *Hoyt's Pty Ltd v Spencer* (1919) 27 CLR 133.

this alleged collateral contract was not binding on the lessor because it was inconsistent with the main contract.[166] The High Court explained that the requirement of consistency means that while a collateral contract may add to the main contract, it must not alter the provisions of the main contract.[167] The two contracts must be able to stand together. The High Court said that the rationale for this rule is that the collateral contract must be "supplementary only to the main contract".[168]

In *Mainieri v Cirillo*,[169] the respondent sold her house and went to live with the appellants, her son and daughter-in-law. The proceeds of the sale were applied to reduce the appellants' mortgage. A written contract provided that in consideration of a gift from the respondent, the appellants would accommodate and look after her for life. The relationship broke down and the respondent asked for her money back. The Court of Appeal of the Supreme Court of Victoria admitted evidence of the prior oral agreement, on the ground that evidence of the events showed the written agreement was not the sole repository of the agreement between the parties.[170] Alternatively, the oral agreement was a collateral contract. The agreement was sufficiently precise to be promissory and induced entry into the principal agreement.[171] There was no inconsistency between the written agreement to accommodate the respondent and the agreement to apply the proceeds of sale in reduction of the mortgage.[172] The joint endeavour having failed, the respondent was entitled to an equitable lien or charge over the appellants' property to secure repayment of their money.[173]

Estoppel

[12.200] The doctrine of promissory estoppel may apply to provide relief to a party who has relied on an assumption that the other party would modify, or refrain from, enforcing the terms of a contract in writing. The operation of the doctrine of estoppel in this context is discussed in Chapter 9.[174]

Consumer protection

[12.210] A plaintiff who has been induced to enter into a contract, or has relied on a pre-contractual statement that does not form a term of the contract, may have claims in misrepresentation or under consumer protection legislation, claims for misleading or deceptive conduct,[175] or for failure to comply with an "express warranty".[176] All of these claims are independent of the contract and the parol evidence rule has no application.

166 *Hoyt's Pty Ltd v Spencer* (1919) 27 CLR 133, 141, 148.

167 *Hoyt's Pty Ltd v Spencer* (1919) 27 CLR 133, 147.

168 *Hoyt's Pty Ltd v Spencer* (1919) 27 CLR 133, 147. There is no strict rule that a collateral contract between a party to the principal contract and a stranger to the principal contract must be consistent with the terms of the principal contract: *Manning Motel Pty Ltd v DH MB Pty Ltd* [2013] NSWSC 1582, [25]–[26], appeal dismissed in *DH MB Pty Ltd v Manning Motel Pty Ltd* [2014] NSWCA 396.

169 *Mainieri v Cirillo* [2014] VSCA 227; (2014) 47 VR 127.

170 *Mainieri v Cirillo* [2014] VSCA 227; (2014) 47 VR 127, [12], [13].

171 *Mainieri v Cirillo* [2014] VSCA 227; (2014) 47 VR 127, [21]–[23].

172 *Mainieri v Cirillo* [2014] VSCA 227; (2014) 47 VR 127, [16]–[20].

173 *Mainieri v Cirillo* [2014] VSCA 227; (2014) 47 VR 127, [40].

174 See [9.190]ff.

175 *Australian Consumer Law*, s 18.

176 *Australian Consumer Law*, s 59.

CHAPTER **13**

Construing the terms

CONSTRUCTION

[13.05] Construction is the process through which courts determine the meaning and legal effect of contract terms. The words "construction" and "interpretation" are now usually used interchangeably to refer to that process. The word "interpretation" is sometimes used more narrowly to refer to the meaning of the words, as distinct from their legal effect.[1] The High Court observed in *Collector of Customs v Agfa-Gevert Ltd*,[2] however, that such a distinction between interpretation and construction "seems artificial, if not illusory". Construing a legal text and identifying the meaning of particular words within it are not separate processes but rather are interdependent.[3] The word "construction" is sometimes used in a broader sense which encompasses the identification of implied terms.[4] As we will see in Chapter 14, the identification of implied terms in the business efficacy category can be understood as an interpretive exercise and can accurately be characterised as part of the process of construction of a contract.

Disputes over the construction of terms arise because parties cannot foresee all of the events that may affect performance of their contract. Unexpected events or circumstances sometimes reveal areas of disagreement between the parties as to who bears the burden of particular risks. Terms that appeared adequate at the time the contract was drafted may prove

1 *Life Insurance Co of Australia Ltd v Phillips* (1925) 36 CLR 60, 78 (meaning of words said to be a question of fact and their legal effect a question of law).

2 *Collector of Customs v Agfa-Gevert Ltd* (1996) 186 CLR 389, 396 (Brennan CJ, Dawson, Toohey, Gaudron and McHugh JJ).

3 *Collector of Customs v Agfa-Gevert Ltd* (1996) 186 CLR 389, 396–7. See also Heydon, *Heydon on Contract* (2019), [8.50]; McMeel, *The Construction of Contracts* (3rd ed, 2017), [9.03]; Carter, *The Construction of Commercial Contracts* (2013), [1-05].

4 Heydon, *Heydon on Contracts* (2019), [8.80]; Robertson, "The Foundations of Implied Terms: Logic, Efficacy and Purpose", in Degeling, Edelman and Goudkamp (eds), *Contract in Commercial Law* (2016), 143, 150.

to be ambiguous when they are considered in the context of events or changed circumstances that affect performance of the contract. Moreover, in some cases, "ambiguities may arise from a deliberate decision to keep the terms of the agreement between the parties vague, because they are difficult to define, and it is hoped there will be no occasion for disagreement".[5] Parties to contractual negotiations sometimes choose to avoid discussion of broad issues of risk allocation, choosing instead just to bargain to find a form of words that is acceptable to both parties.[6] Parties may be "at pains not to expose what they want from the terms and operation of an agreement" because it might "damage their bargaining position" to do so.[7]

In construing a contract, courts seek to determine what a reasonable person would understand the terms to mean. In the case of a commercial contract, the aim is to identify what a reasonable business person would understand the terms to mean.[8] That depends on a consideration of the text, context and purposes of the contract, and the idea that the contract should make commercial sense. In other words, the courts direct their attention to the language of the provision in question in light of the contract as a whole, taking account of the purpose or objects of the contract, and assuming that the parties intended to produce a "commercial result" which avoids "making commercial nonsense or working commercial inconvenience".[9]

Until quite recently, it was commonly said that the aim of contractual interpretation was to identify the mutual intentions of the parties.[10] Since the common law takes an objective approach to interpretation, however, it is potentially misleading to describe it as an inquiry that is concerned with the parties' intentions.[11] Moreover, at the time the contract was made, the parties may well have had different intentions, or no intentions at all, in relation to an issue which only later assumes importance.[12] Lord Hoffmann's influential speech in *Investors Compensation Scheme Ltd v West Bromwich Building Society*[13] has now firmly entrenched "the ascertainment of the meaning which the document would convey to reasonable person" as the dominant understanding of the exercise. As in other areas of contract law, there may be a minor role for subjective considerations, but the common law approach to construction is, on the whole, strongly objective. Where there is clear evidence that the parties' actual intentions at the time the contract was made differed from the meaning that a reasonable person would attribute to the contract, there may be grounds to have the contract rectified on the basis of a common mistake.[14]

AVAILABLE EVIDENCE

[13.10] It is often said that a provision in a written contract must be read and understood in its context. The immediate and most relevant context is the contractual document itself.

5 *Hide & Skin Trading Pty Ltd v Oceanic Meat Traders Ltd* (1990) 20 NSWLR 310, 313.
6 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [21].
7 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [21].
8 *Electricity Generation Corporation (trading as Verve Energy) v Woodside Energy Ltd* [2014] HCA 7; (2014) 251 CLR 640, [35].
9 *Electricity Generation Corporation (trading as Verve Energy) v Woodside Energy Ltd* [2014] HCA 7; (2014) 251 CLR 640, [35], quoting *Zhu v Treasurer* (NSW) (2004) 218 CLR 530, [82].
10 See Lewison, *The Interpretation of Contracts* (6th ed, 2015).
11 See Robertson, "Purposive Contractual Interpretation" (2019) 39 *Legal Studies* 230, 231–3.
12 See Summit Investment Inc v British Steel Corporation (The "Sounion") [1987] l Lloyd's Rep 230, 233.
13 *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896, esp 912–3.
14 See [31.65].

A fundamental rule of construction is that a contractual provision must be read in light of the instrument as a whole: "the meaning of any one part of it may be revealed by other parts" and "every clause must if possible be construed so as to render them all harmonious with one another".[15] Any "contract, document or statutory provision referred to in the text of a contract" is also considered part of the internal context which can always be taken into account.[16] Although the issue is controversial, there is widely understood to be a general rule that extrinsic evidence is inadmissible on questions of interpretation. In *L Schuler AG v Wickman Machine Tool Sales Ltd*,[17] for example, Lord Wilberforce said:

> The general rule is that extrinsic evidence is not admissible for the construction of a written contract; the parties' intention must be ascertained, on legal principles of construction, from the words they have used. It is one and the same principle which excludes evidence of statements, or actions, during negotiations, at the time of the contract, or subsequent to the contract, any of which to the lay mind might at first sight seem to be proper to receive.

This general rule is sometimes referred to as an aspect or strand of the parol evidence rule, which operates in relation to the identification of the terms of a contract and was discussed at [12.110].[18] The exclusion of extrinsic evidence for the purpose of identifying terms and the exclusion of extrinsic evidence for the purpose of construing terms have similar rationales. As Heydon has observed, they are both concerned to give respect, finality and certainty to the written record the parties have created and to "avoid tenders of controversial evidence seeking to upset those agreements".[19] Since the rules operate in quite different ways, with entirely different sets of qualifications and exceptions, they are probably best treated as two separate rules in order to avoid confusion.

Lord Wilberforce noted in *L Schuler AG v Wickman Machine Tool Sales Ltd*[20] that there are exceptions to the general rule set out above, including rules that:

> evidence may be admitted of surrounding circumstances or in order to explain technical expressions or to identify the subject matter of an agreement: or (an overlapping exception), to resolve a latent ambiguity. But ambiguity in this context is not to be equated with difficulty of construction, even difficulty to a point where judicial opinion as to meaning has differed. This is, I venture to think, elementary law.

As we will see below, whether an exception relating to "surrounding circumstances" is recognised in Australian law has become a contentious question.

It is common in this context to talk about whether evidence is "admissible", and sometimes whether it is "receivable" or is "excluded". In *Franklins Pty Ltd v Metcash Trading Ltd*,[21] Campbell JA observed that:

> The word "admissible" is itself ambiguous, even when used in a legal context. It can refer to a rule of evidence, under which, if evidence is not admissible, it is neither received nor considered by the court. Alternatively, it can mean that evidence that is not "admissible" is evidence that is not legitimately able to be used by a court in some particular reasoning process.

15 *Australian Broadcasting Commission v Australasian Performing Right Association Ltd* (1973) 129 CLR 99, 109.

16 *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* [2015] HCA 37; (2015) 256 CLR 104, [46].

17 *L Schuler AG v Wickman Machine Tool Sales Ltd* [1974] AC 235, 261, quoted with approval in *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 348.

18 See, eg, *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 347.

19 Heydon, *Heydon on Contract* (2019), [9.140].

20 *L Schuler AG v Wickman Machine Tool Sales Ltd* [1974] AC 235, 261.

21 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [258].

References to the "admissibility" of evidence in the context of contract interpretation should be understood to refer primarily to the second meaning above: that is, whether the evidence can legitimately be used or taken into account in the determination of a construction question.[22] Evidence that is irrelevant or which cannot legitimately be used may be excluded at trial, but extrinsic evidence is commonly received, at least provisionally. There are at least three reasons for this. First, it may not be possible or feasible for a judge to determine until the conclusion of a trial whether extrinsic evidence can legitimately be used.[23] Secondly, receiving the evidence will avoid a new trial if the evidence is ruled admissible on appeal.[24] Thirdly, the evidence in question may be received in any case because it is unquestionably relevant to another claim in the proceedings, such as a formation question, estoppel by convention or rectification.

Surrounding circumstances

[13.15] In *Reardon Smith Line v Hansen-Tangen*, Lord Wilberforce said that:

> In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.[25]

Following this statement, in England, the House of Lords and the Supreme Court have confirmed that evidence of the surrounding circumstances is always admissible in construing a contract.[26] In *Investors Compensation Scheme Ltd v West Bromwich Building Society*, Lord Hoffmann set out a restatement of the principles of contractual interpretation which has since been very influential. These principles assigned a generous role to surrounding circumstances or background information in construing a contract:

(1) Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.

(2) The background was famously referred to by Lord Wilberforce as the "matrix of fact", but this phrase is, if anything, an understated description of what the background may include. Subject to the requirement that it should have been reasonably available to the parties and to the exception to be mentioned next, it includes absolutely anything which would have affected the way in which the language of the edocument would have been understood by a reasonable man.[27]

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22 On this issue, see *Cherry v Steel-Park* [2017] NSWCA 295; (2017) 96 NSWLR 548, [49]–[56].

23 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [260].

24 *McCourt v Cranston* [2012] WASCA 60, [25]–[26].

25 *Reardon Smith Line v Hansen-Tangen* [1976] 1 WLR 989, 995–6.

26 *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1997] UKHL 28; [1998] 1 WLR 896, 912–3; *ICS Ltd v West Bromwich Building Society* [1998] 1 WLR 896, 912–3; *Bank of Credit and Commerce International SA v Ali* [2001] UKHL 8; [2002] 1 AC 251, [8], [39]; *Arnold v Britton* [2015] UKSC 36; [2015] AC 1619, [15]. See also *Zurich Insurance (Singapore) Pte Ltd v B-Gold Interior Design & Construction Pte Ltd* [2008] SGCA 27; [2008] 3 SLR 1029; *Fully Profit (Asia) Ltd v Secretary for Justice* [2013] HKCFA 40; 6 HKC 374.

27 *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1997] UKHL 28; [1998] 1 WLR 896, 913. Lord Hoffmann clarified this statement in *Bank of Credit and Commerce International SA v Ali* [2001] UKHL 8; [2002] 1 AC 251, [39] saying:

> when … I said that the admissible background included "absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man", I did not think it necessary to emphasise that I meant anything which a reasonable man would have regarded as *relevant*. I was merely saying that there is no conceptual limit to what can be regarded as background.

Lord Hoffmann also explained why it was necessary for courts to have regard to the surrounding circumstances in construing a contract:

> (4) The meaning which a document (or any other utterance) would convey to a reasonable man is not the same thing as the meaning of its words. The meaning of words is a matter of dictionaries and grammars; the meaning of the document is what the parties using those words against the relevant background would reasonably have been understood to mean. The background may not merely enable the reasonable man to choose between the possible meanings of words which are ambiguous but even (as occasionally happens in ordinary life) to conclude that the parties must, for whatever reason, have used the wrong words or syntax.[28]

In Australia, a more restrictive approach to admitting evidence of the surrounding circumstances is generally taken, although it remains controversial and is not universally followed. In *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (*Codelfa*),[29] Mason J stated that "the true rule is that evidence of surrounding circumstances is admissible to assist in the interpretation of the contract if the language is ambiguous or susceptible of more than one meaning".[30] One interpretation of this statement is that recourse to evidence of the surrounding circumstances in construing a contract is only permissible in cases of ambiguity, which must be identified without regard to those circumstances. Another interpretation is that Mason J was merely confirming that "there are very real limits to the extent to which the grammatical meaning can be displaced by contextual considerations".[31] On this view, the surrounding circumstances can influence the interpretation of a contract but cannot be used to improve on or contradict the written terms of that contract.

In *Royal Botanic Gardens and Domain Trust v South Sydney City Council*,[32] Gleeson CJ, Gaudron, HcHugh, Gummow and Hayne JJ referred to both the decision of the House of Lords in *Investors Compensation Scheme Ltd v West Bromwich Building Society* and Mason J's judgment in *Codelfa*, and said:

> It is unnecessary to determine whether their Lordships there took a broader view of the admissible "background" than was taken in *Codelfa* or, if so, whether those views should be preferred to those of this court. Until that determination is made by this court, other Australian courts, if they discern any inconsistency with *Codelfa*, should continue to follow *Codelfa*.[33]

The effect of this statement is itself ambiguous. It might be interpreted to suggest that a court should consider evidence of the circumstances surrounding the contract only where the language is ambiguous or susceptible of more than one meaning.[34] Alternatively, their Honours might have been saying that, to the extent that the types of evidence of the surrounding

28 *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1997] UKHL 28; [1998] 1 WLR 896, 921–3.

29 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 351.

30 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 352. See also *Bacchus Marsh Concentrated Milk Co Ltd v Joseph Nathan & Co Ltd* (1919) 26 CLR 410, 427; *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, [139].

31 *Mainteck Services Pty Ltd v Stein Heurtey SA* [2014] NSWCA 184; (2014) 89 NSWLR 633, [80].

32 *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45.

33 *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45, [39].

34 See further the discussion of this statement in *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [15]–[17], [49], [239]–[292].

circumstances referred to as admissible in Investors are wider than those recognised in *Codelfa*, *Codelfa* should be preferred.[35]

Subsequent High Court decisions appeared to suggest that the process of construing a contract should, as a matter of course, involve considering the full range of objectively known circumstances surrounding the transaction.[36] For example, in *Maggbury Pty Ltd v Hafele Australia Pty Ltd*, the High Court stated:[37]

> Interpretation of a written contract involves, as Lord Hoffmann has put it: "the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract".

A number of intermediate appellate courts took these statements as confirming that a court did not need to find that the language of a contract was ambiguous before admitting evidence of the circumstances surrounding the contract for the purpose of construing that contract.[38] In *Franklins Pty Ltd v Metcash Trading Ltd*, the NSW Court of Appeal considered that, since *Codelfa*, there had clearly been a change in the principles governing the admission of the surrounding circumstances in construing a contract, and that the position was now consistent with that in England. Allsop JA said:

> The construction and interpretation of written contracts is to be undertaken by an examination of the text of the document in the context of the surrounding circumstances known to the parties, including the purpose and object of the transaction and by assessing how a reasonable person would have understood the language in that context. There is no place in that structure, so expressed, for a requirement to discern textual, or any other, ambiguity in the words of the document before any resort can be made to such evidence of surrounding circumstances.[39]

A further statement of the High Court's view of the correct approach was given in *Western Export Services Inc v Jireh International Pty Ltd*[40] in response to an application for special leave to appeal. The High Court refused special leave but took the unusual step of giving a short judgment. Gummow, Heydon and Bell JJ referred to *Franklins Pty Ltd v Metcash Trading Ltd*, in which the NSW Court of Appeal held that there was no requirement for a court to identify

35 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [281].

36 *Pacific Carriers Ltd v BNP Paribas* [2004] HCA 35, [22]; (2004) 218 CLR 451, 461–2; *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52, [40]; (2004) 219 CLR 165, 179; *International Air Transport Association v Ansett Australia Holdings Ltd* [2008] HCA 3; (2008) 234 CLR 151, [8]; *Byrnes v Kendle* [2011] HCA 26; (2011) 243 CLR 253, [98]–[99].The approach also has support in a number of Australian decisions prior to *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45. See, eg, *Trawl Industries Australia Pty Ltd v Effem Foods Pty Ltd (t/as Uncle Ben's of Australia)* (1992) 27 NSWLR 326, 358–9; B & *B Constructions (Aust) Pty Ltd v Brian A Cheeseman & Associates Pty Ltd (1994) Pty Ltd* (1994) 35 NSWLR 227, 236, 243; *Acorn Consolidated Pty Ltd v Hawkslade Investments Pty Ltd* (1999) 21 WAR 425.

37 *Maggbury Pty Ltd v Hafele Australia Pty Ltd* [2001] HCA 70; (2001) 210 CLR 181, [11] (Gleeson CJ, Gummow and Hayne JJ) (with whom Kirby J [62] and Callinan J [89] agreed generally on this point).

38 See in particular *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [14]–[17], [49], [239]–[292]; *MBF Investments Pty Ltd v Nolan* [2011] VSCA 114, [195]–[204]. Also *Lion Nathan Australia Pty Ltd v Coopers Brewery Ltd* [2006] FCAFC 144; (2006) 156 FCR 1, [46], [100], [238]; *Masterton Homes Pty Ltd v Palm Assets Pty Ltd* [2009] NSWCA 234, [113]; *Callide Power Management Pty Ltd v Callide Coalfields (Sales) Pty Ltd* [2008] QCA 182, [64]; *Australian Medical Insurance Ltd v CGU Insurance Ltd* [2010] QCA 189, [74]. But cf *Quirke v FCL Interstate Transport Services Pty Ltd* [2005] SASC 226; (2005) 92 SASR 249.

39 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [14] (Allsop P) (Giles JA [63] agreeing), [239]–[305] (Campbell JA) (Giles JA [42]–[43] agreeing).

40 *Western Export Services Inc v Jireh International Pty Ltd* [2011] HCA 45.

ambiguity in the language of the contract before having regard to the surrounding circumstances and object of the transaction. The High Court rejected this approach, stating that it:

> would require reconsideration by this Court of what was said in *Codelfa Construction Pty Ltd v State Rail Authority of NSW* by Mason J, with the concurrence of Stephen J and Wilson J, to be the "true rule" as to the admission of evidence of surrounding circumstances. Until this Court embarks upon that exercise and disapproves or revises what was said in Codelfa, intermediate appellate courts are bound to follow that precedent. The same is true of primary judges, notwithstanding what may appear to have been said by intermediate appellate courts.
>
> The position of Codelfa, as a binding authority, was made clear in the joint reasons of five Justices in *Royal Botanic Gardens and Domain Trust v South Sydney City Council* and it should not have been necessary to reiterate the point here.[41]

This statement has failed to resolve the uncertainty over the admissibility of evidence of the surrounding circumstances. As noted by the High Court itself in *Mount Bruce Mining Pty Limited v Wright Prospecting Pty Ltd* (*Mount Bruce Mining*), applications for special leave "create no precedent and are binding on no one".[42] In a subsequent decision, *Electricity Generation Corporation v Woodside Energy Ltd*, the High Court appeared again to acknowledge the importance of context in construing a contract.[43] French CJ, Hayne, Crennan and Kiefel JJ stated that:

> The meaning of the terms of a commercial contract is to be determined by what a reasonable business person would have understood those terms to mean … it will require consideration of the language used by the parties, the surrounding circumstances known to them and the commercial purpose or objects to be secured by the contract.[44]

These apparently inconsistent statements left lower courts in a difficult and uncertain position.[45] Some courts continued to follow the direction in *Western Export Services Inc v Jireh International Pty Ltd*[46] and to treat ambiguity as a gateway requirement to considering evidence of the surrounding circumstances.[47] The New South Wales Court of Appeal and the Full Federal Court interpreted *Electricity Generation Corporation v Woodside Energy Ltd*,[48] as affirming the approach in *Franklins Pty Ltd v Metcash Trading Ltd*,[49] and the view that in "construing a contract, the Court may take into account evidence of circumstances attending formation of the contract, even in the absence of ambiguity".[50]

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41 *Western Export Services Inc v Jireh International Pty Ltd* [2011] HCA 45.

42 *Mount Bruce Mining Pty Limited v Wright Prospecting Pty Ltd* [2015] HCA 37; (2015) 256 CLR 104, [52], [112], [119].

43 *Electricity Generation Corporation v Woodside Energy Ltd* [2014] HCA 7; (2014) 251 CLR 640.

44 *Electricity Generation Corporation v Woodside Energy Ltd* [2014] HCA 7; (2014) 251 CLR 640, [35].

45 See *McCourt v Cranston* [2012] WASCA 60, [22]–[26]. Also Lindgren, "The Ambiguity of 'Ambiguity' in the Construction of Contracts" (2014) 38 *Australian Bar Review* 153.

46 *Western Export Services Inc v Jireh International Pty Ltd* [2011] HCA 45.

47 See, eg, *Gladstone Area Water Board v AJ Lucas Operations Pty Ltd* [2014] QSC 311, [153]–[168]; *State of Victoria v Tatts Group* [2014] VSCA 311, [118]; *Technomin Australia Pty Ltd v Xstrata Nickel Australasia Operations Pty Ltd* [2014] WASCA 164; (2014) 38 WAR 261, [73].

48 *Electricity Generation Corporation (trading as Verve Energy) v Woodside Energy Ltd* [2014] HCA 7; (2014) 251 CLR 640.

49 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603.

50 See, eg, *Neale v Ancher Mortlock & Woolley Pty Ltd* [2014] NSWCA 72, [63]; *Mainteck Services Pty Ltd v Stein Heurtey SA* [2014] NSWCA 184; (2014) 89 NSWLR 633, [86]; *Newey v Westpac Banking Corporation* [2014] NSWCA 319, [86]; *Stratton Finance Pty Ltd v Webb* [2014] FCAFC 110, [40].

In *Mount Bruce Mining*, the High Court declined to resolve the question of whether "ambiguity must be shown before a court interpreting a written contract can have regard to background circumstances", on the ground that it was not raised by the case.[51] The Court affirmed the position as stated in *Codelfa* as binding authority until that time.[52] French CJ, Nettle and Gordon J also affirmed the primacy of the written document, stating:

> Ordinarily, this process of construction is possible by reference to the contract alone. Indeed, if an expression in a contract is unambiguous or susceptible of only one meaning, evidence of surrounding circumstances (events, circumstances and things external to the contract) cannot be adduced to contradict its plain meaning.[53]

In *Cherry v Steele-Park*,[54] the New South Wales Court of Appeal adhered to the position it had adopted before *Mount Bruce Mining*[55] that, on its interpretation of the relevant authorities, regard may be had to surrounding circumstances "without passing through an 'ambiguity gateway' ". Leeming JA expressed the view that two decisions of the High Court handed down since *Mount Bruce Mining* "strengthen the conclusion reiterated that 'ambiguity' is a conclusion, rather than a precondition to the admissibility of evidence of surrounding circumstances".[56] In *Mainteck Services Pty Ltd v Stein Heurtey SA*, Leeming JA had reasoned that whether contractual language is ambiguous or has a plain meaning is a conclusion that "cannot be reached until one has had regard to the context".[57] That is because the meaning of words can only be understood in light of the circumstances in which they are used.[58] The impossibility of reaching a conclusion in relation to ambiguity without regard to the surrounding circumstances is evidenced by the well-established recognition of the potential for latent ambiguity, discussed at [13.20].[59]

Note that there are two issues here. The first issue is whether extrinsic evidence of surrounding circumstances can always be taken into account in construing a contractual provision, as it can under English law. In the Victorian Court of Appeal in *Apple and Pear Australia Ltd v Pink Lady America LLC*, Tate JA respectfully disagreed with Leeming JA's analysis and gave a negative answer to that question.[60] Tate JA said:

> In my view, it follows from what was said in *Mount Bruce* that it would be wrong to conclude that the High Court has endorsed an approach to the construction of commercial contracts, whereby the surrounding circumstances, including, relevantly, pre-contractual negotiations, can invariably be relied upon to assist construction. This is not to deny that the objective

51 *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* [2015] HCA 37; (2015) 256 CLR 104, [52], [113], [118].

52 *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* [2015] HCA 37; (2015) 256 CLR 104, [52], [119].

53 *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* [2015] HCA 37; (2015) 256 CLR 104, [48].

54 *Cherry v Steel-Park* [2017] NSWCA 295; (2017) 96 NSWLR 548, [71], [68]–[86].

55 For example, *Mainteck Services Pty Ltd v Stein Heurtey SA* [2014] NSWCA 184; (2014) 89 NSWLR 633, [71]–[85].

56 *Cherry v Steel-Park* [2017] NSWCA 295; (2017) 96 NSWLR 548, [79], citing and discussing *Victoria v Tatts Group Ltd* [2016] HCA 5 and *Simic v NSW Land and Housing Corporation* [2016] HCA 47; (2016) 260 CLR 85. See also *WIN Corporation Pty Ltd v Nine Network Australia Pty Ltd* [2016] NSWCA 297, [59].

57 *Mainteck Services Pty Ltd v Stein Heurtey SA* [2014] NSWCA 184; (2014) 89 NSWLR 633, [79].

58 *Mainteck Services Pty Ltd v Stein Heurtey SA* [2014] NSWCA 184; (2014) 89 NSWLR 633, [73].

59 See also the examples given in *Mainteck Services Pty Ltd v Stein Heurtey SA* [2014] NSWCA 184; (2014) 89 NSWLR 633, [76].

60 *Apple and Pear Australia Ltd v Pink Lady America LLC* [2016] VSCA 280, [136]–[137].

> approach to contractual interpretation requires, as confirmed by French CJ, Nettle and Gordon JJ in *Mount Bruce*, reference to the 'text, context (the entire text of the contract as well as any contract, document or statutory provision referred to in the text of the contract) and purpose'.[61]

The second issue is whether, if evidence of surrounding circumstances is not always available to be used, extrinsic evidence can nevertheless be relied upon to establish an ambiguity. Because the extrinsic evidence relied upon in *Apple and Pear Australia Ltd v Pink Lady America LLC* did not raise any relevant ambiguity, Ferguson and McLeish JJA expressly declined to address that controversy.[62]

Ambiguity

[13.20] The meaning of "ambiguity" justifying recourse to extrinsic evidence in construing a contract is itself open to a number of interpretations. As Leeming JA observed in *Cherry v Steel-Park*: "'Ambiguous' (like 'awkward' or 'polysyllabic') is autological."[63]

Ambiguity is clearly present where words used in a contract do not have a readily ascertainable meaning or are used in an inconsistent manner. This is sometimes referred to as "patent" ambiguity. For example, in *RW Cameron & Co v Slutzkin Pty Ltd*, the parties entered into a contract for the sale of "Matchless 2475 39/40 White Voile". The words were not of well-known significance in the trade. The purchaser had entered into the contract on the basis of being shown a sample of the fabric labelled "Matchless 2475 39/40 White Voile". The High Court held that evidence of this sample and the conversation between the parties was admissible for the purpose of identifying the subject matter of the contract. The words in question had no definite meaning unless explained by this evidence.[64]

A second type of ambiguity, known as a "latent" ambiguity, arises where a description in a contractual document "evidently meant to apply to only one person or thing, is shown to be equally applicable to more than one person or thing".[65] A promise by A to sell "my car" to B is not ambiguous on its face but is revealed to contain a latent ambiguity if extrinsic evidence shows that A owns two cars.[66] Latham CJ said in *Hope v RCA Photophone of Australia Pty Ltd* that a latent ambiguity "is raised by extrinsic evidence and it is allowed to be removed by similar evidence".[67] This has long been accepted[68] and has been classed an exception to the exclusionary rule relation to extrinsic evidence.[69]

It is now generally accepted that, for the purposes of admitting evidence of the surrounding circumstances, ambiguity "is not confined to lexical, grammatical or syntactical ambiguity"[70]

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61 *Apple and Pear Australia Ltd v Pink Lady America LLC* [2016] VSCA 280, [137], citing *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* [2015] HCA 37; (2015) 256 CLR 104, [46].

62 *Apple and Pear Australia Ltd v Pink Lady America LLC* [2016] VSCA 280, [232].

63 *Cherry v Steele-Park* [2017] NSWCA 295; (2017) 96 NSWLR 548, [71].

64 *RW Cameron & Co v Slutzkin Pty Ltd* (1923) 32 CLR 81, 86, 91, 94.

65 *Hope v RCA Photophone of Australia Pty Ltd* (1937) 59 CLR 348, 356.

66 See further *Mainteck Services Pty Ltd v Stein Heurtey SA* [2014] NSWCA 184; (2014) 89 NSWLR 633, [76].

67 *Hope v RCA Photophone of Australia Pty Ltd* (1937) 59 CLR 348, 357.

68 *Lord Cheyney's Case* (1591) 5 Co Rep 68; 77 ER 158 (in the context of a will); *Macdonald v Longbottom* (1860) 1 El & El 987, 989; 120 ER 1181, 1181.

69 *L Schuler AG v Wickman Machine Tool Sales Ltd* [1974] AC 235, 261.

70 *Technomin Australia Pty Ltd v Xstrata Nickel Australasia Operations Pty Ltd* [2014] WASCA 164; (2014) 38 WAR 261, [73].

but extends to any situation in which a contractual provision is "susceptible of more than one meaning".[71] The Western Australian Court of Appeal has held that relevant ambiguity may be found in "any situation in which the scope or applicability of a contract is, for whatever reason, doubtful", but:

> The fact that adversaries can formulate and advance materially different constructions of the language of a contract does not itself satisfy the gateway requirement. Having regard to the language of the contract as a whole and what can be gleaned from that source as to the contractual purpose, *competing constructions must be reasonably arguable*.[72]

Particular categories of extrinsic evidence

[13.25] We have seen that, where a "constructional choice" arises from a contractual ambiguity, it is permissible to have regard to "events circumstances and things external to a contract".[73] The next question is what extrinsic evidence can be considered. It is clearly permissible to have regard to evidence identifying "the genesis of the transaction, the background, the context, the market in which the parties are operating".[74] In *Mount Bruce Mining*, French CJ, Nettle and Gordon JJ said:

> Each of the events, circumstances and things external to the contract to which recourse may be had is objective. What may be referred to are events, circumstances and things external to the contract which are known to the parties or which assist in identifying the purpose or object of the transaction, which may include its history, background and context and the market in which the parties were operating.[75]

There are some types of extrinsic evidence that can be referred to only in particular circumstances, and some that can be used only in particular ways.

Subjective intentions

[13.30] Where evidence of the surrounding circumstances is admissible, it is limited to objectively known facts and does not include evidence of the parties' subjective intentions.[76] As Heydon and Crennan JJ stated in *Byrnes v Kendle*, "these conclusions flow from the objective theory of contractual obligation. Contractual obligation does not depend on actual mental agreement".[77] Their honours quoted Oliver Wendell Holmes' famous statement that "nothing

71 *Codelfa Construction Pty Ltd v State Rail Authority of NSW* (1982) 149 CLR 337, 350 (where Mason J referred to "an ambiguity, that is, where the words are susceptible of more than one meaning"). The proposition in the text is supported by *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45, 52 and *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* [2015] HCA 37; (2015) 256 CLR 104, [48]. See also Heydon, *Heydon on Contract* (2019), [9.680]–[9.720].

72 *Technomin Australia Pty Ltd v Xstrata Nickel Australasia Operations Pty Ltd* [2014] WASCA 164; (2014) 38 WAR 261, [73]–[74] (McLure P, with whom Newnes JA agreed) (emphasis added).

73 *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* [2015] HCA 37; (2015) 256 CLR 104, [49].

74 *Reardon Smith Line v Hansen-Tangen* [1976] 1 WLR 989, 995, quoted with approval numerous times in High Court judgments: see, eg, *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* [2015] HCA 37; (2015) 256 CLR 104, [49].

75 *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* [2015] HCA 37; (2015) 256 CLR 104, [50].

76 See, eg, *Life Insurance Co of Australia Ltd v Phillips* (1925) 36 CLR 60, 71; *Secured Income Real Estate (Australia) v St Martin's Investments Pty Ltd* (1979) 144 CLR 596, 606; *Pacific Carriers Ltd v BNP Paribas* [2004] HCA 35; (2004) 218 CLR 451, [22].

77 *Byrnes v Kendle* [2011] HCA 26; (2011) 243 CLR 253, [100].

is more certain than that parties may be bound by a contract to things which neither of them intended".[78] Evidence of the parties' subjective intentions is never relevant to the process of determining what a reasonable person would understand the contract to mean.

In *Codelfa*, Mason J suggested that evidence of the actual intentions of the parties might, in one very limited category of case, be admissible and permitted to prevail over the meaning that a reasonable person would attribute to the contract:

> If it transpires that the parties have refused to include in their contract a provision which would give effect to the presumed intention of persons in their position it may be proper to receive evidence of that refusal.[79]

Pre-contractual negotiations

[13.35] When it comes to evidence of the parties' pre-contractual negotiations, it is necessary to distinguish between evidence that establishes mutually known background facts and evidence as to the aspirations and intentions of the parties. Negotiations leading to the formation of a contract are inadmissible to the extent that they consist of "statements and actions" of the parties which reflect their "actual intentions and expectations" and "reveal the terms of the contract which the parties intended or hoped to make".[80] Evidence of negotiations may, however, be admissible to the extent that it establishes "objective background facts which were known to both parties", [81] and this would seem to include the genesis and objectively manifested aim of the contract.[82] Evidence of negotiations may also be used, at least in the case of ambiguity, to identify the subject matter of the contract or the meaning of a descriptive term.

Identifying the subject matter or the meaning of a descriptive term

[13.40] In *Prenn v Simmonds*, Lord Wilberforce observed that it has been clear since the decision in *Macdonald v Longbottom*[83] that "evidence of mutually known facts may be admitted to identify the meaning of a descriptive term".[84] In *Macdonald v Longbottom*, the defendant agreed by an exchange of letters to buy "your wool" from the plaintiffs. One of the plaintiffs had previously told the defendant's agent that the plaintiffs had a quantity of wool to sell, some from their own farm and some from neighbouring farms, which they were selling as a single lot. The conversation was held to be "admissible to identify the subject matter of the contract and to shew what 'your wool' really was".[85] Lord Campbell said:

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78 *Byrnes v Kendle* [2011] HCA 26; (2011) 243 CLR 253, [100], quoting Holmes, "The Path of the Law" (1897) 10 *Harvard Law Review* 457, 463. See further at [13.60].

79 *Codelfa Construction Pty Ltd v State Rail Authority of NSW* (1982) 149 CLR 337, 352. See also *Esso Australia Ltd v Australian Petroleum Agents' & Distributors' Association* (1999) 3 VR 642, [19]; *Elesanar Constructions Pty Ltd v Queensland* [2007] QCA 208; *Sunset Vineyard Management Pty Ltd v Southcorp Wines Pty Ltd* [2008] VSCA 96, [48]; *Mrocki v Mountview Prestige Homes Pty Ltd* [2012] VSCA 74.

80 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 352.

81 *Codelfa Construction Pty Ltd v State Railway Authority of NSW* (1982) 149 CLR 337, 352.

82 *Prenn v Simmonds* [1971] 1 WLR 1381, 1385, quoted in *Codelfa Construction Pty Ltd v State Railway Authority of NSW* (1982) 149 CLR 337, 351.

83 *Macdonald v Longbottom* (1859) 1 El & El 977; 120 ER 1177.

84 *Prenn v Simmonds* [1971] 1 WLR 1381, 1384.

85 *Macdonald v Longbottom* (1859) 1 El & El 977, 986; 120 ER 1177, 1180.

> I am of opinion that, when there is a contract for the sale or a specific subject-matter, oral evidence may be received, for the purpose of shewing what that subject-matter was, of every fact within the knowledge of the parties before and at the time of the contract.[86]

Byles J in the Court of Exchequer Chamber justified the decision on the ground that a latent ambiguity "which is raised by extrinsic evidence, may be removed by extrinsic evidence".[87] There was clearly a latent ambiguity in the expression "your wool".

It is not clear whether evidence identifying the subject matter of a contract or the meaning of a descriptive term is always admissible, or only in the case of an ambiguity. In *L Schuler AG v Wickman Machine Tool Sales*, Lord Wilberforce treated evidence identifying the subject matter of the agreement as an independent exception to the exclusionary rule.[88] It is clear that extrinsic evidence may be given to identify the parties to, or subject matter of, a contract where these features are not revealed by the written contract.[89] Where the subject matter is expressly identified, however, extrinsic evidence may only be admissible where the description is subject to a patent or latent ambiguity. In *Bank of New Zealand v Simpson*, the Privy Council said in reference to *Macdonald v Longbottom* that: "Of course, if the words in question have a fixed meaning not susceptible of explanation, parol evidence is not admissible to shew that the parties meant something different from what they have said."[90]

Post-contractual conduct

[13.42] It is well established that in construing a contract, it is not generally legitimate to have regard to things said or done by the contracting parties after the contract was made.[91] This reflects the objective approach to interpretation: the post-contractual behaviour of the parties may provide some indication as to what the parties themselves understood the contract to mean but does not assist a court in determining what a reasonable person would have understood the contract to mean.[92] The exceptions to the general rule are consistent with the objective approach.[93] Possibly the only genuine exception is that post contractual events may provide "retrospectant evidence of a surrounding circumstance that was known to the

86 *Macdonald v Longbottom* (1859) 1 El & El 977, 983; 120 ER 1177, 1179.

87 *Macdonald v Longbottom* (1860) 1 El & El 987, 989; 120 ER 1181, 1181.

88 *L Schuler AG v Wickman Machine Tool Sales Ltd* [1974] AC 235, 261.

89 *Edwards v Edwards* (1918) 24 CLR 312; *RW Cameron & Co v Slutzkin Pty Ltd* (1923) 32 CLR 81; *White v Australian and New Zealand Theatres Ltd* (1943) 67 CLR 266; *Gilberto v Kenny* (1983) 48 ALR 620. See also *Retirement Services Australia (RSA) Pty Ltd v 3143 Victoria St Doncaster Pty Ltd* [2012] VSCA 134; (2012) 37 VR 486, [97].

90 *Bank of New Zealand v Simpson* [1900] AC 182, 189.

91 *James Miller & Partners Ltd v Whitworth Street Estates (Manchester) Ltd* [1970] AC 583, 603, quoted in *Agricultural and Rural Finance Pty Ltd v Gardiner* [2008] HCA 57; (2008) 238 CLR 570, [35], [163]. See also *Farmer v Honan* (1919) 26 CLR 183, 197; *White v Australian and New Zealand Theatres Ltd* (1943) 67 CLR 266, 271, 281; *Pethybridge v Stedikas Holdings Pty Ltd* [2007] NSWCA 154, [59]; *Masterton Homes Pty Ltd v Palm Assets Pty Ltd* [2009] NSWCA 234, [114]; *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [6], [11]; *Current Images Pty Ltd v Dupack Pty Ltd* [2012] NSWCA 99, [32]. See also the different view expressed in *Administration of the Territory of Papua and New Guinea v Daera Guba* (1973) 130 CLR 353, 446; *Posgold (Big Bell) Pty Ltd v Placer (Western Australia) Pty Ltd* [1999] WASCA 217; (1999) 21 WAR 350.

92 See Heydon, *Heydon on Contract* (2019), [9.1640]; cf Pilkington, "Subsequent Conduct and the Objective Theory of Contract" (2018) 45 *Australian Bar Review* 244.

93 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407, [327].

parties at the time of contracting".[94] Subsequent conduct has also been taken into account for the purpose of ascertaining the terms of a contract that is not wholly in writing.[95] It is well established that evidence of conduct after the supposed formation of a contract may be taken into account in order to determine whether a contract was in fact made, as distinct from what it means.[96]

Custom or trade usage

[13.45] Where parties have used in a contractual document language that has a special meaning in a particular context or locality, or in the parties' particular trade or industry, extrinsic evidence of that meaning may be admitted even in the absence of any apparent ambiguity.[97] In *Smith v Wilson*,[98] for example, an obligation to pay an amount "per thousand" rabbits was interpreted to mean "per 1,200" rabbits because, according to a well-established custom in that part of the country, rabbits were counted at "100 dozen to the thousand". To be admissible on this basis, however, the custom or trade meaning must be "well-known, uniform and certain".[99] It must also be known to both parties.[100]

An example of this principle is *Appleby v Pursell*,[101] which concerned a contract for the lease of rural land which obliged the lessors to "push and stack" the timber on the land. The lessors left the base of the trunks standing. The lessee complained that the lessors had breached the terms of the lease because this method left the land unsuitable for farming. A dispute accordingly arose as to the nature of the obligation imposed by the words "push and stack". The trial judge found in favour of the lessee, holding that the lease obliged the lessors to clear the timber in a manner that would bring the land into a condition suitable for farming. In reaching this conclusion, the judge admitted evidence of advertisements for the lease that referred to the land being "immediately available for farming" and of a conversation between the parties in which one of the lessors said that, for the amount of rent they were expecting for the land, "it would have to be farmed". An appeal against the decision was dismissed by the majority of the New South Wales Court of Appeal. The words "push" and "stack" do have a dictionary meaning. In circumstances where the phrase had a particular meaning in a trade or industry, however, evidence was admissible to establish that usage. Their Honours said that the evidence of the advertisements and the conversation between the parties was admissible to establish the background against which the parties had been contracting.[102]

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94 *Lym International Pty Ltd v Marcolongo* [2011] NSWCA 303, [142]. See also *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407, [324].

95 *Lym International Pty Ltd v Marcolongo* [2011] NSWCA 303, [143]; *County Securities Pty Limited v Challenger Group Holdings Pty Limited* [2008] NSWCA 193, [19]–[25].

96 *Australian Broadcasting Corporation v XIVth Commonwealth Games Ltd* (1988) 18 NSWLR 540, 550–1; *Sagacious Procurement Pty Ltd v Symbion Health Ltd (formerly Mayne Group Ltd)* [2008] NSWCA 149, [99]; *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407, [326].

97 See, eg, *Appleby v Pursell* [1973] 2 NSWLR 879, 889; *Homestake Australia Ltd v Metana Minerals NL* (1991) 11 WAR 435, 447; *Hodgson & Hodgson v Morella Pastoral Co Pty Ltd* (1975) 13 SASR 51, 62–3.

98 *Smith v Wilson* (1832) 3 B & Ad 728; 110 ER 266, 266.

99 *Homestake Australia Ltd v Metana Minerals NL* (1991) 11 WAR 435, 447–8.

100 *Kirchner v Venus* (1859) 12 Moo PC 361, 399; 14 ER 938, 963.

101 *Appleby v Pursell* [1973] 2 NSWLR 879.

102 *Appleby v Pursell* [1973] 2 NSWLR 879, 890, 896. See also, eg, *CNW Oil (Australasia) Pty Ltd v Australian Occidental Pty Ltd* (1984) 55 ALR 599.

The private dictionary principle

[13.47] In *Partenreederei MS Karen Oltmann v Scarsdale Shipping Co Ltd (The "Karen Oltmann")*, Kerr J held that where words in a contract are capable of bearing more than one meaning, it is permissible to admit extrinsic evidence which shows that the parties have used the words in a particular sense, "so they have in effect given their own dictionary meaning to the words as a result of their common intention".[103] The correspondence between the parties in that case showed that the word "after" in the expression "after 12 months trading" was used in an agreed sense to mean "on the expiry of" rather than "at any time after".

In *Chartbrook Ltd v Persimmon Homes Ltd*, Lord Hoffmann disapproved of Kerr J's decision as "an illegitimate extension of the 'private dictionary' principle which, taken to its logical conclusion, would destroy the exclusionary rule and any practical advantages which it may have".[104] Lord Hoffmann said that the "private dictionary" principle is akin to the custom and trade usage principle discussed above and is confined to the use of evidence "that the parties habitually used words in an unconventional sense in order to support an argument that words in a contract should bear a similar unconventional meaning".[105] On the facts of *Partenreederei MS Karen Oltmann v Scarsdale Shipping Co Ltd (The "Karen Oltmann")*, there was no private dictionary. The case simply "involved a choice between two perfectly conventional meanings of the word 'after' ".[106] Lord Hoffmann also noted that estoppel by convention (discussed at [9.200]) and rectification (discussed at [31.65]) provide "legitimate safety devices" which prevent injustice in cases falling outside the private dictionary principle.[107]

THE PROCESS OF CONSTRUING A CONTRACT

[13.50] In construing or interpreting a contract, the courts will be guided primarily by reference to the words used by the parties and also, in so far as this evidence is admissible, the factual and commercial context of the contract. In *Arnold v Britton*, Lord Neuberger said that the meaning of a contractual provision is assessed in light of:

> (i) the natural and ordinary meaning of the clause, (ii) any other relevant provisions of the [contract], (iii) the overall purpose of the clause and the [contract], (iv) the facts and circumstances known or assumed by the parties at the time that the document was executed, and (v) commercial common sense, but (vi) disregarding subjective evidence of any party's intentions.[108]

This is a helpful summary, although for the purposes of Australian law element (iv) needs to be qualified with the words "to the extent that evidence of these facts and circumstances are admissible".

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103 *Partenreederei MS Karen Oltmann v Scarsdale Shipping Co Ltd (The "Karen Oltmann")* [1976] 2 Lloyd's Rep 712, approved in various Australian cases such as *Gate Gourmet Australia Pty Ltd (in liq) v Gate Gourmet Holding AG* [2004] NSWSC 149, [182].

104 *Chartbrook Ltd v Persimmon Homes Ltd* [2009] UKHL 38; [2009] 1 AC 1101, [47].

105 *Chartbrook Ltd v Persimmon Homes Ltd* [2009] UKHL 38; [2009] 1 AC 1101, [45].

106 *Chartbrook Ltd v Persimmon Homes Ltd* [2009] UKHL 38; [2009] 1 AC 1101, [45].

107 *Chartbrook Ltd v Persimmon Homes Ltd* [2009] UKHL 38; [2009] 1 AC 1101, [47].

108 *Arnold v Britton* [2015] UKSC 36; [2015] AC 1619, [15].

The objective approach

[13.55] The terms of a contract are construed objectively, by reference to what a reasonable person in the position of the parties would have understood them to mean when read in light of the contract as a whole.[109] Although it is sometimes said that, in construing a contract, a court aims to give effect to the parties' intentions, those intentions are determined objectively, primarily on the basis of the words they have used in their contract. Courts do not consider what the parties privately intended the terms of their contract to mean, but rather what the words used would convey to a reasonable person in the position of the parties. In *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd*, the High Court said "[r]eferences to the common intention of the parties to a contract are to be understood as referring to what a reasonable person would understand by the language in which the parties have expressed their agreement".[110]

The justification for the objective standard of the reasonable person in construing a contract is commonly seen as based on considerations of "practical policy".[111] These considerations include ensuring certainty for contracting parties[112] and keeping litigation within reasonable bounds.[113] In *Equuscorp Pty Ltd v Glengallan Investments Pty Ltd*, the High Court of Australia explained that:

> in the nature of things, oral agreements will sometimes be disputable. Resolving such disputation is commonly difficult, time-consuming, expensive and problematic. Where parties enter into a written agreement, the Court will generally hold them to the obligations, which they have assumed by that agreement … In a time of growing international trade with parties in legal systems having the same or even stronger deference to the obligations of written agreements (and frequently communicating in different languages and from the standpoint of different cultures) this is not a time to ignore the rules of the common law upholding obligations undertaken in written agreements.[114]

[13.60] The objective approach to contract interpretation might not appear consistent with theories that conceive of contract as a realm of self-imposed obligations.[115] The construction given to the words of a contract through the objective standard of a reasonable person has typically been understood as giving effect to the "presumed" or "manifest", as opposed to the "actual" or "real", intentions of the parties.[116] Particularly if courts make use of the full range of evidence available to them about the circumstances in which the contract was made, it is likely that the parties' real intentions will usually coincide with the construction arrived at by the court using the standard of the reasonable person.[117] However, the objective approach means that it is the reasonable person, not the parties' actual intentions, that determines the

109 *Ecosse Property Holdings Pty Ltd v Gee Dee Nominees Pty Ltd* [2017] HCA 12; (2017) 261 CLR 544, [73].

110 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [40]. See also *Pacific Carriers Ltd v BNP Paribas* [2004] HCA 35; (2004) 218 CLR 451, [22].

111 *Investors Compensation Scheme v West Bromwich Building Society* [1997] UKHL 28; [1988] 1 WLR 896, 912–3.

112 *Pacific Carriers Ltd v BNP Paribas* [2004] HCA 35; (2004) 218 CLR 451, [22].

113 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 352.

114 *Equuscorp Pty Ltd v Glengallan Investments Pty Ltd* [2004] HCA 5; (2004) 218 CLR 471, [35].

115 See Chapter 1.

116 See, eg, *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 353 (Mason J); *Sirius International Insurance Co (Publ) v RAI General Insurance Ltd* [2004] 1 WLR 3251, [18] (Lord Steyn).

117 McLauchlan, "Contract Interpretation: What Is It About?" (2009) 31 *Sydney Law Review* 5; Vorster, "A Comment on the Meaning of Objectivity in Contract" (1987) 103 *Law Quarterly Review* 274.

meaning of their contract.[118] In extreme cases, a contract might have a meaning that was intended by neither party, as noted at [13.30]. In *Brambles Holdings Ltd v Bathurst City Council*, for example, Heydon JA noted that there was some evidence that the parties did not share the Court's conclusions as to what the contract meant, "but in the absence of any argument for a decree of rectification or for an estoppel by convention the actual opinions of the parties are irrelevant".[119]

There have been a number of scholarly attempts to reconcile the objective standard of the reasonable person that is used in construing a contract with the classical conception of contractual obligations as created by the parties.[120] In this context, scholars have drawn on linguistic philosophy, and in particular the work of Ludwig Wittgenstein,[121] to explain that construction is merely an application of the ordinary process of attributing meaning to words. Scholars drawing on linguistic philosophy argue that the meaning of an utterance is never determined by reference to the private intentions of the speaker of that utterance for the simple reason that we never have access to each other's private thoughts. As Jeff Goldsworthy explains, "[t]he meaning of a communication cannot be something potentially hidden within the speaker's mind and inaccessible to its intended recipients".[122] Rather, the meaning of an utterance must always be interpreted in a public or objective sense.[123] Thus, Brian Langille and Arthur Ripstein explain that "[t]here is nothing more to what a person means by their words than what others reasonably take them to mean".[124] The way we communicate is through shared language conventions and a common method of interpretation. Adam Kramer explains that it is this shared method that "allows a single jointly salient meaning to be identified from any utterance".[125]

Applied to contract law, scholars drawing on linguistic philosophy argue that the use of the objective standard of the reasonable person in construing a contract does not undermine a conception of contracts as created by the voluntary choices of the parties to that contract. Contracts, like everyday utterances, only ever have an objective meaning, interpreted from the perspective of the recipient of the communication. The reasonable person may therefore be seen merely as representing the ordinary or reasonable approach to interpreting language[126] and not as a judicially imposed standard that in some way subverts the process of giving effect to what the parties intended. A similar rationalisation has been applied to the role of the reasonable person in implying terms in fact, which will be discussed in Chapter 14.

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118 See comments on the extremes to which this approach may be taken in Seddon and Ellinghaus, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [10.31].

119 *Brambles Holdings Ltd v Bathurst City Council* [2001] NSWCA 61; (2001) 53 NSWLR 153, [46].

120 See Robertson, "The Limits of Voluntariness in Contract" (2005) 29 *Melbourne University Law Review* 179, 202.

121 Wittgenstein, *Philosophical Investigations: The German Text with Revised English Translation* (4th ed, 2009).

122 Goldsworthy, "Original Meanings and Contemporary Understandings in Constitutional Interpretation", in Lee and Gerangelos (eds), *Constitutional Advancement in a Frozen Continent* (2009), 245, 249. See also Kramer, "Common Sense Principles of Contract Interpretation (And How We've Been Using Them All Along)" (2003) 23 *Oxford Journal of Legal Studies* 173, 176.

123 Goddard, "The Myth of Subjectivity" (1987) 7 *Legal Studies* 263; Smith, *Contract Theory* (2004) 271, 273.

124 Langille and Ripstein, "Strictly Speaking – It Went Without Saying" (1996) 2 *Legal Theory* 63, 77, also 70.

125 Kramer, "Common Sense Principles of Contract Interpretation (And How We've Been Using Them All Along)" (2003) 23 *Oxford Journal of Legal Studies* 173, 175.

126 Cf *Bank of Credit and Commerce International SA v Ali* [2001] UKHL 8; [2002] 1 AC 251, [62].

Making use of the surrounding circumstances

[13.65] At least in cases of ambiguity,[127] courts have been prepared to acknowledge the importance of construing a contract in the light of "surrounding circumstances". In understanding this phrase, reference is usually made to the statement of Lord Wilberforce in *Reardon Smith Line v Hansen-Tangen* that:

> In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.[128]

The circumstances surrounding the transaction are relevant to the process of construction because the meaning of language is best understood when considered in the context in which it is used.[129] Indeed, it is said that language "can never be understood divorced from its context" and "words can only be understood in relation to the circumstances in which they are used".[130] Very often the context or surrounding circumstances will support the ordinary grammatical meaning of the words used. But this will not always be the case.[131] In *Investors Compensation Scheme Ltd v West Bromwich Building Society*, Lord Hoffmann explained that:

> The meaning which a document (or any other utterance) would convey to a reasonable man is not the same thing as the meaning of its words. The meaning of words is a matter of dictionaries and grammars; the meaning of the document is what the parties using those words against the relevant background would reasonably have been understood to mean. The background may not merely enable the reasonable man to choose between the possible meanings of words which are ambiguous but even (as occasionally happens in ordinary life) to conclude that the parties must, for whatever reason, have used the wrong words or syntax.

There are limits to the extent to which the surrounding circumstances can be used as a legitimate aid in construing a contract.[132] The surrounding circumstances cannot be used to "depart from the ordinary meaning of the words used by the parties merely because [the court] regards the result as inconvenient or unjust".[133] Typically, the surrounding circumstances will be useful in supporting the interpretation produced by the words of the text or in helping the courts distinguish between two plausible competing meanings.

Royal Botanic Gardens and Domain Trust v South Sydney City Council[134] concerned a lease for a term of 50 years, for an area containing a parking station and footway, between

127 See [13.20].

128 *Reardon Smith Line Ltd v Hansen-Tangen* [1976] 1 WLR 989, 995–6.

129 *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1997] UKHL 28; [1998] 1 WLR 896, 913. See also *Bank of Credit and Commerce International SA v Ali* [2001] UKHL 8; [2002] 1 AC 251; *Chartbrook Ltd v Persimmon Homes Ltd* [2009] UKHL 38; [2009] AC 1101. Also Lord Steyn, "The Intractable Problem of the Interpretation of Legal Texts" (2003) 25 *Sydney Law Review* 25. On the interaction between context and literal meaning, see Mitchell, "Contracts and Contract Law: Challenging the Distinction between the Real and Paper Deal" (2009) 29 *Oxford Journal of Legal Studies* 675.

130 Steyn, "The Intractable Problem of the Interpretation of Legal Texts" (2003) 25 *Sydney Law Review* 5, 6.

131 *Mainteck Services Pty Ltd v Stein Heurtey SA* [2014] NSWCA 184; (2014) 89 NSWLR 633, [74].

132 *Newey v Westpac Banking Corporation* [2014] NSWCA 319, [90].

133 *McGrath v Sturesteps* [2011] NSWCA 315; (2011) 81 NSWLR 690, [17]–[18]; *Newey v Westpac Banking Corporation* [2014] NSWCA 319, [90]; *Arnold v Britton* [2015] UKSC 36; [2015] AC 1619, [17], [18]. See also *Mount Bruce Mining Pty Limited v Wright Prospecting Pty Ltd* [2015] HCA 37; (2015) 256 CLR 104, [48].

134 *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45.

the Trustees of the Domain (the lessor) and the Council of the City of Sydney (the lessee). The contract provided for the rental to be varied by the lessor at regular intervals. Clause 4(b) provided that in determining the new rental payable:

> [The lessor] may have regard to additional costs and expenses which they may incur in regard to the surface of the Domain above or in the vicinity of the parking station and the footway and which arise out of the construction operation and maintenance of the parking station by the Lessee.

The property proved commercially very valuable and the lessor sought to increase the rent by a significant amount to reflect this value. The lessee argued that in determining the amount of yearly rent, the lessor was only to have regard to considerations mentioned in the clause (ie, the costs and expenses to the lessor associated with the parking station and footway) and not to any other considerations, such as the commercial value of the land.

Under a strict approach to interpretation, the view might have been taken that "may" is a permissive word which indicates some of the factors that the lessor might consider without precluding other factors thought relevant by the lessor. The view might have been taken that had the parties intended the lessor to be restricted to the considerations specified in the clause, they would have said so, using words such as "may only have regard". Indeed, Kirby J, in dissent, held that there was no ambiguity in cl 4(b). His Honour considered that the "clause identifies some factors to which regard may be had in making the rental determination. But it does not state that these are the only factors to which regard may be had".[135]

By contrast, Glesson CJ, Gaudron, HcHugh, Gummow and Hayne JJ in a joint judgment considered that the lease was ambiguous because it did not make clear whether the specified considerations were the only considerations that could be taken into account.[136] It seems then that the existence of a viable alternative argument as to what the clause might mean was sufficient to constitute ambiguity.

Given that the clause was ambiguous, the majority judges referred to the circumstances of the transaction, including the fact that:

> The parties to the transaction were two public authorities, in one of which there had been vested land long dedicated for public recreation; the purpose of their transaction was the provision of a further public facility, in the form of the parking station and the footway, but without disturbing the availability of the surface for continued public recreation and without providing for the obtaining by one public authority of commercial profit at the expense of the other; it was the lessee which was responsible for the substantial cost of construction of the new facility and the concern of the parties had been to protect the lessor from financial disadvantage suffered from the transaction, namely additional expense which the lessor would or might incur immediately or in the future.[137]

Many of these matters were also reflected in the contract, in particular the fact that the lessee was responsible for the costs of operating and maintaining the car park. However, Glesson CJ, Gaudron, HcHugh, Gummow and Hayne JJ held that the surrounding circumstances reinforced the non-commercial character of the transaction. Their Honours held that cl 4(b),

135 *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45, [82].

136 *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45, [7]–[8]. Callinan J took a similar view.

137 *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45, [30].

read as a whole, contained a statement of the "totality of the matters to be taken into account in fixing the successive rent determinations".[138]

Contractual purposes

[13.67] Authoritative summaries of the factors that must be taken into account in ascertaining the meaning of a contractual provision now routinely include the purposes of the clause in question and the contract as a whole.[139] In most cases, those purposes will be gleaned from the terms of the contract,[140] but extrinsic evidence can be used to identify contractual purposes where the provision in question is ambiguous.[141] One of the leading statements of the factual background which it is legitimate to consider in construing a contractual provision specifically mentions "evidence of the 'genesis' and objectively the 'aim' of the transaction".[142] In *Royal Botanic Gardens and Domain Trust v South Sydney City Council*,[143] as noted above, consideration of the "antecedent materials and circumstances respecting the dealings between the parties" showed that the primary purpose of the transaction was to provide a public facility on a non-commercial basis without causing the lessor any financial disadvantage, and this was an important factor influencing the interpretation of the clause.[144]

A purposive approach to the construction of an ambiguous provision was also adopted by a majority of the High Court in *Ecosse Property Holdings Pty Ltd v Gee Dee Nominees Pty Ltd*.[145] In that case, it was unclear whether a clause of a lease required the tenant to pay all taxes and outgoings levied in respect of the demised land, or only those levied on the tenant itself. The clause was construed by reference to the "commercial purpose" of the lease, which was "to recreate, as far as possible, in a lease, the conditions which would have existed following a sale".[146] In light of that object it was clear that the clause imposed on the tenant an obligation to assume all of the liabilities of an owner and to pay all outgoings levied in respect of the land.[147]

In each of the cases discussed above, a textual ambiguity was resolved by reference to the main purpose of a contract. Where a contractual provision is unambiguous on its face, but would

138 *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45, [36]. Compare also *Pacific Carriers Ltd v BNP Paribas* [2004] HCA 35; (2004) 218 CLR 451, where there was nothing in the surrounding circumstances which would support a different conclusion from that based on the text of the contractual document.

139 *Ecosse Property Holdings Pty Ltd v Gee Dee Nominees Pty Ltd* [2017] HCA 12; (2017) 261 CLR 544; *Arnold v Britton* [2015] UKSC 36; [2015] AC 1619, [15].

140 *Onesteel Manufacturing Pty Ltd v Bluescope Steele (AIS) Pty Ltd* [2013] NSWCA 27; (2013) 85 NSWLR 1, [13].

141 See, eg, *Ecosse Property Holdings Pty Ltd v Gee Dee Nominees Pty Ltd* [2017] HCA 12; (2017) 261 CLR 544; *Cherry v Steele-Park* [2017] NSWCA 295; (2017) 96 NSWLR 548.

142 *Prenn v Simmonds* [1971] 1 WLR 1381, 1385, quoted in *Codelfa Construction Pty Ltd v State Railway Authority of NSW* (1982) 149 CLR 337, 351, To similar effect is [50] (*Mount Bruce Mining Pty Limited v Wright Prospecting Pty Ltd* [2015] HCA 37; (2015) 256 CLR 104): "What may be referred to are events, circumstances and things external to the contract which are known to the parties *or which assist in identifying the purpose or object of the transaction*, which may include its history, background and context and the market in which the parties were operating." (emphasis added)

143 *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45,

144 *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45, [30].

145 *Ecosse Property Holdings Pty Ltd v Gee Dee Nominees Pty Ltd* [2017] HCA 12; (2017) 261 CLR 544.

146 *Ecosse Property Holdings Pty Ltd v Gee Dee Nominees Pty Ltd* [2017] HCA 12; (2017) 261 CLR 544, [17]–[19].

147 *Ecosse Property Holdings Pty Ltd v Gee Dee Nominees Pty Ltd* [2017] HCA 12; (2017) 261 CLR 544, [27].

defeat the main purpose of the contract if given its literal meaning, this raises a constructional choice between protecting the purpose and giving effect to the plain meaning of the provision.[148] How that choice is resolved may depend on factors such as whether the document was carefully drafted with professional assistance or was informal and loosely written.[149] The more careful the drafting, the more closely the courts attend to the contractual language.[150] Conversely, the poorer and more imprecise the drafting, the greater the weight given to ensuring a "sensible and businesslike outcome" and giving effect to contractual purposes.[151]

A reasonable commercial construction

[13.70] In construing an ambiguous contract, courts will favour an interpretation that avoids unreasonable or uncommercial consequences. In *Australian Broadcasting Commission v Australasian Performing Right Association Ltd*, Gibbs CJ explained:

> if the language is open to two constructions, that will be preferred which will avoid consequences which appear to be capricious, unreasonable, inconvenient or unjust, even though the construction adopted is not the most obvious, or the most grammatically accurate.[152]

Similarly, a court is entitled to approach the process of interpretation on the assumption "that the parties ... intended to produce a commercial result".[153] In *Investors Compensation Scheme Ltd v West Bromwich Building Society*, Lord Hoffmann explained that:

> [t]he "rule" that words should be given their "natural and ordinary meaning" reflects the common sense proposition that we do not easily accept that people have made linguistic mistakes, particularly in formal documents. On the other hand, if one would nevertheless conclude from the background that something must have gone wrong with the language, the law does not require judges to attribute to the parties an intention which they plainly could not have had. Lord Diplock made this point more vigorously when he said in *The Antaios Compania Neviera SA v Salen Rederierna AB* [1985] 1 AC 191, 201:
>
> > … if detailed semantic and syntactical analysis of words in a commercial contract is going to lead to a conclusion that flouts business commonsense, it must be made to yield to business commonsense.[154]

148 See, eg, *Glynn v Margetson & Co* [1893] AC 351 and the discussion in Robertson, "Purposive Contractual Interpretation" (2019) 39 *Legal Studies* 230, 237–41.

149 Robertson, "Purposive Contractual Interpretation" (2019) 39 *Legal Studies* 230, 237–41.

150 See eg *Rainy Sky SA v Kookmin Bank* [2011] UKSC 50; [2011] 1 WLR 2900, [26]; *HP Mercantile Pty Ltd v Hartnett* [2016] NSWCA 342, [141]–[147].

151 *Rainy Sky SA v Kookmin Bank* [2011] UKSC 50; [2011] 1 WLR 2900, [26] (quoting *Mitsui Construction Co v Attorney-General of Hong Kong* (1986) 33 BLR 1, 14); *Thorney Park Golf Club Ltd v Myers Catering Ltd* [2015] EWCA Civ 19, [24].

152 *Australian Broadcasting Commission v Australasian Performing Right Association Ltd* (1973) 129 CLR 99, 108, quoting from *Locke v Dunlop* (1888) 39 Ch D 387, 393. Also *Westpac Banking Corporation v Tanzone Pty Ltd* [2000] NSWCA 25.

153 *Electricity Generation Corporation v Woodside Energy Ltd* [2014] HCA 7; (2014) 251 CLR 640, [35]. Also *Maggbury Pty Ltd v Hafele Australia Pty Ltd* [2001] HCA 70; (2001) 210 CLR 181, [43]; *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603, [19]–[23]; *Steggles Ltd v Yarrabee Chicken Company Pty Ltd* [2012] FCAFC 91, [59]; *Mount Bruce Mining Pty Limited v Wright Prospecting Pty Ltd* [2015] HCA 37; (2015) 256 CLR 104, [51].

154 *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1997] UKHL 28; [1998] 1 WLR 896, 913. See also *Mannai Investments Co Pty Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749; *Bank of Credit and Commerce International SA v Ali* [2001] UKHL 8; [2002] 1 AC 251; *Chartbrook Ltd v Persimmon Homes Ltd* [2009] UKHL 38; [2009] AC 1101; *Rainy Sky SA v Kookmin Bank* [2011] UKSC 50; [2011] 1 WLR 290.

There are, however, clear limits to this principle. The need to promote a commercial approach is not an invitation for a court to rewrite the contract to ensure that it makes more commercial sense.[155] If contractual terms are clearly expressed, courts have consistently reiterated that effect should be given to those terms even though this may produce an unreasonable result or lack commercial sense.[156] In *Australian Broadcasting Commission v Australasian Performing Right Association Ltd*, Gibbs J explained that:

> If the words used are unambiguous the court must give effect to them, notwithstanding that the result may appear capricious or unreasonable, and notwithstanding that it may be guessed or suspected that the parties intended something different. The court has no power to remake or amend a contract for the purpose of avoiding a result which is considered to be inconvenient or unjust.[157]

In *Quirke v FCL Interstate Transport Services Pty Ltd*,[158] FCL transported fruit for a company. FCL required a guarantee from a director of the company for payment for its services. The guarantee referred only to goods sold by FCL when in fact FCL only provided services. The Full Court of the Supreme Court of South Australia held that effect must be given to the plain meaning of the words used in the contract and that accordingly the guarantee did not apply to payments for the services provided by FCL.[159]

Absurdity

[13.72] A different approach is adopted where the clear words of a contract would result in an "absurd", as opposed to a merely "unreasonable" or "uncommercial" result. In *Maggbury Pty Ltd v Hafele Australia Pty Ltd*, Gleeson CJ, Gummow and Hayne JJ said the appropriate question to be addressed was whether "something must have gone wrong with the language",[160] an expression used by Lord Hoffmann in *Investors Compensation Scheme Ltd v West Bromwich Building Society*.[161] This statement has been interpreted as prompting "an inquiry into whether the relevant provision would have an absurd operation if construed in accordance with the literal meaning of the words used".[162] Under this approach, if the clear or literal meaning of the relevant provision would lead to an absurd or nonsensical result, courts may supply, correct or omit words in order to avoid that absurdity.[163] Given the authority in Australia that courts should give effect to clearly expressed but unreasonable terms, it is necessary to distinguish between terms that produce an absurd result, and those that produce a result that is merely unreasonable.

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155 *Aysun Pty Ltd v Cregan* [2011] NSWCA 203, [28]; *Miwa Pty Ltd v Siantan Properties Pty Ltd* [2011] NSWCA 297, [18]; *Schwartz v Hadid* [2013] NSWCA 89, [86]; *Arnold v Britton* [2015] UKSC 36; [2015] AC 1619, [15].

156 See, eg, *Arnold v Britton* [2015] UKSC 36; [2015] AC 1619.

157 *Australian Broadcasting Commission v Australasian Performing Right Association Ltd* (1973) 129 CLR 99, 108, quoting from *Locke v Dunlop* (1888) 39 Ch D 387, 393; also *Steggles Ltd v Yarrabee Chicken Company Pty Ltd* [2012] FCAFC 91, [58]; *Arnold v Britton* [2015] UKSC 36; [2015] AC 1619, [19]–[20].

158 *Quirke v FCL Interstate Transport Services Pty Ltd* [2005] SASC 226; (2005) 92 SASR 249.

159 See also *Jireh International Pty Ltd v Western Exports Services Inc* [2011] NSWCA 137.

160 *Maggbury Pty Ltd v Hafele Australia Pty Ltd* [2001] HCA 70; (2002) 210 CLR 181, [43].

161 *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1997] UKHL 28; [1998] 1 WLR 896, 913.

162 *Westpac Banking Corporation v Tanzone Pty Ltd* [2000] NSWCA 25, [19]–[23]; See also *Electricity Generation Corporation v Woodside Energy Ltd* [2014] HCA 7; (2014) 251 CLR 640, [35].

163 *Jireh International Pty Ltd v Western Exports Services Inc* [2011] NSWCA 137, [63]–[64]; *Current Images Pty Ltd v Dupack Pty Limited* [2012] NSWCA 99, [47]; *Newey v Westpac Banking Corporation* [2014] NSWCA 319, [91]; *Bank of Queensland Ltd v Chartis Australia Insurance Ltd* [2013] QCA 183, [36].

In *Fitzgerald v Masters*,[164] contracting parties executed a document which set out some agreed terms and then purported to incorporate the usual conditions of sale approved by the Real Estate Institute of New South Wales "so far as they are inconsistent herewith". Dixon CJ and Fullagar J said:

> Words may generally be supplied, omitted or corrected, in an instrument, where it is clearly necessary in order to avoid absurdity or inconsistency. Here it would be indeed absurd to suppose that the parties, having expressed their agreement on a number of special and essential matters, should intend to incorporate by reference terms inconsistent with what they had specially agreed upon. What they must clearly have intended is to incorporate a set of general conditions except so far as they were inconsistent with what they had specially agreed upon, and cl. 8 must be read as if it said "consistent" or "not inconsistent".[165]

In *Westpac Banking Corporation v Tanzone Pty Ltd*,[166] a clearly worded rent review clause in a 20-year lease had the effect that every two years the rent was increased by reference to the rise in the consumer price index since the beginning of the lease. That had a multiplier effect which had "absurd possible consequences" when considered from the point of view of the parties at the time of formation, and which had no rational explanation.[167] The Court accepted that the effect of a literal reading of the clause went beyond unreasonableness and "fell into the absurdity category". It must have been the result of a mistake.[168] The Court therefore held that the clause should be read with additions to the words used in the formula, so that for all rent reviews after the first, references to the last quarter preceding the date of commencement of the lease were read as references to for the last quarter preceding the immediately preceding review date.[169]

CONSTRUING EXCLUSION CLAUSES

[13.75] *Exclusion clauses*, also referred to as *exemption* or *exception clauses*, aim to reduce or exclude a party's liability for conduct that would otherwise be in breach of contract or constitute a tort, such as negligence.[170] At least in commercial contracts between businesses of equal size and experience, upholding exclusion clauses might be justified as consistent with the principle of freedom of contract. As Collins explains: "This freedom to allocate risks [can] reduce costs by permitting the parties to place risk on the party who [can] avoid or cover the loss at the least cost."[171] Exclusion clauses in many cases simply give effect to the insurance arrangements agreed between the parties. If, for example, A and B agree that A will transport B's goods and B will arrange insurance for the goods, an exclusion clause may be needed to ensure that the risk is not passed back to A.[172]

164 *Fitzgerald v Masters* (1956) 95 CLR 420, discussed in the context of mistake at [31.45].

165 *Fitzgerald v Masters* (1956) 95 CLR 420, 426–7.

166 *Westpac Banking Corporation v Tanzone Pty Ltd* [2000] NSWCA 25.

167 *Westpac Banking Corporation v Tanzone Pty Ltd* [2000] NSWCA 25, [27]–[29].

168 *Westpac Banking Corporation v Tanzone Pty Ltd* [2000] NSWCA 25, [37].

169 *Westpac Banking Corporation v Tanzone Pty Ltd* [2000] NSWCA 25, [36].

170 On exclusion clauses, see generally Coote, *Exception Clauses* (1964).

171 Collins, *Regulating Contracts* (1999), 47.

172 See, eg, *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165, [24], [64] and the submissions of SJ Gageler SC, 167.

There may be more cause for concern about the use of exclusion clauses in standard form contracts involving a substantial degree of inequality of bargaining power between the parties to the transaction, such as is usually the case in contracts involving consumers or large and small businesses. In this context, Collins explains that the effect of the principle of "freedom of contract" was that:

> businesses took advantage of small print in standard form contracts in order to place the risk of loss upon the consumer, without the consumer usually being aware of this allocation and without a commensurate price reduction.[173]

Legislative restrictions on exclusion clauses

[13.80] Legislation has now been passed to address some of the concerns about the misuse of exclusion clauses in consumer contracts.[174] Exclusion clauses in contracts for the supply of goods and services by traders to consumers are now subject to regulation under the *Australian Consumer Law*, as discussed in Chapters 16 and 17.

The common law approach to exclusion clauses

[13.85] Where not regulated by legislation, three questions need to be asked in determining whether an exclusion clause applies to reduce or exclude a party's liability under a contract.

1. First, it must be considered whether or not the exclusion clause was properly incorporated into the contract an issue discussed in Chapter 12.
2. Secondly, it must be considered whether the person seeking to rely on the protection of the clause was a party to the contract, an issue discussed in Chapter 11.
3. Thirdly, it must be determined whether, as a matter of construction, the clause applies to exclude or reduce the liability in dispute.

Does the clause apply, exclude or reduce the liability in dispute?

Ordinary principles of construction

[13.90] The High Court has stressed that the meaning and effect of an exclusion clause is to be determined by the ordinary processes of construction of a contract.[175] Thus, in *Darlington Futures Ltd v Delco Aust Pty Ltd* (*Darlington*),[176] and again in *Nissho Iwai Australia Ltd v Malaysian International Shipping Corp, Berhad*,[177] the High Court stated that an exclusion clause is to be construed:

> according to its natural and ordinary meaning, read in the light of the contract as a whole, thereby giving due weight to the context in which the clause appears including the nature and object of the contract …[178]

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173 Collins, *Regulating Contracts* (1999), 47.

174 See further Chapter 17.

175 *Insight Vacations Pty Ltd v Young* [2011] HCA 16; (2011) 243 CLR 149.

176 *Darlington Futures Ltd v Delco Aust Pty Ltd* (1986) 161 CLR 500.

177 *Nissho Iwai Australia Ltd v Malaysian International Shipping Corp, Berhad* (1989) 167 CLR 219.

178 *Darlington Futures Ltd v Delco Australia Pty Ltd* (1986) 161 CLR 500, 510, approved in *Nissho Iwai Australia Ltd v Malaysian International Shipping Corp, Berhad* (1989) 167 CLR 219, 227.

Darlington involved a contract between a futures broker and its client. The broker engaged in trading on the futures market in a way that was not authorised by the client and, as a result, the client incurred substantial losses. The broker sought to limit its liability by relying on two exclusion clauses contained in the contract. Clause 6 of the contract excluded the broker from liability for "loss arising in any way out of any trading activity undertaken on behalf of the [c]lient whether pursuant to this agreement or not …". The High Court considered that this clause did not protect the broker because the words of the clause plainly referred to activity undertaken by the broker with the client's authority. It could not be supposed that the parties intended to exclude the broker from liability for losses from trading activity that the broker had no authority to undertake.

Clause 7(c) of the contract limited the broker's liability to $100 in respect of "any claim arising out of or in connection with the relationship established by this agreement". The lower Court had held that the clause had no application to claims arising from conduct that was outside the scope of the agreement. The High Court considered that this was an overly restrictive interpretation and held that the clause did limit the broker's liability in the case in question.[179] The clause was expressed as covering claims arising out of or *in connection* with the contract. The High Court stated that: "A claim in respect of an unauthorised transaction may nonetheless have a connection, indeed a substantial connection, with the relationship of broker and client established by the agreement."[180]

Contra proferentem

[13.93] It is a very old rule of contractual interpretation that an ambiguity should be resolved against the *proferens*, meaning the person who proffered or put forward the provision in question for inclusion in the contract.[181] In practice, the person seeking to rely on a clause is often treated as the proferens for the purpose of this rule. Except in the special case of contracts of guarantee, the *Contra proferentem* principle is treated as a rule "of last resort", which means that it will be applied "only when ambiguity remains after all other avenues of construction have been exhausted".[182]

The High Court has affirmed that an exclusion clause may be construed *Contra proferentem* where it is ambiguous.[183] This means that where on ordinary principles of construction the words of the clause are capable of more than one meaning, an exclusion clause may be construed strictly against the interest of the party seeking to rely on the clause. The High Court has indicated that this approach is also appropriate in relation to guarantees and indemnities.[184] Thus, ambiguity in an indemnity should be construed in favour of the person

179 *Darlington Futures Ltd v Delco Australia Pty Ltd* (1986) 161 CLR 500, 511.

180 *Darlington Futures Ltd v Delco Australia Pty Ltd* (1986) 161 CLR 500, 511.

181 See McCunn, "The *Contra proferentem* Rule: Contract Law's Great Survivor" (2019) 39 *Oxford Journal of Legal Studies* 483.

182 *Zhang v ROC Services (NSW) Pty Ltd* [2016] NSWCA 370; (2016) 93 NSWLR 561, [140], quoting *Beefeater Sales International Pty Ltd v MIS Funding No 1 Pty Ltd* [2016] NSWCA 217, [66]. See also *Bank of Queensland Ltd v Chartis Australia Insurance Ltd* [2013] QCA 183, [38].

183 *Darlington Futures Ltd v Delco Australia Pty Ltd* (1986) 161 CLR 500, 510. See also *Andar Transport Limited v Brambles Limited* [2004] HCA 28; (2004) 217 CLR 424, [17]–[18].

184 *Ankar Pty Limited v National Westminster Finance (Australia) Limited* (1987) 162 CLR 549, 561; *Andar Transport Limited v Brambles Limited* [2004] HCA 28; (2004) 217 CLR 424, [17]–[18]; discussed in *Gardiner v Agricultural and Rural Finance Pty Ltd* [2007] NSWCA 235, [14]–[21].

providing the indemnity and, similarly, ambiguity in a guarantee should be construed in favour of the guarantor.

The application of the *Contra proferentem* principle is illustrated by *Wallis Son & Wells v Pratt & Haynes*.[185] That case involved a contract for the sale of seed specified as "common English sainfoin". The sellers delivered a different type of seed – "giant sainfoin" – which was inferior to the seed specified under the contract. The buyers alleged a breach of the condition implied under the *Sale of Goods Act 1893* (UK), which provided that goods shall correspond with their description. The sellers sought to rely on an exclusion clause in the contract, which provided that the sellers "give no warranty expressed or implied as to growth, description or any other matters". The word "warranty" may be used to mean any term in a contract or it may be used in a strict legal sense to mean terms that are not conditions under a contract.[186] The House of Lords construed the clause strictly to refer to a warranty in the legal sense. Thus, the House of Lords considered that the clause did not exclude liability for breaches of terms that were classified as conditions, such as the one in question.[187]

Other principles of strict construction

[13.95] Courts have, at times, relied on a number of principles of strict construction which reduced considerably the scope of broadly expressed exclusion clauses. In particular, English courts responded to concerns about the use of broad reaching exclusion clauses by requiring any excluded events to be expressed exceedingly clearly, and by invoking a variety of devices to limit the scope of exclusion clauses. English courts accordingly developed rules that precluded a party from relying on an exclusion clause to protect him or herself from a "fundamental breach" of the contract or a breach of a "fundamental term".[188] In some cases, these rules were applied as rules of law, rather than rules of construction; that is, it was held that an exclusion clause could never apply to fundamental breach or to breach of a fundamental term. The application of such principles has now been rejected in England by the House of Lords,[189] which has taken the view that legislation regulating exclusion clauses has reduced the need for judicial intervention under common law principles. In *Photo Production Ltd v Securicor Transport Ltd*, Lord Wilberforce stated that:

> In commercial matters generally, when the parties are not of unequal bargaining power, and where the risks are normally borne by insurance, not only is the case for judicial intervention undemonstrated, but there is everything to be said, and this seems to have been Parliament's intention, for leaving the parties free to apportion the risks as they think fit and for respecting their decisions.[190]

185 *Wallis Son & Wells v Pratt & Haynes* [1911] AC 394.

186 For the distinction between warranties and conditions, see Chapter 21.

187 *Wallis Son & Wells v Pratt & Haynes* [1911] AC 394, esp 395, 398. See also *McRae v Commonwealth Disposals Commission* (1951) 84 CLR 377, 398; *Nissho Iwai Australia Ltd v Malaysian International Shipping Corp, Berhad* (1989) 167 CLR 219.

188 See further Greig and Davis, *The Law of Contract* (1987), 636–66.

189 *Suisse Atlantique Societe d'Armement Maritime SA v NV Rotterdamschhe Kolen Centrale* [1967] 1 AC 361, 392, 399, 405, 410, 425, 431–2; *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827, 845, 850–1, 853; *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd* [1983] 2 AC 803, 813.

190 *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827, 843, see also 851.

These rules were never authoritatively accepted as part of the law in Australia.[191] The High Court has stressed that exclusion clauses should be analysed according to ordinary principles of construction.[192]

Given the emphasis by the High Court in cases such as *Darlington Futures Ltd v Delco Aust Pty Ltd*[193] and *Nissho Iwai Australia Ltd v Malaysian International Shipping Corp, Berhad*[194] on applying the ordinary process of construction to exclusion clauses, these principles must now largely be seen as of historical interest, or perhaps as applications of the *Contra proferentem* rule.[195] Where the meaning of the words of an exclusion or limitation clause can be ascertained through the ordinary processes of construction, there should be no scope for a restrictive interpretation.[196] After all, as noted above, the *Contra proferentem* rule is a "rule of last result", applied only where other ordinary processes of construction fail.

Four corners rule

[13.100] Historically, courts were unwilling to construe an exclusion clause as excluding liability for acts that were not authorised by,[197] or outside of, the main object or "four corners" of the contract.[198] In *Nissho Iwai Australia Ltd v Malaysian International Shipping Corp, Berhad*, the High Court stated that a clearly worded exclusion clause may apply to exclude liability, even for events occurring in circumstances that would defeat the main object of the contract.[199]

Negligence

[13.110] Courts traditionally took the view that it was "inherently improbable that one party to a contract should intend to absolve the other party from the consequences of his own negligence".[200] Thus, traditionally, courts have stated that "clear words are necessary to exclude liability for negligence".[201] However, the decision of the High Court in *Darlington Futures Ltd v Delco Australia Pty Ltd*[202] requires that the scope of any exclusion clause will be determined by construing the clause according to its natural and ordinary meaning.[203] Thus, a clause expressed in general but expansive language – for example, excluding liability for losses "howsoever caused" or stating that "under no circumstances" will the party in question be

191 *Darlington Futures Ltd v Delco Australia Pty Ltd* (1986) 161 CLR 500, 510, approved in *Nissho Iwai Australia Ltd v Malaysian International Shipping Corp, Berhad* (1989) 167 CLR 219, 227.

192 *Sydney City Council v West* (1965) 114 CLR 481, 488, 498.

193 *Darlington Futures Ltd v Delco Australia Pty Ltd* (1986) 161 CLR 500, 510.

194 *Nissho Iwai Australia Ltd v Malaysian International Shipping Corp, Berhad* (1989) 167 CLR 219, 227.

195 *Bright v Sampson and Duncan Enterprises Pty Ltd* (1985) 1 NSWLR 346, 366.

196 *Electricity Corporation t/as Verve Energy v Woodside Energy Ltd* [2013] WASCA 36, [38], [42], [138], [140].

197 See, eg, *Council of the City of Sydney v West* (1965) 114 CLR 481.

198 See, eg, *Thomas National Transport (Melbourne) Pty Ltd v May & Baker (Australia) Pty Ltd* (1966) 115 CLR 353, 376.

199 *Nissho Iwai Australia Ltd v Malaysian International Shipping Corp, Berhad* (1989) 167 CLR 219, 227. Cf *Kamil Export (Aust) Pty Ltd v NPL (Australia) Pty Ltd* [1996] 1 VR 538, 552, 558–9.

200 *Gillespie Bros & Co Ltd v Roy Bowles Transport Ltd* [1973] 1 QB 400, 419.

201 See generally Carter, "Commercial Construction and the SS Canada Rules" (1995) 9 *Journal of Contract Law* 69.

202 *Darlington Futures Ltd v Delco Australia Pty Ltd* (1986) 161 CLR 500, 510.

203 See *MWH Australia Pty Ltd v Wynton Stone Australia Pty Ltd* [2010] VSCA 245; (2010) 31 VR 575. Also *Davis v Pearce Parking Station Pty Ltd* (1954) 91 CLR 642, 652.

liable – may be sufficient to exclude negligence.[204] If negligence is the only basis on which a plaintiff may be liable, general words are also likely to be sufficient to exclude liability for such negligence.[205] Of course, the most effective way for parties to exclude liability for negligence is to include in their contract a specific reference to negligence as an excluded head of liability.

Deliberate breach

[13.115] Courts have tended to require clear words before an exclusion clause will be construed as excluding liability for a deliberate breach of contract.[206] Again, a clearly worded clause may have this effect.[207]

204 See, eg, *Commissioner for Railways (NSW) v Quinn* (1946) 72 CLR 345, 371–2; *Gillespie Bros & Co Ltd v Roy Bowles Transport Ltd* [1973] QB 400, esp 420–1.

205 See *Canada Steamship Lines Ltd v R* [1952] AC 192; *Bright v Sampson and Duncan Enterprises Pty Ltd* (1985) 1 NSWLR 346, 367; *Davis v Pearce Parking Station Pty Ltd* (1954) 91 CLR 642, 651.

206 *Davis v Pearce Parking Station Pty Ltd* (1954) 91 CLR 642, 652; *Council of the City of Sydney v West* (1965) 114 CLR 481, 488, 493, 497, 502; *Thomas National Transport (Melbourne) Pty Ltd v May & Baker (Australia) Pty Ltd* (1966) 115 CLR 353, 385; *Kamil Export (Aust) Pty Ltd v NPL (Australia) Pty Ltd* [1996] 1 VR 538, 533. See also Coote, "Exception Clauses, Deliberate Acts and the Onus of Proof in Bailment Cases" (1997) 12 *Journal of Contract Law* 169.

207 *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827, 846.

GAP FILLING

PART VI

Gap-filling terms

[PtVI.05] In some cases, the express terms of a contract will fail to provide, or to provide adequately, for the consequences of certain events affecting performance of the contract. For example, in a contract for the lease of a flat in a large apartment block, the contract may fail to specify whether it is the landlord or the tenants who should be responsible for replacing light bulbs in the stairwell.[1] There are two possible responses to these sorts of cases. The court might consider that the express terms of the contract should prevail and the risk should lie where it falls. In the case of the apartment block, this approach would mean that neither party was responsible for replacing the light bulbs, with the consequence that the tenants would themselves have to take charge or live with the issue. The other response to events not provided for in a contract is to accept that there is a gap in the express terms of the contract which may be filled with a term or a legal rule that provides a different allocation of risk than would otherwise have been the case. For example, in the case of an apartment block, the court might decide that the landlord is best placed to be responsible for lighting in the stairwell and hence imply an obligation that he or she must take reasonable care of the area.

Terms and doctrines provided by a court to fill a gap in a contract can be described as *gap-filling* terms, or *gap fillers*.[2] The main examples of gap fillers are implied terms. Chapter 14 discusses the rules determining when a term may be implied in a contract and also a prominent, if controversial, example of a gap-filling term, the implied duty of good faith. The doctrine of frustration, discussed in Chapter 15, might also be seen as a gap-filling rule. This is because the doctrine applies where, as a matter of construction, the parties have failed to provide in their contract for the consequences of a catastrophic event disrupting performance of the contract. However, courts have stated that the doctrine of frustration itself is not based on an implied term premised on the parties' presumed intentions.[3]

The inevitability of gaps and the role of gap-filling terms

[PtVI.10] Gaps in the express terms of all but the simplest of contracts are inevitable.[4] At the time the contract is made, the parties will not be able to foresee all of the possible contingencies which may affect the performance of their contract.

1 See below *Liverpool City Council v Irwin* [1977] AC 239.
2 See [1.50].
3 See in particular, *Davis Contractors Ltd v Farnham UDC* [1956] AC 696, 728.
4 See further Goetz and Scott, "Principles of Relational Contracts" (1981) 67 *Virginia Law Review* 1089; Farnsworth, "Disputes over Omission in Contracts" (1968) 68 *Columbia Law Review* 860.

When making their contract, the parties may have been focusing on performance and thus did not consider the possibility of disruptive events.[5] Moreover, even though the parties may be able to foresee some contingencies, those contingencies may be extremely unlikely to occur. The parties may well consider that the cost of attempting to negotiate terms dealing with such contingencies is likely to exceed the benefits of the negotiations.[6] The rational response may be for parties to accept the risk of a gap in their contract and that courts may fill that gap should the need arise. Indeed, where the courts routinely imply certain terms into contracts of a particular class, parties may decide to rely on those terms, rather than attempt to draft a response to the relevant issue. Standardised terms or rules that are provided by the law in the absence of contrary intention are more accurately described as *default rules* rather than gap fillers. Rather than filling gaps in particular agreements, they operate generally in default of any stipulation by the parties.[7] Many terms implied by law might be described as default rules, as may the doctrine of frustration.

5 Macaulay, "Non-contractual Relations in Business: A Preliminary Study" (1963) 28 *American Sociological Review* 55, 60.

6 Posner, *Economic Analysis of Law* (9th ed, 2014) §4.1.

7 See *Equitable Life Assurance Society v Hyman* [2002] 1 AC 408, 458–9, discussed at [14.65]; see also [1.45].

CHAPTER **14**

Implied terms

WHEN WILL TERMS BE IMPLIED?

[14.05] The common law recognises three main classes of implied term. First, terms are implied in particular contracts to make them workable or give them "business efficacy". Secondly, terms are implied as legal incidents of all contracts falling within a particular class, such as employment contracts, leases, and sale of goods contracts. Thirdly, and less commonly, terms are implied by custom or trade usage. As we shall see, these classes of implied term have different bases for implication, although in practice, there may be considerable overlap between them.[1] Terms implied to give business efficacy are commonly described as terms implied "in fact" and terms implied in particular classes of contract described as implied "in law". A duty to cooperate is recognised as being implied in all contracts as a matter of law. The duty to cooperate is increasingly being seen as an aspect of a broader duty to act in good faith. Whether and when a duty to act in good faith is implied, and what it requires of

1 *Parramatta Design & Developments Pty Ltd v Concrete Pty Ltd* [2005] FCAFC 138; (2005) 144 FCR 264, [16] (point not addressed in *Concrete Pty Ltd v Paramatta Design & Development* [2006] HCA 55; (2006) 229 CLR 577).

contracting parties, have been controversial and much-discussed questions in recent years and will be explored in detail in this chapter.

Some statutes also imply terms in particular types of contract. For example, the Sale of Goods Acts imply various conditions and warranties in contracts for the sale of goods, including undertakings by the seller that the goods will correspond with their description, will be of merchantable quality and will be fit for their purpose.[2] In addition, the *Australian Consumer Law* provides a range of similar minimum quality standards or "consumer guarantees" that apply to consumer transactions as statutory rights and are independent of the parties' contract.[3]

Excluding implied terms

[14.10] Terms will not be implied in law, in fact or by custom where they are expressly excluded by the parties or are inconsistent with the express terms of the contract.[4] An implied term will not necessarily be excluded by an *entire contract clause*, a clause stating that the written contract represents the whole of the parties' agreement.[5] In *Hart v MacDonald*,[6] Isaacs J stated:

> [An entire agreement clause] excludes what is extraneous to the written contract: but it does not in terms exclude implications arising on a fair construction of the agreement itself, and in the absence of definite exclusion, an implication is as much a part of a contract as any term couched in express words.[7]

TERMS IMPLIED IN FACT

Nature of terms implied in fact

[14.15] Terms implied to give business efficacy to a particular contract are traditionally said to be based on the *presumed* intentions of the parties concerned.[8] The implication of terms on this basis is closely related to the construction of express terms. Indeed, on one influential view, implication is merely an exercise in the construction of a contractual document.[9] On this view, the implication of terms in fact does not involve any addition to the instrument but just spells out what a reasonable person would understand it to mean.[10] The identification of terms required to give business efficacy to a contract is an exercise in the construction of a

2 See, eg, *Goods Act 1958* (Vic), ss 17–20.
3 See Chapter 17.
4 *Castlemaine Tooheys Ltd v Carlton & United Brewers Ltd* (1987) 10 NSWLR 468, 490–3; *Devefi v Mateffy Perl Nagy Pty Ltd* (1993) 113 ALR 225, 240–1; *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 449.
5 On entire contract clauses, see also [12.105].
6 *Hart v MacDonald* (1910) 10 CLR 417.
7 *Hart v MacDonald* (1910) 10 CLR 417, 427, 430. See also *Johnson Matthey Ltd v A C Rochester Overseas Corp* (1990) 23 NSWLR 190, 196, but cf *Hope v RCA Photophone of Australia Pty Ltd* (1937) 59 CLR 348, 358, 363, 365, 368.
8 For example, *BP Refinery (Westernport) Pty Ltd v Shire of Hastings* (1977) 180 CLR 266, 283; *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 352–3; *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 422, 441.
9 See further the discussion at [14.150]. Lord Neuberger has since emphasized that the exercise should not be confused with the interpretation of express terms: *Marks and Spencer plc v BNP Paribas Securities Services Trust Company (Jersey) Ltd* [2015] UKSC 72; [2016] AC 742, [27]–[28].
10 *Attorney General of Belize v Belize Telecom Ltd* [2009] UKPC 10; [2009] 1 WLR 1988, [19].

contractual document in the sense identified by Francis Lieber, who observed that construing a legal text involves "the drawing of conclusions respecting subjects, that lie beyond the direct expression of the text, from elements known from and given in the text—conclusions which are in the spirit, though not within the letter of the text".[11]

Formal contracts

The BP Refinery formula

[14.20] In *BP Refinery (Westernport) Pty Ltd v Hastings Shire Council* (*BP Refinery*), Lord Simon identified the requirements for implication in fact as follows:

> For a term to be implied, the following conditions (which may overlap) must be satisfied: (1) it must be reasonable and equitable; (2) it must be necessary to give business efficacy to the contract so that no term will be implied if the contract is effective without it; (3) it must be so obvious that "it goes without saying"; (4) it must be capable of clear expression; (5) it must not contradict any express term of the contract.[12]

The *BP Refinery* formula has been approved by the High Court on numerous occasions.[13] It has, however, been criticised. It has been argued that if terms implied in fact are premised on giving effect to the presumed intentions of the parties, the focus of inquiry in implying a term should be those intentions or expectations, not compliance with a set of formal criteria.[14] In *Attorney General of Belize v Belize Telecom Ltd*, Lord Hoffmann, giving the judgment of the Privy Council, suggested that the formula should not distract attention from the fact that the court is involved in a process of construction, which is simply an exercise in determining what a contract means.[15] A leading judgment in the UK Supreme Court has since reaffirmed the *BP Refinery* test, but with some relaxation of its requirements, as will be discussed below.[16]

Reasonable and equitable

[14.25] The first requirement under the *BP Refinery* framework is that the term claimed to be implied must be reasonable and equitable. A term that, although beneficial to one party, imposes a significant detriment or burden on the other party is unlikely to be reasonable

11 Lieber, *Legal and Political Hermeneutics* (1859), p 56. See further Robertson, "The Foundations of Implied Terms: Logic, Efficacy and Purpose" in Degeling, Edelman and Goudkamp (eds), *Contract in Commercial Law* (2016), 143, 148–52.

12 *BP Refinery (Westernport) Pty Ltd v Shire of Hastings* (1977) 180 CLR 266, 283.

13 *Secured Income Real Estate (Australia) Ltd v St Martin's Investments Pty Ltd* (1979) 144 CLR 596, 605–6; *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 347, 404; *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41, 66, 117–8; *Adelaide City Corp v Jennings Industries Ltd* (1985) 156 CLR 274, 274; *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 422, 441.

14 See Davenport, "Implied Terms" (1990) 106 *Law Quarterly Review* 179; Paterson, "Terms Implied in Fact: The Basis for Implication" (1998) 13 *Journal of Contract Law* 103; Peden, *Good Faith in the Performance of Contracts* (2003), Ch 4.

15 *Attorney General of Belize v Belize Telecom Ltd* [2009] UKPC 10; [2009] 1 WLR 1988, [16]–[27] (the *BP Refinery* formula is best regarded, "not as series of independent tests which must each be surmounted, but rather as a collection of different ways in which judges have tried to express the central idea that the proposed implied term must spell out what the contract actually means, or in which they have explained why they did not think that it did so").

16 *Marks and Spencer plc v BNP Paribas Securities Services Trust Company (Jersey) Ltd* [2015] UKSC 72; [2016] AC 742, [21]–[24] (Lord Neuberger, with whom Lord Sumption and Lord Hodge agreed).

and equitable.[17] This is illustrated by the decision in *BP Refinery (Westernport) Pty Ltd v Shire of Hastings* itself.[18] That case concerned an agreement between the Shire of Hastings (the Shire) and BP Refinery (Westernport) Pty Ltd (the Company), a member of a group of oil companies (BP Group), in relation to a site within the Shire on which the BP Group was to construct an oil refinery. Under the agreement, the Company was to have a preferential status with respect to rates charged for the use of the land. The agreement had a duration of 40 years and contained no provision for earlier termination. After approximately five years, the Company yielded occupation of the site to another company in the BP Group, which also sought the benefit of the agreement. The Shire levied the general rate on the new occupier, contending that the rating agreement only operated while the Company was in occupation.

The majority of the Privy Council rejected the Shire's contention.[19] They held that the rating agreement contained an implied term, allowing the right to preferential rates to be assigned to other members of the BP Group. The majority summed up the consequences of precluding the Company from assigning the benefit of the rating agreement as follows:

> Having invested enormous sums in a refinery sited to the advantage of the [Shire] and the State, [the BP Group] would either have to accept being (contrary to the intention of the refinery agreement) locked into an outmoded and inconvenient corporate structure or have to forego the preferential rating which was the incentive held out for the installation and subsequent maintenance and operation of the refinery within the district.[20]

Lord Simon noted that a group of companies like the BP Group may from time to time have good reasons to make changes to its corporate structure during the course of the agreement, "and the identity of the member of the BP group occupying the refinery site cannot have been of the least importance to the respondents."[21] In this context, the majority of the Privy Council considered that the Shire's proposed term precluding assignment was neither reasonable nor equitable.[22]

In *Marks and Spencer plc v BNP Paribas Securities Services Trust Company (Jersey) Ltd*, Lord Neuberger questioned whether the requirement of reasonableness and equitableness adds anything to the other elements of the test.[23] He suggested that "if a term satisfies the other requirements, it is hard to think that it would not be reasonable and equitable."[24]

Business efficacy

[14.30] The core of the *BP Refinery* test is the requirement that the term in question must be necessary to give business efficacy to the contract. This requirement is usually understood as prompting an inquiry into whether the proposed term is necessary to make the contract work

17 See Greig and Davis, *The Law of Contract* (1987), pp 548–50.

18 *BP Refinery (Westernport) Pty Ltd v Shire of Hastings* (1977) 180 CLR 266.

19 Viscount Dilhorne, Lord Simon and Lord Keith. Lord Wilberforce and Lord Morris dissented.

20 *BP Refinery (Westernport) Pty Ltd v Shire of Hastings* (1977) 180 CLR 266, 280.

21 *BP Refinery (Westernport) Pty Ltd v Shire of Hastings* (1977) 180 CLR 266, 280, 284.

22 *BP Refinery (Westernport) Pty Ltd v Shire of Hastings* (1977) 180 CLR 266, 284.

23 *Marks and Spencer plc v BNP Paribas Securities Services Trust Company (Jersey) Ltd* [2015] UKSC 72; [2016] AC 742, [21].

24 *Marks and Spencer plc v BNP Paribas Securities Services Trust Company (Jersey) Ltd* [2015] UKSC 72; [2016] AC 742, [21].

"or to avoid an unworkable situation".[25] As Sulan J explained in *Sekisui Rib Loc Australia Pty Ltd v Rocla Pty Ltd*:[26]

> The necessity to give "business efficacy" contemplates a term needed "in order to make the agreement work, or conversely, in order to avoid an unworkable situation". This is a consideration of what would make the contract workable in a business sense. A term may be commercially necessary notwithstanding that the contract can operate without it.

The *BP Refinery* case (discussed at [14.25] above) provides a good example of necessity of the requisite kind: the rating agreement could operate without the implication allowing assignment, but it would be unworkable in a business sense if the BP Group could not be restructured over the forty-year life of the agreement without losing the benefit of the rating concession.

The seminal case on "business efficacy" is *The Moorcock*.[27] In this case, the parties had entered into a contract for a ship-owner to discharge and load his vessel at a jetty owners' wharf on the river Thames. For that purpose, the vessel was to be moored at the jetty owners' nearby jetty. During low tide, the vessel would rest on the mud at the bottom of the river. The vessel suffered damage as a result of resting on a ridge of hard ground beneath the mud. The English Court of Appeal held that the jetty owners were liable for the damage. The jetty owners were in breach of an implied term requiring them to take reasonable care to ascertain the condition of the berth and "either have it made reasonably fit for the purpose, or inform the persons with whom they have contracted that it is not so".[28]

Some measures to verify the safety of the berth were clearly necessary for the performance of the contract. Who should be responsible for this task was determined by considering which of the two parties was in the better position to undertake it. As explained by Bowen LJ:

> The parties also knew that with regard to the safety of the ground outside the jetty the ship-owner could know nothing at all, and the jetty owner might with reasonable care know everything. The owners of the jetty, or their servants, were there at high and low tide, and with little trouble they could satisfy themselves, in case of doubt, as to whether the berth was reasonably safe. The ship's owner, on the other hand, had not the means of verifying the state of the jetty, because the berth itself opposite the jetty might be occupied by another ship at any moment.[29]

A more modern example of necessity for business efficacy is *Re Ronim Pty Ltd*.[30] In this case, a contract for the sale of land specified a date at which the transaction should be completed; ie, the purchase price paid in exchange for title to the land. It is a standard conveyancing practice for a purchaser to search the title for the land on the day of completion and not to settle without such a search. On the date for completion of the contract in question, the purchaser could not search the title for the land because the Titles Office's computer was not working. The Queensland Court of Appeal found a term was implied in fact in the contract to the effect that where, through no fault of their own, on the day for completion the parties

25 *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41, 66. A contract could also be said to lack business efficacy if a term is needed to ensure the fulfilment of a contractual purpose: Robertson, "Purposive Contractual Interpretation" (2019) 39 *Legal Studies* 230, 242–6.

26 *Sekisui Rib Loc Australia Pty Ltd v Rocla Pty Ltd* [2012] SASCFC 21, [50] (Sulan J, with whom David and Peek JJ agreed).

27 *The Moorcock* (1889) LR 14 PD 64.

28 *The Moorcock* (1889) LR 14 PD 64, 67, 70.

29 *The Moorcock* (1889) LR 14 PD 64, 69, also 67.

30 *Re Ronim Pty Ltd* [1989] 2 Qd R 172.

cannot carry out the necessary computer searches to verify title because the relevant computer is not operative, the obligation to settle is suspended until the search can be completed.[31] In relation to the requirement of business efficacy, the Court explained:

> while it is true that the contract could operate without such a provision, it could not in these circumstances operate effectively, because the purchaser would be quite unable to determine whether it would, in exchange for the balance of the purchase moneys, receive the title it has been promised.[32]

By contrast, in *Breen v Williams*[33], the High Court concluded that a contract between a doctor and his patient did not contain an ad hoc implied term entitling the patient to obtain her medical records. The High Court considered that the term was not necessary for the reasonable or effective performance of the contract.[34] Access to the doctor's records was not needed for any therapeutic reason relating to the careful and skilful treatment of the patient.[35]

In England, the business efficacy and obviousness requirements are treated as alternatives rather than cumulative requirements.[36] Terms have been held to be implied which could not be said to be necessary to give business efficacy to the contracts in question.[37] It may, however, be doubted whether "obviousness" is the best explanation for the implication of those terms since it is not clear what reasoning process can or should be undertaken in order to determine whether a term is "obvious".[38]

Obviousness

[14.35] In discussing the *BP Refinery* requirement of obviousness in implying a term in fact, reference is often made to the following dictum of Mackinnon LJ in *Shirlaw v Southern Foundries (1926) Ltd*:

> Prima facie that which in any contract is left to be implied and need not be expressed is something so obvious that it goes without saying; so that, if, while the parties were making their bargain, an officious bystander were to suggest some express provision for it in their agreement, they would testily suppress him with a common "Oh, of course!".[39]

In *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales*,[40] the parties contracted on the assumption that construction work could proceed on the basis of three shifts per day. Because of the noise, dirt and disruption, local residents obtained an injunction preventing work from being carried out on Sundays or between the hours of 10 pm and

31 *Re Ronim Pty Ltd* [1989] 2 Qd R 172, 180.

32 *Re Ronim Pty Ltd* [1989] 2 Qd R 172, 180.

33 *Breen v Williams* (1996) 186 CLR 71. See also Carter and Tolhurst, "Implied Terms: Refining the New Law" (1997) 12 *Journal of Contract Law* 152.

34 *Breen v Williams* (1996) 186 CLR 71, 80, 91, 105, 124.

35 *Breen v Williams* (1996) 186 CLR 71, 80, 91. See also, eg, *South Sydney District Rugby League Football Club Ltd v News Ltd* [2000] FCA 1541, [415].

36 *Marks and Spencer plc v BNP Paribas Securities Services Trust Company (Jersey) Ltd* [2015] UKSC 72; [2016] AC 742, [21].

37 See eg, *Equitable Life Assurance Society v Hyman* [2002] 1 AC 408, 459 and *Mosvolds Rederi A/S v Food Corp of India (The "Damodar General TJ Park" and "King Theras")* [1986] 2 Lloyd's Rep 68, discussed in Robertson, "The Foundations of Implied Terms: Logic, Efficacy and Purpose" in Degeling, Edelman and Goudkamp (eds), *Contract in Commercial Law* (2016), 143, 156–64.

38 See Robertson, "Purposive Contractual Interpretation" (2019) 39 *Legal Studies* 230, 244.

39 *Shirlaw v Southern Foundries (1926) Ltd* [1939] 2 KB 206, 227.

40 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337.

6 am. This increased Codelfa's costs. The State Rail Authority refused to pay these costs on the ground that they were not provided for in the contract. Codelfa sought to imply a term providing for compensation, but its claim was denied by the High Court.[41] Mason J explained:

> [This is] not a case in which an obvious provision was overlooked by the parties and omitted from the contract. Rather it was a case in which the parties made a common assumption which masked the need to explore what provision should be made to cover the event which occurred. In ordinary circumstances negotiation about the matter might have yielded any one of a number of alternative provisions, each being regarded as a reasonable solution.[42]

A case where the proposed implied term was "obvious" in the sense that it could be said to "go without saying" was *Gwam Investments Pty Ltd v Outback Health Screenings Pty Ltd*.[43] The case concerned a contract for Gwam to design and construct a mobile health unit on a truck owned by Outback Health (for drug testing of employees of mining companies in remote locations). Once the health unit was constructed, the overall weight of the truck exceeded the maximum loaded mass requirements allowable for that truck and accordingly could not lawfully be driven on a road. The Full Court of the Supreme Court of South Australia agreed with the trial judge that a term should be implied into the contract that the overall package of the truck together with the unit should be capable of being driven on public roads. Such a requirement satisfied the tests in *BP Refinery* and, in particular, the term "went without saying" and was "reasonable".[44]

Two potential problems with the "obviousness" requirement were identified by the Privy Council in *Attorney General of Belize v Belize Telecom Ltd*.[45] The first is that the officious bystander test brings to mind the actual parties, inviting the court to speculate on how those parties might have responded, rather than adopting an objective approach to the construction of the instrument.[46] The fact that judges not uncommonly have the innocent bystander answering his or her own question illustrates the confusing nature of the inquiry. In *Regreen Asset Holdings Pty Ltd v Castricum Brothers Australia Pty Ltd*,[47] for example, the primary judge held that: "In my opinion a reasonable bystander would, at the time of the making of the [contract], have said 'oh, of course!'." The second criticism is that it should not be fatal to the implication of a term that the matter in question is complicated. Careful consideration may be required before one can conclude that there is only one answer to the problem that has arisen that is consistent with the express terms.[48] As the above quote from *Codelfa Construction*

41 The High Court found instead that the contract had been frustrated: see discussion at [15.45].

42 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 355–6; see also 375 (Aickin J).

43 *Gwam Investments Pty Ltd v Outback Health Screenings Pty Ltd* [2010] SASC 37.

44 *Gwam Investments Pty Ltd v Outback Health Screenings Pty Ltd* [2010] SASC 37, [38], [111].

45 *Attorney General of Belize v Belize Telecom Ltd* [2009] UKPC 10; [2009] 1 WLR 1988, [25]

46 *Attorney General of Belize v Belize Telecom Ltd* [2009] UKPC 10; [2009] 1 WLR 1988, [25]. See also Hoffman, "The Intolerable Wrestle with Words and Meaning" (1997) 114 *South African Law Journal* 656, 662 and Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [10.61] (the officious bystander test is "transparently artificial" and would make implication "practically impossible" if applied literally).

47 *Regreen Asset Holdings Pty Ltd v Castricum Brothers Australia Pty Ltd* [2015] VSCA 286, [65]. See also Peden, *Good Faith in the Performance of Contracts* (2003), para 4.6. Cf Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [10.61] (suggesting that it would be better if the bystander answered the question).

48 *Attorney General of Belize v Belize Telecom Ltd* [2009] UKPC 10; [2009] 1 WLR 1988, [25]. See also *Servcorp WA Pty Ltd v Perron Investments Pty Ltd* [2016] WASCA 79; (2016) 50 WAR 226, [159].

indicates, what is required for this category of implication is not a situation in which a solution to the problem that has arisen is obvious in the sense of being *immediately apparent*, but a situation in which there is a *singularly appropriate solution*, rather than multiple options which the parties might have chosen.[49]

Clarity

[14.40] The fourth element of the *BP Refinery* formula is that a term will only be implied if it is capable of being expressed in a clear or precise manner. In *Ansett Transport Industries v Commonwealth*,[50] the plaintiff argued that the issue of import permits to two new companies seeking to carry freight by air would be in breach of an implied term in an agreement made between it and the Commonwealth. The argument was rejected by the High Court. One of the reasons given by Gibbs J was:

> If a term were to be implied it would be to the effect that the Commonwealth would do whatever it might lawfully do to maintain the position (which has already been secured) that there are two and more than two operators of trunk route airline services in Australia, or, put negatively, that it would not do anything which would destroy or undermine that position. The width and lack of precision of such a condition is an argument against implying it.[51]

Consistency

[14.45] The final element in the *BP Refinery* formula is the fundamentally important requirement that the term that is claimed to be implied must be consistent with the express terms of the contract. This has been said to be "perhaps the most frequently invoked ground for refusing to imply a term".[52] As Heydon observes,[53] this means that a term will not be implied if: first, an express term specifically excludes implied terms;[54] secondly the term claimed to be implied contradicts or is directly inconsistent with an express term[55] or thirdly, an express term "appears to be intended to cover the field that would otherwise be occupied by the implied term"[56] and leaves no room for the implication.

Why strict tests?

[14.50] Courts have repeatedly stated that a term may not be implied simply because it is fair or reasonable;[57] the term must also be necessary or obvious.[58] Jeff Goldsworthy argues that

49 See Robertson, "The Foundations of Implied Terms: Logic, Efficacy and Purpose" in Degeling, Edelman and Goudkamp (eds), *Contract in Commercial Law* (2016), 143, 162–3.

50 *Ansett Transport Industries v Commonwealth* (1977) 139 CLR 54.

51 *Ansett Transport Industries v Commonwealth* (1977) 139 CLR 54, 62.

52 Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (10th Aust ed, 2017), [10.60].

53 Heydon, *Heydon on Contract* (2019), [10.840]–[10.860].

54 For example, *Australian Guarantee Corporation Ltd v Ross* [1983] 2 VR 319, 322.

55 For example, *Farrow Mortgage Services Pty Ltd (in liq) v Edgar* (1993) 114 ALR 1, 8–9.

56 *Gemmell Power Farming Co Ltd v Nies* (1935) 35 SR (NSW) 469, 477 (in reference to term implied by statute); see, eg, *Ikin v The Danish Club "Danebrog" Inc* [2001] VSCA 123 for application of the principle to exclude a term implied in fact.

57 See, eg, *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 401–3; *Biotechnology Australia Pty Ltd v Pace* (1988) 15 NSWLR 130, 132.

58 See, eg, *Liverpool City Council v Irwin* [1977] AC 239, 253–4; *Durham Tees Valley Airport Ltd v BMI Baby Ltd* [2009] All ER 233 (Comm), [87].

the need for strict tests for implying terms in fact, such as those in *BP Refinery*, arises from the very rationalisation of these terms as expressing the implicit assumptions of the parties.[59] An assumption that is implicit is something that the parties have taken for granted and must therefore be obvious in the context in which they are dealing. Accordingly, to imply a term in fact, the implicit assumption on which the term is based must be so obvious that it goes without saying.[60]

This strict test for implying terms recognises that parties take more for granted in conversation than in legal documents. In face-to-face communication, parties will have a greater range of cues for ascertaining meaning, such as intonation and facial expression, than they will in written documents.[61] Accordingly, parties will take care to express themselves clearly in written documents and have fewer assumptions about what "goes without saying". In contracts, parties typically intend to spell out the full range of their undertakings and not to leave important matters to rest as a matter of assumption or implication.[62] Thus, the more significant the incursion into the parties' contract a proposed implied term is, the less likely it is the term goes without saying and the more suspicion should be exerted about whether the term was one that was "tacitly assumed" by the parties.

Informal contracts

[14.60] The *BP Refinery*[63] framework imposes a stringent test for implying a term in fact: all five requirements must be satisfied. The requirements may not be strictly applied in the case of informal contracts. These are cases in which the parties have not recorded their agreement in a comprehensive written form.[64] In *Byrne v Australian Airlines Ltd*, McHugh and Gummow JJ said that in such cases "caution is required against an automatic or rigid application of the cumulative criteria identified in *BP*."[65] Examples of this type of less formal contracting arrangement might include an employment contract or a verbal contract for the provision of professional or other services.

Where the contract is informal, the court must first identify the actual terms of the contract. To the extent that the terms have not been articulated by the parties, they may be identified by inference on the basis of the kind of relationship in question.[66] The court may then consider the possibility of implied terms, although the distinction between implied terms and terms identified as a matter of inference may not always be easy to draw.[67] In implying terms in an informal contract, the High Court has suggested that a flexible approach is required.[68]

59 See also *Attorney General of Belize v Belize Telecom Ltd* [2009] UKPC 10; [2009] 1 WLR 1988, [17].

60 Goldsworthy, "Implications in Language, Law and the Constitution" in Lindell (ed) *Future Directions in Constitutional Law* (1994), 158, pp 169–70.

61 Goldsworthy, "Implications in Language, Law and the Constitution" in Lindell (ed) *Future Directions in Constitutional Law* (1994) 158, p 164.

62 Kramer, "Common Sense Principles of Contract Interpretation (and how we've been using them all along)" (2003) 23 *Oxford Journal of Legal Studies* 173, 179.

63 *BP Refinery (Westernport) Pty Ltd v Shire of Hastings* (1977) 180 CLR 266.

64 *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 442.

65 *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 442.

66 See *Hawkins v Clayton* (1988) 164 CLR 539, esp at 469–71.

67 *Hawkins v Clayton* (1988) 164 CLR 539, 470–1; *Breen v Williams* (1996) 186 CLR 71, 91.

68 *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41, 121; *Hawkins v Clayton* (1988) 164 CLR 539; *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 422, 442.

The High Court has approved the following statement of principle of Deane J in *Hawkins v Clayton*:

> In a case where it is apparent that the parties have not attempted to spell out the full terms of their contract, the court should imply a term by reference to the imputed intention of the parties if, but only if, it can be seen that the implication of the particular term is necessary for the reasonable or effective operation of a contract of that nature in the circumstances of the case.[69]

This statement indicates that a term may be implied in an informal contract if the term is necessary for the reasonable operation of the contract, even if it is not necessary for the effective operation of the contract. This suggestion seems surprising in the face of authority that reasonableness alone is not a sufficient basis for implying terms in fact. Tolhurst and Carter suggest the "better view is that 'efficacy' is the overriding concern, and a term will not be implied into a contract effective without it even if it would lead to a more reasonable operation".[70]

It seems clear from the judgment of McHugh and Gummow JJ in *Byrne v Australian Airlines Ltd* that all of the other elements of the *BP Refinery* framework must be satisfied for a term to be implied in an informal contract. Their Honours noted that obviousness remains an important element in implying a term in an informal contract.[71] One of the reasons they gave as to why the term in question was not implied on the facts of the case is that it "would operate in a partisan fashion" and would favour the interests of one party over the other (thus indicating that, to be implied in this context, a term must be reasonable and equitable).[72] They said nothing of the requirement that a term must be capable of clear expression, but "it would seem impossible to argue for the implication of a term which cannot be clearly expressed."[73] They also said nothing of the requirement of consistency with the express terms, but this requirement is fundamental. It could not be relaxed without upending the nature and basis of implied terms, and there is no reason to relax it in the case of an informal contract. On the contrary, those terms that have been expressly agreed between the parties have particular salience in the case of informal contracts.

TERMS IMPLIED IN LAW

[14.65] Terms that are implied "in law" are implied in all contracts of a particular class or description.[74] These terms are implied on the basis that they are necessary incidents of all contracts falling within the class in question. The terms are said to be "read into the contract as the nature of the contract itself implicitly requires, no more, no less: a test, in other words, of necessity."[75] Some doubt whether necessity provides an adequate explanation and insist

69 *Hawkins v Clayton* (1988) 164 CLR 539, 573; approved in *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 422, 442; *Breen v Williams* (1996) 186 CLR 71, 90, 91, 123. See also *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41, 121.

70 Tolhurst and Carter, "The New Law on Implied Terms" (1996) 11 *Journal of Contract Law* 76, 86.

71 *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 442, 444.

72 *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 442, 442–3.

73 Tolhurst and Carter, "The New Law on Implied Terms" (1996) 11 *Journal of Contract Law* 76, 85.

74 *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 440, 448.

75 For example, *Liverpool City Council v Irwin* [1977] AC 239, 254.

that considerations of policy are involved.[76] In *Commonwealth Bank v Barker*, Gageler J maintained that reference to necessity "does not exclude considerations of justice and policy" but only serves to emphasise that "a court should not imply a new term other than by reference to considerations that are compelling."[77] Keifel J also recognised that "broad considerations" may inform implications in law.[78] French CJ, Bell and Keane JJ, on the other hand, appeared to take a narrower view, suggesting that the "necessity" requirement reminds courts:

> that implications in law must be kept within the limits of the judicial function. They are a species of judicial law-making and are not to be made lightly. It is a necessary condition that they are justified functionally by reference to the effective performance of the class of contract to which they apply, or of contracts generally in cases of universal implications, such as the duty to cooperate.[79]

In *Byrne v Australian Airlines Ltd*,[80] McHugh and Gummow JJ said that there was "much force" in the suggestion that many terms that would now be classified as implied by law in particular classes of contracts had their origins as terms implied in fact on the basis of the presumed intentions of the parties "but thereafter became so much a part of the common understanding as to be imported into all transactions of the particular description".[81] Traditional examples of terms implied in law include:

> the implied conditions of reasonable fitness and merchantable quality on a contract for the sale of goods, the rule that payment and delivery of goods are concurrent conditions, the implied warranty of seaworthiness, the implied condition on the letting of a furnished house that it is reasonably fit for habitation, the implied promise by one who agrees to build a house that the house will be reasonably fit for habitation, the implied promise by a servant not to disclose secret processes, not to hand over to a rival written work completed for the master, and not, while still in his master's employment, to solicit the master's customers to transfer their custom to himself, the implied promise by an employer (in some cases) to furnish work, the implied duty of care in the carriage of passengers and in looking after bailed goods, and the implied promise by a banker not to disclose the state of his customers' account.[82]

In *Equitable Life Assurance Society v Hyman*,[83] Lord Steyn helpfully distinguished terms implied in law from those implied in fact on the basis that terms implied in law are standardised terms impliedly annexed to particular kinds of contract, which "operate as general default rules". In other words, they are included by default based on the nature of the contract if the parties fail to specify otherwise. Terms implied in fact on the basis of business efficacy, on the other hand, "operate as ad hoc gap fillers".[84] In other words, they arise to fill gaps in particular

76 *Simonius Vischer & Co v Holt & Thompson* [1979] 2 NSWLR 322, 348; *South Sydney District Rugby League Football Club Ltd v News Ltd* [2000] FCA 1541, [392]; *University of Western Australia v Gray* [2009] FCFC 116; (2009) 179 FCR 346, [142]

77 *Commonwealth Bank of Australia v Barker* [2014] HCA 32; (2014) 253 CLR 169, [114].

78 *Commonwealth Bank of Australia v Barker* [2014] HCA 32; (2014) 253 CLR 169, [37].

79 *Commonwealth Bank of Australia v Barker* [2014] HCA 32; (2014) 253 CLR 169, [29].

80 *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410.

81 *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 448. See also *Breen v Williams* (1996) 186 CLR 71, 103.

82 Williams, "Language and the Law IV" (1945) 61 *Law Quarterly Review* 384, 403, quoted in *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 448.

83 *Equitable Life Assurance Society v Hyman* [2002] 1 AC 408, 458–9 (Lord Steyn, with whom Lord Slynn, Lord Hoffmann, Lord Cooke and Lord Hobhouse agreed).

84 *Equitable Life Assurance Society v Hyman* [2002] 1 AC 408, 459.

contracts based on what is required in the context of the particular contract in question, so the court's attention is focused on the express terms and the "particular commercial setting."[85]

Requirements for implying terms in law for the first time

[14.70] The categories of terms implied in law are not closed. New terms that will be implied in law may develop over time. In deciding whether or not a new term should be recognised as implied in law, there are two issues to consider. First, the term must be applicable to a definable class of contractual relationship.[86] Secondly, subject to the qualifications noted above at [14.65] and below at [14.75], the term must be "necessary" in all contracts of that class. In *Byrne v Australian Airlines Ltd*, McHugh and Gummow JJ explained that:

> [The requirement of necessity reflects] the concern of the courts that, unless such a term be implied, the enjoyment of the rights conferred by the contract would or could be rendered nugatory, worthless, or, perhaps, be seriously undermined.[87]

The test of necessity is illustrated by the decision of the House of Lords in *Liverpool City Council v Irwin*.[88] The case concerned the obligations of a landlord of a 15-storey apartment block with respect to the common areas of the stairs and lifts. The landlord was a public authority. Under statute, it was responsible for providing housing for members of the public, selected because of their need, at a subsidised rent. The express terms of the contract between the parties contained a list of obligations owed by the tenant; however, none were owed by the landlord. The House of Lords held that the landlord was under an implied obligation to take reasonable care of the common areas. The House of Lords was prepared to imply the term in law in the class of contract in question, namely tenancies in high-rise apartment blocks.[89] Applying the test of necessity, Lord Wilberforce considered:

> [The stairs and the lifts] are not just facilities, or conveniences provided at discretion: they are essentials of the tenancy without which life in the dwellings, as a tenant, is not possible. To leave the landlord free of obligation as regards these matters, and subject only to administrative or political pressure, is, in my opinion, inconsistent totally with the nature of this relationship. The subject matter of the lease (high rise blocks) and the relationship created by the tenancy demand, of their nature, some contractual obligation on the landlord.[90]

The House of Lords refused to imply a term imposing an absolute obligation on the landlord for care of the common areas.[91] Their Lordships suggested that an absolute obligation would go beyond what was reasonable.[92] The concern was expressed that the tenants should not be relieved of the responsibility themselves to take reasonable care of the common areas.

In *Breen v Williams*,[93] the High Court held that there was no term implied in law in a contract between a patient and a doctor giving the patient a right of access to his or her medical

85 *Equitable Life Assurance Society v Hyman* [2002] 1 AC 408, 459.

86 *Scally v Southern Health and Social Services Board* [1992] 1 AC 294, 307.

87 *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 450. See also *Esso Australia Resources Ltd v Plowman* (1995) 183 CLR 10, 30; *Australis Media Holdings Pty Ltd v Telstra Corporation* (1998) 43 NSWLR 104, 124.

88 *Liverpool City Council v Irwin* [1977] AC 239.

89 *Liverpool City Council v Irwin* [1977] AC 239, 254, 257, 266.

90 *Liverpool City Council v Irwin* [1977] AC 239, 254, 262–3.

91 *Liverpool City Council v Irwin* [1977] AC 239, 256, 259, 263, 269.

92 *Liverpool City Council v Irwin* [1977] AC 239, 256, 269.

93 *Breen v Williams* (1996) 186 CLR 71.

records. The doctor was subject to an implied obligation to exercise reasonable care in treating the patient. Gummow J concluded that it could not be said that unless a term relating to the access of records was implied as a matter of law, the enjoyment of the rights conferred on the patient by the contract would or could be rendered worthless or seriously undermined.[94]

The relationship between "business efficacy" and "necessity"

[14.75] As discussed above, in implying a term in fact, courts make use of a test of business efficacy. Does this test differ from the test of necessity in implying a term in law for the first time? In *University of Western Australia v Gray*, the Full Court of the Federal Court said that "necessity" in the context of implying a term in law for the first time "has a different shade of meaning from that which it has in formulations of the business efficacy test".[95] This was because implication in law rests "upon more general considerations".[96] These considerations included "the inherent nature of the contract and of the relationship thereby established".[97] They might also include issues of "justice and policy" and of "social consequences".[98] The Court also stated that:[99]

> considerations of policy ... can be of considerable significance in negativing the making of an implication, or else in demonstrating that the issues raised by the proposed implication are of such a character or complexity as to make it inappropriate for a court, as distinct from a legislature, to impose the obligation in question.

In *University of Western Australia v Gray*, the University of Western Australia argued that Gray's duty expressly to undertake research carried with it "a duty to invent". This duty was argued to found the basis for implying a further term vesting ownership of Gray's inventions in UWA as his employer. The Full Court of the Federal Court rejected the argument. The Court said that the "insuperable difficulty" in UWA's submissions was that Dr Gray's employment duties did not require him to perform tasks from which inventions might result. "The subject matter and the manner of discharge of his duty to research were in his discretion. He was not employed to invent."[100] The Full Court also considered that the trial judge had correctly identified a range of other considerations that were inconsistent with the proposed implied term, including the facts that an academic researcher at a university had freedom to choose the subject and manner of research, to publish that research and to work with other collaborators.[101]

TERMS IMPLIED BY CUSTOM

[14.80] In some cases, a term may be implied on the basis of custom or usage in a particular market or context. The basis for implication is that where a custom is "well known and acquiesced in", then "everyone making a contract in that situation can reasonably be presumed

94 *Breen v Williams* (1996) 186 CLR 71, 124 (Gummow J).

95 *University of Western Australia v Gray* [2009] FCFC 116; (2009) 179 FCR 346, [142].

96 *Lister v Romford Ice and Cold Storage Co Pty Ltd* [1957] AC 555, 576; *Scally v Southern Health and Social Services Board* [1992] 1 AC 294.

97 *University of Western Australia v Gray* [2009] FCFC 116; (2009) 179 FCR 346, [142].

98 *University of Western Australia v Gray* [2009] FCFC 116; (2009) 179 FCR 346, [142]. Also *Hughes Aircraft Systems International v Airservices Australia* (1997) 76 FCR 151, 194–7.

99 *University of Western Australia v Gray* [2009] FCFC 116; (2009) 179 FCR 346, [146].

100 *University of Western Australia v Gray* [2009] FCFC 116; (2009) 179 FCR 346, [195].

101 *University of Western Australia v Gray* [2009] FCFC 116; (2009) 179 FCR 346, [207]–[209].

to have imported that term into the contract".[102] In implying a term on the basis of custom, it has been said that:

> Seeing that custom is only to be inferred from a large number of individual acts, it is evident that the only proof of the existence of a usage must be by the multiplication or aggregation of a great number of particular instances; but these instances must not be miscellaneous in character, but must have a principle of unity running through their variety, and that unity must show a certain course of business and an established understanding respecting it.[103]

In *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur Insurance (Australia) Pty Ltd*, the High Court (Gibbs CJ, Mason, Wilson, Brennan and Dawson JJ) outlined the following principles for implying a term on the basis of custom:

1. "The existence of a custom or usage that will justify the implication of a term into a contract is a question of fact".
2. While it need not be "universally accepted", "there must be evidence that the custom relied on is so well known and acquiesced in that everyone making a contract in that situation can reasonably be presumed to have imported that term into the contract".
3. "A term will not be implied into a contract on the basis of custom where it is contrary to the express terms of the agreement".
4. "A person may be bound by a custom notwithstanding the fact that he [or she] had no knowledge of it".[104]

These requirements are strict, and consequently, there are few examples of terms implied by custom.[105] This point is illustrated by the decision in *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur Insurance (Australia) Ltd*.[106] In this case, the defendants paid an insurance premium to the broker who had arranged their insurance. The broker went into liquidation before passing the payment on to the plaintiff insurers. The insurers brought an action seeking to recover the payment from the defendants. The defendants sought to establish a term implied into the insurance contract by custom to the effect that where a contract of insurance was arranged by a broker, the broker, not the insured party, was liable to pay the premium to the insurers. This argument was rejected by the High Court. In order to imply such a term on the basis of custom, it was not sufficient to show that in the ordinary course of events, the premium was paid to the insurer by the broker or that the insurer's first demand for payment was addressed to the broker. It was necessary to establish a clear course of conduct under which insurers did not look to the insured for the payment of the premium.[107] Moreover, the court observed that "a custom that falls short of involving a recognition of rights and

102 *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur Insurance (Australia) Ltd* (1986) 160 CLR 226, 236. See also *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 423, 440.

103 *Goodman Fielder Consumer Foods Ltd v Cospak International Pty Ltd* [2004] NSWSC 704, [64] quoting from *Browne on Usage and Custom* (1875).

104 *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur Insurance (Australia) Ltd* (1986) 160 CLR 226, 236–8, as summarised in *Goodman Fielder Consumer Foods Ltd v Cospak International Pty Ltd* [2004] NSWSC 704, [64].

105 See, eg, *Goodman Fielder Consumer Foods Ltd v Cospak International Pty Ltd* [2004] NSWSC 704.

106 *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur Insurance (Australia) Ltd* (1986) 160 CLR 226.

107 *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur Insurance (Australia) Ltd* (1986) 160 CLR 226, 238.

liabilities fails to provide a firm foundation for the implication of terms in a contract."[108] The court considered that there was insufficient evidence to establish such a custom.

THE IMPLIED DUTY OF GOOD FAITH IN CONTRACT PERFORMANCE

[14.85] One unique, and controversial, type of implied term frequently raised in Australian contract law is a duty to perform in good faith.[109]

Why recognise a duty of good faith?

[14.90] The reason usually given for recognising an implied duty of good faith is to ensure an acceptable level of co-operation and fairness in contract performance. The duty of good faith performance supplements the express terms of a contract to preclude certain types of uncooperative or unfair conduct in the course of performing a contract or exercising contractual powers. For example, consider the following situations:

1. A vendor and a purchaser enter into a contract for the sale of land. Performance of the contract is subject to the government approving a plan of subdivision, which means that either of the parties can terminate the contract should the approval not be given. After an unexpected rise in the value of the land, the vendor decides that she does not want to proceed with the sale to the purchaser but instead wants to sell the property at an increased price to someone else. Accordingly, the vendor does not apply for the approval of the subdivision and seeks to terminate the contract.
2. A principal engages a contractor to excavate a construction site. The contract provides that the principal may terminate the contract following any specified breach of the contract by the contractor, subject to the contractor being given opportunity to "show cause" to the "satisfaction" of the principal why the contract should not be terminated. The contractor breaches the contract but presents a reasonably good excuse to the principal for that breach. Relying on rumours overheard in a bar, the principal nonetheless decides that the contractor is unreliable. The principal terminates the contract on the ground that the contractor has not shown cause to the principal's satisfaction.

In each of these two cases, it might be considered that the party given a contractual right – the vendor and principal respectively – should not be entitled to exercise the right in the circumstances that have occurred. It might be considered that the exercise of the party's rights should be restricted because that exercise would be uncooperative, unfair or contrary to what the parties intended when they made the contract. In these sorts of situation, there may be a role for a duty of good faith in promoting co-operation in contract performance and fair dealing in the exercise of contractual powers.

In Australian law there are a number of traditional doctrines that may, in appropriate cases, have the effect of promoting fair dealing or at least precluding egregious conduct in the performance of a contract. For example, as a matter of construction, an apparently broad contractual right might be qualified by reference to the other terms of the contract or the

108 *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur Insurance (Australia) Ltd* (1986) 160 CLR 226, 240.

109 See generally, Paterson, "Good Faith Duties in Contract Performance" (2014) 14 *Oxford Commonwealth Law Journal* 283.

surrounding circumstances.[110] Specific terms may be implied in law or fact to regulate parties' conduct.[111] A duty of good faith may not go any further than the more traditionally implied terms.[112] Nonetheless, recognition of a general implied duty of good faith might be seen as important because it would directly acknowledge the relevance of good faith and fair dealing to contractual relationships.[113] Conversely, critics of an implied duty of good faith argue that there is little reason to adopt a duty of largely unknown content unless the existing relevant doctrines are shown to be inadequate or in need of reform.[114]

Recognition of a duty of good faith

[14.95] The question of whether Australian law should recognise an implied duty of good faith in contract performance[115] is yet to be decided by the High Court. In *Royal Botanic Gardens and Domain Trust v South Sydney City Council*,[116] the High Court left the issue open. Gleeson CJ and Gaudron, McHugh, Gummow and Hayne JJ,[117] as well as Callinan J,[118] considered that the case was not an appropriate occasion for considering the question. Kirby J, although also finding it unnecessary to explore the question further, stated that a duty of good faith appeared to "conflict with fundamental notions of caveat emptor that are inherent (statute and equitable intervention apart) in common law conceptions of economic freedom".[119] In *Commonwealth Bank of Australia v Barker*, the High Court declined to determine whether there is a general obligation to act in good faith in the performance of contracts in Australian law.[120]

A duty of good faith in contract performance has been recognised by Federal and State courts.[121] However, there are few examples of the duty having actually been breached.[122] The content and character of the duty also both remain to be confirmed.

110 See *Marks v GIO Australia Holdings Ltd* (1996) 63 FCR 304, 317.

111 See, eg, *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234; *Hughes Aircraft Systems International v Airservices Australia* (1997) 76 FCR 151.

112 See *Hughes Aircraft Systems International v Airservices Australia* (1997) 76 FCR 151, 193.

113 See Brownsword, "Two Concepts of Good Faith" (1994) 7 *Journal of Contract Law* 197.

114 *Service Station Association v Berg Bennett* (1993) 45 FCR 84, 97. See also Bridge, "Does Anglo-Canadian Law Need a Doctrine of Good Faith?" (1984) 9 *Canadian Business Law Journal* 385.

115 A duty of good faith may arise in specific contexts, in particular, in contracts of insurance under the *Insurance Contracts Act 1984* (Cth), s 13, and circumstances where the parties are in a fiduciary relationship; see further *The Laws of Australia*, Equity 15.2 "Fiduciaries".

116 *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45.

117 *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45, [40].

118 *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45, [156].

119 *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45, [88]–[89].

120 *Commonwealth Bank of Australia v Barker* [2014] HCA 32; (2014) 253 CLR 169, [42], [107].

121 See, eg, *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 263–8; *Hughes Aircraft Systems International v Airservices Australia* (1997) 76 FCR 151, 191–3; *South Sydney District Rugby League Football Club v News Ltd* [2000] FCA 1541; *Far Horizons Pty Ltd v McDonalds Australia Ltd* [2000] VSC 310; *CBFC Ltd v Edwards* [2001] SADC 40; *Central Exchange Ltd v Anaconda Nickel Ltd* [2002] WASCA 94; (2002) 26 WAR 33, [16], [55]; *Esso Australia Resources Pty Ltd v Southern Pacific Petroleum NL (Receivers and Managers appointed) (Administrators appointed)* [2005] VSCA 228; *Tone Tasmania Pty Ltd v Garrott* [2008] TASSC 86; [2008] 17 Tas R 320; *Cordon Investments Pty Ltd v Lesdor Properties Pty Ltd* [2012] NSWCA 184.

122 See, eg, *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558; *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2005] FCA 288 (issue not decided on appeal in *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2006] FCAFC 40; (2006) 149 FCR 395, [119]).

Some level of support for an implied duty of good faith performance in Australian contract law is also drawn from the recognition of such a duty in other jurisdictions.[123] The concept of good faith in contracting has historical origins in Roman law and an important place in civil law.[124] In the United States, a jurisdiction whose contract law more closely resembles that of Australia, a duty of good faith is implied in contracts for the sale of goods under the *Uniform Commercial Code* (US).[125] Some United States courts have also been prepared to follow the *Restatement of Contracts (2d)* (US)[126] in implying a general law duty of good faith in the performance of contracts.[127]

Good faith has received a more mixed reception in other Commonwealth countries. English courts have traditionally denied any role for a general implied duty of good faith in contract performance.[128] In *Yam Seng Ltd v International Trade Corporation Ltd*, Leggatt J thought that English law had not yet reached the stage "where it is ready to recognise a requirement of good faith as a duty implied by law". However, Leggatt J saw no difficulty in English law in implying such a term in fact "in any ordinary commercial contract based on the presumed intention of the parties".[129]

In Canada, different views have been expressed about whether there should be a general obligation of good faith in the performance of contracts.[130] In *Bhasin v Hrynew*, the Supreme Court of Canada was prepared to acknowledge the role of good faith as a general "organising principle" of the common law of contract.[131] The particular manifestation of the organising principle of good faith recognised in *Bhasin v Hrynew* was a duty to act honestly in the performance of contractual obligations, requiring "the parties to be honest with each other in relation to the performance of their contractual obligations".[132]

Good faith and unconscionable conduct

[14.100] In its concern with the conduct of contracting parties, good faith has some general similarity to fiduciary duties and the equitable doctrines precluding unconscionable

123 See generally, *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 263–8.

124 See Powell, "Good Faith in Contracts" [1956] *Current Legal Problems* 17.

125 *Uniform Commercial Code* (2014), § 1-203.

126 American Law Institute, *Restatement of Contracts (2d)* (1981), § 205.

127 See, eg, *Shell Oil Co v Marinello* 294 A 2d 253 (NJ Super Ct, 1972) (affirmed on appeal: 307 A 2d 598 (NJ Sup Ct, 1973)); *Texaco Inc v Appleget* 307 A 2d 603 (NJ Sup Ct, 1973); *Arnott v American Oil Co* 609 F 2d 873 (8th Cir 1979), 884; *Dayan v McDonald's Corp* 466 NE 2d 958 (Ill Ct App, 1984); *Cambee's Furniture v Doughboy Recreational Inc* 825 F 2d 167 (8th Cir 1987), 175.

128 *Yam Seng Ltd v International Trade Corporation Ltd* [2013] EWHC 111 (QB) (Leggatt J), citing Hugh Beale (ed), *Chitty on Contracts* (31st ed, 2012), Vol 1, para 1–039.

129 *Yam Seng Ltd v International Trade Corporation Ltd* [2013] EWHC 111, [131]. See also the more cautious approach in *Mid Essex Hospital Services NHS Trust v Compass Group UK and Ireland Ltd* [2013] EWCA Civ 200, [154].

130 *Bhasin v Hrynew* [2014] SCC 71; [2014] 3 SCR 494, [37]. See also Bridge, "Does Anglo-Canadian Contract Law Need a Doctrine of Good Faith?" (1984) 9 *Canadian Business Law Journal* 385; O'Byrne, "The Implied Term of Good Faith and Fair Dealing: Recent Developments" [2007] 86 *Canadian Bar Review* 194 and "Good Faith in Contract Performance: Recent Developments" [1995] 74 *Canadian Bar Review* 70; Stack, "Two Standards of Good Faith in Canadian Contract Law" (1999) 62 *Saskatchewan Law Review* 201; Waddams, "Good Faith, Unconscionability and Reasonable Expectations" (1995) 9 *Journal of Contract Law* 55.

131 *Bhasin v Hrynew* [2014] SCC 71; [2014] 3 SCR 494.

132 *Bhasin v Hrynew* [2014] SCC 71; [2014] 3 SCR 494, [73].

conduct. What is the relationship between these standards of conduct? Stapleton and Webb equate good faith with unconscionability.[133] Stapleton argues that "the principle of good faith restrains the deliberate pursuit of self-interest where this is judged unconscionable for certain specific reasons".[134] This type of explanation of the relationship between the doctrines can be criticised as making good faith superfluous, since it adds little to the concept of unconscionability.

Finn classifies good faith, unconscionability and fiduciary law by reference to a "three tier hierarchy of standards of protective responsibility".[135] Finn explains that "[c]ommon to all three standards mentioned is a concern with the extent to which one party to a relationship is obliged to acknowledge and to respect the interests of the other".[136] The demarcation between the standards, Finn suggests, lies in the extent to which a party is entitled to have regard to his or her own self-interests in a transaction.

Finn explains that the fiduciary standard "enjoins one party to act in the interests of the other – to act selflessly and with undivided loyalty".[137] The unconscionability standard "accepts that one party is entitled as of course to act self-interestedly in his actions towards the other. Yet, in deference to that other's interests, it then proscribes excessively self-interested or exploitative conduct".[138] Good faith also permits a party to act self-interestedly, but "qualifies this by positively requiring that party, in his decision and actions, to have regard to the legitimate interests therein of the other".[139]

The prohibition on unconscionable conduct under the *Australian Consumer Law* includes as a factor that courts may consider the extent to which the parties have acted in good faith.[140] It remains to be seen whether a lack of good faith is on its own sufficient to amount to unconscionable conduct offending this statutory prohibition.

Is good faith an implied term?

[14.103] Peden argues that the duty of good faith should be treated as a principle of construction, requiring a court to construe "all contracts on the basis that there is an expectancy of good faith in all terms, unless there is something explicit to suggest otherwise".[141] Peden suggests that the tenets of construction are based on a theory of co-operation or good faith so that "courts construe contracts on the basis that the parties

133 Stapleton, "Good Faith in Private Law" [1999] *Current Legal Problems* 1, 7. See also *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 265; *Dickson Property Management Services Pty Ltd v Centro Property Management (Vic) Pty Ltd* [2000] FCA 1742, [10].

134 Stapleton, "Good Faith in Private Law" [1999] *Current Legal Problems* 1, 7. See also Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (10th Aust ed, 2017), [10.44]; Mason, "Contract, Good Faith and Equitable Standards in Fair Dealing" (2000) 116 Law Quarterly Review 66, 90.

135 Finn, "The Fiduciary Principle" in T G Youdan (ed), *Equity, Fiduciaries and Trusts* (1989), p 3.

136 Finn, "The Fiduciary Principle" in T G Youdan (ed), *Equity, Fiduciaries and Trusts* (1989), p 4.

137 Finn, "The Fiduciary Principle" in T G Youdan (ed), *Equity, Fiduciaries and Trusts* (1989), p 4.

138 Finn, "The Fiduciary Principle" in T G Youdan (ed), *Equity, Fiduciaries and Trusts* (1989), p 4.

139 Finn, "The Fiduciary Principle" in T G Youdan (ed), *Equity, Fiduciaries and Trusts* (1989), p 4.

140 See ACL, s 22(1)(l) and (2)(l).

141 Peden, "Incorporating Terms of Good Faith in Contract Law in Australia" (2001) 23 *Sydney Law Review* 223, 230; see also Peden, "Co-operation in English Contract Law – To Construe or Imply" (2000) 16 *Journal of Contract Law* 56; Peden, *Good Faith in the Performance of Contracts* (2003).

intended them to work".[142] Some support for this approach is found in *Commonwealth Bank of Australia v Barker*.[143]

Some cases suggest a unique, universal duty of good faith. In *Alcatel Australia Ltd v Scarcella*,[144] Sheller JA, said:

> With great respect, there is much to be said for a generalisation of universal application, an ideal which the High Court has pursued and sometimes achieved in other areas of the law, such as the breach of the duty of care in the law of negligence and the principles of estoppel.[145]

Subsequently, however, courts have distanced themselves from such general statements.[146]

Most courts have treated the duty of good faith as an implied term.[147] Some courts have treated the duty of good faith as a term implied in law. In *Burger King Corporation v Hungry Jack's Pty Ltd*,[148] the New South Wales Court of Appeal stated that "[t]here also appears to be increasing acceptance … that if terms of good faith and reasonableness are to be implied, they are to be implied as a matter of law".[149] As Steytler J commented in *Central Exchange Ltd v Anaconda Nickel Ltd*, "[the] preference for implication as a matter of law is, no doubt due to the difficulty of complying with the criteria for an implication in fact enunciated in *BP Refinery (Westernport) Pty Ltd v Hastings Shire Council*".[150]

To the extent that a duty of good faith is a term implied in law, the classes of contract to which it applies is still undefined. Good faith has been implied in a variety of types of commercial contract, including building contracts,[151] franchise contracts,[152] commercial leases[153] and loan contracts.[154] In *Burger King v Hungry Jacks* Sheller, Beazley and Stein JJA said that the case law indicated "obligations of good faith and reasonableness will be more readily implied in standard form contracts, particularly if such contracts contain a general power of termination".[155]

The Victorian Court of Appeal has consistently maintained that an obligation to act in good faith is not implied as a matter of law in all commercial contracts. Such an obligation will only be implied in a particular contract where the requirements for implication in fact are

142 Peden, *Good Faith in the Performance of Contracts* (2003), p 113.

143 *Commonwealth Bank of Australia v Barker* [2014] HCA 32; (2014) 253 CLR 169, [25] and [37].

144 *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349.

145 *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349, 366. See also *Hughes Aircraft Systems International v Airservices Australia* (1997) 76 FCR 151, 193; *Bhasin v Hrynew* [2014] SCC 71; [2014] 3 SCR 494.

146 See, eg, *CGU Workers Compensation (NSW) Limited v Garcia* [2007] NSWCA 193; (2007) NSWLR 704–5, [131]–[134].

147 *Vodafone Pacific Ltd v Mobile Innovations Ltd* [2004] NSWCA 15, [206].

148 *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558.

149 *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558, [164], 569 (NSWLR).

150 *Central Exchange Ltd v Anaconda Nickel Ltd* [2002] WASCA 94; (2002) 26 WAR 33, [52].

151 *Renard Constructions (ME) v Minister for Public Works* (1992) NSWLR 234.

152 *Far Horizons Pty Ltd v McDonalds Australia Ltd* [2000] VSC 310; *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558; *Shelanu Inc v Print Three Franchising Corp* (2003) 226 DLR (4th) 577.

153 *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349; *Gateway Realty Ltd v Arton Holdings Ltd* (1991) 106 NSR (2d) 180.

154 *Commonwealth Bank of Australia v Renstel Nominees Pty Ltd* [2001] VSC 167

155 *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187, [163].

satisfied.[156] This approach raises difficult questions as to how the tests for implication set out in *BP Refinery* are to be satisfied in relation to a duty of good faith.[157]

WHAT DOES GOOD FAITH REQUIRE?

[14.105] There is no clear statement from, or even much agreement among, courts or commentators as to what the implied duty of good faith requires from contracting parties. Partly, this is because there are very few cases in which the duty of good faith has been breached.[158] In *Esso Australia Resources Pty Ltd v Southern Pacific Petroleum NL*, Warren CJ commented that "courts have, more often than not, decided these matters on other bases and thereby avoided the conceptual difficulty that can attend the concept of a duty of good faith".[159] In giving content to the concept, Australian courts have commonly drawn upon the statements of Sir Anthony Mason to the effect that the concept of good faith embraces:[160]

> (1) an obligation on the parties to co-operate in achieving the contractual objects (loyalty to the promise itself); (2) compliance with honest standards of conduct; and (3) compliance with standards of contract which are reasonable having regard to the interests of the parties.

This third element is often encapsulated in the idea that each party is required "to exercise the powers conferred upon it by the agreement in good faith and reasonably, and not capriciously or for some extraneous purpose".[161]

Co-operation in performance

[14.110] A duty to co-operate is well established in Australian contract law.[162] In *Secured Income Real Estate (Australia) Ltd v St Martins Investments Pty Ltd*,[163] the High Court

156 *Esso Australia Resources Pty Ltd v Southern Pacific Petroleum NL (Receivers and Managers appointed) (Administrators appointed)* [2005] VSCA 228, [2]–[5], [22]–[25]; *Specialist Diagnostic Services Pty Ltd v Healthscope Ltd* [2012] VSCA 175; (2012) 41 VR 1, [86]; *Androvitsaneas v Members First Broker Network* [2013] VSCA 212, [108]. See also Dixon, "Good Faith in Contractual Performance and Enforcement – Australian Doctrinal Hurdles" (2011) 39 *Australian Business Law Review* 227 and, eg, *GSA Group Pty Ltd v Siebe plc* (1993) 30 NSWLR 573, 580; *News Ltd v Australian Rugby Football League Ltd* (1996) 58 FCR 447, 541; *Tote Tasmania Pty Ltd v Garrott* [2008] TASSC 86, [16]; *Driveforce Pty Ltd v Gunns Ltd (No 3)* [2010] TASSC 38; *AMC Commercial Cleaning (NSW) Pty Ltd v Coade (No 3)* [2010] NSWSC 1428 (NSW SC).

157 See, eg, *South Sydney District Rugby League Football Club Ltd v News Ltd* [2000] FCA 1541; *Overlook Management BV v Foxtel Management Pty Ltd* [2002] NSWSC 17; see also *De Pasquale v The Australian Chess Federation Incorporated* [2000] ACTSC 94, [17]; *Starlink International Group Pty Ltd v Coles Supermarkets Australia Pty Ltd* [2011] NSWSC 1154; *Thong Guan Plastic and Paper Industries SDN BHD v Vicpac Industries Australia Pty Ltd* [2010] VSC 11; *Felsink Pty Ltd v City of Maribyrnong* [2010] VSC 110; *Vakras v Cripps* [2015] VSCA 193, [416]–[424].

158 See, eg, *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558; *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2005] FCA 288, [60] (issue not decided on appeal in *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2006] FCAFC 40; (2006) 149 FCR 395, [119]).

159 *Esso Australia Resources Pty Ltd v Southern Pacific Petroleum NL (Receivers and Managers appointed) (Administrators appointed)* [2005] VSCA 228.

160 Mason, "Contract, Good Faith and Equitable Standards in Fair Dealing" (2000) 116 *Law Quarterly Review* 66, 69. See *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558, [171]; *Macquarie International Health Clinic Pty Ltd v Sydney South West Area Health Service* [2010] NSWCA 268, [12].

161 *Far Horizons Pty Ltd v McDonalds Australia Ltd* [2000] VSC 310, [120].

162 See, eg, *Butt v McDonald* (1896) 7 QLJ 68, 70–1; *Secured Income Real Estate (Australia) Ltd v St Martins Investments Pty Ltd* (1979) 144 CLR 596, 607.

163 *Secured Income Real Estate (Australia) Ltd v St Martins Investments Pty Ltd* (1979) 144 CLR 596, 607.

affirmed the following principle stated by Griffith CJ in *Butt v McDonald*: "[It] is a general rule applicable to every contract that each party agrees, by implication, to do all such things as are necessary on his part to enable the other party to have the benefit of the contract."[164] Mason J did note, however, that whether there is a duty to cooperate in doing acts that are not essential to the performance of a contract will depend less on the general principle and more on "the intention of the parties as manifested by the contract itself."[165] Many terms implied in fact might alternatively be explained as applications of the duty to cooperate.[166] However, it is important to recognise that the duty does not require a particular contractual outcome. It merely requires contracting parties to do such things as are "reasonably necessary"[167] to allow the other party the opportunity to obtain the benefits contemplated under the contract.[168]

The duty to co-operate has proved particularly pertinent where the performance of a contract is qualified by a contingent condition, requiring the occurrence of some specified event before the parties are obliged to continue with the performance of their contract.[169] Although neither party may have undertaken to ensure that the event occurs, the duty of co-operation may require one or both of the parties to do all that is reasonably necessary to satisfy the condition. Thus, where a contract for the sale of land is subject to the approval of a plan of subdivision, the vendor may be under an implied duty to co-operate by submitting the plan to the government for approval.[170]

A related concept is an implied duty of best efforts in performing discretionary obligations. Like the duty to co-operate, the duty to use best efforts requires a party to take steps to promote successful performance of the contract. For example, in *Hospital Products Ltd v United States Surgical Corp*,[171] Gibbs CJ was prepared to follow the United States approach and recognise an agent's implied duty to use its "best efforts" in a distributorship contract where the agent had been given an exclusive licence to sell a product on behalf of a principal.

The implied duty of co-operation only relates to enforceable obligations under a contract.[172] Moreover, it only requires reasonable acts of co-operation from contracting parties.[173] What is reasonable is assessed by reference to the agreement itself and a party is not required to disregard its own interests.[174] Indeed, in *Council of the City of Sydney v Goldspar*, Gyles J said

164 *Butt v McDonald* (1896) 7 QLJ 68, 70–1.

165 *Secured Income Real Estate (Australia) Ltd v St Martins Investments Pty Ltd* (1979) 144 CLR 596, 607.

166 cf Collins, "Implied Terms: The Foundation in Good Faith and Fair Dealing" (2014) 67 *Current Legal Problems* 1. But cf *Commonwealth Bank of Australia v Barker* [2014] HCA 32; (2014) 253 CLR 169, [26].

167 See eg, *Brauer & Co (Great Britain) Ltd v James Clark (Brush Materials) Ltd* [1952] 2 All ER 497 (CA), 500–1; *Secured Income Real Estate (Australia) Ltd v St Martins Investments Pty Ltd* (1979) 144 CLR 596; *Paltara Pty Ltd v Dempster* [1991] 6 WAR 85, 89, 101 (WASC). See also *Electricity Generation Corporation v Woodside Energy Ltd* [2014] HCA 7; (2014) 251 CLR 640, [41].

168 *McMahon v National Foods Milk Ltd* [2009] VSCA 153, [13].

169 On contingent conditions, see Chapter 20.

170 See, eg, *Butts v O'Dwyer* (1952) 87 CLR 267; *Meehan v Jones* (1982) 149 CLR 571; *Booker Industries Pty Ltd v Wilson Parking (Qld) Pty Ltd* (1982) 149 CLR 600; *CSS Investments Pty Ltd v Lopiron* (1987) 16 FCR 15.

171 *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41, 63.

172 *Australis Media Holdings Pty Ltd v Telstra Corporation* (1998) 43 NSWLR 104, 124.

173 See, eg, *Secured Income Real Estate (Australia) Ltd v St Martins Investments Pty Ltd* (1979) 144 CLR 596; *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349; *Howtrac Rentals Pty Ltd v Thiess Contractors (NZ) Limited* [2000] VSC 415.

174 *Farmstock Pty Ltd v Body Corporate for No 9 Port Douglas Road Community Title Scheme 24368* [2013] QCA 354, [14].

that the duty to cooperate "is not a mechanism for alleviating the consequences of hard, even harsh or unconscionable, contractual provisions".[175] In *Alcatel Australia Ltd v Scarcella*,[176] a lease obliged the lessee to comply with any requirements imposed by the local council and to indemnify the lessor against any liability in respect of those requirements. The lessee argued that the lessor had breached its duty to co-operate by pressing the council to impose strict fire requirements on the premises, thus subjecting the lessee to what it considered to be unreasonable expense. The Court of Appeal of the Supreme Court of New South Wales accepted that a duty of good faith, requiring co-operation, could be implied as a part of the lease but had not been breached. The lessee had not demonstrated that the requirements of the fire order were unreasonable. Sheller JA explained:

> In a commercial context it cannot be said, in my opinion, that a property owner acts unconscionably or in breach of an implied duty of good faith in a lease of the property by taking steps to ensure that the requirements for fire safety advised by an expert fire engineer should be put in place.[177]

Good faith and fair dealing in the exercise of contractual discretion

[14.115] The duty of good faith has a key role in qualifying the exercise of discretionary contractual powers.[178] The duty of good faith does not preclude the exercise of a contractual power whenever that exercise will have harsh consequences for the other party. Rather, the duty qualifies the decision to exercise the power to ensure some level of regard for the interests of the other party. To this end, courts have identified a number of different standards by which good faith may be measured.

Reasonableness

[14.120] Australian courts have often equated the standard of conduct required by a duty of good faith with reasonableness.[179] In the leading case of *Renard Constructions (ME) v Minister for Public Works* (*Renard*),[180] Priestley JA was prepared to imply a duty of reasonableness tempering the powers of a principal to terminate a construction contract. His Honour considered that this duty of reasonableness had "much in common" with a duty of good faith.[181]

It may be that a major aspect of a duty of reasonableness will be the imposition of obligations relating to the process through which a decision is made.[182] The *Renard* case concerned a

175 *Council of the City of Sydney v Goldspar* [2006] FCA 472, [161].

176 *Alcatel Australia Ltd v Scarcella* [1998] 44 NSWLR 349.

177 *Alcatel Australia Ltd v Scarcella* [1998] 44 NSWLR 349, 369–70.

178 See Hooley, "Controlling Contractual Discretion" (2013) 72 *Cambridge Law Journal* 65; Paterson, "Implied Fetters on the Exercise of Discretionary Contractual Power" (2009) 35 *Monash University Law Review* 45.

179 See *Macquarie International Health Clinic Pty Ltd v Sydney South West Area Health Service* [2010] NSWCA 268, [15]; *AMC Commercial Cleaning (NSW) Pty Ltd v Coade (No 3)* [2010] NSWSC 1428; *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, [288]; *Virk Pty Ltd (in liq) v YUM! Restaurants Australia Pty Ltd* [2017] FCAFC 190, [164]–[192]. See also criticism of this approach in Stapleton, "Good Faith in Private Law" [1999] *Current Legal Problems* 1, 8.

180 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234.

181 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 263. See also *Alcatel Australia Ltd v Scarcella* [1998] 44 NSWLR 349, 368; *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* [1999] FCA 903 and *Virk Pty Ltd (in liq) v YUM! Restaurants Australia Pty Ltd* [2017] FCAFC 190.

182 See *Bartlett v Australia & New Zealand Banking Group Ltd* [2016] NSWCA 30; (2016) 92 NSWLR 639, [39]–[56].

clause in a building contract which provided that a principal's right to exercise certain powers, including the power to terminate the contract, was conditional upon the contractor failing to show cause to the "satisfaction" of the principal why the powers should not be exercised. The Court of Appeal of the Supreme Court of New South Wales found that the principal had not exercised the power properly. In the view of the majority, this was because the principal had not acted reasonably.[183] The unreasonable behaviour in question was extreme. The arbitrator had found that the principal's decision was grounded on "misleading, incomplete and prejudicial information".[184] The decision suggests that, under a duty of good faith or reasonableness, a party exercising a contractual discretion must act in an unbiased way, must not act unreasonably and perhaps also must make an attempt to verify the information on which the decision is to be based.[185]

In the United States, reference has also sometimes been made to reasonableness in assessing good faith. Commonly, the reasonableness of a decision is assessed by reference to actual standards of industry practice. Thus, under the *Uniform Commercial Code* (US), in contracts for the sale of goods where the party subject to the duty is a merchant, good faith means "honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade".[186] A common explanation of the standard of conduct required by the duty of good faith implied under the general law is that a party must have some "legitimate" business reason for the exercise of its rights under the contract.[187] There are similar trends in the interpretation of the meaning of good faith in Australian law, as will be seen in the following discussion.

Extraneous purpose

[14.125] Some Australian cases have suggested that an implied duty of good faith should preclude a party from exercising a contractual power *capriciously* or for an *extraneous purpose*.[188] Such statements direct attention to a party's motives for a particular action. In *Trampoline Enterprises Pty Ltd v Fresh Retailing Pty Ltd*,[189] the purchaser of a franchised ice cream business was held to have breached an express contractual duty to act in good faith by deliberately slowing down the completion and opening of a new outlet. The purchaser was held to have taken steps to delay the opening of the new store in order to avoid triggering an obligation to make a substantial payment to the seller of the business which would, under the terms of the contract, have arisen if the store had opened two days earlier.

183 Priestley and Handley JJA. Meagher JA found that the principal had acted improperly on narrower grounds.

184 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 276.

185 See also *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 260; *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558 at [177], [181], 572 (NSWLR).

186 *Uniform Commercial Code* (US) (2014), § 2-103(1)(b).

187 See, eg, *Brattleboro Auto Sales Inc v Subaru of New England Inc* 633 F 2d 649, 652 (2nd Cir 1980); *KMC Co v Irving Trust Co* 757 F 2d 752, 759 (6th Cir, 1985); *American Mart Corp v Joseph E Seagram & Sons* 824 F 2d 733 (9th Cir, 1987), 734; *Scott Motorcycle Supply Inc v American Honda Motor Company Inc* 976 F 2d 58, 63–4 (1st Cir, 1992). Also Hadfield, "Problematic Relations: Franchising and the Law of Incomplete Contracts" (1990) 42 *Stanford Law Review* 927, 980–5.

188 See *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349, 368; *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* [1999] FCA 903, [34]; *Far Horizons Pty Ltd v McDonald's Australia Ltd* [2000] VSC 310, [115]; *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558, [185], 573 (NSWLR); *Network Ltd v Lynton Ainsley Speck* [2009] VSC 235. See also *Braganza v BP Shipping Ltd* [2015] UKSC 17; [2015] 1 WLR 1661, 1672 [28], 1677 [53] and 1688 [103].

189 *Trampoline Enterprises Pty Ltd v Fresh Retailing Pty Ltd* [2019] VSCA 74.

In *Burger King Corporation v Hungry Jack's Pty Ltd*,[190] a franchisee was required to develop a certain number of new franchise restaurants each year, subject to the franchisor's approval. The franchisor refused to give the approval needed for the franchisee to comply with this requirement. The franchise agreement specified three types of approval as necessary conditions for the franchisor to allow further development. The agreement gave the franchisor the "sole discretion" in deciding whether or not to grant these approvals and outlined the factors relevant to the approvals. The Court of Appeal of the Supreme Court of New South Wales considered that the franchisor's discretion in relation to the approvals was subject to an implied duty of good faith, which precluded the franchisor from exercising its discretion for a purpose extraneous to the contract.[191] The court considered that the franchisor's refusal to give the approvals was not in fact based on the specified factors[192] and that the franchisor's refusal was directed to preventing the franchisee from performing its obligations under the agreement. The court approved the conclusion of the trial judge that:

> the franchisor was acting as part of a "deliberate plan to prevent [the franchisee] expanding" and instead to enable the franchisor itself "to develop the Australian market [that is, through operating its own outlets] unhindered by its contractual arrangements with [the franchisee]".[193]

Accordingly, the court considered that the franchisor had acted in breach of its duty of good faith.[194]

Legitimate interests

[14.130] The standard of conduct required by a duty of good faith has sometimes been described by reference to a party's "legitimate interests".[195] Under this approach, "[good faith will] not operate so as to restrict decisions and actions, reasonably taken, which are designed to promote the legitimate interests of a party and which are not otherwise in breach of an express contractual term".[196]

What are a party's "legitimate interests"? In *South Sydney District Rugby League Football Club Ltd v News Ltd*,[197] Finn J suggested that the concept required "loyalty" to the contract and precluded "evasion of the spirit of the bargain".[198] This may be a similar notion to not acting for an "extraneous purpose", discussed above.

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190 *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558.

191 *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558, [185].

192 *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558, [223], [250], [306], [307], [368].

193 *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558, [310].

194 *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558, [224], [308], [316], [368].

195 See, eg, *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349; *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* [1999] FCA 903; *Automasters Australia Pty Ltd v Bruness Pty Ltd* [1999] WASC 39; *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558, [185], 583 (NSWLR); *South Sydney District Rugby League Football Club Ltd v News Ltd* [2000] FCA 1541, [394]; *Beerens v Bluescope Distributions Pty Ltd* [2012] VSCA 209; (2012) 39 VR 1, [55], [167]; *Cordon Investments Pty Ltd v Lesdor Properties Pty Ltd* [2012] NSWCA 184, [144].

196 *South Sydney District Rugby League Football Club Ltd v News Ltd* [2000] FCA 1541, [394].

197 *South Sydney District Rugby League Football Club Ltd v News Ltd* [2000] FCA 1541.

198 *South Sydney District Rugby League Football Club Ltd v News Ltd* [2000] FCA 1541, [426] quoting the American Law Institute, *Restatement of Contracts (2d)* (1981), § 205, comment d.

The decision in *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd*[199] indicates that the concept of "legitimate interests" may extend beyond a party's immediate commercial interests to include consideration of the ongoing relationship with the other party to the contract. The case concerned a car dealership. The supplier implemented a new marketing program aimed at improving the image of its dealers in the marketplace. The dealer did not comply, and indicated that it was unwilling to comply, with the program. As a result, the supplier gave notice of termination of the dealership in accordance with a term under the contract. The dealer then indicated that it was willing to comply with the program. However, the supplier was not willing to withdraw its notice of termination.

Finkelstein J in the Federal Court accepted that a duty of good faith might be implied to restrict the exercise of a right to terminate. His Honour also considered that such a duty would not operate "so as to restrict actions designed to promote the legitimate interests" of the supplier.[200] In the case in question, Finkelstein J considered that there was no breach of any duty of good faith.[201] The supplier was entitled to treat the dealer's refusal to implement the program as contrary to the supplier's own business interests. Moreover, Finkelstein J considered that the 13 months' notice of termination given by the supplier was sufficient to enable the dealer to reorganise its affairs. Finkelstein J did not consider that the supplier's refusal to withdraw its notice of termination constituted unconscionable conduct in contravention of s 51AC of the *Trade Practices Act 1974* (Cth) (now s 22 of the ACL).[202] Presumably His Honour also did not consider such a refusal contrary to good faith. Although the dealer had indicated it would comply with the new marketing program, Finkelstein J considered that the conduct of the dealer in failing to adopt the program could reasonably be regarded by the supplier as an indication that the dealer was not willing to act in the best interests of the dealership group as a whole.

This situation was not remedied by the dealer's subsequent indication that it would comply with the program. Finkelstein J considered that the dealer's conduct had "no doubt" led to the supplier losing confidence in the dealer and that this loss would not necessarily be overcome by a change in the attitude on the part of the dealer. Finkelstein J then explained that:

> Many relationships can only operate satisfactorily if there is mutual trust and confidence. Once that confidence and trust has broken down the position is not easily restored. It is not unconscionable to terminate a relationship where that trust and confidence has been undermined.[203]

CAN A DUTY OF GOOD FAITH BE EXCLUDED?

[14.135] If the duty of good faith is characterised as an implied term, then it would follow that the duty will not be implied where contrary to the clearly expressed intentions of the parties.[204] It has been suggested that an entire agreement clause – which states that the contract

199 *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* [1999] FCA 903.

200 *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* [1999] FCA 903, [37].

201 *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* [1999] FCA 903, [38].

202 *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* [1999] FCA 903, [46].

203 *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* [1999] FCA 903, [46].

204 *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349, 368; *Hungry Jack's Pty Ltd v Burger King Corporation* [2001] NSWCA 187; (2001) 69 NSWLR 558, [173]. See also *Central Exchange Ltd v Anaconda Nickel Ltd* [2002] WASCA 94; (2002) 26 WAR 33, [64].

represents to the entire of agreement of the parties – may not be sufficient to exclude a duty of good faith in contract performance.[205] However, it appears that words that clearly and expressly grant one party a broad discretion in the exercise of a contractual power may be effective in either excluding the duty of good faith or in narrowing its scope.

In *Vodafone Pacific Ltd v Mobile Innovations Ltd*,[206] the contract granted Vodafone a power to set the sales levels for its distributor Mobile. The power was expressed to be "in the sole discretion" of Vodafone. The contact also provided that: "To the full extent permitted by Law and other than as expressly set out in this Agreement the parties exclude all implied terms…". The New South Wales Court of Appeal held that each of these provisions was sufficient to exclude the implication of a duty of good faith. Australian courts have generally not recognised implied good faith qualifications on the exercise of a broadly expressed contractual power to terminate, such as, for example, termination "at will", "without cause" or "for convenience".[207]

By contrast, the UNIDROIT *Principles for International Commercial Contracts 2016* Art 1.7(2) states that: "The parties may not exclude or limit this duty."[208]

ON WHAT BASIS SHOULD TERMS BE IMPLIED?

Rationale for implication

[14.140] While courts have identified requirements for implying terms, they have not made clear the underlying rationale of implication. Terms implied in law have been justified as based on considerations of "policy" and "necessity", but the courts have not identified the particular policy considerations informing this area of law. Courts have stated that terms implied in fact are based on the "presumed intentions" of the parties to the contract in question, but the notion of presumed intent is ambiguous. It is not very persuasive to suggest that terms can be implied on the basis of the parties' actual, but unexpressed, intentions. In many cases where there is a gap in a contract, the parties are unlikely to have had any actual intentions as to the terms that should be implied; the gap will have arisen precisely because the parties did not consider the events that have given rise to the need for an implied term. Probably, the most courts can aim for in implying terms is to replicate the hypothetical intentions of the parties, in the sense of the intention the parties would probably have had if they had negotiated a response to the issue in dispute when making their contract.[209]

205 See *Commonwealth Bank of Australia v Spira* [2002] NSWSC 905, [144] (appeal dismissed without comment on this point: *Spira v Commonwealth Bank of Australia* [2003] NSWCA 180; *GEC Marconi Systems Pty Ltd v BHP Information Technology Pty Ltd* [2003] FCA 50; (2003) 128 FCR 1, [920]–[921]. But contra *NT Power Generation Pty Ltd v Power and Water Authority* [2001] FCA 334.

206 *Vodafone Pacific Ltd v Mobile Innovations Ltd* [2004] NSWCA 15, [198].

207 *Starlink International Group Pty Ltd v Coles Supermarkets Australia Pty Ltd* [2011] NSWSC 1154, [19]; *Trans Petroleum (Australia) Pty Ltd v White Gum Petroleum Pty Ltd* [2012] WASCA 165, [155]; *Dura (Aust) Constructions Pty Ltd v Hue Boutique Living Pty Ltd (No 3)* [2012] VSC 99, [421]; *NSW Rifle Association Inc v The Commonwealth of Australia* [2012] NSWSC 818, [200]; *Tim Barr Pty Ltd v Narui Gold Coast Pty Ltd* [2010] NSWSC 29, [418]; *DPN Solutions Pty Ltd v Tridant Pty Ltd* [2014] VSC 511, [111].

208 See [1.180].

209 Williams, "Language and the Law IV" (1945) 61 *Law Quarterly Review* 384, 401. Also Paterson, "Terms Implied in Fact: the Basis for Implication" (1998) 13 *Journal of Contract Law* 103.

Promise and consent theories of contract

[14.145] The fact that implied terms cannot be said to represent the actual intentions of contracting parties would seem to challenge theories[210] which base contract law on the will of the parties.[211] Barnett recognises the problems caused for his consent theory of contract by implied terms.[212] However, Barnett argues that implied terms or, more generally, "default rules" may be seen as consistent with consent theory and may indeed bolster the "theoretical importance of consent".[213] Barnett argues that consent plays a role in the implication of terms in two respects. First, "the presence of consent to be legally bound is essential to justify the legal enforcement of any default rules".[214] By choosing to enter into a contract, contracting parties implicitly commit themselves to the jurisdiction of a legal system, including the use of the "background rules of contract law to fill gaps in their agreement".[215] The second way in which consent is relevant to the implication of terms, according to Barnett, is that consent "operates to justify the selection of particular default rules".[216] Where terms are required to fill gaps in contracts, Barnett suggests that those terms should reflect the "conventional or common-sense understanding existing in the relevant community of discourse".[217]

Barnett's attempt to reconcile consent theory and implied terms is not entirely successful. His attempts to define consent in terms of consent to the legal system may be criticised as stretching the notion of consent beyond meaningful bounds. The idea that courts select default rules or gap-filling terms to correspond to the common-sense understanding of the community in which the parties are contracting may mean that courts replicate the terms parties would have agreed on if they had considered the issue when making their contract. However, hypothetical consent is not the same thing as actual consent, and reliance on such a notion may be seen to weaken the consent theory.

In contrast to Barnett, Charles Fried does not, in laying out his promise theory of contract, attempt to reconcile the existence of implied terms with the intentions of the parties themselves. Rather, Fried argues that, when the relations between parties are not governed by the actual promises they have made, they are governed by "residual general principles of law".[218] Fried argues that:

> Since actual intent is (by hypothesis) missing, a court respects the autonomy of the parties so far as possible by construing an allocation of burden and benefits that reasonable persons would have made in this kind of arrangement.[219]

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210 On these theories, see [1.125].

211 See Craswell, "Contract Law, Default Rules and the Philosophy of Promising" (1989) 88 *Michigan Law Review* 489.

212 Barnett, "A Consent Theory of Contract" (1986) 86 *Columbia Law Review* 269, discussed [1.25].

213 Barnett, "The Sound of Silence: Default Rules and Contractual Consent" (1992) 78 *Virginia Law Review* 821, 826.

214 Barnett, "The Sound of Silence: Default Rules and Contractual Consent" (1992) 78 *Virginia Law Review* 821, 827.

215 Barnett, "The Sound of Silence: Default Rules and Contractual Consent" (1992) 78 *Virginia Law Review* 821, 828, 859–74.

216 Barnett, "The Sound of Silence: Default Rules and Contractual Consent" (1992) 78 *Virginia Law Review* 821, 827.

217 Barnett, "The Sound of Silence: Default Rules and Contractual Consent" (1992) 78 *Virginia Law Review* 821, 829, 874–905.

218 Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), p 69, discussed at [1.20].

219 Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), p 73.

Linguistic theories

[14.150] Other scholars have appealed to linguistic theory to challenge the gap-filling analysis and the view that implied terms are in some way "added" to the parties' contract.[220] These scholars dispute the traditional assumption that a meaning must actually have been in the mind of the speaker to be included as the meaning of that utterance.[221] Adam Kramer has argued that whether or not something crossed the mind of a contracting party is not to the point because "'[c]rossing our minds' simply does not make sense as a description of how we in fact communicate".[222] Scholars drawing on linguistic philosophy argue that when we communicate we draw on a range of background assumptions that, quite literally, go without saying. Jeff Goldsworthy explains that utterances are inevitably supplemented by "implicit assumptions" that the parties "take for granted".[223] Adam Kramer has argued that the implication of terms is part of the process of construing a contract and giving effect to the actual intentions of the parties.[224] Kramer argues that:[225]

> One can intend what goes without saying and what does not cross one's mind. A communicator intends the background of social norms and his goals and principles within which he (non-consciously) formulated his utterance. These norms and goals and principles are thus intended to be used to determine issues that are undetermined by the express utterance.

Applying these insights, it can be said that terms implied in fact may not be additions to a contract which fill gaps in the terms agreed by the parties. In many cases, terms implied in fact may be implicit in the contract as expressing assumptions that the parties have "taken for granted".[226] Under this approach, the process of implication might better be described as one of inference and seen as part of the process of construing a contract, an approach referred to above.[227] Kramer's example of something that is intended but not brought to mind is that a person booking a hotel room can properly be taken to intend the room to include a bed, even if the bed is not brought to mind.[228] This example works because "hotel room" is a description of the subject matter, and contracting parties can be taken to intend the subject matter to have certain fundamental characteristics which are not necessarily brought to mind. But the further we move away from the fundamentals of a contract, the more difficult it becomes to say whether something did or did not go without saying.[229]

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220 See, eg, Farnsworth, "Disputes Over Omissions in Contracts" (1968) 68 *Columbia Law Review* 860–91, 875; A Kramer, "Implication on Fact as an Instance of Contractual Interpretation" (2004) 63 *Cambridge Law Journal* 384; Langille and Ripstein, "Strictly Speaking – It Went Without Saying" (1996) 2 *Legal Theory* 63, 63–81.

221 Langille and Ripstein, "Strictly Speaking – It Went Without Saying" (1996) 2 *Legal Theory* 63, 68.

222 Kramer, "Common Sense Principles of Contract Interpretation (and how we've been using them all along)" (2003) 23 *Oxford Journal of Legal Studies* 173, 192.

223 Goldsworthy, "Implications in Language, Law and the Constitution" in Lindell (ed) *Future Directions in Constitutional Law* (1994) 158–84, 164.

224 Kramer, "Implication on Fact as an Instance of Contractual Interpretation" (2004) 64 *Cambridge Law Journal* 384.

225 Kramer, "Implication on Fact as an Instance of Contractual Interpretation" (2004) 64 *Cambridge Law Journal* 384, 385.

226 Goldsworthy, "Implications in Language, Law and the Constitution" in Lindell (ed) *Future Directions in Constitutional Law* (1994) 158, 163–4.

227 See [14.15].

228 Kramer, "Implication on Fact as an Instance of Contractual Interpretation" (2004) 64 *Cambridge Law Journal* 384, 390.

229 Robertson, "The Foundations of Implied Terms: Logic, Efficacy and Purpose" in Degeling, Edelman and Goudkamp (eds), *Contract in Commercial Law* (2016), 143, 147–8.

Another problem with this type of interpretive approach is that there is no necessary correlation between the external standards used by courts in implying terms and the internal standards of the parties who failed to deal expressly with an issue in the contract.[230] Thus, it will not always be possible to say that implied terms can in some way be attributed to the parties' intentions on the ground that there is a shared background of norms relied upon by courts in implying those terms.

Law and economics

[14.155] From an economic perspective, Richard Posner argues that implied terms should be based on what the parties would have agreed if they had considered the issue in question when making their contract, that is, their hypothetical intentions.[231] In predicting the parties' hypothetical intentions, Posner assumes that parties generally would have agreed to an efficient response to the event that has necessitated the need for the implication of a term in their contract.[232] Often this will mean that responsibility for the event should be imposed on the party in the best position to deal with that event, such as by taking precautions against the risk of the event or by taking out insurance.

A good example of a case in which the term implied was both efficient and likely to have been intended by the parties at the time of contracting is *The Moorcock*.[233] The case concerned a contract involving the mooring of a vessel at the jetty owners' wharf on the river Thames. The vessel suffered damage when at low tide it came to rest on a ridge of hard ground beneath the mud. The English Court of Appeal held that the jetty owners were in breach of an implied term requiring them to take reasonable care to ascertain the condition of the berth.[234]

The reasoning employed by the court to reach this conclusion was effectively a simple form of cost-benefit analysis identifying the efficient response to the dispute. The precaution of taking reasonable care to ascertain the safety of the berth would have reduced the risk of damage to the ship. The jetty owners' proximity to the site made them the party best placed to take that precaution and hence liability was assigned to them.[235] The very simplicity of this analysis also makes the term implied a plausible approximation of what the parties would probably have agreed if they had considered the issue when making their contract. The precaution would have increased the cost of the contract to the jetty owners. However, the ship-owner was likely to have been prepared to pay more for this arrangement because it was cheaper than taking the precautions itself.

The economic approach may be criticised on at least three grounds. The first criticism arises in respect of terms implied in law. Such terms, because they will be implied in all contracts of a particular class, must apply to many different parties. Unless the parties in the relevant class are highly homogeneous, the efficient response to the issue in dispute may vary between

230 See further Robertson, "The Limits of Voluntariness in Contract" (2005) 29 *Melbourne University Law Review* 180.

231 Posner, *Economic Analysis of Law* (8th ed, 2011), §4.1.

232 Posner, *Economic Analysis of Law* (8th ed, 2011), §4.1. See also Craswell, "Efficiency and Rational Bargaining" (1992) 5 *Harvard Journal of Law and Public Policy* 805.

233 *The Moorcock* (1889) 14 PD 64, discussed at [14.30].

234 *The Moorcock* (1889) 14 PD 64, 67, 70.

235 *The Moorcock* (1889) 14 PD 64, 67, 69.

those parties.[236] It may be difficult to decide which term should be implied to produce the most efficient overall result. This sort of difficulty is illustrated by the disagreement between Ayres and Gertner, on the one hand, and Johnston, on the other, about what would be the most efficient gap-filling term to limit liability for the extent of damages suffered by a plaintiff through a breach of contract.[237]

A second criticism of the economic approach relates to the assumption that parties are likely to have agreed on an efficient response to a dispute. This assumption fails to take account of the possibility that parties will not always behave in such a rational manner. Consider, for example, *Liverpool City Council v Irwin*,[238] which, as discussed at [**14.70**], involved a lease between a local public authority and its low-income tenants in a high-rise apartment block. The written contract was in a standard form detailing the obligations of the tenants but imposing no obligations on the landlord. The House of Lords held that the landlord was under an implied obligation to take reasonable care of the common areas, such as the stairs and lift areas. We might apply a simple form of cost-benefit analysis to argue that the term implied was efficient. It would be a waste of a valuable asset for the flats to fall into disrepair and become unusable because no-one took care of the common areas. In a high-rise apartment block, the landlord will typically be the party best placed to perform these tasks. Landlords have general control over the premises and regular contact with the tenants. For the tenants to have the primary responsibility for the common areas would require a large amount of costly co-ordination by them.

While the result in *Liverpool City Council v Irwin* may be efficient, it is not so clear that it is a term on which both parties would have agreed had they considered the issue at the time of making their contract. It is possible that, even if the parties had considered the issue of who should be responsible for the care of the common areas at the time of making the contract, the landlord would not have assumed the obligation. As Collins points out, the apparent intention of the landlord, as indicated from the form of the lease, was to minimise its obligations.[239] This might have been because it was not possible to pass on the cost of repairs to tenants on limited incomes. Moreover, low-income tenants are unlikely to have many housing options and therefore may not have been in a position to require such a term.

A third, more broadly based, criticism of the economic approach is that the models of bargaining on which it is based are too simplistic. It might be argued that a range of "relational norms", such as co-operation and fairness, should be considered when implying terms in contracts. Moreover, the economic approach might be criticised as neglecting social values other than "efficiency". For example, Rakoff argues: "[Responsible] judges, judges who face up to the seriousness of what they do, have to work not merely in the realm of efficiency, but also in the realms of distributive justice, cultural symbolism, procedural fairness, and so forth."[240]

236 See Craswell, "Efficiency and Rational Bargaining" (1992) 15 *Harvard Journal of Law and Public Policy* 805, 815–20.

237 See Ayres and Gertner, "Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules" (1989) 99 *Yale Law Journal* 87 and Johnston, "Strategic Bargaining and the Economic Theory of Contract Default Rules" (1990) 100 *Yale Law Journal* 615. See also the discussion in Hillman, *The Richness of Contract Law: An Analysis and Critique of Contemporary Theories of Contract Law* (1997), pp 225–34.

238 *Liverpool City Council v Irwin* [1977] AC 239, discussed at [14.70].

239 Collins, *Regulating Contracts* (1999), p 46.

240 Rakoff, "The Implied Terms of Contracts: Of 'Default Rules' and 'Situation Sense'", in Beatson and D Friedmann (eds), *Good Faith and Fault in Contract Law* (1995), p 201.

"Situation sense"

[14.160] Todd Rakoff suggests an approach to determining default rules based on a practical wisdom or "situation sense".[241] Situation sense involves a close examination of the context of the problem and the use of common sense and judgment to find a solution.[242] More formally, Rakoff explains that situation sense:

> recognises a multiplicity of values and points of view; it suggests that they can be put together coherently (not solely by rational thought but rather by a combination of reason and social understanding); and it sees this reconciliation occurring more towards ground level than at the peaks … Situation sense takes as its standard the wise result as understood by someone who comprehends all the claims of value (including their fair weight) that might be made by the different role participants in a situation and who sees himself or herself as impartial – that is, equally likely to be in any of the roles.[243]

The situation sense approach might be criticised for failing to provide much guidance for parties trying to predict the likely response of a court should a gap arise in their contract. It effectually asks parties to accept that courts are "wise" and so will reach a socially acceptable response to the need for an implied term. On the other hand, as the approach emphasises, it is undeniable that in implying terms courts need to consider a range of factors, including the context of the case, any social values that may be involved, cost and the likely objectives of the parties in contracting. Indeed, it may be that the approach would not result in a substantially different result than is currently reached by courts, although it counsels a clear articulation of the relevant considerations. Consider again *Liverpool City Council v Irwin*,[244] in which the House of Lords held that a landlord to a high-rise apartment block was under an implied obligation to take reasonable care of the common areas, such as the stairs and lift areas. The House of Lords based its decision on what was necessary to the life of the tenant in the dwelling and on the nature of the relationship between the parties.[245] These seem just the sort of factors the situation sense approach would suggest that a court should take into account. It might be argued that the implied duty of good faith invites courts to invoke similar considerations. Good faith is a general, open textured concept that is given content by reference to the implicit expectations of the parties about the nature of their contractual relationship and the trust and loyalty required to make that relationship work.[246]

241 Drawing on the work of the American realist scholar Llewellyn, *The Common Law Tradition* (1960).

242 For a detailed discussion of the elements of situation sense see Rakoff, "The Implied Terms of Contracts: Of 'Default Rules' and 'Situation Sense' ", in Beatson and Friedmann (eds), *Good Faith and Fault in Contract Law* (1995), pp 216–9.

243 Rakoff, "The Implied Terms of Contracts: Of 'Default Rules' and 'Situation Sense' ", in Beatson and Friedmann (eds), *Good Faith and Fault in Contract Law* (1995), pp 224–7.

244 *Liverpool City Council v Irwin* [1977] AC 239, discussed at [14.70].

245 *Liverpool City Council v Irwin* [1977] AC 239, 254, 262–3.

246 Campbell, "Good Faith and the Ubiquity of the 'Relational' Contract" (2014) 77 *Modern Law Review* 475.

CHAPTER **15**

Frustration

AN EXCUSE FOR NON-PERFORMANCE

[15.05] The performance of a contract may be disrupted by events outside the control of the parties. For example, a ship transporting goods may be delayed by a hurricane. The hall in which a concert is planned may burn down. The government might prohibit the importation of the goods that are the subject of the contract. In such circumstances, the law of contract is asked to respond by determining the consequences of disruptions to the anticipated course of contract performance. The key question is which party should bear the risk of the disruptive event? If the contract is found still to be on foot, then the party who can no longer perform may be required to pay damages to the other party. If the contract is set aside, then the party who has incurred costs in anticipation of performance may be disadvantaged.

In many cases, the parties themselves provide for the outcome of disruptive contingencies by including in their contract an express term dealing with the consequences such events. In the absence of an express term, it may be possible to conclude that parties have foreseen the possibility of the disruptive event and allocated the risk to the party affected. In other cases, the disruptive event may be so unusual or of such catastrophic proportions that it goes well beyond what the parties could have anticipated at the time of making their contract. The doctrine of frustration provides an excuse for non-performance in these sorts of cases.[1] It is, in this sense, a "gap filler", as discussed in Pt VI.05. Frustration discharges a contract where, without fault of the party seeking discharge, events occurring after the contract was made render performance of the contract "radically different from that which was undertaken by the contract".[2]

1 See generally Treitel, *Frustration and Force Majeure* (3rd ed, 2014).
2 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337.

WHEN IS A CONTRACT FRUSTRATED?

The modern doctrine

[15.10] Courts have taken the view that the doctrine of frustration should be kept within narrow limits and that a contract should be frustrated only in exceptional circumstances.[3] The modern test for determining when a contract is frustrated was expressed by Lord Radcliffe in *Davis Contractors Ltd v Fareham UDC*,[4] and approved by the High Court of Australia in *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales*, as follows:

> Frustration occurs whenever the law recognises that without default of either party a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract. *Non haec in foedera veni*. It was not this that I promised to do.[5]

The process is one of construction. As Lord Reid explained in *Davis Contractors Ltd v Fareham UDC*, the task of the court is to determine:

> [O]n the true construction of the terms which are in the contract read in light of the nature of the contract and of the relevant surrounding circumstances, … [and] whether the contract which they did make is … wide enough to apply to the new situation …[6]

It is necessary to compare the contract agreed by the parties, interpreted in the light of the surrounding circumstances with the situation produced by the disruptive event. If the performance contemplated by the contract and the state of affairs produced by the event that disrupts this contemplated performance are "radically"[7] or "fundamentally"[8] different, the contract will be frustrated.[9]

Doctrinal basis of the test for frustration

[15.15] The modern test for frustration is based on the construction of the contract. There are different ways of understanding this process. On one view, the doctrine of frustration is a response to a "gap" in the parties' contract.[10] The doctrine applies where the events that have occurred to disrupt performance go beyond the contemplated scope of the contract. This "gap" in the parties' agreement is then "filled" by the courts finding that the contract is frustrated. On another view, the doctrine of frustration is merely a result of the ordinary process of interpretation whereby the court gives effect to both the parties' explicit and

3 *Bank Line Ltd v Arthur Capel and Co* [1919] AC 435, 459; *Davis Contractors Ltd v Fareham Urban District Council* [1956] AC 696, 715; *J Lauritzen AS v Wijsmuller BV (The "Super Servant Two")* [1990] 1 Lloyd's Rep 1, 8.

4 *Davis Contractors Ltd v Fareham UDC* [1956] AC 696, 729.

5 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337.

6 *Davis Contractors Ltd v Fareham UDC* [1956] AC 696, 720–1. Endorsed in *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 357 (Mason J).

7 *Davis Contractors Ltd v Fareham UDC* [1956] AC 696, 729; *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 357.

8 *Davis Contractors Ltd v Fareham UDC* [1956] AC 696, 723; *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 360, 407.

9 See also *Brisbane City Council v Group Projects Pty Ltd* (1979) 145 CLR 143, 160.

10 See, eg, Trebilcock, "The Role of Insurance Considerations in the Choice of Efficient Civil Liability Rules" (1988) 4(2) *Journal of Law, Economics and Organization* 243, 249–55 and Trebilcock, *The Limits of Freedom of Contract* (1993); Triantis, "Contractual Allocations of Unknown Risks: A Critique of the Doctrine of Commercial Impracticability" (1992) 42(4) *University of Toronto Law Journal* 450.

implicit allocations of risk under the contract.[11] The problem with this view is that it is difficult to see how the parties could, even implicitly, have allocated the risk of an unforeseen and catastrophic disruptive event.[12]

Over its lifetime, a number of different analyses of the doctrinal basis of frustration have been suggested.[13] These include seeing frustration as based on the removal of the foundation of the contract, a total failure of consideration and an implied term.[14] Courts have stated on a number of occasions that the various theories of frustration produce similar results,[15] and that cases decided under the earlier theories were not wrongly decided.[16] Accordingly, the earlier cases on frustration remain valid examples of frustrating events, even though they may have been explained on a different basis from that which would now be preferred.

Illustrations of when a contract may be frustrated

[15.20] In general terms, frustration encompasses cases in which performance becomes literally impossible[17] or where future performance has been rendered commercially unfeasible.[18] Events such as hardship, inconvenience or material loss occasioned by being required to perform the contract as agreed between the parties are not generally sufficient to frustrate a contract.[19] A contract will not be frustrated merely because one party has made a bad bargain or because the results that one party had expected or hoped for do not eventuate.[20] These risks are inherent in contracting.

In *Finlayson v Finlayson*,[21] the parties were husband and wife. They entered into a contract for the sale of a property from the wife's parents. The expectation was that the property would be the matrimonial home. Before the settlement of the contract, the parties separated. The parties commenced legal action, with the parents effectively seeking a declaration that they remained owners of the property. One of the arguments made by the parents was that the contract for the sale of land was frustrated by the breakdown of the marriage, with the result that the couple or, more pertinently, the husband, had no interest in the property. The Full Court of the Family Court held that the contract was not frustrated; "the contract … was simply one for the sale and purchase of real estate at an agreed 'market price' determined by an 'independent valuer' ".[22]

11 See, eg, Langille and Ripstein, "Strictly Speaking: It Went Without Saying" (1996) 2(1) *Legal Theory* 63; Morris, "Practical Reasoning and Contract as Promise: Extending Contract-Based Criteria to Decide Excuse Cases" (1997) 56(1) *Cambridge Law Journal* 147. See also [1.20].

12 See further Robertson, "The Limits of Voluntariness in Contract" (2005) 29(1) *Melbourne University Law Review* 179, 211–16.

13 See discussion in *National Carriers Ltd v Panalpina (Northern) Ltd* [1981] AC 675, 693.

14 See also Smith, *Contract Theory* (2006).

15 *Davis Contractors Ltd v Fareham UDC* [1956] AC 696, 728; *National Carriers Ltd v Panalpina (Northern) Ltd* [1981] AC 675, 693. But cf *Davis Contractors Ltd v Fareham UDC* [1956] AC 696, 719.

16 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 357.

17 See, eg, *Taylor v Caldwell* (1863) 3 B&S 826; 122 ER 309, discussed at [15.35].

18 See, eg, *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, discussed at [15.45].

19 See *Davis Contractors Ltd v Fareham UDC* [1956] AC 696, 729.

20 See, eg, *Scanlan's New Neon Ltd v Tooheys Ltd* (1943) 67 CLR 169; *Ross v IceTV* [2010] NSWCA 272.

21 *Finlayson v Finlayson* [2002] FamCA 898.

22 *Finlayson v Finlayson* [2002] FamCA 898, [107].

Some of the categories of event that have been held by the courts to frustrate a contract are discussed in the following sections. These categories are merely illustrative. Whether or not a particular contract is frustrated will depend on the circumstances of the case.

Illegality

[15.25] A contract may be frustrated where performance becomes illegal. Illegality may frustrate a contract in time of war due to a prohibition against dealing with the enemy.[23] Illegality may also frustrate a contract where, after the contract was made, the law changes to prohibit performance.[24]

Delay

[15.30] A contract may be frustrated by events that cause, or are likely to cause, an inordinate delay in the performance of the contract. The delay must be such as to seriously affect the intended performance of the contract; mere delay is not sufficient.[25] The question of whether a contract has been frustrated by delay is considered at the time when the event that gave rise to the delay occurred.[26] Accordingly, a contract may be treated as frustrated at the time a delay begins, on the basis that a long delay seems probable. Courts have taken the view that, particularly in a commercial contract, parties should not be required to wait and see how long the delay proves to be in fact before concluding that the contract is frustrated.[27]

An example is *Bank Line Ltd v Arthur Capel and Co*,[28] which involved a contract under which the shipowner agreed to let, and the charterer agreed to hire, a steamship for a period of 12 months. In May 1915, before the ship had been delivered to the charterers, the ship was requisitioned by the British Government to assist in the war effort. The ship was released on 2 September 1915. The House of Lords accepted that the charter had been frustrated by, and from the date of, the requisition. The important factor in reaching this conclusion was the probable length of the delay. The House of Lords pointed out that at the time the ship was requisitioned, the parties could not know when, if ever, the ship might be returned.

In assessing whether or not a contract is frustrated by delay, it may be relevant to compare the probable length of the delay with the remaining length of the contract. For this reason, long-term contracts may be less easily frustrated than short-term contracts.[29] In *National Carriers Ltd v Panalpina (Northern) Ltd*,[30] the lessee was denied access to a leased property for a period of 20 months out of a term of 10 years, with nearly three years left to run on the lease. The House of Lords considered that this delay was not sufficient to frustrate the contract.[31]

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23 See, eg, *Ertel Bieber and Co v Rio Tinto Co Ltd* [1918] AC 260.

24 See, eg, *Metropolitan Water Board v Dick Kerr & Co Ltd* [1918] AC 119; *Denny Mott & Dickson Ltd v James B Fraser & Co Ltd* [1944] AC 265.

25 See *Ringstad v Gollin & Co Pty Ltd* (1924) 35 CLR 303.

26 See *Bank Line Ltd v Arthur Capel and Co* [1919] AC 435; *Scanlan's New Neon Ltd v Tooheys Ltd* (1943) 67 CLR 169, 184.

27 *Bank Line Ltd v Arthur Capel and Co* [1919] AC 435, 454; *Pioneer Shipping Ltd v B T P Tioxide Ltd (The Nema)* [1982] AC 724, 752.

28 *Bank Line Ltd v Arthur Capel and Co* [1919] AC 435.

29 *National Carriers Ltd v Panalpina (Northern) Ltd* [1981] AC 675, 651.

30 *National Carriers Ltd v Panalpina (Northern) Ltd* [1981] AC 675.

31 See also *Ringstad v Gollin & Co Pty Ltd* (1924) 35 CLR 303.

Destruction of subject matter

[15.35] A contract is likely to be frustrated where the subject matter of the contract is destroyed. In *Taylor v Caldwell*,[32] the parties had entered into a contract for the use of a music hall for the purpose of giving a series of concerts and night fetes. After the contract was made, but before any concert was to be given, the hall was destroyed by fire. The plaintiffs lost money paid by them in preparing for the concerts, including in printing advertisements of, and in advertising, the concerts. The plaintiffs sought to recover this expenditure, alleging that the defendants had breached the contract. The Court held that the contract was frustrated. Accordingly, the owners of the hall were not liable for breach of contract for failing to make the hall available. The Court considered this conclusion was justified because the parties contracted on the basis of the continued existence of the hall and the existence of this subject matter was essential to the contract.[33] Applying a similar principle, the Sale of Goods Acts provide that an agreement to sell specific goods is avoided where the goods perish before the risk passes to the buyer.[34]

Disappearance of the basis of the contract

[15.40] A contract may be frustrated not only where the subject matter of the contract has been destroyed, but also where the event in question destroys the very basis or foundation of the contract. In *Krell v Henry*,[35] the parties had entered into a contract for the hire of rooms on Pall Mall on two dates. These were dates on which the coronation procession of King Edward VII would take place and pass along Pall Mall. The coronation was postponed due to the King's illness. The party hiring the rooms declined to pay the hire for them. The English Court of Appeal held that the contract was frustrated and thus no hire was owing. Having regard to the surrounding circumstances, the Court considered that the procession was "regarded by both contracting parties as the foundation of the contract".[36]

The decision has been criticised.[37] There was nothing that stopped the rooms being used. It might have been argued that the party hiring the rooms took the risk that the contemplated purpose of hiring the rooms, watching the procession, would not eventuate. In many subsequent cases, the risk of a cancelled event has been treated as allocated to the affected party.[38]

However, a modern example of the category of "frustrated purpose" is *Brisbane CC v Group Projects Pty Ltd*.[39] Group Projects owned land zoned as "future urban" which they wished to develop as a residential subdivision. The Brisbane City Council agreed to make the necessary application to have the land zoned as residential in consideration of Group Projects carrying out certain works if rezoning was approved, such as the construction of roads, footpaths, drains and other things appropriate for a residential subdivision. Much of

32 *Taylor v Caldwell* (1863) 3 B&S 826; 122 ER 309.

33 *Taylor v Caldwell* (1863) 3 B&S 826; 122 ER 309, 840.

34 *Sale of Goods Act 1954* (ACT), s 12; *Sale of Goods Act 1923* (NSW), s 12; *Sale of Goods Act* (NT), s 12; *Sale of Goods Act 1896* (Qld), s 10; *Sale of Goods Act 1895* (SA), s 7; *Sale of Goods Act 1896* (Tas), s 12; *Goods Act 1958* (Vic), s 12; *Sale of Goods Act 1895* (WA), s 7.

35 *Krell v Henry* [1903] 2 KB 740.

36 *Krell v Henry* [1903] 2 KB 740, 750.

37 See, eg, *Larrinaga & Co Ltd v Société Franco-Americaine des Phosphates de Médulla, Paris* (1923) 39 TLR 316, 318. Also *Maritime National Fish Ltd v Ocean Trawlers Ltd* [1935] AC 524, 529.

38 See, eg, *Herne Bay Steamboat Co v Hutton* [1903] 2 KB 683.

39 *Brisbane CC v Group Projects Pty Ltd* (1979) 145 CLR 143.

this work was to be carried out on sites other than the land in question. The rezoning was approved. Subsequently, the land was resumed by the Crown for development as a school. Group Projects therefore no longer owned the land and could not proceed with the proposed subdivision. The council contended that Group Projects' obligations remained in place. Those members of the High Court who considered the question found that the contract had been frustrated.[40] This was not a case where performance was rendered impossible. The bulk of the work was to be done off the land in question and was therefore unaffected by the resumption by the Crown. However, the acquisition of the land had "wholly destroyed Group Projects' " purpose in undertaking any obligations at all.[41]

The principle should not be taken too far. While in these two illustrations, the contracts were frustrated when an intervening event destroyed the very foundation of the contract, the same result will not apply merely because the contract cannot be performed as expected. *Scanlan's New Neon Ltd v Tooheys Ltd*[42] concerned contracts for the hire of neon advertising signs. The signs could not be illuminated at night due to war-time security orders. The High Court held that the contracts were not frustrated. The parties no doubt expected that the signs would be illuminated.[43] However, the lessees promised to pay the rent in absolute terms and the lessors did not warrant that the signs could be illuminated.[44] Latham CJ noted that:[45]

> When a man agrees to buy a pair of boots for himself, both parties expect that he will be able to wear them. If he has an accident, so that he can no longer wear boots, he nevertheless still has to pay for them. If a man buys or hires a motor car, both parties know that he expects to be able to drive it. The stoppage of the sale of petrol, which would make it impossible for him to drive it, does not excuse him from his obligation to pay the purchase money or the hire for the agreed period.

State of affairs essential to performance

[15.45] A contract may be frustrated by the disappearance of a state of affairs necessary to enable the contract to be performed in the manner contemplated by the parties. In *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales*,[46] the State Rail Authority of New South Wales (SRA) entered into a contract with Codelfa for the construction of certain parts of a railway. The common understanding of the parties in making the contract was that, in order to complete the work within the time specified in the contract, Codelfa would work three shifts per day. Codelfa and the SRA had received, and acted upon, erroneous legal advice that the contract work could not be impeded by the grant of an injunction to restrain a nuisance. In fact, local residents obtained an injunction restraining Codelfa from performing work on the construction site at night and on Sundays. Codelfa claimed from the SRA an amount additional to the price payable under the contract in respect of the additional costs that were incurred by it, and the profit it did not earn by reason of the change in working methods that it was constrained to adopt.

40 Stephen and Murphy JJ agreeing.

41 *Brisbane CC v Group Projects Pty Ltd* (1979) 145 CLR 143, 158.

42 *Scanlan's New Neon Ltd v Tooheys Ltd* (1943) 67 CLR 169.

43 *Scanlan's New Neon Ltd v Tooheys Ltd* (1943) 67 CLR 169, 194.

44 *Scanlan's New Neon Ltd v Tooheys Ltd* (1943) 67 CLR 169, 194, 217.

45 *Scanlan's New Neon Ltd v Tooheys Ltd* (1943) 67 CLR 169, 191.

46 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337.

The High Court refused to imply a term into the contract that would give Codelfa the requested relief. The Court instead found that the contract was frustrated.[47] The Court considered that the granting of the injunction made the situation in which performance was to occur fundamentally different from the situation contemplated by the parties, as revealed by the construction of the contract in the light of the surrounding circumstances.[48] The injunction meant that the contractor could not do the work according to the schedule contemplated by the parties.

A change in the state of affairs affecting performance may not frustrate the contract where there is an alternative method of performance which, although more onerous, is not radically different from that contemplated under the contract. An example is *Tsakiroglou and Co Ltd v Noblee Thorl GmbH*,[49] which involved a contract for the sale of goods to be shipped from the Port of Sudan to Hamburg. The goods were to have been shipped via the Suez Canal. When the Canal was closed, the alternative route was around the Cape of Good Hope. This route took more than twice as long and was, accordingly, more expensive. Nonetheless, the Court held that the contract was not frustrated. In the circumstances of the case, an alternative to the usual route was available. The greater cost of that route was not a ground for frustration.[50]

The distinction between an event that renders performance radically different and so frustrates the contract, and an event that merely makes performance more onerous, will sometimes be a fine one. As in all frustration cases, the issue must depend on the court's assessment of the facts of the particular case.

Death or incapacity of a party

[15.50] A contract may be frustrated by the death or permanent incapacity of a party whose existence is essential to performance of the contract.[51] An example of such a contract is an employment contract that relies on the personal skills of the employee.[52] Employment contracts often contain, or are affected by, provisions specifically dealing with issues of illness and incapacity, which may exclude the application of the doctrine of frustration.[53]

Contracts involving land

[15.55] The doctrine of frustration applies to contracts for the sale of land, but its application is restricted.[54] The reasons for the restriction relate to the special nature of contracts involving land. In particular, the general common law rule is that the risk of loss passes to the purchaser of land as soon as the contract is made. Under this rule, if buildings on the land are damaged

47 Stephen, Mason, Aickin, and Wilson JJ. Brennan J dissented.

48 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 363, 381.

49 *Tsakiroglou and Co Ltd v Noblee Thorl GmbH* [1962] AC 93.

50 See also *Ocean Tramp Tankers Corp v V/O Sovfracht (The Eugenia)* [1964] 2 QB 226.

51 See, eg, *Lobb v Vasey Housing Auxiliary (War Widows Guild)* [1963] VR 239; *Chapman v Taylor* [2004] NSWCA 456. Cf *Ezishop.com Ltd v Veremu Pty Ltd* [2003] NSWSC 156 (insolvency of company did not frustrate the contract).

52 See, eg, *Simmons Ltd v Hay* (1964) 81 WN (Pt 1) (NSW) 358; *FC Shepherd & Co Ltd v Jerrom* [1987] QB 301.

53 See further *Finch v Sayers* [1976] 2 NSWLR 540, but cf *Notcutt v Universal Equipment Co (London) Ltd* [1986] 1 WLR 641.

54 *Scanlan's New Neon Ltd v Tooheys Ltd* (1943) 67 CLR 169, 229. See also Greig and Davis, *The Law of Contract* (1987), pp 1323–31.

or destroyed, the purchaser bears the loss and the contract is not frustrated.[55] A contract for the sale of land might be frustrated by catastrophic events affecting the land itself. For example, in *Wong Lai Ying v Chinachem Investment Co Ltd*,[56] a contract for the sale of flats in a tower block was frustrated by a landslip that significantly delayed the building of the tower block. In *McRoss Developments Pty Ltd v Caltex Petroleum Pty Ltd*,[57] a contract was frustrated by compulsory acquisition of the land by the government.

In *National Carriers Ltd v Panalpina (Northern) Ltd*,[58] the House of Lords considered that there was no good reason why the doctrine of frustration should not apply to a lease. The position in Australia is, however, uncertain. In *Firth v Halloran*, Knox CJ and Gavan Duffy J endorsed the decision of the Full Court of the Supreme Court of New South Wales[59] that the doctrine of frustration does not apply to a lease.[60] In *Progressive Mailing House Pty Ltd v Tabali Pty Ltd*[61] the High Court held that the general principles of contract law apply to leases, but expressly reserved decision on the application of the doctrine of frustration. More recently, some lower courts have been prepared to accept that the doctrine of frustration applies to a contract for a lease.[62]

Assuming that the doctrine of frustration does apply to leases, it may be suggested that, as with contracts for the sale of land, cases of frustration will be "extremely rare".[63] For example, it has been suggested that a lease might be frustrated if "some vast convulsion of nature swallowed up the property altogether, or buried it in the depths of the sea".[64]

WHEN SHOULD A CONTRACT BE FRUSTRATED?

[15.60] The modern test for frustration is based on the construction of the contract.[65] In what circumstances should a court find that disruptive events have caused the performance of the contract to be sufficiently different from that contemplated under the contract that the contract should be frustrated? The cases we have discussed illustrate that a contract will be frustrated only in exceptional circumstances.[66] For a contract to be frustrated, the circumstances in which performance is called for must be radically or fundamentally different from those undertaken by the parties at the time of making their contract. Is this high standard for what amounts to a frustrating event appropriate?

55 See, eg, *Fletcher v Manton* (1940) 64 CLR 37.

56 *Wong Lai Ying v Chinachem Investment Co Ltd* (1979) 13 Build LR 81.

57 *McRoss Developments Pty Ltd v Caltex Petroleum Pty Ltd* [2004] NSWSC 183.

58 *National Carriers Ltd v Panalpina (Northern) Ltd* [1981] AC 675.

59 *Halloran v Firth* (1926) 26 SR (NSW) 18.

60 *Firth v Halloran* (1926) 38 CLR 261.

61 *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17.

62 *City of Subiaco v Heytesbury Properties Pty Ltd* [2001] WASCA 140; (2001) 24 WAR 146; *Tim Barr Pty Ltd v Narui Gold Coast Pty Ltd* [2010] NSWSC 29.

63 *City of Subiaco v Heytesbury Properties Pty Ltd* [2001] WASCA 140; (2001) 24 WAR 146.

64 *Cricklewood Property and Investment Trust Ltd v Leighton's Investment Trust Ltd* [1945] AC 221, 229. See also *National Carriers Ltd v Panalpina (Northern) Ltd* [1981] AC 675, 691, 700–1, 713.

65 See [15.15].

66 *Bank Line Ltd v Arthur Capel and Co* [1919] AC 435, 459; *Davis Contractors Ltd v Fareham Urban District Council* [1956] AC 696, 715; *J Lauritzen AS v Wijsmuller BV (The "Super Servant Two")* [1990] 1 Lloyd's Rep 1, 8.

Those drawing on relational contract theory might suggest a more flexible approach to determining when a contract is frustrated. Macneil has argued that the rules regulating changes to a contractual relationship should take into account the broad social norms relevant to that relationship.[67] Hillman, influenced by the work of Macneil, proposes that in the application of a doctrine such as frustration, courts should be guided by "fairness norms".[68] These norms include balancing the equities between the parties, avoiding harm to parties, rewarding a party who has behaved reasonably, and ensuring parties benefit from the contract roughly according to the contract allocation.[69] Trebilcock criticises the relational approach as failing to provide any determinative principles for guiding courts.[70]

Posner and Rosenfield apply an economic analysis to argue that discharge of a contract for frustration should be allowed when the promisee (ie, the party seeking performance) is the superior risk bearer. In assessing which party is the superior risk bearer, Posner and Rosenfield identify as relevant factors which party can estimate the probability of loss, which party can best estimate the magnitude of the loss, and which party is better placed to reduce the transaction costs of insurance.[71] Trebilcock criticises this approach as uncertain, noting that when applied to the facts of many cases, the criteria often point in different directions.[72]

Applying an economic analysis, Triantis suggests that while contracting parties will not be able to foresee all of the risks that might disrupt performance of their contract, this does not mean that the risk of unforeseen events has not been allocated by the parties at the time of making their contract. At least parties entering into a commercial contract are likely to be aware of the risk of disruptive events in a more general sense.[73] Triantis explains that risks that cannot be specifically foreseen may be "priced and allocated as part of the package of a more broadly framed risk".[74]

> For example, consider a party who agrees to transport a shipment of goods for a fixed fee. The risk of a nuclear accident in the Middle East that causes a dramatic decrease in the production of oil and a consequent increase in its price might not be foreseen. As a result, this risk cannot be allocated explicitly in the contract. However, the broader risk of a large increase in the

67 See, eg, Macneil, "Contracts: Adjustment of Long-term Economic Relations under Classical, Neoclassical, and Relational Contract Law" (1977–78) 72(6) *Northwestern University Law Review* 854.

68 Hillman, "An Analysis of the Cessation of Contractual Relations" (1983) 68(5) *Cornell Law Review* 617 and Hillman, "Court Adjustment of Long-term Contracts: An Analysis under Modern Contract Law" [1987] *Duke Law Journal* 1. For a feminist perspective on this approach, see Frug, "Rescuing Impossibility Doctrine: A Postmodern Feminist Analysis of Contract Law" (1992) 140(3) *University of Pennsylvania Law Review* 1029.

69 Hillman, "An Analysis of the Cessation of Contractual Relations" (1983) 68(5) *Cornell Law Review* 617, 618–19, 629–39.

70 Trebilcock, *The Limits of Freedom of Contract* (1993), pp 141–2.

71 Posner and Rosenfield, "Impossibility and Related Doctrines in Contract Law: An Economic Analysis" (1977) 6(1) *Journal of Legal Studies* 83.

72 Trebilcock, "The Role of Insurance Considerations in the Choice of Efficient Civil Liability Rules", (1988) 4(2) *Journal of Law, Economics and Organization* 243, 249–55 and Trebilcock, *The Limits of Freedom of Contract* (1993), pp 132–41. See also Triantis, "Contractual Allocations of Unknown Risks: A Critique of the Doctrine of Commercial Impracticability" (1992) 42(4) *University of Toronto Law Journal* 450, 476–7.

73 Triantis, "Contractual Allocations of Unknown Risks: A Critique of the Doctrine of Commercial Impracticability" (1992) 42(4) *University of Toronto Law Journal* 450.

74 Triantis, "Contractual Allocations of Unknown Risks: A Critique of the Doctrine of Commercial Impracticability" (1992) 42(4) *University of Toronto Law Journal* 450, 452.

> price of oil for any reason can be. Therefore, there is no gap to be filled by the doctrine of [frustration]: the risk of nuclear accident, although unforeseen, is allocated implicitly.[75]

Trebilcock agrees, arguing that in commercial contracts, the parties' failure in their contract to specify a response to a particular risk will usually indicate an intention to assign that general category of risk to the party affected.[76] Accordingly, Trebilcock supports an "austere" rule that restricts frustration to "exceptional cases of outlandish risks".[77] Only these sorts of risks are unlikely to have been foreseen and allocated by the parties either specifically or in a general sense.

LIMITS ON THE DOCTRINE

[15.65] There are three important limitations on the doctrine of frustration. First, the risk of the frustrating event must not have been provided for by the parties in their contract. Second, the event must not have been foreseeable by the parties at the time of making their contract. Third, the frustrating event must have occurred without fault by the party seeking to rely on frustration.

Express provision in the contract

Ways of providing expressly for disruptive events

[15.70] The first limitation on the doctrine of frustration is that a contract will not be frustrated where the parties have expressly provided in their contract for the consequences of the particular event that has occurred.[78] Clearly, the occurrence of an event provided for in the contract will not make performance radically different from that contemplated by the parties when making their contract.

There are a number of different ways a contract may allocate the risk of disruptive events. For example, the parties may provide that one of them bears the risk of the event occurring or the parties may agree that the risk be shared between them. In commercial contracts contemplated to last over a long period of time, parties may include a broad catch-all provision known as a *force majeure clause*.[79] A force majeure clause will list a large range of categories of otherwise potentially frustrating events, ranging from lightning strikes, earthquakes and floods to acts of war and terrorism. Should one of the events occur, force majeure clauses frequently suspend performance by providing that the contract is not to come to an end unless the event has continued for a specified period of time and/or is incapable of remedy by one of the parties within a specified time. The clause will also commonly specify the consequences for the parties of suspension or termination of the contract.

When does a clause in a contract exclude frustration?

[15.75] Whether or not a clause in a contract excludes the doctrine of frustration is a matter of construction. The fact that a clause specifies the consequences of a broad

75 Triantis, "Contractual Allocations of Unknown Risks: A Critique of the Doctrine of Commercial Impracticability" (1992) 42(4) *University of Toronto Law Journal* 450, 452.

76 See Trebilcock, *The Limits of Freedom of Contract* (1993), pp 127–30, 144.

77 Trebilcock, *The Limits of Freedom of Contract* (1993), p 145.

78 *Joseph Constantine Steamship Line Ltd v Imperial Smelting Corp Ltd* [1942] AC 154, 163. See also generally McKendrick (ed), *Force Majeure and Frustration of Contract* (2nd ed, 1995).

79 See, eg, *Yara Nipro P/L v Interfert Australia P/L* [2010] QCA 128.

class of potentially disruptive events does not necessarily prevent the contract from being frustrated by an event apparently within that class.[80] Courts may take the view that the event that has occurred was of a different character from that which could have been contemplated by the parties when making their contract. In such a case, the court may consider that the clause should be construed narrowly so as not to apply to the event and that the contract should instead be treated as frustrated. This possible interpretation of a clause is illustrated by the decision in *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales*.[81]

As already discussed,[82] in *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales*, the contract was found to be frustrated after the grant of an injunction prevented work being carried out in the manner contemplated by the parties. The contract contained clauses dealing with the possibility of a major restriction of working hours and of measures being taken to reduce noise and pollution. The Court considered that these provisions did not bar the contract from being frustrated. The provisions were "quite consistent with the contemplated method of work being an essential element of the contract".[83] In other words, it seemed that the provisions only operated in the context of the work proceeding as contemplated by the parties.

In some cases, the fact that the parties have expressly provided for the consequences of certain disruptive events may support the conclusion that the parties intended the risk of events that are not specified to be borne by the party affected. For example, in *Meriton Apartments Pty Ltd v Mclaurin & Tait (Developments) Pty Ltd*,[84] the parties had entered into a contract for a group of properties in Sydney. The purchaser proposed to redevelop the properties, and the contract was subject to the relevant council approving the development application. Such approval was given. The property then became the subject of "green bans", embargos imposed by certain trade unions that opposed the proposed development of the land. The High Court held that the imposition of the green bans did not frustrate the contract. Although the imposition of the bans reduced the value of the land and prevented the use of the land for the purpose for which the purchaser bought it, the Court considered that this was not enough to frustrate the contract. The availability of the land for the purchaser's proposed purpose was not a term of the contract. Moreover, the Court considered that the term relating to council approval was significant. The Court accepted the view of the trial judge that the assignment of this one risk affecting the development to the vendor left all other risks to be borne by the purchaser.[85]

Foreseen events

[15.80] The second limitation on the doctrine of frustration is that the purported frustrating event must not be one that the parties could "reasonably be thought to have

80 See, eg, *Bank Line Ltd v Arthur Capel and Co Ltd* [1919] AC 435, 455–6; *Metropolitan Water Board v Dick Kerr & Co* [1918] AC 119; *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337.

81 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337.

82 See [17.45].

83 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 362.

84 *Meriton Apartments Pty Ltd v Mclaurin & Tait (Developments) Pty Ltd* (1976) 133 CLR 671.

85 *Meriton Apartments Pty Ltd v Mclaurin & Tait (Developments) Pty Ltd* (1976) 133 CLR 671, 678.

foreseen".[86] Where an event could reasonably have been foreseen, it may be presumed that the parties have, at least implicitly, allocated the risk of the event occurring to the party affected. If the parties had wanted a different result, then they could have included provisions to this effect in their contract.

In *Davis Contractors Ltd v Fareham UDC*,[87] a builder agreed to build 78 houses for a fixed price, with the work to be completed in eight months. Owing to bad weather and a shortage of labour and materials, the work took 22 months to complete. The builder claimed that the contract had been frustrated and further claimed £17,000 as reasonable remuneration for the work that had been done. The House of Lords held that the contract had not been frustrated. One reason was that the cause of delay should have been foreseen by the parties: "the possibility of enough labour and materials not being available was before their eyes and could have been the subject of special contractual stipulation".[88]

Despite the fact that foresight is commonly expressed as a limitation on the doctrine of frustration, the concept is not entirely straightforward.[89] We might ask whether or not there is some threshold level of probability at which the event in question must reasonably have been foreseen to preclude the event from frustrating the contract.[90] For example, an event might have been contemplated but then dismissed by the parties as improbable. We might also ask whether or not there should be some threshold level of particularity with which the event must have reasonably been foreseen. For example, the parties might have foreseen the risk of a particular event in a general sense, but the effect of the event, when it occurs, might go well beyond what the parties contemplated.[91]

Fault and self-induced frustration

[15.85] The third limitation on frustration is that the frustrating event must arise without blame or fault by the party seeking to rely on the contract being frustrated.[92] The rationale for qualifying the doctrine of frustration in this way is that a party should not be able to rely on an event as discharging him or her from performance of a contract that he or she has had the means and opportunity of preventing.[93]

The meaning of "fault"

[15.90] The "fault" that will preclude a party from relying on a contract being frustrated has not been precisely defined.[94] It is established that a party cannot rely on an event as frustrating

86 *Davis Contractors Ltd v Fareham UDC* [1956] AC 696, 731. See also *Krell v Henry* [1903] 2 KB 740, 751; *Paal Wilson & Co A/S v Partenreederei* [1983] 1 AC 909; *Codelfa Construction Pty Ltd v State Rail Authority of NSW* (1982) 149 CLR 337, 359.

87 *Davis Contractors Ltd v Fareham UDC* [1956] AC 696.

88 *Davis Contractors Ltd v Fareham UDC* [1956] AC 696, 731.

89 See also *Beaton v McDivitt* (1987) 13 NSWLR 162 at 176–7; *Ooh! Media Roadside Pty Ltd (formerly Power Panels Pty Ltd) v Diamond Wheels Pty Ltd & Anor* [2011] VSCA 116; (2011) 32 VR 255, [72]–[75].

90 Treitel, *Frustration and Force Majeure* (2nd ed, 2004), [13-012].

91 See *Tatem v Gamboa* [1939] 1 KB 132 at 135; *Simmons Ltd v Hay* (1964) 81 WN (Pt 1) (NSW) 358; *Pioneer Shipping Ltd v BTP Tioxide Ltd (The Nema)* [1982] AC 724.

92 *Bank Line Ltd v Arthur Capel & Co* [1919] AC 435, 452; *Paal Wilson and Co A/S v Partenreederei Hannah Blumenthal (The Hannah Blumenthal)* [1983] 1 AC 854, 909; *J Lauritzen AS v Wijsmuller BV (The "Super Servant Two")* [1990] 1 Lloyd's Rep 1, 8.

93 *J Lauritzen AS v Wijsmuller BV (The "Super Servant Two")* [1990] 1 Lloyd's Rep 1, 10.

94 See Peel, *Treitel's Law of Contract* (Sweet & Maxwell, 14th ed, 2015) [19-082]–[19-089].

a contract where such an event was caused by that party's own breach of contract.[95] Further, a party may not be able to rely on an event that was caused by the deliberate act of that party as frustrating a contract, even though the act was not a breach of the contract.[96] For example, an employer, but not an employee, may be able successfully to claim that an employment contract is frustrated where the employee is imprisoned for a criminal offence.[97]

In some circumstances, negligence may amount to fault, disqualifying a party from relying on frustration. For example, a shipper may not be able to rely on the sinking of the ship as frustrating a contract for the carriage of goods where the ship is lost as a result of the carelessness of the shipper.[98] The degree to which negligence should be relevant in assessing whether a contract has been frustrated has not been settled, particularly in relation to contracts for personal performance. It is established that a contract for personal services may be frustrated where the employee becomes ill or dies.[99] It is uncertain what the result should be if this incapacity is caused by some want of care on the part of the employee. Thus, as Lord Simon explained in *Joseph Constantine Steamship Line Ltd v Imperial Smelting Corp Ltd*:

> Some day it may have to be finally determined whether a prima donna is excused by complete loss of voice from an executory contract to sing if it is proved that her condition was caused by her carelessness in not changing her wet clothes after being out in the rain.[100]

The innocent party

[15.95] Fault by one party in producing a frustrating event does not preclude the other innocent party from relying on frustration.[101] This means that an innocent party may rely on an event as frustrating a contract where the event was produced by the fault of the other party and thus, where the other party would not be able to rely on the event as frustrating the contract. The onus of proof is on the party alleging that the frustration was induced by the other party's fault.[102]

THE CONSEQUENCES OF FRUSTRATION

General effect of frustration

[15.100] Once a contract is frustrated, the contract is brought to an end automatically and there is no requirement for either of the parties to elect to terminate.[103] Frustration discharges

95 See, eg, *Mertens v Home Freeholds Co* [1921] 2 KB 526; *Ocean Tramp Tankers Corp v V/O Sovfracht (The Eugenia)* [1964] 2 QB 226, 237, 243; *Paal Wilson and Co A/S v Partenreederei Hannah Blumenthal (The Hannah Blumenthal)* [1983] 1 AC 854.

96 *Denmark Productions Ltd v Boscobel Productions Ltd* [1969] 1 QB 699, 725, 736; *F C Shepherd & Co Ltd v Jerrom* [1987] 1 QB 320. See also *Maritime National Fish Ltd v Ocean Trawlers Ltd* [1935] AC 524.

97 *F C Shepherd & Co Ltd v Jerrom* [1987] 1 QB 320.

98 *J Lauritzen AS v Wijsmuller BV (The "Super Servant Two")* [1990] 1 Lloyd's Rep 1.

99 *Lobb v Vasey Housing Auxiliary (War Widows Guild)* [1963] VR 239; *Chapman v Taylor* [2004] NSWCA 456.

100 *Joseph Constantine Steamship Line Ltd v Imperial Smelting Corp Ltd* [1942] AC 154, 166. The point was raised but not pursued in *Chapman v Taylor* [2004] NSWCA 456, [8].

101 *F C Shepherd & Co Ltd v Jerrom* [1987] 1 QB 320.

102 *Joseph Constantine Steamship Line Ltd v Imperial Smelting Corp Ltd* [1942] AC 154.

103 *Scanlan's New Neon Ltd v Tooheys Ltd* (1943) 67 CLR 169, 203; *J Lauritzen AS v Wijsmuller BV (The "Super Servant Two")* [1990] 1 Lloyd's Rep 1, 8.

the parties from most future obligations under the contract.[104] Thus, a party will not be liable for failing to perform those of his or her obligations falling due after the frustrating event. The qualification on this principle is that terms regulating the parties' future relationship may survive frustration of the contract if intended to do so by the parties.[105] An example of a term likely to be intended to survive frustration is an arbitration clause, requiring the parties to submit disputes under the contract to arbitration.[106]

At common law, rights and liabilities which have unconditionally accrued prior to the time of the frustrating event will remain in place.[107] This approach produces somewhat unsatisfactory results, and legislation has been enacted in some Australian jurisdictions to deal with the issue.[108] Nonetheless, it remains necessary to understand the common law rules. Not all contracts are covered by the legislation. Moreover, the common law rules produce the situation that the legislation is designed to address.

The consequences of frustration under the common law

[15.105] For the purpose of analysing the common law rules regulating the parties' rights and liabilities under a frustrated contract, it is useful to distinguish between claims for the recovery of money paid, or due to be paid, prior to the frustrating event, and claims for payment for work done prior to the frustrating event.

Money payable under the contract

[15.110] A party (the *paying party*) may sometimes make, or have been required to make, payment to the other party under the contract before its completion. From the perspective of a party providing goods or services, a requirement for pre-payment makes good sense, reducing the risk of non-payment due to insolvency. If the contract is frustrated, then the paying party may want to recover any payments made or, if the payment has not yet been made, to be discharged from the obligation to pay.

At common law, the rights of the parties in relation to payments made, or due, before the contract was frustrated depend on whether there has been a total failure of consideration. A paying party will be entitled to restitution (ie, repayment) of money he or she has paid under a frustrated contract where the consideration for that payment has totally failed.[109] "Consideration" under this doctrine has a broader meaning than that in regard to contract formation. In contract formation, consideration usually takes the form of a promise given as the price of a counter-promise.[110] Under the doctrine of total failure of consideration,

104 *Hirsch v The Zinc Corp Ltd* (1917) 24 CLR 34, 64; *Fibrosa Spolka Akcyjina v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32.

105 *BP Exploration Co (Libya) Ltd v Hunt (No 2)* [1979] 1 WLR 783, 829 (affirmed on appeal: *Fibrosa Spolka Akcyjina v Fairbairn Lawson Combe Barbour Ltd* [1983] 2 AC 352).

106 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 363–7, 392; *Paal Wilson & Co A/S v Partenreederei Hannah Blumenthal* [1983] 1 AC 854, 917.

107 *Joseph Constantine SS Line Ltd v Imperial Smelting Corp Ltd* [1942] AC 154, 170.

108 *Frustrated Contracts Act 1978* (NSW); *Frustrated Contracts Act 1988* (SA); *Australian Consumer Law and Fair Trading Act 2012* (Vic), Pt 3.2.

109 See *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32. Also on total failure of consideration, see [10.25] and [10.80].

110 See Chapter 4.

consideration refers to performance of the promise.[111] In other words, a party will be entitled to recover a payment made under a contract that later becomes frustrated where he or she has not received any of the performance that the money was paid to secure. In such circumstances, a party will also be released from the obligation to pay any money that has fallen due.

The operation of the principle of total failure of consideration is illustrated by the decision in *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd*.[112] That case involved a contract made in 1939 between the sellers, an English company, and the purchasers, a Polish company, for the sale of machinery at a price of £4800. In accordance with the contract, the purchasers made an initial payment to the sellers of £1000. Later that year, Germany invaded Poland and Britain declared war on Germany. The contract was found to be frustrated. The issue then was what should happen to the £1000 paid to the sellers. The purchasers requested the return of the money. The sellers sought to retain the money on the basis that they had done considerable work in manufacturing the machinery. The House of Lords held that the purchasers could recover their £1000 because there had been a total failure of the consideration supporting the payment. Although the seller had incurred expenses in preparing to perform the contract, the consideration in this case was the delivery of the machinery, which had not taken place.

The *Fibrosa* case illustrates that the mere fact that a party has incurred expenses in preparing to perform a contract does not prevent there being a total failure of consideration. At common law, if no actual performance has been rendered, then money paid towards the performance contracted for cannot be kept to cover expenses. Moreover, for there to be a common law right to restitution of money paid under a frustrated contract on the basis of failure of consideration, the failure must be total, not partial.[113] The common law does not allow apportionment of contractual payments to reflect a partial performance of the contract. This means that a party who has received part of the performance bargained for under a contract will not be entitled to recover a payment made in respect of that performance, even though the performance, being only partial, does not equal the value of the payment that has been made.

Payment for work done

[15.115] The converse of the situation just discussed is where a party has performed work, under a contract prior to its being frustrated, for which he or she has not yet been paid. After the contract is frustrated, the party who has performed is likely to want to claim payment for the work done. If the contract provides a right to payment for the portion of the work that has been done, then the performing party will be able to seek payment in accordance with the contract. This is because rights that accrue before a contract is frustrated remain effective.[114]

A party who has fully performed his or her obligations before the contract was frustrated is likely to have a contractual right to payment. There may not be a contractual right to payment for only partial performance of a contract.[115] A performing party who has partially performed

111 *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32, 48, 72.

112 *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32.

113 *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32; *Bank of Boston Connecticut v European Grain and Shipping Ltd* [1989] AC 1056, 1108.

114 *Joseph Constantine SS Line Ltd v Imperial Smelting Corp Ltd* [1942] AC 154, 170.

115 On the degree of performance which will entitle a party to the contract price, see [29.30].

a contract, but who has no contractual right to payment for that work, may not be entitled to a claim in restitution for a reasonable remuneration for the work done, known as a recovery on a quantum meruit.[116]

The leading authority on this point is *Cutter v Powell*.[117] That case concerned a contract whereby a sailor (Cutter) was employed to act as second mate on a ship sailing from Jamaica to Liverpool. The letter of engagement provided that he would be paid "the sum of thirty guineas, provided he proceeds, continues and does his duty as second mate in the said ship from hence to the port of Liverpool". The lump sum payment envisaged by the letter was considerably higher than normally paid for the voyage. Cutter died approximately three-quarters of the way through the journey. Cutter was not entitled to payment under the contract unless the whole of his duties was performed and the Court held that no claim could be made on a quantum meruit.[118] The principle for which the case is usually cited as authority, that restitution for work done under an entire contract[119] will not be available if the contract is frustrated before the performance is complete, might be given a more limited application on the facts of the case. As discussed in Chapter 10, the case might be better seen as one in which restitution was not available because the contract placed on Cutter the risk of performance not being completed.[120]

Work done after a contract is frustrated

[15.120] The position in relation to work done *before* a contract is frustrated may be contrasted with the position in relation to work done *after* the contract was frustrated. A party may succeed in a claim in restitution for reasonable remuneration for work done *after* the contract was discharged by frustration.[121]

Inequities in the common law position

[15.125] The common law approach to frustration is largely to leave the losses caused by the frustration of the contract with the party on whom they fall.[122] As just discussed, there are a number of consequences that may result from this approach. Frustration of a contract may mean that a party who has paid money under the contract, and received very little of the promised performance in return, will not be entitled to recover that payment.[123] Alternatively, a party who has partially performed a contract may not be entitled to any payment for that performance.[124] Moreover, a party who has incurred expenses in preparing to perform the contract may have no right to recover even part of those expenses.[125]

116 See [10.45] and [10.80].

117 *Cutter v Powell* (1795) 6 TR 320.

118 See also *Appleby v Myers* (1867) LR 2 CP 651; *Hirsch v The Zinc Corp Ltd* (1917) 24 CLR 34; *Re Continental C & G Rubber Co Pty Ltd* (1919) 27 CLR 194. Cf *Pavey & Matthews Pty Ltd v Paul* (1987) 162 CLR 221, 256.

119 An entire contract is one that requires a party to perform his or her obligations in full before he or she will be entitled to payment: see further at [29.15].

120 See [10.80].

121 See, eg, *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 150 CLR 29.

122 See generally the comments in *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32.

123 See [15.110].

124 See [15.115].

125 See, eg, *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32, discussed at [15.110].

The justification for this approach is that contracting parties are generally entitled to act in their own interests, and thus there is no reason to require them to apportion losses arising from frustration.[126] Nonetheless, there are many commentators who are critical of the common law approach to the consequences of frustration. They argue that a fairer response would be for losses to be shared equitably between the parties.[127] This approach is advocated on the ground that both parties are innocent with regards to a frustrating event in the sense that neither could have foreseen the event that occurred, and neither was at fault in causing it.

The statutory response to the consequences of frustration

[15.130] New South Wales, South Australia and Victoria have passed legislation that is aimed at ameliorating at least some of the harsh consequences of frustration at common law.[128] The legislation does not seek to define when a contract is frustrated, leaving common law principles in that regard in place. Once a contract is frustrated, the legislation seeks to distribute some of the cost of frustration between the parties. The significant provisions are outlined briefly at [15.140]–[15.150].[129]

Contracts not covered

[15.135] All three Acts dealing with the consequences of frustration exclude a number of different types of contracts from their operation, in particular contracts for the carriage of goods by sea, certain types of charter party and insurance contracts.[130] The parties may also, themselves, exclude the operation of the Acts.[131]

New South Wales

[15.140] The *Frustrated Contracts Act 1978* (NSW) seeks to apportion the losses caused by frustration between the parties through detailed provisions aimed at establishing a complete code for adjusting the parties' rights.[132] There are four main situations contemplated by the Act. First, the Act requires the return of money paid before the contract was frustrated.[133] Second, where expenses have been incurred for the purpose of performance of the contract that is not rendered, the Act provides for the loss relating to those expenses to be shared between the parties.[134] Third, where a party has performed his or her obligations under the contract,

126 See Stewart, "The South Australian Frustrated Contracts Act" (1992) 5(3) *Journal of Contract Law* 220, 226–7.

127 See, eg, Fried, *Contract as Promise* (1981), p 71; Hillman, "An Analysis of the Cessation of Contractual Relations" (1983) 68(5) *Cornell Law Review* 617 and Hillman, "Court Adjustment of Long-term Contracts: An Analysis under Modern Contract Law" [1987] *Duke Law Journal* 1; Trebilcock, *The Limits of Freedom of Contract* (1993), p 145.

128 *Frustrated Contracts Act 1978* (NSW); *Frustrated Contracts Act 1988* (SA); *Australian Consumer Law and Fair Trading Act 2012* (Vic), Pt 3.2.

129 On the legislation dealing with frustrated contracts, see further Greig and Davis, *The Law of Contract* (1987), pp 1336–50; Stewart and Carter, "Frustrated Contracts and Statutory Adjustment" [1992] *Cambridge Law Journal* 66; Stewart, "The South Australian Frustrated Contracts Act" (1992) 5(3) *Journal of Contract Law* 220.

130 *Frustrated Contracts Act 1978* (NSW), s 6(1)(b)–(d), (2), (3); *Frustrated Contracts Act 1988* (SA), s 4(2); *Australian Consumer Law and Fair Trading Act 2012* (Vic), s 35(3).

131 *Frustrated Contracts Act 1978* (NSW), s 6(1)(e); *Frustrated Contracts Act 1988* (SA), s 4(1)(b); *Australian Consumer Law and Fair Trading Act 2012* (Vic), s 41.

132 See *Frustrated Contracts Act 1978* (NSW), ss 10–15.

133 *Frustrated Contracts Act 1978* (NSW), s 12.

134 *Frustrated Contracts Act 1978* (NSW), s 13.

the Act provides for compensation to be paid.[135] Fourth, where only partial performance has been rendered, the Act sets out complex provisions for valuing the compensation to be paid for that performance.[136] The amount payable depends on the extent to which the acts performed were beneficial to the other party. The court may disregard the detailed adjustment provisions where their application would be "manifestly inadequate or inappropriate", would cause "manifest injustice", or would be "excessively difficult or expensive".[137]

South Australia

[15.145] The *Frustrated Contracts Act 1988* (SA) seeks to apportion the losses caused by frustration between the parties. It does this through the following guiding principle: "[w]here a contract is frustrated, there will be an adjustment between the parties so that no party is unfairly advantaged or disadvantaged in the consequences of frustration."[138]

The Act provides guidelines for how the adjustment between the parties is to be made.[139] Nonetheless, the Act gives a discretion to the court to proceed on a "more equitable basis".[140]

Victoria

[15.150] The provisions dealing with frustrated contracts in the *Australian Consumer Law and Fair Trading Act 2012* (Vic), Pt 3.2,[141] do not seek to apportion or share the losses caused by frustration between the parties. Instead, the provisions adjust the parties' rights in three main respects. First, the provisions provide for the recovery of sums paid before a contract was frustrated and, similarly, the release of the obligation to pay sums payable before a contract was frustrated.[142] Second, in cases where money has been paid or was payable under the contract (and only in these cases), the provisions provide for a party who has incurred expenses for the purpose of performing the contract to recover remuneration for those expenses out of the sum payable where the court "considers it just to do so having regard to all the circumstances of the case".[143] Third, the provisions provide for a party who has obtained a valuable benefit before the contract is frustrated to pay for that benefit as the court considers just.[144]

UNIDROIT Principles of International Commercial Contracts

[15.155] A different approach to events disrupting performance of a contract is found in the *UNIDROIT Principles of International Commercial Contracts 2010* (UPICC).[145] The UPICC

135 *Frustrated Contracts Act 1978* (NSW), s 10.

136 *Frustrated Contracts Act 1978* (NSW), s 11.

137 *Frustrated Contracts Act 1978* (NSW), s 15.

138 *Frustrated Contracts Act 1988* (SA), s 7(1).

139 *Frustrated Contracts Act 1988* (SA), s 7(2).

140 *Frustrated Contracts Act 1988* (SA), s 7(4).

141 Based on the *Law Reform (Frustrated Contracts) Act 1943* (Imp), 6 and 7 Geo 6, c 40.

142 See *Fair Trading Act 1999* (Vic), s 36.

143 *Australian Consumer Law and Fair Trading Act 2012* (Vic), s 37. See further *Lobb v Vasey Housing Auxiliary (War Widows Guild)* [1963] VR 239; *BP Exploration Co Libya Ltd v Hunt (No 2)* [1979] 1 WLR 783, affirmed [1983] 2 AC 352.

144 *Australian Consumer Law and Fair Trading Act 2012* (Vic), s 38.

145 See also [1.180].

distinguishes between events that prevent performance and events that make performance more onerous. Article 7.1.7 deals with "Force Majeure". It provides:

> Non-performance by a party is excused if that party proves that the non-performance was due to an impediment beyond its control and that it could not reasonably be expected to have taken the impediment into account at the time of the conclusion of the contract or to have avoided or overcome it or its consequences.

The principles do not make any provision for the consequences of a force majeure event. A different approach applies to cases of "hardship". Under art 6.2.2:

> There is hardship where the occurrence of events fundamentally alters the equilibrium of the contract either because the cost of a party's performance has increased or because the value of the performance a party received has diminished, and
>
> (a) the events occur or become known to the disadvantaged party after the conclusion of the contract;
>
> (b) the events could not reasonably have been taken into account by the disadvantaged party at the time of the conclusion of the contract;
>
> (c) the events are beyond the control of the disadvantaged party; and
>
> (d) the risk of the events was not assumed by the disadvantaged party.

Under art 6.2.3, in a case of hardship, the disadvantaged party is entitled to request renegotiation of the contract. If, within a reasonable time, the parties fail to reach agreement on the renegotiations, either party may resort to the court. A court may, where reasonable, terminate or adapt the contract.

It seems possible that the concept of hardship in the UPICC would not extend beyond the events recognised under the common law as frustrating a contract. Article 6.2.2 requires a *fundamental* alteration of the equilibrium of the contract, which suggests that merely because performance has become more onerous may not be sufficient.[146] The UPICC does differ from the common law in imposing a duty to renegotiate where the expected performance of the contract is affected by hardship and in allowing the court to adapt the contract in order to restore its "equilibrium".

146 Cf [15.20].

CONSUMER CONTRACTS

PART VII

Consumers and standard form contracts

[PtVII.05] A *standard form contract* (also sometimes called a contract of adhesion) is a document prepared by one party (usually a trader in goods and services) and used by the trader in all transactions of a similar kind. Standard form contracts are routinely used in many types of transactions, both those between businesses and consumers, for example, in contracts for travel, car hire, credit and telecommunication services, and in those between businesses, for example, supply or commodity contracts. The significant feature of standard form contracts is that they are concluded without negotiation; the standard terms of the trader being presented to consumers on a "take it or leave it" basis.[1]

There can be little objection to the use of standard form contracts in transactions between businesses of comparable size and experience. In this context, standard form contracts are likely to reduce the costs associated with the transaction by reducing the time the parties spend negotiating the contract.[2] Indeed, such contracts often represent the end result of extensive prior negotiations between parties in the industry and their lawyers.[3]

Standard form contracts present more of a challenge to courts and regulators when used by traders in their dealings with *consumers* (ie, individual purchasers of goods or services for their own use).[4] The use of standard form contracts may benefit consumers by reducing the cost of the transaction. The concern with standard form contracts is often said to arise from the *inequality of bargaining power* between the parties.[5] This phrase is usually taken to refer to the disparity in information, experience, expertise and resources that typically exist between a trader and its consumer customers.

Classical contract theory emphasises the role of consent in contracting.[6] Yet, due to the inequality of bargaining power that typically exists between consumer and traders, it might be asked whether there is any meaningful or fair consent by consumers to the terms of a standard form contract presented by a trader. Ideally, consumers can vote with their feet and refuse to transact with those traders who

1 See generally Rakoff, "Contracts of Adhesion: An Essay in Reconstruction" (1983) 96 *Harvard Law Review* 1173.

2 Duggan, The Economics of Consumer Protection: A Critique of the Chicago School Case Against Intervention (1982), p 62.

3 *Macaulay v Schroeder Publishing Co Ltd* [1974] 1 WLR 1308, 1316 (Lord Diplock).

4 Small businesses may also be faced with similar problems to consumers in respect to standard form contracts.

5 *Macaulay v Schroeder Publishing Co Ltd* [1974] 1 WLR 1308, 1316 (Lord Diplock).

6 See also Chapter 1.

use standard form contracts with overly harsh or onerous terms.[7] Competition in the market for customers should encourage traders to provide contracts that have a fair or acceptable balance of risks between the parties. Indeed, it is sometimes suggested that there only needs to be a small group of vigilant consumers dealing with traders to ensure monitoring of their contract terms.

Yet, even if, theoretically, consumers have the option of choosing between different traders offering different contract terms when purchasing goods or services, in practice, consumers are likely to fail to exercise this choice.[8] Many consumers simply may not have the time to read and attempt to negotiate the terms of the standard form contracts presented to them.[9] For example, a person hiring a car upon arriving at an airport after a long flight is unlikely to want to read and negotiate the terms of the hire contract. He or she may feel that the main issues are price and getting away from the airport. Traders of goods and serves might even exploit this situation by pressuring the consumer, subtly or otherwise, to conclude the deal. Consumers may value a sense of goodwill in the transaction and not want to jeopardize this feeling by aggressive negotiations over the details of the deal. Businesses might present more favourable terms to more vigilant customers while retaining the harsher versions for the remaining customers.[10]

Moreover, it is undeniably difficult for consumers to read, assess and negotiate the contracts presented to them for everyday transactions by large businesses. Many standard form contracts are presented in a way which makes them difficult to read and/or understand. In particular, the terms may be written in small print or expressed in complicated and convoluted language. Studies have shown that individuals tend to underestimate the risks faced by them.[11] Accordingly, a consumer who does read the terms of a standard form contract might be overly optimistic in dismissing those terms as dealing with risks unlikely to eventuate.

This reality of restricted opportunities for any meaningful consent by consumers entering into standard form contracts raises the question whether consumers should in such circumstances be bound by terms that are harsh or onerous? For example, should consumers lose all the rights they would otherwise have to complain about defective or faulty goods? Should consumers be subject to heavy financial penalties for even small defaults in performing their obligations under the contract? Should the trader be able to cancel the contract at any time without notice or to change the terms of the contract at his or her "sole discretion"?

7 See further Hillman and Rachlinski, "Standard-form Contracting in the Electronic Age" (2002) 77 *New York University Law Review* 429, 441–3.

8 Hillman and Rachlinski, "Standard-form Contracting in the Electronic Age" (2002) 77 *New York University Law Review* 429, 446–51.

9 *Baltic Shipping Co v Dillon* "Mikhail Lermontov" [1991] NSWCA 19; (1991) 22 NSWLR 1, 25 (Kirby P). See also *Suisse Atlantique Société d'Armement Maritime SA v NV Rotterdamsche Kolen Centrale* [1967] 1 AC 361, 406 (Lord Reid).

10 Hillman and Rachlinski, "Standard-form Contracting in the Electronic Age" (2002) 77 *New York University Law Review* 429, 443.

11 See generally Korobkin, "Bounded Rationality, Standard Form Contracts, and Unconscionability" (2003) 70 *University of Chicago Law Review* 1203; Hillman and Rachlinski, "Standard-form Contracting in the Electronic Age" (2002) 77 *New York University Law Review* 429.

Contract and consumer protection

[PtVII.10] There are a number of examples of what might be seen as the private law of contract providing protection for consumers, particularly those entering into standard form contracts. The equitable doctrines of unconscionable dealing and undue influence may grant relief where advantage is taken of a vulnerable party.[12] Courts have held that it is more difficult for a trader to incorporate delivered or displayed terms into a contract where they are not contained in what might reasonably be considered a contractual document.[13] Courts have also gone some way toward requiring certain unusual clauses to be clearly pointed out to parties entering into standard form contracts, at least in respect to contracts that have not been signed.[14]

However, predominantly, in both Australia and the United Kingdom, consumer protection is the domain of legislation.[15] As discussed in Chapter 2, the *Australian Consumer Law* (ACL) provides a comprehensive regime of consumer protection law applying across Australia. It provides protection for consumers against misleading and deceptive conduct and unconscionable conduct.[16] The ACL also contains new regimes regulating unfair terms in standard form consumer contracts, discussed in Chapter 16, and providing minimum standards of quality, consumer guarantees, that apply to all supplies of goods and services to consumers, as discussed in Chapter 17.

12 See Part XI: Vitiating Factors.

13 See above Chapter 12.

14 See above Chapter 12.

15 See further Paterson, *Corones' Australian Consumer Law* (4th ed, 2019).

16 See Chapters 33 and 38.

CHAPTER **16**

Unfair contract terms

[16.05] Part 2-3 of the *Australian Consumer Law* (ACL)[1] and Pt 2 Div 2 Subdiv BA of the *Australian Securities and Investments Commission Act 2001* (Cth) (ASIC Act)[2] contain equivalent regimes regulating unfair contract terms in standard form consumer contracts, the "Unfair Contract Terms Law" (UCTL). The UCTL is based on similar regimes regulating unfair contract terms in the United Kingdom under the *Unfair Terms in Consumer Contracts Regulations 1999* (UK)[3], now part of the *Consumer Rights Act 2015*, and in Victoria, under Pt 2B (now repealed) of the *Fair Trading Act 1999* (Vic).

Typically, the general law of contract does not apply to regulate the substantive fairness of the terms of a contract. Largely, parties can agree on whatever terms they choose. The contracting safeguards provided by the general law of contract law are typically focused on the process of contract formation. As discussed in Part X, a contract may be set aside where the the bargaining process has been tainted by conduct that misleads or amounts to illegitimate pressure, undue influence or unconscionable advantage taking.

The UCTL focuses on the substantive fairness of the terms of a contract. It does this in recognition of the difficulties consumers face in finding time meaningfully to read the terms

1 CCA, s 130 provides that the "Australian Consumer Law" means Sch 2 as applied under Subdiv A of Div 2 of Pt XI.

2 Under the CCA, s 131A, the ACL does not apply to contracts that are financial products or contracts for the supply or possible supply of services that are financial services.

3 SI 1999/2083.

of standard form contracts, assess the impact of the risks allocated to them by those contracts and try to negotiate to change the terms of the contracts they do not like.[4]

Although beginning as a form of consumer protection, the UCTL has been extended to cover small business contracts.

CONTRACTS TO WHICH THE UCTL APPLIES

[16.10] The UCTL applies to *standard form* contracts in *consumer* and in *small business* transactions.

Standard form contracts

[16.15] The UCTL applies only to standard form contracts.[5] Standard form contracts are not defined in the UCTL. However, the UCTL creates a rebuttable presumption that a contract is a standard form contract in circumstances where a consumer alleges that the contract is of such a kind.[6] In determining whether a contract is a standard form contract, the UCTL states that a court "may take into account such matters as it thinks relevant but must take into account" the following list of specified factors:[7]

a) whether one of the parties has all or most of the bargaining power relating to the transaction;

b) whether the contract was prepared by one party before any discussion relating to the transaction occurred between the parties;

c) whether another party was, in effect, required either to accept or reject the terms of the contract … in the form in which they were presented;

d) whether another party was given an effective opportunity to negotiate the terms of the contract …;

e) whether the terms of the contract … take into account the specific characteristics of another party or the particular transaction;

f) any other matter prescribed by the regulations.

In general contract law, the phrase "standard form contract" is usually understood to refer to a document prepared by a trader and routinely used in all transactions. The significant feature of standard form contracts is that they are concluded without negotiation. It is commonly said that standard form contracts are contracts presented by a trader to consumers on a "take it or leave it" basis.[8] These ideas are apparent in the list of factors that a court is directed to take into account in determining whether a contract is a standard form contract under the UCTL.[9]

4 See further Paterson, *Corones' Australian Consumer Law* (4th ed, 2019), Ch 5.
5 ACL, s 23(1)(b); ASIC Act, s 12BF(1)(b).
6 ACL, s 27(1); ASIC Act, s 12BK(1).
7 ACL, s 27(2); ASIC Act, s 12BK(2).
8 *A Schroeder Music Publishing Co Ltd v Macaulay* [1974] 3 All ER 616, 624 (Lord Diplock) (*Schroeder Music Publishing*); *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd* [1982] EWCA Civ 5; [1983] QB 284, 297, 302 (Lord Denning MR) (*George Mitchell*); Atiyah, *An Introduction to the Law of Contract* (5th ed, 1995), pp 16–17; Rakoff, "Contracts of Adhesion: An Essay in Reconstruction" (1983) 96 *Harvard Law Review* 1173.
9 ACL, s 27(2); ASIC Act, s 12BK(2).

Consumer contracts

[16.20] A consumer contract:

> is a contract for:
>
> (a) a supply of goods or services; or
>
> (b) a sale or grant of an interest in land;
>
> to an individual whose acquisition of the goods, services or interest is wholly or predominantly for personal, domestic or household use or consumption.[10]

This definition of a consumer contract differs from the definitions of a consumer for the purposes of the consumer guarantee regime discussed in Chapter 17. Unlike the consumer guarantee regime, the definition of a consumer contract for the purposes of the UCTL looks to the actual purpose for which the interest in land, goods or services were acquired and not to their price or ordinary purpose.

Small business contracts

[16.25] From 2016, the UCTL was extended to protect small business, with new provisions providing that unfair terms in standard form "small business contracts" are void.[11] Small business contracts are defined as contracts for the supply of goods or services, or the sale or grant of an interest in land, where:

i. at the time the contract was entered into, the business seeking protection employed fewer than 20 people; and

ii. the "upfront price" payable under the contract is not more than $300,000 (or $1,000,000 if the duration of the contract is more than 12 months).[12]

The justification for extending the UCTL to cover small business is that in many ordinary tractions, small businesses are in no better position than consumers in dealing with standard form contracts that may impinge on their rights and yet may be difficult to understand and assess, as well as presented on a "take it or leave it" basis.[13]

Contracts to which the UCTL does not apply

[16.30] The UCTL does not apply to certain shipping contracts or to contracts that are constitutions of companies, managed investment schemes or other kinds of bodies.[14] Section 15 of the *Insurance Contracts Act 1984* (Cth) has the effect that the UCTL will not apply to those terms that are regulated by that Act.

10 ACL, s 23(3). Similarly ASIC Act, s 12BF(3).

11 *Treasury Legislation Amendment (Small Business and Unfair Contract Terms) Act 2015* (Cth).

12 ACL, s 23(4); ASIC Act, s 12BF(4).

13 Explanatory Memorandum, Treasury Legislation Amendment (Small Business and Unfair Contract Terms) Bill, 2015.

14 ACL, s 28; ASIC Act, s 12BL.

Terms to which the UCTL does not apply

[16.35] The UCTL does not apply to terms that define "the main subject matter of the contract",[15] set "the upfront price payable under the contract"[16] or are "required, or expressly permitted, by a law of the Commonwealth, a State or a Territory".[17]

Main subject matter

[16.40] Terms that define the main subject matter of the contract are exempted from review as unfair terms under UCTL.[18] The rationale for exempting these terms dealing with the main subject matter, and also the upfront price, is that consumers generally exercise some choice over subject matter and price, rather than these being boilerplate terms that consumers do not notice or consider and certainly do not negotiate.[19]

Upfront price

[16.45] The UCTL exempts from review a term that "sets the upfront price payable under the contract".[20] The upfront price payable under a contract is "the consideration that":

(a) is provided, or is to be provided, for the supply, sale or grant under the contract; and

(b) is disclosed at or before the time the contract is entered into;

but does not include any other consideration that is contingent on the occurrence or non-occurrence of a particular event.[21]

The upfront price covers the cash price payable for goods or services. Consideration which is not part of the upfront price will include payments contingent on the occurrence or non-occurrence of a particular event occurring after the contract is made. The prime example of a term imposing this kind of contingent consideration, that can be reviewed for fairness under the UCTL, is a term imposing a fee for late payment, events of default or early termination.[22]

Terms expressly permitted as a matter of law

[16.50] The UCTL excludes from review as an unfair term "a term required, or expressly permitted, by a law of the Commonwealth, a State or a Territory".[23] An example of this category may be terms permitted under s 139A of the *Competition and Consumer Act* (and equivalent provisions in some State and Territory jurisdictions)[24], which expressly allows for terms that limit or exclude liability for a failure to comply with the consumer guarantees under the ACL by suppliers of recreational services.

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15 ACL, s 26(1)(a); ASIC Act, s 12BI(1)(a).

16 ACL, s 26(1)(b); ASIC Act, s 12BI(1)(b).

17 ACL, s 26(1)(c); ASIC Act, s 12BI(1)(c).

18 ACL, s 26(1)(a); ASIC Act, s 12BI(1)(a). See, eg, *The Office of Fair Trading v Ashbourne Management Services Ltd* [2011] EWHC 1237 (Ch).

19 Productivity Commission, *Review of Australia's Consumer Policy Framework Volume 2*, Inquiry Report No 45 (Commonwealth of Australia, 2008), pp 161–2.

20 ACL, s 26(1)(b); ASIC Act, s 12BI(1)(b).

21 ACL, s 26(2). See similarly ASIC Act, s 12BI(2).

22 See, eg, *Australian Competition and Consumer Commission v Ashley & Martin Pty Ltd* [2019] FCA 1436.

23 ACL, s 26(1)(c); ASIC Act, s 12BI(1)(c).

24 See [1.210].

THE TEST OF AN UNFAIR TERM

[16.55] The UCTL test for an unfair term consists of three elements. Under the UCTL a term will be unfair if:[25]

(a) it would cause a significant imbalance in the parties' rights and obligations arising under the contract; and

(b) it is not reasonably necessary in order to protect the legitimate interests of the party who would be advantaged by the term; and

(c) it would cause detriment (whether financial or otherwise) to a party if it were to be applied or relied on.[26]

A significant imbalance

[16.60] The first element of the test for an unfair term considers whether the term "would cause a significant imbalance in the parties' rights and obligations arising under the contract".[27] There are two matters to be considered: whether the term would cause an imbalance in the rights and obligations of the parties arising under the contract and whether that imbalance is significant.

Imbalance in the rights and obligations of the parties

[16.65] Whether the term causes an imbalance in the parties' rights and obligations under the contract may be the most straightforward aspect of the test of an unfair term. Courts have said that an imbalance may be found in "the granting to the trader of a beneficial option or discretion or power, or by the imposing on the consumer of a disadvantageous burden or risk or duty".[28] This category will cover overtly one sided terms – that only apply to the consumer or small business. It will also cover terms that fall more heavily on the consumer or small business than on the party who drafted the term. For example, a term in a standard form consumer contract that provides the written contract represents the "entire agreement" of the parties may not appear to cause an imbalance in the parties' rights and obligations because it applies to both parties. However, the effect of the term may be balanced against the interests of consumers, who will typically have less opportunity than traders to amend the written terms of a standard form contract to incorporate any oral representations.[29]

A significant imbalance

[16.70] Having identified an imbalance in the rights and obligations of the parties arising under the contract, it must be considered whether that imbalance is "significant". In assessing whether an imbalance in the rights and obligations of the parties arising under the contract is "significant", it may be relevant to consider whether the term would detract from the rights

25 ACL, s 24(1); ASIC Act, s 12BG(1).

26 ACL, s 24(1); ASIC Act, s 12BG(1).

27 ACL, s 24(1)(a); ASIC Act, s 12BG(1)(a).

28 *Director General of Fair Trading v First National Bank plc* [2001] UKHL 52; [2002] 1 AC 481, [17] (Lord Bingham). Applied in *Australian Competition and Consumer Commission v ACN 117 372 915 Pty Limited (in liq) (formerly Advanced Medical Institute Pty Limited)* [2015] FCA 368, [950] (North J); *Australian Competition and Consumer Commission v JJ Richards & Sons Pty Ltd* [2017] FCA 1224, [19] (Moshinsky J).

29 *Office of Fair Trading v MB Designs (Scotland) Ltd & Ors* [2005] CSOH 85; [2005] SLT 691, [43] (Lord Young).

of consumers or small businesses under the common law or from the reasonable expectations of consumers or small businesses as to the likely distribution of rights and obligations under the contract.[30]

The common law of contract provides a range of "default" rules governing the rights and obligations of the parties to a contract. The common law default rules of contract, having evolved over a long period of time under constant judicial scrutiny, may be presumed to represent a fair balance between the interests of the parties. Any imbalance in the parties' rights and obligations caused by a term that attempts to realign the effect of common law rules may therefore be considered significant.

In *Director General of Fair Trading v First National Bank plc*, Lord Millett indicated some support for the relevance of the default position under the common law in determining whether a term is unfair. Lord Millett said that "[i]t is obviously useful to assess the impact of an impugned term on the parties' rights and obligations by comparing the effect of the contract with the term and the effect it would have without it".[31] The approach has been adopted by Australian courts, in *Australian Competition and Consumer Commission v CLA Trading Pty Ltd*,[32] *Australian Competition and Consumer Commission v JJ Richards & Sons Pty Ltd*[33] and *Australian Competition and Consumer Commission v Servcorp Limited*,[34] and also by the English Supreme Court in *ParkingEye Ltd v Beavis*.[35] This comparison of the contract with, and without, the term being challenged as unfair necessarily involves considering the default rules of contract and the impact on the parties' rights and obligations under those rules of the term being challenged.

Consider, for example, a termination clause that gives the trader the right to broad rights to terminate the contract, even in the event of a trivial breach by the consumer. In the absence of any countervailing factors elsewhere in the contract, this type of clause may be characterised as causing a significant imbalance in the rights and obligations of the parties under the contract. Only the trader, not the consumer, is given the right to terminate for trivial breaches of the contract. The imbalance may also be characterised as "significant". Broad termination clauses go beyond the common law default position under which a trader will typically only be entitled to terminate a contract in response to significant events, such as a breach of a condition, a serious breach of an intermediate term or a repudiation of the contract by the consumer.[36]

Where the common law rules are not applicable to provide a benchmark for assessing whether a term causes a substantial imbalance in the rights and obligations of the parties, another possible measure might be found in the reasonable expectations of consumers.[37]

30 See further Paterson, "The Australian Unfair Terms Law: The Rise of Substantive Unfairness as a Ground for Review of Standard Form Consumer Contracts" (2009) 33 *Melbourne University Review* 934.

31 *Director General of Fair Trading v First National Bank plc* [2001] UKHL 52; [2002] 1 AC 481, [54] (Lord Millet).

32 *ACCC v CLA Trading Pty Ltd* [2016] FCA 377, [66] (Gilmour J).

33 *Australian Competition and Consumer Commission v JJ Richards & Sons Pty Ltd* [2017] FCA 1224, [19] (Moshinsky J).

34 *Australian Competition and Consumer Commission v Servcorp Limited* [2018] FCA 1044, [15] (Markovic J).

35 *ParkingEye Ltd v Beavis* [2015] UKSC 67; [2016] AC 1172; [105] (Lord Neuberger and Lord Sumption (with whom Lord Carnwath agreed)), [307] (Lord Toulson).

36 See Chapter 21.

37 Willett, *Fairness in Consumer Contracts: The Case of Unfair Terms* (2007) p 49.

Under this approach, an imbalance in the rights and obligations of the parties will be significant if the degree of imbalance was contrary to what consumers would reasonably expect in a contract of that kind. Consumers might reasonably expect that a contract for goods or services will contain some terms protecting the interests of the trader. Terms that go beyond what a reasonable consumer would expect may be classified as causing a significant imbalance in the rights and obligations of the parties. Expressed another way, terms that would cause an unfair surprise to consumers are also to be vulnerable to review under the UCTL.[38]

Not reasonably necessary in order to protect the legitimate interests of the trader

[16.75] The second element of the test for an unfair term under the UCTL is whether the term is "not reasonably necessary in order to protect the legitimate interests of the party who would be advantaged by the term".[39] The legitimate interests of a party extend beyond monetary payments but may also include "interests in contractual performance which are intangible and unquantifiable".[40]

The UCTL also provides that, for the purposes of this test, "a term of a consumer contract is presumed not to be reasonably necessary in order to protect the legitimate interests of [the trader], unless that [trader] proves otherwise".[41] Thus, to defend a term that has been challenged as unfair, a trader must bring evidence of how or why that term is reasonably necessary to protect its legitimate interests.

There are two stages to the inquiry. First, it must be shown that the term protects a legitimate interest of the trader. Typically, this requirement will be satisfied by showing that the term protects the trader from business risks inherent in the transaction, as opposed to being an opportunistic attempt to appropriate gains not contemplated as part of the original bargain. In *Australian Competition and Consumer Commission v JJ Richards & Sons Pty Ltd*, Moshinsky J observed that:

> A term is less likely to give rise to a significant imbalance if there is a meaningful relationship between the term and the protection of a party, and that relationship is reasonably foreseeable at the time of contracting. The fact that a party might profit from breaches of contract by a customer, without the customer in breach acquiring something in return, would not alone be sufficient to allow it to be concluded that the term caused a significant imbalance in the parties' rights and obligations arising under the contract.[42]

Secondly, it must be shown that the term is "reasonably necessary" to protect the trader's legitimate interests. Typically, a term will only be reasonably necessary to protect the legitimate

38 Cf *Director General of Fair Trading v First National Bank plc* [2001] UKHL 52; [2002] 1 AC 481, [54] (Lord Millet).

39 ACL, s 24(1)(b); ASIC Act, s 12BG(1)(b).

40 *Australian Competition and Consumer Commission v Ashley & Martin Pty Ltd* [2019] FCA 1436, citing *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [26] (Kiefel J), [161] (Gageler J), [216], [266], [298] (Keane J).

41 ACL, s 24(4); ASIC Act, s 12BG(4).

42 *Australian Competition and Consumer Commission v JJ Richards & Sons Pty Ltd* [2017] FCA 1224, [31] (Moshinsky J) citing *Paciocco v Australia & New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [201] (Gageler J).

interests of the trader where the term represents a proportionate response to the risk it seeks to address.[43]

In *Ferme v Kimberley Discovery Cruises Pty Ltd*,[44] Kimberley Discovery Cruises Pty Ltd (KDC) offered cruises from Wyndham to Derby in Western Australia. The contract contained a "cancellation clause", which provided that if there were an "unexpected event" such as a tropical cyclone, KDC was entitled to cancel the cruise and the passenger accepted that they (the passenger) would not be entitled to any compensation or a refund of the fare paid. KDC cancelled the cruise because of a tropical cyclone, and the applicants' insurer exercised its right of subrogation to recover from KDC the amounts paid by the applicants for their cruise on the basis that the cancellation clause was void under s 23(1) of the ACL.

KDC argued that it had a legitimate interest, namely reputation in the market (its business goodwill) and the preservation of the financial position of KDC. The fares that KDC retained by reason of the cancellation clause provided the funds necessary to meet the costs associated with the preparations undertaken for the cruise. There was evidence in the form of receipts and invoices for food, crew wages and fuel, but no breakdown of costs incurred leading up to the commencement of the cruise.

The Federal Circuit Court held that the respondent had not proved that the cancellation clause was reasonably necessary in order to protect the legitimate interests of KDC. Jarrett J observed:

> If there was evidence of that nature and if the forfeiture term provided for a "sliding scale" of the amount that would be retained by the respondent in the event that the respondent cancelled a cruise, it might be the case that such a term would be reasonably necessary.[45]

Detriment

[16.80] The third element of the test of an unfair term looks to whether the term "would cause detriment (whether financial or otherwise) to a party if it were to be applied or relied on".[46] In other words, a term in a standard form consumer contract will only be unfair where it would, or could potentially, be detrimental to the party against whom it is invoked (usually consumers). Generally, this will not be a difficult criteria to satisfy. In *Director General of Fair Trading v First National Bank plc*, Lord Steyn stated that the element of detriment under what is now the *Consumer Rights Act 2015* (UK) did not "add much" to the formulation for identifying an unfair term but instead "serves to make clear that the directive is aimed at significant imbalance against the consumer, rather than the seller or supplier".[47]

43 See *Director of Consumer Affairs Victoria v AAPT Ltd (Civil Claims)* [2006] VCAT 1493, [50] (Morris J); *Director of Consumer Affairs Victoria v Trainstation Health Clubs Pty Ltd (Civil Claims)* [2008] VCAT 2092, [175] (Harbison J); *Director of Consumer Affairs Victoria v Backloads.com Pty Ltd (Civil Claims)* [2009] VCAT 754, [248]–[250] (Harbison J).

44 *Ferme v Kimberley Discovery Cruises Pty Ltd* [2015] FCCA 2384.

45 *Ferme v Kimberley Discovery Cruises Pty Ltd* [2015] FCCA 2384, [73] (Jarrett J). See also *Turner v MyBudget Pty Limited* [2018] FCA 1407, [67] (Lee J).

46 ACL, s 24(1)(c); ASIC Act, s 12BG(1)(c).

47 *Director General of Fair Trading v First National Bank plc* [2001] UKHL 52; [2002] 1 AC 481, [36] (Lord Steyn).

MATTERS RELEVANT IN DETERMINING WHETHER A TERM IS UNFAIR

[16.85] The UCTL provides that in determining whether a term of a standard form consumer contract is unfair under the specified test of an unfair term, "a court may take into account such matters as it thinks relevant but must take into account the following":

(a) the extent to which the term is transparent;

(b) the contract as a whole.[48]

The UCTL provides that a term is transparent if the term is:

(a) expressed in reasonably plain language; and

(b) legible; and

(c) presented clearly; and

(d) readily available to any party affected by the term.[49]

Transparency

[16.90] Issues of transparency are usually seen as relevant to procedural unfairness issues, as impediments to consumers' understanding and consenting to the terms of a contract. This might suggest that the fact that a term is not transparent does not make it substantively unfair. It has yet to be determined whether transparency may create of itself an imbalance in the rights and obligations of the parties.

Transparency is perhaps best seen as relevant to establishing whether there was a significant imbalance in the rights and obligations of the parties.[50] For example where an apparently harsh and one-sided term favouring the interests of the trader is expressed and presented in a way that is not transparent, this may undermine any argument that consumers had accepted the term in return for other concessions under the contract, such as in price. Conversely, transparency will not cure a grossly unfair term.

> The legislation proceeds on the assumption that some terms in consumer contracts, especially in standard form consumer contracts, may be inherently unfair, regardless of how comprehensively they might be drawn to the consumer's attention.[51]

In *Australian Competition and Consumer Commission v ACN 117 372 915 Pty Limited (in liq) (formerly Advanced Medical Institute Pty Limited)*, NRM conducted a business promoting and supplying medication and services for the treatment of male sexual dysfunction. NRM patients seeking to terminate their contracts were required to provide 30 days' written notice to NRM and to pay a 15 per cent administration fee, a pro-rata fee for the expired portion of the treatment, a pro-rata fee for the 30-day notice period, and the cost of medication supplied or prepared for the patient. The term operated whether the reason for the termination was a change of mind very soon after the phone consultation, a severe adverse side effect or

48 ACL, s 24(2); ASIC Act, s 12BG(2).

49 ACL, s 24(3); ASIC Act, s 12BG(3).

50 *Australian Competition and Consumer Commission v Chrisco Hampers Australia Limited* [2015] FCA 1204; (2015) 239 FCR 33, [74] (Edelman J). See also Second Explanatory Memorandum, *Trade Practices Amendment (Australian Consumer Law) Bill (No 2) 2010*, [5.39].

51 *ACCC v CLA Trading Pty Ltd* [2016] FCA 377, [54] (Gilmour J). Also *Australian Competition and Consumer Commission v JJ Richards & Sons Pty Ltd* [2017] FCA 1224, [19] (Moshinsky J); *Australian Competition and Consumer Commission v Servcorp Limited* [2018] FCA 1044, [15] (Markovic J).

the medication proving ineffective. In litigation initiated by the Australian Competition and Consumer Commission, the Federal Court declared that the term was unfair. The term caused a significant imbalance in the parties' rights and obligations because it had the effect of binding patients to continue treatment in disadvantageous circumstances, or alternatively suffer a financial penalty.[52] The term also lacked transparency to a significant extent. The basis on which the administration fee was calculated and the cost of the medication was not disclosed to patients.[53] North J concluded that:

> The contract provided for the supply of medications which were not regarded by the medical profession as the usual forms of treatment and there was no cogent evidence that they were effective to treat [the conditions in question]. In those circumstances it was unfair to hold the patient to the agreement on penalty of payment of fees, the method of calculation of which was unknown, imposed in order to cancel the treatment.[54]

In any event, the requirement for courts to consider the extent to which a term is transparent in assessing whether it is unfair means that traders should take care in the way in which their standard form consumer contracts are drafted and presented, aiming for clear and accessible terms.[55]

The contract as a whole

[16.95] Under the UCTL, courts are specifically directed to consider the contract "as a whole" in deciding whether a particular term is unfair.[56] This means that in deciding whether the term causes a significant imbalance in the rights and obligations of the parties, a court should consider the extent to which an apparently harsh and one-sided term is balanced by other terms in the contract, including potentially the contract price.

Australian Competition and Consumer Commission v Chrisco Hampers Australia Limited[57] involved the "HeadStart" arrangements inserted by Chrisco Hampers Australia Limited into its lay-by contracts with consumers. The term allowed Chrisco to continue to take payments by direct debit from the consumer's bank account even after the consumer had made full payment for the lay-by order. The term would apply unless the consumer opted out of it. The money withdrawn from the consumer's bank account would then be used for any future order made by the consumer.

Edelman J held the term was unfair. Edelman J concluded:

> Ultimately, it suffices to say that the sums of money lost by Chrisco's withdrawals from the consumer's account, without any obligation upon Chrisco to pay interest and with no discount for the consumer who subsequently chose to place an order, involved a significant detriment to the consumer. That detriment was not balanced by any substantial corresponding right that the

52 *Australian Competition and Consumer Commission v ACN 117 372 915 Pty Limited (in liq) (formerly Advanced Medical Institute Pty Limited)* [2015] FCA 368, [951] (North J).

53 *Australian Competition and Consumer Commission v ACN 117 372 915 Pty Limited (in liq) (formerly Advanced Medical Institute Pty Limited)* [2015] FCA 368, [953] (North J).

54 *Australian Competition and Consumer Commission v ACN 117 372 915 Pty Limited (in liq) (formerly Advanced Medical Institute Pty Limited)* [2015] FCA 368, [954] (North J).

55 On transparency in electronic contracts, see Paterson, "Consumer Contracting in the Age of the Digital Natives" (2011) 27 *Journal of Contract Law* 152.

56 ACL, s 24(2); ASIC Act, s 12BG(2).

57 *Australian Competition and Consumer Commission v Chrisco Hampers Australia Limited* [2015] FCA 1204; (2015) 239 FCR 33.

> consumer obtained against Chrisco. By itself, it is not necessarily determinative that there is no substantial right to a consumer, or duty upon Chrisco, that corresponds with the consumer's obligations under the HeadStart term. The evaluative exercise involves consideration of the contract as a whole to determine whether there is a significant imbalance in the parties' rights and obligations arising under the contract.[58]

Edelman J concluded that the nature of the HeadStart term, in the context of the contract as a whole combined with a distinct lack of transparency in the operation of the arrangement led to the HeadStart term, causing a significant imbalance in the rights and obligations of the parties under the contract.[59]

EXAMPLES OF THE KINDS OF TERMS THAT MAY BE UNFAIR

[16.100] The UCTL sets out a list of examples of the kind of terms of a consumer contract that may be unfair.[60] The examples are expressed in general language and any particular term under review for fairness must still be assessed with regard to the tests specified in the UCTL.

Thus, s 25 of the ACL provides:

(a) a term that permits, or has the effect of permitting, one party (but not another party) to avoid or limit performance of the contract;

(b) a term that permits, or has the effect of permitting, one party (but not another party) to terminate the contract;

(c) a term that penalises, or has the effect of penalising, one party (but not another party) for a breach or termination of the contract;

(d) a term that permits, or has the effect of permitting, one party (but not another party) to vary the terms of the contract;

(e) a term that permits, or has the effect of permitting, one party (but not another party) to renew or not renew the contract;

(f) a term that permits, or has the effect of permitting, one party to vary the upfront price payable under the contract without the right of another party to terminate the contract;

(g) a term that permits, or has the effect of permitting, one party unilaterally to vary the characteristics of the goods or services to be supplied, or the interest in land to be sold or granted, under the contract;

(h) a term that permits, or has the effect of permitting, one party unilaterally to determine whether the contract has been breached or to interpret its meaning;

(i) a term that limits, or has the effect of limiting, one party's vicarious liability for its agents;

(j) a term that permits, or has the effect of permitting, one party to assign the contract to the detriment of another party without that other party's consent;

(k) a term that limits, or has the effect of limiting, one party's right to sue another party;

(l) a term that limits, or has the effect of limiting, the evidence one party can adduce in proceedings relating to the contract;

(m) a term that imposes, or has the effect of imposing, the evidential burden on one party in proceedings relating to the contract;

(n) a term of a kind, or a term that has an effect of a kind, prescribed by the regulations.

58 *Australian Competition and Consumer Commission v Chrisco Hampers Australia Limited* [2015] FCA 1204; (2015) 239 FCR 33, [69]–[70] (Edelman J).

59 *Australian Competition and Consumer Commission v Chrisco Hampers Australia Limited* [2015] FCA 1204; (2015) 239 FCR 33, [97] (Edelman J).

60 ACL, s 25; ASIC Act, s 12BH.

Paragraph (a) refers to a term that "permits, or has the effect of permitting, one party to limit or avoid performance of the contract". Paragraph (k) refers to a term that limits, or has the effect of limiting, a consumer's right to sue the trader. Many exclusion or limitation clauses of the kind contemplated by these clauses will already be void as purporting to exclude or limit liability in respect of the consumer guarantees in the ACL[61] or the terms implied under the ASIC Act.[62] They may also be unfair terms under the UCTL.[63]

Paragraph (b) refers to a term that "permits, or has the effect of permitting, one party (but not another party) to terminate the contract". A term in a standard form consumer contract that gives the trader rights to terminate its contract with consumers in any circumstances or "at will" may be void as an unfair term. For example, the following term was declared to be unfair in *Australian Competition and Consumer Commission v Bytecard Pty Limited*:

> NetSpeed reserves the right to terminate any account at any time with or without cause or reason…[64]

Paragraph (c) refers to "a term that penalises, or has the effect of penalising, one party (but not another party) for a breach or termination of the contract". Following the decision in *Paciocco v Australia and New Zealand Banking Group Ltd*,[65] discussed in Chapter 28, there would appear to be a very high benchmark for establishing that a sum payable on breach, or otherwise to promote performance of the contract, is invalid as a penalty under the general law or statute.[66]

In *Paciocco*, the majority of the High Court held that credit card late payment fees charged by ANZ were not penalties. Nor were they unconscionable or unfair under the ASIC Act. The key issue in assessing whether the sum was a penalty, or otherwise an unfair term not reasonably necessary to protect a legitimate interest under the contract, was not whether the term was an accurate pre-estimate of the loss that would be sustained to ANZ by late payment. It was whether the fee was "extravagant, exorbitant or unconscionable" when regard was had to the ANZ's interest in the performance of the contract[67] or "'out of all proportion' to the interests said to be damaged in the event of default".[68] The Court held that the term imposing the fee was not an unfair term prohibited under legislation because it protected the legitimate interests of the bank in the face of considerable potential losses resulting from non-payment of the credit card debt.[69]

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61 ACL, s 64. See also Chapter 17.

62 ASIC Act, s 12EB.

63 *Malam v Graysonline, Rumbles Removals and Storage (General)* [2012] NSWCTTT 197.

64 NetSpeed *General Terms and Conditions* 1.7. Declared to be an unfair terms in *Australian Competition and Consumer Commission v Bytecard Pty Limited* Consent order (P)VID301/2013. See also *Director of Consumer Affairs Victoria v AAPT Ltd (Civil Claims)* [2006] VCAT 1493, [53] (Morris J). See also ACCC, *Unfair Contract Terms – Industry Review Outcomes* (2013), p 11.

65 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525. See also *ParkingEye Limited v Beavis* [2015] UKSC 67; [2016] AC 1172.

66 But see *Australian Competition and Consumer Commission v Ashley & Martin Pty Ltd* [2019] FCA 1436.

67 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525 (Keane J).

68 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [57] (Kiefel J).

69 See esp [295]–[304] (Keane J (French CJ and Kiefel J agreeing)). See similarly *ParkingEye Limited v Beavis* [2015] UKSC 67; [2016] AC 1172. See further Yip and Goh, "Convergence between Australian Common Law and English Common Law: The Rule Against Penalties in the Age of Freedom of Contract" (2017) 48 *Common Law World Review* 61.

A case where a fee payable on early termination was an unfair term is *Australian Competition and Consumer Commission v Ashley & Martin Pty Ltd*.[70] In this case, a term requiring consumers to pay the entire contract price for 12 months of treatment should they terminate the contract before this time was an unfair term. It applied before consumers had consulted a doctor about the treatment and even where consumers stopped treatment on medical advice or due to an adverse response to the medication.

Paragraph (d) refers to "a term that permits, or has the effect of permitting, one party (but not another party) to vary the terms of the contract", and (f) and (g) are of similar effect. Terms allowing the trader to change the subject matter, price or terms of a contract may clearly result in a significant imbalance under the contract to the detriment of consumers. Such terms may also not be regarded as necessary to protect the legitimate interests of the trader if they allow the trader to make any changes it wants in any circumstances. Consistently, the following term was declared to be unfair in *Australian Competition and Consumer Commission v Bytecard Pty Limited*:

> NetSpeed reserves the right to change prices or services at any time without prior notice to customers or the public, except when the service is an Australian Broadband Guarantee Service. Price changes will not be retroactive for existing prepaid customers. It is the User's responsibility to check this online.[71]

Terms giving the trader a unilateral right of variation are more likely to be viewed as fair if the discretion granted by the term is in some way constrained. A "fair" unilateral variation clause might, for example, specify the circumstances under which the variations may be made or allow consumers to exit the contract if they object to the variations made by the trader.[72]

EFFECT OF A TERM BEING UNFAIR

An unfair term is void

[16.105] The UCTL renders unfair terms in standard form consumer and small business contracts void,[73] which means the term will be of no effect. The contract continues to bind the parties if it is capable of operating without the unfair term.[74]

Remedies

[16.110] A consumer may rely on an unfair term being void under the UCTL as a defence in an action to enforce the term. A consumer or a regulator may also take pre-emptive action against an unfair term in a standard form consumer contract by seeking a declaration that the term is unfair and therefore void.[75] There are a range of remedies potentially available to

70 *Australian Competition and Consumer Commission v Ashley & Martin Pty Ltd* [2019] FCA 1436.

71 NetSpeed, *General Terms and Conditions* 1.7. Declared to be unfair terms in *Australian Competition and Consumer Commission v Bytecard Pty Limited* Consent order (P)VID301/2013. See also *Director of Consumer Affairs Victoria v AAPT Ltd (Civil Claims)* [2006] VCAT 1493, [50] (Morris J).

72 Australian Competition and Consumer Commission, *A Guide to the Unfair Contract Terms Law* (2010), p 20; Office of Fair Trading (UK), *Unfair Contract Terms Guidance: Guidance for the Unfair Terms in Consumer Contracts Regulations* (2008), [10.3].

73 ACL, s 23(1); ASIC Act, s 12BF(1).

74 ACL, s 23(2); ASIC Act, s 12BF(2b).

75 ACL, s 250(1); ASIC Act, s 12GND(1).

regulators and consumers in response to the use by traders of a term that has been declared unfair. These remedies are:

- injunctions;[76]
- compensation orders;[77] and
- compensation orders for non-parties.[78]

Enforcement action

[16.115] The regulatory body responsible for enforcing the ACL throughout Australia, the Australian Competition and Consumer Commission (ACCC) has generally preferred a consultative approach to the regime regulating unfair contract terms. This has meant reviewing common industry contracts and then consulting with businesses where terms are considered by the ACCC to be unfair.[79] Where businesses do not co-operate in these consultations, the ACCC may consider court action to deal with terms it considers operate unfairly.[80] In recent years, the ACCC has been extremely active in pursuing court declarations that particular terms in both consumer[81] and small business[82] standard form contracts are void.

76 ACL, s 232; ASIC Act, s 12GD.

77 ACL, s 237; ASIC Act, s 12GM.

78 ACL, s 239; ASIC Act, s 12GNB.

79 Australian Competition and Consumer Commission, *Unfair Contract Terms – Industry Review Outcomes* (2013).

80 Australian Competition and Consumer Commission, *Unfair Contract Terms – Industry Review Outcomes* (2013), p 3.

81 See, eg, *Australian Competition and Consumer Commission v Bytecard Pty Limited* Consent order (P)VID301/2013; *Australian Competition and Consumer Commission v ACN 117 372 915 Pty Limited (in liq) (formerly Advanced Medical Institute Pty Limited)* [2015] FCA 368; *Australian Competition and Consumer Commission v Chrisco Hampers Australia Limited* [2015] FCA 1204; (2015) 239 FCR 33.

82 *Australian Competition and Consumer Commission v JJ Richards & Sons Pty Ltd* [2017] FCA 1224; *Australian Competition and Consumer Commission v Servcorp Limited* [2018] FCA 1044.

CHAPTER **17**

Consumer guarantees

THE CGL

[17.05] One important addition to private law rights in sales, introduced by the *Australian Consumer Law* (ACL), is the Consumer Guarantee Law (CGL), which is found in Pt 3-2, Div 1 and Pt 5-4 of the ACL.[1] The CGL complements the Unfair Contract Terms Law (UCTL), discussed in Chapter 16, in regulating the substantive content of consumer contracts. While the UCTL renders void unfair terms in standard form consumer and small business contracts, the CGL provides minimum mandatory standards of quality applying to the supply of goods and services to consumers.[2] The concept of consumer in the CGL is broadly defined and so will provide protection not only in business to consumer transactions, but will also apply to some business to business transactions.

The CGL replaces the previous regime of implied terms

[17.10] The *Trade Practices Act 1974* (Cth), and equivalent State and Territory legislation, implied a range of mandatory terms providing minimum quality standards in contracts for the supply of goods and services to consumers.[3] The CGL replaces these implied terms with a regime

1 Paterson, "The Consumer Guarantee Law" (2011) 35 *Melbourne University Law Review* 252.
2 On the CGL, see further Paterson, *Corones' Australian Consumer Law* (2019).
3 *Trade Practices Act 1974* (Cth), Pt V Div 2.

of "consumer guarantees" that operate as statutory rights. These statutory rights are not based in contract, but apply by force of statute and are accompanied by their own statutory remedial regime.[4] As with the implied terms under the *Trade Practices Act 1974* (Cth), the consumer guarantees are mandatory and cannot be excluded, restricted or modified by contract.[5]

Reasons for introducing the CGL

[17.15] Mandatory quality standards such as the CGL apply to address the "information asymmetry" that exists between consumers and suppliers.[6] Consumers are typically less knowledgeable about the goods and services that they might be purchasing than suppliers. Consumers may not be aware of the defects likely to occur in the goods or may be unable to bargain for a fair contractual allocation of those risks. Mandatory standards of quality address this information asymmetry by giving consumers a right of redress in the event that the goods or services they have purchased prove to be faulty or defective.[7]

WHEN DOES THE CGL APPLY?

Consumers

[17.20] The CGL applies to the supply of goods and services to a "consumer". The definition of "consumer" differs from the definition of "consumer contract" under the UCTL.[8] For the purposes of the CGL, there is a three-part test to identify whether goods or services were purchased by a consumer:

1. A person will be taken to have acquired goods or services as a consumer if the price of those goods or services did not exceed $40,000.
2. Where the price of the goods or services exceeds that amount, a person will be taken to have acquired goods or services as a consumer if
   (a) "the goods [or services] were of a kind ordinarily acquired for personal, domestic or household use or consumption"; or
   (b) the goods "consisted of a vehicle or trailer acquired for use principally in the transport of goods on public roads".[9]

Exclusions

The definition of a consumer does not apply where the goods are purchased to be used in another commercial process or resold. Thus, under ACL s 3(2), a person will not be a consumer for the purposes of the CGL if the person acquired the goods or held himself or herself out as acquiring the goods:

4 ACL, Pt 3-2 Div 1; Pt 5-4.
5 ACL, s 64.
6 *Trade Practices Amendment (Australian Consumer Law) Bill (No 2) 2010, Explanatory Memorandum*, p 607, [25.45]; Hadfield, Howse and Trebilcock, "Information-Based Principles for Rethinking Consumer Protection Policy" (1998) 21 *Journal of Consumer Policy* 131, 141; Howells and Weatherill, *Consumer Protection Law* (2nd ed, Ashgate, 2005), p 146.
7 Howells and Weatherill, *Consumer Protection Law* (2nd ed, Ashgate, 2005), pp 145–7.
8 See Chapter 16.
9 ACL, s 3(1).

(a) for the purpose of re-supply; or

(b) for the purpose of using them up or transforming them, in trade or commerce:

(i) in the course of a process of production or manufacture; or

(ii) in the course of repairing or treating other goods or fixtures on land.[10]

[17.25] The guarantees as to services do not apply to services that are, or are to be, supplied under:

(a) a contract for or in relation to the transportation or storage of goods for the purposes of a business, trade, profession or occupation carried on or engaged in by the person for whom the goods are transported or stored;[11] or

(b) a contract of insurance.[12]

The guarantee of fitness of services for a particular purpose "does not apply to a supply of services of a professional nature by a qualified architect or engineer".[13]

Financial services

[17.30] The ACL containing the CGL does not apply "to the supply, or possible supply, of services that are financial services, or of financial products".[14] These contracts are regulated under the ASIC Act. While most relevant aspects of the ACL, including the UCTL, have also been included in the ASIC Act, the ASIC Act has not been amended to include the CGL. The ASIC Act continues to imply into contracts, for the supply of financial services, mandatory warranties that the services will be rendered with "due care and skill",[15] and that any materials supplied in connection with those services will be "reasonably fit" for the purpose for which they are supplied.[16]

Trade and commerce

[17.35] The consumer guarantees of title, undisturbed possession, and undisclosed securities apply to all supplies of goods.[17] The other guarantees will only apply if the goods or services in question are supplied in trade or commerce.

Auctions

[17.40] The consumer guarantees of acceptable quality, fitness for any disclosed purpose, supply of goods by description, supply of goods by sample, or demonstration model, repairs and spare parts, and express warranties do not apply to goods sold by auction. Under the ACL, *sale by auction*, "in relation to the supply of goods by a person, means a sale by auction that is conducted by an agent of the person (whether the agent acts in person or by electronic

10 ACL, s 3(2).
11 ACL, s 63(a).
12 ACL, s 63(b).
13 ACL, s 61(4).
14 CCA, s 131A.
15 ASIC Act, s 12ED(1).
16 ASIC Act, s 12ED(2).
17 ACL, ss 51–53.

means)".[18] Under this definition, a sale by auction will not include sales through online auctions where, such as in the case of services like eBay, the operator of the site is merely providing a venue for sale, rather than acting on behalf of the seller.[19] A sale through eBay will accordingly be regulated by the CGL.

Rights of gift recipients

[17.45] The CGL provides gift recipients of goods with rights and remedies against suppliers in respect to the consumer guarantees.[20]

GUARANTEES IN RESPECT TO GOODS

[17.50] The consumer guarantees applying to the supply of goods are in Ch 3, Pt 3-2, Div 1, Subdiv A of the ACL. They provide that:

- the seller has a right to dispose of the goods;[21]
- the consumer will have undisturbed possession of the goods;[22]
- the goods are free from any undisclosed securities;[23]
- the goods will be of acceptable quality;[24]
- the goods are fit for any disclosed purpose;[25]
- in the case of a sale of goods by description, that the goods match their description;[26]
- that if the goods are sold by reference to a sample or demonstration model, the goods will correspond to that sample or demonstration model;[27]
- compliance with express warranties.[28]

Acceptable quality

[17.55] Perhaps the most significant guarantee applying to the supply of goods is "acceptable quality". Goods will be of acceptable quality if they are as:

(a) fit for all the purposes for which goods of that kind are commonly supplied; and

(b) acceptable in appearance and finish; and

(c) free from defects; and

(d) safe; and

(e) durable;

18 ACL, s 2.

19 See Bevan, Dugan and Grainer, *Consumer Law* (LexisNexis, Wellington, 2009), [4.21].

20 ACL, s 266.

21 ACL, s 51.

22 ACL, s 52.

23 ACL, s 53.

24 ACL, s 54.

25 ACL, s 55.

26 ACL, s 56.

27 ACL, s 57.

28 ACL, s 59.

as a reasonable consumer fully acquainted with the state and condition of the goods (including any hidden defects of the goods), would regard as acceptable having regard to the matters in subs (3).[29]

The matters that may be taken into account are:

(a) the nature of the goods;

(b) the price of the goods (if relevant);

(c) any statements made about the goods on any packaging or label on the goods;

(d) any representation made about the goods by the supplier or manufacturer of the goods; and

(e) any other relevant circumstances relating to the supply of the goods.[30]

The nature and price of goods will logically be relevant in assessing acceptable quality.[31] More will be expected of high-quality goods than cheaper types and of new goods than second hand goods. However, if goods are sold as useable, then they must be in useable condition, even if they are second-hand or not "top of the range" in quality terms.[32]

The express reference to "durability" in assessing acceptable quality suggests that goods are required to remain free from defects for a reasonable time following purchase.[33] This reasonable period will not be set by reference to the period of time over which manufacturers and retailers may provide express warranties for repair of the goods. Durability will be assessed by reference to the period of time a reasonable and informed consumer would expect the goods to function without fault, having regard to the nature of the goods and the other factors identified as relevant in the ACL.[34] For example, the warranty period for many electrical goods is one year, yet consumers might reasonably expect such goods to function effectively for a much longer period, having regard to their purpose and price.

Goods will not fail to be of acceptable quality with regard to defects specifically drawn to the consumer's attention,[35] defects caused by abnormal use,[36] and defects that the consumer should reasonably have become aware of in cases where the consumer examined the goods before buying them.[37]

Gallant v Larry Woods Used Cars Ltd[38] provides an illustration of the defence of "abnormal use". In this case, the consumer had bought an eight-year-old vehicle that needed a major repair three weeks after purchase, but following the consumer driving around 3000 miles. The New Brunswick Queen's Bench held that the guarantee as to acceptable quality had not been breached because the failure was due to the consumer overusing the vehicle.

29 ACL, s 54(2).

30 ACL, s 54(3).

31 ACL, s 54(3)(a), (b).

32 *WM Johnson Pty Ltd v Maxwelton (Oaklands) Pty Ltd* [2000] NSWCA 286, [25].

33 Compare, discussing the TPA, Kapnoullas and Clarke, "Countdown to Zero: The Duration of Statutory Rights for Unfit and Unmerchantable Goods" (1999) 14 *Journal of Contract Law* 154, 155, 158–9.

34 ACL, s 54(2).

35 ACL, s 54(4).

36 ACL, s 54(6).

37 ACL, s 54(7).

38 *Gallant v Larry Woods Used Cars Ltd* (1982) 38 NBR (2d) 262.

Fitness for disclosed purpose

[17.60] The ACL provides a guarantee that goods supplied to a consumer will be "reasonably fit for any disclosed purpose, and for any purpose for which the supplier represents that they are reasonably fit".[39] The purpose for which goods are required may be made known expressly, and also by implication, which will usually be based on the nature of the goods acquired.[40] In cases where goods are unfit for their common purpose, they will also have breached the guarantee as to acceptable quality, discussed above. This requires goods to be as fit for all purposes for which the goods are commonly supplied as a reasonable consumer would regard as acceptable in the circumstances. The fitness for purpose guarantee provides protection beyond that of acceptable quality in circumstances where a consumer purchases a product for a particular purpose, which is not a common purpose, and makes this purpose known to the supplier.

In *Baldry v Marshall*,[41] the plaintiff told the defendant car seller that he wanted a fast car, which would be flexible and easily managed, and one that would be comfortable and suitable for the ordinary purposes of a touring car. The defendant recommended a Bugatti car to satisfy those requirements. The Bugatti car that was delivered was not comfortable or suitable for touring purposes. Greer J held that there the car was not reasonably fit for the purpose made known by the plaintiff.

The guarantee of fitness for purpose will not apply "if the circumstances show that the consumer did not rely on, or that it was unreasonable for the consumer to rely on, the skill or judgment" of the person to whom the purpose was disclosed.[42] Accordingly, a consumer will not be able to rely on the guarantee of fitness for purpose in circumstances where, although he or she made a particular purpose known, the circumstances were such as to suggest that the supplier had no particular expertise or where the consumer ignored the advice of the supplier.

Express warranties

[17.65] The CGL provides a guarantee of compliance with an "express warranty".[43] Express warranties are broadly defined to include *any* undertaking, assertion or representation in respect of the "quality, state, condition, performance or characteristics of the goods … the natural tendency of which is to induce persons to acquire the goods".[44] Accordingly, pre-contractual representations by a supplier about the quality or characteristics of the goods may take effect as a consumer guarantee that cannot be excluded by contract. This aspect of the CGL provides a new basis for liability for pre-contractual statements, adding to that potentially accruing through the statement being a term of the contract,[45] giving rise to an estoppel,[46] or constituting misleading and deceptive conduct.[47] Where a pre-contractual

39 ACL, s 55(1). See also the *Consumer Guarantees Act 1993* (NZ).

40 *Rasell v Cavalier Marketing (Aust) Pty Ltd* (1990) 96 ALR 375, 382; *Peterson v Merck Sharpe & Dohme (Aust) Pty Ltd* [2010] FCA 180, [941].

41 *Baldry v Marshall* [1925] 1 KB 260.

42 ACL, s 55(3).

43 ACL, s 59.

44 ACL, s 2.

45 See above Chapter 12.

46 See above Chapter 9.

47 See below Chapter 33.

statement is an express warranty, suppliers will not be able to use an "entire agreement" clause to prevent consumers from seeking to enforce that statement. An entire agreement clause may also be an unfair term under the UCTL.[48]

SERVICES

[17.70] Chapter 3, Pt 3-2, Div 1, Subdiv B of the ACL sets out the consumer guarantees that apply to the supply, in trade and commerce of services, to a consumer. There are consumer guarantees that services:

- will be rendered with due care and skill;[49] and
- any product resulting from the services, will be fit for a purpose that the consumer made known to the supplier;[50] and
- will be supplied within a reasonable time.[51]

The consumer guarantee that services supplied to a consumer "will be rendered with due care and skill" means that the services should be provided with care, but does not guarantee that the consumer will obtain his or her desired result.[52] Unlike the guarantee that goods must be of acceptable quality, this guarantee requires the consumer to prove fault.

The guarantees of fitness for a particular purpose do "not apply if the circumstances show that the consumer did not rely on, or that it was unreasonable for the consumer to rely on, the skill or judgment of the supplier".[53]

GUARANTEES ARE MANDATORY

[17.75] In most cases, the guarantees under the CGL are mandatory and cannot be excluded by contract.[54] Attempts to do so will be void and may also amount to misleading conduct contrary to s 29(2)(m) of the ACL.[55]

ACCC v Valve Corporation (No 3)[56] and, on appeal, *Valve Corp v ACCC*,[57] concerned Subscriber Service Agreements for an online game distribution network. These agreements purported to exclude the right to a refund in the event that the computer software (goods) supplied failed to comply with the guarantee of acceptable quality.[58] The Full Federal Court upheld the finding of the trial judge, Edelman J, that a term stating fees "are not refundable" was void under s 64 and amounted to a misleading representation

48 See [16.45].

49 ACL, s 60.

50 ACL, s 61(1).

51 ACL, s 62.

52 See, eg, *Wilson v Best Travel Ltd* [1993] 1 All ER 353.

53 ACL s 61(3). See, eg, *Dixon v Totara Coatings (1993) Ltd* (High Court, Wellington, 3 February 2005, CIV-2004-485-811), [125].

54 ACL, s 64.

55 See, eg, *Valve Corporation v Australian Competition and Consumer Commission* [2017] FCAFC 224; (2017) 258 FCR 190.

56 *Australian Competition and Consumer Commission v Valve Corporation (No 3)* [2016] FCA 196.

57 *Valve Corporation v Australian Competition and Consumer Commission* [2017] FCAFC 224; (2017) 258 FCR 190.

58 The argument that the contract was governed by the law of the state of Washington was also rejected as contrary to ACL, s 67.

contrary to s 29(1)(m). A statement, "we do not offer refunds", was equally void and misleading.[59]

By contrast, a term of the Refund Policy stating "unless required by local law, we do not offer refunds or exchanges", did not contravene s 29(1)(m) because they did not contain a misleading representation about the protection provided to consumers under the CGL. "In particular the 'local law' qualification was (i) in the same clause where the representation was made, (ii) in the same typeface and font and (iii) would reasonably have been understood by a consumer to mean the laws in which the consumer was located".[60] This aspect of the decision was not contested on appeal.[61]

Some scope for a supplier to limit its liability for failure to comply with the consumer guarantees exists where the goods or services in question are not ordinarily acquired for personal, domestic or household use or consumption.[62] The *Competition and Consumer Act 2010* (Cth) also expressly provides that a term of a contract for the supply of recreational services to a consumer is not void under the ACL only because the term excludes, restricts or modifies the application of the CGL or liability arising under the CGL.[63] The exception to liability under the CGL only applies if the exclusion of liability is limited to personal injury,[64] and does not apply if the defendant's conduct has been "reckless".[65]

EXTENDED WARRANTIES

[17.80] With some purchases of goods the retailer or manufacturer may provide a "voluntary warranty" undertaking to repair the goods if they break or cease to work properly within a specified period of time. Another type of warranty against defects is an extended warranty. An extended warranty is an undertaking to repair or replace faulty goods for a specified "extended" period of time that is purchased from the manufacturer, supplier, or third party through a separate contract with the consumer.

The statutory protections in the ACL will often provide equivalent or even broader protection than that provided by an extended warranty. In the event of conflict, it is the statutory rights under the ACL that prevail. However, research conducted prior to the introduction of the ACL suggested that consumers, and indeed suppliers, did not understand the relationship between extended warranties and the implied terms or consumer guarantees provided under statute.[66] If consumers are not aware of their rights under statute, it is unlikely that they will be able accurately to price the value of the extended warranty to them or assess a fair price to pay for such a warranty.

59 *Valve Corporation v Australian Competition and Consumer Commission* [2017] FCAFC 224; (2017) 258 FCR 190 at [162]–[163].

60 *Australian Competition and Consumer Commission v Valve Corporation (No 3)* [2016] FCA 196, [270].

61 *Valve Corporation v Australian Competition and Consumer Commission* [2017] FCAFC 224; (2017) 258 FCR 190, [59].

62 ACL, s 64A(1). For services, see s 64A(2).

63 CCA, s 139A.

64 This is a strict requirement and an exclusion clause that goes beyond these parameters will be void: see *Perisher Blue Pty Ltd v Nair-Smith* [2015] NSWCA 90, [201]; *Alameddine v Glenworth Valley Horse Riding Pty Ltd* [2015] NSWCA 219, [66].

65 CCA, s 139A(4).

66 See Commonwealth Consumer Affairs Advisory Council, Department of Treasury, *Consumer Rights: Reforming Statutory Implied Conditions and Warranties – Final Report* (2009); Consumer Affairs Victoria, "Warranties and Refunds in the Electronic Goods, White Goods and Mobile Telephone Industries" (2009), Research Paper No 17.

There are three important protections provided under the ACL for consumers purchasing an extended warranty.

1. To the extent that an extended warranty is a "warranty against defects"[67], consumers must be provided with the information about the warranty. The ACL specifies information that must be given to consumers under a warranty against defects, including details of who is giving the warranty, the period for which the warranty applies and how to claim under the warranty.[68] In addition, the written document providing a warranty against defects must expressly advise consumers of the existence of the consumer guarantees under the ACL, as follows:

   > Our goods come with guarantees that cannot be excluded under the *Australian Consumer Law*. You are entitled to a replacement or refund for a major failure and for compensation for any other reasonably foreseeable loss or damage. You are also entitled to have the goods repaired or replaced if the goods fail to be of acceptable quality and the failure does not amount to a major failure.[69]

   This provision may alert consumers to the possible overlap between their statutory rights under the ACL and the supplementary rights provided by an extended warranty.

2. The ACL requires suppliers to take care in any representations they make about the relationship between the consumer guarantees provided under the legislation, and any extended warranty sold by the supplier. Section 29(1)(n) prohibits false or misleading representations concerning a "requirement to pay for a contractual right that is wholly or partly equivalent to any guarantee [under the CGL]".[70] A supplier who represents that a consumer must purchase an extended warranty in order to obtain rights equivalent to those provided under the CGL will contravene this provision.

3. It might be argued that if an extended warranty does not extend the protection available to consumers beyond that provided under the ACL, the extended warranty itself will be in breach of the implied guarantee of fitness for purpose under ACL, s 61.[71]

REMEDIES

[17.85] The remedies available to consumers for a failure to comply with a consumer guarantee are set out in Pt 5-4 of the ACL. The nature of the remedy available depends on the nature of the supplier's failure to comply with the guarantee. The CGL distinguishes between major and minor failures.

For goods, a major failure occurs if:

- the goods would not have been acquired by a reasonable consumer fully acquainted with the nature and extent of the failure;[72]

67 ACL, s 102(3).

68 *Competition and Consumer Regulations 2010* (Cth), reg 90.

69 *Competition and Consumer Regulations 2010* (Cth), reg 90(2).

70 ACL, s 29(1)(n).

71 *S v W & N Ltd* [2010] NZ Disp T 33 (30 May 2010).

72 ACL, s 260(a).

- the goods depart significantly from their description or a sample or demonstration model that was used when selling the goods;[73]
- the goods cannot easily be remedied to make them fit for purpose within a reasonable time;[74] or
- the goods are not of acceptable quality because they are unsafe.[75]

In *Vautin v BY Winddown, Inc (formerly Bertram Yachts) (No 4)*[76] the applicant purchased a recreational fishing vessel, some 74 feet long, for ocean-going travel, named "Revive". The laminated PVC foam core of the vessel (being the hull, the decks and the superstructure) were not constructed in accordance with the manufacturer's own specifications. For this reason, Derrington J held that there had been major failures to comply with the guarantees under ss 54 and 55 of the ACL. Revive would not have been acquired by a reasonable consumer fully acquainted with the nature and the extent of the defects which rendered the vessel unfit for the purpose for which vessels of that nature are commonly supplied; being ocean going, voyaging, and fishing.[77]

For services, a major failure occurs where:

- the services would not have been acquired by a reasonable consumer fully acquainted with the nature and extent of the failure;[78]
- the services or any product resulting from the services cannot easily be remedied to make them fir for purpose or achieve the result desired by consumers within a reasonable time;[79] or
- the supply of the services creates an unsafe situation.[80]

If a supplier's failure to comply with a consumer guarantee can be remedied and is not a major failure, the consumer may require the supplier to remedy the failure within a reasonable time.[81] The supplier may choose between providing a refund, a replacement, or a repair.[82] If the supplier refuses or fails to comply with a request to remedy a failure, the consumer may recover the reasonable costs of having the failure rectified or notify the supplier that the consumer rejects the goods.[83]

If a supplier's failure to comply with a consumer guarantee cannot be remedied or is a major failure, the consumer may reject the goods[84] or recover compensation for the reduction in the value of the goods.[85] In the case of services, if the failure to comply with the guarantee is

73 ACL, s 260(b).
74 ACL, s 260(c) and (d).
75 ACL, s 260(e)
76 *Vautin v BY Winddown, Inc. (formerly Bertram Yachts) (No 4)* [2018] FCA 426.
77 *Vautin v BY Winddown, Inc. (formerly Bertram Yachts) (No 4)* [2018] FCA 426, [252].
78 ACL, s 268(a).
79 See ACL, s 268(b), (c) and (d).
80 ACL, s 268(e).
81 ACL, ss 259(2)(a), 267(2).
82 ACL, s 261.
83 ACL, ss 259(2)(b), 267(2)(b).
84 See ACL, s 263 for the consequences of rejecting goods. See ACL, s 269 for the consequences of terminating a contract for the supply of services.
85 ACL, s 259(3).

a major failure or cannot be remedied, a consumer may terminate the contract for the supply of services or recover compensation for any reduction in the value of the services below the price payable by the consumer.[86]

A consumer may also recover compensation for any loss or damage they suffered because of the failure of a supplier to comply with a guarantee, if it was reasonably foreseeable that the consumer would suffer loss or damage because of the failure of the goods to comply with a consumer guarantee. For example, a consumer might recover water damage to a carpet caused by a faulty washing machine, or the costs of alternative transport where a bicycle bought to ride to work proved to be defective.

Limits on the remedies available for failure to comply with a consumer guarantee

[17.90] A consumer is not entitled to reject goods under the CGL if:

(a) the rejection period for the goods has ended;

(b) the goods have been lost, destroyed or disposed of by the consumer;

(c) the goods were damaged after being delivered to the consumer for reasons not related to their state or condition at the time of supply; or

(d) the goods have been attached to, or incorporated in, any real or personal property and they cannot be detached or isolated without damaging them.[87]

The rejection period for goods is the period from the time of the supply of the goods to the consumer, within which it would be reasonable to expect the relevant failure to comply with a guarantee to become apparent, having regard to:

(a) the type of goods;

(b) the use to which a consumer is likely to put them;

(c) the length of time for which it is reasonable for them to be used; and

(d) the amount of use to which it is reasonable for them to be put before such a failure becomes apparent.[88]

In *Nesbit v Porter*,[89] the New Zealand Court of Appeal held that the period of time that is considered reasonable is likely to be longer in cases where the goods are new or are of a kind used infrequently, or used only at a particular time of year.[90] The Court used the example of a pair of skis, noting that it would not be reasonable to expect a defect in skis bought in the summer to become apparent before the next winter. The Court also held that where the goods are of a type where regular inspection for defects is customary, or (as in the case of motor vehicles) required by the law, then the time period that is deemed reasonable will be shorter.[91]

86 ACL, s 267(3).

87 ACL, s 262.

88 ACL, s 262(2).

89 *Nesbit v Porter* [2000] 2 NZLR 465.

90 *Nesbit v Porter* [2000] 2 NZLR 465, [36].

91 *Nesbit v Porter* [2000] 2 NZLR 465, [37].

Actions for damages against manufacturers of goods

[17.95] Part 5-4, Div 2 of the ACL provides for consumers to claim damages against manufacturers for failures of goods to comply with the consumer guarantees. Consumers are able to seek damages from a manufacturer if goods are not of acceptable quality,[92] do not match their description,[93] fail to comply with an express warranty made by the manufacturer,[94] or if spare parts and repair facilities are not made available for a reasonable period.[95] Manufacturers are required to indemnify suppliers in respect of the costs of complying with the guarantee obligations relating to acceptable quality, descriptions applied to goods by manufacturers, and fitness for a purpose that a consumer makes known to a manufacturer.[96]

CGL and misleading conduct

[17.100] The ACL prohibits a person from making a misleading representation about the existence or exclusion of the consumer guarantees. It provides that:[97]

> [a] person must not, in trade or commerce, in connection with the supply or possible supply of goods or services or in connection with the promotion by any means of the supply or use of goods or services:
>
> …
>
> (m) make a false or misleading representation concerning the existence, exclusion or effect of any condition, warranty, guarantee, right or remedy (including a guarantee under Division 1 of Part 3-2);

Thus, for example, a supplier who states that a consumer has no recourse for goods that fail to be of acceptable quality, would breach this prohibition, as would signs displayed in a shop asserting that no refunds are available in any circumstances.

The Australian Competition and Consumer Commission and other state and territory-based regulators have the power to seek payment of a civil pecuniary penalty from a person who contravenes the prohibitions in s 29.[98]

ENFORCEMENT ACTION

[17.105] In enforcing the CGL, the Australian Competition and Consumer Commission has relied extensively on the prohibitions on misleading consumers as to the effect of the CGL, and the need to pay to purchase equivalent protection in ACL, s 29.[99]

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92 ACL, s 271(1).

93 ACL, s 271(3).

94 ACL, s 271(5).

95 ACL, s 271(5).

96 ACL, s 274.

97 ACL, s 29(1).

98 See ACL, s 224.

99 See, eg, *Australian Competition and Consumer Commission v Hewlett-Packard Australia Pty Ltd* [2013] FCA 653; *Australian Competition and Consumer Commission v Launceston Superstore Pty Ltd* [2013] FCA 1315; *Australian Competition and Consumer Commission v HP Superstore Pty Ltd* [2013] FCA 1317; *Australian Competition and Consumer Commission v Camavit Pty Ltd* [2013] FCA 1397; *Australian Competition and Consumer Commission v Avitalb Pty Ltd* [2014] FCA 222; *Australian Competition and Consumer Commission v Gordon Superstore Pty Ltd* [2014] FCA 452; *Australian Competition and Consumer Commission v Mandurvit Pty Ltd* [2014] FCA 464; *Australian Competition and Consumer Commission v Chopra* [2015] FCA 539; *Valve Corporation v Australian Competition and Consumer Commission* [2017] FCAFC 224; (2017) 258 FCR 190.

PERFORMANCE AND BREACH

PART VIII

CHAPTER **18**

Performance and breach

CONTRACTUAL DISPUTES

[18.05] It is important to appreciate that the cases usually studied in a course on contract law only represent a very small percentage of all contracts. The cases studied involve disputes between the parties which are litigated in court. Most contracts are performed without problems, and any problems arising are settled without judicial intervention. In those cases in which disputes arise, commonly the dispute is over either whether a contract was made at all (an issue discussed in Part II) or whether there has been a breach of that contract. A breach of contract occurs where a party does not perform his or her obligations in accordance with the terms of the contract.

THE PERFORMANCE REQUIRED BY THE CONTRACT

[18.10] Whether a breach has occurred depends on compliance with the terms of the contract, not on whether the party in breach was blameworthy, careless or affected by events outside his or her control.[1] Contractual liability is, in this sense, strict. What is required by way of performance of a contract depends on the terms of the contract and the construction of those terms, discussed in Part V.

In assessing whether there has been performance in accordance with the terms of a contract, important issues will be the standard of performance required and the time at which performance is required. A party must perform both in the way required by the contract and at the time required by the contract. In some cases, the standard of performance required by a contract will be expressly specified. For example, in a contract for the sale of apples, the contract may specify the type and grade of apple to be provided. In the absence of an express statement, the required standard of performance will be determined as a matter of construction or will be found in an implied term.[2] For example, in a contract between a solicitor and a client, there is an implied term that the solicitor will use the degree of care expected from an ordinary competent solicitor.[3] Similarly, the time at which performance is required may be specified in the contract. If a time is not specified, courts will imply a term requiring performance within a reasonable time.

1 Subject to the doctrine of frustration discussed in Chapter 15.
2 See discussion of terms implied in law in Chapter 14.
3 See also *Hawkins v Clayton* (1988) 164 CLR 539.

ORDER OF PERFORMANCE

[18.15] A contract may specify the order in which the parties must perform their obligations. Otherwise, the order of performance is a matter of construction.[4] Obligations may be consecutive; that is, the parties perform their respective obligations at different times. Obligations may also be concurrent. In these cases, the parties must be ready and willing to perform at the same time. For example, in a contract for the sale of land, the seller's obligation to transfer the land and the buyer's obligation to pay are mutually dependent and must therefore be performed concurrently.[5] Similarly, under the Sale of Goods Acts, unless otherwise agreed, "the seller must be ready and willing to give possession of the goods to the buyer in exchange for the price, and the buyer must be ready and willing to pay the price in exchange for possession of the goods".[6]

RESPONSES TO A BREACH OF CONTRACT

[18.20] Where one party (the *aggrieved party*) alleges that the other party has breached the contract, the other party may respond in a number of different ways. He or she may acknowledge the breach and possibly try to rectify the situation. The other party may also dispute that the breach has occurred, perhaps arguing that the aggrieved party's interpretation of what is required under the contract is incorrect. The other party might argue that there is a term in the contract limiting his or her liability for the breach (see Chapter 13). Another response is for the party alleged to be in breach to attempt to excuse his or her failure to perform in accordance with the terms of the contract. He or she may argue that there was some excuse for his or her failure to perform, for example, that the contract was not properly formed (see Part II), that the contract was frustrated (see Chapter 15) or that the enforceability of the contract is affected by misinformation, an abuse of power or illegality (see Part X).

REMEDIES AND THE RIGHT TO TERMINATE

[18.25] If a breach of contract is established, the aggrieved party will have a right to damages to compensate for any loss caused by the breach. If the contract has been fully performed, this may be a sufficient remedy. If the contract has been only partially performed, the aggrieved party may claim damages to compensate him or her for losses occasioned by the breach and also elect to continue with performance of the remainder of the contract. The other party may be more than happy with this course of action, which preserves the relationship between the parties. If the other party objects to continued performance, the aggrieved party may seek the remedy of specific performance of the contract (see Chapter 30).

In some cases, an aggrieved party might want to terminate the contract following breach. Termination is a "self-help" response to breach which does not directly require the assistance of a court. The aggrieved party may be motivated to terminate the contract because he or she no longer trusts the other party to perform the contract or the aggrieved party might be using

4 See, eg, *Burton v Palmer* [1980] 2 NSWLR 878, 895.

5 See, eg, *Foran v Wight* (1989) 168 CLR 385.

6 *Sale of Goods Act 1954* (ACT), s 32; *Sale of Goods Act 1923* (NSW), s 31; *Sale of Goods Act* (NT), s 31; *Sale of Goods Act 1896* (Qld), s 30; *Sale of Goods Act 1895* (SA), s 28; *Sale of Goods Act 1896* (Tas), s 33; *Goods Act 1958* (Vic), s 35; *Sale of Goods Act 1895* (WA), s 28.

the breach as a reason to escape a contract he or she no longer finds beneficial. Not all breaches give rise to a right to terminate a contract. The right to terminate for breach or otherwise is discussed in Part VIII. The right to terminate a contract may be lost in some circumstances. These circumstances (and restrictions on the right to terminate) are discussed in Chapter 25. Following termination, the aggrieved party will continue to have a right to damages. He or she may also have claims in debt (see Chapter 29) and restitution (see Chapter 10).

TERMINATION

PART IX

Bringing a contract to its end

[PtIX.05] Having discussed the formation and terms of a contract, we now consider how a contract may be brought to an end. Ordinarily, the parties will perform all of the obligations required under their contract. In some cases, one or both of the parties may have a right to terminate the contract before it has been completely performed. Termination releases the parties from any obligation to perform the contract any further.

A right to terminate may have a number of benefits for the party (the *terminating party*) entitled to exercise that right. A right to terminate may give the terminating party a "self-help" response to breaches of the contract. This right of response may in turn increase the other party's incentive to comply with the terms of the contract. This is because if a contract is terminated, the other party may lose the benefit he or she expected to gain from performance of the contract and also any expenditure incurred in preparing to perform the contract.[1] A right to terminate may also be a useful bargaining chip. For example, it may provide the terminating party with a means of initiating renegotiation of the contract where the express terms prove inadequate to deal with events affecting its performance. Alternatively, a right to terminate may provide the terminating party with the power to end a contractual relationship which has broken down.

Under the common law, a right to terminate may arise in a number of different ways, including the agreement of the parties, non-fulfilment of a contingent condition, breach of a condition, breach of an intermediate term which is sufficiently serious, fundamental breach or repudiation (sometimes also referred to as renunciation).[2] Each of these different sources of a right to terminate is discussed in the following chapters, as are the consequences of termination and restrictions on the right to terminate.

1 See Harris, "Incentives to Perform, or Break Contracts" [1992] *Current Legal Problems* 29, 36, 41.

2 See [22.05].

Termination vs rescission

[PtIX.10] Termination of a contract has a prospective effect. While termination discharges the parties from contractual obligations arising in the future, any rights that have accrued prior to termination continue unaffected and may be enforced by the relevant party.[3] Termination may be contrasted with rescission. Rescission is the remedy often granted where the contract is found to be vitiated by reason of misrepresentation, mistake, undue influence or unconscionable dealing. Rescission has a retrospective effect. Where a contract is rescinded, the contract is unwound and the parties are restored to the positions they were in before the contract was made. However, courts do not always use the term "rescission" in this precise sense.[4] In many of the cases dealing with what is properly characterised as termination of a contract, courts refer to rescission.[5] Whatever label is used, the proper consequences of the response sought should be kept in mind.

3 *McDonald v Dennys Lascelles Ltd* (1933) 48 CLR 457, 477.
4 See *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827, 844.
5 *FCT v Reliance Carpet Co Pty Ltd* [2008] HCA 22; (2008) 236 CLR 342, [2].

CHAPTER **19**

Termination by agreement

CATEGORIES OF AGREEMENT TO TERMINATE

[19.05] The law of contract concerns consensual obligations. It is not surprising, therefore, that contract law allows parties to make an agreement about terminating their contract. This may be done in a number of ways. The parties' original contract may include an express term providing for its termination. Alternatively, the parties may make a subsequent agreement expressly terminating their original contract. It is also possible that courts may find an implied agreement by the parties to terminate their contract, in either an existing contract or a subsequent contract.

TERMINATION UNDER THE ORIGINAL CONTRACT

Express powers to terminate

[19.10] It is common, particularly in long-term commercial contracts, for parties to include an express term providing for when or how their contract may be brought to an end. A number of different models may be used. The parties might deal with termination by providing that the contract is to last for a fixed period of time. After that time expires, the contract will automatically come to an end. An example of a fixed-term contract would be a lease for a specified number of years. Alternatively, or additionally, the parties might agree that one or both of them will have the right to terminate the contract. A right to terminate may take different forms. One of the parties might be given a broad discretionary right to terminate at any time. This is sometimes described as termination "at will". A party might be given a right to terminate after a specified period of notice. Yet another possibility is for a party to be given a right to terminate which is "triggered" by certain specified events, such as a breach of the contract by the other party or the non-fulfilment of a contingent condition.[1]

A term dealing with termination may specify a procedure to be followed before the contract is terminated. For example, the contract may require a party to give notice of his or her decision to terminate in a particular form. In some cases, courts have required precise compliance with

1 On contingent conditions, see Chapter 20.

the termination procedure, resolving any questions of interpretation against the interests of the party purporting to terminate a contract. The result of this sort of strict interpretation is that a party purporting to exercise a contractual right to terminate may lose the right through some minor or technical failure to comply precisely with the termination procedure.[2]

However, the decision of the High Court in *Pan Foods Company Importers & Distributors Pty Ltd v Australia and New Zealand Banking Group Ltd*[3] suggests that requirements of commercial contracts should not be construed in an overly technical or restrictive manner. Kirby J stated that commercial contracts "should be construed practically, so as to give effect to [the parties'] presumed commercial purposes and so as not to defeat the achievement of such purposes by an excessively narrow and artificially restricted construction".[4] On this approach, it would not be fatal that a party did not comply with a strict construction of a specified procedure for termination, provided the apparent defect did not prejudice the other party in any substantial way.

In *Pan Foods Company Importers & Distributors Pty Ltd v Australia and New Zealand Banking Group Ltd*, a bank provided finance to Pan Foods in the form of a number of loans. The relevant loan contract provided that if any of a number of specified events of default occurred, the bank could terminate its obligations under the agreement and declare any moneys owing immediately due and payable. In order to terminate, the bank was required to give Pan Foods notice. Under the terms of the contract, notice of termination by the bank had to be given by an "authorised representative" of the bank in writing. Following an event of default by Pan Foods, the bank instructed its solicitors to prepare the necessary notice. An officer of the bank, who was an authorised representative, then attended the premises of Pan Foods, where he handed the notice to the office holders of Pan Foods with an explanation of its purpose. Pan Foods sought to challenge the validity of the notice. One argument was that the notice was from the solicitors of the bank, not the bank itself. This argument was rejected by the High Court. The agreement did not specifically require the notice to be signed. The circumstances in which the notice was handed over made it clear that the notice was from the bank.[5]

Implied right to terminate a contract of otherwise indefinite duration

[19.15] Where a contract is silent as to its duration, courts may be prepared to imply a right for one or both of the parties to terminate the contract.[6] The right will be based on the inference that the parties would not have intended the contract to continue indefinitely. Where a right to terminate is implied in a contract of otherwise indefinite duration, courts will usually require the party terminating to give reasonable notice of termination to the other party. The requirement of reasonable notice allows the parties "to bring to an end in an orderly way [their] relationship" and "a reasonable opportunity to enter into alternative arrangements and to wind up matters which arise out of their relationship".[7]

2 See, eg, *Lintel Pines Pty Ltd v Nixon* [1991] VR 287.
3 *Pan Foods Company Importers & Distributors Pty Ltd v Australia and New Zealand Banking Group Ltd* [2000] HCA 20.
4 *Pan Foods Company Importers & Distributors Pty Ltd v Australia and New Zealand Banking Group Ltd* [2000] HCA 20, [24].
5 *Pan Foods Company Importers & Distributors Pty Ltd v Australia and New Zealand Banking Group Ltd* [2000] HCA 20, [5]–[6], [25], [56].
6 See, eg, *Crawford Fitting Co v Sydney Valve & Fitting Pty Ltd* (1988) 14 NSWLR 438.
7 *Crawford Fitting Co v Sydney Valve & Fitting Pty Ltd* (1988) 14 NSWLR 438, 448.

The period of time required for reasonable notice will depend on the circumstances of the particular case.[8] What is a reasonable period of time is a question of fact and, as Brooking J noted in *Alivar v Calandra & Co Pty Ltd*, it "is a matter about which opinions will probably differ substantially".[9] The appropriate period of reasonable notice was considered in *Crawford Fitting Co v Sydney Valve & Fitting Pty Ltd*[10] in relation to a distributorship contract. Under a distributorship contract, one party, the distributor, contracts to sell the products of a manufacturer. In performing the contract, the distributor may incur considerable expenditure in establishing and then expanding its distribution network. The distributor will hope to recoup this expenditure through the successful operation of the business. On the particular facts of *Crawford Fitting Co v Sydney Valve & Fitting Pty Ltd*, the New South Wales Court of Appeal concluded that a period of six months' notice prior to terminating the contract under an implied term was sufficient. Some more general comments on the requirement of notice were made by McHugh JA. His Honour said:

> It will often be a common purpose of a distributorship agreement that the relationship of the parties will continue for long enough after the giving of a notice of termination to enable the distributor to recoup any extraordinary expenditure or effort. Otherwise a distributor would have no incentive to make or outlay additional effort or expenditure for the mutual benefit of the parties. … An appropriate period of notice can give the distributor the opportunity to exploit any extraordinary effort or expenditure.[11]

McHugh JA also indicated that ordinary effort or expenditure will not usually be relevant to the period of notice. His Honour explained:

> Inability to reap the benefits of ordinary expenditure or effort incurred during the course of the agreement may be regarded as a business risk which a distributor takes when he enters into an agreement terminable at any time. If the nature of the business produces a lapse of time between effort or expenditure and earning, a certain amount of such effort or expenditure will go unrewarded whatever period of notice is given.[12]

TERMINATION BY SUBSEQUENT AGREEMENT

Express agreements

[19.20] Parties may terminate a contract by making a subsequent agreement under which each agrees to release the other from the original contract. To be binding in law, an agreement to terminate an existing agreement must comply with the ordinary rules of contract formation, including the requirement of consideration.[13] Where both parties still have obligations to perform under the contract, each party will provide consideration in agreeing to release the other party from his or her remaining obligations.

Partly performed contracts and the issue of consideration

[19.25] The issue of consideration becomes more difficult where one party (the *performing party*) has fully performed the original contract and the other party (the *non-performing party*) has not. The performing party will be able to give good consideration by agreeing to

8 *Crawford Fitting Co v Sydney Valve & Fitting Pty Ltd* (1988) 14 NSWLR 438, 444.
9 *Alivar v Calandra & Co Pty Ltd* (Unreported, Supreme Court of Victoria, Brooking J, 21 February 1988), 13.
10 *Crawford Fitting Co v Sydney Valve & Fitting Pty Ltd* (1988) 14 NSWLR 438.
11 *Crawford Fitting Co v Sydney Valve & Fitting Pty Ltd* (1988) 14 NSWLR 438, 445–6.
12 *Crawford Fitting Co v Sydney Valve & Fitting Pty Ltd* (1988) 14 NSWLR 438, 445–6.
13 On consideration, see Chapter 4. On the other formation requirements, see Chapters 3 and 5–7.

release the non-performing party from his or her obligations. However, because the performing party has no remaining obligations under the contract, the non-performing party cannot give consideration by providing a release.

Parties who wish to make a binding agreement to terminate a contract that one of them has fully performed may avoid the difficulties of consideration by executing a deed to terminate the contract.[14] The difficulties may also be avoided by the non-performing party providing some "fresh" consideration.[15] In this situation, the parties may make a contract known as an *accord and satisfaction*:

> [An] accord and satisfaction is the purchase of a release from an obligation whether arising under contract or tort by means of any valuable consideration, not being the actual performance of the obligation itself. The accord is the agreement by which the obligation is discharged. The satisfaction is the consideration which makes the agreement operative.[16]

An accord and satisfaction may be used where one party agrees to release another party from any cause of action in contract or tort. We are here concerned with the use of an accord and satisfaction where a performing party agrees to release a non-performing party from any further obligation to perform a contract. In this context, under an accord and satisfaction, the non-performing party will provide to the performing party some fresh consideration, additional to his or her obligations under the original contract. For example, the non-performing party may agree to pay money to the performing party or to perform new or different obligations. This additional consideration will support the promise from the performing party to release the non-performing party from his or her obligations under the original contract.

The fresh consideration provided under an accord and satisfaction may be provided by the non-performing party in the form of a promise or by the actual doing of the promised act.[17] If the consideration from the non-performing party is a promise – for example, a promise to pay money – the accord and satisfaction will be complete and the non-performing party will be released from the obligation to further perform the original contract immediately upon the promise being made. If the consideration is the promised act – for example, actually paying the money – the release will only occur once the act is performed.

Whether the consideration for an accord and satisfaction is a promise or an act is a matter of interpretation.[18] It has been suggested that, where the issue is uncertain, courts are inclined to interpret an accord and satisfaction as requiring performance of the promised act, not merely the promise.[19] This interpretation provides better protection for a performing party in releasing the non-performing party from his or her obligations.

Formal requirements

[19.30] As already discussed, in all Australian jurisdictions, the equivalent of the *Statute of Frauds 1677* (29 Car II c 3) (UK) requires certain contracts to be in writing.[20] However, it has

14 On deeds, see [4.120].

15 On fresh consideration, see [4.80].

16 *British Russian Gazette & Trade Outlook Ltd v Associated Newspapers Ltd* [1933] 2 KB 616, 643–4.

17 *McDermott v Black* (1940) 63 CLR 161, 184; *Tallerman & Co Pty Ltd v Nathan's Merchandise (Vic) Pty Ltd* (1957) 98 CLR 93, 114.

18 *McDermott v Black* (1940) 63 CLR 161, 185.

19 See Greig and Davis, *The Law of Contract* (1987), p 1185.

20 On the *Statute of Frauds 1677* (29 Car II c 3) (UK), see Chapter 7.

been held that writing is not required for an agreement to terminate an existing contract.[21] An original contract required to be in writing may be terminated by a subsequent oral contract. Writing will be required where the subsequent contract seeks to vary, rather than terminate, the original contract.[22]

Termination inferred from subsequent agreement

[19.35] The parties may sometimes make a subsequent agreement without explaining how that agreement is to interact with their original contract. In such cases, there are two possible interpretations of the parties' subsequent agreement. The parties may have intended the subsequent agreement to replace, and thus terminate, the original contract,[23] or they may have intended the subsequent agreement merely to vary or supplement the original contract.[24] In some cases, it may be necessary to decide which of these two possibilities has occurred: "For example, something may turn upon the place, or the time, or the form, of the contract, and it may therefore be necessary to decide whether the original subsists."[25]

In the absence of an express term explaining the relationship between the two agreements, whether a subsequent agreement varies or terminates the original contract will depend on the intentions of the parties as disclosed by the terms and circumstances of the subsequent agreement.[26] The distinction between the two possibilities is a "matter of degree".[27] An intention to terminate the original contract will be inferred where, because the obligations in the subsequent agreement are inconsistent with those in the original contract, the two agreements cannot be supposed to have been intended to co-exist.[28] Conversely, the parties are unlikely to have intended to terminate the original contract where the subsequent agreement cannot stand alone as a new and independent contract.[29] More generally, an intention to terminate the original contract is unlikely to be inferred where the parties cannot be presumed to have intended to abandon their rights under the original contract.[30]

The importance of the distinction between termination and variation is illustrated by the decision of the High Court in *Concut Pty Ltd v Worrell*.[31] In 1980, an employee commenced employment under an oral contract. In 1986, the parties executed a written employment contract. In 1988, the employer terminated the employment of the employee without notice.

21 See *Tallerman & Co Pty Ltd v Nathan's Merchandise (Vic) Pty Ltd* (1957) 98 CLR 93, 113, 122.

22 See *Suttor v Gundowda Pty Ltd* (1950) 81 CLR 418, 440; *Tallerman & Co Pty Ltd v Nathan's Merchandise (Vic) Pty Ltd* (1957) 98 CLR 93, 113, 122.

23 *Wallace-Smith v Thiess Infraco (Swanston) Pty Ltd* [2005] FCAFC 49; (2005) 218 ALR 1.

24 *Tallerman & Co Pty Ltd v Nathan's Merchandise (Vic) Pty Ltd* (1957) 98 CLR 93, 112–3, 122, 135, 144.

25 *Commissioner of Taxation v Sara Lee Household & Body Care (Aust) Pty Ltd* [2000] HCA 35; (2000) 201 CLR 520, [22].

26 *Tallerman & Co Pty Ltd v Nathan's Merchandise (Vic) Pty Ltd* (1957) 98 CLR 93, 112–3, 122–6, 135, 144; *Commissioner of Taxation v Sara Lee Household & Body Care (Aust) Pty Ltd* [2000] HCA 35; (2000) 201 CLR 520, [19]–[26]; *Concut Pty Ltd v Worrell* [2000] HCA 64, [20], [56].

27 *Tallerman & Co Pty Ltd v Nathan's Merchandise (Vic) Pty Ltd* (1957) 98 CLR 93, 113.

28 See *British & Beningtons Ltd v North Western Cachar Tea Co Ltd* [1923] AC 48, 62.

29 See *Tallerman & Co Pty Ltd v Nathan's Merchandise (Vic) Pty Ltd* (1957) 98 CLR 93, 112–3.

30 *Concut Pty Ltd v Worrell* [2000] HCA 64, [20], [56].

31 *Concut Pty Ltd v Worrell* [2000] HCA 64. See also criticism of this decision in Carter and Stewart, "The Effect of Formalising an Employment Contract: The High Court Misses an Opportunity" (2001) 17 *Journal of Contract Law* 181.

The employer defended this action on the ground that the employee had breached his conditions of employment. The misconduct occurred prior to 1986. The Court of Appeal for the Supreme Court of Queensland held that the written agreement was a new and discrete contract which terminated and replaced the oral contract. Accordingly, as there had been no breach of any term of the written agreement, the employer had no right to terminate the employment of the employee without notice. The High Court allowed an appeal against this decision.

The High Court held that the text of the written agreement, as well as the surrounding circumstances, indicated the parties' intention was not for the written agreement to become the exclusive charter of the contractual rights and duties of the parties.[32] For example, the court noted that the written agreement expressly preserved the accrued rights of the employee in respect of leave entitlements.[33] More generally, the court considered it unlikely that the parties adopted the written agreement with the purpose of depriving the employer of any accrued rights under the original contract.[34] The court concluded that the employment relationship established under the original oral contract continued, supplemented by the written agreement. Consequently, the employer was not precluded by the existence of the written agreement from relying on an earlier breach to dismiss the employee.[35]

Where a subsequent contract does not change the obligations under the original contract, but rather substitutes new parties, the subsequent contract is known as a *novation* and is treated as a new contract discharging the original one.[36]

Termination by abandonment

[19.40] In some cases, courts will treat the parties as having conducted themselves so as to mutually abandon their contract.[37]

Abandonment may be inferred where the parties to a contract indicate that neither considers the contract should be further performed.[38] Termination by abandonment is sometimes analysed as an inferred agreement to discharge the contract.[39] Similarly, parties may find themselves estopped from relying on the provisions of the contract where they have induced an assumption that they have abandoned their contractual rights.

In *DTR Nominees Pty Ltd v Mona Homes Pty Ltd*,[40] the parties adopted different interpretations of the contract and both purported to terminate the contract for the other's repudiation. The High Court held that neither of the notices of termination was effective and that the contract was at that time still in existence. However, Stephen, Mason and Jacobs JJ, with whom Aickin J agreed, considered that, by the time the proceedings were commenced,

32 *Concut Pty Ltd v Worrell* [2000] HCA 64, [20].

33 *Concut Pty Ltd v Worrell* [2000] HCA 64, [54].

34 *Concut Pty Ltd v Worrell* [2000] HCA 64, [54].

35 *Concut Pty Ltd v Worrell* [2000] HCA 64, [56].

36 See [11.37]. See further *Vickery v Woods* (1952) 85 CLR 336, 344, 345, 349; *T C Industrial Plant Pty Ltd v Robert's Queensland Pty Ltd* (1963) 180 CLR 130, 137–8; *Flightvision Pty Ltd v Onisforou* [1999] NSWCA 323; (1999) 47 NSWLR 473.

37 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 434; see also *Summers v Commonwealth* (1918) 25 CLR 144; *Paal Wilson and Co /S v Partenreederei Hannah Blumenthal* [1983] 1 AC 854.

38 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 434 (see [22.60]).

39 *Fitzgerald v Masters* (1956) 95 CLR 420, 432–3.

40 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423.

neither party regarded the contract as still being on foot. Accordingly, the parties should be regarded as having abandoned their contract.[41] As McLure P (Newnes J and Le Miere J agreeing) noted in *Hancock Prospecting Pty Ltd v Wright Prospecting Pty Ltd*, "there was no express finding of an estoppel or an implied contract to abandon"[42] in *DTR Nominees Pty Ltd v Mona Homes Pty Ltd*. McLure P suggests that the court's abandonment finding is thus best understood as based on principles of waiver.[43]

A court may also infer abandonment where an "inordinate" length of time has been allowed to elapse "during which neither party has attempted to perform, or called on the other to perform".[44] However, where one party has partly performed a contract, courts may be less likely to conclude from a later period of inactivity that the contract has been abandoned. In such cases, it will generally be unlikely that the party who has partly performed would have been prepared to walk away from the work done or money paid.[45]

In *Cedar Meats (Aust) Ptd Ltd v Five Star Lamb Pty Ltd*,[46] the Victorian Court of Appeal considered the consequences of finding that a contract has been abandoned. The court found that "[a]bsent a clear indication to the contrary, it is to be inferred that the abandonment of a contract operates prospectively without prejudice to accrued entitlements".[47] The appellant entered a contract with the respondent to provide meat processing services. When the respondent experienced financial difficulty, the appellant agreed with the respondent that the contract should come to an end, subject to the respondent giving a commitment that it would re-engage the appellant if its financial position improved. The court held that the parties' agreement amounted to an abandonment of the contract. The respondent argued that the appellant's delay in enforcing its rights amounted to an election to waive rights that had accrued under the abandoned contract. The court rejected this argument. In the context of the circumstances that led to the abandonment, the appellant could not be said to have elected to waive its right to enforce accrued rights.

41 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 434.

42 *Hancock Prospecting Pty Ltd v Wright Prospecting Pty Ltd* [2012] WASCA 216, [211].

43 *Hancock Prospecting Pty Ltd v Wright Prospecting Pty Ltd* [2012] WASCA 216, [213].

44 *Fitzgerald v Masters* (1956) 95 CLR 420, 432.

45 See, eg, *Fitzgerald v Masters* (1956) 95 CLR 420.

46 *Cedar Meats (Aust) Ptd Ltd v Five Star Lamb Pty Ltd* [2014] VSCA 32.

47 *Cedar Meats (Aust) Ptd Ltd v Five Star Lamb Pty Ltd* [2014] VSCA 32, [19].

CHAPTER **20**

Failure of a contingent condition

CONTINGENT CONDITIONS

[20.05] Parties may make the performance of their contract conditional upon the occurrence of a specified event that neither party promises to ensure will occur. For example, a buyer may undertake to buy the seller's car subject to the buyer obtaining a loan or a mechanic's approval of the car. This sort of qualifying term is sometimes called a *contingent condition*. The term is a condition in the sense that the performance of the contract is conditional upon the specified event taking place. The term is contingent in the sense that neither party undertakes to ensure that the event specified in the condition will occur.

Parties may also make performance of their contract conditional upon a particular event *not* occurring. For example, the parties may provide that their contract for the sale of goods will come to an end should the seller's licence to import the goods be revoked. Most of the following discussion refers to conditions which contemplate an event occurring. However, the same principles apply to contingent conditions that depend on an event not occurring.

A contingent condition may qualify the performance of all of the obligations under a contract or a particular obligation only. The following discussion generally refers to conditions that qualify performance of all obligations. Many of the principles discussed also apply to a contingent condition qualifying performance of a particular obligation.

DIFFERENT USES OF THE WORD "CONDITION"

Contingent and promissory conditions

[20.10] As just discussed, a contract term may be described as a *contingent condition* where the performance of the contract is conditional on the occurrence of an event that neither party promises to ensure. If the event does not occur, then one or both of the parties will be entitled to terminate the contract. However, there will be no breach of the contract because neither party has promised to ensure that the condition will occur and hence no right to damages will accrue. For example, a contract for the sale of land may be made subject to the purchaser obtaining finance to complete the purchase. If the purchaser does not obtain finance by the required date, either party may terminate the contract, but the purchaser will not be liable for damages merely for failing to obtain the finance.

The word "condition" is also sometimes used to refer to a contractual promise which is *essential* in that a breach of the promise by one party will entitle the other party to terminate the contract and claim damages.[1] For example, where a contract for the sale of land fixes a date at which the parties must perform their respective obligations – payment of money and transfer of the property – and further states that performance by each party on this date is essential, then the time for performance of the obligations will be a promissory condition.[2] If one party fails to perform at the specified time, the other party may terminate the contract and will have a right to damages for the breach of the condition. Whether a condition is promissory or contingent depends on the construction of the contract in the circumstances of the case.[3]

Contingent conditions to performance and formation

[20.15] Where a contingent condition qualifies the *performance* of a contract, the parties will not be obliged to perform the contract until the condition is fulfilled. Their obligation to perform is in this sense "suspended". However, the presence of a contingent condition relating to performance does not prevent a contract from coming into existence. Even before the condition is fulfilled, the parties will be bound to the contract and may not do anything inconsistent with the relevant contractual obligations. For example, consider a contract for the sale of land subject to the purchaser obtaining finance to complete the sale. Neither party will be obliged to perform the contract unless, and until, the purchaser obtains finance or the condition is waived.[4] However, the vendor would breach the contract by selling the property to someone else. The vendor would only be free to sell the property to another party after the original contract had been terminated on the ground that the purchaser could not obtain finance or did not obtain finance by the required time.[5]

A contingent condition may also qualify the *formation* of a contract.[6] Where a contingent condition qualifies formation of a contract, the parties are not bound by the contract unless and until the condition is fulfilled. For example, consider a document which states that the

1 See Chapter 21.
2 On time being of the essence, see further Chapter 23.
3 *McTier v Haupt* [1992] 1 VR 653, 658–9.
4 On waiver of a contingent condition, see [20.55].
5 Cf *Nyhuis v Anton* [1980] Qd R 34, 37.
6 See [5.70].

parties' agreement in respect of the sale of land is subject to the preparation of a formal contract by the parties' solicitors and the execution of that contract. The condition in this case is likely to be interpreted as relating to the formation of a binding contract. If so, the parties will have no contractual obligations until a formal contract is prepared and executed; either party may withdraw from the agreement prior to that time.

While the issue depends on the construction of the parties' agreement, courts tend to prefer to treat a contingent condition as qualifying performance, and not formation.[7] In support of this approach, the High Court has explained: "In most cases it is artificial to say, in the face of the details settled upon by the parties, that there is no binding contract unless the event in question happens."[8]

Contingent conditions precedent and subsequent to performance

[20.20] A contingent *condition precedent* to performance is one that must be fulfilled before the parties are bound to perform their contract.[9] A *condition subsequent* is one where the parties' obligation to perform is immediately binding but will come to an end should the event specified in the condition occur.[10] For example, a contingent condition in a contract for the sale of goods providing that performance of the parties' obligations is subject to the vendor obtaining an import licence would be a condition precedent. A condition that performance of the contract is subject to the vendor's import licence not being revoked would be a condition subsequent.

The distinction between conditions precedent and subsequent has been criticised as "an artificial and theoretical question".[11] As Mason J explained in *Meehan v Jones*:

> In one sense performance of the condition or non-avoidance for breach of it is precedent to the right of a party to call for the performance of a contract. In another sense there is a valid and binding contract which may be determined for non-performance of the condition, and in this sense the condition is subsequent, not precedent.[12]

In dealing with contingent conditions, it is more important to identify the effect of the condition than to attach the labels "precedent" or "subsequent".[13]

THE DUTY TO CO-OPERATE

[20.25] Where a condition is contingent, the parties do not undertake to ensure that the condition is fulfilled. Nonetheless, the parties may be under some obligation with respect to the condition. The contract may expressly require one or both of the parties to use a certain level of effort in attempting to ensure that the condition is fulfilled, for example, by requiring a party to use his or her "best endeavours" or "best efforts".[14] In the absence of an express

7 *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 552.
8 *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 552.
9 See, eg, *Meehan v Jones* (1982) 149 CLR 571; *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537.
10 See, eg, *Maynard v Goode* (1926) 37 CLR 529; *Suttor v Gundowda Pty Ltd* (1950) 81 CLR 418.
11 *Meehan v Jones* (1982) 149 CLR 571, 592. See also *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 541, 556.
12 *Meehan v Jones* (1982) 149 CLR 571, 592.
13 *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 541.
14 See, eg, *Hawkins v Pender Bros Pty Ltd* [1990] 1 Qd R 135; *Etna v Arif* [1999] VSCA 99; [1999] 2 VR 353.

obligation of this kind, the parties may be under an implied duty to co-operate.[15] A duty to co-operate will require the parties to do everything reasonably within their power to see that the condition is fulfilled.[16] For example, in *Butts v O'Dwyer*,[17] the court was of the opinion that, where a transfer of property was subject to the Minister's consent being obtained, there was an implied obligation on the part of the transferor to do all things reasonable to obtain the consent.[18]

If a contingent condition is not fulfilled due to a breach of the implied duty to co-operate, the party in breach will not be entitled to rely on the failure of the condition as a reason for terminating the contract.[19] In some such cases, the condition may be treated as fulfilled, probably on the ground of estoppel.[20] For example, *Mackay v Dick*[21] concerned a contract for the sale of a digging machine. The buyer argued that he did not have to pay for the machine because it did not satisfy certain tests specified in the contract. In fact, the machine had never been properly tested. The House of Lords held that, in failing to test the machine, the buyer had breached the duty to co-operate. Due to this breach, the buyer was not entitled to rely on the failure of the condition relating to testing as a reason for not paying for the machine.[22]

By contrast, in *Newmont Pty Ltd v Laverton Nickel NL*,[23] a contract for a joint venture between two companies in provisional liquidation was subject to the approval of the court. One of the companies breached the obligation to do all that was reasonably required to ensure that the contingent condition was fulfilled. The Privy Council held that this was not a case where the condition should be treated as fulfilled. The companies had no power to dispense with performance of the condition, which was for the benefit of others, and the agreement could not be performed unless the condition was fulfilled.[24]

Where a party breaches the duty to co-operate in fulfilling a contingent condition, damages will usually be available to the other party. It is possible that the damages will be discounted to take account of the fact that, even if the party in breach had co-operated, the condition might not have been fulfilled.

NON-FULFILMENT

When will a contingent condition not be fulfilled?

[20.30] A contingent condition will not be fulfilled where the events that occur are contrary to what was contemplated in the condition. For example, where performance of a contract

15 On the duty to co-operate, see also [14.135].

16 See, eg, *Butts v O'Dwyer* (1952) 87 CLR 267; *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537.

17 *Butts v O'Dwyer* (1952) 87 CLR 267, 280.

18 See also *Meehan v Jones* (1982) 149 CLR 571; *Booker Industries Pty Ltd v Wilson Parking (Qld) Pty Ltd* (1982) 149 CLR 600; *CSS Investments Pty Ltd v Lopiron Pty Ltd* (1987) 76 ALR 463; *Service Station Association Ltd v Berg Bennett & Associates Pty Ltd* (1993) 45 FCR 84, 99.

19 *Suttor v Gundowda Pty Ltd* (1950) 81 CLR 418, 441; *Gange v Sullivan* (1966) 116 CLR 418, 441–2; *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 545, 566; *Lombardo v Morgan* [1957] VR 153, 159.

20 Carter, *Contract Law in Australia* (7th ed, 2018), [28-09].

21 *Mackay v Dick* (1881) 6 App Cas 251.

22 *Mackay v Dick* (1881) 6 App Cas 251, 264, 270.

23 *Newmont Pty Ltd v Laverton Nickel NL* [1983] 1 NSWLR 181.

24 *Newmont Pty Ltd v Laverton Nickel NL* [1983] 1 NSWLR 181, 188–9.

is subject to the purchaser obtaining an import licence, the condition will fail if the licence is refused.

A contingent condition will also fail where the condition is not fulfilled within the period of time required by the contract. The time for fulfilment of a contingent condition may be expressly specified in the contract. If no time is specified, courts will construe the contract as requiring the condition to be fulfilled within a reasonable period of time.[25] What amount of time is reasonable will be determined by the circumstances of the case. Where a date is fixed for completion of the contract, but not for the fulfilment of a condition precedent, the date by which the condition must be fulfilled will usually be the date of completion.[26]

Objective or subjective test?

[20.35] Whether the fulfilment of a contingent condition is judged by an objective or a subjective test depends on the language of the condition. In some cases, the condition will clearly refer to an objective fact. For example, where performance of a contract is subject to the purchaser obtaining an import licence, the condition either will or will not be fulfilled depending on the objective fact of whether or not the licence is granted.

In other cases, a contingent condition may depend upon a discretionary judgment on the part of one of the parties, for example, one party may have to be "satisfied" with or "approve" a particular matter. In these sorts of cases, fulfilment of the condition will have a subjective element; the party making the judgment must at least act honestly in deciding whether or not the condition has been fulfilled.[27] There is also a question as to whether the party making the judgment must act reasonably. For example, a contract for the sale of land may be subject to the purchaser obtaining "satisfactory finance". The purchaser will not be entitled to claim that the condition has failed unless the purchaser is honestly dissatisfied with the finance offered to him or her. Assuming the purchaser is honestly dissatisfied, should the purchaser also have to be reasonably dissatisfied with the finance offered before claiming that the condition has not been fulfilled?

Whether a duty of reasonableness should apply to a condition of satisfaction has not been resolved in Australian contract law. The leading High Court authority, *Meehan v Jones*,[28] concerned a contract for the sale of land subject to the purchaser obtaining "satisfactory finance". Gibbs CJ and Murphy J thought that the purchaser merely had to make an honest assessment of the finance available.[29] Mason J expressly refrained from making a decision and acknowledged arguments for both parties.[30] Mason J commented:

> There is some ground for thinking that the parties contemplated that the question was to be left to the honest judgment of the [party given the discretion] rather than the judgment of the court as to whether [that party] acted reasonably in the circumstances.

25 *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 543, 554, 559, 567–8.

26 For example, *Aberfoyle Plantations Ltd v Cheng* [1960] AC 115; *Australian Mutual Provident Society v Landsa Ltd* [1997] 1 VR 564, 574.

27 *Meehan v Jones* (1982) 149 CLR 571, 589.

28 *Meehan v Jones* (1982) 149 CLR 571.

29 *Meehan v Jones* (1982) 149 CLR 571, 580, 597.

30 *Meehan v Jones* (1982) 149 CLR 571, 591. See also *Zieme v Gregory* [1963] VR 214, 223; *Freedom v AHR Constructions Pty Ltd* (1987) 1 Qd R 59, 61.

> [On the other hand] it would make for greater consistency to say that, if the purchaser is bound to act reasonably in seeking to obtain finance, he is bound to act reasonably as well as honestly in deciding whether finance was satisfactory. So understood the special condition would reserve an even balance between the vendors and the purchaser.'[31]

Wilson J also did not express a concluded view, but indicated a preference for the obligation being one of honesty only.[32]

Somewhat stronger support for a standard of reasonableness in assessing "satisfaction" with a particular matter under a contract is found in the decision of the Court of Appeal for the Supreme Court of New South Wales in *Renard Constructions (ME) Pty Ltd v Minister for Public Works*.[33] That case concerned a clause that conferred, among other things, a power on the principal to terminate a building contract for certain breaches by the contractor. The clause also imposed conditions upon the principal's exercise of the power to terminate. The clause provided that, upon default, the contractor was entitled to be given the opportunity to show cause why the power should not be exercised and that the principal was only entitled to exercise the power if he or she was not satisfied with the cause shown.

Handley and Priestley JJA each held that the principal was subject to an obligation to act reasonably in considering whether or not the contractor had shown cause to his or her satisfaction and, where the contractor failed to satisfy the principal, in considering whether or not the powers should be exercised.[34] Handley JA considered that the obligation arose as a matter of construction of the clause in context.[35] Priestley JA suggested that the obligation of reasonableness might be supported as implied in fact,[36] as necessary to give business efficacy to the particular contract in question, or in law, as generally implied in all contracts of this kind.[37] Priestley JA also drew an analogy with the duty of good faith recognised in civil law countries and the United States[38] and with the ideas that have led to the equitable interference in the exercise of legal rights.[39] A narrower approach was taken by Meagher JA, who held that the powers conferred by the clause could be exercised in the principal's own interests provided the principal understood what he or she was doing.[40] This formulation did not, however, result in a different decision on the facts of the case. This is because Meagher JA held that the principal's decision was based on a fundamental misunderstanding of relevant matters.[41]

31 *Meehan v Jones* (1982) 149 CLR 571, 591. See also *Zieme v Gregory* [1963] VR 214, 223; *Freedom v AHR Constructions Pty Ltd* (1987) 1 Qd R 59, 61.

32 *Meehan v Jones* (1982) 149 CLR 571, 597–8. See also *Bellmere Park Pty Ltd v Benson* [2007] QCA 102, [23]–[26].

33 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234.

34 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 257, 263, 279.

35 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 279.

36 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 256–60.

37 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 260–3.

38 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 263–8. On the duty of good faith, see Chapter 14.

39 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 268–70.

40 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 275–6.

41 *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 276.

THE CONSEQUENCES OF NON-FULFILMENT OF A CONTINGENT CONDITION

Non-fulfilment excuses performance

[20.37] Non-fulfilment of a contingent condition excuses performance, even where non-fulfilment of the condition may seem objectively unimportant. As Mason J noted in *Perri v Coolangatta Investments Pty Ltd*, "the expression of a provision in the form of a condition precedent endows it with the character of essentiality".[42] In determining whether or not a condition has been fulfilled, the courts adopt a strict approach; exact compliance is required.[43]

If a contingent condition has not been fulfilled by the due date, but neither party then terminates the contract, the contract remains on foot. If the condition has been inserted for the benefit of one party (eg, a subject to finance clause inserted for the benefit of the purchaser of land), that party could waive fulfilment of the condition and enforce the contract against the other party (see [20.55]). The contract cannot, however, be enforced against the party for whose benefit the condition was included because the contract remains subject to a contingent condition which has not been fulfilled.[44] The only options for the other party are to terminate the contract (see [20.50]) or wait to see if the condition is fulfilled.

Void or voidable

[20.40] The consequences of a contingent condition not being fulfilled are determined as a matter of construction of the contract in question.[45] However, some general principles may be discerned. If a contingent condition which relates only to a particular obligation is not fulfilled, then generally the parties will be excused from performance of that obligation, although the contract will remain on foot. If a contingent condition relating to performance of the whole of a contract is not fulfilled, the contract will generally be voidable.[46] This means one or both of the parties may individually have a right to elect to terminate the contract.[47] If neither party elects to do so, the contract will continue on foot. If the contract is terminated, neither of the parties will be liable in damages merely for the fact that the condition has not been fulfilled, unless there has been a breach of the implied duty to co-operate.

In some cases, the contract may provide that, upon non-fulfilment of a contingent condition, the contract will be "deemed to" or will "automatically" come to an end. In *Suttor v Gundowda Pty Ltd*,[48] the parties had agreed that the contract in question "should be deemed to be cancelled"[49] in the event that the Treasurer did not consent to the contract by a specified date. The court held that where the event upon which the condition depends may be brought about by the default of one of the parties (eg, by failing to take reasonable steps to co-operate in fulfilling the condition), the contract is voidable at the option of the party not in

42 *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 554.

43 *Highmist Pty Ltd v Tricare Ltd* [2005] QCA 357, [41].

44 *Margush v Maddeford* [2014] SASCFC 129; (2014) 121 SASR 199.

45 See generally, MacDonald and McGill, *Legal Drafting: A How to Guide* (2015), pp 88–101.

46 See *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 553–4.

47 On election, see Chapter 25.

48 *Suttor v Gundowda Pty Ltd* (1950) 81 CLR 418.

49 *Suttor v Gundowda Pty Ltd* (1950) 81 CLR 418, 439–40.

default.[50] Thus, despite the fact that the words used by the parties appear to have provided for automatic termination, the High Court held that the condition had the effect of making the contract voidable, not void. If neither party is in default, the contract is voidable at the option of either party.[51] However, where the condition concerns an event over which neither party has control, for example, where the performance of a contract is subject to "it not raining",[52] courts have been more willing to accept that parties intended automatic termination in the event that the condition is not fulfilled.

In *MK & JA Roche Pty Ltd v Metro Edgley Pty Ltd*,[53] the New South Wales Court of Appeal considered the effect of a contractual clause that provided that the contract would "be deemed to be automatically rescinded and of no force or effect" if the conditions precedent were not satisfied. The court noted that *Suttor v Gundowda Pty Ltd*[54] could be viewed as establishing a principle of law that applied irrespective of the intentions expressed by the parties or as a principle to guide construction of a contract which can give way to sufficiently clear expressions of intention to the contrary.[55] The Court of Appeal was firmly of the opinion that the latter was the preferable view and was more consistent with well-established principles concerning the construction of contracts.[56] Any concern that a party could take advantage of its own default (which seems to have motivated the approach adopted in *Suttor v Gundowda Pty Ltd*)[57] could be dealt with by direct application of the principle that a party cannot take advantage of its own wrong, rather than by overriding the parties' clearly expressed intentions that the contract was to automatically terminate where the contingent condition was not fulfilled.

By a process of very similar reasoning, Brereton J of the New South Wales Court of Appeal in *Waterman v Gerling Australia Insurance Co Pty Ltd*[58] held that where a provision provided that the contract "shall be deemed to have ceased" upon the non-fulfilment of a condition, the contract was automatically brought to an end when that condition was not met.[59] However, where one of the parties acts to his or her detriment on the assumption that the contract is continuing, the other party may be estopped from asserting that the contract has automatically come to an end if he or she induced the assumption in the other party. The approach adopted in *MK & JA Roche Pty Ltd v Metro Edgley Pty Ltd* and *Waterman*

50 *Suttor v Gundowda Pty Ltd* (1950) 81 CLR 418, 441; see also *Gange v Sullivan* (1966) 116 CLR 418, 441; *Havenbar Pty Ltd v Butterfield* (1974) 133 CLR 449, 455-6; *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 545, 566.

51 *Suttor v Gundowda Pty Ltd* (1950) 81 CLR 418, 443.

52 *New Zealand Shipping Co Ltd v Société des Ateliers et Chantiers de France* [1919] AC 1, 9.

53 *MK & JA Roche Pty Ltd v Metro Edgley Pty Ltd* [2005] NSWCA 39.

54 *Suttor v Gundowda Pty Ltd* (1950) 81 CLR 418.

55 In *New Zealand Shipping Co Ltd v Société des Ateliers et Chantiers de France* [1919] AC 1, the House of Lords appears to have adopted a principle of law that overrode the express intentions of the parties to prevent one party taking advantage of its own default.

56 *MK & JA Roche Pty Ltd v Metro Edgley Pty Ltd* [2005] NSWCA 39, [44].

57 See *Waterman v Gerling Australia Insurance Co Pty Ltd* [2005] NSWSC 1066; (2005) 65 NSWLR 300, [36] (discussing the approach adopted in *New Zealand Shipping Co Ltd v Société des Ateliers et Chantiers de France* [1919] AC 1).

58 *Waterman v Gerling Australia Insurance Co Pty Ltd* [2005] NSWSC 1066; (2005) 65 NSWLR 300.

59 *Waterman v Gerling Australia Insurance Co Pty Ltd* [2005] NSWSC 1066; (2005) 65 NSWLR 300, [53].

v Gerling Australian Insurance Co Pty Ltd has not been accepted in all jurisdictions.[60] In particular, the approach was not initially well received by the Queensland courts because the courts interpreted *Suttor v Gundowda* as demonstrating a plain disposition to treat such clauses as rendering the contract voidable, not void.[61] More recently in *Principal Properties Pty Ltd v Brisbane Broncos Leagues Club Ltd*, Jackson J of the Supreme Court of Queensland described the approach adopted in *MK & JA Roche Pty Ltd v Metro Edgley Pty Ltd* as "the principle to be adopted in this context".[62] His Honour also pointed out that the two approaches will generate the same outcome – a party whose default has contributed to the non-fulfilment of the contingent condition will be prevented from terminating the contract. Under the *Suttor* approach, the defaulting party's wrong results in the court reading down the clause so that it does not provide for automatic termination. Under the *Metro Edgley* approach, the defaulting party's conduct triggers the direct application of the principle that a party cannot rely on his or her own wrong.[63]

Notice

[20.45] Where a contingent condition fails to be fulfilled, notice is not required before the contract can be terminated.[64]

Who can elect to terminate?

[20.50] Whether one or both of the parties can terminate a contract for non-fulfilment of a contingent condition will depend on the construction of the contract.[65] It seems that typically both parties will be entitled to terminate.[66] However, if the condition was not fulfilled because of the default of one of the parties in failing to co-operate, that party will not be entitled to rely on the failure of the condition as a reason for terminating the contract.[67]

WAIVER OF A CONTINGENT CONDITION

[20.55] Both parties acting together may agree to waive a contingent condition, in which case they will be bound by that agreement and may not terminate the contract for non-fulfilment of the condition. In some cases, fulfilment of a contingent condition may also be waived by one party acting alone. Where a party waives compliance with a contingent condition, that action

60 In *Rasch Nominees Pty Ltd v Bartholomaeus* [2012] SASC 70; (2012) 114 SASR 448, [141] and *Rehins Pty Ltd v Debin Nominees Pty Ltd (No 2)* [2011] WASC 168, [141], Kourakis and Murray JJ respectively referred to the Suttor principle without mentioning *Metro Edgley*.

61 See, eg, *Donaldson v Bexton* [2006] QCA 559; [2007] 1 Qd R 525; *Quinn Villages Pty Ltd v Mulherin* [2006] QCA 433, [50].

62 *MK & JA Roche Pty Ltd v Metro Edgley Pty Ltd* [2013] QSC 148; [2014] 2 Qd R 132, [79].

63 *MK & JA Roche Pty Ltd v Metro Edgley Pty Ltd* [2013] QSC 148; [2014] 2 Qd R 132, [80].

64 *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 546, 569–70. On notice relating to termination for breach where time is not of the essence, see Chapter 23.

65 See *Gange v Sullivan* (1966) 116 CLR 418, 441; *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 553.

66 *Suttor v Gundowda Pty Ltd* (1950) 81 CLR 418, 441; *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 546, cf 565.

67 *Suttor v Gundowda Pty Ltd* (1950) 81 CLR 418, 441; *Gange v Sullivan* (1966) 116 CLR 418, 441–2; *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 545, 566; *Etna v Arif* [1999] VSCA 99; [1999] 2 VR 353.

prevents either of the parties from terminating the contract or refusing to perform the contract on grounds of non-fulfilment of the condition.

One party alone will have a right to waive compliance with a contingent condition where the condition is for the benefit of that party.[68] When a condition will be "for the benefit" of a party is not entirely clear.[69] The test has been described as requiring the condition simply to be for the "benefit"[70] of a party. Other cases stated that the condition must be "primarily",[71] "wholly"[72] and "solely"[73] for the benefit of the party seeking to waive the condition. Regardless of which adjective is preferred, whether or not a contingent condition is for the benefit of one party is a matter of construction. The following examples give an indication of the courts' approach.

In *Perri v Coolangatta Investments Pty Ltd*,[74] the High Court considered that a condition making a contract for the sale of land subject to the sale of the purchaser's property was for the benefit of the purchaser alone and so was capable of being waived by the purchaser.[75] In such a case, it might be suggested that the condition was for the benefit of the purchaser because it protected the purchaser from being committed to two properties. The vendor had no interest in whether or not the purchaser sold its property, provided the purchaser was able to pay the vendor for the new property. Somewhat similarly, in *Gange v Sullivan*,[76] the contract was subject to the purchaser obtaining development approval. There was no suggestion that the vendor was retaining any interest in the land or that the vendor would be affected by the purchaser's use of the land in question. The Court concluded that the contingent condition was included in the contract for the benefit of the purchaser and accordingly could be waived by the purchaser.[77]

Gange v Sullivan may be contrasted with *Gough Bay Holdings Pty Ltd v Tyrwhitt-Drake*,[78] in which a contract was made conditional upon the local authority approving the purchaser's plan of subdivision. The vendors were retaining land adjacent to the land to be sold, as well as other land in the area. There was evidence that the land retained by the vendors would be enhanced by the purchaser successfully subdividing the land the subject of the sale. The court concluded that the condition benefited the vendors as well as the purchaser and, accordingly, that the condition was not capable of being unilaterally waived by the purchaser.[79]

Even though a contingent condition is for the benefit of one party, thus entitling that party to waive fulfilment of the condition, the other party may still be entitled to rely on non-fulfilment of the condition as a reason for terminating the contract in the absence of waiver.

68 See *Gange v Sullivan* (1966) 116 CLR 418, 430, 443; *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 543, 552, 560, 565.

69 See generally, MacDonald and McGill, *Legal Drafting: A How to Guide* (2015).

70 *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 543, 565.

71 *Gange v Sullivan* (1966) 116 CLR 418, 430, 444.

72 *Maynard v Goode* (1926) 37 CLR 529, 537; *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 560.

73 *Maynard v Goode* (1926) 37 CLR 529, 536; *George v Roach* (1942) 67 CLR 253, 260, 263; *Sandra Investments Pty Ltd v Booth* (1983) 153 CLR 153, 159.

74 *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537; see also *Tait v Bonnice* [1975] VR 102.

75 *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537, 543, cf 553.

76 *Gange v Sullivan* (1966) 116 CLR 418.

77 *Gange v Sullivan* (1966) 116 CLR 418, 429.

78 *Gough Bay Holdings Pty Ltd v Tyrwhitt-Drake* [1976] VR 195.

79 *Gough Bay Holdings Pty Ltd v Tyrwhitt-Drake* [1976] VR 195, 204.

For example, in *Perri v Coolangatta Investments Pty Ltd*,[80] the High Court considered that a condition making a contract for the sale of land subject to the sale of the purchaser's property was capable of being waived by the purchaser. However, provided the condition had not been waived by the purchaser, the vendor was entitled to terminate the contract for non-fulfilment of the condition. Conversely, an attempt by the purchaser to waive the condition would only have been effective if the vendor had not first terminated for non-fulfilment of the condition.[81]

RESTRICTIONS ON THE RIGHT TO TERMINATE FOR NON-FULFILMENT OF A CONTINGENT CONDITION

Prevention

[20.57] A party may lose its right to terminate for non-fulfilment of a contingent condition if the party has prevented its performance or has intimated that he or she does not intend to perform the contract.[82] This result has been explained sometimes in terms of waiver[83] and sometimes in terms of estoppel.[84] *Grieve v Enge*[85] involved a contract for the sale of land that was subject to the purchaser obtaining finance by a specified date. The vendor refused to allow the purchaser's financier access to the property. The vendor also sent a letter that purported to retract the sale before entering into a contract of sale with a new purchaser. However, the purchaser's response to these acts of renunciation[86] was to affirm the contract, thus keeping the contract on foot. The vendor attempted to rely on the purchaser's failure to obtain finance by the specified date to terminate the contract. As the vendor's refusal to provide access caused the non-fulfilment of the condition, he was prevented from terminating the contract on the basis of the non-fulfilment of the contingent condition.

Other restrictions

[20.60] The right to terminate a contract for non-fulfilment of a contingent condition is subject to a number of other restrictions. Generally, the restrictions that apply to the right to terminate for breach, which are discussed in Chapter 25, apply to the right to terminate for non-fulfilment of a condition. Of particular importance is the principle that a party who waives the right to rely on non-fulfilment of a contingent condition will be bound by this decision once it has been communicated to the other party.

The right to terminate for non-fulfilment of a contingent condition may also be restricted by the doctrines of estoppel and good faith, which are also discussed in Chapter 25.[87] Where one party falsely leads the other party to believe that he or she will not exercise his or her

80 *Perri v Coolangatta Investments Pty Ltd* (1982) 149 CLR 537.

81 See, eg, *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 353 (Mason J); *Sirius International Insurance Co (Publ) v RAI General Insurance Ltd* [2004] 1 WLR 3251, [18] (Lord Steyn).

82 *Nyhuis v Anton* [1980] Qd R 34, 41; *Park v Brothers* [2005] HCA 73, [42]–[43].

83 *Foran v Wight* (1989) 168 CLR 385, 396 (per Mason CJ).

84 *Foran v Wight* (1989) 168 CLR 385, 422, 434 (per Brennan J and Deane J respectively).

85 *Grieve v Enge* [2006] QCA 213.

86 See Chapter 22.

87 As to when relief against forfeiture may be granted, see [25.125].

right to terminate the contract on the basis of non-fulfilment of a contingent condition, this may constitute misleading or deceptive conduct in trade or commerce in breach of s 18 of the *Australian Consumer Law*.[88] The court may be prepared to make an order under s 237 of the *Australian Consumer Law* that prevents the party from terminating the contract on the basis of non-fulfilment of a contingent condition.[89]

88 See Chapter 33 and *Anaconda Nickel Ltd v Edensor Nominees Pty Ltd* [2004] VSCA 167, discussed at [9.195].

89 *Edensor Nominees Pty Ltd v Anaconda Nickel Ltd* [2001] VSC 502, [176]–[180], [198] (upheld in *Anaconda Nickel Ltd v Edensor Nominees Pty Ltd* [2004] VSCA 167).

CHAPTER **21**

Termination for breach

RIGHTS CONFERRED BY THE COMMON LAW

[21.05] In Chapter 19, we discussed the possibility of a term in a contract expressly granting one of the parties the right to terminate for breach of the contract. This chapter discusses the circumstances in which the law will confer on one party (the *aggrieved party*) a right to terminate the contract for breach by the other party (the *party in breach*). The law will also confer a right to terminate where a party *repudiates* his or her obligations under the contract, that is, where a party shows an absence of willingness or ability to perform. Repudiation (which is also sometimes referred to as renunciation)[1] is discussed in Chapter 22.

The common law rules on termination are most significant where the contract does not expressly grant a party the right to terminate the contract in response to breaches of a contract and where the aggrieved party is claiming loss of bargain damages.[2] If a party has an express right to terminate a contract, then often it will be unnecessary to consider whether he or she also has a common law right to terminate. The express right will be sufficient to enable termination. However, often terms conferring an express right to terminate specify a procedure to be followed before the contract can be terminated. Where the aggrieved party has failed to comply with the specified procedure, his or her purported termination may be valid if the breach in question also gives rise to a right to terminate at common law.[3] The courts have rejected the argument that reliance on a contractual right to terminate constitutes an election to affirm the contract and in turn the loss of any common law right to terminate.[4]

The rights to terminate a contract conferred by the common law may be considered *default rules* of contract law.[5] This is because the rights apply in the absence of an expression of

1 See [22.05].
2 On loss of bargain damages, see [27.130].
3 *W & R Pty Ltd v Birdseye* [2008] SASC 321; (2008) 102 SASR 477.
4 *Waters Lane Pty Ltd v Sweeney* [2007] NSWCA 200. See also *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17, 31, 55.
5 See the discussion of default rules at [1.25] and [PtVI.10].

contrary intention by the parties.[6] Thus, the rights to terminate conferred by the common law may be excluded where the express terms of the contract provide a comprehensive code governing termination.[7] However, the mere presence of an express power to terminate will not generally be regarded as excluding the rights conferred by the common law. In many cases express contractual terms dealing with termination may be "regarded as designed to augment rather than to restrict or remove the rights at common law which a party otherwise would have had on breach".[8] As the court noted in *Concut Pty Ltd v Worrell*,[9] clear words are needed to rebut the presumption raised by the express right. The Full Court of the Supreme Court of South Australia considered the effect of an express right to terminate on the aggrieved party's common law rights to terminate in *W & R Pty Ltd v Birdseye*.[10] Clause 7.1.2 provided that "[i]f the purchaser fails to pay the Deposit in accordance with this agreement … the Vendor may, without Prejudice to any other legal rights or remedies the vendor may have, give the Purchaser notice in writing requiring such default to be remedied within a period of three business days … If the default is not remedied within the period specified, this Agreement will automatically terminate". When Birdseye failed to pay a deposit as required by the contract of sale, W & R sought to terminate the contract. However, W & R's notice of termination did not comply with cl 7.1. Nevertheless, the court found that the aggrieved party retained its common law right to terminate for breach of the obligation to pay the deposit. In reaching this conclusion, Doyle CJ (with whom Duggan J agreed) was influenced by the fact that the right to terminate under cl 7.1 was expressed to be without prejudice to any other legal rights or remedies.[11] Anderson J found that there was "no inconsistency in maintaining, on the one hand, the provision of an entitlement to give three days warning to be followed by automatic termination and, on the other hand, the overriding right of immediate unilateral termination".[12]

WHEN IS THERE A RIGHT TO TERMINATE FOR BREACH?

[21.10] Although damages are available for all breaches of contract, the common law only confers a right to terminate in respect of some breaches.[13] Whether there is a common law right to terminate for breach of contract depends primarily on a tripartite classification of terms into conditions, intermediate or innominate terms and warranties:

1. If a term is a *condition*, there will be a common law right to terminate in respect of any breach of that term.
2. If a term is an *intermediate* term, the right to terminate depends on the gravity of the breach and its consequences.

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6 *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17, 31, 55–6.

7 See *Amann Aviation Pty Ltd v Commonwealth* (1990) 22 FCR 527, 532, 542, affirmed on other grounds sub nom *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64; *Dover Fisheries Pty Ltd v Bottrill Research Pty Ltd* (1994) 63 SASR 557, 573.

8 *Concut Pty Ltd v Worrell* [2000] HCA 64, [23]; see also *Stocznia Gdanska SA v Latvian Shipping Co* [1998] 1 WLR 574, 585.

9 *Concut Pty Ltd v Worrell* [2000] HCA 64, [23].

10 *W & R Pty Ltd v Birdseye* [2008] SASC 321; (2008) 102 SASR 477.

11 *W & R Pty Ltd v Birdseye* [2008] SASC 321; (2008) 102 SASR 477, [35].

12 *W & R Pty Ltd v Birdseye* [2008] SASC 321; (2008) 102 SASR 477, [194].

13 But see discussion of anticipatory breach at [22.10].

3. If a term is a *warranty*, a breach of the term will not of itself give rise to a right to terminate the contract.[14]

Background to the tripartite classification of terms

[21.15] The tripartite classification of terms is a relatively recent development. Influenced by the *Sale of Goods Act 1893*, English courts tended to rely on a rigid dichotomy between conditions and warranties in determining whether or not a breach of contract gave rise to a right to terminate.[15] This approach resulted in an "all or nothing" analysis which focused on the nature of the term, rather than the nature of the breach. Where there has been a breach of a condition, the right to terminate follows from the status of the term. Conversely, where the term is classified as a warranty, there will be no right to terminate for breach, only a right to damages. A change in approach was brought about through the English case *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd*,[16] in which the Court of Appeal recognised that there may be a third category of term in respect of which the right to terminate depends on the gravity of the breach and its consequences.[17] This third category of term has subsequently been described as *innominate*[18] or *intermediate*.[19] The category "is 'intermediate' because it lies in the middle, between a condition and a warranty … and it is 'innominate' because it is not called a condition or a warranty but assumes the character of each in turn".[20]

It may be argued that Australian courts have for some time recognised a tripartite classification of terms in analysing whether or not a breach gives rise to a common law right to terminate. Australian courts have accepted that there is a category of term, known as a condition or essential term, for which strict performance is required, and that an aggrieved party is entitled to terminate for any breach of a condition, however slight.[21] Australian courts have also recognised that if a term is a warranty, there is no right to terminate for breach.[22] Although the doctrine of intermediate terms was only expressly accepted by the High Court as being part of Australian law in 2007,[23] Australian courts had been prepared in earlier decisions to consider the gravity of a breach in deciding whether or not there is a

14 See also possibility of repudiation at [22.20].

15 See Greig and Davis, *The Law of Contract* (1987), pp 1199–213; Greig, "Condition – Or Warranty?" (1973) 89 *Law Quarterly Review* 93.

16 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26. See also Nolan, "Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd, The Hongkong Fir (1961)" in Mitchell and Mitchell (eds), *Landmark Cases in the Law of Contract* (2008), p 269.

17 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 63–4, 70.

18 See, eg, *L Schuler AG v Wickman Machine Tool Sales Ltd* [1974] AC 235, 264; *Bunge Corporation New York v Tradax Export SA Panama* [1981] 1 WLR 711, 717, 719, 724.

19 See, eg, *Cehave NV v Bremer Handelgesellschaft mbH* [1976] QB 44, 60; *Bunge Corporation v Tradax Export SA* [1981] 1 WLR 711, 714, 717, 719; *Ankar Pty Ltd v National Westminster Finance (Australia) Ltd* (1987) 162 CLR 549, 562.

20 *Bunge Corporation v Tradax Export SA* [1981] 1 WLR 711, 719.

21 See, eg, *Bowes v Chaleyer* (1923) 32 CLR 159; *Tramways Advertising Pty Ltd v Luna Park Ltd* (1938) 38 SR (NSW) 632, 641–2; *Luna Park (NSW) Ltd v Tramways Advertising Pty Ltd* (1938) 61 CLR 286, 304; *Associated Newspapers Ltd v Bancks* (1951) 83 CLR 322, 336; *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 430–1; *Ankar Pty Ltd v National Westminster Finance (Australia) Ltd* (1987) 162 CLR 549, 562.

22 *Tramways Advertising Pty Ltd v Luna Park (NSW) Ltd* (1938) 38 SR (NSW) 632, 641–2; *Associated Newspapers Ltd v Bancks* (1951) 83 CLR 322, 337.

23 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115. However, the High Court had commented favourably about the doctrine of intermediate terms in *Ankar Pty Ltd v*

right to terminate.[24] For example, in *Tramways Advertising Pty Ltd v Luna Park (NSW) Ltd*,[25] Jordan CJ referred to an essential promise for which any "substantial breach" would give rise to a right to terminate.[26] In *Associated Newspapers Ltd v Bancks*,[27] the High Court said that the term in question formed a condition "a substantial failure in the performance of which would entitle the defendant to treat the contract as at an end".[28]

In referring to terms for which only a substantial failure to perform justifies termination, the courts in these cases seem to have recognised that there is a category of term for which the right to terminate will depend on the gravity of the breach and its consequences. The cases quoted describe this type of term as an "essential term"[29] or a "condition".[30] This suggests two types of conditions: one for which strict performance is required and one for which the right to terminate will depend on whether or not the breach is serious or fundamental. However, generally, the term "condition" is used to describe the former. Furthermore, following the High Court's decision in *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd*[31] (discussed at [21.72]), the latter category of "conditions" will now be analysed as intermediate terms.[32] The term "condition" is now likely to be exclusively used to describe a contractual term which, if not strictly performed, automatically gives the non-breaching party the right to terminate the contract irrespective of the objective consequences of breach.[33]

In the ninth edition of *Cheshire and Fifoot's Law of Contract*, current at the time of the *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd*, the authors of the Australian edition of *Cheshire and Fifoot's Law of Contract* argued that:

> It is difficult to see the necessity for introducing such a third category of terms as a means of legitimising termination by reference to the extent of the loss actually caused by a breach. Unless otherwise agreed, a breach that substantially deprives the other party of the benefit of a contract should entitle that party to terminate it, no matter whether the term in question is essential, intermediate, or inessential.[34]

This view found favour with Kirby J in *Koompahtoo Local Aboriginal Council v Sanpine Pty Ltd*. His Honour described the innominate or intermediate term label as "meaningless"[35] and

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National Westminster Finance (Australia) Ltd, noting that the category of intermediate terms "brings a greater flexibility to the law of contract": *Ankar Pty Ltd v National Westminster Finance (Australia) Ltd* (1987) 162 CLR 549, 562.

24 See also Greig and Davis, *The Law of Contract* (1987), pp 1212–13.

25 *Tramways Advertising Pty Ltd v Luna Park (NSW) Ltd* (1938) 38 SR (NSW) 632, 642.

26 *Tramways Advertising Pty Ltd v Luna Park (NSW) Ltd* (1938) 38 SR (NSW) 632, 642.

27 *Associated Newspapers Ltd v Bancks* (1951) 83 CLR 322.

28 *Associated Newspapers Ltd v Bancks* (1951) 83 CLR 322, 339.

29 *Tramways Advertising Pty Ltd v Luna Park (NSW) Ltd* (1938) 38 SR (NSW) 632, 642.

30 *Associated Newspapers Ltd v Bancks* (1951) 83 CLR 322, 339.

31 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115.

32 See also *Direct Acceptance Finance Ltd v Cumberland Furnishing Pty Ltd* [1965] NSWR 1504, 1511; *Tricontinental Corporation Ltd v HDFI Ltd* (1990) 21 NSWLR 689, 697; *Amann Aviation Pty Ltd v The Commonwealth* (1990) 22 FCR 527, 532, 542, affirmed on other grounds sub nom *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64; *Dover Fisheries Pty Ltd v Bottrill Research Pty Ltd* (1994) 63 SASR 557, 572.

33 See, eg, *VIP Home Services (NSW) Pty Ltd v Swan* [2011] SASC 110; (2011) 110 SASR 157.

34 Seddon and Ellinghaus, *Cheshire and Fifoot's Law of Contract* (9th Australian ed, 2008), [21.22].

35 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115, [107].

stated that there were in fact only two types of terms: essential (conditions) and non-essential terms. In Kirby J's view, a right to terminate arises in respect of breach of an essential term or breach of a non-essential term causing substantial loss of benefit.[36] Against this view, it might be argued that the category of intermediate term is useful for the purpose of distinguishing terms for which the seriousness of the breach is significant in assessing the right to terminate for breach from conditions and warranties in which it is not.

A majority of the High Court in *Koompahtoo Local Aboriginal Council v Sanpine Pty Ltd* clearly adopted the tripartite classification described above and took pains to make it clear that they regarded that as part of the ratio of their decision. The tripartite classification, therefore, clearly represents the law in Australia. However, some lower court judges appear to be following an approach similar to that advocated in *Cheshire and Fifoot's Law of Contract* and favoured by Kirby J. For example, in *Idameneo (No 123) Pty Ltd v Robalino*,[37] McDougall J was content to rest his decision that Idameneo could terminate the contract on a finding that Robalino's breaches were sufficiently serious. His Honour stated that it was not necessary to consider whether the contractual clauses breached were essential.[38] Rather, McDougall J was content to assume, without deciding, that the terms in question were not essential but intermediate terms.

In *VIP Homes Services (NSW) Pty Ltd v Swan*,[39] Doyle CJ appeared to recognise four types of term. The first is a condition, which is a term "*any* breach of which gives rise to a right … to terminate".[40] The second is an "essential term" which is a term that was of such importance that the promisee would not have entered into the contract if not assured of *strict* or *substantial* performance. Termination for breach of such a term is only permitted if there has been a substantial failure to comply with the promise. The third is an intermediate term, only a serious breach of which will permit termination. Although his Honour did not discuss warranties, the judgment appears to assume the continuation of the final residual category of warranty.

Continued relevance of the category of warranty

[21.20] Warranty is the residual category of terms for which there is no right to terminate for breach.[41] Generally, the classification of a term as a condition, warranty or intermediate term is a matter of construction depending on the presumed intentions of the parties as derived from the terms of the contract and the circumstances of the case. Nonetheless, it may be that the category of warranty will rarely be applied, except where prescribed by legislation. The classification of a term as intermediate is likely to be preferred for the reason that it gives courts greater flexibility in dealing with a breach. For example, in *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd*,[42] Lord Diplock suggested that, in the absence of a clearly expressed intention to the contrary, a term will only properly be classified as a warranty if it

36 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115, [114].

37 *Idameneo (No 123) Pty Ltd v Robalino* [2009] NSWSC 969.

38 *Idameneo (No 123) Pty Ltd v Robalino* [2009] NSWSC 969, [105]. See also *Foggo v O'Sullivan Partners (Advisory) Pty Ltd* [2011] NSWSC 501, [112].

39 *VIP Home Services (NSW) Pty Ltd v Swan* [2011] SASC 110; (2011) 110 SASR 157.

40 *VIP Home Services (NSW) Pty Ltd v Swan* [2011] SASC 110; (2011) 110 SASR 157, [45].

41 But see also discussion of repudiation at [22.20].

42 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26.

is such that no possible breach could give rise to an event which would deprive the aggrieved party of substantially the whole of the benefit which it was intended he or she should receive from the contract.[43]

TERMINATION FOR BREACH OF A CONDITION

[21.25] Where a term is classified as a condition, any breach of the term will give the aggrieved party a right to terminate the contract. The right to terminate arises regardless of the gravity of the breach. The effect of a term being classified as a condition is illustrated by the decision in *Arcos v Ronaasen*.[44] This case involved a contract for the sale of timber which the buyers intended to use for the manufacture of barrels. When delivered, the timber did not match its description. Between the time of making the contract and the time of delivery, the price of timber fell. This meant that the buyers would benefit from terminating the contract because they could buy timber more cheaply elsewhere. The timber delivered by the sellers was only fractionally different from its contract specifications and was still suitable for its intended purpose. Correspondence with description was deemed to be a condition under the Sale of Goods Acts. Accordingly, the House of Lords affirmed the right of the buyers to terminate the contract. The relatively minor nature of the seller's breach and the possibly opportunistic reason for the buyer's decision to terminate were not relevant to determining whether the buyer had the right to terminate.[45]

Classifying a term as a condition or essential term

[21.30] Even though there is a distinction between the term "condition" and "essential term",[46] the two terms are often used interchangeably. An *essential* term is often described as a term which goes to the *root* of the contract. A term may be classified as a condition by statute,[47] by the parties or by the courts on the basis of the construction of the contract.

Designation by the parties

[21.35] A term may be classified as a condition on the basis of the express words used by the parties.[48] However, before courts will conclude a particular term is a condition, with the consequence that any breach will entitle the aggrieved party to terminate, the parties must clearly have expressed their intention for the term to have this status. The use of the word "condition" is not conclusive.[49] This is because parties may not always have intended to use the word in its technical legal sense. For example, the printed words on a simple standard form contract – "conditions of sale" or "see back for conditions" – might simply refer to the terms of the contract. Similar arguments might be applied to the use of the word "warranty".

43 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 69–70.

44 *Arcos v Ronaasen* [1933] AC 470.

45 See also discussion of this case at [25.175].

46 See [21.15].

47 See, eg, the classification of terms implied by the Sale of Goods Acts.

48 See, eg, *Shevill v Builders Licensing Board* (1982) 149 CLR 620, 627.

49 See, eg, *L Schuler AG v Wickman Machine Tool Sales Ltd* [1974] AC 235, 250, 256; *Australia and New Zealand Banking Group Ltd v Beneficial Finance Corporation Ltd* [1983] 1 NSWLR 199, 204; *Amann Aviation Pty Ltd v Commonwealth* (1990) 22 FCR 527, 532, affirmed on other grounds sub nom *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64.

However, where it is clear that the parties are using these words in their legal sense, the court must give effect to the intentions of the parties and classify the terms accordingly.[50]

The fact that a contract has expressly conferred a right to terminate for breach of a particular term will not necessarily make that term a condition so as to confer a right to terminate for breach under the common law.[51] While an express right to terminate for breach of a particular term may support a conclusion that the term in question is "essential", the other circumstances of the case will remain relevant. One way for parties to indicate an intention that a particular term be a condition of the contract is to state that "any breach will give rise to a right to terminate".[52] Of course, as already discussed, if one party has, by the express terms of the contract, been given a right to terminate for breach, the classification of the term as a condition, intermediate term, or warranty will be of less importance.[53] The party will, by reason of the express term, have a clear right to terminate. However, the classification of the term breached may have an effect on the amount of damages available to the aggrieved party.[54]

Where there is no express designation by the parties

[21.40] In the absence of classification by statute or by an express statement by the parties, whether or not a term is a condition is determined as a matter of construction of the contract in question.[55] Some courts have suggested it should not be too readily concluded that a term is a condition, any breach of which gives rise to a right to terminate. This suggestion is based on the view that courts should prefer a construction that encourages the continued performance, rather than the avoidance, of a contract.[56] Where a term is a condition, an aggrieved party may terminate even for a trivial or insubstantial breach that would cause him or her no real loss, as was illustrated in our earlier discussion of *Arcos v Ronaasen*.[57] Nonetheless, in some cases, there will be factors that support the classification of the term as a condition and outweigh the courts' desire to promote continued performance of the contract.

In assessing whether or not a term should be classified as a condition, the High Court has approved the statement of Jordan CJ in *Tramways Advertising Pty Ltd v Luna Park Ltd*:

> The test of essentiality is whether it appears from the general nature of the contract considered as a whole, or from some particular term or terms, that the promise is of such importance to the promisee that he would not have entered into the contract unless he had been assured of a strict or substantial performance of the promise … and this ought to have been apparent to the promisor.[58]

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50 *Gumland Property Holdings Pty Ltd v Duffy Bros Fruit Market (Campelltown) Pty Ltd* [2008] HCA 10; (2008) 234 CLR 237, [53].

51 See *Shevill v Builders Licensing Board* (1982) 149 CLR 620.

52 See also Carter, *Carter's Breach of Contract* (2nd ed, 2018), [5-07].

53 See *Idameneo (No 123) Pty Ltd v Ticco Pty Ltd* [2004] NSWCA 329, [95].

54 See [27.130].

55 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha* [1972] 2 QB 26, 60; *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 430.

56 *Cehave NV v Bremer Handelgesellschaft mbH (The Hansa Nord)* [1976] QB 44, 70–1; *Bunge Corporation v Tradax Export SA* [1981] 1 WLR 711, 715–6; *Ankar Pty Ltd v National Westminster Finance (Australia) Ltd* (1987) 162 CLR 549, 556.

57 *Arcos v Ronaasen* [1933] AC 470, discussed at [21.25].

58 *Tramways Advertising Pty Ltd v Luna Park (NSW) Ltd* (1938) 38 SR (NSW) 632, 641–2, reversed on other grounds in *Luna Park (NSW) Ltd v Tramways Advertising Pty Ltd* (1938) 61 CLR 286, approved by the High

In *DTR Nominees Pty Ltd v Mona Homes Pty Ltd*,[59] Stephen, Mason and Jacobs JJ provided further explanation of the relevant test:

> [T]he quality of essentiality depends … on a judgment which is made of the general nature of the contract and its particular provisions, a judgment which takes close account of the importance which the parties have attached to the provision as evidenced by the contract itself as applied to the surrounding circumstances.

Accordingly, in assessing whether or not a term is a condition, courts will consider whether or not the parties would only have entered into a contract on the understanding that there would be strict compliance with the term. The parties' probable intentions as to the significance of particular terms are determined objectively, having regard to the terms of the contract and the surrounding circumstances.[60] The question of essentiality falls to be considered not at the time of the breach, but at the time when the contract was made. If a term was a condition at the time the contract was entered into, it does not lose that quality because the term is now of less value or significance to the promisee.[61]

Relevant factors in assessing whether a term is a condition

Previous decisions

[21.45] If a term has been classified in a previous judicial decision, that classification is likely to be followed in subsequent cases.[62]

Promoting certainty

[21.50] The need for certainty in the parties' dealings may influence a court to classify a term as a condition. Where a term is a condition, parties have the certainty of knowing their rights, rather than having to wait and assess the gravity of any breach that occurs.[63] Such certainty may be particularly important in mercantile contracts, which are commercial contracts for the sale of goods.[64] Mercantile contracts may be part of a series of contracts in which the performance of each contract is dependent on timely performance of the others.[65] Accordingly, a term is more likely to be classified as a condition in a mercantile contract than in other sorts of contract, particularly non-commercial contracts.

The language in which the obligation is described

[21.55] The way in which the parties describe an obligation may be relevant in assessing the importance to the parties of strict performance of that obligation. An obligation described

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Court in *Associated Newspapers Ltd v Bancks* (1951) 83 CLR 322, 337; *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 430–1; *Shevill v Builders Licensing Board* (1982) 149 CLR 620, 627, 636; *Ankar Pty Ltd v National Westminster Finance (Australia) Ltd* (1987) 162 CLR 549, 556.

59 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 431.

60 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 431.

61 *South Dowling Pty Ltd v Cody Outdoor Advertising Pty Ltd* [2005] NSWSC 391, [59].

62 See also *Maredelanto Compania Naviera SA v Bergbau-Handel GmbH* [1971] 1 QB 164.

63 See also *Bunge Corporation v Tradax Export SA* [1981] 1 WLR 711, 725.

64 See, eg, *Bowes v Chaleyer* (1923) 32 CLR 159, 168, 196; *Bunge Corporation v Tradax Export SA* [1981] 1 WLR 711, 715, 718, 720, 725; *Compagnie Commerciale Sucres et Denrees v C Czarnikow Ltd* [1990] 1 WLR 1337, 1348.

65 See *Bunge Corporation v Tradax Export SA* [1981] 1 WLR 711, 716, 720, 726.

in clear and precise language is more likely to be a condition than one expressed in more general or vague terms. *Luna Park Ltd v Tramways Advertising Pty Ltd*[66] concerned a contract whereby Tramways agreed to exhibit advertisements for Luna Park on boards on Sydney trams. The contract provided that "[w]e [Tramways] guarantee that these boards will be on the tracks at least eight hours per day throughout your [Luna Park's] season". After some time, Luna Park complained that Tramways had not complied with this undertaking; each board had not been displayed for at least eight hours on each and every day. On this basis, Luna Park claimed that it was not bound by the contract any further and ceased making payments for the advertising. Tramways admitted that the boards were not on display for eight hours each day, but argued that its obligations under the contract were satisfied by each board being displayed for an *average* of eight hours per day.

The majority of the High Court considered that, as a matter of construction, the contract required the boards to be on view for at least substantially eight hours each day.[67] The High Court also concluded that the undertaking was a condition. Any breach of the undertaking accordingly entitled Luna Park to terminate the contract.[68] One of the factors influencing the Court's conclusion about the status of the term was the language used to describe the undertaking; "we guarantee" were words of strong obligation which emphasised the importance of the term to the parties.[69]

By contrast, in *Amann Aviation Pty Ltd v Commonwealth of Australia*,[70] a term requiring performance "as soon as possible" expressed a relative concept and, accordingly, was not a condition.[71]

The other terms of the contract

[21.60] Inferences about the probable importance to the parties of strict performance of a particular term may sometimes be drawn from the other terms of the contract.[72] For example, consider a case where the parties have expressly granted the aggrieved party a right to terminate the contract in respect of breaches of some terms but not others. The fact that the parties have considered the matter of termination for breach and decided not to provide an express right to terminate for breach of the term in question may suggest that the term was not sufficiently important to the parties to be classified as a condition.[73]

The likely character of the breach

[21.65] If *every* breach of a term is likely to have serious consequences for an aggrieved party – depriving the aggrieved party of "substantially the whole of the benefit" which it was intended he or she should obtain from the contract – then the term is likely to be classified as

66 *Luna Park (NSW) Ltd v Tramways Advertising Pty Ltd* (1938) 61 CLR 286.

67 *Luna Park (NSW) Ltd v Tramways Advertising Pty Ltd* (1938) 61 CLR 286, 304, Latham CJ, Rich and McTiernan JJ, Dixon J dissenting.

68 *Luna Park (NSW) Ltd v Tramways Advertising Pty Ltd* (1938) 61 CLR 286, 302.

69 *Luna Park (NSW) Ltd v Tramways Advertising Pty Ltd* (1938) 61 CLR 286, 303.

70 *Amann Aviation Pty Ltd v Commonwealth* (1990) 22 FCR 527.

71 *Amann Aviation Pty Ltd v Commonwealth* (1990) 22 FCR 527, 558; see also *Bowes v Chaleyer* (1923) 32 CLR 159.

72 *Gumland Property Holdings Pty Ltd v Duffy Bros Fruit Market (Campbelltown) Pty Ltd* [2008] HCA 10; (2008) 234 CLR 237, [46]–[48].

73 See, eg, *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 430.

a condition. Conversely, a term which may be breached in a variety of ways, from the trivial to the significant, is more likely to be an intermediate term than a condition.[74] Courts presume that the parties are generally interested in performance and are unlikely to have intended one party to be able to terminate the contract merely for a trivial breach.

In *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd*,[75] the Court of Appeal concluded that a term in a charterparty requiring the ship to be seaworthy was not a condition. The conclusion was influenced by the fact that the seaworthiness clause could be breached by the slightest failure of the ship to be "fitted in every way for service".[76] Possible breaches ranged from minor matters – such as a nail missing from one of the timbers of a wooden vessel – to serious defects which might result in the loss of the ship.[77] It was considered "unthinkable that all the relatively trivial matters which have been held to be unseaworthiness could be regarded as conditions of the contract".[78] Similarly, in *Cehave NV v Bremer mbH (The Hansa Nord)*,[79] the court considered that a term in a contract for the sale of goods stating that the goods would be shipped in "good condition" was not a condition because the term could be breached in a variety of ways.[80]

Whether damages would be an adequate remedy

[21.70] If damages would not adequately compensate the aggrieved party for the breach of a particular term or would be difficult to prove, courts may be more inclined to treat the term as a condition.[81] In such cases, the aggrieved party's right to terminate will be of particular importance in protecting that party's interests. However, a similar result could be achieved by classifying the term as an intermediate term and considering whether damages would be an adequate remedy as part of the analysis of the consequences of the breach. As a result of the recognition of the intermediate term concept in *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd*,[82] courts may start employing this approach, rather than drawing indirect inferences about the importance of the term to the non-breaching party from the fact that damages may be an inadequate remedy.

TERMINATION FOR BREACH OF AN INTERMEDIATE TERM

Koompahtoo

[21.72] Although the High Court had previously hinted that it would accept the doctrine of intermediate terms into Australian law,[83] *Koompahtoo Local Aboriginal Land Council v*

74 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 69. See also *L Schuler AG v Wickman Machine Tool Sales Ltd* [1974] AC 235, 251, 259.

75 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26.

76 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 62.

77 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 62, 71.

78 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 56, also 62–3, 71.

79 *Cehave NV v Bremer mbH (The Hansa Nord)* [1976] QB 44.

80 *Cehave NV v Bremer Handelgesellschaft mbH* [1976] QB 44, 61, 70, 73, 78, 84.

81 See, eg, *Ankar Pty Ltd v National Westminster Finance (Australia) Ltd* (1987) 162 CLR 549, 556.

82 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115.

83 *Ankar Pty Ltd v National Westminster Finance (Australia) Ltd* (1987) 162 CLR 549, 562.

Sanpine Pty Ltd[84] was the first case in which the High Court did so expressly. The majority noted that the adoption of other taxonomies for contractual stipulations might achieve similar outcomes, but decided to adopt the doctrine of intermediate terms recognised by the English Court of Appeal in *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd*[85] on the basis that it "has long since passed into the mainstream law of contract as understood and practised in Australia".[86] Koompahtoo and Sanpine were parties to a joint-venture agreement under which Koompahtoo agreed to contribute land and Sanpine agreed to manage the development of that land. The development agreement imposed many reporting obligations on Sanpine, including obligations to maintain books that permitted the affairs of the joint venture to be duly assessed and to deal with project funds in a particular way. Sanpine's breaches of the joint-venture agreement were revealed when Koompahtoo went into administration and Sanpine was unable to inform the administrator of the true financial position of the joint venture and how the money borrowed from financiers had been applied. On the basis of these breaches, the administrator terminated the joint-venture agreement. Sanpine commenced proceedings, seeking a declaration that the administrator's termination of the joint-venture agreement was invalid. The High Court held that Koompahtoo's termination was justified. Although there was much to be said for the argument that the clauses breached were properly classified as conditions,[87] Gleeson CJ, Gummow, Heydon and Crennan JJ ultimately decided that they were intermediate terms. As Sanpine's breaches of those terms went to the root of the contract, Koompahtoo's termination of the contract was valid.[88]

What is an intermediate term?

[21.73] Exactly what constitutes an intermediate term has not received great judicial attention. This is probably because in most cases, the facts demonstrate that breach of the term in question is capable of having more than trivial consequences and must therefore be more than a contractual warranty. It may only be possible to define intermediate terms negatively as follows: an intermediate term is less than an essential term but more than a warranty.[89]

When will breach justify termination?

[21.75] Unlike the condition/warranty approach, which deals only with consequences the parties expected breach to have at the time the contract was formed, the analysis of an intermediate term deals with actual, not hypothetical, consequences of breach, measured at the time of the breach.[90] Where a term is intermediate, the right to terminate depends

84 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115.

85 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26. See [21.75].

86 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115, [50].

87 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115, [69].

88 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115, [71]. Kirby J did not endorse the intermediate term concept. See [21.15].

89 See, eg, Giles JA's judgment in *Sanpine Pty Ltd v Koompahtoo Local Aboriginal Land Council* [2006] NSWCA 291, [176]. See also Carter, Tolhurst and Peden, "Developing the Intermediate Term Concept" (2006) 22 *Journal of Contract Law* 268, 271.

90 See Phang, "On Architecture and Justice in Twentieth Century Contract Law" (2003) 19 *Journal of Contract Law* 229, 241.

on the nature of the breach and its foreseeable consequences.[91] Courts have used different descriptions to refer to the type of breach that will entitle an aggrieved party to terminate. Courts have referred to a breach which is "grave",[92] "serious",[93] "fundamental",[94] which goes to the "root" of the contract[95] or which gives rise to events frustrating the "commercial purpose" of the contract.[96] It has been said that the breach must deprive the innocent party of "a substantial part of the benefit for which it contracted".[97] The majority in *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd*[98] asked whether the breach went to the root of the contract, noting that this rests primarily upon the construction of the contract. The majority noted that this description "takes account of the nature of the contract and the relationship it creates; the nature of the term; the kind and degree of breach; and the consequences of the breach for the other party".[99] The majority also noted that as:

> the corollary of a conclusion that there is no right to terminate is likely to be that the party not in default is left to rely upon a right to damages, the adequacy of damages as a remedy may be a material factor in deciding whether the breach goes to the root of the contract.[100]

Ultimately, the majority concluded that Sanpine's breaches were sufficiently serious to allow Koompahtoo to terminate the contract. The difficulties experienced by the administrator when he sought to inform himself of the financial position of the joint venture was said to support this conclusion.

In *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd*,[101] Diplock LJ stated:

> The test … has been stated in a number of metaphors all of which I think amount to the same thing: does the occurrence of the event deprive the party who has further undertakings still to perform of substantially the whole benefit which it was the intention of the parties as expressed in the contract that he should obtain as the consideration for performing those undertakings?[102]

Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd concerned the breach of a clause in a charterparty requiring the ship to be seaworthy. The breach in question had resulted in the ship being unavailable for some seven months out of a total hire period of 24 months. As the clause breach was an intermediate term, the existence of a right to terminate depended on the nature and consequences of the breach.[103] Their Lordships agreed with the finding of the trial judge that these events were not such as to justify termination.[104] Although there

91 See also *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 70.

92 *Ankar Pty Ltd v National Westminster Finance (Australia) Ltd* (1987) 162 CLR 549, 562.

93 *Ankar Pty Ltd v National Westminster Finance (Australia) Ltd* (1987) 162 CLR 549, 562.

94 *Direct Acceptance Finance Ltd v Cumberland Furnishing Pty Ltd* [1965] NSWR 1504, 1510–1.

95 See, eg, *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 64; *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115, [71].

96 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 64, 72.

97 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115, [71].

98 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115.

99 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115, [54].

100 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115, [54].

101 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26.

102 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 64.

103 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 64, 71–2.

104 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 65, 73.

was some delay caused by the need for repairs, the ship was still made available for about 17 months under the charterparty.[105]

In *Idameneo (No 123) v Robalino*,[106] Dr Robalino agreed to work at medical centres owned and operated by Idameneo. Dr Robalino breached the contract by working less than the minimum number of hours specified in the contract and by carrying on a medical practice from his home. McDougall J held that the effect of these breaches was sufficiently serious to justify Idameneo's termination of the contract. Dr Robalino's failure to adhere to the terms of the contract had a disruptive effect and required others at the medical practice to work longer hours seeing patients and re-organising rosters.

Breach of intermediate term distinguished from repudiation

[21.80] Some have argued that the intermediate term doctrine can be understood as an application of the doctrine of repudiation.[107] Repudiation and serious breach of an intermediate term are, however, conceptually and practically distinct. As Carter has noted, "If repudiation is alleged, the principal focus is on the objective intention of the promisor, whereas the *Hongkong Fir* doctrine focuses on the impact of the breach on the promisee."[108] In *Carr v JA Berriman Pty Ltd*,[109] for example, one of the promisor's breaches was a failure to prepare and hand over possession of a building site by a particular date. The evidence suggested that heavy rain had made it very difficult to excavate and clear the site. The court held that the weather had to be taken into account in deciding whether the promisor had *repudiated* the contract by evincing an unwillingness to perform, but was irrelevant to the question whether the promisor had *breached* the contract.[110] The weather in such a situation would also be irrelevant to a question whether the committed a breach of an intermediate term which justified termination, since that would depend on the effect of the breach on the promisee.

105 *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 40.

106 *Idameneo (No 123) Pty Ltd v Robalino* [2009] NSWSC 969.

107 See, eg, Greig and Davis, *The Law of Contract* (1987), pp 1209–10.

108 Carter, *Carter's Breach of Contract* (2nd ed, 2011), [6-45].

109 *Carr v JA Berriman Pty Ltd* (1953) 89 CLR 327.

110 *Carr v JA Berriman Pty Ltd* (1953) 89 CLR 327, 350.

CHAPTER **22**

Termination for repudiation

REPUDIATION

Overview

[22.05] Where one party manifests an unwillingness or inability to perform his or her obligations under the contract, the other party may have the right to terminate. Traditionally, the party who is unwilling or unable to perform the contract has been said to have repudiated the contract. However, more recently, the High Court appears to have adopted new terminology. For example, in *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd*,[1] the majority used the term renunciation to describe conduct of a party who is no longer willing or able to perform the contract.[2] The majority also suggested that the term repudiation should be used to describe any breach of contract which justifies termination by the other party.[3] However, in the discussion below, the traditional terminology is used.

In *Shevill v Builders Licensing Board*, Gibbs CJ[4] (with whom Murphy and Brennan JJ agreed) provided the following leading statement of principle on repudiation:

> [A] contract may be repudiated if one party renounces his liabilities under it – if he evinces an intention no longer to be bound by the contract or shows that he intends to fulfil the contract only in a manner substantially inconsistent with his obligations and not in any other way.

Whether or not a party has repudiated is determined on an objective basis, "not … by an inquiry into the subjective state of mind of the party in default".[5] As Deane and Dawson JJ said in *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd*:[6]

1 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115.
2 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115, [44].
3 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115, [44].
4 *Shevill v Builders Licensing Board* (1982) 149 CLR 620, 625.
5 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 647 (per Brennan J).
6 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 620.

> An issue of repudiation turns upon objective acts and omissions and not upon uncommunicated intention … It suffices that, viewed objectively, the conduct of the relevant party has been such as to convey to a reasonable person, in the situation of the other party, repudiation or disavowal either of the contract as a whole or of a fundamental obligation under it.

Repudiation of a contract is a serious matter and "is not to be lightly found or inferred".[7] To amount to repudiation, the absence of willingness or ability to perform must relate to the whole of the contract, to a condition of the contract or be "fundamental". Repudiation may be evidenced by a single act or by an accumulation of conduct. A repudiation of a contract by one party (the *repudiating party*) will entitle the other party (the *aggrieved party*) to elect to terminate the contract.[8] Unwillingness or inability to perform amounting to repudiation will be established objectively on the basis of the repudiating party's words or conduct.[9] Repudiation may also be shown by a factual inability to perform.

Rationale

[22.10] Several rationales have been advanced for the doctrine of repudiation. For example, it has been suggested that the doctrine of repudiation is based on the breach of an implied term not to render future performance futile: "[O]ne essential promise which is implied in every contract is that neither party will without just cause repudiate his obligations under the contract, whether the time for performance has arrived or not."[10]

A very practical rationale for repudiation, at least in relation to anticipatory breach, is that an aggrieved party should not be bound to a contract that the other party has indicated he or she will not or cannot perform. In these circumstances, the aggrieved party should be able to rely on the other party's intimation of future non-performance and redirect his or her resources into alternative arrangements.[11]

Repudiation and anticipatory breach

[22.15] An important aspect of the doctrine of repudiation concerns *anticipatory breach*. Anticipatory breach has been described as a "species of the genus repudiation"[12] and occurs when one party repudiates his or her obligations under the contract prior to the time set for performance of those obligations. An aggrieved party may, by *accepting* the repudiation, elect to terminate the contract and claim damages.[13] However, a unique feature of anticipatory breach is that if an aggrieved party chooses not to accept a repudiation occurring before the

7 *Ross T Smyth & Co Ltd v T D Bailey Son & Co* [1940] 3 All ER 60, 71 (per Lord Wright); *Shevill v Builders Licensing Board* (1982) 149 CLR 603, 633.

8 On election, see Chapter 25.

9 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 647.

10 *Tramways Advertising Pty Ltd v Luna Park Ltd* (1938) 38 SR (NSW) 632, 646; see also *Hochster v De La Tour* (1853) 118 ER 922, 926.

11 See also *Woodar Investment Development Ltd v Wimpey Construction UK Ltd* [1980] 1 WLR 277, 296–7; Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), p 130.

12 *Afovos Shipping Co SA v Pagnan* [1983] 1 WLR 195, 203.

13 *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17, 48; *Foran v Wight* (1989) 168 CLR 385, 416, 441–2.

time set for performance, not only will the contract continue on foot, but also there will be no right to damages unless and until an actual breach occurs.[14]

In some cases, an actual breach may indicate a repudiation of a party's remaining contractual obligations. While such an occurrence is sometimes referred to as an anticipatory breach on the basis that the actual breach suggests that further breaches are likely in the future, Carter suggests that this usage is misleading.[15] Carter suggests that the phrase "anticipatory breach" is best reserved for a repudiation that occurs before the time for performance of a party's obligations (ie, one not involving an actual breach) and is accepted by the aggrieved party.[16]

In *Mackenzie v Rees*,[17] Dixon J stated that the doctrine of anticipatory breach does not apply "to contracts completely executed on one side".[18] Under this principle, an aggrieved party who has fully performed his or her obligations under a contract will not be able to terminate the contract and claim damages in respect of an anticipatory breach by the repudiating party. Rather, the aggrieved party must wait to claim damages until there is an actual breach by the other party. This restriction may be confined to an obligation by the party who has repudiated the contract to pay money to the aggrieved party or even to bills of exchange on the ground that this was the issue in *Mackenzie v Rees*. In *Wigan v Edwards*,[19] the scope of the restriction was left open by the High Court. In *Progressive Mailing House Ltd v Tabali Pty Ltd*,[20] Brennan J indicated some support for the restriction, at least in relation to an obligation to pay money.

The restriction on termination for anticipatory breach identified in *Mackenzie v Rees* is based on a concern not to enlarge the obligations of a party who has repudiated a contract. In *Progressive Mailing House Ltd v Tabali Pty Ltd*, Brennan J explained that an aggrieved party who has performed his or her obligations under a contract is entitled to no more than the full and timely performance of the contract by the other party and that an "immediate award of damages for anticipatory breach of those obligations gives him more than the benefit of the bargain".[21] This concern is particularly pertinent where the outstanding obligation of the party who has repudiated the contract is to pay money. In these circumstances, Brennan J said it might be asked why "should repudiation entitle the [aggrieved party] to accelerated payment when the contract stipulates that, in the circumstances that have occurred, that party should receive payment at a later time"?[22] The opposing view, also acknowledged by Brennan J, is that it is anomalous to refuse damages for anticipatory breach where the aggrieved party has fully performed his or her obligations but grant them where he or she has not.[23]

14 But see Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [23.21] (arguing that "damages for anticipatory breach should not depend absolutely on whether the contract was terminated").

15 Carter, *Carter's Breach of Contract* (2nd ed, 2018), [7-08]–[7-11].

16 Carter, *Carter's Breach of Contract* (2nd ed, 2018), [7-08]–[7-11].

17 *Mackenzie v Rees* (1941) 65 CLR 1.

18 *Mackenzie v Rees* (1941) 65 CLR 1, 15–7.

19 *Wigan v Edwards* (1973) 1 ALR 497, 503.

20 *Progressive Mailing House Ltd v Tabali Pty Ltd* (1985) 157 CLR 17, 44–6; cf *Moschi v Lep Air Services Ltd* [1973] AC 331.

21 *Progressive Mailing House Ltd v Tabali Pty Ltd* (1985) 157 CLR 17, 45.

22 *Progressive Mailing House Ltd v Tabali Pty Ltd* (1985) 157 CLR 17, 46.

23 *Progressive Mailing House Ltd v Tabali Pty Ltd* (1985) 157 CLR 17, 45.

Repudiation and other grounds for terminating

[22.20] There is a considerable overlap between repudiation and the other rights to terminate a contract conferred by the common law. A breach of a condition may also amount to a repudiation of the contract. However, since a breach of condition gives an aggrieved party the right to terminate the contract, it will usually not be necessary to determine whether or not a breach of condition is also repudiatory.[24] A breach of an intermediate term that is sufficiently serious to justify termination may indicate a lack of willingness or ability to perform the contract.[25] Indeed, courts do not always distinguish clearly between termination for breach of an intermediate term and termination for repudiation.[26] In both cases, courts may consider whether the breach is fundamental and whether the breach will deprive the aggrieved party of substantially the whole of the benefit of the contract. As noted at [21.80], however, there are important differences between repudiation and serious breach of an intermediate term.

As discussed in Chapter 21, where a term is classified as a warranty, there will be no right to terminate merely on grounds of a breach of that term, only a right to damages for any loss caused by the breach. However, a breach or threatened breach of a warranty may amount to a repudiation of the contract and therefore provide a right to terminate.[27] In *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd*,[28] Gleeson CJ, Gummow, Heydon and Crennan JJ said:

> There may be cases where a failure to perform even if not a breach of an essential term … manifests unwillingness or inability to perform in such circumstances that the other party is entitled to conclude that the contract will not be performed substantially according to its requirements.

In such cases, the breach or threatened breach on which the alleged repudiation was based would have to demonstrate an absence of willingness or ability to perform substantially the whole of the contract, or otherwise be fundamental. Repudiation might perhaps be found in a series of breaches of different warranties under a contract[29] or in repeated breaches of a warranty under an instalment contract.[30]

AN ABSENCE OF WILLINGNESS OR ABILITY

[22.25] Not every indication that a party is unwilling or unable to perform his or her obligations under the contract will amount to a repudiation of the contract. There will be a repudiation of the contract where a party's absence of willingness or ability to perform relates to the whole of the contract.[31] A party may also repudiate a contract through a lack of willingness or ability to perform particular obligations. This will be the case where the unwillingness or inability to

24 See *Wood Factory Pty Ltd v Kiritos Pty Ltd* (1985) 2 NSWLR 105, 144–5. On breach of a condition, see Chapter 21.

25 On breach of an intermediate term, see Chapter 21.

26 See, eg, *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17, esp 31 and 52; cf *Shevill v Builders Licensing Board* (1982) 149 CLR 620, 626.

27 See, eg, *Associated Newspapers Ltd v Bancks* (1951) 83 CLR 322, 339; *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 64; *Universal Cargo Carriers Corp v Citati* [1957] 2 QB 401, 430–1.

28 *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115.

29 See, eg, [22.50].

30 See, eg, [22.55].

31 See, eg, *Hochster v De La Tour* (1853) 2 E&B 678, 118 ER 922; *Psaltis v Schultz* (1948) 76 CLR 547.

perform relates to a condition or essential term of the contract.[32] Further, breach of a non-essential term may also evidence an intention to be no longer bound by the terms of the contract.[33] There will also be a repudiation of the contract where a party's unwillingness or inability to perform particular obligations is "fundamental". An absence of willingness or readiness to perform will be fundamental where it would deprive the aggrieved party of substantially the whole of the benefit of the obligations remaining to be performed under the contract.[34]

The relevance of the consequences of a threatened breach in assessing whether one party has repudiated the contract is illustrated in *Federal Commerce & Navigation Co Ltd v Molena Alpha Inc*.[35] In this case, the owners of a ship directed the masters of the ship not to sign any bills of lading endorsed "freight pre-paid". The House of Lords held that this direction was not authorised by the terms of the contract and constituted a repudiation of the contract. The majority of the House of Lords considered that the repudiation was a threatened or anticipatory breach of contract because the masters had not yet acted on the instruction.[36] The threatened breach was not a breach of a condition.[37] However, the House of Lords considered that the owners' conduct was a repudiation of the contract because it "went to the root of the contract as depriving the charterers of substantially the whole of the benefit of the contract".[38] The consequences of the orders given by the owners of the ship were "extremely serious" for the charterers.[39] Without the issue of freight pre-paid bills of lading, the charterers would be largely debarred from their trade in the carriage of grain and steel, they would be unable to comply with existing obligations and they were likely to be blacklisted by one of the world's largest shippers of grain.[40]

CONDUCT AMOUNTING TO A REPUDIATION

[22.30] A party will repudiate a contract where he or she evidences a lack of willingness or ability to perform the contract. Either unwillingness or inability will suffice. Thus, repudiation may be shown where a party, although genuinely willing, is unable to perform.[41]

Express statement of unwillingness or inability

[22.35] The most straightforward case of repudiation is where a party makes an express statement to the effect that he or she is unwilling or unable to perform the contract.[42] A party who states "I will not or cannot perform" may be taken at his or her word.

32 *Federal Commerce & Navigation Co Ltd v Molena Alpha Ltd* [1979] AC 757, 778, 783, 785; *Foran v Wight* (1989) 168 CLR 385, 395, 416, 441.

33 *Shevill v Builders Licensing Board* (1982) 149 CLR 620. See also *Allphones Retail Pty Ltd v Hoy Mobile Pty Ltd* [2009] FCAFC 85; (2009) 178 FCR 57, [49].

34 *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17, 31; *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 641–4; *Foran v Wight* (1989) 168 CLR 385, 441.

35 Inc *Federal Commerce & Navigation Co Ltd v Molena Alpha* [1979] AC 757.

36 See Inc *Federal Commerce & Navigation Co Ltd v Molena Alpha Inc* [1979] AC 757, 778, 782. Viscount Dilhourne and Lord Russell of Killowen held that the conduct was an actual breach.

37 Inc *Federal Commerce & Navigation Co Ltd v Molena Alpha Inc* [1979] AC 757, 778, 783, 785.

38 Inc *Federal Commerce & Navigation Co Ltd v Molena Alpha Inc* [1979] AC 757, 779, also 783–4, 785.

39 Inc *Federal Commerce & Navigation Co Ltd v Molena Alpha Inc* [1979] AC 757, 775.

40 Inc *Federal Commerce & Navigation Co Ltd v Molena Alpha Inc* [1979] AC 757, 775.

41 *Universal Cargo Carriers Corporation v Citati* [1957] 2 QB 401, 437; *Peter Turnbull & Co Pty Ltd v Munduus Trading Co (Australasia) Pty Ltd* (1954) 90 CLR 235, 253.

42 See, eg, *Hoad v Swan* (1920) 28 CLR 258, 264.

Why would a party ever admit to being unwilling or unable to perform? By giving notice of his or her impending failure to perform the contract, a party may at least give his or her contracting partner the opportunity to make other arrangements. Such a warning may go some way towards preserving the good reputation of the party who cannot perform, which is an important consideration for a party who deals frequently in a particular market. Moreover, if a repudiation of a contract is accepted, the aggrieved party's duty to mitigate his or her losses may in some circumstances reduce the damages for which the repudiating party will be liable.[43]

Repudiation based on words or conduct

[22.40] In the absence of an express statement of unwillingness or inability to perform, a party's words or conduct may indicate that he or she is repudiating the contract. In making this assessment, courts are generally[44] not concerned with the subjective intentions of the party in question.[45] The test is whether or not the words or conduct of the party would lead a reasonable person to conclude that the party did not intend or was unable to perform the contract.[46]

Conduct showing an inability or unwillingness to perform

[22.45] A party may repudiate a contract through conduct which puts it out of his or her power to perform that contract. For example, a purchaser under a contract for the sale of specific property may conclude that the seller has repudiated the contract where the seller disposes of the property to a third party before the date of the sale under the contract.[47]

Similarly, repudiation may be found in conduct which indicates that a party will not perform the contract according to its terms. For example, in *Carr v J A Berriman Pty Ltd*,[48] it was held that a building owner repudiated the contract by announcing that he had engaged another contractor to carry out a large part of the work comprised in the contract. In such a case, "a reasonable man could hardly draw any other inference than that the building owner does not intend to take the contract seriously, that he is prepared to carry out his part of the contract only if and when it suits him".[49]

However, it should not be assumed that continued breach of contractual obligations automatically constitutes repudiation. Where one party has not formally complied with the terms of the contract, but the other party has been happy to continue on with the contract despite the breach, such conduct is unlikely to sustain an inference of repudiation.[50]

43 On damages and mitigation for anticipatory breach, see [27.155].

44 But see discussion of an erroneous interpretation of the contract at [22.60].

45 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 647, 657–8.

46 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 647–8, 657.

47 See *Hoad v Swann* (1920) 28 CLR 258.

48 *Carr v JA Berriman Pty Ltd* (1953) 89 CLR 327, 351.

49 *Carr v JA Berriman Pty Ltd* (1953) 89 CLR 327, 351.

50 *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2006] FCAFC 40; (2006) 149 FCR 395, [101]; *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61; (2007) 233 CLR 115. A similar approach is adopted in the context of a party insisting on an erroneous interpretation of the contract: see *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, discussed at [22.60].

Repudiation inferred from combination of events

[22.50] Repudiation may be found in a combination of events, which, on their own, would not entitle the aggrieved party to terminate the contract. In *Progressive Mailing House Pty Ltd v Tabali Pty Ltd*,[51] the lessee had engaged in a number of breaches of contract, including inflicting physical damage to the premises, failing to rectify that damage, subletting the premises without the consent of the lessor and failing to pay rent. The High Court considered that, while the failure to pay rent on its own may not have been sufficient, this breach, in association with the other breaches, amounted to a fundamental breach or repudiation, justifying the lessor's termination of the lease.[52]

In *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd*,[53] the parties entered into an agreement for the lease of a shop. As part of this contract, the lessor undertook to procure the registration of a formal lease or to deliver a registerable lease to the lessee. The lessee authorised the lessor to complete any details required for the registration of the lease and paid the stamp duty and registration fees to the lessor. The lessee then took possession of the premises. In the following months, the lessee was told that the lease would be delivered "shortly" and in the not "too distant future". Some 10 months after the original agreement was made, the lessee wrote to the lessor's solicitor requesting registration within 14 days. The solicitors did not respond until the last day before the expiry of the notice and then merely stated that they were seeking instructions. The lease was not registered and the lessee terminated the agreement.

The High Court concluded that the lessor's conduct constituted a repudiation of the contract that entitled the lessee to terminate.[54] The time for providing a registered or registerable lease was not "of the essence".[55] This meant that mere delay on the part of the lessor would not have entitled the lessee to terminate the contract.[56] However, the court considered that the lessor's conduct viewed as a whole indicated that the lessor was not prepared to perform the contract. The lessor had not only delayed in fulfilling its obligation to procure a registered or registerable lease, but also had not given an adequate response to the lessee's repeated inquiries about the progress of the matter. As Mason J explained, the lessor's conduct towards the lessee was "not only dilatory but also cavalier and recalcitrant".[57]

Instalment contracts

[22.55] In some contracts, one or both of the parties' obligations may be divided into a number of instalments. For example, in a contract for the sale of goods, the seller may undertake to deliver the goods in a number of instalments to the buyer, with the buyer undertaking to pay for each instalment as delivered.[58] Failure to deliver or pay for one or more instalments may indicate that the party in breach is unwilling or unable to perform the remainder of

51 *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17.

52 *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17, 36–7, 40, 55. See also *Carr v J A Berriman Pty Ltd* (1953) 89 CLR 327.

53 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623.

54 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 637.

55 On time being of the essence, see Chapter 23.

56 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 633.

57 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 636.

58 See also the discussion of divisible contracts in Chapter 29.

his or her obligations under the contract and is thus repudiating the contract.[59] The Sale of Goods Acts require a court to have regard to the terms of the contract and the circumstances of the case in deciding whether or not a breach amounts to a repudiation of an instalment contract.[60] In making this assessment, in *Maple Flock Co Ltd v Universal Furniture Products (Wembley) Ltd*,[61] the English Court of Appeal identified two considerations as relevant: first, the quantitative ratio the breach bears to the contract as a whole and, secondly, the degree of probability or improbability that such a breach will be repeated.[62]

Maple Flock Co Ltd v Universal Furniture Products (Wembley) Ltd concerned a contract for the sale of 100 tons of rag flock to be delivered at the rate of three loads per week with one-and-a-half tons in each load. Part-way through the contract period, one load was found to be defective. The English Court of Appeal held that the breach was not a repudiation entitling the purchaser to terminate. The delivery complained about involved only a small ratio of the whole, being only one-and-a-half tons out of the total 100 tons deliverable under the contract.[63] The chance of the breach being repeated was "practically negligible".[64] The seller's business was carefully conducted, and the breach complained of was an isolated incident affecting one delivery out of 20 made both before and after the defective instalment.[65]

Repudiation and an erroneous interpretation of the contract

[22.60] A party may be found to have repudiated the contract by acting on or asserting an erroneous interpretation of the contract. Thus, a party who refuses to perform his or her obligations under a contract, or will not accept performance from another party except according to an incorrect interpretation of those obligations, may be found to have repudiated that contract.[66] Similarly, a party who attempts to terminate a contract where no such right exists may have repudiated.[67] In such cases, the conduct of the party asserting the incorrect interpretation may indicate that the party is unwilling to perform the contract according to its terms. However, there are two principles that reduce the likelihood of repudiation in these circumstances.

First, where an aggrieved party has relied on a ground for terminating that proves invalid, that party will generally be able to justify the termination by reference to any other grounds, even though those grounds were not, at the time of termination, raised by or even known to the aggrieved party and thus did not factor into his or her decision to terminate the

59 See, eg, *International Leasing Corp (Vic) Ltd v Aiken* [1967] 2 NSWLR 427.

60 *Sale of Goods Act 1954* (ACT), s 35(2); *Sale of Goods Act 1923* (NSW), s 34(2); *Sale of Goods Act* (NT), s 34(2); *Sale of Goods Act 1896* (Qld), s 33(2); *Sale of Goods Act 1895* (SA), s 31(2); *Sale of Goods Act 1896* (Tas), s 36(2); *Goods Act 1958* (Vic), s 38(2); *Sale of Goods Act 1895* (WA), s 31(2).

61 *Maple Flock Co Ltd v Universal Furniture Products (Wembley) Ltd* [1934] 1 KB 148.

62 *Maple Flock Co Ltd v Universal Furniture Products (Wembley) Ltd* [1934] 1 KB 148, 157. In focusing on the consequences of a breach, these tests might equally be applied to the breach of an intermediate term to determine whether or not there is a right to terminate: see Greig and Davis, *The Law of Contract* (1987), p 1215.

63 *Maple Flock Co Ltd v Universal Furniture Products (Wembley) Ltd* [1934] 1 KB 148, 157.

64 *Maple Flock Co Ltd v Universal Furniture Products (Wembley) Ltd* [1934] 1 KB 148, 157.

65 *Maple Flock Co Ltd v Universal Furniture Products (Wembley) Ltd* [1934] 1 KB 148, 157.

66 See, eg, *Luna Park (NSW) Ltd v Tramways Advertising Pty Ltd* (1938) 61 CLR 286; *Federal Commerce and Navigation v Molena Alpha Inc* [1979] AC 757.

67 See,eg, *Petrie v Dwyer* (1954) 91 CLR 99, 104; *Ogle v Comboyuro Investments Pty Ltd* (1976) 136 CLR 444, 453.

contract.[68] For example, if an employer dismisses an employee for committing a wrong that would not justify the termination of the contract, the employer will be justified in terminating the contract if the employee has committed other, serious wrongs that would justify termination. It would not matter that when the employer purported to terminate the contract he or she was unaware of the latter wrongs.[69]

Secondly, courts have held that the honesty or "bona fides" of a party propounding an incorrect interpretation of a contract will be relevant in assessing whether or not that party has repudiated the contract.[70] The reason for this approach is that a party who asserts an erroneous interpretation of a contract believing it to be correct may not be rejecting the contract.[71] In a sense, the party is attempting to rely on the terms of the contract; it is just that his or her interpretation of those terms is incorrect. It is possible that, if the error had been explained, the party would have been prepared to perform the contract according to its terms.[72] This approach appears to be an exception to the general principle that the conduct of a repudiating party is judged objectively.[73]

DTR Nominees Pty Ltd v Mona Homes Pty Ltd[74] concerned a contract for the sale of land that was to be subdivided by the vendor. The vendor considered that the contract permitted it to subdivide the land in two stages. This interpretation was incorrect. The purchasers purported to terminate the contract on the ground that the vendor had shown an unwillingness to perform the contract according to its terms and so had repudiated the contract. The vendor asserted that the purchasers' termination was wrongful and itself constituted a repudiation of the contract. The majority of the High Court held that neither party had repudiated the contract.[75] The vendor had not repudiated the contract because it had honestly believed in its interpretation. Stephen, Mason and Jacobs JJ explained:

> In this case the vendor acted on its view of the contract without realising that the purchasers were insisting upon a different view until such time as they purported to rescind. It was not a case in which any attempt was made to persuade the vendor of the error of its ways or indeed to give it any opportunity to reconsider its position in the light of an assertion of the correct interpretation. There is therefore no basis on which one can infer that the vendor was persisting in its interpretation willy nilly in the face of a clear enunciation of the true agreement.[76]

68 See, eg, *Rawson v Hobbs* (1961) 107 CLR 466. See also *Shepherd v Felt and Textiles of Australia Ltd* (1931) 45 CLR 359, 373, 377–8; *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 431–3; *Concut Pty Ltd v Worrell* [2000] HCA 64, [27]–[29].

69 See, eg, *Downer EDI Ltd v Gillies* [2012] NSWCA 333.

70 See, eg, *Green v Sommerville* (1979) 141 CLR 594, 601, 611; *Woodar Investment Ltd v Wimpey Construction (UK) Ltd* [1980] 1 WLR 227; *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423; *Dainford Ltd v Smith* (1985) 155 CLR 342, 350, 365–6; *Trawl Industries Australia Pty Ltd v Effem Foods Pty Ltd (t/as "Uncle Ben's of Australia")* (1992) 27 NSWLR 326, 358; *Vaswani v Italian Motors (Sales and Service) Ltd* [1996] 1 WLR 270, 276–7; *Roadshow Entertainment Pty Ltd v (ACN 053 006 269) Pty Ltd Receiver & Manager Appointed* (1997) 42 NSWLR 462, 479.

71 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 432; *Woodar Investment Ltd v Wimpey Construction (UK) Ltd* [1980] 1 WLR 277, 280, 283, 297, 299.

72 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 432; *Woodar Investment Ltd v Wimpey Construction (UK) Ltd* [1980] 1 WLR 277, 297, 299.

73 See [22.40].

74 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423.

75 Stephen, Mason and Jacobs JJ (Aickin J agreeing), Murphy J dissenting.

76 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 432.

The court concluded that, since the vendor was the party in error, the vendor could not terminate on the basis of the purchasers' wrongful termination.[77] The purchasers' termination indicated no more than an intention not to proceed on the incorrect interpretation of the contract advanced by the vendor. Instead, the parties were considered to have abandoned the contract.[78]

How should an aggrieved party respond?

[22.65] What should an aggrieved party do when the other party refuses to proceed other than on an incorrect interpretation of the contract? Given that a party asserting an incorrect but honest interpretation of a contract may not have repudiated the contract, it will often not be prudent for an aggrieved party to attempt to terminate a contract on the basis of such conduct. As in *DTR Nominees Pty Ltd v Mona Homes Pty Ltd*, after costly litigation, a court may find that the aggrieved party had no right to terminate. *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* suggests that in such a case, the aggrieved party should take steps to persuade the mistaken party of his or her error.[79]

What if the aggrieved party's explanation of the contract is rejected? In *DTR Nominees Pty Ltd v Mona Homes Pty Ltd*, the High Court suggested that the problem of one party maintaining an incorrect interpretation of a contract might be resolved by the parties seeking an "authoritative exposition of the correct interpretation",[80] presumably from a court.[81] Where the party asserting an incorrect interpretation indicates that he or she is willing to perform the contract in accordance with such a determination, an inference of repudiation cannot be drawn.[82]

Limits to the relevance of a mistaken party's honesty

[22.70] There are cases in which a party who has asserted an incorrect interpretation of a contract has been found to have repudiated the contract, regardless of the honesty of that party in asserting the interpretation. Carter suggests that the honesty of a party asserting an incorrect interpretation of a contract may not be relevant in cases where the aggrieved party needs to respond to the apparent repudiation promptly to protect his or her interests and there is no time to obtain a court's ruling on the correct interpretation of the contract.[83] In *Vaswani v Italian Motors Ltd*,[84] the Privy Council indicated that a party who asserts an incorrect interpretation, albeit honestly, will be found to have repudiated the contract where that party has also engaged in conduct detrimental to the aggrieved party or inconsistent with the contract remaining on foot.

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77 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 433.

78 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 433. See also discussion of abandonment at [19.40].

79 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 432–3.

80 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 432. See also *Savoy Investments (Qld) Pty Ltd v Global Nominees Pty Ltd* [2008] QCA 282, [41].

81 See *Woodar Investment Ltd v Wimpey Construction (UK) Ltd* [1980] 1 WLR 277.

82 *Highmist Pty Ltd v Tricare Ltd* [2005] QCA 357, [54].

83 Carter, "Regrettable Developments in the Law of Contract?" [1980] *Cambridge Law Journal* 256, 257, giving as an example *Federal Commerce and Navigation v Molena Alpha Inc* [1979] AC 757.

84 *Vaswani v Italian Motors Ltd* [1996] 1 WLR 270, 276–7.

Inability in fact

[22.75] As already noted, a party's words or conduct are not the only means of establishing repudiation. Repudiation may also be established by showing that a party would, as a matter of fact, be unable to perform his or her obligations under the contract, a situation sometimes termed *factual inability* or *impossibility*.

There are very few cases directly addressing the issue of factual impossibility.[85] This is because an aggrieved party wishing to terminate for repudiation will usually be able to rely on the conduct of the other party as indicating an inability to perform. Moreover, establishing repudiation on the basis of an inability to perform in fact is more difficult than establishing repudiation based on a party's words or conduct.[86] Repudiation based on words or conduct is assessed by considering the inference a reasonable person would draw from the conduct. Factual impossibility as a basis for repudiation "must be proved in fact not supposition".[87] This means the aggrieved party must show that, as a matter of fact, the repudiating party was "wholly and finally" disabled from performing.[88] Termination for impossibility may prove relevant where an aggrieved party has purported to terminate on a ground that proved invalid. The aggrieved party may justify the termination by demonstrating that the other party had become wholly and finally disabled from performing his or her contractual obligations.[89]

Universal Cargo Carriers Corporation v Citati[90] concerned a charterparty of a ship. The charterers were under an obligation to finish loading the ship by a specified time. The owner terminated the charter party before the expiry of this time on the ground that the charterers could not have loaded within the time remaining and so had repudiated the contract. The arbitrator found that, at the date of termination, the owners could have inferred from the charterer's conduct that the charterer could not have performed within a reasonable time after the time for loading required by the contract, but could have performed before the delay became so long as to frustrate the purpose of the contract. Devlin J held that these findings precluded a conclusion that the charterers had repudiated by conduct.[91] This is because the test for repudiation by conduct based on delay is not whether the delay was unreasonable but whether it was sufficient to frustrate the commercial purpose of the contract.[92] Delvin J also held that the owners could justify termination on grounds of impossibility if they could establish in fact, as opposed to inference, that the charterer was, at the time of termination by the owners, unable to find and to load a cargo in a shorter period of time than was necessary to frustrate the commercial purpose of the contract.[93] The case was remitted to the arbitrator for determination of that question.

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85 But see, eg, *Universal Cargo Carriers Corporation v Citati* [1957] 2 QB 401; *Rawson v Hobbs* (1961) 107 CLR 466.

86 See, eg, *Winterton Constructions Pty Ltd v Hambros Australia Ltd* (1992) 39 FCR 97, 111.

87 *Universal Cargo Carriers Corporation v Citati* [1957] 2 QB 401, 449–50. For criticism, see Carter, *Breach of Contract* (2nd ed, 1991), pp 674–5; Greig and Davis, *The Law of Contract* (1987), p 1251.

88 *Universal Cargo Carriers Corporation v Citati* [1957] 2 QB 401, 446.

89 *British & Benningtons Ltd v North Western Cachar Tea Co Ltd* [1923] AC 48, 70; *Universal Cargo Carriers Corp v Citati* [1957] 2 QB 401, 443; *Rawson v Hobbs* (1961) 107 CLR 466.

90 *Universal Cargo Carriers Corporation v Citati* [1957] 2 QB 401.

91 *Universal Cargo Carriers Corporation v Citati* [1957] 2 QB 401, 439.

92 *Universal Cargo Carriers Corporation v Citati* [1957] 2 QB 401, 430, 435.

93 *Universal Cargo Carriers Corporation v Citati* [1957] 2 QB 401, 446.

RIGHTS TO SUSPEND PERFORMANCE

[22.80] In some cases, an aggrieved party may believe but not be able to establish that the other party is not willing or able to perform the contract. In such a case, the aggrieved party has few options for safeguarding his or her position. If the aggrieved party waits until the date for performance, and it does not take place, the aggrieved party may suffer a loss. However, an aggrieved party seeking to terminate, risks being proven wrong in his or her assessment that the other party has repudiated. An aggrieved party who wrongfully attempts to terminate a contract on the basis of the other party's repudiation may then be liable in damages for wrongful termination. A party who doubts the ability of the other party to perform cannot demand an assurance that the other party is willing and able to perform under Australian contract law,[94] although the parties might expressly provide in their contract for such a right. This position may be contrasted with that of the *United Nations Convention on Contracts for the International Sale of Goods* (CISG)[95] and the *UNIDROIT Principles of International Commercial Contracts 2016* (UPICC).[96] Under the CISG, an aggrieved party may suspend performance if it "becomes apparent that the other party will not perform a substantial part of his [or her] obligations".[97] The aggrieved party must however continue with performance if the other party provides "adequate assurance" of his or her performance.[98] Under the UPICC, an aggrieved party may suspend his or her own performance and demand adequate assurance of due performance from the other party where the aggrieved party "reasonably believes that there will be a fundamental non-performance by the other party".[99]

94 See generally Carter, "Adequate Assurance of Due Performance" (1996) 10 *Journal of Contract Law* 1.

95 See also [1.180].

96 See also [1.180].

97 Article 71(1).

98 Article 71(3).

99 Article 7.3.4.

CHAPTER **23**

Termination for delay

WHY A SEPARATE ANALYSIS?

[23.05] A delay in performance will give rise to breach and in turn a right of termination at law in the same circumstances as for breach or repudiation[1] of other terms of a contract.[2] Nevertheless, termination for delay is usually given a separate discussion in textbooks. This is due to the distinctive character of a breach constituted by delay. Lindgren explains:

> A stipulation of a time for the doing of an act is different from the substantive obligation to do the act, eg the obligations to convey property and to pay money for it. Whereas the promises to convey and to pay are correlative and concurrent and the breach of them involves a measurable loss, a time stipulation is a machinery aspect of a substantive obligation and breach of it merely involves a delay in performance which may involve no loss at all.[3]

Special terminology is associated with the right to terminate for delay. Where a term governing the time for performance has the status of a condition – so that breach gives rise to a right to terminate – it is said that *time is of the essence* under the contract. Much of this chapter concerns the rules regarding where time is of the essence and where it is not. The chapter also discusses the use of a *notice* procedure through which parties may gain a right to terminate for delay, even where time is not of the essence under the contract.

1 Repudiation is sometimes referred to as renunciation (see [22.05]). The discussion in this chapter employs the term repudiation.
2 See Chapters 21 and 22.
3 Lindgren, *Time in the Performance of Contracts* (2nd ed, 1982), p 1.

AT WHAT TIME IS PERFORMANCE REQUIRED?

[23.10] In some cases, the contract will specify precisely the time at which particular obligations are to be performed. In other cases, the time specified for performance will be more general, for example, requiring performance within a specified period of time or, even more generally, within a "reasonable time". Where a contract does not expressly specify the time at which an obligation is to be performed, a term will be implied requiring performance of the obligation within a reasonable time.[4] What is a reasonable time will depend on the circumstances of the case, including the subject matter of the contract and the context in which it was made.[5]

WHERE TIME IS OF THE ESSENCE

[23.15] A time stipulation which has the status of a condition is usually described as *essential* and it is said that time is *of the essence*. Where time is of the essence, any delay amounting to breach of the time stipulation will entitle the party not in breach (the aggrieved party) to elect to terminate the contract.

Express designation

[23.20] The parties may expressly agree that time is to be essential in relation to some or all of the obligations in their contract. The most common formulation is a statement that "time is to be of the essence". The parties may also make time essential by specifying that a breach of a time stipulation will be a repudiation of the contract, for which the aggrieved party may terminate.[6] There is some suggestion that an express right to terminate a contract for delay does not conclusively make time of the essence and that an inquiry into the issue will still be required.[7]

No express stipulation

[23.25] By the 19th century, common law and equity took different approaches to time stipulations,[8] particularly in contracts for the sale of land.[9] The common law treated time stipulations strictly. At common law, unless there was an expression of contrary intention by the parties, time was usually treated as essential. In equity, time would only be considered of the essence where it could be concluded that the parties had intended this result. Where time

4 *Reid v Moreland Timber Co Pty Ltd* (1946) 73 CLR 1, 13. See also *Handley v Gunner* [2008] NSWCA 113, [124].

5 *Canning v Temby* (1905) 3 CLR 419, 426.

6 See, eg, *Lombard North Central plc v Butterworth* [1987] 1 QB 527.

7 See *Hewitt v Debus* [2004] NSWCA 54; (2004) 59 NSWLR 617. But see also the criticism of this case in Stone, "Hewitt v Debus – Untangling Law and Equity's View of the Right to Terminate" (2004) 20 *Journal of Contract Law* 255. Note also that Meagher JA in his dissenting judgment in *Hewitt v Debus* described the approach adopted by the majority as wholly mis-stating the law in a very fundamental way: *Hewitt v Debus* [2004] NSWCA 54, (2004) 59 NSWLR 617 [1]. Meagher JA was of the opinion that it is only necessary to show that time is of the essence if equitable relief is sought. Thus an express right to terminate should be given effect to, even if it cannot be established that time was of the essence.

8 See the discussion in *Holland v Wiltshire* (1954) 90 CLR 409, 418–9; *Louinder v Leis* (1982) 149 CLR 509, 524–5, 532. See also Lindgren, *Time in the Performance of Contracts* (2nd ed, 1982), Ch 2.

9 Lindgren, *Time in the Performance of Contracts* (2nd ed, 1982), p 1 comments that most of the contract cases dealing with time involve contracts for the sale of land.

was not of the essence, courts of equity would, in appropriate cases, prevent the exercise of an aggrieved party's common law right to terminate for breach of a time stipulation by ordering specific performance of the contract.

The equitable approach to time stipulations now prevails. This result was originally brought about by legislation based on s 25(7) of the *Judicature Act 1873*, which provided:

> Stipulations in contracts, as to time or otherwise, which would not before the passing of this Act have been deemed to be or have become of the essence of such contracts in a court of equity, shall receive in all courts the same construction and effect as they would have heretofore received in equity.[10]

Provisions in substantially similar terms have been enacted in all of the Australian States and Territories.[11] Accordingly, in the absence of express stipulation by the parties, whether or not time is of the essence is a matter of construction of the contract in question.

Construing time stipulations as being of the essence

[23.30] In deciding whether or not a time stipulation should be construed as essential, the considerations discussed in relation to the classification of terms as conditions will apply.[12] Courts are most likely to construe time as being of the essence in commercial contracts for the sale of goods (which are known as *mercantile* contracts).[13] Certainty about the time at which obligations will be performed is particularly important in mercantile contracts, where there may be a long chain of buyers and sellers, each of whom relies on timely performance of the contract in order to fulfil their obligations under other contracts. Accordingly, terms specifying a time for the shipment or delivery of goods will commonly be construed as essential.[14] However, there is no uniform rule that time is essential in mercantile contracts. For example, under the *Sale of Goods Acts*, the time for payment is deemed not to be of the essence of a contract of sale unless a different intention appears from the terms of the contract.[15]

WHERE TIME IS NOT OF THE ESSENCE

[23.35] Where time is not of the essence, breach of a time stipulation will not, of itself, give the aggrieved party a right to terminate. In the absence of notice, termination will in such

10 On time becoming of the essence, see discussion of the notice procedure at [23.50]ff.

11 See *Civil Law (Property) Act 2006* (ACT), s 501; *Conveyancing Act 1919* (NSW), s 13; *Law of Property Act* (NT), s 65; *Property Law Act 1974* (Qld), s 62; *Law of Property Act 1936* (SA), s 16; *Supreme Court Civil Procedure Act 1932* (Tas), s 11(7); *Property Law Act 1958* (Vic), s 41; *Property Law Act 1969* (WA), s 21. On the effect of this provision, see *Holland v Wiltshire* (1954) 90 CLR 409, 418–9; *Bunge Corporation New York v Tradax Export SA Panama* [1981] 1 WLR 711; Lindgren, *Time in the Performance of Contracts* (2nd ed, 1982), [223]–[251].

12 See Chapter 21.

13 *United Scientific Holdings Ltd v Burnley Borough Council* [1978] AC 904, 924, 937, 950; *Bunge Corporation New York v Tradax Export SA Panama* [1980] 1 Lloyd's Rep 294, 306, 310.

14 See, eg, *Harrington v Browne* (1917) 23 CLR 297; *Bowes v Chaleyer* (1923) 32 CLR 159; *Toepfer v Lenersan-Poortman NV* [1980] 1 Lloyd's Rep 143.

15 *Sale of Goods Act 1954* (ACT), s 15(1); *Sale of Goods Act 1923* (NSW), s 15(1); *Sale of Goods Act* (NT), s 15(1); *Sale of Goods Act 1896* (Qld), s 13(1); *Sale of Goods Act 1895* (SA), s 10(1); *Sale of Goods Act 1896* (Tas), s 15; *Goods Act 1958* (Vic), s 15; *Sale of Goods Act 1895* (WA), s 10(1).

cases only be justified where there is delay amounting to repudiation and, possibly, for a serious breach of an intermediate term. As noted earlier in this chapter, where the parties have not stipulated a time for performance, the courts will imply an obligation to perform within a reasonable time. In such circumstances, it is highly unlikely that time will be viewed as being of the essence,[16] unless failure to perform within a reasonable time will have serious consequences for the aggrieved party.[17]

Time stipulations as intermediate terms

[23.40] It is not certain whether or not the category of intermediate terms applies to time stipulations. As discussed earlier, where a term is intermediate, the right to terminate for breach depends on the gravity of the breach and its consequences.[18] In *Bunge Corp New York v Tradax Export SA Panama*,[19] Lord Wilberforce considered there to be a "fundamental fallacy" in attempting to apply the intermediate term analysis to a time stipulation because "there is only one kind of breach possible, namely to be late".[20] In *Ankar Pty Ltd v National Westminster Finance (Australia) Ltd*,[21] the majority in the High Court referred to this comment and expressly refrained from expressing a view as to whether or not it was correct.[22] In support of the view that a time stipulation might be classed an intermediate term, Carter observes that, although only one type of breach of a time stipulation is possible, the degree and consequences of such a breach may vary.[23]

Repudiation

[23.45] Where time is not essential, an aggrieved party may nonetheless gain a right to terminate for delay where the delay amounts to a repudiation of the contract.[24] For delay to amount to repudiation, the delay must be such as to evidence an intention on the part of the delaying party no longer to be bound by the contract.[25] This means that the delay must be "gross" or "protracted".[26] It has been said that the delay must be such as to frustrate the commercial purpose of the contract.[27] It is also possible that delay may be combined with other conduct to indicate a repudiation of the contract.[28]

16 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623.

17 *Douglas v Cicirello* [2006] WASCA 226, [16].

18 See discussion of intermediate terms in Chapter 21.

19 *Bunge Corp New York v Tradax Export SA Panama* [1981] 1 WLR 711.

20 *Bunge Corp New York v Tradax Export SA Panama* [1981] 1 WLR 711, 715.

21 *Ankar Pty Ltd v National Westminster Finance (Australia) Ltd* (1987) 162 CLR 549.

22 *Ankar Pty Ltd v National Westminster Finance (Australia) Ltd* (1987) 162 CLR 549, 562.

23 Carter, *Contract Law in Australia* (7th ed, 2018), [30-52].

24 *Louinder v Leis* (1982) 149 CLR 509, 526; *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 633, 643.

25 *Carr v J A Berriman Pty Ltd* (1953) 89 CLR 327, 349.

26 *Neeta (Epping) Pty Ltd v Phillips* (1974) 131 CLR 286, 302; *Sindel v Georgiou* (1984) 154 CLR 661, 671.

27 *Universal Cargo Carriers Corporation v Citati* [1957] 2 QB 401, 430.

28 See, eg, *Holland v Wiltshire* (1954) 90 CLR 409; *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623.

NOTICE

The notice procedure

[23.50] Where time is not of the essence and the delay in breach of contract does not amount to a serious breach of an intermediate term or a repudiation of the contract, an aggrieved party may nonetheless gain a right to terminate through the procedure of providing notice. Although the notice procedure is most commonly used in conveyancing transactions, it is applicable to contracts of all kinds.[29] It was, for example, assumed by the High Court in *Carr v JA Berriman Pty Ltd* to be applicable to a building contract.[30]

An aggrieved party will be entitled to give notice to a party who, through delay, has breached the contract, as soon as the delay is evident. If the other party has failed to perform by the time required by the contract, he or she is in breach of the contract and there is no need for the aggrieved party to wait for an unreasonable delay before giving notice.[31] The notice must set a reasonable time for performance of the obligation. If the party in breach does not perform the obligation in question within the reasonable time specified in the notice, the aggrieved party may immediately terminate the contract.[32]

The requirements for a valid notice

[23.55] A valid notice to perform a contract or contractual obligation must satisfy three requirements:

1. the notice must specify a time for performance;
2. the time allowed must be reasonable; and
3. the notice must clearly convey either that the time fixed for performance is of the essence or that the party giving the notice will regard himself or herself as being entitled to terminate should the notice not be complied with.[33]

In addition, the party issuing the notice must be ready and willing to perform his or her contractual obligations at the time the notice is issued.[34] Not all breaches prevent a party from issuing a notice to complete. Breach of inessential obligations that could easily sound in damages will not preclude the giving of a notice to complete.[35]

A notice which does not satisfy these three requirements will not be effective. In *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd*,[36] the parties entered into a contract for the lease of a shop forming part of a retail centre. As part of this contract, the lessor undertook to procure the registration of a formal lease or to deliver a registerable lease to the lessee.

29 See Carter, *Contract Law in Australia* (7th ed, 2018), [30-62].

30 *Carr v JA Berriman Pty Ltd* (1953) 89 CLR 327, 348-9.

31 *Louinder v Leis* (1982) 149 CLR 509, 514, 524.

32 *Louinder v Leis* (1982) 149 CLR 509, 514, 526, 532–3.

33 On this requirement, see further *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 653–4.

34 *W & R Pty Ltd v Birdseye* [2008] SASC 321; (2008) 102 SASR 477, [66]. On the readiness requirement, see further Chapter 25.

35 *Alexus Pty Ltd v Pont Holdings Pty Ltd* [2000] NSWSC 1171, [22]–[24].

36 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623.

After considerable delay, the lessee's solicitors wrote to the lessor's solicitor requiring the lessor to complete registration within 14 days. The notice stated that if registration was not completed within the required time, "our clients [the lessees] naturally reserve their rights in respect of your client's default". The lease was not registered within the specified 14-day period and the lessee terminated the agreement. The High Court considered that the notice was not effective to give the lessee a right to terminate. The time specified in the notice was not reasonable.[37] Evidence had been given to the effect that registration of a lease required a longer time than 14 days.[38] Further, the notice did not communicate its consequences.[39] Accordingly, the lessor's failure to comply with the notice did not of itself give the lessee a right to terminate the contract. However, the court considered that the lessor's conduct viewed as a whole sustained the inference of repudiation.

Notice must be given in relation to the provision that has been breached

[23.60] To be effective, notice must be given in relation to the time stipulation that has been breached. The notice procedure cannot be used to require the performance of some other obligation, the time for performance of which has not yet arisen. In *Louinder v Leis*,[40] a contract for the sale of land did not fix a date for completion and did not state that time was of the essence. The contract provided that, within 28 days from the delivery of the vendor's statement of title, the purchaser should tender a transfer to the vendor for execution. When the purchaser did not comply with this provision, the vendor's solicitor posted a notice to the purchaser requiring completion of the contract within 21 days. When this notice was not complied with, the vendor purported to terminate the contract. The High Court held that the notice did not entitle the vendor to terminate the contract. While the vendor would have been entitled to give the purchaser a notice requiring a transfer to be tendered within a reasonable time, the vendor was not entitled to give a notice requiring completion of the contract. Since no time for completion was specified, the obligation was to be performed within a reasonable time. There had not been an unreasonable delay in completing the contract that would breach the implied time stipulation and justify the vendor giving a notice to complete.[41]

What is a reasonable time for compliance with a notice?

[23.65] Whether the time for performance specified in a notice is reasonable will depend on the circumstances of the case.[42] Courts have identified a number of factors that may be taken into account. These include the subject matter of the obligation, what remains to be done at the date of the notice,[43] whether the aggrieved party has been continually pressing for performance[44] and any unnecessary delay on the part of the party in breach before the notice was given.[45]

37 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 640, 647, 655.
38 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 639, 647.
39 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 638, 646, 655.
40 *Louinder v Leis* (1982) 149 CLR 509.
41 *Louinder v Leis* (1982) 149 CLR 509, 514, 529, 536.
42 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 638.
43 *Strickney v Keeble* [1915] AC 386, 419.
44 *Strickney v Keeble* [1915] AC 386, 419.
45 *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623, 638.

Expert evidence about the time required to perform the obligation in question may also be relevant.[46] The contract may include an express provision that defines a sufficient time for the giving of any notice pursuant to the contract. However, where a shorter period of time is specified in the notice, the notice may nevertheless be effective provided the period of time specified is reasonable.[47]

Why does failure to comply with a valid notice give rise to a right to terminate?

[23.70] A notice is often described as making time "of the essence". To say a notice makes time essential is a "convenient description" of the effect of notice because it indicates that a failure to comply with the notice will give the aggrieved party a right to terminate the contract.[48] However, strictly, a notice does not change the status of the time fixed for performance by the contract.[49] Rather, courts have explained that failure by the party in breach to comply with a notice setting a reasonable time for performance will amount to an unreasonable delay in complying with a non-essential time stipulation. The unreasonable delay is evidence from which repudiation may be inferred which, in turn, gives the aggrieved party a right to terminate.[50]

WHERE THE CONTRACT IS SILENT ABOUT THE TIME FOR PERFORMANCE

[23.75] As already discussed, where a contract does not expressly specify the time at which particular obligations are to be performed, a term will be implied requiring performance within a reasonable time. In such a case, there will only be a breach of the implied time stipulation where there is an unreasonable delay in performance. Where no time is specified under the contract, time is unlikely to be of the essence.[51] Consequently, the mere fact of unreasonable delay will not usually entitle an aggrieved party to terminate the contract. To terminate for breach of an implied stipulation to perform within a reasonable time, an aggrieved party must usually rely either on repudiation or non-compliance with a notice by the party in breach. It is important to remember that in cases where a time for performance is not specified, there must be an initial period of unreasonable delay before a breach arises.[52] Accordingly, repudiation will only be inferred from a substantial delay that goes beyond or, in the cases of anticipatory breach, is likely to go beyond this initial period of unreasonable delay. A notice setting a reasonable time to perform can only be given after an initial period of unreasonable delay constituting the breach of contract.

46 See, eg, *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623.

47 See, eg, *McQueen v Leduva Pty Ltd* [2008] NSWSC 284.

48 *Louinder v Leis* (1982) 149 CLR 509, 532.

49 *Louinder v Leis* (1982) 149 CLR 509, 533.

50 See *Louinder v Leis* (1982) 149 CLR 509, 526; *Ciavarella v Balmer* (1983) 153 CLR 438, 446.

51 See, eg, *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623.

52 See also *Louinder v Leis* (1982) 149 CLR 509, 527.

THE EFFECT OF AN EXTENSION OF THE TIME FOR PERFORMANCE

[23.80] Where one party is having difficulties in performing his or her obligations within the time required by the contract, the other party may decide to give an extension of time for performance. Such an extension will usually be binding on the party who has granted it. The extension may in some cases constitute a variation of the contract. Alternatively, the extension may give rise to an estoppel preventing the party who has given the extension from exercising his or her original rights under the contract. The rights of the party granting the extension to terminate after the extension of time has expired depend on the nature of the obligation and of the extension.

If time was originally of the essence, and the extension specified a new time at which the obligation in question was to be performed, time generally will remain of the essence. Accordingly, the party granting the extension will be entitled to terminate the contract immediately should the obligation not be performed by the time specified in the extension.[53] If time was originally of the essence, but the extension did not specify a new time for performance, instead merely indicating a willingness to accept late performance, then time will no longer be of the essence.[54] In order to regain a right to terminate for delay if the obligation is not performed after the time specified in the extension, the party granting the extension must either establish repudiation or give a notice specifying a reasonable time for the obligation to be performed. If time was not originally of the essence and the obligation is not performed by the end of the extension, then time still is not of the essence and the party granting the extension must show repudiation or rely on the notice procedure in order to gain a right to terminate.

53 *Mehmet v Benson* (1965) 113 CLR 295, 305; *Tropical Traders Ltd v Goonan* (1964) 111 CLR 41.

54 *Ogle v Comboyuro Investments Pty Ltd* (1976) 136 CLR 444, 459.

CHAPTER **24**

Consequences of affirmation or termination

THE NEED TO ELECT

[24.05] A party cannot, by breaching or repudiating[1] a contract, bring the contract to an end or compel the other party (the *aggrieved party*) to bring the contract to an end.[2] Where there is a breach or repudiation giving rise to a right to terminate, the aggrieved party has a choice. The aggrieved party may elect between terminating and continuing with the contract. The aggrieved party is said to affirm the contract when he or she elects to continue with it. The notion of election is discussed in more detail in Chapter 25.

As we have discussed, the right to terminate is a very effective self-help remedy available to an aggrieved party who has decided that a particular contractual relationship is no longer in his or her best interests.[3] Conversely, an aggrieved party may have good reasons for affirming, rather than terminating, a contract. Termination is likely to cause a certain amount of inconvenience to the aggrieved party. In particular, termination will mean that the aggrieved party will have to find a new contracting partner. The aggrieved party may consider that attempting to resolve any problems between the parties is preferable to this inconvenience. The aggrieved party may also value continuing his or her relationship with the other party over any short-term advantage gained by terminating.

Conduct constituting an election is discussed in Chapter 25. In this chapter, we look at the consequences of an aggrieved party's decision either to affirm or to terminate a contract for both the aggrieved party and the other party.

WHERE THE CONTRACT IS AFFIRMED

Consequences of affirmation for the aggrieved party

Damages

[24.10] If an aggrieved party affirms a contract, he or she retains a right to claim damages for loss caused by the breach, subject to one qualification. The qualification arises in the case of

1 Repudiation is sometimes referred to as renunciation (see [22.05]). The discussion in this chapter employs the term repudiation.

2 *Automatic Fire Sprinklers Pty Ltd v Watson* (1946) 72 CLR 435; *Carr v JA Berriman Pty Ltd* (1953) 89 CLR 327; *White & Carter (Councils) Ltd v McGregor* [1962] AC 413.

3 See [PtXI.05].

anticipatory breach.[4] Damages will be available for a repudiation occurring before the time set for performance that is accepted by the aggrieved party terminating the contract.[5] However, if the repudiation is not accepted, then the contract will continue on foot and there will be no right to damages. Should the obligation in question not be performed at the required time, there will be an actual breach, which will give the aggrieved party a new right to terminate the contract and a right to damages.[6]

Earning the contract price

[24.15] In some situations, an aggrieved party who elects to continue with a contract following a repudiation by the other party may be able to completely perform his or her own obligations under the contract. In such a case, the aggrieved party will earn a right to payment of the contract price.[7] This principle and its limits are discussed in Chapter 29.

Does the aggrieved party still have to perform?

[24.20] An aggrieved party who affirms a contract keeps the contract alive for the benefit of both of the parties.[8] In principle, this means that the aggrieved party remains liable to perform his or her own contractual obligations. However, the preferable course of action for an aggrieved party faced with a breach or repudiation will often be to wait and see whether or not the other party changes his or her position and becomes ready to perform. While there is no general right to this effect,[9] the principle that an aggrieved party who affirms a contract remains liable to perform is subject to a qualification, now seen as based on the doctrine of estoppel.[10]

An aggrieved party may be absolved of the consequences of non-performance of his or her own obligations where the other party intimates that performance would be futile.[11] The other party's repudiation may itself constitute an intimation that performance will be futile.[12] If the other party intimates that he or she is either unable or unwilling to perform the contract, then often the aggrieved party may reasonably assume that performance of his or her own obligations will not be required unless and until the other party signals a readiness to perform. In such cases, the other party may be estopped from insisting on performance from the aggrieved party.

In *Peter Turnbull & Co Pty Ltd v Mundus Trading Co (Australasia) Pty Ltd*,[13] the buyer agreed to buy a quantity of oats to be loaded on a ship nominated by the buyer in Sydney. The seller subsequently informed the buyer that it could not supply the oats in Sydney but might

4 On anticipatory breach, see Chapter 22.
5 *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17, 48; *Foran v Wight* (1989) 168 CLR 385, 416, 441–2.
6 *Foran v Wight* (1989) 168 CLR 385, 419, 441–2.
7 See *White & Carter (Councils) Ltd v McGregor* [1962] AC 413.
8 *Bowes v Chaleyer* (1923) 32 CLR 159, 168–9, 190, 198; *Fercometal SARL v Mediterranean Shipping Co SA* [1989] 1 AC 788, 805; *Austral Standard Cables Pty Ltd v Walker Nominees Pty Ltd* (1992) 26 NSWLR 524, 532–3; *Murphy v Zamonex Pty Ltd* (1993) 31 NSWLR 439, 454.
9 See *Fercometal SARL v Mediterranean Shipping Co SA* [1989] 1 AC 788.
10 *Foran v Wight* (1989) 168 CLR 385, 396, 420–2, 434, 442, 456.
11 See, eg, *Peter Turnbull & Co Pty Ltd v Mundus Trading Co (Australasia) Pty Ltd* (1954) 90 CLR 235; *Austral Standard Cables Pty Ltd v Walker Nominees Pty Ltd* (1992) 26 NSWLR 524.
12 See *Foran v Wight* (1989) 168 CLR 385.
13 *Peter Turnbull & Co Pty Ltd v Mundus Trading Co (Australasia) Pty Ltd* (1954) 90 CLR 235.

be available to supply them in Melbourne. By this conduct, the seller repudiated the contract. The repudiation was not accepted by the buyer until a later time. The buyer claimed damages from the seller. In defence, the seller argued that prior to terminating the contract the buyer had failed to perform its own contractual obligation of nominating a ship in Sydney. The majority of the High Court held that the seller, by its conduct, had dispensed with the need for the buyer to perform that obligation.[14] Dixon CJ explained that by "persisting that it could not perform the contract according to its terms, the [seller] clearly intimated to the [buyer] that it was useless to pursue the condition of the contract applicable to shipment in Sydney and that the [buyer] need not do so".[15]

In order to be absolved of the consequences of non-performance of his or her obligations under a contract, an aggrieved party must show that he or she was ready and willing to perform those obligations at the time of the other party's breach or repudiation, except possibly in the case of repudiation based on anticipatory breach.[16] As the doctrine is based on estoppel, the aggrieved party must also show that he or she relied on the other party's repudiation as a reason for not tendering performance of his or her obligations.[17] As it is not reasonable to expect the aggrieved party to make expensive preparatory steps to complete when the other party has made it clear that he or she will not be performing, the courts are quite comfortable inferring reliance unless there is evidence to counter the inference.[18]

Where an aggrieved party elects to affirm a contract, the party who has breached or repudiated may, on giving reasonable notice, declare that he or she is willing to perform and requires completion of the contract.[19] The effect of any estoppel protecting the aggrieved party from the consequences of non-performance will then be removed and the aggrieved party will be required to perform his or her obligations under the contract as they fall due.

Consequences of affirmation for the breaching or repudiating party

[24.25] As affirmation keeps the contract alive for the benefit of both parties,[20] a party who has breached or repudiated a contract may be able to rely to his or her advantage on subsequent events. Should an event occur that frustrates the contract, the contract will be terminated without liability on the part of either party.[21] After a contract is frustrated, accrued rights remain in place. This means that the aggrieved party will retain a right to damages for any breach that has occurred. However, since the contract was brought to an end by frustration, the aggrieved party will not be entitled to claim that the breach caused the termination of the contract so as to claim damages for the whole of the loss of the bargain.

14 Dixon CJ, Webb and Kitto JJ, Taylor J dissenting.

15 *Peter Turnbull & Co Pty Ltd v Mundus Trading Co (Australasia) Pty Ltd* (1954) 90 CLR 235, 445–6.

16 See [25.20]. On readiness and willingness, see also [25.10]–[25.25].

17 See *Foran v Wight* (1989) 168 CLR 385, 412, 436; *Austral Standard Cables Pty Ltd v Walker Nominees Pty Ltd* (1992) 26 NSWLR 524, 533, 538.

18 See, eg, *K & K Real Estate Pty Ltd v Adellos Pty Ltd* [2010] NSWCA 302.

19 *Peter Turnbull and Co Pty Ltd v Mundus Trading Co (Australasia) Pty Ltd* (1954) 90 CLR 235, 250; *Foran v Wight* (1989) 168 CLR 385, 396, 420–1, 441–2.

20 *Bowes v Chaleyer* (1923) 32 CLR 159, 197; *Foran v Wight* (1989) 168 CLR 385, 395, 441.

21 See, eg, *Avery v Bowden* (1855) 5 E&B 714; 119 ER 647. On frustration, see Chapter 15.

The fact that an affirmed contract remains on foot also means that a party who has breached or repudiated a contract may himself or herself become entitled to terminate the contract on the ground of subsequent breaches by the aggrieved party.[22] In *Bowes v Chaleyer*,[23] the buyer had ordered goods from the seller. The contract provided for delivery of "Half [the goods] as soon as possible. Half two months later". Before the first parcel of goods had been delivered, the buyer purported to cancel the contract. The seller did not accept this repudiation. When the goods were delivered, the delivery was not in accordance with the contract. The goods had been shipped in three portions in a period shorter than two months. The goods were rejected by the buyer, and the seller claimed damages for breach of contract. The majority of the High Court held that the delivery terms were conditions of the contract, any breach of which entitled the buyer to terminate.[24] Since the seller had elected not to accept the repudiation by the buyer, the seller remained liable to perform his part of the contract. The buyer was accordingly entitled to take advantage of any subsequent default by the seller.[25]

We might ask why the seller could not rely on the qualification, discussed earlier in this chapter, which absolves an aggrieved party of the consequences of failing to perform where the other party has repudiated the contract.[26] The answer may lie in the fact that in *Bowes v Chaleyer*,[27] the seller's breach consisted of a failure to comply with the terms in the contract governing delivery of the goods. There was no suggestion that the seller had been induced to alter his conduct by reason of anything the buyer had said or done.[28] In other words, as the qualification of an aggrieved party's obligation to perform is now explained in terms of estoppel, there was no detrimental reliance by the seller on the buyer's repudiation.

WHERE THE CONTRACT IS TERMINATED

Consequences of terminating for the aggrieved party

Rights that survive termination

[24.30] Termination of a contract brings to an end both parties' future obligations to perform under that contract. However, the contract is not rescinded from the beginning.[29] This means that rights already unconditionally acquired or accrued are not discharged.[30] Examples of rights that may have accrued before a contract is terminated include the right to recover payment for any part of the contract which has been performed[31] and the right to claim damages for

22 *Bowes v Chaleyer* (1923) 32 CLR 159.

23 *Bowes v Chaleyer* (1923) 32 CLR 159 (Isaacs and Rich JJ dissenting).

24 *Bowes v Chaleyer* (1923) 32 CLR 159, 168, 188, 197.

25 *Bowes v Chaleyer* (1923) 32 CLR 159, 169, 190, 198.

26 See [24.20].

27 *Bowes v Chaleyer* (1923) 32 CLR 159.

28 *Bowes v Chaleyer* (1923) 32 CLR 159, 198.

29 On rescission, see Chapter 39.

30 *McDonald v Dennys Lascelles Ltd* (1933) 48 CLR 457, 476–7, also 469–70; *Holland v Wiltshire* (1954) 90 CLR 409, 416.

31 On the action for debt, see Chapter 29.

any breaches occurring up until the time the contract was terminated.[32] Arbitration clauses included in a contract will also remain binding after termination.[33]

Restitution

[24.35] Termination of a contract may also make available to the aggrieved party restitutionary remedies in respect of money paid or goods provided, an issue discussed in Chapter 10.

Alternative grounds for termination

[24.40] An aggrieved party who has purported to terminate a contract on an invalid ground is entitled to rely upon any other valid ground that was in existence at the time of the termination, even though that ground was not, at that time, raised by or even known to the aggrieved party.[34] For example, in *Rawson v Hobbs*,[35] the purchasers had originally purported to rely on a contractual right to terminate. When this ground proved invalid, they were able to rely instead on the vendor's factual inability to perform at the relevant time. The ability of an aggrieved party to rely on alternative grounds for termination may in some cases be limited by estoppel[36] and possibly also relief against forfeiture.[37]

Consequences of termination for the non-performing party

[24.45] As just noted, where a contract is terminated, rights which have accrued prior to termination continue in force and may accordingly be relied upon even by a party who has breached or repudiated the contract. In some cases, restitutionary remedies might also be available, even to the party in breach.[38]

RIGHT TO CURE A BREACH?

[24.50] The common law of contract does not recognise any general right to cure or rectify a breach before an aggrieved party terminates the contract, unless the parties contract expressly for such a result. This position may be contrasted with that under the *United Nations Convention on Contracts for the International Sale of Goods* (CISG)[39] and the *UNIDROIT Principles of International Commercial Contracts 2016* (UPICC)[40] which, in circumstances where there would be no undue prejudice to the interests of the aggrieved party, allow a party in breach to remedy, at his or her own expense, any defect in performance.

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32 On damages, see Chapter 26.

33 *Codelfa Construction Pty Ltd v State Rail Authority of NSW* (1982) 149 CLR 337, 365.

34 *Shepherd v Felt & Textiles of Australia Ltd* (1931) 45 CLR 359, 377–8; *Sunbird Plaza Pty Ltd v Mahoney* (1988) 166 CLR 245, 262, 274-5.

35 *Rawson v Hobbs* (1961) 107 CLR 466.

36 See *Glencore Grain Rotterdam BV v Lebanese Organisation for International Commerce* [1997] 4 All ER 514, 526–31. On estoppel as a restriction on the right to terminate, see [25.110].

37 *Sunbird Plaza Pty Ltd v Maloney* (1988) 166 CLR 245, 262–3. On relief against forfeiture, see [25.125]. See also *Heisler v Anglo-Dal LD* [1954] 1 WLR 1273 and generally *Glencare Grain Rotterdam BV v Lebanese Organisation for International Commerce* [1997] 4 All ER 514, 526–31; Carter, "Panchaud Freres Explained" (1999) 14 *Journal of Contract Law* 239.

38 See Chapter 10.

39 Article 48. On the CISG, see also [1.180].

40 Article 7.1.4. On the UPICC, see also [1.180].

CHAPTER **25**

Restrictions

RESTRICTIONS ON THE RIGHT TO TERMINATE

[25.05] There are a number of restrictions on the right of a party (the *aggrieved party*) to terminate a contract, generally based on the conduct of the aggrieved party. While these restrictions prevent the aggrieved party from terminating the contract, generally they do not preclude his or her right to claim damages for any breaches of the contract that have occurred.[1] This chapter deals primarily with those restrictions on the right to terminate imposed by the common law and equity. The parties may themselves impose restrictions through the contract terms, and some statutes also impose restrictions on the right to terminate. In this chapter, statutory restrictions are only discussed in relation to unconscionable conduct.

The restrictions discussed in this chapter apply primarily to rights to terminate conferred by the general law.[2] The restrictions – other than the requirement of readiness and willingness[3]

1 But see discussion of anticipatory breach in Chapter 22.
2 See Chapters 21–23.
3 *Lantry v Tomule Pty Ltd* [2007] NSWSC 81, [76]–[78].

and, it would seem, relief against forfeiture[4] – also apply to a right to terminate for non-fulfilment of a contingent condition.[5]

READINESS AND WILLINGNESS

Common law right to terminate

[25.10] At common law, to be entitled to terminate a contract for actual breach (whether that be breach of an essential term, serious breach of an intermediate term or breach of an inessential term that amounts to repudiation),[6] an aggrieved party must show that he or she was ready – that is, able – and willing to perform the contract. If the aggrieved party was not ready and willing to perform, then the aggrieved party was also at fault. He or she should not, therefore, be entitled to take advantage of the other party's breach or repudiation merely because it came first in time.[7] In this sense, the requirement of readiness and willingness is really a prerequisite of a right to terminate, rather than a restriction on the exercise of that right.

Contractual right to terminate

[25.12] The requirement that a terminating party be ready and willing to perform the contract has been held to be confined to termination at common law and not to extend to termination under an express contractual provision. Although the requirement is sometimes said to extend to contractual rights to terminate, in *Allphones Retail Pty Ltd v Hoy Mobile Pty Ltd*,[8] Perram J reviewed the caselaw and the literature and could find no convincing support for such a rule, either in principle or authority. Perram J observed that: "As a general principle, where a contract is terminated in reliance on such a contractual right, the parties' rights are primarily defined by the contract and not by the general law." In that case, Allphones purported to terminate its franchise agreement with Hoy Mobile when Hoy Mobile fraudulently sold "unlocked" mobile phones in breach of the franchise agreement. Clause 9.3 of that agreement gave Allphones the right to terminate the agreement if, inter alia, Hoy Mobile was fraudulent in connection with the operation of the franchise business. Hoy Mobile argued that Allphones could not exercise the express right to terminate because Allphones had itself repudiated the contract by fraudulently failing to pass on certain commissions to Hoy Mobile. The Full Court held that Allphones could terminate the contract pursuant to an express termination clause even though it had itself repudiated the contract.

Actual breach

[25.15] To be entitled to terminate a contract for an actual breach by the other party, an aggrieved party must show that he or she was ready and willing to perform his or her own obligations at the time of the breach.[9] The fact that the party who wishes to terminate has

4 See [25.125].
5 See Chapter 20.
6 See Chapter 21.
7 See *Foran v Wight* (1989) 168 CLR 385, 423. See also [24.20].
8 *Allphones Retail Pty Ltd v Hoy Mobile Pty Ltd* [2009] FCAFC 85; (2009) 178 FCR 57, [55]–[76] (Perram J, with whom Goldberg and Jacobson JJ agreed).
9 *Foran v Wight* (1989) 168 CLR 385.

himself or herself breached the contract does not generally prevent that party from terminating. There are two views as to what kind of breach will preclude termination by the party in breach. One view is that a party who is in breach of *any essential term* will not be considered ready and willing to perform and will be precluded from terminating.[10] The second view, which would appear to have stronger support, is that a party who is in breach even of an essential term can nevertheless terminate, provided the obligations breached by the two parties are *not interdependent*, and the breach by the party who wishes to terminate has *not caused the other party's breach*.[11] In *Sharjade Pty Ltd v Commonwealth*, Hodgson JA said that:

> In the absence of such interdependence or a proved causal link, the circumstance that a party is itself in breach does not generally disentitle it to rely on the other party's breach of contract, if that breach would otherwise entitle the former to terminate … Even if the terminating party's breach were itself sufficient to justify termination, in my opinion the better view is that this would not of itself preclude termination by that party, so long as the terms breached were independent and the causal link referred to earlier was not established …[12]

Where the parties' obligations are concurrent and interdependent – which means that the contract requires the parties to perform at the same time, each in exchange for the other – the aggrieved party must generally[13] have tendered (ie, offered) performance of his or her own obligations to the other party before terminating for breach by the other party.[14] This is classically the case in a contract for the sale of land. For example, if a purchaser fails to complete a contract for the sale of land, the vendor must, in order to be entitled to terminate, show that he or she tendered performance of his or her obligation to convey title. If the vendor has not tendered performance, then the purchaser has committed no breach. However, the vendor need only be ready and willing to perform the concurrent and interdependent obligation. In *Chandos Developments Pty Ltd v Mulkearns*,[15] the vendor was obliged to maintain the property in good repair. Even though the vendor had not complied with this obligation, the New South Wales Court of Appeal held that the vendor was entitled to terminate the contract in response to the purchaser's failure to complete the transaction. The purchaser's promise to complete was dependent upon the vendor's ability to convey good title. As the vendor was able to do so, it was entitled to terminate the contract. In the event that the vendor did not undertake the maintenance work required under the contract, damages could be awarded to the purchaser.

Anticipatory breach

Where the repudiation is accepted

[25.20] There is some uncertainty as to whether an aggrieved party who seeks to terminate a contract on the basis of repudiation by the other party prior to the time set for

10 *Rona v Shimden Pty Ltd* [2005] NSWSC 818, [92]; *Lantry v Tomule Pty Ltd* [2007] NSWSC 81, [81].

11 *Sharjade Pty Ltd v Commonwealth* [2009] NSWCA 373, [54] (Hodgson JA), supported by obiter dicta in *Roadshow Entertainment Pty Ltd v (ACN 053006269) Pty Ltd (rec & man appt)* (1997) 42 NSWLR 462, 479–80; *State Trading Corporation of India Ltd v M Golodetz Ltd* [1989] 2 Lloyd's Rep 277, 286. See also O'Brien, "Breach Ordinarily No Bar to Termination" (2014) 88 *Australian Law Journal* 38 and *Sharjade Pty Ltd v Commonwealth* [2009] NSWCA 373, [163]–[174] (Sackville AJA).

12 *Sharjade Pty Ltd v Commonwealth* [2009] NSWCA 373, [57] (Hodgson JA).

13 Unless the other party has already repudiated the contract and thereby intimated that it would be futile to attempt to perform: see *Foran v Wight* (1989) 168 CLR 385, 410, 427, 433, 442, 456, discussed at [25.25].

14 *Mahoney v Lindsay* (1980) 33 ALR 601.

15 *Chandos Developments Pty Ltd v Mulkearns* [2008] NSWCA 62.

performance (ie, on the basis of an anticipatory breach)[16] needs to show that he or she was ready and willing to perform his or her own obligations under the contract at the time of the repudiation.

In *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (*DTR Nominees*), Stephen, Mason and Jacobs JJ stated that "[a] party in order to be entitled to rescind for anticipatory breach must at the time of the rescission himself be willing to perform the contract on its proper interpretation",[17] although that was said in the context of a misinterpretation of the contract by the party seeking to terminate. The Court was focused on the party's willingness to perform the contract "according to its proper interpretation" and not on the notion of a general bar on termination for a party in breach. The passage from *DTR Nominees* was cited with approval by Dawson J in *Foran v Wight*,[18] and similar statements of general principle were made by Mason CJ and Brennan J.[19] In the same case, however, Deane J rejected such a requirement. His Honour believed that such a requirement is "unjustified by principle or commonsense"[20] and would require "useless and futile expenditure by an innocent party".[21]

In *Sharjade Pty Ltd v Commonwealth*,[22] Hodgson JA found that the views expressed in *Foran v Wight* and *DTR Nominees* were obiter and that, as a matter of principle, Deane J's view in *Foran v Wight* was preferable.[23] Hodgson JA found that an anticipatory breach that amounts to repudiation should justify termination by the aggrieved party whether or not the aggrieved party was itself ready and willing to perform. According to Hodgson JA, in such circumstances, the aggrieved party need only establish that he or she was ready and willing to perform the contract if he or she seeks damages.[24] Young JA[25] and Sackville AJA[26] agreed in principle with Hodgson JA's view but decided the case on a more traditional basis. They found that as the aggrieved party had only breached a non-essential term, the aggrieved party was entitled to terminate the contract.[27]

In *Almond Investors Ltd v Kualitree Nursery Pty Ltd*,[28] Bathurst CJ (with whom Giles JA and Handley AJA agreed) said:

> It is important in my opinion that the passage from the judgment of Stephen, Mason and Jacobs JJ in *DTR Nominees* did not say that a party in breach of a non-essential term was not entitled to terminate for anticipatory breach. Rather they stated the party must have been willing to perform the contract according to its proper interpretation. It is not inconsistent with such

16 Repudiation is sometimes referred to as renunciation (see [22.05]). The discussion in this chapter employs the phrase repudiation.

17 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423, 433.

18 *Foran v Wight* (1989) 168 CLR 385, 452.

19 *Foran v Wight* (1989) 168 CLR 385, 408 (Mason CJ), 427 (Brennan J).

20 *Foran v Wight* (1989) 168 CLR 385, 437.

21 *Foran v Wight* (1989) 168 CLR 385, 437.

22 *Sharjade Pty Ltd v Commonwealth* [2009] NSWCA 373.

23 *Sharjade Pty Ltd v Commonwealth* [2009] NSWCA 373, [62]–[68]. Hodgson JA expressed a similar view in *Macquarie International Health Clinic Pty Ltd v Sydney South West Area Health Service* [2010] NSWCA 268, [162].

24 *Sharjade Pty Ltd v Commonwealth* [2009] NSWCA 373, [68]. See also [27.145].

25 *Sharjade Pty Ltd v Commonwealth* [2009] NSWCA 373, [145], [156].

26 *Sharjade Pty Ltd v Commonwealth* [2009] NSWCA 373, [163].

27 See [25.15].

28 *Almond Investors Ltd v Kualitree Nursery Pty Ltd* [2011] NSWCA 198.

> willingness that there is a failure to perform a non-essential term when the other contracting party is either incapable or refusing to perform the contract according to its terms.[29]

Even those judges who view readiness and willingness as a prerequisite to the right to terminate for anticipatory breach amounting to repudiation are mindful of Deane J's concerns about requiring the aggrieved party to undertake unnecessary expenditure. Courts have held that the test of readiness and willingness in the case of an anticipatory breach is less stringent than for actual breach. An aggrieved party will generally be able to satisfy the requirement by showing that, at the time of the other party's repudiation, he or she was not substantially disabled or incapacitated from performing at the time set for performance.[30] In *Rawson v Hobbs*, Dixon CJ explained that "[o]ne must be very careful to see that nothing but a substantial incapacity or definitive resolve or decision against doing in the future what the contract requires is counted as an absence of readiness and willingness".[31]

For example, if a seller seeks to terminate a contract for the sale of goods for repudiation by the buyer occurring before the time set for performance of the contract, the seller must show that he or she was not substantially disabled from delivering the goods to the buyer. The seller might do this by showing that, at the time of the repudiation, he or she already had the goods or was in a position to have manufactured or obtained the goods by the time set for performance of the contract.

A recent example of a case in which a party was unable to terminate because it was not itself ready and willing to perform its own interdependent obligations was *Upside Property Group Pty Ltd v Tekin*.[32] A purchaser of commercial property purported to terminate the contract on the basis of the vendor's repudiation, but evidence of the purchaser's capacity to obtain finance to complete the purchase was "vague, entirely lacking in detail, and not supported by any testimony from the suggested source of finance". The purchaser needed to show that, at the time of termination, it "was not substantially incapacitated from completing" or that it had "a reasonable prospect" of raising the funds.[33] The evidence was insufficient to establish that.

Where the contract is not terminated

[25.25] An aggrieved party who chooses not to terminate a contract in response to an anticipatory breach may not be required to perform those of his or her obligations that fall due after the repudiation.[34] The party who has repudiated may, by the repudiation, be taken to have intimated that it is useless for the aggrieved party to perform.[35] If the aggrieved party later seeks to terminate the contract for an actual breach, the aggrieved party may not be required to show that he or she was ready and willing to perform at the time the contract was terminated. The aggrieved party will usually only be required to show that he or she

29 *Almond Investors Ltd v Kualitree Nursery Pty Ltd* [2011] NSWCA 198, [77].

30 *Foran v Wight* (1989) 168 CLR 385, 408, 425, 453.

31 Rawson v Hobbs (1961) 107 CLR 466, 481.

32 *Upside Property Group Pty Ltd v Tekin* [2017] NSWCA 336.

33 *Upside Property Group Pty Ltd v Tekin* [2017] NSWCA 336, [34].

34 *Peter Turnbull & Co Pty Ltd v Mundus Trading Co (Australasia) Pty Ltd* (1954) 90 CLR 235. See also discussion of this principle at [24.20].

35 *Foran v Wight* (1989) 168 CLR 385, 396, 417, 433, 451, 456.

was willing and ready to perform at the time of the anticipatory breach and, moreover, was ready and willing in the sense, as discussed above, of not being substantially disabled or incapacitated from performing.[36]

These concessions to an aggrieved party were explained by the High Court in *Foran v Wight*[37] as being based on the doctrine of estoppel. A party may be estopped by his or her repudiation from insisting on performance, or even actual readiness and willingness to perform, at the time set for performance by the aggrieved party. As the doctrine is based on estoppel, the aggrieved party must demonstrate detrimental reliance on an assumption induced by the repudiating party. This means the aggrieved party must show that his or her failure to tender performance or to be ready and willing to perform was due to his or her reliance on the repudiating party's intimation that performance of the contract would be futile, rather than some other factor.[38]

The leading Australian authority on these issues is *Foran v Wight*.[39] The case involved a contract for the sale of land. The sale was due to be completed on 22 June 1983 and time was specified as being of the essence in this respect. On 20 June, the vendors' solicitor advised the purchasers' solicitor that the vendors would not be able to settle – that is, complete the contract – on 22 June because the vendors had not been able to complete registration of a right of way required by the contract. At this time, the purchasers would have had a right to terminate for anticipatory breach because the vendors had indicated that they would not comply with an essential term of the contract. However, the purchasers chose not to terminate. On 22 June, neither party attempted to settle. On 24 June, the purchasers purported to terminate the contract and claimed return of their deposit.[40] The purchasers were now relying on an actual breach of the contract as giving rise to the right to terminate. The vendors contended that the purported termination was invalid because on that date the purchasers did not have the funds available for completion and therefore were themselves not ready and willing to complete. The trial judge found that the purchasers had not proved their ability to perform.

The majority of the justices of the High Court held that the purchasers had validly terminated the contract and were entitled to the return of their deposit. Their Honours' reasons for reaching this decision differed. Brennan, Deane and Dawson JJ found that, at the time of the repudiation, the purchasers were not "substantially incapable" of raising the needed finance.[41] Brennan J explained that:

> The purchasers were undoubtedly encountering grave difficulties in raising the finance they needed – on 20 June they were perhaps $10,000 short of the amount needed to complete – but their difficulties were not so grave that in their view it was futile to continue the effort.[42]

36 See *Foran v Wight* (1989) 168 CLR 385.

37 *Foran v Wight* (1989) 168 CLR 385, 410–12, 420–2, 434–6, 442, 450, 454, 456. See also *Austral Standard Cable Pty Ltd v Walker Nominees Pty Ltd* (1992) 26 NSWLR 524, 533.

38 See *Foran v Wight* (1989) 168 CLR 385, 412, 436; *Austral Standard Cables Pty Ltd v Walker Nominees Pty Ltd* (1992) 26 NSWLR 524, 533, 538. See also [24.20].

39 See also Carter, "Foran v Wight" (1990) 3 *Journal of Contract Law* 70.

40 On the role of a deposit, see [29.50].

41 *Foran v Wight* (1989) 168 CLR 385, 431, 436, 454.

42 *Foran v Wight* (1989) 168 CLR 385, 431.

The majority accepted that the purchasers had relied on the vendors' intimation that they would not perform by giving up the chance of obtaining finance.[43] Deane J explained that it was:

> clear from the evidence that there was, at the least, a real chance that, if they had not been induced to cease their efforts to arrange finance by the vendor's intimation, the purchasers would have been able to obtain the balance of … the purchase price.[44]

Having satisfied the requirement of being ready and willing to perform at the time of the vendors' repudiation, the purchasers were entitled to terminate the contract. Brennan, Deane and Dawson JJ held that the purchasers were therefore also entitled to recover their deposit.[45] Gaudron J reached a similar conclusion but by relying on waiver.[46]

While agreeing that the purchasers could rely on estoppel, Deane J also took the view that to be entitled merely to terminate the contract – as opposed to claiming damages – an aggrieved party should not need to show that he or she would have been able to perform.[47] Deane J said:

> It is difficult to see why, as a matter of principle or common sense, actual breach or even repudiation by one party to a contract should prevent that party from rescinding the contract by accepting a repudiation of the contract by the other party. Put differently, it is difficult to see why the law should insist that, even though both parties to a contract have repudiated it, the contract must hang like an albatross around their necks unless and until they can reach a new agreement about its termination.[48]

Mason CJ dissented on the basis that the purchasers had failed to show that they had acted to their detriment in reliance on the vendors' intimation that they were unable to complete on the appointed day.[49] Mason CJ held that the purchasers had not shown that, had they not relied on the intimation, they would have been in a financial position to tender performance on the appointed date. Mason CJ did accept, however, that "when the defendant has dispensed with performance by the plaintiff of a mutually dependent and concurrent obligation, it remains for the plaintiff to show not that he was ready and willing to perform, but that he would have been ready and willing to perform had the defendant not dispensed with performance".[50]

Claims for damages

[25.30] The majority of the justices of the High Court in *Foran v Wight* held that different rules apply if an aggrieved party wants not merely to terminate a contract but also to claim damages for loss of the bargain following termination. As just discussed, it is unclear whether in order to be entitled to terminate in response to a repudiation occurring before the time set for performance, an aggrieved party must show that he or she was ready and willing to perform the contract. In *Foran v Wight*,[51] the majority held that to claim damages for the loss

43 *Foran v Wight* (1989) 168 CLR 385, 431, 436, 454.
44 *Foran v Wight* (1989) 168 CLR 385, 436.
45 *Foran v Wight* (1989) 168 CLR 385, 431, 438, 455.
46 *Foran v Wight* (1989) 168 CLR 385, 459.
47 *Foran v Wight* (1989) 168 CLR 385, 437.
48 *Foran v Wight* (1989) 168 CLR 385, 437–8.
49 *Foran v Wight* (1989) 168 CLR 385, 412–13.
50 *Foran v Wight* (1989) 168 CLR 385, 403.
51 (1989) 168 CLR 385, 430–1, 438–9, 454–5.

of the benefit of a contract in such a case, an aggrieved party must establish his or her loss on the balance of probabilities. This means the aggrieved party must show on the balance of probabilities that, but for the repudiating conduct, he or she would have been ready and willing to perform the contract at the stipulated time.

ELECTION

Election as a restriction on termination

[25.35] An aggrieved party faced with an event that entitles him or her to terminate the contract has a choice between terminating and continuing with, or *affirming*, the contract. The doctrine of *election* refers to this choice between alternative rights (in this context, the right to terminate a contract for breach and the alternative right to affirm the contract).[52] The choices are alternatives because, once made, an election is generally final and cannot be retracted.[53] Thus, an aggrieved party who terminates a contract loses the right to further performance. Conversely, an aggrieved party who affirms a contract loses the right to terminate in respect of the event that gave rise to the right to terminate. This aspect of election constitutes a restriction on the right to terminate. The restriction is, however, subject to two qualifications.

Further breaches

[25.40] An aggrieved party who has affirmed a contract following a particular event giving rise to a right to terminate will not generally be prevented from terminating the contract in response to a further event giving rise to a right to terminate.[54] Similarly, an aggrieved party who chooses not to terminate a contract in response to an anticipatory breach does not lose the right to terminate for actual breach. If the repudiating party still is not able or willing to perform at the time set for performance, the aggrieved party will gain a new right to terminate the contract.[55]

Continuing breach

[25.45] An aggrieved party's decision to affirm a contract following a breach giving rise to a right to terminate will not preclude him or her from terminating in response to that breach at a later time if the breach can be classified as a *continuing* breach, as opposed to a *once and for all* breach. The distinction between a once and for all breach and a continuing breach was explained by Dixon J in *Larking v Great Western (Nepean) Gravel Ltd (in liq)*[56] as depending on the nature of the term in question. Dixon J explained that there will be a once and for all breach where a party has undertaken to do a "definite act and omits to do it within the time allowed for the purpose". In such a case, the party "has broken his covenant finally and his continued failure to do the act is nothing but a failure to remedy his past breach, not the commission of any further breach of his covenant".[57] If an aggrieved party affirms the

52 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 656.

53 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 656.

54 *Tropical Traders Ltd v Goonan* (1964) 111 CLR 41.

55 See the discussion of anticipatory breach in Chapter 22.

56 *Larking v Great Western (Nepean) Gravel Ltd (in liq)* (1940) 64 CLR 221, 236.

57 *Larking v Great Western (Nepean) Gravel Ltd (in liq)* (1940) 64 CLR 221, 236.

contract following a once and for all breach, he or she will have lost the right to terminate in respect of that breach.

In *Larking v Great Western (Nepean) Gravel Ltd (in liq)*, Larking had granted a licence to Great Western to remove sand and gravel from a riverbed adjoining Larking's land. In return, Great Western promised to pay Larking certain royalties. The contract required Great Western to erect fences and a gate. This was not done. Over a period of more than two years, Larking made numerous complaints and eventually wrote to Great Western demanding that the fence and gate be erected within 14 days. Great Western did not comply. Larking subsequently accepted a payment of royalties from Great Western. The High Court of Australia considered that the erection of the fences and gate was a definite act to be done within a reasonable time. Great Western's failure to perform this obligation gave rise to a breach once and for all.[58] In allowing the contract to continue and in accepting royalties for the period, it was held that Larking had affirmed the contract and lost the right to terminate.[59]

A continuing breach will occur where a party has promised to "maintain a state or condition of affairs" and fails to do so.[60] Examples of such obligations include "maintaining a building in repair, keeping the insurance of a life on foot, or affording a particular kind of lateral or vertical support to a tenement".[61] In the case of a continuing breach, a further breach arises "in every successive moment of time during which the state or condition is not as promised".[62] Accordingly, despite having initially affirmed the breach, an aggrieved party will retain a right to terminate if the breach continues.

In *Galafassi v Kelly*,[63] the New South Wales Court of Appeal found that the same principles apply to continuing acts that amount to repudiation. The appellants purchased a house from the respondents. The appellants were unable to sell their own home and, as a result, were unable to complete the contract of sale. On several occasions, the appellants told the respondents of this inability. Although these statements clearly amounted to repudiation of the contract by the appellants, the respondent elected to affirm the contract and (originally) sued for an order of specific performance. Despite having affirmed the appellant's repudiatory conduct, the respondent nevertheless had a right to terminate for breach and sue for damages (its ultimate claim). The appellants' statements of its inability to complete were unretracted representations of existing fact, each of which "was a continuing representation unless and until it was withdrawn".[64] The repudiatory conduct was thus continuing which in turn gave the respondents a right to terminate that continued until the repudiatory representations were withdrawn.

Requirements of election

[25.50] There are two requirements for an election to affirm a contract. These are, first, knowledge of at least the facts giving rise to the right to terminate and, secondly, unequivocal conduct consistent only with a choice to continue with the contract.

58 *Larking v Great Western (Nepean) Gravel Ltd (in liq)* (1940) 64 CLR 221, 228, 231, 239.

59 *Larking v Great Western (Nepean) Gravel Ltd (in liq)* (1940) 64 CLR 221, 229, 231, 240.

60 *Larking v Great Western (Nepean) Gravel Ltd (in liq)* (1940) 64 CLR 221, 236.

61 *Larking v Great Western (Nepean) Gravel Ltd (in liq)* (1940) 64 CLR 221, 236.

62 *Larking v Great Western (Nepean) Gravel Ltd (in liq)* (1940) 64 CLR 221, 236.

63 *Galafassi v Kelly* [2014] NSWCA 190; (2014) 87 NSWLR 119. See also *K&K Real Estate v Adellos Pty Ltd* [2010] NSWCA 302, [135] and *Qin v Smith (No 2)* [2013] VSC 476, [70].

64 *Galafassi v Kelly* [2014] NSWCA 190; (2014) 87 NSWLR 119, [66].

Knowledge

[25.55] The doctrine of election involves a choice between inconsistent rights. In order to make a choice, the aggrieved party must have some knowledge in respect to the right to terminate.[65] However, the precise type of knowledge needed for an aggrieved party to affirm a contract is not settled.[66] Is it simply knowledge of the facts that give rise to the legal right to terminate or is it knowledge of the facts and also awareness that those facts confer a legal right to terminate?

In *Sargent v ASL Developments Ltd*,[67] the majority of the High Court considered that where the right to terminate was conferred by the contract itself, knowledge of the facts giving rise to the right to terminate would be sufficient.[68] Stephen J explained that where the contract itself conferred the right to elect to terminate, "there can be no question whether a party had knowledge of his choice of rights. He is deemed to know the terms of his own contract and the rights it confers".[69] Stephen J left open the question of what sort of knowledge should be required where the right to terminate was conferred by law.[70] By contrast, Mason J said that however the right to terminate arose, knowledge only of the existence of the facts giving rise to the right to terminate would be sufficient for the aggrieved party to make a binding election.[71]

The aggrieved party may gain the requisite knowledge in a variety of ways including by undertaking due diligence. In *Savoy Investments (Qld) Pty Ltd v Global Nominees Pty Ltd*,[72] the property in question was sold subject to a lease, and Special Condition 3 of the contract of sale obliged Global Nominees (the vendor) to secure a personal guarantee from the lessee's directors. Savoy Investments (the purchaser) undertook due diligence and, through this process, became aware that no guarantee arrangements had been put in place. Nevertheless, it paid the balance of the deposit to Global Nominees. When Savoy Investments sought a declaration that it was entitled to terminate a contract because of Global Nominees' failure to secure the relevant guarantee, Global Nominees argued that Savoy Investment's had affirmed the contract. The Court of Appeal of the Supreme Court of Queensland held that Savoy Nominees had affirmed the contract by failing to terminate for breach of Special Condition 3 when it became aware of that breach as a result of its due diligence enquiries.[73]

Conduct

[25.60] An election will be found in any unequivocal communication or conduct that conveys the aggrieved party's choice either to affirm or to terminate the contract. The conduct must be "unequivocal in the sense that it is consistent only with the exercise of one of the two sets of rights and inconsistent with other".[74] It is not necessary to show that the aggrieved party

65 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 642.

66 Compare the question of knowledge in relation to the right of rescission: [39.60].

67 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634 (Stephen J, with whom McTiernan ACJ agreed).

68 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 644–5; see also *Khoury v Government Insurance Office of New South Wales* (1984) 165 CLR 622, 634.

69 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 645.

70 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 644–5.

71 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 658.

72 *Savoy Investments (Qld) Pty Ltd v Global Nominees Pty Ltd* [2008] QCA 282.

73 *Savoy Investments (Qld) Pty Ltd v Global Nominees Pty Ltd* [2008] QCA 282, [29].

74 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 646; see also *Immer (No 145) Pty Ltd v Uniting Church in Australia Property Trust (NSW)* (1993) 182 CLR 26, 30–2, 43.

formed an actual, subjective intention to elect. Rather, "an election is the effect which the law attributes to conduct justifiable only if such an election had been made".[75] What type of conduct will amount to an unequivocal election to affirm will depend on the circumstances of the case. Some examples are set out in the following text.

Accepting or encouraging performance

[25.65] An aggrieved party may be found to have affirmed a contract where, following the event giving rise to a right to terminate, the aggrieved party accepts or insists upon receiving performance from the other party to the contract.[76] For example, in *Idameneo (No 123) Pty Ltd v Ticco Pty Ltd*,[77] continued acceptance of the services provided by the respondent doctor meant that the appellant could not establish that it had accepted the doctor's alleged repudiation.[78] Requesting a reduction in the contract price on the basis of the other party's breach may also be viewed as an irrevocable election to affirm the contract.[79]

Acts contemplated under the contract

[25.70] An aggrieved party may be found to have affirmed a contract where he or she continues to perform acts contemplated by the contract. In *Sargent v ASL Developments Ltd*,[80] the parties had entered into a contract for the sale of land. The contract contained a contingent condition of performance, which provided that either party would have the right to terminate the contract should it be established that the land was subject to town planning controls otherwise than as stated in the contract.[81] The vendor sought to terminate the contract in reliance on this provision some 32 months after entering into the contract. During this time, the vendor had performed a number of acts in connection with the contract, including receiving from the purchaser quarterly payments due under the contract, calling on the purchaser to pay rates and joining with the purchaser in seeking to have the land brought under the provisions of the *Real Property Act 1900* (NSW). The High Court held that this conduct constituted an election to continue with the contract, which prevented the vendor from terminating. The vendor's acts were consistent only with the contract continuing on foot.[82] However, continuing performance of the contract will not constitute affirmation of the contract where the party has asserted his or her right to terminate and has continued performance subject to the preservation of that right.[83]

Delay in exercising the right to terminate

[25.75] An aggrieved party confronted with the choice of terminating or affirming a contract is not required to elect immediately.[84] An aggrieved party is entitled to a reasonable time to

75 *Sargent v ASL Developments Pty Ltd* (1974) 131 CLR 634, 646.
76 See, eg, *Carr v J A Berriman Pty Ltd* (1953) 89 CLR 327.
77 *Idameneo (No 123) Pty Ltd v Ticco Pty Ltd* [2004] NSWCA 329.
78 *Idameneo (No 123) Pty Ltd v Ticco Pty Ltd* [2004] NSWCA 329, [99].
79 *Liberty Grove (Concord) Pty Ltd v Yeo* [2006] NSWSC 1373.
80 *Sargent v ASL Developments Pty Ltd* (1974) 131 CLR 634.
81 See Chapter 20.
82 *Sargent v ASL Developments Pty Ltd* (1974) 131 CLR 634, 650, 659.
83 *Wallace-Smith v Thiess Infraco (Swanston) Pty Ltd* [2005] FCAFC 49, [89].
84 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 656.

consider his or her position, provided he or she does not otherwise affirm the contract or cause prejudice to the other party.[85] An aggrieved party may be taken to have affirmed the contract if the choice is not made within a reasonable time.[86] What amounts to a reasonable time depends on the circumstances of the case and the acts done during the period of delay.[87]

Extensions of time

[25.80] An aggrieved party may sometimes grant a party in breach an extension of time in which to perform the obligation in question. A mere extension of time is unlikely to amount to affirmation of the contract. In *Tropical Traders Ltd v Goonan*,[88] a contract for the sale of land provided that the purchase price was to be paid by a deposit, followed by four sums at 12-monthly intervals, and then the balance of the price five years from the date of the agreement. The contract provided that time should be of the essence of the contract in all respects. The purchasers were late in paying the first three instalments but made the fourth payment early. The purchasers then sought an extension of time to pay the final sum. The vendor agreed to grant the extension but specified that this extension "must be regarded as an act of grace on the part of the [vendor] and without prejudice to and in no way varying the [vendor's] right to the strict enforcement of the contract".[89]

Having not received the required payment on the date specified in the extension, the vendor gave notice terminating the contract and sought a declaration that the contract had been validly terminated. The purchasers counterclaimed for specific performance. They argued, among other things, that by voluntarily accepting late payments for the first three instalments, the vendor lost the right to terminate for late payment of the final sum. Such conduct had dispensed with the stipulation that time was of the essence under the contract. The argument was rejected.

The High Court found that the vendor had validly terminated the contract. Each acceptance by the vendor of a late payment operated as an election not to terminate the contract for non-payment of the particular instalment on the due date. However, that conduct was not sufficient to indicate that time was not of the essence in the future. In the circumstances of the case, a few days' grace in relation to the earlier payments did not mean the requirement that time was to be of the essence should be abandoned in respect of the final payment.[90] Nor did the extension of time in which to make the final payment assist the purchasers' case. The extension expressly preserved the vendor's rights and announced an intention to refrain from electing either way until the new specified date arrived.[91]

What would have been the result in *Tropical Traders Ltd v Goonan* if the extension of time had not expressly preserved the vendor's rights? Arguably, the vendor would still not have affirmed the contract. By specifying a new date for performance, the vendor was indicating that it still expected the purchasers to perform within a particular period of time.

85 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 641, 656; *Immer (No 145) Pty Ltd v Uniting Church in Australia Property Trust (NSW)* (1993) 182 CLR 26, 30–2.

86 *Champtaloup v Thomas* [1976] 2 NSWLR 264, 273; *Mardorf Peach & Co Ltd v Attica Sea Carriers Corporation of Liberia* [1977] AC 850, 856.

87 *O'Connor v SP Bray Ltd* (1936) 36 SR (NSW) 248, 261–2.

88 *Tropical Traders Ltd v Goonan* (1964) 111 CLR 41.

89 *Tropical Traders Ltd v Goonan* (1964) 111 CLR 41, 44.

90 *Tropical Traders Ltd v Goonan* (1964) 111 CLR 41, 52.

91 *Tropical Traders Ltd v Goonan* (1964) 111 CLR 41, 53–5.

Where the date for performance passes without an extension being sought and the innocent party elects to affirm the contract, the contract must be performed within a reasonable time. However, time will no longer be of the essence and, in order to terminate, it may be necessary to make time of the essence by giving reasonable notice to the other party.[92]

Claim for specific performance

[25.85] Where the aggrieved party responds to the breaching party's purported termination by seeking an order of specific performance, the aggrieved party is likely to be viewed as having elected to affirm the contract.[93] However, it must be remembered that if the breach is continuing[94] and is not remedied, the aggrieved party will not be precluded from later rescinding the contract even if the aggrieved party's initial response to the breach was to seek an order for specific performance.[95]

Failure to perform

[25.90] An aggrieved party may be found to have elected to terminate a contract where, following an event giving the aggrieved party the right to terminate, the aggrieved party fails to perform his or her own obligations under the contract.[96] In *Vitol SA v Norelf Ltd*,[97] Lord Steyn explained that:

> One cannot generalise on the point. It all depends on the particular contractual relationship and the particular circumstances of the case. But I am satisfied that a failure to perform may sometimes signify to a repudiating party an election by the aggrieved party to treat the contract as at an end. … [An] example may be an overseas sale providing for shipment on a named ship in a given month. The seller is obliged to obtain an export licence. The buyer repudiates the contract before loading starts. To the knowledge of the buyer the seller does not apply for an export license with the result that the transaction cannot proceed. In such circumstances it may well be that an ordinary businessman, circumstanced as the parties were, would conclude that the seller was treating the contract as at an end.[98]

Acts which prevent performance

[25.95] An election to terminate a contract may be constituted by any act which puts it out of the power of an aggrieved party to perform a contract. For example, in *Holland v Wiltshire*,[99] the purchaser repudiated a contract for the sale of land. The High Court considered that the vendor's subsequent sale of the land to another party amounted to an acceptance of the purchasers' repudiation.

Conduct must be unequivocal

[25.100] In deciding whether or not an aggrieved party has made an election, the most important consideration will be whether or not the conduct was unequivocal. Accordingly,

92 *Highmist Pty Ltd v Tricare Ltd* [2005] QCA 357, [49].

93 *Park v Brothers* [2005] HCA 73, [40]; *Highmist Pty Ltd v Tricare Ltd* [2005] QCA 357, [44].

94 See [25.45].

95 *Ogle v Comboyuro Investments Pty Ltd* (1976) 136 CLR 444, 457–9; *Galafassi v Kelly* [2014] NSWCA 190; (2014) 87 NSWLR 119, [85]–[90].

96 See further Carter, "'Acceptance' of a Repudiation" (1994) 7 *Journal of Contract Law* 156.

97 *Vitol SA v Norelf Ltd* [1996] AC 800.

98 *Vitol SA v Norelf Ltd* [1996] AC 800, 811–2.

99 *Holland v Wiltshire* (1954) 90 CLR 409.

explanations for the aggrieved party's course of conduct which are not consistent with an election must always be considered.

In *Immer (No 145) Pty Ltd v The Uniting Church in Australia Property Trust (NSW)*,[100] the contract was for the transfer of excess airspace rights. Under Sydney town planning codes, buildings were restricted to a maximum floor space ratio. However, where a historic building could not utilise its full ratio, the unused airspace could be transferred to another site, so enabling that site to bear a higher building. Under the terms of the contract, the purchaser was entitled to terminate the contract should council approval of the transfer not be received by a specified date. The council approval was conditional upon refurbishment of the historic building in question. The refurbishment was not completed by the specified date, and approval for the transfer was accordingly not given.

Some time after the specified date, the purchaser sent the documents for settlement to the vendor, including a draft deed of assignment. The deed recited that the council had given approval for the transfer. The documents were sent in the mistaken belief that this was the case. The purchaser then realised that the approval had in fact not been given and notified the vendor that it was terminating the contract. The vendor sought specific performance, arguing that the purchaser had by its conduct and the passage of time affirmed the agreement.

The vendor's argument was rejected by the High Court of Australia. In a joint judgment, Deane, Toohey, Gaudron and McHugh JJ considered that the case did not turn on the issue of the purchaser's knowledge. The purchaser, although originally mistaken as to whether or not the council had subsequently approved the transfer, was aware of the relevant fact giving rise to the right to terminate, namely that approval had not been granted by the council for the transfer by the date specified in the contract.[101]

For Deane, Toohey, Gaudron and McHugh JJ, the issue was whether or not the purchaser had been faced with the need to elect between different courses of action. Their Honours said that "[i]t is of the essence of election that the party electing shall be 'confronted' with two mutually exclusive courses of action between which he must, in fairness to the other party, make his choice".[102] The judges noted that in this case, the right to terminate the contract arose and, moreover, continued after the council failed to approve the transfer by the date specified in the contract.[103] This meant that the purchaser had not been confronted with the necessity of making an election at the time the documents were forwarded to the vendor.[104] Accordingly, Deane, Toohey, Gaudron and McHugh JJ concluded that in a context where, unbeknown to the purchaser, the council had not approved the transfer and where there was as yet no necessity for the purchaser to make a choice between affirming and terminating the contract, the purchaser's conduct did not constitute an election to proceed with the contract regardless of whether or not the council had approved the transfer.[105]

100 *Immer (No 145) Pty Ltd v Uniting Church in Australia Property Trust (NSW)* (1993) 182 CLR 26.

101 *Immer (No 145) Pty Ltd v Uniting Church in Australia Property Trust (NSW)* (1993) 182 CLR 26, 41.

102 *Immer (No 145) Pty Ltd v Uniting Church in Australia Property Trust (NSW)* (1993) 182 CLR 26, 41, quoting Spencer, Bower and Turner, *The Law Relating to Estoppel by Representation* (3rd ed, 1977), p 313.

103 *Immer (No 145) Pty Ltd v Uniting Church in Australia Property Trust (NSW)* (1993) 182 CLR 26, 42.

104 *Immer (No 145) Pty Ltd v Uniting Church in Australia Property Trust (NSW)* (1993) 182 CLR 26, 43.

105 *Immer (No 145) Pty Ltd v Uniting Church in Australia Property Trust (NSW)* (1993) 182 CLR 26, 43.

Brennan J considered that the conduct of the purchaser in forwarding the documents was not an unequivocal election to affirm the contract. It was merely an intimation that if the vendor was in a position to complete the transaction – that is, had obtained council approval – the purchaser was not intending to exercise its right to terminate the contract.[106] In circumstances where the council had not approved the transfer, the vendor was not able to complete. Accordingly, the purchaser was entitled to elect to rescind.

Communication of election

[25.105] An aggrieved party need not personally communicate his or her election to the other party. It has been suggested that it is sufficient for the fact of the election to come to the attention of the party in breach,[107] such as "by notification by an unauthorised broker or other intermediary".[108] Nonetheless, it may be prudent for the aggrieved party to communicate his or her choice so as to avoid arguments at a later time about what the aggrieved party's conduct signified.

ESTOPPEL

Estoppel and termination for breach

[25.110] The exercise of a right to terminate a contract may, like other legal rights, be restricted by equitable estoppel where an aggrieved party has induced the other party to believe that the contract will not be terminated, and the other party has relied on that assumption. For example, consider a contract for the sale of land in which time is expressed to be of the essence. Before the date for settlement, the purchaser approaches the vendor and asks if the vendor would allow him to tender the purchase price a few days after the date specified in the contract, because he is having difficulty obtaining finance to fund the purchase. The vendor says that she will grant the purchaser two additional days to complete the contract. In such a case, the vendor may be estopped from relying on the purchaser's failure to pay the purchase price on the date specified in the contract as a reason for terminating the contract.[109] The elements of equitable estoppel would need to be satisfied.[110] In particular, the purchaser would need to show that he relied to his detriment on the vendor's representation that she would accept late payment. This might be done by showing that the purchaser could have obtained the money to fund the purchase by the specified date but, in reliance on the vendor's representation, did not do so. The mere fact the purchaser did not have the money on the date of settlement specified in the contract would not of itself amount to detrimental reliance. The purchaser would need to show that he had acted on the vendor's representation by refraining from making arrangements to obtain funding by the due date. Furthermore, where the

106 *Immer (No 145) Pty Ltd v Uniting Church in Australia Property Trust (NSW)* (1993) 182 CLR 26, 30.

107 *Wood Factory Pty Ltd v Kiritos Pty Ltd* (1985) 2 NSWLR 105, 146; *Majik Markets Pty Ltd v S & M Motor Repairs Pty Ltd (No 1)* (1987) 10 NSWLR 49, 54; *Vitol SA v Norelf Ltd* [1996] AC 800, 810–11. See also Carter, *Contract Law in Australia* (7th ed, 2018), [31-04].

108 *Vitol SA v Norelf Ltd* [1996] AC 800, 810–1.

109 Cf *Legione v Hateley* (1983) 152 CLR 406.

110 See Chapter 9.

contract contains a clause that provides that delay in exercising rights under the contract will not operate as a waiver, it may be difficult to show that the assumption made by the purchaser was induced by the vendor.[111]

In *W & R Pty Ltd v Birdseye*,[112] the Full Court of the Supreme Court of South Australia considered whether an aggrieved party who has validly terminated the contract may be estopped from denying the enforceability of the contract based on post-termination conduct. W & R, the vendor, validly terminated the contract in response to Birdseye's failure to pay the deposit as required by the contract. Doyle CJ (with whom Duggan J agreed) held that as the parties subsequently conducted themselves as though the contract was still on foot, an estoppel by convention arose and the parties' rights were to be determined on the basis that the contract remained in force. Anderson J disagreed. As no further contract was entered into, and because the parties had not agreed about future settlement, his Honour held that the contract was not affirmed by the parties' subsequent conduct.

Estoppel and failure of a condition

[25.112] As noted at [20.40], some courts are now more willing to give effect to clauses that purport to terminate a contract automatically upon the non-fulfilment of a condition. However, where both parties conduct themselves as though the contract is still on foot, even though the condition has not been fulfilled, an estoppel by convention may arise which will prevent the parties from asserting that non-fulfilment of the condition has brought the contract to an end automatically.[113] Similarly, where, during the course of their relationship, the parties have conducted themselves on the basis that failure of the condition will not bring about automatic termination, an estoppel by convention may apply.[114] In *Waterman v Gerling Australia Insurance Co Pty Ltd*,[115] the contract provided that it was a condition of the contract that, in the event that an instalment of the insurance premium was not paid on time, the policy would be deemed to have ceased. Brereton J held that automatic cessation was intended.[116] However, the insurance company's prior acceptance of late payments and practice of issuing reminder notices where payment was not received on time established that the parties were proceeding on the assumption that punctual payment of premium instalments was not essential to the maintenance of cover under the policy. As the parties had operated on the basis of this assumed state of affairs, and because the insured had acted to his detriment by not paying any outstanding balance promptly, an estoppel by convention prevented the insurance company from terminating the contract.[117]

A party may also be estopped from terminating the contract on the basis of non-fulfilment of a contingent condition if he or she leads the other party to believe that he or she will not terminate the contract on this basis and the other party relies on that assumption to its detriment.[118]

111 *Kostopoulos v GE Commercial Finance Australia Pty Ltd* [2005] QCA 311, [57].

112 *W & R Pty Ltd v Birdseye* [2008] SASC 321; (2008) 102 SASR 477.

113 *MK & JA Roche Pty Ltd v Metro Edgley Pty Ltd* [2005] NSWCA 39.

114 *Waterman v Gerling Australia Insurance Co Pty Ltd* [2005] NSWSC 1066; (2005) 65 NSWLR 300, [78].

115 *Waterman v Gerling Australia Insurance Co Pty Ltd* [2005] NSWSC 1066; (2005) 65 NSWLR 300.

116 *Waterman v Gerling Australia Insurance Co Pty Ltd* [2005] NSWSC 1066; (2005) 65 NSWLR 300, [53].

117 *Waterman v Gerling Australia Insurance Co Pty Ltd* [2005] NSWSC 1066; (2005) 65 NSWLR 300, [96]–[98].

118 *Anaconda Nickel Ltd v Edensor Nominees Pty Ltd* [2004] VSCA 167, discussed at [9.195].

The relationship between the doctrines of estoppel and election

[25.115] Although the doctrines of estoppel and election may overlap in some cases, the two doctrines have different requirements and may produce different results. Election is based on the concept of a binding choice, which requires knowledge of the facts giving rise to the right to terminate, and possibly also knowledge of the legal right to terminate. Estoppel is based on detrimental reliance on an assumption induced by the other party. The role of knowledge in estoppel in this context is uncertain. Might an aggrieved party be estopped from asserting a right to terminate a contract on the ground that, although not aware of the existence of the right, the aggrieved party has induced the party in breach to act on the assumption that a right of termination will not be exercised? In *Sargent v ASL Developments Ltd*, Stephen J stated that, in appropriate circumstances, such an estoppel might arise.[119] On the other hand, it might be argued that in many cases, it would not be unconscionable for an aggrieved party to depart from the assumption if the aggrieved party was unaware of the facts giving rise to the right to terminate.

It is clear that, unlike estoppel, election does not require detrimental reliance by the party in breach.[120] Another important difference between election and estoppel concerns the effect of the doctrines. An election once made is final; the aggrieved party has no right to change his or her mind later. By contrast, estoppel may have a temporary effect.[121] In some cases, an aggrieved party may regain his or her right to terminate by giving reasonable notice to the party in breach advising that party of his or her intention to terminate should the breach not be rectified.[122] Further, estoppel may not always prevent a right of termination from being exercised. The aggrieved party may be able to exercise a right of termination if he or she compensates the party in breach for any loss suffered as a result of reliance on the assumption that the contract would not be terminated.[123]

WAIVER

[25.120] We have already discussed the concept of waiver in relation to contingent conditions.[124] The word "waiver" is also sometimes used to describe a restriction on the right to terminate a contract. It is also sometimes misleadingly used to describe the doctrines of election or estoppel.[125] The aggrieved party is sometimes said to "waive" a breach if he or she indicates an intention to continue with performance. However, most cases which purport to be resolved on the basis of waiver are really decided on the basis of election or estoppel.[126]

Despite acknowledging that often arguments framed in terms of waiver are actually, in substance, claims of election or estoppel, some judges nevertheless continue to analyse election

119 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 642.

120 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 655.

121 See, eg, *Hughes v Metropolitan Railway Co* (1877) 2 App Cas 439.

122 *Wallace-Smith v Thiess Infraco (Swanston) Pty Ltd* [2005] FCAFC 49, [64].

123 See [9.115].

124 See Chapter 20.

125 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 655; *Foran v Wight* (1989) 168 CLR 385, 434; *Commonwealth v Verwayen* (1990) 170 CLR 394, 406, 451–2, 480–1, 481. See also Carter, "Waiver (of Contractual Rights) Distributed" (1991) 4 *Journal of Contract Law* 59.

126 *Commonwealth v Verwayen* (1990) 170 CLR 394, 481 (McHugh J). See also *Agricultural and Rural Finance Pty Ltd v Gardiner* [2008] HCA 57; (2008) 238 CLR 570, [83]–[84], [128].

or estoppel arguments using the language of waiver.[127] Others appear to view the terms election and waiver as interchangeable.[128]

The High Court of Australia has considered whether, in the context of contractual rights, the term waiver has any content outside the established categories of contractual variation, estoppel and election. *Agricultural and Rural Finance Pty Ltd v Gardiner*[129] arose out of a failed agricultural investment scheme. Agricultural and Rural Finance (the lender) loaned money to Mr Gardiner so that he could participate in an agricultural project. Mr Gardiner also entered into indemnity agreements with an associated company of the lender, Oceanic Agricultural Ltd (the indemnifier). Under the terms of the indemnity agreements, the indemnifier agreed to indemnify the borrower against any demand by the lender for repayment under the loan agreements where the borrower ceased to participate in the agricultural project for one of the reasons specified in the indemnity agreements. Further, the loan agreements themselves provided that the lender was unable to have recourse to the borrower if the indemnity was effective and enforceable.

Clause 2 of the indemnity agreements made punctual payment of the loan agreement a condition of the enforceability of the indemnity agreement. Mr Gardiner had failed to make punctual payments. A term of the loan agreements gave the lender the right to accelerate the obligation to pay in these circumstances. The lender did not exercise this right, and Mr Gardiner eventually met his obligations under the loan agreements. When the agricultural project collapsed, Mr Gardiner sought to rely on the indemnity agreements. The indemnifier asserted that it was not bound to indemnify Mr Gardiner because the condition in clause 2 of the indemnity agreement had not been satisfied. In response, Mr Gardiner argued that the indemnifier had waived its right to rely on clause 2. Mr Gardiner relied on four separate events in support of his "waiver" argument. First, he asserted that Mr Lloyd (the indemnifier's managing director) had made oral representations that the borrower would receive reminder notices. Secondly, he asserted that Mr Lloyd had told him that he "need not be concerned about the indemnity". Thirdly, he claimed that Ms Edwards (who it was held worked for the lender) had told him "there would be no adverse consequences as a result of the delay in payment". Finally, he relied on a letter sent by Ms Edwards that stated "as [the lender] failed to send reminder notices we will accept payment as 'on time' up until 30 June 1999". On credit grounds, all five judges did not accept that the first three events had occurred, at least in the manner as described by Mr Gardiner. Their Honours accepted that the fourth event took place but held that Ms Edwards had been speaking for the lender, not the indemnifier.

Mr Gardiner argued that the rights had been waived in one or more of three different senses: an election between inconsistent rights; an application of the common law doctrine of forbearance; or the abandonment or renunciation of a right. The election argument failed. Election involves the choice between inconsistent rights.[130] Mr Gardiner's failure to pay the loan agreements punctually did not require the indemnifier to choose between terminating the agreement and insisting upon further performance. Rather, Mr Gardiner's failure simply relieved the indemnifier of its obligations under the indemnification agreements.[131] The forbearance

127 See, eg, *Kostopoulos v GE Commercial Finance Australia Pty Ltd* [2005] QCA 311, [36]–[47].

128 See, eg, *Waterman v Gerling Australia Insurance Co Pty Ltd* [2005] NSWSC 1066; (2005) 65 NSWLR 300, [71].

129 *Agricultural and Rural Finance Pty Ltd v Gardiner* [2008] HCA 57; (2008) 238 CLR 570.

130 See [23.35].

131 *Agricultural and Rural Finance Pty Ltd v Gardiner* [2008] HCA 57; (2008) 238 CLR 570, [64]–[65].

argument also failed. The cases cited by Mr Gardiner in support of the common law doctrine involved a promisor agreeing not to enforce a particular right and the promisee acting upon the basis that the right was not being enforced. As a result, Gummow, Hayne and Kiefel JJ (with whom Heydon J agreed) noted that the forbearance argument "seems little different from estoppel"[132] and that the cases relied upon by Mr Gardiner were, properly analysed, better understood as turning on accepted principles of estoppel and contractual variation.[133] The abandonment argument also failed as the time for abandonment or renunciation of the right had not arrived when the four events said to constitute waiver allegedly occurred. Gummow, Hayne and Kiefel JJ seemed critical of the abandonment argument, noting that "[p]ropositions expressed in terms of abandonment or renunciation of a right … are statements of conclusion. They are not statements that reveal the process of reasoning which leads to the assignment of the chosen description".[134]

Mr Gardiner did not argue for the existence of a residual category of waiver based on unfairness. Accordingly, Gummow, Hayne and Kiefel JJ stated that it was "unnecessary to determine whether such a residual category or general principle exists in the common law of Australia".[135] However, their Honours stressed that their "silence on the subject should not be taken as an encouragement to further speculation".[136] Gummow, Hayne and Kiefel JJ then noted that although there is support for a category of waiver based on unfairness in some decisions in other jurisdictions, quite often the word waiver is being used in contexts that are far removed from the contractual context. Further, reference to "unfairness" in those cases may not be to a defining principle. For example, it may convey no more than the fact that there has been detrimental reliance sufficient to ground an estoppel. Kirby J agreed that the waiver case put to the Court should fail. However, his Honour indicated a willingness to recognise a free-standing doctrine of waiver independent of estoppel, election or contractual variation. Under the doctrine contemplated by Kirby J, "the facts must be such that it would be manifestly unfair for the party which had earlier waived its legal rights later to adopt an inconsistent position and to seek to enforce them".[137] Applying this test to the facts at hand, Kirby J held that the indemnifier had not waived its rights. Like Gummow, Hayne and Kiefel JJ, Kirby J also did not accept that the first three events listed above had occurred. Further, as Ms Edwards did not have the authority to act on behalf of the indemnifier, it could not be said that it was "manifestly unfair" to allow the indemnifier to rely on clause 2 of the indemnification agreements.

RELIEF AGAINST FORFEITURE

Forfeiture arising on breach of contract

[25.125] Termination brings to an end the right of each party to further performance of the contract. Depending on the circumstances, this may have the effect that the party in

132 *Agricultural and Rural Finance Pty Ltd v Gardiner* [2008] HCA 57; (2008) 238 CLR 570, [71].
133 *Agricultural and Rural Finance Pty Ltd v Gardiner* [2008] HCA 57; (2008) 238 CLR 570, [71]–[87].
134 *Agricultural and Rural Finance Pty Ltd v Gardiner* [2008] HCA 57; (2008) 238 CLR 570, [90].
135 *Agricultural and Rural Finance Pty Ltd v Gardiner* [2008] HCA 57; (2008) 238 CLR 570, [98].
136 *Agricultural and Rural Finance Pty Ltd v Gardiner* [2008] HCA 57; (2008) 238 CLR 570, [98].
137 *Agricultural and Rural Finance Pty Ltd v Gardiner* [2008] HCA 57; (2008) 238 CLR 570, [145].

breach will forfeit property rights (eg, under a lease or a contract of sale), payments of money (eg, payments made under an instalment contract of sale) or valuable contractual rights. Courts of equity have long exercised a jurisdiction to provide relief against forfeiture. In an appropriate case, a court may grant relief against an unjust or unconscionable forfeiture by decreeing specific performance of the contract.[138]

Relief against forfeiture is generally understood to operate only as a restriction on termination for breach, and not as a restriction on termination for non-fulfilment of a condition.[139] Where a contract for the sale of land is subject to a contingent condition, then any interest the purchaser has in the land remains conditional until the contingency occurs. Granting relief against forfeiture in the absence of fulfilment of the condition would have the effect of vesting in the purchaser something that he or she did not securely hold.[140] Although, as a matter of principle, relief against forfeiture would seem to be inapplicable in cases of termination for non-fulfilment of a condition, there is some doubt about this.[141]

The need for a property interest

[25.130] Relief against forfeiture has traditionally been granted with respect to payments of money and interests in property. Where termination of a contract of sale results in the forfeiture of instalment payments exceeding a reasonable deposit, relief will generally be granted with respect to those instalments.[142] Otherwise, relief against forfeiture has traditionally been made "available in equity to lessees, with respect to their interest in reversion, and mortgagors with respect to their interest in the equity of redemption".[143] The principle developed by analogy to protect property rights more generally.[144] Commonly this interest is in land. For example, courts have been prepared to grant relief against forfeiture to a lessee where, pursuant to a term in the contract, the lessor has determined the lease for a default by the lessee in paying rent.[145] The High Court has also been prepared to grant relief against the loss of a purchaser's interest in land under a contract for the sale of the land, notwithstanding a breach by the purchaser of an essential time stipulation entitling the vendor to terminate the contract.[146] Relief against forfeiture may apply to protect interests in personal property.[147]

The notion that relief against forfeiture can be granted only with respect to proprietary rights is increasingly being called into question. In *Mineralogy Pty Ltd v Sino Iron Pty Ltd*

138 On relief against forfeiture of money paid by the party in breach under the contract, see also [29.45] and [29.50].

139 *Sanctuary Investments Pty Ltd v St Gregory's Armenian School Incorporated* [1998] NSWSC 788.

140 *Sanctuary Investments Pty Ltd v St Gregory's Armenian School Incorporated* [1998] NSWSC 788.

141 See Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [20.12].

142 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315, [54], [78]. See also [29.45]–[29.50].

143 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315, [87].

144 See generally Tilbury and Rossiter, "Relief Against Forfeiture", in Parkinson (ed), *The Principles of Equity* (2nd ed, 2003), Chapter 9.

145 Some statutes also contain provision for relief against forfeiture to be granted. See, eg, in relation to leases, *Conveyancing Act 1919* (NSW), s 129(2); *Law of Property Act* (NT), s 138(2); *Property Law Act 1974* (Qld), s 124(2); *Property Law Act 1958* (Vic), s 146(2); *Property Law Act 1969* (WA), s 81(2).

146 On the purchaser's equitable interest in land, see further *Stern v McArthur* (1988) 165 CLR 489, 521–4.

147 See, eg, *BICC plc v Burndy Corporation* [1985] Ch 232, 252; *On Demand Information plc v Gerson (Finance) plc* [2001] 1 WLR 155.

(No 6), Edelman J was willing to proceed on the assumption that the principle could be applied to relieve against forfeiture of contractual rights, although he found it to be unavailable for other reasons.[148] His Honour noted that any confinement of the doctrine to proprietary rights was difficult to justify as a matter of principle and raised difficult questions as to what rights are considered proprietary for this purpose.[149] As Edelman J observed, the right to contractual performance has been characterised as "quasi-proprietary" to the extent that it is protected against interference by third parties.[150] On appeal in *Mineralogy Pty Ltd v Sino Iron Pty Ltd*, the Full Court agreed that relief against forfeiture of a contractual right "may be taken to be available in principle".[151] The Chief Judge in Equity of the Supreme Court of New South Wales has also accepted that relief against forfeiture may be available with respect to non-proprietary rights.[152] Other courts have followed suit, though in each case relief against forfeiture has been found to be unavailable for other reasons.[153]

The unconscientious exercise of legal rights

What is an unconscientious exercise of legal rights?

[25.135] The High Court has stated that relief against forfeiture is based on the unconscionable exercise of legal rights. In *Tanwar Enterprises Pty Ltd v Cauchi* (*Tanwar*),[154] Gleeson CJ, McHugh, Gummow, Hayne and Heydon JJ stated that the term "unconscientious conduct" was more accurate. The term "unconscientious conduct" directs attention to the specific question of "why the [aggrieved party] ought not to be heard to assert the exercise of their legal right to terminate in answer to the claim by [the party in breach] for specific performance".[155] By contrast, the term "unconscionable conduct" runs the risk of suggesting that relief may be granted whenever there is some general element of unfairness or hardship.

The High Court has retreated from earlier observations[156] that relief against forfeiture will only be granted in exceptional circumstances because the term is apt to be misunderstood.[157] However, a court must not be too ready to deprive an aggrieved party of his or her right to terminate a contract.[158] The Court must also be confident that it can, by its orders, achieve the principal objects of the transaction. Thus, a court would not provide relief against forfeiture unless the applicant is in a position to complete his or her side of the bargain.[159]

148 *Mineralogy Pty Ltd v Sino Iron Pty Ltd (No 6)* [2015] FCA 825.

149 *Mineralogy Pty Ltd v Sino Iron Pty Ltd (No 6)* [2015] FCA 825, [978]–[990].

150 *Zhu v Treasurer of NSW* [2004] HCA 56; (2004) 218 CLR 530, [125].

151 *Mineralogy Pty Ltd v Sino Iron Pty Ltd* [2017] FCAFC 55, [421].

152 *Auburn Shopping Village Pty Ltd v Nelmeer Hoteliers Pty Ltd* [2017] NSWSC 1230, [212] (Ward CJ in Eq).

153 *JPA Finance Pty Ltd v Gordon Nominees Pty Ltd* [2019] VSCA 159, [82] (McLeish JA, with whom Beach and Niall JJA agreed); *Ayers Rock SkyShip Pty Ltd v Voyages Indigenous Tourism Australia Pty Ltd* [2019] NSWSC 828, [106].

154 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315.

155 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315, [22].

156 *Legione v Hateley* (1983) 152 CLR 406, 429, 449; *Ciavarella v Balmer* (1983) 153 CLR 438, 454.

157 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57;(2003) 217 CLR 315, [39].

158 See, eg, *Stern v McArthur* (1988) 165 CLR 489, 501.

159 *Kostopoulos v GE Commercial Finance Australia Pty Ltd* [2005] QCA 311, [50].

As explained by Lord Wilberforce in *Shiloh Spinners Ltd v Harding* (*Shiloh Spinners*),[160] traditionally there are two circumstances where equity may grant relief against forfeiture:

> First, where it is possible to state that the object of the transaction and of the insertion of the right to forfeit is essentially to secure the payment of money, equity has been willing to relieve on terms that the payment is made with interest, if appropriate, and also costs … Secondly, there were the heads of fraud, accident, mistake or surprise, always a ground for equity's intervention, the inclusion of which entailed the exclusion of mere inadvertence and a fortiori of wilful defaults.

In *Legione v Hateley* (*Legione*) and *Stern v McArthur*, the High Court stated that these elements do not exhaust the scope of unconscientious conduct.[161] In *Legione*,[162] Mason and Deane JJ identified the following factors as relevant in deciding whether or not a case is appropriate for the grant of relief against forfeiture:

(1) Did the conduct of the [aggrieved party] contribute to the [other party's] breach?

(2) Was the [other party's] breach (a) trivial or slight, and (b) inadvertent and not wilful?

(3) What damage or other adverse consequences did the [aggrieved party] suffer by reason of the [other party's] breach?

(4) What is the magnitude of the purchaser's loss and the vendor's gain if the forfeiture is to stand?

(5) Is specific performance with or without compensation an adequate safeguard for the vendor?

However, in *Tanwar*,[163] Gleeson CJ, McHugh, Gummow, Hayne and Heydon JJ, in a joint judgment, expressed doubt over the role of these sorts of considerations, at least in a case concerning specific performance of a contract which has been terminated for breach of an essential time stipulation. Their Honours indicated instead a preference for the statement of Lord Wilberforce in *Shiloh Spinners* and noted that equity does not intervene to reshape contractual relations in a form the Court thinks more reasonable or fair.[164] Their Honours also viewed *Legione* as an example of the narrower equitable concept of "surprise".[165] The result in *Romanos v Pentagold Investments Pty Ltd*,[166] which was heard concurrently with *Tanwar*, also supports the return to the stricter, traditional approach. However, as discussed later in this chapter, the joint judgment in *Tanwar* also found that factors identified by Lord Wilberforce in *Shiloh Spinners* "do not disclose exhaustively the circumstances which merit this equitable intervention".[167] As a result, some judges continue to consider the factors identified by Mason and Deane JJ in *Legione*.[168]

160 *Shiloh Spinners Ltd v Harding* [1973] AC 691, 722, cited in *Stern v McArthur* (1988) 165 CLR 489, 500, 512, 527.

161 *Legione v Hateley* (1983) 152 CLR 406, 447–9; *Stern v McArthur* (1988) 165 CLR 489, 526.

162 *Legione v Hateley* (1983) 152 CLR 406, 449.

163 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315.

164 See *Romanos v Pentagold Investments Pty Ltd* [2003] HCA 58; (2003) 217 CLR 367, 375 (commenting on *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315).

165 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315, [61].

166 *Romanos v Pentagold Investments Pty Ltd* [2003] HCA 58; (2003) 217 CLR 367.

167 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315, [58]. See also Getzler, "Forfeiture for Breach of a Time Stipulation" (2004) 120 *Law Quarterly Review* 203.

168 See, eg, *Tim Barr Pty Ltd v Narui Gold Coast Pty Ltd* [2010] NSWSC 29, [398].

Legione

[25.140] *Legione*[169] was discussed earlier in relation to estoppel.[170] Briefly, the case concerned a contract for the sale of land. The vendor sought to terminate the contract for failure by the purchasers to complete the contract on the required date. Prior to this date, the purchasers had asked whether a further seven days would be allowed for completion. The vendor's solicitor's secretary replied: "I think that will be alright but I'll have to get instructions." When the purchasers did not tender the money on the required date, the vendor terminated the contract. The majority of the High Court considered that there were some factors that might support the availability of relief against forfeiture. However, because the matter had not been fully argued at the trial, the question was remitted to the Supreme Court for determination.

In holding that relief against forfeiture was potentially available, the majority noted that the purchasers' breach was inadvertent and not wilful.[171] Mason and Deane JJ also considered it relevant that the vendor's solicitors had contributed to the breach by creating the impression that they would accept completion of the contract in a few days.[172] We might remember that the majority in *Legione* did not consider that the vendor should be estopped from terminating the contract. Mason and Deane JJ considered that the secretary's comments were not a clear or unequivocal representation that the time would be extended.[173] Yet Mason and Deane JJ considered that this same conduct might have supported relief against forfeiture being granted. Both estoppel and relief against forfeiture are based on unconscionable conduct. It appears, then, that the concept of unconscionable conduct may differ in some respects between the two doctrines.

The decision of the majority in *Legione* that relief against forfeiture was potentially available was also influenced by the fact that the purchasers had erected a house on the land which would accrue as a windfall to the vendors should the contract be terminated.[174] This concern as a justification for relief against forfeiture was developed in *Stern v McArthur*.[175]

Stern

[25.145] In *Stern v McArthur*,[176] a contract for the sale of land provided for the price to be payable in instalments. The purchasers fell behind in their payments, and the vendors terminated the contract. The vendors were prepared to allow the purchasers the benefit of any improvements made to the land but claimed the increase in the value of the land for the vendors' own benefit. The High Court, by majority, granted the purchasers relief against forfeiture of their interest in the land.[177] Deane and Dawson JJ held that a contract for the sale of land with the price payable by instalments was similar in substance to the vendor providing finance to the purchaser on the security of a mortgage. Both arrangements involve financing the purchase on the security of the land. Deane and Dawson JJ noted that equity has

169 *Legione v Hateley* (1983) 152 CLR 406.

170 See [9.60].

171 *Legione v Hateley* (1983) 152 CLR 406, 429, 450.

172 *Legione v Hateley* (1983) 152 CLR 406, 450.

173 *Legione v Hateley* (1983) 152 CLR 406, 440, 454, but cf 421–2.

174 *Legione v Hateley* (1983) 152 CLR 406, 429, 450.

175 *Stern v McArthur* (1988) 165 CLR 489.

176 *Stern v McArthur* (1988) 165 CLR 489.

177 Brennan and Mason JJ dissenting.

traditionally been prepared to grant relief against forfeiture of a mortgagor's interest in land, "without regard to any stipulation as to time".[178] Deane and Dawson JJ considered that there was no good reason for refusing to extend similar protection to a purchaser who has entered into a transaction of a similar character.[179]

Deane and Dawson JJ and Gaudron J also indicated a concern to avoid the vendors gaining a windfall from the forfeiture because the land had increased in value since the contract was made. Their Honours considered that it was the purchasers who had a reasonable expectation of benefiting from any increase in the value of the land with the passage of time.[180] This aspect of the majority decision indicates a broad approach to the unconscientious conduct justifying relief against forfeiture. The concern of the judges was not with the conduct leading up to the decision to terminate, but rather, with the consequences of the decision to terminate, in particular the windfall benefit for the vendors.[181] As Glover has commented, these decisions raise the question of whether "a party is acting *unconscionably* … by insisting on being *unjustly enriched*".[182]

In *Stern v McArthur*, Mason CJ and Brennan J dissented. Their Honours considered that this was not a case where relief against forfeiture should be granted. The conduct of the vendors had not led the purchasers to breach the contract. Nor was the breach trivial.[183] The increase in the value of the land was merely a benefit which went with the land and whoever was entitled to the land.[184] Brennan J did not accept that the distinction between a mortgage and a contract of sale by instalments should be eliminated.[185] More generally, both judges were critical of an overly generous approach to granting relief against forfeiture. Mason CJ stated that the "jurisdiction to grant relief against forfeiture does not authorise a court to reshape contractual relations into a form that a court thinks more reasonable or fair where subsequent events have rendered one side's situation more favourable".[186] His Honour considered that to characterise the vendors' conduct in this case as unconscionable "would be to drain unconscionability of any meaning".[187]

Tanwar

[25.150] In *Tanwar*,[188] the parties had entered into contracts for the sale of land and deposits had been paid. The purchaser experienced difficulties meeting the completion date specified in the contracts and was granted an extension. The newly agreed completion date for the contracts was 25 June 2001. Time was stated to be of the essence. The funds for the purchase were coming from Singapore. The funds did not arrive until 26 June 2001. The vendors served

178 *Stern v McArthur* (1988) 165 CLR 489, 527. On what is known as the mortgagor's "equity of redemption", see further Rossiter, *Penalties and Forfeiture* (1992), pp 20–2.

179 *Stern v McArthur* (1988) 165 CLR 489, 528.

180 *Stern v McArthur* (1988) 165 CLR 489, 529, 540–1.

181 See Glover, "Equity and Restitution" in Parkinson (ed), *The Principles of Equity* (1996), pp 107–10.

182 Glover, "Equity and Restitution" in Parkinson (ed), *The Principles of Equity* (1996), p 110.

183 *Stern v McArthur* (1988) 165 CLR 489, 504, 516–17.

184 *Stern v McArthur* (1988) 165 CLR 489, 518.

185 *Stern v McArthur* (1988) 165 CLR 489, 519.

186 *Stern v McArthur* (1988) 165 CLR 489, 503, also 514.

187 *Stern v McArthur* (1988) 165 CLR 489, 505.

188 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315.

notice of termination of each contract. The High Court unanimously rejected the claim of the purchaser, Tanwar, to relief against forfeiture.

The joint majority judgment of Gleeson CJ, McHugh, Gummow, Hayne and Heydon JJ supported the more cautious approach to relief against forfeiture taken by Mason CJ in *Stern v McArthur*.[189] They affirmed a narrower range of circumstances in which relief against forfeiture would be granted on the ground of unconscientious conduct than that envisaged in some aspects of the judgments in *Stern v McArthur* and *Legione*.[190]

Their Honours said that the statement of Lord Wilberforce in *Shiloh Spinners*,[191] referring to the "special heads of fraud, accident, mistake or surprise", identified in a "broad sense" the factors making it unconscientious for the vendors to rely upon their rights to terminate a contract as an answer to Tanwar's claim for specific performance. Their Honours said that:

> No doubt the decided cases in which the operation of these "special heads" is considered do not disclose exhaustively the circumstances which merit this equitable intervention. But, at least where accident and mistake are not involved, it will be necessary to point to the conduct of the vendor as having in some significant respect caused or contributed to the breach of the essential time stipulation. Tanwar's situation falls beyond that pale.[192]

Gleeson CJ, McHugh, Gummow, Hayne and Heydon JJ did not think that the possibility of the vendors reaping the benefit of any improvements made by the purchasers was a sufficient ground for relief. The majority commented that "[t]he contract in *Legione* had permitted the purchasers to enter into possession and any improvements they then made were at risk of the operation of the contractual provisions for termination".[193] In *Tanwar*'s case, there was no indication that, as in *Legione*, the vendors had "helped to lull the purchasers into the belief that they would accept completion provided it occurred within a few days".[194]

Tanwar relied on the jurisdiction to relieve against the consequences of "accident". Referring to academic treatises, Gleeson CJ, McHugh, Gummow, Hayne and Heydon JJ listed classes of "accident" in this context as including, "the accidental diminution of assets in the hands of an executor, lost evidence and the defective execution of powers of appointment".[195] The judges also stated that "equity will not relieve where 'the possibility of the accident may fairly be considered to have been within the contemplation of the contracting parties'".[196] In the present case, the possibility there "might be a failure

189 *Stern v McArthur* (1988) 165 CLR 489.

190 *Legione v Hateley* (1983) 152 CLR 406. The joint judgment also pointed to an element of circularity in relying on a purchaser's proprietary interest in land in granting relief against forfeiture or, more accurately, specific performance following termination of a contract for the sale of land. The majority explained that the purchaser's proprietary interest is commensurate with the availability of specific performance. In seeking relief against forfeiture, "[t]hat availability is the very question in issue where there has been a termination by the vendor for failure to complete as required by the essential stipulation": *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315, [53].

191 *Shiloh Spinners Ltd v Harding* [1973] AC 691, 722.

192 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315, [58]. See also Getzler, "Forfeiture for Breach of a Time Stipulation" (2004) 120 *Law Quarterly Review* 203.

193 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315, [62].

194 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315, [61].

195 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315, [65].

196 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315, [66], citing Smith, *Principles of Equity* (4th ed, 1908), pp 243–4.

by a third party to provide the finance was reasonably within the contemplation of Tanwar".[197]

Although Gleeson CJ, McHugh, Gummow, Hayne and Heydon JJ in *Tanwar* emphasised the "special heads" referred to by Lord Wilberforce in *Shiloh Spinners*,[198] (the second basis of relief mentioned by his Lordship), relief against the forfeiture of a lease remains available on the first basis, namely where the insertion of the right to forfeit is to secure the payment of money and equity relieves on terms that payment is made.[199] In *Riviera Holdings Pty Ltd v Fingal Glen Pty Ltd*,[200] the respondent lessee had a history of late payment. The applicant lessor wrote to the lessee acknowledging the flexibility it had previously displayed regarding late payment and advising that from then onwards it would insist on its right to be paid on time. The lessee was late paying the first two payments due after it received the letter and the lessor terminated the lease. The lessee arranged for payment of outstanding amounts shortly thereafter. Nicholson J stated that "it was common ground that the principles relevant to relief against forfeiture for unpaid rent are distinct from those applicable for breach of other covenants of a lease and potentially provide a more favourable environment for the application of the doctrine of relief against forfeiture".[201] Nicholson J observed that "relief against forfeiture for non-payment of rent is granted, almost as of course, in circumstances where all arrears have been paid and other expenses and costs incurred by the landlord as a result of the breach have been met".[202] Nicholson J found that the lessor would not suffer prejudice if the lease were reinstated. If the lessee continued to pay late, a fresh right to terminate would arise. The lessee, however, faced a real risk of harm. The lessee purchased the business operated on the leased premises from the lessor. The purchase price for the business included a significant premium for the lease and the rights of renewal contained therein. Nicholson J granted relief against forfeiture on this basis.

Nicholson J's observations are not, however, rules of universal application. As Lord Wilberforce noted in the *Shiloh Spinners* case, there "may be cases where to oblige acceptance of a stipulated sum of money even with interest, at a date when receipt had lost its usefulness, might represent an unjust variation of what had been contracted for".[203]

UNCONSCIONABLE TERMINATION

Equity

[25.155] Some Australian courts have suggested that there may be a general equitable power to grant relief against any termination which would be unconscionable.[204] This suggestion draws on some general references of the High Court, such as those of Mason and Deane JJ in

197 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315, [67].

198 *Shiloh Spinners Ltd v Harding* [1973] AC 691.

199 See [25.135].

200 *Riviera Holdings Pty Ltd v Fingal Glen Pty Ltd* [2013] SASC 77; (2013) 120 SASR 450.

201 *Riviera Holdings Pty Ltd v Fingal Glen Pty Ltd* [2013] SASC 77; (2013) 120 SASR 450, [12].

202 *Riviera Holdings Pty Ltd v Fingal Glen Pty Ltd* [2013] SASC 77; (2013) 120 SASR 450, [29].

203 *Shiloh Spinners Ltd v Harding* [1973] AC 691, 722, cited in *Stern v McArthur* (1988) 165 CLR 489, 500, 512, 527.

204 See, eg, *Hortico (Aust) v Energy Equipment Co (Aust) Pty Ltd* (1985) 1 NSWLR 545, 554; *CSS Investments Pty Ltd v Lopiron Pty Ltd* (1987) 16 FCR 15; *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 268–70; *Kayserian Nominees (No 1) Pty Ltd v J R Garner Pty Ltd* [2008] NSWSC 803. See also *Pierce Bell Sales Pty Ltd v Frazer* (1973) 130 CLR 575, 587.

Legione, to "the fundamental principle according to which equity acts, namely that a party having a legal right shall not be permitted to exercise it in such a way that the exercise amounts to unconscionable conduct".[205]

This statement was made in the course of a discussion of relief against forfeiture. It might be interpreted as merely identifying the general principle which underlies established equitable doctrines, without treating unconscionable conduct as an independent restriction on termination. It might also be interpreted as supporting a broad restriction on termination based on unconscionable conduct.[206]

The general equitable power to limit the rights of parties to bring their contractual relations to an end has been raised by parties seeking to prevent the other party from rescinding a contract for non-fulfilment of a contingent condition.[207] The general doctrine is relied upon because, in such circumstances, it is arguable that there is no forfeiture against which relief might be granted.[208]

The Full Court of the Federal Court considered the meaning of the phrase "conduct that is unconscionable, within the meaning of the unwritten law" in what is now s 20 of the *Australian Consumer Law*[209] in *Australian Competition and Consumer Commission v Samton Holdings Pty Ltd* (*Samton Holdings*).[210] The Court found that this phrase referred to the doctrines of unconscionable dealing,[211] third-party impropriety,[212] estoppel,[213] relief against forfeiture and penalty, and unilateral mistake.[214] No mention is made of a general, broad restriction on termination based on unconscionable conduct. The Court did, however, note that this list "may not be exhaustive".[215]

In *Tenth Vandy Pty Ltd v Natwest Markets Australia Pty Ltd*,[216] the Victorian Supreme Court considered this issue in the context of a claim for relief against forfeiture. The appellant was unable to rely on the relief against forfeiture doctrine as it was unable to show that the respondent contributed to its (the appellant's) breach. The Court found that "the five categories of case identified in *Samton Holdings* represent the limits of the circumstances which thus far been recognised as attracting equity's jurisdiction to relieve against the consequences of unconscionable conduct".[217] The Court also acknowledged that the list may

205 *Legione v Hateley* (1983) 152 CLR 406, 444. See also *Godfrey Construction Pty Ltd v Kanangra Park Pty Ltd* (1972) 128 CLR 529, 538; *Stern v McArthur* (1988) 165 CLR 489, 501, 527; *Sunbird Plaza Pty Ltd v Maloney* (1987) 166 CLR 245, 263; *Foran v Wight* (1989) 168 CLR 385, 394.

206 Cf Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [21.35].

207 See, eg, *Kayserian Nominees (No 1) Pty Ltd v J R Garner Pty Ltd* [2008] NSWSC 803; *Actall Pty Ltd v Pacific Bay Development Pty Ltd* [2006] NSWCA 190.

208 *Kayserian Nominees (No 1) Pty Ltd v J R Garner Pty Ltd* [2008] NSWSC 803, [49]–[51].

209 See Chapter 38.

210 *Australian Competition and Consumer Commission v Samton Holdings Pty Ltd* [2002] FCAFC 4; (2002) 189 ALR 76.

211 See Chapter 36.

212 See Chapter 37.

213 See Chapter 9.

214 See Chapter 31.

215 *Australian Competition and Consumer Commission v Samton Holdings Pty Ltd* [2002] FCAFC 4; (2002) 189 ALR 76, 49.

216 *Tenth Vandy Pty Ltd v Natwest Markets Australia Pty Ltd* [2012] VSCA 103.

217 *Tenth Vandy Pty Ltd v Natwest Markets Australia Pty Ltd* [2012] VSCA 103, [134].

not be exhaustive as "[i]n principle, one cannot say the categories of case in which equity will intervene are necessarily closed".[218] The Court then referred to Bengal J's observation in *Cowcher v Cowcher*[219] that, "while equity is not yet past the age of child bearing, her progeny must be legitimate – by precedent out of principle". The Court then approved the following comments made by Kirby J in *Tanwar*:[220]

> In order to tame the elements of unpredictability introduced into legal relationships by the imposition of equitable principles, controls upon what might otherwise become a purely discretionary assessment are accepted. They include respect for the particular categories that have emerged in equitable jurisdiction, such that it is not taken to be at large … The categories are not closed. They may develop to meet new cases so long as such cases are perceived as sufficiently similar to the established ones.

Statute

[25.160] Statutory prohibitions on unconscionable conduct may, in some cases, restrict the right to terminate.[221] There is likely to be an overlap between these provisions in their application to termination and the duty of good faith.[222]

GOOD FAITH

[25.165] The courts have traditionally been concerned in termination cases with the question of whether or not an aggrieved party *has* a right to terminate a contract and have not traditionally inquired into whether the *exercise* of that right would be fair or reasonable. For example, in *Canberra Advance Bank Ltd v Benny*,[223] the Full Federal Court did not accept that a lender should be prevented from exercising its strict contractual rights following an event of default by the borrower, even where the event relied upon was relatively inconsequential. In that case, the borrower was two days late in providing financial reports required under the contract.

The recognition of an implied duty of good faith by some Australian courts, discussed in chapter 13, raises the question whether this duty might be implied to qualify the exercise of a right to terminate a contract.[224] Some Australian courts have suggested that the duty of good faith has an application in this context. In *Burger King Corp v Hungry Jacks Pty Ltd*, Sheller, Beazley and Stein JJA said that the case law indicated that "obligations of good

218 *Tenth Vandy Pty Ltd v Natwest Markets Australia Pty Ltd* [2012] VSCA 103, [134].

219 *Cowcher v Cowcher* [1972] 1 WLR 425, 430.

220 *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315, [86]–[87].

221 See, eg, *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* [1999] FCA 903; *Australian Competition and Consumer Commission v Simply No-Knead (Franchising) Pty Ltd* [2000] FCA 1365; (2000) 104 FCR 253. See also Chapter 38.

222 See also [14.125].

223 *Canberra Advance Bank Ltd v Benny* (1992) 38 FCR 427, 440. See also *Westminster Properties Pty Ltd v Comco Constructions Pty Ltd* (1990) 5 WAR 191, 196–7; *Snowlife Pty Ltd v Robina Land Corporation Ltd (No 2)* [1993] 1 Qd R 584.

224 See, eg, *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 258; *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* [1999] FCA 903; *Commonwealth Bank of Australia v Renstell Nominees Pty Ltd* [2001] VSC 167, [47]; *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187; (2001) 69 NSWLR 558, [167]; *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2005] FCA 288, [64]. See also generally Chapter 14.

faith and reasonableness will be more readily implied in standard form contracts, particularly if such contracts contain a general power of termination".[225] Such a duty might apply to preclude termination for trivial or opportunistic reasons.[226] In one of the few cases in which the argument has been successful, *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd*,[227] Finkelstein J found that Pacific Brands breached its duty of good faith by terminating a sub-licence on the grounds of a trivial breach, not because of the harm caused to Pacific Brands by the breach but because the sub-licensee refused to comply with the demands of Pacific Brands to enter into a direct licence.[228]

[25.170] More typically, however, Australian courts have been sceptical of the role of good faith in qualifying contractual termination powers.[229] Good faith does not require parties to forgo their own legitimate interests,[230] and these will usually be at stake where a party seeks to terminate a contract.[231] In particular, Australian courts have been unwilling to recognise implied good faith qualifications on the exercise of an absolute contractual power to terminate, such as where the contract provides for termination "at will", "without cause" or "for convenience".[232] This approach reflects the very purpose of such provisions, which is to grant one party an unfettered discretion to terminate the contract for whatever reason it finds compelling, or even for no reason.[233] In *Starlink International Group Pty Ltd v Coles Supermarkets Australia Pty Ltd*, the contract permitted the principal to terminate a service agreement "at any time without a reason" on giving 45 days notice.[234] The principal terminated the contract on the basis of a belief that the contractor had engaged in serious criminal activity. The contractor argued that the principal had insufficient evidence of the activity and that its conduct breached the duty of good faith because it was not honest or

225 *Burger King Corp v Hungry Jacks Pty Ltd* (2001) 69 NSWLR 558, 569. See also *Bhasin v Hrynew* [2014] SCC 71, [2014] 3 SCR 494; *Mohamed v Information Systems Architects Inc*, 2018 ONCA 428 and MacQueen and O'Byrne, "The Principle of Good Faith in Contractual Performance: A Scottish-Canadian Comparison" (2019) 23 *Edinburgh Law Review* 301.

226 See, eg, *Burger King Corp v Hungry Jacks Pty Ltd* [2001] NSWCA 187, (2001) 69 NSWLR 558, [163]; *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2005] FCA 288, [66]; *Mangrove Mountain Quarries Pty Ltd v Barlow* [2007] NSWSC 492, [28]; *Transpacific Pty Ltd v Prudential Retirement Insurance and Annuity Company* [2011] FCA 630, [18]; *Cordon Investments Pty Ltd v Lesdor Properties Pty Ltd* [2012] NSWCA 184, [153]. See also Brownsword, "Two Concepts of Good Faith" (1994) 7 *Journal of Contract Law* 197.

227 *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2005] FCA 288, [66].

228 *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2005] FCA 288, [66].

229 Paterson, "Good Faith Duties in Contract Performance" (2014) 14 *Oxford University Commonwealth Law Journal* 283.

230 See, eg: *Burger King Corp v Hungry Jacks Pty Ltd* [2001] NSWCA 187, (2001) 69 NSWLR 558, 573; *South Sydney District Rugby League Football Club Ltd v News Ltd* [2000] FCA 1541, [394]; *Bundanoon Sandstone Pty Ltd v Cenric Group Pty Ltd* [2019] NSWCA 87, [154].

231 See, eg, *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* [1999] FCA 903.

232 *Starlink International Group Pty Ltd v Coles Supermarkets Australia Pty Ltd* [2011] NSWSC 1154, [19]; *Trans Petroleum (Australia) Pty Ltd v White Gum Petroleum Pty Ltd* [2012] WASCA 165, [155]; *Dura (Aust) Constructions Pty Ltd v Hue Boutique Living Pty Ltd (No 3)* [2012] VSC 99, [421]; *NSW Rifle Association Inc v The Commonwealth of Australia* [2012] NSWSC 818, [200]; *Tim Barr Pty Ltd v Narui Gold Coast Pty Ltd* [2010] NSWSC 29 [418]; *DPN Solutions Pty Ltd v Tridant Pty Ltd* [2014] VSC 511, [111].

233 Cf *Clough Engineering Ltd v Oil and Natural Gas Corporation Ltd* [2008] FCAFC 136, [138]; *Tymshare Inc v Covell* 727 F 2d 1145, 1153 (1984).

234 *Starlink International Group Pty Ltd v Coles Supermarkets Australia Pty Ltd* [2011] NSWSC 1154.

reasonable.[235] The Supreme Court of New South Wales rejected this argument. Bergin CJ held that because the termination clause expressly provided that there was no need for any "cause" or "reason" for the exercise of the right to terminate, there was no justification for requiring the principal to have a good reason for exercising its rights.[236]

English courts have also rejected the application of good faith duties to qualify the exercise of a contractual power to terminate a contract.[237] Good faith duties have little application in the exercise of a contractual right to end a contractual relationship. In *Monde Petroleum SA v WesternZagros Ltd*, Richard Salter QC said:

> The purpose of a contractual right to terminate is to give the party on whom that right is conferred the power to bring the contract to an end. It is a right to bring an end to the parties' shared endeavour. In my judgment, it is unlikely that the hypothetical reasonable commercial man or woman would expect the party exercising that right to be obliged to consult anyone's interests but its own.[238]

CONTRACTUAL RESTRICTIONS

[25.180] Contracting parties are generally free to impose additional restrictions on their rights to terminate, and contractual provisions that restrict the parties' right to terminate are be construed "according to [their] natural and ordinary meaning".[239] In identifying the effect that clauses dealing with termination for breach of a contract are intended to have, it is necessary to keep in mind that "clear words are needed to rebut the presumption that a contracting party does not intend to abandon any remedies for breach of contract arising by operation of law".[240] In *Wallace-Smith v Thiess Infraco (Swanston) Pty Ltd*,[241] Thiess (a maintenance provider) sought loss of bargain damages when an unsuccessful tram-operation franchise failed to make payments due under the maintenance agreement between the parties. Although this constituted a breach of an essential term and repudiatory conduct, the administrators of the tram-operation franchise contested Thiess' claim for loss of bargain damages by arguing that the maintenance agreement was terminated by consent, not on the basis of the franchisee's breach. Clause 24.4 placed significant restraints on Thiess' ability to terminate the agreement. Thiess was not permitted to terminate the agreement unless the Department of Transport was satisfied that arrangements had been made that would ensure the continued operation of Melbourne's tram services. This condition was only satisfied when, approximately six months after the franchisee's breach, the Victorian Government entered into an agreement with Thiess

235 *Starlink International Group Pty Ltd v Coles Supermarkets Australia Pty Ltd* [2011] NSWSC 1154, [19].

236 *Starlink International Group Pty Ltd v Coles Supermarkets Australia Pty Ltd* [2011] NSWSC 1154, [33].

237 *Lomas v JFB Firth Rixson Inc* [2012] EWCA Civ 419, [46]; *TSG Building Services Plc v South Anglia Housing Ltd* [2013] EWHC 1151 (TCC), [51]; *Monde Petroleum SA v WesternZagros Ltd* [2016] EWHC 1472 (Comm), [272]. See also *Mid Essex NHS Trust v Compass Group UK and Ireland Ltd* [2013] EWCA Civ 200, [83]. See also Courtney, "Good Faith and Termination: The English and Australian Experience" (2019) 1 *Journal of Commonwealth Law* 185; Foxton, "A Good Faith Goodbye? Good Faith Obligations and Contractual Termination Rights" [2017] *Lloyd's Maritime and Commercial Law Quarterly* 360.

238 *Monde Petroleum SA v WesternZagros Ltd* [2016] EWHC 1472 (Comm), [272], appeal on different points dismissed in *Monde Petroleum SA v WesternZagros* [2018] EWCA Civ 25.

239 *Wallace-Smith v Thiess Infraco (Swanston) Pty Ltd* [2005] FCAFC 49, [61].

240 *Wallace-Smith v Thiess Infraco (Swanston) Pty Ltd* [2005] FCAFC 49, [62], citing *Concut v Worrell* [2000] HCA 64, 317.

241 *Wallace-Smith v Thiess Infraco (Swanston) Pty Ltd* [2005] FCAFC 49.

and a new franchisee. French J noted that cl 24.4 could be interpreted in two ways, one that saw the common law right to terminate extinguished and the other that saw the right deferred until the condition specified had been satisfied. French J held that the second interpretation was appropriate on the basis that such a construction was consistent with the language of cl 24.4 and least disturbed the common law rights to terminate.[242]

242 *Wallace-Smith v Thiess Infraco (Swanston) Pty Ltd* [2005] FCAFC 49, [70]. Cf Allsop J's dissenting judgment.

REMEDIES FOR BREACH

PART X

[PtX.05] This part discusses the principles governing the remedies available to a party (*plaintiff*) on breach of contract. In a common law system, the primary remedy for breach of contract is damages. In most cases,[1] the right to damages will apply regardless of whether or not the party seeking the damages also terminates the contract.[2] Damages for a breach of contract are available to the plaintiff as of right. Indeed, the obligations created by a contract may be analysed as primary obligations, with the breach of a primary obligation giving rise to a substituted or secondary obligation to pay damages.[3] The right to damages may be contrasted with the equitable remedies of specific performance and injunction, which are awarded at the discretion of the court.

Parties may themselves attempt to specify in advance the damages payable for breach of contract, through a clause known as an agreed or liquidated damages clause. The breadth of an agreed damages clause is limited by the rule against penalties. In circumstances where a party fails to pay money owing under a contract, the other party may, sometimes as an alternative to damages, bring an action to recover the sum as a debt.

1 An exception exists in relation to anticipatory breach, discussed at [27.145].

2 *Luna Park (NSW) Ltd v Tramways Advertising Pty Ltd* (1938) 61 CLR 286. Whether or not the contract is terminated may affect the amount of damages available.

3 See *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827, 848–51.

CHAPTER **26**

The measure of damages

CONTRACT DAMAGES

[26.05] Whenever one party to a contract (the *defendant*) breaches that contract, the other party (the *plaintiff*) will be entitled to an award of damages. Damages for breach of contract are available as of a right. Damages for breach of contract aim to put the plaintiff in the position he or she would have been in if the contract had been performed. In this chapter, we discuss the rules for measuring damages aimed at giving effect to this objective.

The different measures of damages

[26.10] The general principle governing the measure of damages in contract law was stated by Parke B in *Robinson v Harman* as follows:

> Where a party sustains a loss by reason of a breach of contract, he is, so far as money can do it, to be placed in the same situation with respect to damages as if the contract had been performed.[1]

This statement has been approved by the High Court on numerous occasions.[2]

It is implicit in the *Robinson v Harman* principle that contract damages are not punitive; they do not aim to punish the defendant. It follows that in Australia, *exemplary damages* which penalise a defendant are not awarded for breach of contract.[3]

Generally, in giving effect to the *Robinson v Harman* principle, courts make an award of what are called *expectation damages*. Expectation damages compensate the plaintiff for the loss of the benefit he or she expected to gain from performance of the contract. Expectation damages are commonly based on a market measure of the value of the lost performance. Some scholars have suggested that damages for the loss of performance should be conceptualised as *vindicating* the plaintiff's lost performance interest.[4] However, it appears that Australian and English continue to treat the primary aim of contract damages as being compensation for the loss of the promised performance.[5]

Expectation damages may also cover *consequential losses* sustained by reason of the breach. This measure goes beyond compensating direct losses, primarily the value of the lost performance interest, to provide compensation for the incidental losses that flow from the breach,[6] such as search costs for a replacement for goods or materials that were not delivered or the loss of lucrative contracts that, due to the breach, cannot now be performed.

Different measures of damages may be utilised in some cases to give effect to the value of the lost performance. In cases where the breach relates to faulty repairs or building work, courts may look to the cost of *rectification or repair*. In cases where the plaintiff cannot establish the value of the benefit that he or she would have gained had the contract been performed, courts may award damages to compensate the plaintiff for expenditure incurred in reliance on the contract being performed. These are known as *reliance damages*. Reliance damages may be seen as an approximation of expectation damages. Damages for *loss of a chance* may be awarded where all the plaintiff expected to gain from performance of the contract was the chance of a benefit.

In England, the House of Lords has raised the possibility of an *account of profits* or *disgorgement* damages being available in response to a breach of contract, which require the defendant to account for or "disgorge" any profit made by reason of his or her breach.[7] Such

1 *Robinson v Harman* [1848] 1 Ex 850, 855; 154 ER 363, 365. Compare the measure of damages in torts: see [2.40].

2 See, eg, *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 80, 98, 117, 134, 148, 161; *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [13]; *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [7], [11], [60], [106].

3 *Butler v Fairclough* (1917) 23 CLR 78, 89; *Gray v Motor Accident Compensation Commission* (1998) 196 CLR 1, [13]. Cf Duggan, "Exemplary Damages in Equity: A Law and Economics Perspective" (2006) 26 *Oxford Journal of Legal Studies* 303, esp 324–5.

4 Stevens, *Torts and Rights* (2007). Compare Winterton, *Money Awards in Contract Law* (2015). Also, in the Australian context, Barnett, "Great Expectations: A Dissection of Expectation Damages in Contract in England and Australia" (2016) 33 *Journal of Contract Law* 163.

5 See Burrows, *Remedies for Torts, Breach of Contract and Equitable Wrongs* (4th ed, 2019), pp 46–50.

6 Edelman (ed), *McGregor on Damages* (20th ed, 2018), [3.008].

7 *Attorney-General v Blake* [2001] 1 AC 268.

an award is not based on a principle of compensation but is rather based on the gain made by a defendant as a result of the breach of contract.

Proving and quantifying damages

[26.15] Generally, a plaintiff seeking an award of damages bears the onus of proving that he or she has suffered a loss as a result of the breach of contract on the balance of probabilities.[8] Where no loss is established, the plaintiff will usually recover only nominal damages.[9] Nominal damages are a sum of money awarded in recognition of the fact that the plaintiff's legal rights have been infringed, but without compensating any actual loss.[10] A plaintiff who establishes a loss caused by a breach of contract will, subject to the limits discussed in Chapter 27, be entitled to substantial damages, meaning an amount to compensate that loss.[11] Courts will accept that in some cases, a plaintiff will not be able to produce precise evidence of the loss he or she has suffered by reason of the defendant's breach.[12] However, the "mere difficulty" of estimating damages does not relieve a court of the responsibility of placing a value on what has been lost.[13]

Date for assessing damages

[26.20] In most cases, damages are assessed at the date of the breach of contract.[14] However, the rule is not absolute and may be applied in a flexible manner.[15] Courts have the power to depart from the general rule and fix some other date for assessing damages "whenever it is necessary to do so in the interests of justice".[16] For example, in cases of contracts for the sale of goods which the seller fails to deliver, damages will normally be assessed at the date of non-delivery.[17] An exception is where there is no market in which the plaintiff can buy substitute goods. In such a case, fixing damages at a later date, when the plaintiff is actually able to purchase replacement goods, may be more appropriate.[18] This will allow any increase in the price of the goods over the search period to be taken into account. On the date for assessing damages and supervening events, see [26.95].

8 *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 80, 99, 137. Also *Placer (Granny Smith) Pty Ltd v Thiess Contractors Pty Ltd* [2003] HCA 10; (2003) 196 ALR 257, [38].

9 See, eg, *Luna Park (NSW) Ltd v Tramways Advertising Pty Ltd* (1938) 61 CLR 286.

10 *Owners of SS "Mediana" v Owners etc of SS "Comet"* [1900] AC 113, 116.

11 *Placer (Granny Smith) Pty Ltd v Thiess Contractors Pty Ltd* [2003] HCA 10; (2003) 196 ALR 257.

12 *Placer (Granny Smith) Pty Ltd v Thiess Contractors Pty Ltd* [2003] HCA 10; (2003) 196 ALR 257, [38].

13 *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 88. See also *Fink v Fink* (1946) 74 CLR 127, 143; *McRae v Commonwealth Disposals Commission* (1951) 84 CLR 377, 411–2; *Chaplin v Hicks* (1911) 2 KB 786, 792; *Placer (Granny Smith) Pty Ltd v Thiess Contractors Pty Ltd* [2003] HCA 10; (2003) 196 ALR 257, [38].

14 *Johnson v Perez* (1988) 166 CLR 351, 355, 367, 380, 386.

15 *Johnson v Perez* (1988) 166 CLR 351, 356–8, 367, 380, 386–9. See also *Golden Strait Corporation v Nippon Yusen Kubishika Kaisha* [2007] UKHL 12; [2007] 3 AC 353.

16 *Johnson v Perez* (1988) 166 CLR 351, 356.

17 A similar rule applies in assessing damages for breach of a contract for the sale of land, see *Ng v Filmlock Pty Ltd* (2014) 88 NSWLR 146.

18 See *Johnson v Perez* (1988) 166 CLR 351, 357, 388–9; *Wenham v Ella* (1972) 127 CLR 454; *Ronnoc Finance v Spectrum Network Ltd* (1997) NSWLR 624.

EXPECTATION DAMAGES

Direct and consequential losses

[26.25] In most cases, *expectation* damages will be based on the lost value of the performance that was promised under the contract. This is why expectation damages are sometimes described as *loss of bargain* damages. Loss of the expected performance is a *direct loss* because it is directly linked to the defendant's breach of contract.

Where a contract is not terminated, expectation damages will commonly represent the difference in value between what the defendant has provided (if anything) and what should have been provided had the defendant complied with the contract. For example, consider a contract for the sale of a truckload of apples at a price of $100. The apples are not of the high quality promised in the contract. If the apples had complied with the contract, their value based on the cost of obtaining equivalent apples would be $200. The poor-quality apples delivered by the defendant have a value of only $150.[19] The damages payable to the buyer would be $50, subject to the limiting principles discussed in Chapter 27.

Where the contract is terminated, expectation damages will usually represent the value of the benefit promised under the contract. For example, consider again a contract for the sale of apples at a price of $100. If the purchaser breaches the contract by failing to accept delivery of the apples, the seller may sell them elsewhere. Assume the seller only resells the apples at a price of $75. The seller may recover $25 to put the seller in the position he would have been in if the contract with the original buyer had been performed. If the seller breaches the contract by failing to deliver the apples, the purchaser may be able to obtain equivalent apples from another source. If equivalent apples were only available at a cost of $175, the purchaser may recover $75 in damages, being the amount that would put the purchaser in the position as if the contract had been performed, again subject to the limiting principles discussed in Chapter 27.

A plaintiff may also be entitled to recover damages as compensation for *consequential losses*. Consequential losses are losses beyond the direct loss of performance which have been incurred by reason of the breach.[20] Consequential losses might include the loss of profit on a subsequent transaction or expenses which have reasonably been incurred by the plaintiff as a result of the breach. For example, consider a contract for the sale of machinery for a factory. If the purchaser breaches the contract by refusing to accept the machinery, the seller may be able to recover as damages not only the direct loss of the contract price but also the cost of storing the machinery after it is rejected by the purchaser. If the seller breaches the contract, the purchaser may be able to recover, in addition to the cost of purchasing alternative machinery, the profits lost through not having the machinery in operation at the time specified in the contract, subject to the limiting principles discussed later in this chapter.

DAMAGES FOR BREACH OF AN OBLIGATION TO BUILD OR REPAIR

[26.30] In cases where the defendant has breached an obligation to build or repair property, the general expectation measure of damages might suggest an award based on the loss of value

19 For another example see *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1.

20 Consequential losses are not the same as losses under the second limb of *Hadley v Baxendale* discussed in Chapter 27: *Environmental Systems Pty Ltd v Peerless Holdings Pty Ltd* [2008] VSCA 26; (2008) 19 VR 358, [93].

of the property. Thus, the award in such cases might represent the difference between the market value of the property without the building or repairs and the value the property would have had if the building or repairs had been carried out in accordance with the contract. However, in some cases, this measure may not be adequate. For example, where the promised work would have a predominantly aesthetic value, the effect on the market value of the property of not having the work done may be nominal. In other cases, the difference between the market value of the property with and without the work being done in accordance with the contract may not cover the cost to the plaintiff of rectifying the defective work. In such cases, courts have sometimes been prepared instead to award damages based on the cost to the plaintiff of rectifying the work to make it conform to the contract specifications. This preparedness to award damages based on the cost of rectification illustrates a concern to put the plaintiff genuinely in the position she or he would be in if the contract had been performed.

In Australia, the leading cases are *Bellgrove v Eldridge*[21] and *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd*.[22] In *Bellgrove v Eldridge*,[23] a builder breached its contract with the owner by building a house substantially at variance with the contractual specifications. The defects were so extreme that the house was unstable. The High Court rejected the builder's argument that the plaintiff's damages should be measured by the difference between the value of the house built and the value that it would have borne if constructed in accordance with the contract. The Court upheld an award of damages for the cost of demolishing the house and erecting one which did comply with the contract. This was the only measure that would genuinely compensate the owner. The Court explained that

> [the owner] was entitled to have a building erected upon her land in accordance with the contract and the plans and specifications which formed part of it, and her damage is the loss which she has sustained by the failure of the [builder] to perform his obligations to her. This loss … can, prima facie, be measured only by ascertaining the amount required to rectify the defects complained of and so give to her the equivalent of a building on her land which is substantially in accordance with the contract.[24]

In *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* (*Tabcorp*)[25] the lease for office premises for a term of ten years contained a covenant by the tenant not to make or permit to be made any substantial alteration or addition to the demised premises without the written approval of the landlord (which was not to be unreasonably withheld or delayed). The tenant applied for consent but was told by the landlord on 11 July 1997 that the application could not be considered before the proposed alterations were examined at a site meeting on 14 July. In "contumelious disregard" for the rights of the landlord,[26] the tenant commenced work on the proposed alterations before the site meeting was held and completed the work without the consent of the landlord. The landlord sued the tenant in the Federal Court. The trial judge awarded damages based on the diminution in the value of the building caused by the new building work, a sum of $34,820. The Full Court of the Federal Court increased the damages to $1.38 million, comprising $580,000 as the cost of restoring the foyer to its

21 *Bellgrove v Eldridge* (1954) 90 CLR 613.

22 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272.

23 *Bellgrove v Eldridge* (1954) 90 CLR 613.

24 *Bellgrove v Eldridge* (1954) 90 CLR 613, 617.

25 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272.

26 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [4].

original condition and $800,000 for rent lost during the restoration period. An appeal to the High Court was dismissed.

The High Court (French CJ, Gummow, Heydon, Crennan and Kiefel JJ) held that the

> Landlord was contractually entitled to the preservation of the premises without alterations not consented to, its measure of damages is the loss sustained by the failure of the tenant to perform that obligation and that loss is the cost of restoring the premises to the condition in which they would have been if the obligation had not been breached.[27]

The High Court referred to the principle of compensation from *Robinson v Harman*[28] and explained that putting the plaintiff in the same position as if the contract had been performed does not mean "as good a *financial* position as if the contract had been performed".[29] The High Court said that:

> In some circumstances putting the innocent party into 'the same situation … as if the contract had been performed' will coincide with placing the party into the same financial situation. Thus, in the case of the supply of defective goods, the prima facie measure of damages is the difference in value between the contract goods and the goods supplied. But as Staughton LJ explained in *Ruxley Electronics Ltd v Forsyth* such a measure of damages seeks only to reflect the financial consequences of a notional transaction whereby the buyer sells the defective goods on the market and purchases the contract goods. The buyer is thus placed in the 'same situation … as if the contract had been performed', with the loss being the difference in market value. However, in cases where the contract is not for the sale of marketable commodities, selling the defective item and purchasing an item corresponding with the contract is not possible. In such cases, diminution in value damages will not restore the innocent party to the 'same situation … as if the contract had been performed'.[30]

In such cases rectification damages will be necessary.

The reasonableness of rectification

[26.35] In *Bellgrove v Eldridge*[31] the High Court stated that the award of rectification damages was subject to the qualification that "the work undertaken be necessary to produce conformity [with the contract], but that also, it must be a reasonable course to adopt".[32] Rectification was reasonable in *Bellgrove v Eldridge* because, by reason of the breach of contract, the foundations of the house were defective and the building was unstable.[33] Accordingly, there was a real and practical necessity for the work to be redone. What is reasonable in any particular case is not measured in purely economic terms; the personal preferences of the plaintiff may be considered.[34] In *Bellgrove v Eldridge*, the High Court gave the example of a room being painted in a different colour from that specified in the contract and suggested that a plaintiff would be entitled to damages for the cost of repainting the room.[35]

27 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [15].
28 *Robinson v Harman* [1848] EngR 135; (1848) 1 Exch 850; 154 ER 363, 855 (Exch), 365 (ER).
29 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8, [13]; (2009) 236 CLR 272.
30 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [13].
31 *Bellgrove v Eldridge* (1954) 90 CLR 613, 618.
32 *Bellgrove v Eldridge* (1954) 90 CLR 613, 616.
33 *Bellgrove v Eldridge* (1954) 90 CLR 613, 618–9.
34 *Bowen Investments Pty Ltd v Tabcorp Holdings* [2008] FCAFC 38; (2008) 166 FCR 494, [29].
35 *Bellgrove v Eldridge* (1954) 90 CLR 613, 616.

In *Tabcorp*, the tenant attempted to resist the landlord's claim for rectification damages by arguing that rectification was not reasonable or necessary. This was because

> [t]he Tenant contended that the Landlord had never run a case that it valued the foyer for its aesthetic qualities as distinct from its having 'pulling power' as a 'leasing tool', and it relied on the trial judge's implicit finding, based on the resolution of conflicting expert evidence, that the old foyer was no more effective as a leasing tool than the new foyer.[36]

The argument was rejected by the High Court. The High Court quoted Oliver J in *Radford v De Froberville*:[37]

> Now, it may be that, viewed objectively, it is not to the plaintiff's financial advantage to be supplied with the article or service which he has stipulated. It may be that another person might say that what the plaintiff has stipulated for will not serve his commercial interests so well as some other scheme or course of action. And that may be quite right. But that, surely, must be for the plaintiff to judge. Pacta sunt servanda. If he contracts for the supply of that which he thinks serves his interests — be they commercial, aesthetic or merely eccentric — then if that which is contracted for is not supplied by the other contracting party I do not see why, in principle, he should not be compensated by being provided with the cost of supplying it through someone else or in a different way, subject to the proviso, of course, that he is seeking compensation for a genuine loss and not merely using a technical breach to secure an uncovenanted profit.[38]

The High Court in *Tabcorp* thought that the test of "unreasonableness" precluding rectification damages would only be satisfied "by fairly exceptional circumstances".[39] In *Bellgrove v Eldridge*, the High Court said that it would not be reasonable to require rebuilding of a house where the contract provided for second-hand bricks and new bricks were used instead.[40] Similarly, in *Brewarrina Shire Council v Beckhaus Civil Pty Ltd*,[41] rectification of the dry side of a levee was unreasonable when the levee would adequately perform its function and the rectification work would not increase its capacity to repel floodwater.

An award of damages for the cost of rectification may be unreasonable where the cost of rectification would be wholly disproportionate to the benefit obtained.[42] In the English case of *Ruxley Electronics and Constructions Ltd v Forsyth*,[43] the builders contracted to build a swimming pool for the respondent in his garden. The contract specified that the pool should have a diving area seven feet six inches deep. When completed, the pool was suitable for diving but was only six feet deep. The estimated cost of rebuilding the pool was £21,560. The House of Lords rejected the respondent's claim for damages for the cost of rectifying the defect. The House of Lords considered that the expenditure required to rectify the defect was out of all proportion to the benefit that would be obtained by the respondent. Damages were instead to be based on the diminution in the value of the pool caused by the breach.[44]

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36 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [16].

37 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [16].

38 *Radford v De Froberville* [1977] 1 WLR 1262, 1270.

39 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [18].

40 *Bellgrove v Eldridge* (1954) 90 CLR 613, 618.

41 *Brewarrina Shire Council v Beckhaus Civil Pty Ltd* [2006] NSWCA 361.

42 *Wheeler v Ecroplot Pty Ltd* [2010] NSWCA 61, [81].

43 *Ruxley Electronics and Constructions Ltd v Forsyth* [1996] 1 AC 344.

44 See also *Bellgrove v Eldridge* (1954) 90 CLR 613, 618.

In *Tabcorp*, the High Court discussed *Ruxley Electronics & Construction Ltd v Forsyth* and noted that, on one view, the finding was not consistent with the statement of Oliver J set out above.[45] The High Court also commented that the facts of *Ruxley Electronics & Construction Ltd v Forsyth* were "quite exceptional".[46]

Supervening events preclude rectification

[26.40] Rectification may not be reasonable to achieve the contractual objective where supervening events mean that the rectification work cannot be carried out.[47] For example, in *Central Coast Leagues Club v Gosford City Council*,[48] the rectification work could not be carried out because other, more extensive work had to be carried out in order to comply with later court orders. Giles JA held that the fact the work would not be undertaken gave occasion to conclude that it was not a reasonable course to adopt.

Rectification and sale of the property

[26.45] Sale of the property by the plaintiff need not of itself displace the entitlement to damages according to the rectification measure. This is because the plaintiff may still be under an obligation to rectify the work for the purchaser or may feel morally obliged to do so.[49] However, some courts have suggested that the fact of sale is "one of the circumstances that would have to be considered in relation to the question whether it would be reasonable to effect the remedial work".[50] In *Westpoint Management Ltd v Chocolate Factory Apartments Ltd*, Giles JA explained that:

> If sale of the property to a contented purchaser means that the plaintiff did not think and the purchaser does not think the rectification work needs to be carried out, it may well be found to be unreasonable to carry out, the rectification work.[51]

Whether this approach is consistent with the High Court's suggestion in *Tabcorp* that the circumstances in which rectification damages will be unreasonable must be "exceptional"[52] remains to be seen.

Is it relevant whether the plaintiff intends to carry out the repairs?

[26.50] In some cases of defective building work, the plaintiff may not actually intend to carry out the work required to rectify the building, even though damages are being sought on this basis. Whether the plaintiff's intention should be relevant in assessing damages for the cost of rectification is currently unsettled in Australian law. One view is that the subjective intentions

45 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [18].

46 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [18].

47 *Westpoint Management Ltd v Chocolate Factory Apartments Ltd* [2007] NSWCA 253, [61]; *Cordon Investments Pty Ltd v Lesdor Properties Pty Ltd* [2012] NSWCA 184, [230].

48 (Unreported, Supreme Court of NSW, Giles J, 9 June 1998).

49 *Director of War Service Homes v Harris* (1968) Qd R 275; *De Cesare v Deluxe Motors Pty Ltd* (1996) SASR 28; *Scott Carver Pty Ltd v SAS Trustee Corporation* [2005] NSWCA 462.

50 *Director of War Service Homes v Harris* (1968) Qd R 275, 278 per Gibbs J, with whom the other members of the Full Court agreed.

51 *Westpoint Management Ltd v Chocolate Factory Apartments Ltd* [2007] NSWCA 253, [61].

52 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [18].

of the plaintiff are immaterial. In *Bellgrove v Eldridge*, having held that the remedial work of demolition and re-erection was reasonable, the High Court said:

> It was suggested during the course of argument that if the respondent retains her present judgment and it is satisfied, she may or may not demolish the existing house and re-erect another. If she does not, it is said, she will have a house together with the cost of erecting another one. To our mind this circumstance is quite immaterial and is but one variation of a feature which so often presents itself in the assessment of damages in cases where they must be assessed once and for all.[53]

The concern behind this view is that an inquiry into a plaintiff's subjective intentions is not part of the ordinary approach to contract damages and, moreover, use of this sort of criterion will produce commercial uncertainty.[54]

A different approach, taken by English courts, is that the plaintiff's intention actually to rectify is relevant in assessing damages for the cost of rectification, but only to the question of whether the award is reasonable.[55] This approach focuses on the compensatory nature of damages, namely that "if the plaintiff will not put itself in the position it would have been in had the contract been performed, the plaintiff should not be given the means of doing so".[56] In *Westpoint Management Ltd v Chocolate Factory Apartments Ltd*, Giles JA, with whom McColl and Campbell JJA agreed, also preferred the view that the plaintiff's intention to carry out rectification is relevant to the reasonableness of the award. Giles JA explained that:

> An intention not to carry out the rectification work will not of itself make carrying out the work unreasonable, but it may be evidentiary of unreasonableness; if the reason for the intention is that the property is perfectly functional and aesthetically pleasing despite the non-complying work, for example, it may well be found that rectification is out of all proportion to achievement of the contractual objective or to the benefit to be thereby obtained.[57]

The High Court did not directly address the issue in *Tabcorp*. The Court did, however, affirm that "the diminution in value measure of damages will only apply where the innocent party is 'merely using a technical breach to secure an uncovented profit' ".[58] This statement might suggest that the intention of the plaintiff not to proceed with rectification is relevant only so far as it provides evidence of such conduct.[59]

RELIANCE DAMAGES

Reliance loss as part of expectation damages

[26.55] A party may incur significant costs in reliance upon a contract being performed. For example, a party contracted to perform building work may purchase equipment and materials suitable only for that work. This expenditure will be wasted if, by reason of the defendant's breach, the contract is not performed.

53 *Bellgrove v Eldridge* (1954) 90 CLR 613, 620.

54 *Bowen Investments Pty Ltd v Tabcorp Holdings* [2008] FCAFC 38; (2008) 166 FCR 494, [84]–[86].

55 *Tito v Waddell (No 2)* [1977] Ch 106, 332; *Ruxley Electronics and Constructions Ltd v Forsyth* [1996] 1 AC 344, 359, 372–3.

56 *Westpoint Management Ltd v Chocolate Factory Apartments Ltd* [2007] NSWCA 253, [55].

57 *Westpoint Management Ltd v Chocolate Factory Apartments Ltd* [2007] NSWCA 253, [61].

58 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [17].

59 *Unique Building Pty Ltd v Brown* [2010] SASC 106, [91]–[93].

A plaintiff will not normally need to make a separate claim to be awarded damages to recover the costs incurred in reliance on a contract being performed. Such losses will usually be covered in the ordinary award of expectation damages. In a contract for goods or services, the plaintiff will usually have calculated the contract price (*gross receipts* for those goods or services to allow him or her to recover both the expenditure expected to be incurred in performing, or preparing to perform, the contract (the *costs of performance*) and a margin of profit over and above the expenses of performance (the *net profit*).[60] Where a plaintiff terminates such a contract by reason of the defendant's breach, the plaintiff will usually recover as expectation damages an amount equivalent to the price payable under the contract. If the contract is terminated before the plaintiff completes performance, the plaintiff may be saved some costs that would otherwise have been incurred in performing his or her obligations. So that the plaintiff is not over-compensated, these saved costs of performance will be deducted from an award of expectation damages based on the contract price.[61]

For example, consider a contract for the sale of machinery for a factory. If the cost to the seller of constructing the machinery is $8,000, then the contract price is likely to be an amount above $8,000, perhaps $10,000. If the purchaser breaches the contract by refusing to accept the machinery, the seller's damages, measured on an expectation basis, will generally be the contract price, which will cover the cost of constructing the machinery ($8,000), plus the net profit lost on the sale ($2,000). If the seller has not yet constructed the machinery when the contract is terminated, the seller's damages would only be $2,000, being the contract price less the saved costs of construction (and subject to the limiting principles discussed in Chapter 27).

Reliance damages where the plaintiff cannot prove his or her expectation loss

[26.60] In some cases, a plaintiff may not be able to prove the benefit he or she expected to gain from performance of the contract. In such a case, the court will not be able to award expectation damages based on the loss of that expected benefit. Nonetheless, it may seem unfair for the plaintiff to recover only nominal damages. In cases where the plaintiff is unable to prove the value of the benefit expected from performance of the contract, courts have held that the plaintiff may instead be able to recover damages compensating the plaintiff for expenditure incurred in reasonable reliance on the contract being performed.[62] Such damages are termed *reliance damages* or *wasted expenditure damages*.

The award of reliance damages is illustrated by the decision of the High Court in *McRae v Commonwealth Disposals Commission*.[63] In this case, the plaintiffs entered into a contract with the Commonwealth Disposals Commission for the purchase of a wrecked oil tanker that they intended to salvage. The tanker was described as "wrecked on Jourmaund Reef". The plaintiffs were also given coordinates of the supposed wreck. In fact, there was no oil tanker

60 Courts sometimes use the term "profit" to refer to the contract price or gross receipts under a contract, which will include both the costs of performance and the net profit. On these concepts see further Campbell and Halson, "Expectation and Reliance: One Principle or Two" (2015) 32 *Journal of Contract Law* 231.

61 See further *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 100.

62 *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 81–90, 126–8, 143, 154–7, discussed further below at [26.65]. See generally Bridge, "Expectation Damages and Uncertain Future Losses" in Beatson and Friedmann (eds), *Good Faith and Fault in Contract Law* (1995), p 427.

63 *McRae v Commonwealth Disposals Commission* (1951) 84 CLR 377.

lying anywhere near this location. However, before discovering this fact, the plaintiffs incurred considerable expenditure in fitting out a salvage operation.

The High Court held that the Commonwealth Disposals Commission had breached an implied promise that the tanker existed. An issue of the appropriate damages arose. The difficulty for the plaintiffs was in establishing what loss they had suffered. It was impossible to place a value on the salvage of a non-existent tanker. The Court accepted that the plaintiffs had incurred the expense of mounting a salvage operation on the basis of the Commission's promise that there was a tanker. There being no tanker, the burden was thrown on the Commission to establish that, if there had been a tanker, the expense incurred would have been wasted.[64] This the Commission could not do. Accordingly, the Court considered that the plaintiffs were entitled to recover damages for the breach of contract measured by reference to the expenditure reasonably incurred and wasted in reliance on the Commission's promise.

Loss making contracts

[26.65] Reliance damages will not be available where the defendant can establish that, even if the contract had been fully performed, the plaintiff would not have recouped his or her expenditure incurred in reliance on the contract being performed. In this sense, the onus may be said to be on the defendant to show that the benefit expected from performance would not have covered the plaintiff's costs of performance or, more simply, that the plaintiff had entered into a loss-making contract.[65] The reason a plaintiff will not be awarded damages to cover wasted expenditure in the case of a loss-making contract is that an award of damages should not put the plaintiff in a better position than he or she would have been in had the contract been performed.[66]

Where a defendant proves that the plaintiff would not, if the contract had been performed, have earned enough to cover the costs of performance, the plaintiff will be entitled to damages only to the extent of his or her expected benefit under the contract. For example, consider a case similar to *McRae v Commonwealth Disposals Commission*,[67] in which the tanker did, in fact, exist, but not at the location advised by the Commission. Assume also that, due to the speculative nature of the venture, the plaintiffs were unable to show what their profit would have been if they had salvaged the tanker. In such a case, the plaintiff would be entitled to claim reliance damages subject to the Commission showing that the contract would have been loss-making. If the Commission had been able to show that, even if the tanker had been salvaged, the value of the salvage would not have covered all of the plaintiffs' costs in undertaking the salvage, then the plaintiffs' damages would have been reduced. If the cost of the salvage was $6,000, but the return from the salvage was only likely to be $4,000, then the plaintiffs would be restricted to recovering damages of $4,000.

More complicated issues involving loss-making contracts arose in *Commonwealth v Amann Aviation Pty Ltd*.[68] The case involved a contract under which Amann was to provide coastal surveillance flights for the Commonwealth over a period of three years. The Commonwealth

64 *McRae v Commonwealth Disposals Commission* (1951) 84 CLR 377, 414.

65 See different views on the nature of the onus in *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 86–90; 105–8, 137–43, 154, 165–6.

66 *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 82.

67 *McRae v Commonwealth Disposals Commission* (1951) 84 CLR 377.

68 *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64.

wrongfully terminated the contract. Amann treated this action as a repudiation of the contract, elected to terminate the contract and then claimed damages. In order to carry out the contract, Amann had incurred heavy expenditure, primarily in acquiring and fitting out aircraft. Amann required a significantly longer period of operation than three years to recoup this expenditure.

Amann's ability to recoup the initial expenditure and to make a profit depended on the contract being renewed for a further term after the initial three-year period. Amann could not prove that the contract would have been renewed. This meant that if damages had been assessed on an expectation basis, Amann would only have recovered the receipts owing to it under the original contract. Once the amounts saved by Amann in not continuing with the performance of the contract had been deducted, this amount would not have covered the expenditure already incurred by Amann.[69] However, Amann claimed that, in assessing the benefits it would have gained from performance of the contract, the prospect of renewal of the original contract should be taken into account. Given that Amann could not prove the value of what it expected to gain from renewal of the contract, Amann instead sought reliance damages to cover its wasted expenditure.

To defeat Amann's claim for reliance damages, the Commonwealth needed to show that the expenditure incurred by Amann would have been wasted even if the original contract had been performed. Since it was under no obligation to renew the contract with Amann, the Commonwealth argued that the prospect of renewal should not be taken into account in determining whether or not Amann would have recouped its expenditure. This argument was rejected by the majority of justices in the High Court.[70] As Mason CJ and Dawson J noted, Amann would be in a good position to secure renewal because it would "have had the necessary equipment … facilities and personnel in place at the relevant time".[71] The Court also considered that the Commonwealth could not show that the value of the prospect of renewal (even though not a certainty), when combined with the remuneration under the original contract, would not cover the expenditure incurred by Amann.[72] Accordingly, Amann was entitled to substantial reliance damages.

No double compensation

[26.70] A plaintiff will not recover an award of both reliance damages and expectation damages. Such an award would over-compensate a plaintiff. This is because, in most cases, expectation damages based on the contract price will cover both the costs of performing the contract and a margin of net profit.

Reasonable reliance?

[26.75] In discussing reliance damages, the courts often refer to "reasonable expenditure" incurred by the plaintiff in reliance on the contract being performed.[73] However, courts do not seem to have treated the reasonableness of the plaintiff's expenditure as a separate element in deciding whether or not reliance damages should be awarded. Reasonableness of the plaintiff's

69 See, in particular, *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 108.

70 *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 90–2, 111–12, 130, 146, McHugh J dissenting.

71 *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 90.

72 *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 94, 113, 131.

73 See, eg, *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64.

expenditure might be considered in relation to remoteness of damage. It might be argued that expenditure that was unreasonably incurred by a plaintiff would be unlikely to have been contemplated by the parties and is therefore too remote to be recovered as damages.[74]

Are reliance damages just a form of expectation damages?

[26.80] Expectation damages seek to put the plaintiff in the position he or she would have been in if the contract had been performed. Reliance damages might seem to proceed on a different basis. By compensating the plaintiff for costs incurred in reliance on the contract being performed, reliance damages return the plaintiff to the position he or she would have been in if the contract had not been made.[75] However, in *Commonwealth v Amann Aviation Pty Ltd*,[76] a number of members of the Court considered that reliance damages were consistent with the principle governing expectation damages. Mason CJ and Dawson J explained that where a plaintiff cannot prove the profit lost by reason of the breach of contract,

> the law considers the just result in such a case is to allow a plaintiff to recover such expenditure as is reasonably incurred in reliance on the defendant's promise. In this case, the law assumes that a plaintiff would at least have recovered his or her expenditure had the contract been fully performed.[77]

The assumption that a plaintiff would at least have recouped the expenditure incurred in reliance on the contract being performed is based on the view that a plaintiff would be unlikely to have entered into a contract that would not have recouped these costs.[78] If we accept this assumption, reliance damages may be regarded as a form of expectation damages. Courts may be seen as using reliance damages to put the plaintiff in the position he or she would have been in had the contract been performed by at least compensating the plaintiff for the wasted costs of performance which he or she would have expected to recoup if the contract had been fully performed. This view of reliance damages as a form of expectation damages is supported by the refusal of courts to award reliance damages where the contract would have been loss-making if it had been performed.

On the other hand, there is a significant difference between reliance damages compensating wasted costs of performance and expectation damages, in the ordinary sense, which compensate a plaintiff for the loss of the benefit expected under the contract. This difference lies in the proof demanded from a plaintiff. To recover expectation damages in the ordinary sense, a plaintiff is required to prove on the balance of probabilities that he or she would have made some benefit or profit if the contract had been performed. To recover reliance damages, the plaintiff is not required to prove his or her loss. Rather, as we have seen, the onus effectively shifts to the defendant who, to avoid paying an award of reliance damages, is required to show that, if the contract had been performed, the plaintiff would not have recouped his or her expenditure. In allowing the recovery of reliance damages where a plaintiff cannot establish his or her expectation loss, the law is making a concession to a plaintiff with evidentiary

74 See *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377.

75 See *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 86.

76 *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64.

77 *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 86, also 107, 126, 142–3, 155, 166. But cf Treitel, "Damages for Breach of Contract in the High Court of Australia" (1992) 108 *Law Quarterly Review* 226, 229.

78 But cf *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 165.

difficulties. On this ground, we might treat reliance damages as a special category of damages that, for reasons of justice, allow a concession to a plaintiff who would otherwise be denied substantial damages.

DAMAGES FOR LOSS OF A CHANCE

[26.85] In some cases, a plaintiff may not be able to show, on the balance of probabilities, that he or she has lost a benefit by reason of the defendant's breach of contract. However, the plaintiff may be able to show that he or she has lost the chance or the opportunity of obtaining a benefit. This will be the case where the likelihood of the benefit being obtained depends on a contingency, rather than merely on the parties completing their performance under the contract. Although not a certainty, the chance of a benefit may still be of value. Thus, courts have been prepared to award damages compensating a plaintiff for the loss of a chance.[79] Damages for the loss of a chance are consistent with the compensation principle in *Robinson v Harman*[80] and may be seen as a form of expectation damages. Damages for loss of a chance aim to put the plaintiff in the position he or she would have been in if the contract had been performed in cases where performance would have provided the plaintiff with a chance of a benefit.

Damages for loss of a chance have been awarded where the breach of contract has deprived the plaintiff of a chance to succeed in a contest or game.[81] In *Howe v Teefy*,[82] the defendant leased a racehorse to the plaintiff, who was a trainer, for a period of three years. After about three months, the defendant took the horse away from the plaintiff without justification. The plaintiff brought an action for breach of contract and claimed damages for the loss of opportunity to win prizes with the horse, to place and win bets on the horse and to make profits from supplying information to other people. The Full Court of the Supreme Court in New South Wales declined to interfere with the jury's award of £250 in damages for these losses.

Damages for loss of a chance may also be awarded for the loss of the chance to pursue a potentially successful commercial opportunity.[83] This is illustrated by *Commonwealth v Amann Aviation Pty Ltd*.[84] As we have seen, the High Court was prepared to take the prospect of renewal of an aircraft surveillance contract into account in calculating the damages available to Amann.[85] The majority of the justices considered that the prospect of renewal was an opportunity of real commercial value that would have been contemplated by the parties as accruing to Amann by reason of its performance of the contract.[86]

79 See further *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 118; Bridge, "Expectation Damages and Uncertain Future Losses" in Beatson and Friedman (eds), *Good Faith and Fault in Contract Law* (1995).

80 *Robinson v Harman* (1848) 1 Ex 850; 154 ER 363, 855: see [26.10].

81 See, eg, *Chaplin v Hicks* [1911] 2 KB 786; *Howe v Teefy* (1927) 27 SR (NSW) 301.

82 *Howe v Teefy* (1927) 27 SR (NSW) 301.

83 *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 92, 102–4, 189–90.

84 *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64.

85 Mason CJ, Brennan, Dawson and Toohey JJ, McHugh J dissenting.

86 *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 90–2, 111–2, 130, 146. See also *Sellars v Adelaide Petroleum NL* (1994) 179 CLR 332, 349; *Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd* (1991) 24 NSWLR 1, 25; *Cadoks Pty Ltd v Wallace Westley & Vigar Pty Ltd* [2000] VSC 167; [2000] 2 VR 531, [192]. On damages for the chance of renewal of an employment contract compare the different views expressed in

Quantifying the loss of a chance

[26.90] Quantifying the damages awarded to compensate a plaintiff for the loss of a chance will inevitably involve some speculation. To obtain damages for the loss of a chance, the plaintiff must show on the balance of probabilities that he or she lost a chance of some value.[87] Once it is shown that the plaintiff has lost a chance of some value, it will not matter that the value of the lost chance may only be estimated by reference to a degree of probability which is less than 50 per cent and indeed may involve an element of speculation.[88] In quantifying the damages, the court will adjust the award to reflect the fact there was only a chance of success.[89] Accordingly, the value of the benefit the plaintiff had a chance of obtaining may be discounted by the probability of success. For example, the loss of a 25 per cent chance of obtaining $80 might result in a damages award of $20.

SUPERVENING EVENTS

[26.95] Courts will reduce the plaintiff's damages for loss of an expected future benefit by the probability of events adverse to the plaintiff.[90] While damages are normally assessed at the date of the breach, if, after that time but before the court sets the damages, an event that would reduce the loss suffered by the plaintiff actually occurs, then the court will have regard to that event in quantifying the damages awarded to a plaintiff.[91] For example, in *G&A Lanteri Nominees Pty Ltd v Fishers Stores Consolidated Pty Ltd*,[92] the landlord terminated a lease for the lessee's breach of contract and sued for the loss of the bargain, being the rent due over the term of the lease. The landlord had, however, sold the property before the date of the trial and this sale was taken into account in calculating damages.

Will a court take into account factors that would have led the defendant in any event to cancel a contract? The leading case is *The Golden Victory*,[93] in which a charterer renounced a seven-year charter-party and returned the ship to its owner when there were almost four years left to run on the charter. Three days later the owner accepted the repudiation and claimed the difference between the contract and market rates of hire for the remaining charter period. The contract gave either party the right to cancel the charter if war broke out between two or more of a number of countries. On 20 March 2003, 14 months after the repudiation was accepted, the Second Gulf War commenced. This event would have enabled either party to cancel if

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Walker v Citigroup Global Markets Australia Pty Limited [2006] FCAFC 101; (2006) 233 ALR 687 and *Murray Irrigation Ltd v Balsdon* [2006] NSWCA 253; (2006) 67 NSWLR 73.

87 *Sellars v Adelaide Petroleum NL* (1994) 179 CLR 332, 359; *Sensis Pty Ltd v McMaster-Fay* [2005] NSWCA 163; cf *Bak v Glenleigh Homes Pty Ltd* [2006] NSWCA 10, [74].

88 *Sellars v Adelaide Petroleum NL* (1994) 179 CLR 332, 355.

89 *Malec v J C Hutton Pty Ltd* (1990) 169 CLR 638, 643; *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 114, 131–2, 146–7, 176–7; *Sellars v Adelaide Petroleum NL* (1994) 179 CLR 332, 350, 368. See also *Fightvision Pty Ltd v Onisforou* [1999] NSWCA 323; (1999) 47 NSWLR 473.

90 *TCN Channel 9 Pty Ltd v Hayden Enterprises Pty Ltd* (1989) 16 NSWLR 130, 155G–156C; *Walker v Citigroup Global Markets Australia Pty Limited* [2006] FCAFC 101; (2006) 233 ALR 687 at [84].

91 *Wenham v Ella* (1972) 127 CLR 454, 474; *Golden Strait Corporation v Nippon Yusen Kubishika Kaisha* [2007] UKHL 12; [2007] 2 AC 363; *Bunge SA v Nidera BV* [2015] UKSC 43.

92 *G&A Lanteri Nominees Pty Ltd v Fishers Stores Consolidated Pty Ltd* [2007] VSCA 4.

93 *Golden Strait Corporation v Nippon Yusen Kubishika Kaisha* [2007] UKHL 12; [2007] 2 AC 363. See also *McCrohon v Harith* [2010] NSWCA 67, [54], [57]–[59]; *Janos v Chama Motors Pty Ltd* [2011] NSWCA 238, [35], [39]–[41].

the charter were still subsisting. It was accepted that the charterer would have cancelled at this time if the charter had remained on foot. The majority in the House of Lords held that the damages paid to the ship owner should be reduced to take into account the right of early termination.

The approach has been controversial: garnering both strong support[94] and criticism[95] from the scholarly community. The criticism generally centres on the loss of commercial certainty caused by departing from the clear signal sent by the ordinary rule that assesses damages on the date of breach. Nonetheless, the majority in the *Golden Victory* held that the ordinary rule should not be applied in a case where subsequent events establish the contract would have in any event been brought to an end because a plaintiff seeking damages for breach of contract should not be placed in a better position than if the contract had been performed.[96] In *Bunge SA v Nidera BV* the UK Supreme Court reaffirmed the principle that events subsequent to termination must be taken into account in the assessment of contract damages.[97] This was on the ground that while commercial certainty was undoubtedly important, it could "rarely be thought to justify an award of substantial damages to someone who has not suffered any loss".[98] Lord Toulson (with whom Lord Neuberger, Lord Mance and Lord Clarke agreed) said:

> Should the assessment be made on the facts as known at the date of the assessment or should the tribunal apply a retrospective assessment of how the chances would have appeared at the date of the repudiation? I see no virtue in such circumstances in the court attempting some form of retrospective assessment of prospective risk when the answer is known. To do so would run counter to the fundamental compensatory principle. In *The Golden Victory* Lord Bingham acknowledged that the saying "you need not gaze into the crystal ball when you can read the book" is in many contexts a sound approach in law as in life.[99]

GAINS-BASED DAMAGES

[26.100] In some cases, a defendant who breaches a contract may benefit from that breach without the plaintiff having suffered any easily apparent or quantifiable loss on which expectation damages may be based. For example, the defendant may be saved the cost of performing the contract or of performing to the standard required by the contract.[100] Or the defendant may also make a profit through pursuing a course of action prohibited by the contract.[101] In these kinds of cases, the apparent absence of a loss suffered by the plaintiff

94 See Capper, "A '*Golden Victory*' for Freedom of Contract" (2008) 24 *Journal of Contract Law* 176; Carter and Peden, "Damages Following Termination for Repudiation: Taking Account of Later Events" (2008) 24 *Journal of Contract Law* 145; Winterton, "*Clark v Macourt*: Defective Sperm and Performance Substitutes in the High Court of Australia" (2014) 38 *Melbourne University Law Review* 755, 769.

95 See Morgan, "A Victory for 'Justice' over Commercial Certainty" (2007) 66 *Cambridge Law Journal* 263; Reynolds, "*The Golden Victory* — A Misguided Decision" (2008) 38 *Hong Kong Law Journal* 333; Lord Mustill, "*The Golden Victory* — Some Reflections" (2008) 124 *Law Quarterly Review* 569; Harder, "The Exculpation of Repudiating Parties by a Right to Terminate a Contract" [2009] *Journal of Business Law* 679.

96 *Golden Strait Corporation v Nippon Yusen Kubishika Kaisha* [2007] UKHL 12; [2007] 2 AC 363, [35], [78].

97 *Bunge SA v Nidera BV* [2015] UKSC 43. See also Yip and Goh, "The Compensatory Principle: A Golden Victory for a New Certainty" [2016] (4) *Journal of Business Law* 335.

98 *Bunge SA v Nidera BV* [2015] UKSC 43, [23] (Lord Sumption).

99 *Bunge SA v Nidera BV* [2015] UKSC 43, [86].

100 See, eg, *Tito v Waddell (No 2)* [1977] Ch 106.

101 See, eg, *Attorney General v Blake* [2001] 1 AC 268; *Experience Hendrix LLC v PPX Enterprises Inc* [2003] EWCA Civ 323; [2003] 1 All ER (Comm) 830.

would seem to rule out compensatory damages. A number of scholars have advocated that, in appropriate cases, the plaintiff should be awarded damages based on the gain to the defendant.[102] There are two kinds of gains-based damages: *restitutionary* damages and *disgorgement* or *account of profit* damages. Neither category of damages has been recognised in Australia. They are established in England, although the line of cases that previously were often treated as involving restitutionary damages have recently been characterised by the Supreme Court as based on a category of compensatory damages, described as *user* or *negotiation* damages.[103]

Negotiating or user damages

[26.105] Restitutionary damages are damages which require a defendant to give back a benefit transferred from the plaintiff. "They focus on the benefit received by the defendant rather than any loss suffered by the [plaintiff]".[104] Until recently, the kind of case that illustrated the potential for an award of restitution damages for breach of contract was *Wrotham Park Estate Co Ltd v Parkside Homes Ltd ("Wrotham Park")*.[105] In this case, a developer built housing on land in deliberate breach of a restrictive covenant in favour of the plaintiffs' land. The plaintiffs sought a mandatory injunction to pull the houses down, but this was refused. The value of the plaintiff's land had not been diminished which meant that substantial compensatory damages were not available. Brightman J considered that damages under *Lord Cairns' Act* instead of an injunction should be assessed by reference to the sum that might reasonably have been demanded by the plaintiff for relaxing the covenant, namely 5 per cent of the developer's anticipated profit.[106]

Until recently, *Wrotham Park* had been treated as illustrating the award of "restitutionary damages" based on a reasonable fee payable to the plaintiff for breaching the covenant.[107] Yet another approach would treat the award as a partial disgorgement of the profit made by the defendant through the breach of contract.[108] The award of a "reasonable" fee for the relaxation of the restrictive covenant also might be reconciled with compensatory damages by treating the award as compensation to the plaintiff for a "lost opportunity to bargain".[109] In

102 See, eg, Jones, "The Recovery of Benefits Gained from a Breach of Contract" (1983) 99 *Law Quarterly Review* 443; Birks, "Profits of Breach of Contract" (1993) 109 *Law Quarterly Review* 518. But cf Mitchell, "Remedial Inadequacy in Contract and the Role of Restitutionary Damages" (1999) 15 *Journal of Contract Law* 133.

103 *One Step (Support) Ltd v Morris-Garner* [2018] UKSC 20; [2018] 2 WLR 1353; *Prudential Assurance Co Ltd v Revenue and Customs Commissioners* [2018] UKSC 39; [2018] 3 WLR 652; *Lloyd v Google LLC* [2018] EWHC 2599 (QB).

104 Edelman (ed), *McGregor on Damages* (20th ed, 2018), [14.002].

105 *Wrotham Park Estate Co Ltd v Parkside Homes Ltd* [1974] 1 WLR 798. See also *Experience Hendrix LLC v PPX Enterprises Inc* [2003] EWCA Civ 323; [2003] 1 All ER (Comm) 830; *Vercoe v Rutland Fund Management Ltd* [2010] EWHC 424.

106 See also *WWF-World Wide Fund for Nature v World Wrestling Federation Entertainment Inc* [2007] EWCA Civ 286; [2008] 1 WLR 445; *Experience Hendrix LLC v PPX Enterprises Inc* [2003] EWCA Civ 323; [2003] 1 All ER (Comm) 830.

107 See further Edelman, *Gain-Based Damages: Contract, Tort, Equity and Intellectual Property* (2002).

108 Burrows, "Are "Damages on the *Wrotham Park* Basis" Compensatory, Restitutionary or Neither?" in Saidov and Cunnington (eds), *Contract Damages: Domestic and International Perspectives* (2008) 165, p 178; Barnett, *Accounting for Profit for Breach of Contract: Theory and Practice* (2012).

109 Waddams, "Gains Derived from Breach of Contract: Historical and Conceptual Perspectives" in Cunnington and Saidov (eds), *Contract Damages: Domestic and International Perspectives* (2008) 187, p 192. See also

One Step (Support) Ltd v Morris-Garner,[110] and then again in *Prudential Assurance Co Ltd v Revenue and Customs Commissioners*,[111] the English Supreme Court characterised damages in these kinds of cases as compensation for loss, "albeit not loss of a conventional kind".[112] "User" or "negotiating" damages compensate a plaintiff for the loss of the right to "obtain the economic value of the use in question".[113] They are available "where the breach of contract results in the loss of a valuable asset created or protected by the right which was infringed".[114] The rationale is that a defendant should not be entitled to "take something for nothing, for which the owner was entitled to require payment".[115]

Edelman explains that recovery of negotiating damages or user damages therefore depends on "whether the breach of contract can be said to deprive the claimant of a valuable asset, including an opportunity, that had been created or was protected by the contractual right".[116] Examples of contractual rights protecting an asset in the form of an opportunity to control that may be compensated by damages include;[117] a restrictive covenant over land,[118] an intellectual property agreement[119] or a confidentiality agreement.[120] The category does not include a contractual right to restrain competition or to protect goodwill.[121]

In *One Step (Support) Ltd v Morris-Garner*,[122] the Morris-Garners sold a business to One Step. The contract required the Morris-Garners not to engage in various forms of competition with One Step for a specified time period. The Morris-Garners breached that agreement. It was difficult for One Step to prove the amount of any loss arising from that breach. Lord Sumption JSC observed that proof of financial loss would require it to show (i) how many customers it would have contracted with if the Morris-Garners had not breached the contract,

Cunnington, "The Measure and Availability of Gain-based Damages for Breach of Contract" in Saidov and Cunnington, *Contract Damages: Domestic and International Perspectives* (2008), Ch 9.

110 *One Step (Support) Ltd v Morris-Garner* [2018] UKSC 20; [2018] 2 WLR 1353.

111 *Prudential Assurance Co Ltd v Revenue and Customs Commissioners* [2018] UKSC 39; [2018] 3 WLR 652.

112 *One Step (Support) Ltd v Morris-Garner* [2018] UKSC 20; [2018] 2 WLR 1353, [30] (Lord Reed, with whom Lady Hale, Lord Wilson, and Lord Carnwath agreed). See generally Burrows, *Remedies for Torts, Breach of Contract and Equitable Wrongs* (4th ed, 2019), pp 321–34.

113 *One Step (Support) Ltd v Morris-Garner* [2018] UKSC 20; [2018] 2 WLR 1353, [30] (Lord Reed, with whom Lady Hale, Lord Wilson, and Lord Carnwath agreed). See generally Burrows, *Remedies for Torts, Breach of Contract and Equitable Wrongs* (4th ed, 2019), pp 321–34.

114 *One Step (Support) Ltd v Morris-Garner* [2018] UKSC 20; [2018] 2 WLR 1353, [92] (Lord Reed, with whom Lady Hale, Lord Wilson, and Lord Carnwath agreed), also [95].

115 *One Step (Support) Ltd v Morris-Garner* [2018] UKSC 20; [2018] 2 WLR 1353, [30] (Lord Reed, with whom Lady Hale, Lord Wilson, and Lord Carnwath agreed). See generally Burrows, *Remedies for Torts, Breach of Contract and Equitable Wrongs* (4th ed, 2019), pp 321–334.

116 Edelman (ed), *McGregor on Damages* (20th ed, 2018), [14.A006].

117 *One Step (Support) Ltd v Morris-Garner* [2018] UKSC 20; [2018] 2 WLR 1353, [92]. Also Edelman (ed), *McGregor on Damages* (20th ed, 2018), [14.A006].

118 See, eg, *Wrotham Park Estate Co Ltd v Parkside Homes Ltd* [1974] 1 WLR 798.

119 See, eg, *Experience Hendrix LLC v PPX Enterprises Inc* [2003] EWCA Civ 323.

120 See, eg, *Vercoe v Rutland Fund Management Ltd* [2010] EWHC 424.

121 *One Step (Support) Ltd v Morris-Garner* [2018] UKSC 20; [2018] 2 WLR 1353, [94], [110]. See also *Prudential Assurance Co Ltd v Revenue and Customs Commissioners* [2018] UKSC 39; [2018] 3 WLR 652; *Lloyd v Google LLC* [2018] EWHC 2599 (QB).

122 *One Step (Support) Ltd v Morris-Garner* [2018] UKSC 20; [2018] 2 WLR 1353. See also Davies, "One Step Backwards: Restricting Negotiating Damages for Breach of Contract" [2018] *Lloyd's Maritime and Commercial Law Quarterly* 433.

(ii) when and for how long those contracts would have been made, (iii) the volume of business covered by those contracts, and (iv) how profitable the additional business would have been for One Step.[123]

The Supreme Court held that user or negotiating damages were not available in this case. The contractual restraints were imposed by "a commercial entity whose only interest in the defendants' performance of their obligations under the covenants was commercial".[124] No separate asset of One Step (Support) had been impaired.[125] It was entitled only to damages based on the financial losses that it had suffered.[126]

Disgorgement damages

[26.110] Disgorgement damages are profit stripping damages. Unlike restitutionary damages, they are not premised on any benefit received by the defendant at the expense of the plaintiff.

Common law courts have traditionally denied the plaintiff's entitlement to disgorgement damages or an account of profits as remedies for a breach of contract.[127] However, there are now a number of English cases supporting the award of gains based damages for breach of contract in "exceptional" cases.[128] Disgorgement damages will typically lie where the defendant is subject to "a contractual duty not to profit from an act, not to be in a position of conflict, or to act in the best interests of the other party".[129]

The possibility of a plaintiff obtaining disgorgement damages, or an account of profits for breach of contract, was accepted by the House of Lords in *Attorney-General v Blake*.[130] Blake, the defendant, was a former member of the British Secret Intelligence Service (SIS). In 1944, he signed an undertaking not to divulge any official information gained as a result of his employment. However, the defendant went on to disclose valuable secret information to the Soviet Union. In 1961, he was convicted of spying and sentenced to 42 years imprisonment. In 1966, he escaped and went to live in Moscow. In 1989, he wrote an autobiography, much of which was based on information he acquired as a member of the SIS. The defendant entered into a publishing contract under which he was to obtain three payments of £50,000. The Attorney-General brought an action against the defendant, essentially to prevent him from profiting from the publication of his book. The House of Lords ordered the defendant to account to the plaintiff for the profits obtained from his breach of contract.[131]

Lord Nicholls, with whom the majority of the Law Lords agreed, preferred to avoid the "unhappy" expression "restitutionary damages".[132] Lord Steyn explained that it was not traditional to describe a claim for restitution as damages.[133] Lord Nicholls relied instead on

123 *One Step (Support) Ltd v Morris-Garner* [2018] UKSC 20; [2018] 2 WLR 1353, [105] (Lord Sumption JSC).

124 *One Step (Support) Ltd v Morris-Garner* [2018] UKSC 20; [2018] 2 WLR 1353, [98].

125 *One Step (Support) Ltd v Morris-Garner* [2018] UKSC 20; [2018] 2 WLR 1353.

126 *One Step (Support) Ltd v Morris-Garner* [2018] UKSC 20; [2018] 2 WLR 1353.

127 See, eg, *Tito v Waddell (No 2)* [1977] Ch 106, 332; *Surrey County Council v Bredero Homes Ltd* [1993] 1 WLR 1361.

128 See Barnett, *Accounting for Profit for Breach of Contract: Theory and Practice* (2012).

129 See E Edelman (ed), *McGregor on Damages* (20th ed, 2018), [15.009].

130 *Attorney-General v Blake* [2001] 1 AC 268.

131 Lord Nicholls of Birkenhead, with whom Lord Goff of Chieveley and Lord Browne-Wilkinson agreed, Lord Steyn, Lord Hobhouse of Woodborough dissenting.

132 *Attorney-General v Blake* [2001] 1 AC 268, 284.

133 *Attorney-General v Blake* [2001] 1 AC 268, 291.

the equitable remedy of an account of profits. An account of profits is a remedy given in equity for an equitable wrong, for example, breach of fiduciary duty. Lord Nicholls considered that there was no reason why an account of profits should be ruled out as a remedy for breach of contract.[134] In some cases, it might be just and equitable that a defendant retains no benefit from his or her breach of contract.[135]

Lord Nicholls was unwilling to prescribe any fixed rules on when the remedy would be available, preferring in each case to have regard to all of the circumstances.[136] Lord Nicholls did, however, indicate that an account of profits for breach of contract would only be appropriate in exceptional circumstances where the traditional remedies proved to be inadequate.[137] Lord Nicholls stated that a useful general guide "is whether the plaintiff had a legitimate interest in preventing the defendants profit making activity and, hence, in depriving him of his profit".[138]

The majority of the House of Lords considered that allowing the Crown to recover the defendant's profits arising from the breach of contract was an appropriate remedy in this case for a number of reasons. In particular, Lord Nicholls and Lord Steyn considered that the defendant's undertaking to keep the information confidential was closely akin to a fiduciary obligation.[139] Account of profits is the standard remedy for such a breach by a fiduciary. The majority also considered that the Crown had a legitimate interest in preventing the defendant from profiting from the disclosure of official information, in that members of the SIS should not have a financial incentive to breach their undertakings of confidentiality.[140]

The exceptional nature of full disgorgement of profits as a response to breach of contract emphasised by the House of Lords in *Attorney-General v Blake* has led to the award being refused in subsequent cases in favour of either partial disgorgement or restitutionary damages.[141]

Gains-based damages in Australia

[26.115] The approach taken by the House of Lords in *Attorney-General v Blake*[142] was considered in Australia by the Federal Court in *Hospitality Group Pty Ltd v Australian Rugby Union Ltd*.[143] Hill and Finkelstein JJ held that disgorgement of profits — which look to the gain made by the defendant, rather than the loss of the benefit of performance expected by the plaintiff — would be inconsistent with current principles laid down by the High Court for awarding damages for breach of contract, which are based on a goal of compensation.[144]

134 *Attorney-General v Blake* [2001] 1 AC 268, 284.

135 *Attorney-General v Blake* [2001] 1 AC 268, 285.

136 *Attorney-General v Blake* [2001] 1 AC 268, 285.

137 *Attorney-General v Blake* [2001] 1 AC 268, 285, also 291.

138 *Attorney-General v Blake* [2001] 1 AC 268, 285.

139 *Attorney-General v Blake* [2001] 1 AC 268, 287, 292.

140 *Attorney-General v Blake* [2001] 1 AC 268, 287, 292.

141 See, eg, *WWF-World Wide Fund for Nature v World Wrestling Federation Entertainment Inc* [2007] EWCA Civ 286; [2008] 1 WLR 445; *Experience Hendrix LLC v PPX Enterprises Inc* [2003] EWCA Civ 323; [2003] 1 All ER (Comm) 830.

142 *Attorney-General v Blake* [2001] 1 AC 268.

143 *Hospitality Group Pty Ltd v Australian Rugby Union Ltd* [2001] FCA 1040; (2001) 110 FCR 157.

144 *Hospitality Group Pty Ltd v Australian Rugby Union Ltd* [2001] FCA 1040; (2001) 110 FCR 157, 196. Compare Edelman, "Fiduciaries and Profit Disgorgement for Breach of Contract" (2012) 6 *Journal of Equity* 115.

WHY ARE EXPECTATION DAMAGES THE MAIN MEASURE OF DAMAGES IN CONTRACT?

Fuller and Perdue

[26.120] In a seminal article on contract law written in 1936,[145] Fuller and Perdue identified three principal purposes that might be pursued in awarding contract damages.[146] First, damages might protect the plaintiff's "restitution interest", by requiring a defendant to disgorge any value conferred by the plaintiff on the defendant in reliance on the contract being performed. Secondly, damages might be awarded with the purpose of protecting the "reliance interest", by compensating the plaintiff for harm suffered as a result of reliance on the defendant's promise.[147] Thirdly, damages might be awarded to protect the expectation interest, by putting the plaintiff in as good a position as he or she would have been in if the defendant had performed the contract.[148]

Modern contract law favours expectation damages as the principal remedy for breach of contract. However, Fuller and Perdue argued that "ordinary standards of justice" would regard the expectation interest as having the weakest case for protection:

> The 'restitution interest', involving a combination of unjust impoverishment with unjust gain, presents the strongest case for relief …
>
> On the other hand, the promisee who has actually relied on the promise, even though he may not thereby have enriched the promisor, certainly presents a more pressing case for relief than the promisee who merely demands satisfaction for his disappointment in not getting what was promised him.[149]

Fuller and Perdue then considered why the normal measure of damages in contract law is aimed at protecting the plaintiff's expectation of performance. Three main reasons were suggested. Firstly, they suggested that an award of expectation damages might be justified as allowing a present value to be placed on the expectation of future performance.[150] This ability to place a present value on a promise about the future, an *executory promise*, is an essential feature of the credit economy. Fuller and Perdue also argued that the objection to this kind of justification is that an executory promise only has a present value because the law enforces such promises. The present value of a promise can therefore not explain why the law awards expectation damages for the breach of a contractual promise.[151]

Secondly, Fuller and Perdue argued that such an award of expectation damages may be the most effective means of compensating a plaintiff for his or her various acts of reliance on the contract, reliance losses being potentially numerous and difficult to prove.[152] In particular, Fuller and Perdue suggested that reliance losses may include losses involved in foregoing the opportunity to enter into other contracts.[153] They argued that expectation loss will often have

145 Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936) 46 *Yale Law Journal* 52.
146 Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936) 46 *Yale Law Journal* 52, 53–4.
147 Compare the discussion of reliance damages at [26.25].
148 Compare the discussion of expectation damages at [26.55].
149 Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936) 46 *Yale Law Journal* 52, 56–7.
150 Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936) 46 *Yale Law Journal* 52, 59.
151 Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936) 46 *Yale Law Journal* 52, 60.
152 Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936) 46 *Yale Law Journal* 52, 60.
153 Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936) 46 *Yale Law Journal* 52, 60.

a comparable value to the lost opportunity and that the value of an existing contract is more easily quantified than that of a foregone opportunity.[154]

Thirdly, Fuller and Perdue argued that the measure of expectation damages might be preferred as a "prophylaxis" against "out of pocket" losses: "[s]ince the expectation interest furnishes a more easily administered measure of recovery than the reliance interest, it will in practice offer a more effective sanction against contract breach."[155]

Fuller and Perdue argued that, because of this deterrence effect, the measure of expectation damages has the attraction of making contracts more reliable and thus of encouraging reliance on promises.

Criticisms of Fuller and Perdue

[26.125] Fuller and Perdue's article remains significant. It has influenced the terminology used to describe contract damages.[156] It also has considerable ongoing relevance in its attempt to analyse the different types of awards of damages and the reasons for those awards. However, courts have not accepted Fuller and Perdue's preference for reliance damages, and the plaintiff's expectation loss remains the preferred measure of damages in contract.

Fuller and Perdue's arguments have also been criticised by other commentators. For example, Friedmann has criticised Fuller and Perdue's argument that a plaintiff's reliance interest is likely to be difficult to measure, and thus that expectation damages may be a better method of protecting reliance. He suggests that valuation of the expectation interest may be no less difficult.[157] Friedmann and Lücke each criticise Fuller and Perdue's bias against damages protecting the expectation interest. Fuller and Perdue suggested that expectation damages were justified only insofar as that measure protects and encourages reliance.[158] Friedmann and Lücke argue that an award of expectation damages may be justified by reference to the primary purpose of contract law, which is to enforce promises.[159] It is consistent with this purpose to say that if a defendant breaches a contract, what the plaintiff has lost is the expected benefit promised by the defendant and the remedy of damages should compensate him or her for this loss.

Damages and efficient breach

[26.130] Another justification of expectation damages comes from some proponents of an economic analysis of law who have developed a theory of "efficient breach".[160] Under this

154 Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936) 46 *Yale Law Journal* 52, 61.

155 Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936) 46 *Yale Law Journal* 52, 61.

156 Friedmann, "The Performance Interest in Contract Damages" (1995) 111 *Law Quarterly Review* 628, 633–4. See, eg, *Gates v City Mutual Assurance Society Ltd* (1986) 160 CLR 1, 12.

157 Friedmann, "The Performance Interest in Contract Damages" (1995) 111 *Law Quarterly Review* 628, 633, 635–6.

158 See also Goetz and Scott, "Enforcing Promises: An Examination of the Basis of Contract" (1980) 89 *Yale Law Journal* 1261.

159 Friedmann, "The Performance Interest in Contract Damages" (1995) 111 *Law Quarterly Review* 628, 633, 636–7; Lücke, "Two Types of Expectation Interest in Contract Damages" (1989) 12 *University of New South Wales Law Journal* 98, 104. See also Fried, *Contract as Promise: A Theory of Contractual Obligation* (1981), pp 17–21; Rakoff, "Fuller and Perdue's *The Reliance Interest* as a Work of Legal Scholarship" [1991] *Wisconsin Law Review* 203, 214.

160 Posner, *Economic Analysis of Law* (9th ed, 2014), § 4.10.

theory, the award of expectation damages provides an incentive to parties to breach their contracts and pursue other opportunities where this course of action would be efficient. A breach will be efficient where the defendant's profit from breaching the contract would exceed the loss suffered by the plaintiff as a result of the breach. In such a case, the defendant can compensate the plaintiff for the loss suffered and still also make a profit on the substitute transaction.[161]

For example, consider a contract for the sale of a truckload of wood. The cost to the vendor of providing the wood is $150. The contract price is $170. The cost to the purchaser of purchasing equivalent wood from an alternative source is $190. If the vendor breaches the contract, in order to put the purchaser in the position she would have been in if the contract had been performed, he would have to pay to the purchaser $20 ($190 for the alternative wood less $170 for the wood under the original transaction).

Assume a second buyer offers to buy the wood from the vendor. If the second purchaser offers a price of $180, the vendor will not have an incentive to breach the contract with the first purchaser. The profit to the vendor on the first transaction would be $20 ($170 less $150 for the cost of providing the wood), whereas the profit under a second transaction would only be $10 ($180 less $150 for supplying the wood and less $20 damages paid to the first purchaser for the breach).

If the second purchaser offered $200 for the wood, however, the vendor would have an incentive to breach the contract with the first purchaser. The vendor's profit from this transaction would be $30 ($200 less $150 for the cost of providing the wood and $20 damages payable to the first purchaser), which is greater than the $20 profit contemplated under the transaction with the first purchaser. In this case proponents of the theory of efficient breach would argue that the transaction is efficient. The vendor is better off, having made a profit of $30 after compensating the first purchaser. The second purchaser is better off, having obtained the wood. The first purchaser is no worse off than under the original contract, having been compensated for the breach through the award of expectation damages.

The theory of efficient breach suggests that expectation damages will be more effective than other measures of damages in encouraging only efficient breaches. For example, if the usual measure of damages were the plaintiff's reliance loss, then there would be an incentive for a defendant to breach a contract even where it was not efficient to do so.

Consider again the example of a contract for the sale of wood, where the cost to the vendor of providing the wood is $150, the contract price is $170 and the cost to the purchaser of purchasing wood from an alternative source is $190. Assume that the buyer has incurred $5 in costs in reliance on the contract being performed, perhaps in arranging for storage for the wood. The price offered by the second buyer is $180. If reliance damages were awarded, the seller would have an incentive to breach the contract. This is because the reliance damages would only amount to $5. However, the breach would not be efficient. Although the seller would be better off (with a profit of $25, rather than $20), the buyer would be worse off (having to incur an additional cost of $20).[162]

161 This type of efficiency analysis is sometimes known as *Pareto efficiency*.

162 The theory of efficient breach would also support punitive damages not being generally available: see Collins, *Regulating Contracts* (1999), p 119.

The theory of efficient breach has merit in asking us to consider the probable consequences of different remedies for breach of contract. The theory has also been criticised on the ground that they ignore the inherent value of keeping one's promises and also the availability of remedies such as specific performance.[163] These criticisms are discussed in Chapter 30 in assessing the relative merits of specific performance as a remedy for breach of contract. In *Tabcorp*, the High Court was critical of the implications of an economic analysis of damages. The Courts said that

> underlying the Tenant's submission that the appropriate measure of damages was the diminution in value of the reversion was an assumption that anyone who enters into a contract is at complete liberty to break it provided damages adequate to compensate the innocent party are paid. It is an assumption which at least one distinguished mind has shared. It has been dignified as 'the doctrine of efficient breach'. It led, in the Landlord's submission, to an attempt 'arrogantly [to] impose a form of "economic rationalism"' on the unwilling Landlord. The assumption underlying the Tenant's submission takes no account of the existence of equitable remedies, like decrees of specific performance and injunction, which ensure or encourage the performance of contracts rather than the payment of damages for breach. It is an assumption which underrates the extent to which those remedies are available.[164]

Relational contract theory

[26.135] An economic analysis of law considers the consequences of particular rules. Rather than merely considering the result in a particular case, the economic perspective considers what sort of rule will prove an incentive to efficient behaviour. As we have seen, in assessing the different measures of damages, proponents of an economic analysis of law assume that contracting parties know of and will take into account the implications of the various possible remedies in deciding whether or not to breach a contract.[165] However, it may be that the remedies available for breach of contract have far less effect on the behaviour of contracting parties than assumed by this type of law and economics analysis. As a practical matter, it may be argued that the damages awarded for breach of contract will often not truly compensate a plaintiff's loss, due to such factors as difficulties in calculating a plaintiff's real loss, the expectation that a plaintiff will mitigate and the high cost of litigation.[166] Moreover, empirical studies suggest that, at least in certain industries, parties avoid recourse to the law in the event of disputes and do not treat the terms of a contract as important in governing their relationship.[167] For example, Stewart Macaulay concludes from his survey that "[d]isputes

163 See, eg, Friedmann, "The Efficient Breach Fallacy" (1989) 18 *Journal of Legal Studies* 1, 3; Hillman, *The Richness of Contract Law: An Analysis and Critique of Contemporary Theories of Contract Law* (1997), pp 220–4; Macneil, "Efficient Breach of Contract: Circles in the Sky" (1982) 68 *Virginia Law Review* 947. Cf also Craswell, "Contract Remedies, Renegotiation, and the Theory of Efficient Breach" (1988) 61 *Southern California Law Review* 629, 640.

164 *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [13].

165 See also discussion of the incentives provided by the remoteness rule in *Hadley v Baxendale* in Ayres and Gertner, "Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules" (1989) 99 *Yale Law Journal* 87; Johnston, "Strategic Bargaining and the Economic Theory of Contract Default Rules" (1990) 100 *Yale Law Journal* 615.

166 Collins, *Regulating Contracts* (2002), pp 118–23.

167 See, eg, Beale and Dugdale, "Contracts Between Businessmen: Planning and the Use of Contractual Remedies" (1975) 2 *British Journal of Law and Society* 45; Macaulay, "Non-contractual Relations in Business: A Preliminary Study" (1963) 28 *American Social Review* 55. See also generally Collins, *Regulating Contracts* (2002), Ch 5 and references cited therein.

are frequently settled without reference to the contract or potential or actual legal sanctions. There is a hesitancy to speak of legal rights or to threaten to sue in these negotiations."[168] Macaulay further quotes one businessman as explaining: "[y]ou can settle any dispute if you keep the lawyers and accountants out of it. They just do not understand the give-and-take needed in business."[169]

These issues are explored in some detail by Hugh Collins. Collins reminds us that the exchange of goods and services is a complex social interaction in which not just the law, but also other social bonds, are relevant.[170] Collins argues that in deciding whether or not to enter into a contract, a party will be influenced by the degree to which he or she trusts the other party to perform the contract and by his or her assessment of the efficacy of the sanctions against disappointment in relation to the contract.[171]

While the law provides some forms of sanction against breach of contract, there may also be a number of very effective non-legal sanctions against breaching a contract. In particular, these may arise from the value of a good relationship with a contracting partner and the value of a good reputation in the community in which a party is dealing. A good relationship with the other party to a contract may facilitate successful performance of a contract because parties who get along are more likely to cooperate with each other. Aside from the personal satisfaction a party may gain from having the respect and confidence of his or her business community, a good reputation may improve a party's ability to attract and retain contracting partners in the future.[172] By contrast, a party who behaves in an egregious or opportunistic manner in performing a contract may find that he or she becomes the victim of "tit for tat" retaliation. More dramatically, other parties may refuse to deal with him or her.

The threat of these consequences of loss of reputation may be a very effective sanction against breach. They may mean that the long-term costs of breach outweigh the short-term benefits. Collins argues that the value of a good reputation may provide an incentive against parties invoking legal sanctions. Collins explains that the threat to sue for breach of contract "can rapidly displace norms of trust and cooperation and replace then with antagonistic self-interested assertions of rights".[173]

It may also be argued that there are good reasons not to dismiss the law of contract as irrelevant in providing an incentive for parties to perform their contracts. The role of reputation in providing an incentive to perform a contract is likely to be most effective in relatively close-knit contracting communities and to be less effective in larger, more diverse contracting communities. In particular, the value of a good reputation will only influence a party's behaviour where there is an ongoing contractual relationship or the possibility

168 Macaulay, "Non-contractual Relations in Business: A Preliminary Study" (1963) 28 *American Social Review* 55, 61.

169 Macaulay, "Non-contractual Relations in Business: A Preliminary Study" (1963) 28 *American Social Review* 55, 61.

170 Collins, *Regulating Contracts* (2002), especially Ch 5. See also Harris, "Incentives to Perform or Break Contracts" [1992] *Current Legal Problems* 29.

171 Collins, *Regulating Contracts* (2002), pp 98–102, 121.

172 See Milgrom and Roberts, *Economics, Organization & Management* (1992), pp 139–40, 259–68; Harris, "Incentives to Perform or Break Contracts" [1992] *Current Legal Problems 29*; Muris, "Opportunistic Behaviour and the Law of Contracts" (1981) 65 *Minnesota Law Review* 521, 577.

173 Collins, *Regulating Contracts* (2002), especially p 122.

of repeat transactions. A party who is only dealing once in a market or is moving into a different market will have less concern about such matters. Moreover, reputation will only provide an incentive to refrain from opportunistic behaviour in circumstances where information about that party's contracting behaviour is available to other prospective contracting partners.[174]

174 On the limits of reputation, see, eg, Hadfield, "Problematic Relations: Franchising and the Law of Incomplete Contracts" (1990) 42 *Stanford Law Review* 927, 978, n 232.

CHAPTER **27**

Limitations on the award of damages

LIMITATIONS

[27.05] There are a number of limitations on the award of damages in contract. The primary limitations are causation, remoteness and mitigation. Causation requires the loss of the party seeking damages (the *plaintiff*) to have been caused by the breach of the other party (the *defendant*). Remoteness sets limits beyond which the defendant's responsibility for loss will not extend. Mitigation looks to the reasonable steps that have been or should have been taken by a plaintiff to reduce his or her loss. There are also a number of more specific limitations on the award of damages that may apply in some cases.

CAUSATION

[27.10] In order to recover damages for a breach of contract, a plaintiff must show a causal connection between the defendant's breach and the loss for which the plaintiff is seeking

compensation. For this purpose, it will be sufficient if the defendant's breach was a cause of the plaintiff's loss; the breach need not have been the sole cause of the loss.[1]

Causation has not generally been a controversial issue in contract cases. In most contract cases, there is only one event that has contributed to the plaintiff's loss: the defendant's breach. In these sorts of cases, causation may be analysed through a simple *but for* test, which asks whether or not "but for" the defendant's breach the plaintiff would have suffered the loss in question.[2] If the answer is "no", then the defendant's breach may be considered a cause of the plaintiff's loss. If the answer is "yes", then this suggests that the loss would have occurred anyway, and the defendant's breach may not have caused the loss.

For example, consider a contract for the sale of materials needed for the operation of the buyer's factory. Assume that, in breach of contract, the seller fails to deliver the materials. The buyer incurs the cost of finding replacement materials and a loss of profit over the period in which a replacement source of materials is being found. On the facts given, the defendant's breach may be considered the cause of the plaintiff's losses. Applying the "but for" test, we can say that "but for" the breach, the losses would not have occurred.

More difficult questions of causation arise in those cases where there have been a number of events contributing to the plaintiff's loss.[3] Here the "but for" test may have much less value. The "but for" test suggests that both the defendant's breach and the subsequent events were causes of the plaintiff's loss. The test will not assist in deciding whether or not the defendant's contribution to the loss is such that the defendant should be held liable for that loss. For example, consider a case where the seller, in breach of contract, fails to deliver materials to the buyer's factory. The buyer goes to a warehouse to view an alternative supply of materials and is injured by a falling barrel. The "but for" test would suggest the seller's breach was a cause of the buyer's injury: "but for" the seller's breach, the buyer would not have been at the warehouse. However, as a matter of common sense, it might be thought that the seller should not be treated as liable for the buyer's injury.

In cases of multiple contributing events, a subsequent event that contributes to a plaintiff's loss may sometimes *break the chain* of causation between the defendant's breach of contract and the plaintiff's loss.[4] Such an event is usually described as an *intervening event* or a *novus actus interveniens*. Where there is a break in the chain of causation between the defendant's breach and the plaintiff's loss by reason of an intervening event, the defendant will not be liable for the loss. How does a court decide whether or not there has been a break in the chain of causation? As a general principle, the High Court has said that questions of causation should be determined in a "common sense" way in which value judgments and policy considerations will be relevant.[5] This decision means that whether a subsequent event breaks the chain of

1 *Fitzgerald v Penn* (1954) 91 CLR 268, 273; *Simonius Vischer & Co v Holt & Thompson* [1979] 2 NSWLR 322, 346; *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310, 315, 357–8.

2 See, eg, *Bank of Credit and Commerce International SA v Ali (No 2)* [2002] EWCA Civ 82; [2001] 3 All ER 750, [44].

3 See, eg, *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310; *Mallesons Stephen Jaques v Trenorth Ltd* [1999] 1 VR 727.

4 See, eg, *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310; *Chand v Commonwealth Bank of Australia* [2015] NSWCA 181, [167]–[169].

5 *March v E & M H Stramare Pty Ltd* (1991) 171 CLR 506, 522, 530 (a tort case but applicable to contract); *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 175; *Kenny & Good Pty Ltd v MGICA (No 2) Ltd* [1999] HCA 25; (1999) 100 CLR 413, [21], [28], [119]. See also *Alexander v Cambridge Credit Corp* (1987) 9 NSWLR 310, 315, 350, 351.

causation should be assessed by reference to the standard of "common sense". What does or does not amount to a sufficient causal connection from a position of common sense is not easily rationalised and must in essence involve considerations of policy and values, akin to the assessment of remoteness, discussed below at [27.15].

The use of the "common sense" approach in assessing causation is illustrated by *Alexander v Cambridge Credit Corporation Ltd*.[6] In 1971, the auditors of Cambridge Credit overstated the value of the assets of Cambridge Credit in breach of their contractual duty of care. If the auditors' reports had been prepared correctly, the trustee for debenture holders would have put the company into receivership. Instead, the company continued to trade until 1974 before going into receivership. The trial judge found that, had Cambridge Credit gone into receivership in 1971, the losses would have been around $10 million. By 1974, the losses were $155 million. Cambridge Credit claimed damages of $145 million, representing the difference between these two amounts. The losses in question were affected not only by the company continuing to trade, but also by some external developments adverse to Cambridge Credit, including the collapse of the real estate market in which Cambridge Credit had invested.[7]

In this case, the "but for" test of causation would have been satisfied. "But for" the auditors' negligence, the company would not have continued to trade after 1971 and thus would not have suffered losses after that date. However, the majority of the New South Wales Court of Appeal rejected the claim for damages by Cambridge Credit. The majority considered that the loss suffered by Cambridge Credit was not caused by the breach committed by its auditors. Mahoney JA considered that "allowing the company to remain in existence does not, without more, cause losses from anything which is, in that sense, a danger incidental to existing".[8] McHugh JA said that, as a matter of "common sense", the existence of a company could not be the cause of its subsequent trading losses.[9] Moreover, McHugh JA considered that the auditors' negligence was so "superseded in potency by supervening events as not to rank as a cause either in common sense or law".[10] External economic factors broke the chain of causation between the auditors' negligence and Cambridge's losses.[11] McHugh JA also considered that the losses were too remote from the breach of contract for the auditors to be liable.[12]

REMOTENESS OF DAMAGE

The need for a rule as to remoteness

[27.15] In order for damages to be awarded to compensate a loss, the plaintiff must show that the loss was not too remote. Remoteness is the concept employed by courts to identify the limits beyond which a defendant will not be held liable for the losses caused by his or her breach of contract.[13]

6 *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310, Glass JA dissenting.
7 *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310, 362.
8 *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310, 334.
9 *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310, 359.
10 *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310, 363.
11 *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310, 362–3.
12 *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310, 366–8.
13 Cf *Chapman v Hearse* (1961) 106 CLR 112, 122.

The need for a principle of remoteness may be illustrated by considering a case in which a seller breaches her contract by failing to deliver machinery needed for the plaintiff's business. The plaintiff may suffer loss by having to buy substitute machinery from another source or by not having the machinery in place to operate his business. The plaintiff may breach contracts he has made which require the use of the machinery and so be liable for damages. Not being able to conduct his business effectively may cause the plaintiff to suffer a loss of reputation. The stress caused by the defendant's breach of contract may lead the plaintiff to lose sleep, seek medication and crash his car and so on.

Generally, direct losses caused by a breach of contract, such as the cost of purchasing substitute machinery, are not too remote to be recovered. Remoteness principles primarily apply to contain consequential losses, such as the other types of losses mentioned in the above example.[14]

The rule in *Hadley v Baxendale*

[27.20] The test for when a particular loss caused by a breach of contract is too remote for a plaintiff to recover damages as compensation is laid down in the English case of *Hadley v Baxendale*,[15] which has been adopted by the High Court on numerous occasions.[16] In *Hadley v Baxendale* Alderman B explained:

> Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally, that is, according to the usual course of things, from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it.[17]

The rule has, at times, been treated as consisting of two limbs, one relating to losses arising "naturally" or "according to the usual course of things" and the other covering to losses as "may reasonably have been supposed to have been in the contemplation of the parties".[18] The alternative approach, which now appears to be favoured by the High Court, is to treat the rule in *Hadley v Baxendale* as expressing a single principle. As stated by Mason and Dawson JJ in *Commonwealth v Amann Aviation Pty Ltd*,

> the plaintiff is entitled to recover such damages as arise naturally, that is, according to the usual course of things, from the breach, or such as may reasonably be supposed to have been in the contemplation of both parties at the time they made the contract as the probable result of the breach.[19]

14 Lücke, "Two Types of Expectation Interest in Contract Damages" (1989) 12 *University of New South Wales Law Journal* 98, 103. On consequential losses, see [26.25]. Compare *Environmental Systems Pty Ltd v Peerless Holdings Pty Ltd* [2008] VSCA 26; (2008) 19 VR 358, [93].

15 *Hadley v Baxendale* (1854) 9 Exch 341; 156 ER 145.

16 See, eg, *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653, 658, 667, 623; *Hungerfords v Walker* (1989) 171 CLR 125, 140–4, 161.

17 *Hadley v Baxendale* (1854) 9 Exch 341, 355; 156 ER 145, 151.

18 See *MFM Restaurants Pte Ltd v Fish & Co Restaurants Pte Ltd* [2010] SGCA 36; [2011] 1 SLR 150, [102].

19 *Commonwealth v Amann Aviation Pty Ltd* [1991] HCA 54; (1991) 174 CLR 64, 92. Also *European Bank Limited v Evans* [2010] HCA 6; (2010) 240 CLR 432, [13].

The rule depends on the knowledge of the defendant

[27.22] The application of the rule in *Hadley v Baxendale* will "depend on the degree of relevant knowledge possessed by the defendant in the particular case".[20] Thus, in *C Czarnikow Ltd v Koufos*, Lord Reid explained that:

> The crucial question is whether, on the information available to the defendant when the contract was made, he should, or the reasonable man in his position would, have realised that such loss was sufficiently likely to result from the breach of contract to make it proper to hold that the loss flowed naturally from the breach or that loss of that kind should have been within his contemplation.[21]

The application of the rule in *Hadley v Baxendale* and the relevance of the knowledge of the defendant is illustrated in *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd*.[22] The contract in question was for the sale of a boiler by the defendants to the plaintiffs for use in the plaintiffs' laundry and dyeing business. The boiler was delivered to the plaintiffs some 20 weeks after the time fixed by the contract. The plaintiffs claimed damages for the loss of profit they would have made had the boiler been delivered on time. Included in this claim were the loss of a large number of new customers and the loss of a highly lucrative contract with the Ministry of Supply. The English Court of Appeal concluded that the plaintiffs could recover a general sum for the loss of profit. The defendants knew that the plaintiffs needed the boiler for immediate use in their laundry business but did not know the precise use to which the boiler was to be put. The Court held that the defendants must reasonably be presumed to foresee some loss of business if the boiler was not delivered on time.[23] However, the plaintiffs were not able to recover losses relating to the highly lucrative contracts. For the plaintiffs to recover the profits expected on the special contracts, the defendants would have to know of the prospect of such contracts.[24]

Assumption of responsibility in assessing remoteness

[27.25] An aspect of remoteness that has proved controversial is whether mere knowledge of a risk of loss is sufficient to make a defendant liable for that loss or whether the defendant must also have indicated some willingness to assume responsibility for the risk. The example commonly used is that of a taxi driver who, before accepting a fare, is informed that a passenger will suffer a business loss if the passenger does not get to a critical meeting on time.[25] If the taxi driver breaches the contract and fails to get the passenger to the meeting on time, is the taxi driver liable for the business losses? Common sense might suggest not. One approach would be to suggest that, given the unusual nature of the risk in the context of a taxi hire, the

20 *Commonwealth v Amann Aviation Pty Ltd* [1991] HCA 54; (1991) 174 CLR 64, 92. Also *European Bank Limited v Evans* [2010] HCA 6; (2010) 240 CLR 432, [13].

21 *C Czarnikow v Koufos* [1969] 1 AC 350, 385. See also *Wenham v Ella* (1972) 127 CLR 454, 471–2; *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653, 667.

22 *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd* [1949] 2 KB 528.

23 *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd* [1949] 2 KB 528, 542–3.

24 *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd* [1949] 2 KB 528, 543. For a modern example, see *Stuart Pty Ltd v Condor Commercial Insulation Pty Ltd* [2006] NSWCA 334.

25 *MFM Restaurants Pte Ltd v Fish & Co Restaurants Pte Ltd* [2010] SGCA 36; [2011] 1 SLR 150, [118]–[120]; Kramer, "An Agreement Centred Approach to Remoteness and Contract Damages" in McKendrick and Cohen (eds), *Comparative Remedies for Breach of Contract* (2005), pp 249, 269–70.

precise nature of the risk to be assumed by the taxi driver would have to be disclosed for it to fall within the rule in *Hadley v Baxendale*. Another approach would suggest that the taxi driver could not be liable because the driver had not assumed responsibility for such losses. Yet another approach would suggest that the scenario raises issues of policy, which should be clearly acknowledged.

The extent to which an assumption of responsibility should be relevant in assessing remoteness was considered in the English case of *Transfield Shipping Inc v Mercator Shipping Inc (The Achilleas)*.[26] The claim concerned the late redelivery of a ship to its owners by charterers under a time charter. Shortly prior to the redelivery date, market rates of hire had more than doubled compared with the previous year. The shipowners entered into a new charter fixture, commencing almost immediately after the agreed time of return from the defendant under the first contract. When the vessel was delayed and could not returned to the owners on time, time charter rates had fallen and the owners had to accept a reduced rate of hire on the subsequent charter. The shipowners claimed damages from the defendant for difference between the original daily rate and the reduced daily rate under the new charter.

The general understanding in the shipping market was that liability was restricted to the difference between the market rate and the rate in the original contract. This approach would mean that the higher rate originally agreed under the second contract was not relevant for calculating damages. The House of Lords accepted that the proper measure of damages was based on this market understanding. Lord Roger and Baroness Hale held that the parties would not have had the particular loss of the lucrative second contract within their contemplation at the time the first contract was made.[27] Lord Hoffmann and Lord Hope accepted that the loss of the second contract would have been foreseeable to the parties to the original contract. However, Lord Hoffmann and Lord Hope held that the assumption of responsibility, which forms the basis of the law of remoteness of damage in contract, "is determined by more than what at the time of the contract was reasonably foreseeable".[28] Lord Hoffmann and Lord Hope held that the market practice gave a basis for inferring that the assumption of risk implicitly assumed by the defendant was limited to that represented by the market practice.

Lord Hoffmann explained that in some circumstances "a party may not be liable for foreseeable losses because they are not of the type or kind for which he can be treated as having assumed responsibility".[29] In the circumstances of *The Achilleas* itself:

> If, therefore, one considers what these parties, contracting against the background of market expectations found by the arbitrators, would reasonably have considered the extent of the liability they were undertaking, I think it is clear that they would have considered losses arising from the loss of the following a type or kind of loss for which the charterer was not assuming responsibility.[30]

It is not clear whether, under Lord Hoffmann's approach, the question of assumption of responsibility is part of the inquiry into what was within the contemplation of the parties for the purpose of applying *Hadley v Baxendale* or whether it is a new criterion

26 *Transfield Shipping Inc v Mercator Shipping Inc (The Achilleas)* [2008] UKHL 48; [2009] 1 AC 61.

27 *Transfield Shipping Inc v Mercator Shipping Inc (The Achilleas)* [2008] UKHL 48; [2009] 1 AC 61, [54] (Lord Rodger), [91] (Baroness Hale).

28 *Transfield Shipping Inc v Mercator Shipping Inc (The Achilleas)* [2008] UKHL 48; [2009] 1 AC 61, [11].

29 *Transfield Shipping Inc v Mercator Shipping Inc (The Achilleas)* [2008] UKHL 48; [2009] 1 AC 61, [21].

30 *Transfield Shipping Inc v Mercator Shipping Inc (The Achilleas)* [2008] UKHL 48; [2009] 1 AC 61, [23].

for assessing remoteness.[31] It is clear that Lord Hoffmann considered that the limiting principle would only operate in rare cases.[32] Subsequent cases have confined the principle. Edelman states that:

> Thus, in the years since *The Achilleas* was decided there appear to have been no cases, either at first instance or at Court of Appeal level, in which damages have been cut down, or cut out, by the application of the assumption of responsibility test.[33]

The approach taken by Lord Hoffmann has not been followed in Australia, and nor has it been rejected. The approach has been criticised by some courts and by commentators. These criticisms typically focus on the difficulties involved in identifying responsibility assumed by the parties.[34] In Singapore, in *MFM Restaurants Pte Ltd v Fish & Co Restaurants Pte Ltd*[35] the Court of Appeal declined to follow Lord Hoffmann's approach in *The Achilleas* insofar as it introduced a new criterion into the inquiry into remoteness. The court considered that the rule in *Hadley v Baxendale*

> suffices to provide the court with a sufficiently nuanced approach towards dealing (in a *practical* manner) with whether or not the defendant concerned had assumed responsibility with respect to *natural or ordinary loss* and *extraordinary loss*, respectively.[36]

The Court considered that "the criterion of knowledge furnishes a sufficiently objective basis on which to premise the existence (or otherwise) of an implied obligation or assumption of responsibility on the defendant".[37]

In England, courts have combined the rule in *Hadley v Baxendale* with the considerations raised in Lord Hoffmann's judgment in *The Achilleas*. In *Supershield Ltd v Siemens Building Technologies FE Ltd*[38] the Court of Appeal considered *The Achilleas* is authority for the principle that

> there may be cases where the court, on examining the contract and the commercial background, decides that the standard approach would not reflect the expectation or intention reasonably to be imputed to the parties.[39]

The court noted that in *The Achilleas*:

> the effect was exclusionary; the contract breaker was held not to be liable for loss that resulted from its breach although some loss of the kind was not unlikely. But logically the same principle may have an inclusionary effect. If, on the proper analysis of the contract against its commercial

31 On this later approach see Kramer, "The New Test of Remoteness in Contract" (2009) 125 *Law Quarterly Review* 408.

32 *Transfield Shipping Inc v Mercator Shipping Inc (The Achilleas)* [2008] UKHL 48; [2009] 1 AC 61, [11].

33 Edelman (ed), *McGregor on Damages* (20th ed, 2018), [8.180]. Also *John Grimes Partnership Ltd v Gubbins* [2013] EWCA Civ 37, [25]; *SC Confectia SA v Miss Mania Wholesale Ltd* [2014] EWCA Civ 1484, [15], [24].

34 See Robertson, "The Basis of the Remoteness Rule in Contract" (2008) 28 *Legal Studies* 172, 185; Peel, "Remoteness Revisited" (2009) 125 *Law Quarterly Review* 6, 11.

35 *MFM Restaurants Pte Ltd v Fish & Co Restaurants Pte Ltd* [2010] SGCA 36; [2011] 1 SLR 150.

36 *MFM Restaurants Pte Ltd v Fish & Co Restaurants Pte Ltd* [2010] SGCA 36; [2011] 1 SLR 150, [112]. (Emphasis in original)

37 *MFM Restaurants Pte Ltd v Fish & Co Restaurants Pte Ltd* [2010] SGCA 36; [2011] 1 SLR 150.

38 [2010] 1 Lloyd's Rep 349, [43].

39 *Supershield Ltd v Siemens Building Technologies FE Ltd* [2010] 1 Lloyd's Rep 349, [43]. See also *Sylvia Shipping Co Ltd v Progress Carriers Ltd* [2010] EWHC 542; *John Grimes Partnership Ltd v Gubbins* [2013] EWCA Civ 37.

> background, the loss was within the scope of the duty, it cannot be regarded as too remote, even if it would not have occurred in ordinary circumstances.[40]

The issue remains to be determined in Australia. In *Stuart Pty Ltd v Condor Commercial Insulation Pty Ltd*,[41] decided before *The Achilleas*, the NSW Court of Appeal indicated support for the view that an assumption of responsibility might be inferred from a defendant having sufficient knowledge of a particular risk of loss to be in an informed position to decide whether to accept that risk, and then taking no steps to exclude liability for the risk.[42] No court has subsequently clarified the correct approach.

The extent of damage that must be contemplated

[27.30] It is not necessary for the defendant reasonably to have contemplated the degree or extent of the loss that was in fact suffered or the precise details of the events giving rise to the loss. It is sufficient that the parties contemplated the kind or type of loss or damage suffered[43] and that the event that gave rise to the loss would have appeared to the defendant as "not unlikely to occur".[44]

This principle is illustrated by *H Parsons (Livestock) Ltd v Uttley Ingham & Co Ltd*.[45] In this case, the plaintiffs, pig breeders, ordered a bulk food storage hopper from the defendants. The defendants improperly installed the hopper and the food, which was subsequently stored in the hopper, went mouldy. The plaintiffs were aware of the mould on the food, but nonetheless allowed the pigs to eat it. A large number of the pigs later died from an internal *E coli* infection caused by the mould. The defendants were sued for breach of a warranty that the hopper would be reasonably fit for the purpose of storing animal food in a condition suitable for feeding to the plaintiffs' pigs. The English Court of Appeal found that the death of the pigs was not too remote a loss for damages to be recovered. The Court accepted that the parties might not have contemplated that, if the food was mouldy, the pigs would die from an *E coli* infection. However, the Court considered it was sufficient that the parties would contemplate that food "affected by bad storage conditions might well cause illness in the pigs fed upon it".[46] In other words, the Court considered that death was damage of the same kind as illness.

Degree of likelihood of damage resulting from a breach

[27.35] Different words have been used to describe the degree of likelihood with which damage must be contemplated, or presumed to have been contemplated, by the defendant for

40 *Supershield Ltd v Siemens Building Technologies FE Ltd* [2010] 1 Lloyd's Rep 349, [43]. See also *Sylvia Shipping Co Ltd v Progress Carriers Ltd* [2010] EWHC 542; *John Grimes Partnership Ltd v Gubbins* [2013] EWCA Civ 37.

41 *Stuart Pty Ltd v Condor Commercial Insulation Pty Ltd* [2006] NSWCA 334.

42 *Stuart Pty Ltd v Condor Commercial Insulation Pty Ltd* [2006] NSWCA 334, [52]–[61] citing, in particular *Robophone Facilities Ltd v Blank* [1966] 1 WLR 1428, 1447–1448 and Carter, *Contract Law in Australia* (now at 7th ed, 2018), [2128].

43 See especially *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310.

44 *C Czarnikow v Koufos* [1969] 1 AC 350, 388; *Stuart Pty Ltd v Condor Commercial Insulation Pty Ltd* [2006] NSWCA 334, [98].

45 *H Parsons (Livestock) Ltd v Uttley Ingham & Co Ltd* [1978] QB 791.

46 *H Parsons (Livestock) Ltd v Uttley Ingham & Co Ltd* [1978] QB 791, 813, also 804.

a plaintiff to recover damages. In *C Czarnikow Ltd v Koufos*[47] the House of Lords suggested a number of formulations: the damage reasonably contemplated by the parties must be "not unlikely",[48] "liable to result"[49] or "a serious possibility or real danger".[50] It may be that the difference between these various terms is not significant.[51] What they have in common is suggesting that a plaintiff must show that there is a high but not "a near certainty or an odds-on probability" of damage.[52]

Relationship with the rule of remoteness in tort

[27.40] In the law of the tort of negligence, the rule of remoteness states that a loss is too remote if it was not "reasonably foreseeable". In contract law, the remoteness rule in *Hadley v Baxendale*[53] refers to losses that were "reasonably contemplated" by both parties. Is there a difference between these two tests? Some judges have suggested that the differences between the tests of remoteness in tort and contract are semantic, rather than substantial.[54] By contrast, in *C Czarnikow Ltd v Koufos*,[55] the House of Lords considered that a rule of "reasonable foreseeability" was not appropriate in contract and that the remoteness rule in tort was wider than in contract.[56] In *Alexander v Cambridge Credit Corp*,[57] McHugh J also considered that the difference between reasonable foreseeability and reasonable contemplation was a real one. His Honour explained that:

> The word 'contemplation' seems to be used in *Koufos* in the sense of 'thoughtful consideration' or perhaps 'having a view to the future'. It emphasises that, if the parties had thought about the matter, they would really have considered that the result had at least a 'serious possibility' of occurring.[58]

The basis of the remoteness rule

[27.43] The remoteness rule is commonly seen as giving effect to the implicit allocation of risk made by the parties under their contract.[59] It has been argued, however, that the identification of an implicit allocation of risk does not, and cannot, determine remoteness cases in contract.[60] Robertson argues that the remoteness rule is not directed at the identification

47 *C Czarnikow v Koufos* [1969] 1 AC 350.

48 *C Czarnikow v Koufos* [1969] 1 AC 350, 388.

49 *C Czarnikow v Koufos* [1969] 1 AC 350, 406, 410–1.

50 *C Czarnikow v Koufos* [1969] 1 AC 350, 115; 425.

51 *Wenham v Ella* (1972) 127 CLR 454, 466.

52 *Wenham v Ella* (1972) 127 CLR 454, 471–2. See also *Baltic Shipping Co v Dillon (The Mikhail Lermontov)* (1993) 176 CLR 344, 365, 370.

53 *Hadley v Baxendale* (1854) 9 Exch 341, 355; 156 ER 145, 151.

54 *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd* [1949] 2 KB 528, 535; *H Parsons (Livestock) Ltd v Uttley Ingham & Co Ltd* [1978] QB 791, 807.

55 *C Czarnikow v Koufos* [1969] 1 AC 350.

56 *C Czarnikow v Koufos* [1969] 1 AC 350, 385–6, 411, 413–4, 422. See also *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310, 365.

57 *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310.

58 *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310, 365. See also *Stuart Pty Ltd v Condor Commercial Insulation Pty Ltd* [2006] NSWCA 334, [120].

59 See, eg, Kramer, "An Agreement-centred Approach to Remoteness and Contract Damages" in McKendrick and Cohen (eds), *Comparative Remedies for Breach of Contract* (2005), p 240.

60 Robertson, "The Basis of the Remoteness Rule in Contract" (2008) 28 *Legal Studies* 172.

of an implicit allocation of risk and there is rarely any evidence from which allocation of risk can be inferred. The remoteness rule is therefore better understood as "a gap filling device, which is concerned with ensuring that a contract breaker is not subjected to an unreasonable burden".[61]

The question of how the remoteness rule should be conceived was raised, but not concluded, in *Transfield Shipping Inc v Mercator Shipping Inc (The Achilleas)*.[62] Lord Hoffmann said:

> It seems to me logical to found liability for damage upon the intention of the parties (objectively ascertained) because all contractual liability is voluntarily undertaken. It must be in principle wrong to hold someone liable for risks for which the people entering into such a contract in their particular market, would not reasonably be considered to have undertaken.[63]

MITIGATION OF DAMAGE

[27.45] The third main limitation on an award of damages is the principle of mitigation. Mitigation looks to the steps that have been, or should reasonably have been, taken by a plaintiff to reduce the loss caused by the defendant's breach of contract.[64] Mitigation can be summarised in three rules:[65]

1. The plaintiff cannot recover for avoidable loss.
2. The plaintiff can recover for loss incurred in reasonable attempts to avoid loss.
3. The plaintiff cannot recover for avoided loss.

Avoidable loss: mitigating action that should have been taken

[27.50] A plaintiff may not recover damages for breach of contract for losses that might have been avoided if the plaintiff had taken reasonable steps to minimise that loss.[66] A plaintiff will not be expected to take steps to mitigate the loss unless the plaintiff was aware of the breach giving rise to the loss or ought reasonably have been aware of the breach.[67] There is not strictly a *duty* to mitigate; there is no contractual obligation to mitigate that can be enforced by the defendant.[68] Rather, a failure to take reasonable steps to mitigate reduces the damages the plaintiff can recover. The onus is on the defendant to prove that the plaintiff has not taken reasonable steps to mitigate his or her loss.[69]

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61 Robertson, "The Basis of the Remoteness Rule in Contract" (2008) 28 *Legal Studies* 172, 172.

62 *Transfield Shipping Inc v Mercator Shipping Inc (The Achilleas)* [2008] UKHL 48; [2009] 1 AC 61.

63 *Transfield Shipping Inc v Mercator Shipping Inc (The Achilleas)* [2008] UKHL 48; [2009] 1 AC 61, [12], also [32]–[36] (Lord Hope), 61, 68, also 73–5.

64 The principles of mitigation do not apply to an action for a debt or liquidated sum: see Chapter 29. On the strong relationship between the date for assessing damages and principles of mitigation see Dyson and Kramer, "There is no 'Breach Date Rule': Mitigation, Difference in Value and Date of Assessment" (2014) 130 *Law Quarterly Review* 259.

65 Edelman (ed), *McGregor on Damages* (20th ed, Thomson Reuters, 2018), [9.004]–[9.006]. See also *Simonius Vischer & Co v Holt & Thompson* [1979] 2 NSWLR 322, 356; *Thai Airways International Public Co Ltd v K I Holdings Co Ltd* [2015] EWHC 1250 (Comm).

66 See, eg, *Chand v Commonwealth Bank of Australia* [2015] NSWCA 181, [179]–[183].

67 *Bak v Glenleigh Homes Pty Ltd* [2006] NSWCA 10, [5].

68 *The Alecos M* [1991] 1 Lloyd's Rep 120, 124.

69 *TC Industrial Plant Pty Ltd v Robert's Queensland Pty Ltd* (1963) 180 CLR 130, 138.

Reasonable steps to mitigate a loss will often require the plaintiff to seek a substitute performance for what has been lost by reason of the breach.[70] For example, if a seller in breach of contract fails to deliver machinery to the buyer's factory, the buyer, to mitigate his loss, should seek an alternative source of supply for the machinery. The buyer's damages will then represent the difference between the price of the machinery under the original contract and the price under the substitute contract. If the buyer breaches the contract by refusing to accept the machinery, the seller should attempt to mitigate her losses by finding another buyer for the machinery. If the seller finds another buyer, the amount obtained on this alternative transaction will reduce the damages payable by the first buyer.

Reasonable steps to mitigate may require a plaintiff to accept an offer by the defendant to enter into a new contract as a means of mitigating the loss. For example, where a seller has breached a contract of sale by providing defective goods to the buyer, the buyer may be expected to take up an offer by the seller to repurchase the goods at the contract price.[71] In a contract for the sale of property, mitigation may require a vendor to accept the offer by a purchaser initially unable to raise the purchase price to complete the contract.[72]

A plaintiff is, however, only required to take reasonable steps to mitigate a loss. This means there is a limit to what the defendant can argue the plaintiff ought to have done. The law does not preclude the plaintiff from recovering damages merely because the defendant, with the benefit of hindsight, can suggest steps that might have been more effective in reducing the loss. As explained in *Banco de Portugal v Waterloo & Sons Ltd*:

> Where the sufferer from a breach of contract finds himself in consequence of that breach placed in a position of embarrassment the measures which he may be driven to adopt in order to extricate himself ought not to be weighed in nice scales at the instance of the party whose breach of contract has occasioned the difficulty. It is often easy after an emergency has passed to criticise the steps which have been taken to meet it, but such criticism does not come well from those who have themselves created the emergency.[73]

What steps are reasonable to take in mitigating damage arising from a breach of contract will depend on the circumstances of the particular case. However, it has been said that a plaintiff is not required to do anything other than in the ordinary course of business. For example, a plaintiff is not required to take steps to mitigate his or her loss that would involve excessive risk, cost or uncertainty.[74]

Reasonable steps in mitigation and the impecunious plaintiff

[27.55] What effect does the impecuniosity of the plaintiff have on the principle that a plaintiff will be expected to take reasonable steps to mitigate his or her loss? The courts have stated that damage resulting from a breach of contract that was reasonably within the contemplation of the parties when the contract is made is recoverable, even though the plaintiff's impecuniosity

70 See *Wenham v Ella* (1972) 127 CLR 454, 461, 464, 467.

71 *Houndsditch Warehouse Co Ltd v Waltex Ltd* [1944] KB 579.

72 See *Castle Constructions Pty Ltd v Fekala Pty Ltd* [2006] NSWCA 133; (2006) 65 NSWLR 648.

73 *Banco de Portugal v Waterloo & Sons Ltd* [1932] AC 452, 506.

74 See, eg, *Sacher Investments Pty Ltd v Forma Stereo Consultants Pty Ltd* [1976] 1 NSWLR 5; *Twidale v Bradley* [1990] 2 Qd R 464; *Challenge Bank Ltd v VL Cooper & Associates Pty Ltd* [1996] 1 VR 220; *Wenkart v Pitman* (1998) 46 NSWLR 502.

contributed to the loss.[75] However, somewhat paradoxically, it also appears from the majority decision in *Burns v MAN Automotive (Aust) Pty Ltd*[76] that the fact that a plaintiff cannot afford to take steps to reduce the loss caused by a breach of contract may nonetheless result in a reduction of damages, through the principle of remoteness or mitigation where the plaintiff's failure to mitigate is held to be "unreasonable" in the circumstances.

The case concerned a contract entered into in 1977. Under the contract, the seller agreed to sell a diesel prime mover to a finance company, which would then hire the prime mover to Burns. The seller warranted that the engine of the prime mover had been fully reconditioned. The seller knew that Burns intended to use the prime mover in a business of interstate haulage. It was also found that the seller should have known that Burns was not in affluent circumstances. The engine had not, in fact, been reconditioned. As a result, it caused Burns considerable difficulty in the conduct of his business. In 1978, the vehicle broke down and Burns became aware that the engine had not been fully reconditioned and was defective. Burns could not afford to put the engine into its warranted condition and the seller refused to do so. Burns could no longer use the vehicle on interstate routes and used it instead on less lucrative work within the state. In 1979, the prime mover broke down again and was repossessed by the finance company.

Burns sued the seller for breach of warranty. Burns claimed damages for the loss of the earnings that would have been expected if the engine had been fully reconditioned. The damages were claimed for a four-year period, which was the period for which the engine could have been expected to operate efficiently. The majority of the High Court held that Burns was not entitled to damages for loss of earnings after July 1978, although the reasons given for this result differed.[77]

Wilson, Deane and Dawson JJ held that this was not a case of mitigation of damage, but of remoteness. According to the majority, "[i]t called simply for a determination of that point in time, beyond which any damage suffered by Burns could not be said to have been within the reasonable contemplation of the parties as flowing from the breach."[78]

Their Honours considered that Burns' position had "crystallised" from the point of view of the assessment of damages by July 1978 because by then, it should have been obvious that the vehicle should either be repaired or relinquished by the buyer to the hire company.[79] We might comment that the majority's analysis of remoteness seems to have indirectly involved a question of mitigation. It would seem that the reason why the limits of Burns' losses were set at the date of July 1978 was because, from that date, Burns could reasonably be expected to have acted to mitigate his loss in the manner described by the majority.[80]

Gibbs CJ considered that the damages claimed by Burns were not too remote. It would have been within the reasonable contemplation of the parties that, if the warranty as to the condition of the engine was broken, Burns might lose the profits that he otherwise would have made.[81] Burns should not be debarred from claiming damages attributable to his failure to

75 *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653, 658–9; *Goodridge v Macquarie Bank Ltd* [2010] FCA 67, [228]; *Archibald v Powlett* (2017) 53 VR 645, [76].

76 *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653.

77 Gibbs CJ, Wilson, Deane and Dawson JJ, Brennan J dissenting.

78 *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653, 668.

79 *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653, 669.

80 Cf Seddon and Bigwood, *Cheshire & Fifoot's Law of Contract* (11th Aust ed, 2018), [23.40].

81 *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653, 658.

mitigate when his failure to mitigate resulted from his impecuniosity. This was particularly so where, as in this case, the financial difficulties of the buyer were largely brought about by the actions of the seller in supplying a defective engine and then refusing to remedy the defects.[82] Nonetheless, Gibbs CJ considered that Burns had not done all that was reasonable to mitigate his damage. Gibbs CJ considered that it was not reasonable for Burns to carry on his business with the defective engine once "he knew that he was operating at a loss and should have known that he had no prospect of making profit".[83]

Brennan J, dissenting, considered that the issues of remoteness and mitigation were linked. His Honour explained that the question was: "Do foreseeable losses stop short of the losses incurred at the stage when the injured party, acting reasonably, would mitigate the losses resulting from the breach of warranty?".[84]

Brennan J considered that the losses suffered by Burns in this case were not too remote,[85] nor should such losses be reduced by reason of a failure to take reasonable steps to mitigate.[86] Brennan J considered that the rules of mitigation were "not so draconian as to deny recovery to an impecunious victim who, if he were not so impecunious, could have avoided the loss".[87]

Attempts at mitigation that increase loss

[27.60] The second rule of mitigation identified is that where a plaintiff does take reasonable steps to mitigate his or her damage but, in so doing, actually increases the losses suffered, the plaintiff can recover damages to compensate for those additional losses.[88]

The principle is illustrated in *Simonius Vischer & Co v Holt & Thompson*.[89] The plaintiffs were a firm of wool brokers, based in Switzerland, trading in the wool futures market in Sydney. Staff in the Sydney office consistently exceeded their authority in speculative operations and sought to conceal their conduct from the head office. As a result of these unauthorised activities, the firm lost over £200,000. The plaintiffs successfully sued the defendants, who had acted as the firm's auditors, for breach of duty in failing to discover the unauthorised activities of the Sydney office. When the breach had been discovered, the plaintiffs surveyed the market and concluded that the best course of action would be to hold onto existing contracts. In fact, the plaintiffs' prediction was wrong and further losses were incurred. The defendants argued that, as a result of this conduct, the plaintiffs had failed to mitigate their losses and that, accordingly, the further losses incurred should not be recoverable. This argument was rejected by the New South Wales Court of Appeal. The Court accepted the trial judge's finding that the plaintiffs' conduct in deciding what to do with the open contracts had been reasonable. From this finding, it followed that the defendants were bound to make good the loss sustained.

82 *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653, 659.

83 *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653, 660.

84 *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653, 673.

85 *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653, 675.

86 *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653, 676.

87 *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653, 675.

88 *Banco de Portugal v Waterlow & Sons* [1932] AC 452, 506; *Simonius Vischer & Co v Holt & Thompson* [1979] 2 NSWLR 322, 356. See also *Gwam Investments Pty Ltd v Outback Health Screenings Pty Ltd* [2010] SASC 37; (2010) 106 SASR 167, [57]–[58].

89 *Simonius Vischer & Co v Holt & Thompson* [1979] 2 NSWLR 322.

Avoided losses: mitigating action actually taken

[27.65] The third rule of mitigation is that a plaintiff may not recover damages for losses that have been diminished or avoided by the plaintiff's actions, even where the law would not consider that those actions were part of what should reasonably be done by the plaintiff to reduce his or her loss.[90] Thus, any benefits obtained by the plaintiff as a consequence of the defendant's breach will be taken into account in calculating the plaintiff's damages.[91]

One type of case where the plaintiff's gain will be taken into account in calculating damages is where, by reason of the defendant's breach, the plaintiff enters into an alternative, more beneficial transaction. An illustration is provided by the English case of *British Westinghouse Electric and Manufacturing Co Ltd v Underground Electric Railways Co of London Ltd*.[92] In this case, the defendant breached its contract with the plaintiff by supplying defective electric turbines. The plaintiff replaced the defective turbines with others of greater power and efficiency. The new turbines reduced the plaintiff's operating costs and increased its profits. The plaintiff claimed as damages from the defendant the cost of the new turbines. This claim was rejected by the House of Lords. Once the gains in profit and saved expenses resulting from the use of the new turbines were taken into account, no net loss had been incurred by the plaintiff. The plaintiff was, however, entitled to recover the loss suffered while using the defective machines.

The rule that a plaintiff will not recover for avoided loss applies only to benefits obtained by the plaintiff which arise out of the consequences of the breach.[93] It does not apply to benefits that, although having the effect of reducing the plaintiff's overall financial loss, are wholly collateral.[94] In particular, when calculating damages, a plaintiff is not required to bring into account amounts recovered under a policy of insurance taken out to guard against the consequences of a possible breach.[95] The reason is that the insurance does not arise from the breach, but from an independent contract.

Mitigation and the sale of goods

[27.70] The rules of mitigation have a special application to contracts regulated by the *Sale of Goods Acts*. The Acts assume that where a contract for the sale of goods is breached, the plaintiff will go into the market to reduce his or her losses. Accordingly, the assumption that a plaintiff will (or should) take reasonable steps to mitigate his or her loss is built into the ordinary measure of damages.[96] For example, where in breach of contract, a seller fails to deliver goods, the *Sale of Goods Acts* provide:

90 *British Westinghouse Electric and Manufacturing Co Ltd v Underground Electric Railways Co of London Ltd* [1912] AC 673, 690.

91 See, eg, *Harold R Finger & Co Pty Ltd v Karellas Investments Pty Ltd* [2016] NSWCA 123.

92 *British Westinghouse Electric and Manufacturing Co Ltd v Underground Electric Railways Co of London Ltd* [1912] AC 673.

93 *British Westinghouse Electric and Manufacturing Co Ltd v Underground Electric Railways Co of London Ltd* [1912] AC 673, 690–1.

94 *Lavarack v Woods of Colchester Ltd* [1967] 1 QB 278, 290–1; *Monroe Schneider Associates (Inc) v No 1 Raberem Pty Ltd* (1991) 33 FCR 1, 11–2; *Harold R Finger & Co Pty Ltd v Karellas Investments Pty Ltd* [2016] NSWCA 123, [226].

95 *Bradburn v Great Western Railway Co* (1874) LR 10 Exch 1 (tort).

96 *Radford v De Froberville* [1977] 1 WLR 1262, 1272. For a modern example, see *Cargill Australia Limited v Cater Oil Company Pty Ltd* [2011] VSC 126.

> Where there is an available market for the goods in question, the measure of damages is prima facie to be ascertained by the difference between the contract price and the market or current price of the goods at the time or times when they ought to have been delivered, or if no time was fixed then at the time of the refusal to deliver.[97]

The application of this market-based measure of damages can be illustrated by considering a case where a seller fails, in breach of the seller's contract with the buyer, to deliver a quantity of wheat. Prima facie, damages would be based on how much the buyer must pay to obtain a substitute quantity of wheat in the market. If the contract price was $1,000 at the time the contract was made and the market price was $1,200 on the day of delivery, then the buyer's damages would be $200. Conversely, if the market price on the day of delivery had fallen to $900, prima facie, the plaintiff would not recover any damages for the breach of contract because no loss would have been suffered.[98]

Mitigation and subsequent transactions

[27.72] We have seen that in a case where a seller breaches the contract by failing to deliver goods, the buyer is expected to mitigate his or her loss by purchasing substitute goods. The buyer's damages will then represent the cost of those substitute goods. In some cases, a buyer may be able to recoup the cost of substitute goods by onselling them to third parties at a price that absorbs the increased cost of those goods. Should the measure of damages for breach of contract take into account costs recouped on subsequent sales? There is English authority either way.[99] In Australia, it appears that sales to third parties that merely recoup the cost of the substitute goods should not be taken into account in assessing damages, although additional profits made might be.

The issue was raised in the somewhat unusual case of *Clark v Macourt*.[100] The case involved two registered medical practitioners who each specialised in providing assisted reproductive technology services. In 2002, the appellant agreed to buy certain assets of the St George Fertility Centre Pty Ltd, a company controlled by the respondent. The vendor company agreed to sell to the respondent certain assets of the practice, including a stock of frozen donated sperm contained in batches of "straws". The respondent guaranteed the vendor's obligations under the contract. The vendor warranted that the identification of donors of the sperm complied with specified guidelines. Of the stock of sperm delivered, 1,996 straws did not comply with these guidelines and thus were unusable. The appellant

97 See *Sale of Goods Act 1954* (ACT), s 54(3); *Sale of Goods Act 1923* (NSW), s 53(3); *Sale of Goods Act* (NT), s 53(3); *Sale of Goods Act 1896* (Qld), s 52(3); *Sale of Goods Act 1895* (SA), s 50(3); *Sale of Goods Act 1896* (Tas), s 55(3); *Goods Act 1958* (Vic), s 57(3); *Sale of Goods Act 1895* (WA), s 50(3). A similar rule applies where, in breach of contract, the buyer refuses to accept delivery of goods: see *Sale of Goods Act 1954* (ACT), s 53(3); *Sale of Goods Act 1923* (NSW), s 52(3); *Sale of Goods Act* (NT), s 52(3); *Sale of Goods Act 1896* (Qld), s 51(3); *Sale of Goods Act 1895* (SA), s 49(3); *Sale of Goods Act 1896* (Tas), s 54(3); *Goods Act 1958* (Vic), s 56(3); *Sale of Goods Act 1895* (WA), s 49(3).

98 Where the market measure of damages is not appropriate, the ordinary rules will apply. See also, preserving the second limb of the rule in *Hadley v Baxendale*: *Sale of Goods Act 1954* (ACT), s 57; *Sale of Goods Act 1923* (NSW), s 55; *Sale of Goods Act* (NT), s 55; *Sale of Goods Act 1896* (Qld), s 55; *Sale of Goods Act 1895* (SA), s 53; *Sale of Goods Act 1896* (Tas), s 58; *Goods Act 1958* (Vic), s 60; *Sale of Goods Act 1895* (WA), s 53.

99 Compare *Slater v Hoyle & Smith Ltd* [1920] 2 KB 11; *Bence Graphics International Ltd v Fasson UK Ltd* [1998] QB 87. See also Bridge, "Mitigation of Damages in Contract and the Meaning of Avoidable Loss" (1989) 105 *Law Quarterly Review* 398.

100 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1.

purchased suitable replacement sperm in the United States at a price considerably higher than the price agreed under the contract.

Buying 1,996 straws of replacement sperm from the American supplier ("Xytex") would have cost about $1 million at the time the contract was breached. The purchase price for the assets, including the stock of frozen donated sperm, was less than $400,000. The price increase had, however, been passed onto the patients of the appellant. Moreover, the appellant accepted that ethically she could not charge, and in fact had not charged, any patient a fee for using donated sperm greater than the amount the appellant had outlaid to acquire it.

The question facing the High Court was how the appellant's damages for breach of warranty should be assessed. The appellant brought her claim on the basis of a breach of warranty relating to the sale of goods, rather than as a sale of a business including assets. The High Court majority accepted this approach and did not consider it made a difference to the claim.[101]

The primary judge assessed the damages for breach of warranty as the amount that the appellant would have had to pay Xytex (at the time the contract was breached) to buy 1,996 straws of sperm, holding that this was the best evidence of the market value of substitute sperm at the time of breach. The Court of Appeal held that the appellant should have no damages. The appellant had bought straws of sperm from Xytex to use in treating patients and had charged each patient a fee, which covered the costs the appellant had incurred in buying the straws that were used in treating that patient. The Court of Appeal held that the appellant had therefore avoided any loss. The High Court reinstated the award of damages of $1,020,252.70 made by the primary judge.

The majority justices, Hayne, Crennan, Bell, and Keane JJ, in separate judgments, affirmed the guiding principle that "the position in which the plaintiff is to be put, by an award of damages, is the position in which the plaintiff would have been if the contract had been performed."[102] This meant that damages for breach of contract should be measured by reference to "the loss of the value of what the *promisee would have received* if the promise had been performed".[103] In this case, the appellant should have received, but did not, 1,996 straws of sperm having the warranted qualities. Her damages should represent the cost of obtaining a substitute performance, namely the amount it would have cost at the date of breach to acquire this 1,996 straws of sperm from Xytex. The profit made or not made on the promise was not relevant to this stage of inquiry, as the appellant was not claiming loss of profit.[104]

The purchase price paid for the replacement sperm revealed the value of what was lost when the vendor did not perform the contract.[105] The Court of Appeal had assumed that in buying replacement sperm from Xytex and then by recouping the cost of that sperm from patients, the appellant had mitigated her loss.[106] It is well recognised that a plaintiff cannot recover damages for an "avoided loss".[107] However, the majority justices explained

101 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [13], [30], [108]. Cf Carter, Courtney and Tolhurst, "Issues of Principle in Assessing Contract Damages" (2014) 31 *Journal of Contract Law* 171.

102 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [7], [26], [106]–[108].

103 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [10] (emphasis in original).

104 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [129].

105 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [20].

106 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [14].

107 *British Westinghouse Electric and Manufacturing Co Ltd v Underground Electric Railways Co of London Ltd* [1912] AC 673.

that "avoided loss" in this context refers to cases where the plaintiff has gone further than expected, and in obtaining substitute performance, improves his or her position.[108] The High Court held that the purchase and use of the replacement sperm left the appellant "neither better nor worse off than she was before she undertook those transactions".[109] Thus, Keane J held that damages should not be confined to the likely effects of particular decisions made by a plaintiff as to how she might choose commercially to exploit the assets purchased.[110] Hayne J explained that:

> If she had obtained some advantage, the value of the advantage would have mitigated the loss she otherwise suffered. If she had been left even worse off (for example by losing profit that otherwise would have been made), that additional loss may have aggravated her primary loss.[111]

The appellant could only put herself in the position she should have been in if the contract had been performed by buying replacement sperm from Xytex and this cost showed the value of the lost transaction for which she should be awarded damages.

Gageler J dissented. His Honour accepted that, for the purpose of calculating damages, it should not ordinarily make a difference as to whether a plaintiff could be expected to recoup the cost of equivalent goods purchased following a breach of contract by reselling or otherwise disposing of those goods.[112] However, in this case, there was a critical distinguishing factor. The appellant considered it unethical to profit from buying or selling sperm. Thus, Gageler J considered that the appellant was worse off only to the extent that she had to incur the additional cost of sourcing 1,996 straws of sperm from an alternative supplier and was not able to recoup that cost from her patients.[113]

The decision has been criticised, largely on the ground that the majority justices in the High Court failed fully to take into account the unique circumstances of the case. Barnett argues that that court's refusal to consider the fact that the appellant passed the costs of obtaining a substitute performance on to third parties meant she was put in a better position than if the contract had been performed and "undermines the compensatory principle behind contractual damages".[114] Barnett argues that the unusual nature of the market made it unconvincing to ignore the passing on of the cost.[115] As Gageler J pointed out, the frozen sperm was only ever to be used in treating patients in the appellant's practice.[116] On the other hand, Winterton considers that the result reached by the majority was correct, although he questions some aspects of the reasoning supporting that decision.[117]

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108 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [19], [142].

109 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [19], [38].

110 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [22].

111 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [129].

112 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [67].

113 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [72].

114 Barnett, "Contractual Expectations and Goods" (2014) 130 *Law Quarterly Review* 387, 387. Also Carter, Courtney and Tolhurst, "Issues of Principle in Assessing Contract Damages" (2014) 31 *Journal of Contract Law* 171.

115 Barnett, "Contractual Expectations and Goods" (2014) 130 *Law Quarterly Review* 387, 391.

116 *Clark v Macourt* [2013] HCA 56; (2013) 253 CLR 1, [72].

117 Winterton, "Clark v Macourt: Defective Sperm and Performance Substitutes in the High Court of Australia" (2014) 38 *Melbourne University Law Review* 387.

Reasons for the principle of mitigation

[27.75] There have been a number of justifications advanced for the principle of mitigation, which are discussed by Michael Bridge.[118] Mitigation has been linked to causation, the argument being that a plaintiff's loss cannot be said to have been caused by the defendant's breach if it could reasonably have been avoided by the plaintiff. Mitigation has also been linked to remoteness. It has sometimes been suggested that losses caused by a failure to mitigate are too remote to recover. Another argument is that a legal system should not sanction the economic waste which would be involved in allowing a plaintiff to watch the damages bill of the defendant rise without taking steps reasonably within the plaintiff's power to curb the loss. It has also been suggested that the role of mitigation is to mitigate the strictness of contractual obligations. A further justification for the principle of mitigation is that "it may be harsh on the defendant to permit recovery in full by a plaintiff who has the means to mitigate and thereby diminish his loss".[119] Bridge suggests that no one explanation may be conclusive for all aspects of mitigation, but all may provide insights into the doctrine.[120]

LIMITATIONS RELATING TO SPECIFIC TYPES OF CLAIM

Disappointment, distress, loss of reputation

[27.80] Damages in contract law primarily protect the parties against pecuniary losses caused by a breach of contract, that is, economic or "out of pocket" losses. Contract damages are not generally awarded to compensate non-pecuniary losses, such as any disappointment, anxiety, distress or loss of reputation occurring on breach of contract.[121] For example, in the frequently cited case of *Addis v Gramophone Co Ltd*,[122] the English Court of Appeal held that a wrongfully dismissed employee could not recover damages for injured feelings resulting from the "harsh and humiliating" manner in which he was treated.[123] However, there are exceptions where damages for non-pecuniary losses such as for disappointment and distress and also inconvenience may be awarded.

When damages for disappointment and distress may be available

[27.85] In *Baltic Shipping Co v Dillon*,[124] the High Court affirmed the rule against awarding damages for non-pecuniary losses in an action for breach of contract. The High Court also confirmed that the restrictive rule is subject to at least three significant exceptions. The case

118 Bridge, "Mitigation of Damages in Contract and the Meaning of Avoidable Loss" (1989) 105 *Law Quarterly Review* 398.

119 Bridge, "Mitigation of Damages in Contract and the Meaning of Avoidable Loss" (1989) 105 *Law Quarterly Review* 398, 410.

120 Bridge, "Mitigation of Damages in Contract and the Meaning of Avoidable Loss" (1989) 105 *Law Quarterly Review* 398, 410.

121 *Fink v Fink* (1946) 74 CLR 127, 144; *Baltic Shipping Co v Dillon* (1993) 176 CLR 344.

122 *Addis v Gramophone Co Ltd* [1909] AC 488.

123 *Addis v Gramophone Co Ltd* [1909] AC 488, 491. See also *Johnson v Unisys Ltd* [2001] UKHL 13; [2003] 1 AC 518. Cf *Malik v Bank of Credit and Commerce International SA (in liq)* [1998] AC 20.

124 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344.

concerned a claim for damages for disappointment and distress for breach of a contract to provide a holiday cruise.

First, the High Court in *Baltic Shipping Co v Dillon* confirmed that damages may be obtained for pain and suffering arising from physical injury caused by a breach of contract.[125]

Secondly, the High Court confirmed that damages for disappointment and distress will be available where they relate to physical inconvenience caused by a breach of contract. For example, in *Bailey v Bullock*[126] a solicitor breached his contract by failing to obtain possession of the plaintiff's house. As a result, the plaintiff had to live with his wife's parents in circumstances of physical inconvenience. Damages were awarded for this inconvenience and discomfort.[127] Damages for inconvenience may also be awarded in building cases where the breach of contract causes the plaintiff to physical discomfort, such as living with "offensive odours or a leaking roof, or in unsanitary or dirty conditions or being obliged to vacate the defective premises".[128] Inconvenience does not, however, include the time and trouble of dealing with the consequences of a breach of contract.[129]

Thirdly, the High Court in *Baltic Shipping Co v Dillon* confirmed that damages for disappointment and distress arising from a breach of contract will be available where an object of the contract was to provide enjoyment, relaxation or freedom from distress.[130] For example, damages for disappointment and distress have been awarded where solicitors in breach of their contract failed to obtain an order prohibiting a man from molesting the plaintiff[131] and where a surveyor negligently failed to discover that the house the plaintiff was proposing to buy was substantially affected by aircraft noise.[132] Importantly, under this exception, damages for disappointment and distress may be awarded where a contract to provide a holiday was breached. The facts of *Baltic Shipping Co v Dillon*[133] fell into this category. The plaintiff was a passenger on a cruise ship that sank halfway through the cruise. The defendants refunded a substantial proportion of the plaintiff's fare. The plaintiff also successfully obtained damages for personal injuries suffered and loss of property. One of the main issues before the High Court was whether or not the plaintiff was entitled to damages of $5,000 to compensate for the disappointment and distress at the loss of the facilities and enjoyment she had been promised. The High Court held that the plaintiff was entitled to such damages because the defendants had impliedly promised to provide a pleasurable holiday.[134]

125 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 362, 405.

126 *Bailey v Bullock* [1950] 2 All ER 1167.

127 See also *Athens-Macdonald Travel Service Pty Ltd v Kazis* [1970] SASR 264; *Boncristiano v Lohmann* [1998] 4 VR 82; *Farley v Skinner* [2002] 2 AC 732; *Hamilton Jones v David & Snape* [2003] EWHC 3147 (Ch); [2004] 1 WLR 924.

128 *Archibald v Powlett* (2017) 53 VR 645, [63] (McLeish JA, with whom Redlich and Osborn JJ agreed).

129 *Archibald v Powlett* (2017) 53 VR 645, [65] (McLeish JA, with whom Redlich and Osborn JJ agreed).

130 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 363, 370, 381, 405.

131 *Heywood v Wellers* [1976] 1 QB 446. See also *Aerial Advertising Co v Batchelors Peas Ltd (Manchester)* [1938] 2 All ER 788, 796–7.

132 *Farley v Skinner* [2001] UKHL 49; [2002] 2 AC 732.

133 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344.

134 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 371–2, 382, 406, cf also 366.

Reasons for the restrictive rule

[27.90] As we have noted, the rule that damages for breach of contract are not ordinarily awarded for disappointment or distress arising from breach of contract was accepted by the majority of the High Court in *Baltic Shipping Co v Dillon*.[135] In that case, McHugh J was more critical of the restrictive rule. His Honour noted that the reasons commonly given for the rule include arguments that damages for disappointment are difficult accurately to assess, that such losses are not within the contemplation of the parties and that allowing such damages would increase the cost of entering into contracts.[136] However, McHugh J noted that damages for disappointment or distress might be awarded in many actions of tort, such as defamation and false imprisonment. McHugh J noted that parties to many contracts will be aware that a breach would result in disappointment.[137] His Honour considered it at least arguable that the cost of meeting claims for disappointment or distress arising from breach of contract "does not outweigh the demands of distributive justice in ensuring that individuals are properly compensated for the harm which they suffer by reason of breaches of contract".[138] Had the matter been free from authority, McHugh J would not have subjected damages for disappointment and distress to any special rule. Rather, his Honour would have allowed liability for such losses to be regulated by the ordinary principles of remoteness and causation.[139] However, McHugh J also considered that because counsel for the plaintiff in *Baltic Shipping Co v Dillon* had not argued that the rule should be rejected, the step should not be taken in that case.[140]

In contrast to the common law, under the *UNIDROIT Principles of International Commercial Contracts 2010* ("*UPICC*"), the harm sustained as a result of non-performance of a contract for which an aggrieved party is entitled to compensation may encompass non-pecuniary harm, including for emotional distress.[141]

Effect of civil liability legislation

[27.92] Since the decision in *Baltic Shipping Co v Dillon*,[142] all States and Territories in Australia have enacted legislation that limits the damages that may be claimed by a plaintiff for personal injury caused by a breach of duty of care, whether claimed in tort or contract.[143] While the form of the legislation varies between the jurisdictions, it has been interpreted to apply to limit the damages that may be awarded for disappointment and distress arising from a breach of a contract duty.[144] In *Insight Vacations Pty Ltd v Young*[145] the plaintiff was

135 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 365, 369, 380.

136 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 395–7.

137 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 395–7.

138 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 396.

139 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 404.

140 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 405.

141 Article 7.4.2(2). On the *UNIDROIT Principles of International Commercial Contracts 2010*, see [1.180].

142 *Baltic Shipping Co v Dillon* (1993) 176 CLR 344.

143 *Civil Law (Wrongs) Act 2002* (ACT); *Civil Liability Act 2002* (NSW); *Personal Injuries (Liabilities and Damages) Act* (NT); *Civil Liability Act 2003* (Qld); *Civil Liability Act 1936* (SA); *Civil Liability Act 2002* (Tas); *Wrongs Act 1958* (Vic); *Civil Liability Act 2002* (WA).

144 See eg *Flight Centre Ltd v Louw* [2011] NSWSC 132; (2011) 78 NSWLR 656.

145 *Insight Vacations Pty Ltd v Young* [2010] NSWCA 137; (2010) 78 NSWLR 641, appeal dismissed on a different point in *Insight Vacations Pty Ltd v Young* [2011] HCA 16; (2011) 243 CLR 149.

injured while travelling on a bus in Slovakia as part of a tour organised by the defendant. The defendant was found to have breached its contractual duty to act with reasonable diligence, care and skill. The trial judge awarded the plaintiff damages to compensate for her injuries and also $8,000 for disappointment in being able to enjoy the remainder of the holiday after the accident. The NSW of Appeal Court held that the award of damages for disappointment was subject to the *Civil Liability Act 2002* (NSW), s 16,[146] which provides that damages for personal injury that relate to non-economic loss are to be determined in accordance with a table of recoverable amounts.[147] The plaintiff's damages for disappointment, not having been awarded in accordance with this table, were denied.[148]

The approach is inconsistent with the nature of the award of damages for disappointment and distress for breach of contract. What is being compensated is not physical injury or psychiatric illness but the disappointment caused by a breach of certain types of contract.[149] Nonetheless, the interpretation of the civil liability acts applying to limit this kind of claim is widespread and seemingly established.[150] The limitation does not apply to damages for physical inconvenience caused by a breach of contract.[151]

Contributory negligence

[27.95] In some cases, it might be argued that carelessness or negligence on the part of a plaintiff has contributed to the loss suffered by him or her following a breach of contract by the defendant. There are two possible legal responses to negligence by a plaintiff.

Breaking the chain of causation

[27.100] The first response is to find that negligence on the part of a plaintiff has broken the chain of causation between the defendant's breach and the plaintiff's loss. For example, in *Lexmead (Basingstoke) Ltd v Lewis*[152] a purchaser had purchased from retailers a towing hitch to couple his Land Rover to his trailer. Some time later a part of the towing hitch broke and was in an unsafe condition. The purchaser was aware of this fact but continued to tow using the hitch. Due to the defective state of the hitch, the trailer became detached, causing a serious accident. A claim was brought against the purchaser for negligence. The purchaser brought proceedings against the retailers claiming that the retailers were in breach of their implied obligation under the relevant *Sale of Goods Act* to supply a towing hitch fit for its

146 See also *Personal Injuries (Liabilities and Damages) Act* (NT), s 27; *Civil Liability Act 2003* (Qld), Ch 3; *Civil Liability Act 1936* (SA), s 52; *Civil Liability Act 2002* (Tas), s 27; *Wrongs Act 1958* (Vic) Pt VBA; *Civil Liability Act 2002* (WA), s 9.

147 *Insight Vacations Pty Ltd v Young* [2010] NSWCA 137; (2010) 78 NSWLR 641, [78]–[79], [129]–[130], [174]. Appeal dismissed, on a different point, in *Insight Vacations Pty Ltd v Young* [2011] HCA 16; (2011) 243 CLR 149.

148 See also *Flight Centre v Louw* [2011] NSWSC 132; (2011) 78 NSWLR 656.

149 See Walker and Lewins, "Dashed Expectations? The Impact of Civil Liability Legislation on Contractual Damages for Disappointment and Distress" (2014) 42 *Australian Business Law Review* 465.

150 *New South Wales v Ibbett* (2005) 65 NSWLR 168, [121]–[125]; *Insight Vacations Pty Ltd v Young* (2010) 78 NSWLR 641, [78], [125], [175]; *New South Wales v Corby* (2010) 76 NSWLR 439, [21]–[23]; *New South Wales v Williamson* [2011] NSWCA 183, [67]; *Thomas v Powercor Australia Ltd* [2011] VSC 586, [116]; *Lakic v Prior* [2016] VSC 293, [157]; *Archibald v Powlett* (2017) 53 VR 645, [60].

151 *Archibald v Powlett* (2017) 53 VR 645, [60].

152 *Lexmead (Basingstoke) Ltd v Lewis* [1982] AC 225.

purpose and that this breach was the cause of the accident. The House of Lords rejected this claim. The House of Lords held that the purchaser's conduct in continuing to use the towing hitch had broken the chain of causation between the retailers' breach and the accident that occurred.[153]

Reducing the damages of a careless plaintiff

[27.105] A second response to the case where carelessness or negligence on the part of a plaintiff has contributed to the loss suffered by him or her following a breach of contract by the defendant is to reduce the plaintiff's damages to account for the negligence. This response is now made possible through legislation in all Australian States and Territories in cases where the plaintiff has concurrent claims in tort and contract (i.e. where the defendant's breach of a duty of care gives rise to concurrent liability in the tort of negligence and in contract) and the plaintiff's own negligence would have reduced the liability of the defendant in tort.

Background to contributory negligence and contract

[27.110] Historically, the common law doctrine of contributory negligence provided a complete defence to an action for the tort of negligence. This doctrine has been varied in respect to tort actions by legislation in all Australian jurisdictions. The legislation permits a court to reduce the damages in tort awarded to a plaintiff whose negligence has contributed to his or her own loss to the extent that is "just and equitable".[154]

The common law doctrine of contributory negligence never applied to the law of contract. Prior to the decision in *Astley v Austrust Ltd*,[155] the relevant legislation did not specifically refer to breach of contract in defining the types of claim in which a court might reduce a plaintiff's damages on account of his or her contributory negligence. It had been suggested that the legislation permitting a court to apportion responsibility in tort actions in cases of contributory negligence by a plaintiff should be interpreted also to apply to contract cases, at least where the plaintiff had concurrent claims[156] in tort and contract.[157] However, in *Astley v Austrust Ltd*, the High Court of Australia held that the legislation did not apply to reduce an award of damages for breach of contract on grounds of contributory negligence.[158]

Apportioning liability under legislation for concurrent claims in tort and contract

[27.115] In all Australian States and Territories, legislation was amended in response to the decision in *Astley v Austrust Ltd*.[159] The amended legislation provides that liability may be

153 *Lexmead (Basingstoke) Ltd v Lewis* [1982] AC 225, 276–7.

154 *Civil Law (Wrongs) Act 2002* (ACT), s 102, *Law Reform (Miscellaneous Provisions) Act 1965* (NSW), 9(1); *Law Reform (Miscellaneous Provisions) Act* (NT), s 16; *Law Reform Act 1995* (Qld), s 10(1); *Law Reform (Contributory Negligence and Apportionment of Liability) Act 2001* (SA), s 7; *Wrongs Act 1954* (Tas), s 4; *Wrongs Act 1958* (Vic), s 26(1); *Law Reform (Contributory Negligence and Tortfeasors' Contribution) Act 1947* (WA), s 4(1).

155 *Astley v Austrust Ltd* [1999] HCA 6; (1999) 197 CLR 1.

156 On concurrent claims in tort and contract, see [2.20].

157 See, eg, *Bains Harding Construction and Roofing (Aust) Pty Ltd v McCredie Richmond & Partners Pty Ltd* (1988) 13 NSWLR 437.

158 *Astley v Austrust Ltd* [1999] HCA 6; (1999) 197 CLR 1 (Gleeson CJ, McHugh, Gummow and Hayne JJ, Callinan J dissenting on this point). See generally Davis and Knowler, "Down But Not Out: Contributory Negligence, Contract Statute and Common Law" (1999) 23 *Melbourne University Law Review* 795.

159 *Astley v Austrust Ltd* [1999] HCA 6; (1999) 197 CLR 1.

apportioned in respect of an act or omission that amounts to a breach of a contractual duty of care that is concurrent and coextensive with a duty of care in tort.[160] Accordingly, where the plaintiff has concurrent claims in tort and contract and the plaintiff's own negligence would have reduced the liability of the defendant in tort, the damages payable by the defendant may be reduced to take account of the negligence of the plaintiff in contributing to the loss, regardless of whether the plaintiff claims in tort or contract.

In *Astley v Austrust Ltd*, solicitors failed to give advice to a trust company on how to confine the liability of the company to its creditors. This was in breach of both the implied term of reasonable care that arises by operation of law in a contract for professional services and also the duty in tort to take reasonable care. The High Court held that the trust's own negligence had contributed to its loss.[161] The trust failed to make a proper investigation of the financial viability of the transaction into which it was entering. The High Court found that the applicable legislation (as it existed at that time) had no application to damages in contract. Accordingly, the award of damages payable by the solicitor to the trust for breach of contract was not reduced to reflect the contributory negligence of the trust.[162] The legislative amendments discussed earlier in this section mean that the damages payable by the solicitor would have been reduced by reason of the trust's own contribution to its loss.[163]

Comparison with other jurisdictions

[27.120] In contrast to the position in Australia, in England, it has been held that in cases where there is concurrent liability in tort and contract for negligence, liability may be apportioned in a contract case in accordance with contributory negligence legislation, even though that legislation does not refer to contract claims.[164] An even broader approach is taken in the *UPICC*, which effectively takes contributory negligence into account in all cases.[165] Article 7.4.7 provides that:

> Where harm is due in part to an act or omission of the aggrieved party or to another event as to which that party bears the risk, the amount of damages shall be reduced to the extent that these factors have contributed to the harm, having regard to the conduct of each of the parties.

Apportioning liability between multiple defendants

[27.125] Legislation allows an apportionment of damages between concurrent wrongdoers in "apportionable claims" involving damages for economic loss or damage to property "arising

160 *Civil Law (Wrongs) Act 2002* (ACT) s 101; *Law Reform (Miscellaneous Provisions) Act 1965* (NSW), s 8; *Law Reform Act 1995* (Qld), s 5; *Law Reform (Contributory Negligence and Apportionment of Liability) Act 2001* (SA), s 3; *Wrongs Act 1954* (Tas), s 2; *Wrongs Act 1958* (Vic), s 25; *Law Reform (Contributory Negligence and Tortfeasers' Contribution) Act 1947* (WA), s 3A. Also to similar effect: *Law Reform (Miscellaneous Provisions) Act* (NT), s 15.

161 *Astley v Austrust Ltd* [1999] HCA 6; (1999) 197 CLR 1, [36].

162 See also *Arthur Young & Co v WA Chip & Pulp Co Pty Ltd* [1989] WAR 100.

163 Another example is *O'Meara v Dominican Fathers* [2003] ACTCA 24; (2003) 153 ACTR 1.

164 See *Forsikringsaktieselskapet Vesta v Butcher* [1989] 1 AC 852; *Barclays Bank plc v Fairclough Building Ltd* [1995] QB 214.

165 See [1.180].

from a failure to take reasonable care" and in cases of misleading and deceptive conduct.[166] The provisions raise a range of issues which are beyond the scope of this chapter.[167]

Loss of bargain damages and termination under a term

[27.130] The expressions *loss of bargain* or *loss of profit* damages describe a type of expectation damages commonly awarded when a contract is terminated. Loss of bargain damages are based on the price the plaintiff would have received if the contract had been performed as promised, less the price the plaintiff would receive by entering into a substitute transaction. For example, if a lessor terminates a lease following a breach by the lessee, loss of bargain damages would be the difference between the rent the lessor would have obtained under the contract if the lease had run its full term and the rent the lessor could obtain on the market over the period between termination and the end of the term under the original lease.

A plaintiff will generally be entitled to loss of bargain damages where the plaintiff terminates following a breach which at common law gives rise to a right to terminate.[168] However, in *Shevill v Builders Licensing Board*[169] the High Court held that loss of bargain damages will not be available where a plaintiff has acted pursuant to a term in the contract giving a right to terminate for certain breaches but would not have had a right to terminate conferred by the common law. The High Court affirmed in *Progressive Mailing House Pty Ltd v Tabali Pty Ltd*[170] that the right to loss of bargain damages will depend on the plaintiff showing that, in addition to any term in the contract giving a right to terminate for the breach that has occurred, the plaintiff would also have been entitled to terminate for the same breach under the common law rules on termination.[171]

In *Shevill v Builders Licensing Board*[172] a lessor terminated a commercial lease of land pursuant to a term in the contract. The right to terminate had been triggered by rent being outstanding for a period of 14 days. The High Court considered that this delay in rent would not have entitled the lessor to terminate under the common law. This was because the term in question was not sufficiently important to be a condition and the breach was not sufficiently serious to amount to a repudiation of the contract.[173] Accordingly, the only basis for termination was the term in the contract entitling the lessor to terminate for non-payment. Applying the restrictive rule discussed earlier in this section, the High Court held that because the lessor could rely only on a contractual right to terminate, and not on a common law right, the lessor was entitled to receive arrears in rent, but not loss of bargain damages. In contrast,

166 *Civil Law (Wrongs) Act 2002* (ACT), s 107B; *Civil Liability Act 2002* (NSW), s 34; *Proportionate Liability Act* (NT), s 4; *Law Reform (Contributory Negligence and Apportionment of Liability) Act 2001* (SA), ss 3(2), 8; *Civil Liability Act 2002* (Tas), s 43A; *Wrongs Act 1958* (Vic), s 24AF; *Civil Liability Act 2002* (WA), s 5AI. Also to similar effect: *Civil Liability Act 2003* (Qld), s 28.

167 See further McDonald, "Proportionate Liability in Australia: The Devil in the Detail" (2005) 26 *Australian Bar Review* 29; Watson, "From Contribution to Apportioned Contribution to Proportionate Liability" (2004) 78 *Australian Law Journal* 126.

168 *Sunbird Plaza Pty Ltd v Maloney* (1988) 166 CLR 245, 260, 273.

169 *Shevill v Builders Licensing Board* (1982) 149 CLR 620.

170 *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17.

171 See further Nicholson, "Loss of Bargain Damages for Breach of a Non-Essential Term" (1988) 1 *Journal of Contract Law* 64.

172 *Shevill v Builders Licensing Board* (1982) 149 CLR 620.

173 *Shevill v Builders Licensing Board* (1982) 149 CLR 620.

in *Progressive Mailing House Pty Ltd v Tabali Pty Ltd*[174] there were a number of breaches of contract that not only entitled the lessor to terminate under a term of the contract but also constituted a repudiation of the contract. Because the lessor could rely on a common law right to justify termination, the lessor was entitled to claim loss of bargain damages.

The restriction identified in *Shevill v Builders Licensing Board* on the right of a plaintiff to claim loss of bargain damages has been rationalised on the ground of causation. Courts have suggested that, where a plaintiff terminates under a contractual term rather than a common law right, the loss of the bargain is attributable to the plaintiff's exercise of his or her contractual power to terminate, and not to the breach.[175] This reasoning has been criticised.[176] The purpose of a clause in a contract providing an express right to terminate in response to certain specified breaches of contract is to avoid the need for a plaintiff to justify a decision to terminate by reference to the common law grounds. The utility of such a clause to a plaintiff is undermined if, having terminated the contract, substantial loss of bargain damages are not available. It has been suggested that the restriction on loss of bargain damages identified in *Shevill v Builders Licensing Board* should be revisited, but as yet this has not occurred.[177]

Parties can avoid the restriction on loss of bargain damages through careful drafting.[178] In particular, leases now commonly contain what are sometimes termed "anti- *Shevill*" clauses. These clauses provide that specified terms of the lease are "essential terms", that any breach of those terms will be "fundamental" and that the landlord retains the right to damages on termination by reason of a breach of those essential terms. In *Gumland Property Holdings Pty Limited v Duffy Bros Fruit Market (Campbelltown) Pty Limited*,[179] the High Court confirmed that such clauses will be effective and that effect should be given to the clearly expressed intentions of the parties in such cases.

Damages for the late payment of money

[27.135] There will generally be a delay between the time a plaintiff suffers loss from a breach of contract and the time at which damages to compensate that loss are actually recovered following judgment in favour of the plaintiff. During this period, the general rule that damages are assessed at the date of the breach means that a plaintiff is vulnerable to the effects of inflation.[180] Further, during the period between the loss arising and compensation being paid, the plaintiff may suffer the loss of the use of money paid away or withheld by reason of the breach. To compensate for the loss caused by the breach, the plaintiff may borrow money and thus incur interest. Alternatively, the plaintiff may incur an opportunity cost in being deprived of money which otherwise could have been invested with interest or used to reduce an existing indebtedness.

174 See *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17.

175 *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17, 31; *AMEV-UDC Finance Ltd v Austin* (1986) 162 CLR 170, 217.

176 See, eg, Nicholson, "Loss of Bargain Damages for Breach of a Non-essential Term" (1988-9) 1 *Journal of Contract Law* 64.

177 *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* (1985) 157 CLR 17, 55–6; *AMEV-UDC Finance Ltd v Austin* (1986) 162 CLR 170, 206–7, 217–8.

178 See further Carter, "Termination Clauses" (1990) 3 *Journal of Contract Law* 90, 113–4.

179 *Gumland Property Holdings Pty Limited v Duffy Bros Fruit Market (Campbelltown) Pty Limited* [2008] HCA 10; (2008) 234 CLR 237 (Gleeson CJ, Kirby, Heydon, Crennan and Kiefel JJ).

180 On the time for assessing damages, see [26.20].

Statute gives courts power to order interest to be paid on damages.[181] In the absence of applicable or appropriate legislative power, the common law has traditionally refused to award interest as compensation for the late payment of damages.[182] However, in *Hungerfords v Walker*,[183] the High Court confirmed that a plaintiff may recover damages, based on an applicable interest rate, for the loss of the use of money that the defendant's breach of contract has caused to be paid away or withheld.[184] The right to damages for the loss of use of money must be established according to normal principles in any particular case.[185] In *Hungerfords v Walker*, the High Court considered that such losses would, in most cases, fall within the first limb of the remoteness rule in *Hadley v Baxendale*.[186] Mason and Wilson CJ explained that the costs involved in the loss of use of money — whether the lost opportunity of investing that money elsewhere or the cost of borrowing to replace money paid away or withheld — was a plainly foreseeable loss.[187] It was within the common understanding that these costs would be involved where a plaintiff was deprived of the use of his or her money.

The rule in *Bain v Fothergill*

[27.140] The rule in *Bain v Fothergill*,[188] formulated in the House of Lords and subsequently accepted in Australia,[189] precludes a purchaser from recovering expectation damages in a case where, under a contract for the sale of land, a vendor, without lack of good faith, is unable to convey good title to the land.[190] Under the rule in *Bain v Fothergill*, the purchaser is limited instead to reliance damages, based on the plaintiff's reasonable expenses incurred in investigating the title to the land. To establish good faith, the vendor is normally required to show that he or she used best endeavours to remove the defect from the title.[191] The rule in *Bain v Fothergill* does not apply in cases of fraud by the vendor.[192] The rule has been abolished in Queensland, New South Wales and the Northern Territory.[193]

181 *Court Procedure Rules 2006* (ACT), rr 1619–1623; *Civil Procedure Act 2005* (NSW), Pt 7 Div 3; *Supreme Court Act* (NT), ss 84, 85; *Supreme Court Act 1935* (SA), ss 30C, 114; *Civil Proceedings Act 1991* (Qld), ss 58–59; *Supreme Court Civil Procedure Act 1932* (Tas), ss 34, 165; *Supreme Court Act 1986* (Vic), ss 60, 101; *Supreme Court Act 1935* (WA), s 32. See generally Tilbury, *Civil Remedies* (Vol I, 1990), pp 168–72.

182 See, eg, *London Chatham and Dover Railway Co v South Eastern Railway Co* [1893] AC 429.

183 *Hungerfords v Walker* (1989) 171 CLR 125.

184 *Hungerfords v Walker* (1989) 171 CLR 125, 144, 152, Dawson J dissenting.

185 See also *Hobartville Stud Pty Ltd v Union Insurance Co Ltd* (1991) 25 NSWLR 358, 364; *Garraway Metals Pty Ltd v Comalco Aluminium Ltd* (1993) 114 ALR 118.

186 *Hadley v Baxendale* (1854) 9 Exch 341; 156 ER 145: see [27.25].

187 *Hungerfords v Walker* (1989) 171 CLR 125, 143.

188 *Bain v Fothergill* (1874) LR 7 HL 158. The rule was first stated in *Flureau v Thornhill* (1776) 2 W Bl 1078; 96 ER 635.

189 See, eg, *Powys v Brown* (1924) 25 SR (NSW) 65; *Godfrey Constructions Pty Ltd v Kanangra Park Pty Ltd* (1972) 128 CLR 529.

190 See generally Carter, "Reform of the Rule in *Bain v Fothergill*" (1991) 4 *Journal of Contract Law* 230.

191 See, eg, *Nosske v McGinnis* (1932) 47 CLR 563; *Malhotra v Choudhury* [1980] Ch 52.

192 *Bain v Fothergill* (1874) LR 7 HL 158. See also *ASA Constructions Pty Ltd v Iwanov* [1975] 1 NSWLR 512.

193 See *Property Law Act 1974* (Qld), s 68; *Conveyancing Act 1919* (NSW), s 54B; *Law of Property Act* (NT), s 70.

DAMAGES FOR ANTICIPATORY BREACH

Repudiation must be accepted

[27.145] As already discussed,[194] repudiation of a contract by one party before the time set for performance does not of itself give the other party a right to damages.[195] For an action to exist for damages for anticipatory breach, the other party needs to accept the repudiation and terminate the contract.

Date for assessing damages for anticipatory breach

[27.150] Where a repudiation of a contract is accepted and the contract is terminated before the date set for performance on grounds of anticipatory breach, damages are usually assessed at the time performance was due.[196] To assess damages at the date of the breach would effectively accelerate the defendant's obligations.[197] On when a court will take events occurring after termination into account in assessing damages see [26.20].

Mitigation and anticipatory breach

[27.155] Where a repudiation of a contract precedes the time for performance, the plaintiff will have no right to damages unless he or she accepts the repudiation by terminating the contract. No question of mitigation arises until that time.

Once a contract has been terminated for anticipatory breach, the principle of mitigation will require the plaintiff to take reasonable steps to reduce his or her losses. The expectation that a plaintiff will mitigate his or her losses may qualify the normal principle that damages are assessed at the date at which performance was required under the contract. Thus, in sale of goods cases, mitigation may require a plaintiff to take any reasonable opportunity of reducing his or her losses by buying or selling at a price which is likely to be more favourable at an earlier date.[198] For example, consider a case where a seller repudiates a contract for the sale of wheat prior to the date set for performance. Prima facie, damages would be based on how much the buyer must pay to obtain a substitute quantity of wheat in the market at the time set by the original contract for delivery. However, if the market price for wheat appeared to be rising at the time the contract was terminated, the buyer would be expected to buy a substitute quantity of wheat at the earliest reasonable opportunity. If, contrary to expectations, the market moved against the buyer, so that the price at the date for delivery was lower than the price paid by the buyer, damages would nonetheless be assessed at the time of the buyer's purchase.[199]

194 See Chapter 22.

195 *Progressive Mailing House v Tabali Pty Ltd* (1985) 157 CLR 17, 48; *Foran v Wight* (1989) 168 CLR 385, 416–7, 441–2.

196 See, eg, *Melachrino v Nickoll and Knight* [1920] 1 KB 693; *Tai Hing Cotton Mill Ltd v Kamsing Knitting Factory* [1979] AC 91; *Hoffman v Cali* [1985] 1 Qd R 253; *Ronnoc Finance v Spectrum Network Systems Ltd* (1997) 45 NSWLR 624.

197 Carter, *Contract Law in Australia* (7th ed, 2018), [36-04]; Greig and Davis, *The Law of Contract* (1987), p 1420.

198 *Garnac Grain Co Inc v HNF Faure & Fairclough Ltd* [1968] AC 1130, 1140.

199 *Melachrino v Nickoll and Knight* [1920] 1 KB 693, 697.

CHAPTER **28**

The rule against penalties

[28.05] As a way of managing future risks, contracting parties may, and in commercial contracts commonly do, include in their contract terms that provide a monetary incentive to performance as well as providing for compensation for the probable losses incurred if performance does not occur. As discussed in Chapter 19, in some cases, the contract will provide that specified breaches give rise to a right of the party not in breach to terminate the contract. In other cases, the contract may provide for the payment of money in the event of breach. Parties may also impose additional obligations on the occurrence of specified events, although those events do not amount to a breach of contract. These kinds of terms are sometimes described as *secondary* or *collateral* contractual stipulations, in that they do not impose a primary obligation but rather provide for the consequences of other events.

Parties are free to make these kinds of arrangements, but there are limits to what can be agreed, found in the doctrines of penalties. The penalties doctrine in Australia applies to contractual stipulations "in the nature of a security for and in terrorem of the satisfaction of the primary stipulation".[1]

There are three stages to the penalty analysis:

first, whether the penalties doctrine is engaged;

second, whether the impugned stipulation is penal; and,

third, the consequences of a determination that a stipulation is penal.[2]

As will be apparent in considering stages 1 and 3, the doctrine of penalties in Australia is in a state of "flux".[3] The traditional application of the penalty doctrine in law is to terms

1 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [118] (Gageler J), quoting *Andrews v Australia and New Zealand Banking Group Ltd* (2012) 247 CLR 205, 216 [10].

2 *Australia Capital Financial Management Pty Ltd v Linfield Developments Pty Ltd* (2017) [2017] NSWCA 99, [357].

3 Eldridge, 'The New Law of Penalties: Mapping the Terrain' [2018] *Journal of Business Law* 637. Also Morgan, "The Penalty Clause Doctrine: Unlovable but Untouchable" (2016) 75 *Cambridge Law Journal* 11; Carter,

providing for the payment of money in the event of breach of contract. In equity, the doctrine also applies to stipulations for the payment of money on the occurrence or non-occurrence of events that are not obligations under the contract. It appears, but is uncertain, in Australia that the consequences of a stipulation being penal are different in law and in equity.[4]

IS THE PENALTIES DOCTRINE ENGAGED?

Penalties and terms providing for the payment of money in the event of breach (agreed damages)

[28.10] The parties to a contract may specify in that contract an amount that is payable to the plaintiff in the event of certain breaches of contract, sometimes known as *liquidated* or *agreed* damages clauses. A term providing for the amount payable on breach "makes for greater certainty by allowing the parties to determine more precisely their rights and liabilities consequent upon breach or termination".[5] If one party breaches the contract or otherwise fails to meet a contractual stipulation, the other party may sue to enforce the clause and recover the liquidated sum,[6] instead of being required to prove his or her loss in an action for damages. Such provisions will be valid and binding provided they do not overstep and amount to a penalty. Such terms are therefore always susceptible to being scrutinised under the penalties doctrine.

Collateral (non-promissory) stipulations designed as security for the performance of a primary stipulation

[28.15] Until the decision in *Andrews v Australia and New Zealand Banking Group Ltd*,[7] in Australia it was generally considered that a contractual provision providing for the payment of money on occurrence of certain events was only capable of being a penalty if it secured the performance of a contractual obligation.[8] This meant that the doctrine of penalties was considered only to apply to sums payable in the event of a breach of contract.[9] Sums payable in the event of the failure of a contract term, condition or stipulation, which there was no obligation to perform could not, on this view, be the subject of scrutiny under the penalties doctrine because they were not conditioned on a breach. For example, a fee payable by a

Courtney and Tolhurst, "Assessment of Contractual Penalties: Dunlop Deflated" (2017) 34 *Journal of Contract Law* 4.

4 Eldridge, 'The New Law of Penalties: Mapping the Terrain' [2018] *Journal of Business Law* 637. Cf Tiverios, "A Restatement of Relief Against Contractual Penalties (I): Underlying Principles in Equity and at Common Law" (2017) 11 *Journal of Equity* 1 and "A Restatement of Relief Against Contractual Penalties (II): A Framework for Applying the Australian and English Approaches" (2017) 11 *Journal of Equity* 185.

5 *AMEV-UDC Finance Ltd v Austin* (1986) 162 CLR 170, 193.

6 See Chapter 29.

7 *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205, [78]. For different views on the merits of the decision see Carter et al, "Contractual Penalties: Resurrecting the Equitable Jurisdiction" ' (2013) 30 *Journal of Contract Law* 99 and Peel, "The Rule Against Penalties" (2013) *Law Quarterly Review* 129.

8 *Cedar Meats (Aust) Pty Ltd v Five Star Lamb Pty Ltd* [2014] VSCA 32, [43]. See also *Cavendish Square Holding BV v Talal El Makdessi; Parking Eye Ltd v Beavis* [2015] UKSC 67.

9 *Interstar Wholesale Finance Pty Ltd v Integral Home Loans Pty Ltd* [2008] NSWCA 310, [106]–[134]. Leave to Appeal refused in *Integral Home Loans Pty Ltd v Interstar Wholesale Finance Pty Ltd* [2009] HCA Transcript 87. Also *Kowalczuk v Accom Finance* [2008] NSWCA 343; (2008) 77 NSWLR 205, [162].

customer for breaching the contract by terminating prior to the expiry of a fixed term would be subject to review under the doctrine of penalties but a fee payable by the customer for terminating early pursuant to a term of the contract would not. This view had been criticised as anomalous. In *Bridge v Campbell Discount*, Lord Denning stated:

> Let no one mistake the injustice of this. It means that equity commits itself to this absurd paradox: it will grant relief to a man who breaks his contract but will penalise the man who keeps it. [10]

In *Andrews v Australia and New Zealand Banking Group Ltd* (*Andrews*) [11] the High Court (French CJ, Gummow, Crennan, Kiefel and Bell JJ) held that that equity retained a jurisdiction over penalties and this jurisdiction was not limited to where there had been a breach of contract.[12] The equitable jurisdiction had its origins in the granting of relief against the enforcement of conditional bonds. These instruments provided for the payment of money on a fixed date, subject to a condition that the bond should be discharged upon the satisfaction of some other stipulation, such as the rendering of services or the provision of goods. Chancery would grant relief against the enforcement of conditional bonds where the party relying on the bond was able to seek compensation for the loss actually sustained.[13] Subsequently courts of law began to grant relief against penalties. This equitable jurisdiction had not "withered on the vine" after the courts of common law began to grant relief against the enforcement of penal stipulations triggered by a breach of contract.[14]

The High Court concluded that a contract term imposing a sum payable in the event of certain contingent events may be regarded as a penalty if it secures a primary stipulation, even though that stipulation is not a contractual promise.[15] The court explained that:

> In general terms, a stipulation prima facie imposes a penalty on a party if, as a matter of substance, it is collateral (or accessory) to a primary stipulation in favour of a second party and this collateral stipulation, upon the failure of the primary stipulation, imposes on the first party an additional detriment, the penalty, to the benefit of the second party. In that sense, the collateral or accessory stipulation are described as being in the nature of a security for and in terrorem of the satisfaction of the primary stipulation. If compensation can be made to the second party for the prejudice suffered by failure of the primary stipulation, the collateral stipulation and the penalty are enforced only to the extent of that compensation. [16]

The case involved a representative action brought by ANZ customers which, among other things, sought a declaration that certain provisions in their customer contracts — honour, dishonour, over limit fees and late payment fees — were void and unenforceable as penalties.[17] The Federal Court found that the penalty doctrine applied to the late penalty fees alone as these were the only fees payable upon a breach of contract. The customers subsequently applied for

10 *Bridge v Campbell Discount* [1962] AC 600, 629.

11 *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205.

12 *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205, [78]. For different views on the merits of the decision see Carter et al, "Contractual Penalties: Resurrecting the Equitable Jurisdiction" ' (2013) 30 *Journal of Contract Law* 99 and Peel, "The Rule Against Penalties" (2013) 129 *Law Quarterly Review* 129.

13 *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205, [11].

14 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [31].

15 *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205.

16 *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205, [10].

17 *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205.

leave to appeal to the Full Court of the Federal Court. The grounds for appeal concerned "the nature and scope of the jurisdiction to relieve against penalties and the question whether relief is available only if the penalty is imposed upon a breach of contract".[18] The customers then applied for that appeal to be removed directly to the High Court because, on the current line of authorities, they would not be successful before the Full Federal Court.

The High Court held that the fact the fees were not charged by the bank upon breach of contract and that the customers had no responsibility or obligation to avoid the occurrence of events upon which those fees were charged did not render them incapable of being characterised as penalties.

The effect of the decision in *Andrews* is that a sum payable on the occurrence of a condition, that does not amount to a contractual obligation, may be considered a penalty in equity if it is out of all proportion to the party's interest in securing performance of the contract. As explained by the Victorian Supreme Court of Appeal in *Cedar Meats (Aust) Pty Ltd v Five Star Lamb Pty Ltd*:

> where it is sought to secure the performance of a condition and, instead of exacting a promise from the obligor to perform the condition, the obligee exacts a promise from the obligor to pay a sum of money … if the condition not be performed, the promise is properly to be viewed as a security for the satisfaction of the condition and so, therefore, if the sum of money … is excessive and unconscionable it may ... be treated as penal.[19]

The approach in England

[28.20] This approach, of recognising a penalty jurisdiction extending beyond sums payable on breach of contract, was rejected by the English Supreme Court in *Makdessi v Cavendish Square Holdings BV* ("*Cavendish*").[20] *Cavendish* concerned a commercial contract for the sale of a controlling stake in a marketing company. Under the contract, if the vendor failed to comply with certain restrictive covenants, the vendor would lose its entitlement to certain payment instalments and could be required to sell remaining shares at an adjusted price. The vendor breached the restriction and the purchaser sought to enforce terms proving that no further payments should be made and for the sale of the remaining shares. The vendor claimed the clauses were penal and unenforceable.

The Court of Appeal held that the relevant clauses were not genuine pre-estimates of loss. Their function was to act as a deterrent. Therefore they were unenforceable penalties. The purchaser appealed.

Lord Neuberger and Lord Sumption (with whom Lord Carnwarth agreed) held the provisions were not open to review as a penalty. They operated as price adjustment clauses, not secondary obligations payable in the event of breach.[21] In this regard, the clauses pursued legitimate commercial interests of the buyer.[22] Lord Hodge (with whom Lord Clarke agreed on this point) held the provisions — even if secondary obligations — were not unenforceable.[23]

18 *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205, [18].

19 *Cedar Meats (Aust) Pty Ltd v Five Star Lamb Pty Ltd* [2014] VSCA 32, [43].

20 *Makdessi v Cavendish Square Holdings BV* [2015] UKSC 67; [2016] AC 1172.

21 *Makdessi v Cavendish Square Holdings BV* [2015] UKSC 67; [2016] AC 1172, [76].

22 *Makdessi v Cavendish Square Holdings BV* [2015] UKSC 67; [2016] AC 1172, [76].

23 *Makdessi v Cavendish Square Holdings BV* [2015] UKSC 67; [2016] AC 1172, [282].

The Supreme Court rejected the extension by the High Court in *Andrews* of the rule against penalties beyond circumstances involving breach of contract. Lord Neuberger PSC and Lord Sumption JSC (with whom Lord Carnwath JSC agreed) stated that:

> where a contract contains an obligation on one party to perform an act, and also provides that, if he does not perform it, he will pay the other party a specified sum of money, the obligation to pay the specified sum is a secondary obligation which is capable of being a penalty; but if the contract does not impose (expressly or impliedly) an obligation to perform the act, but simply provides that, if one party does not perform, he will pay the other party a specified sum, the obligation to pay the specified sum is a conditional primary obligation and cannot be a penalty.[24]

The Supreme Court described the approach taken by the High Court of Australia as representing a "radical departure from previous understanding of the law".[25] The Supreme Court also thought that there were legal and commercial policy reasons against introducing such a rule. Lord Neuberger PSC and Lord Sumption JSC (with whom Lord Carnwath JSC agreed) stated:

> the High Court's decision does not address the major legal and commercial implications of transforming a rule for controlling remedies for breach of contract into a jurisdiction to review the content of the substantive obligations which the parties have agreed. Modern contracts contain a very great variety of contingent obligations … The potential assimilation of all of these to clauses imposing penal remedies for breach of contract would represent the expansion of the courts' supervisory jurisdiction into a new territory of uncertain boundaries, which has hitherto been treated as wholly governed by mutual agreement.[26]

In *Paciocco v Australia and New Zealand Banking Group Ltd* (*Paciocco*), both French CJ and Gageler J responded to this criticism. Gageler J expressed the view that the Supreme Court's views were based upon a misunderstanding of the scope of what was actually decided in *Andrews*.[27] French CJ commented that although:

> countries of the common law world have a shared heritage which they owe to the unwritten law of the United Kingdom… [t]hat shared heritage … does not import the necessity, of development proceeding on similar lines.[28]

Contract terms giving rise to additional rights and obligations

[28.25] In *Andrews v Australia and New Zealand Banking Group Ltd*, the High Court held that a stipulation providing for the payment of money in circumstances that do not involve a breach of contract will not attract the penalty doctrine where it gives rise "consensually to an additional obligation".[29] The key distinction therefore is between contract stipulations or terms that impose an obligation to pay money if a condition (not involving an obligation) is not met and a term that provides for the payment of money in return for the other party undertaking additional obligations or providing an additional service. Neither category

24 *Makdessi v Cavendish Square Holdings BV* [2015] UKSC 67; [2016] AC 1172, [14].

25 *Makdessi v Cavendish Square Holdings BV* [2015] UKSC 67; [2016] AC 1172, [41].

26 *Makdessi v Cavendish Square Holdings BV* [2015] UKSC 67; [2016] AC 1172, [42].

27 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [121]–[127].

28 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [7].

29 *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205, [80]–[82].

involves an obligation that is breached in the event of non-performance. Only the first type of term is able to be reviewed under the penalty doctrine.

The distinction between these kinds of terms was considered by the Federal Court in *Paciocco v Australia and New Zealand Banking Group Ltd*.[30] The case arose from the same class action litigation that gave rise to *Andrews*. It concerned two credit card accounts that entitled the bank to charge honour, dishonor, over limit and late payment fees. Paciocco claimed that the terms constituted penalties in law and at equity. The primary judge found that the late payment fees constituted penalties. The primary judge found that the honour, dishonor, and over limit fees were not able to be reviewed as penalties. This was because they were fees charged to the customer of the bank for additional services. The bank successfully appealed to the Full Federal Court in regard the late payment fee, and this decision was affirmed by the High Court.[31] The Full Federal Court upheld the primary judge's treatment of the various honour, dishonor and over limit fees, agreeing that fees in question were payable in respect to financial accommodation.[32]

A similar approach is evidenced in *Cedar Meats (Aust) Pty Ltd v Five Star Lamb Pty Ltd*.[33] The respondent (Five Star) entered into an agreement with the appellant (Cedar Meats) for the manufacturing, processing and packaging of lamb products at Cedar Meats' abattoir (the agreement). Relevantly under the agreement, if the actual daily volume of lamb delivered by Five Star to Cedar Meats fell below an agreed daily volume, Cedar Meats would be entitled to payment for a portion of the shortfall in price (the shortfall payments).

From the agreement's commencement, Five Star fell short in providing Cedar Meats with the agreed daily volume. However, Cedar Meats wanted to provide as much help to Five Star as possible and therefore never pressed for the shortfall payments. In 2010, Five Star's financial situation deteriorated and eventually production ceased at the abattoir because of the very low volume of lamb being delivered. Around that time, Five Star and Cedar Meats met to discuss the ending of the agreement. Cedar Meats did not sign the termination agreement prepared by Five Star; instead Cedar Meats stated that it was prepared to waive the shortfall payments and accept non-deliveries as long as Five Star recommenced production with Cedar Meats whenever it was able to do so.

Throughout 2011, Cedar Meats agreed on occasions to process small quantities of lamb for Five Star when Cedar Meats had space left over from its processing of other products. Both parties saw this arrangement as ad hoc and, among other changes, Cedar Meats charged prices that were higher than those stipulated under the agreement.

When Five Star resumed production in late 2011, it retained another processor rather than returning to Cedar Meats. Cedar Meats then claimed for shortfall payments owing under the agreement. The Victorian Supreme Court of Appeal accepted Cedar Meats' contention that the shortfall payments provisions did not impose a contractual obligation on Five Star to deliver the agreed daily volumes. However, the court also considered the issue was of little consequence. The relevant clause was a promise to pay a sum of money in the event that the relevant qualities of lamb were not provided. Therefore, the sum "(subject once again to

30 *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50; (2015) 236 FCR 199.

31 See [28.25].

32 *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, [215].

33 *Cedar Meats (Aust) Pty Ltd v Five Star Lamb Pty Ltd* [2014] VSCA 32.

questions of excessiveness and unconscionability) was capable of being penal".[34] The matter was remitted to the lower court to make this determination.

IS THE IMPUGNED STIPULATION PENAL?

[28.30] In *Paciocco v Australia and New Zealand Banking Group Ltd*,[35] the High Court clarified a contractual stipulation providing for the payment of a sum on the occurrence of a breach of contract or a specified condition will only be impugned as a penalty where it is out of all proportion to the interest in contract performance that it purports to protect. Thus, Kiefel J, with whom French CJ agreed on this point, described the question as being "whether the sum is 'out of all proportion' to the interests said to be damaged".[36] Gageler J stated that the inquiry was into whether "the stipulation in issue is properly characterised as having no purpose other than to punish",[37] as opposed to protecting the innocent party's interest in contractual performance.[38] Keane J expressed the question as being whether the sum "is exorbitant or unconscionable when regard is had to the innocent party's interest in the performance of the contract".[39] Keane J emphasised that '[i]t is only where the impugned provision requires a payment … which is out of all proportion to the legitimate commercial interests of the party relying upon it that the punitive character of the provision stands revealed'.[40]

This approach to the test for a penalty is similar to that adopted in England in *Makdessi v Cavendish Square Holdings BV (Cavendish)*.[41] In *Cavendish*, the Supreme Court stated that the "true test" of a penalty

> is whether the impugned provision is a secondary obligation which imposes a detriment on the contract-breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation. The innocent party can have no proper interest in simply punishing the defaulter. His interest is in performance or in some appropriate alternative to performance.[42]

Carter, Courtney and Tolhurst have observed that the current approach considerably reduces the likely scope of the penalty doctrine, possibly to "vanishing point".[43] The reason for the high threshold in finding a penalty relates to the important principle of freedom of contract. In *Ringrow Pty Ltd v BP Australia Pty Ltd* the High Court explained that:

> The law of contract normally upholds the freedom of parties, with no relevant disability, to agree upon the terms of their future relationships … Exceptions from that freedom of contract require good reason to attract judicial intervention to set aside the bargains upon which parties

34 *Cedar Meats (Aust) Pty Ltd v Five Star Lamb Pty Ltd* [2014] VSCA 32, [51].

35 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525.

36 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [57], [29].

37 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [166].

38 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [161].

39 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [270].

40 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [256].

41 *Makdessi v Cavendish Square Holdings BV* [2015] UKSC 67; [2016] AC 1172.

42 *Makdessi v Cavendish Square Holdings BV* [2015] UKSC 67; [2016] AC 1172, [32].

43 Carter, Courtney and Tolhurst, 'Assessment of Contractual Penalties: Dunlop Deflated' (2017) 34 *Journal of Contract Law* 4, 7. See also Day, "A Pyrrhic Victory for the Doctrine Against Penalties: Makdessi v Cavendish Square Holding BV" [2016] *Journal of Business Law* 115.

> of full capacity have agreed. That is why the law on penalties is, and is expressed to be, an exception from the general rule.[44]

This importance of contractual freedom was also emphasised by the High Court in *Paciocco v Australia and New Zealand Banking Group Ltd*.[45] Keane J stated:

> Given the importance of the values of commercial certainty and freedom of contract in the law, the courts will not lightly invalidate a contractual provision for an agreed payment on the ground that it has the character of a punishment.[46]

Determining whether an agreed damages clause is a penalty

Interests that may be protected by an agreed damages clause

[28.35] Prior to the decision in *Paciocco v Australia and New Zealand Banking Group Ltd*,[47] courts typically proceeded by comparing the sum imposed by the contract as payable in the event of breach with the probable damages payable for that breach. As expressed in *Ringrow Pty Ltd v BP Australia Pty Ltd*, "in typical penalty cases, the court compares what would be recoverable as unliquidated damages with the sum of money stipulated as payable on breach".[48]

In *Paciocco v Australia and New Zealand Banking Group Ltd*[49] the High Court reformulated the test for a penalty to consider the effect of an agreed damages clause in protecting interests that go beyond compensation for loss occasioned by breach, namely the parties' commercial interests or interests in contract performance.[50] Only Nettle J, dissenting, preferred the approach adopted in earlier decisions that "compares what would be recoverable as unliquidated damages with the sum of money stipulated as payable on breach".[51]

The majority also confirmed that the proper approach was to consider whether the amount stipulated as payable on breach was "out of all proportion"[52] or "extravagant and unconscionable"[53] having regard to the interests protected. In this aspect, the approach set down in *Paciocco* is consistent with statements by the High Court that courts do not require perfect arithmetical accuracy in the parties' pre-estimate of damage in assessing whether a purported agreed damages clause is invalid as a penalty,[54] and look for a sum that is "out of all proportion".[55]

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44 *Ringrow Pty Ltd v BP Australia Pty Ltd* [2005] HCA 71; (2005) 224 CLR 656, [31]–[32].

45 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [54] (Kiefel J), [156] (Gageler J), [220] (Keane J).

46 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [220]. See also *Arab Bank Australia Ltd v Sayde Developments Pty Ltd* (2016) 93 NSWLR 231, [104].

47 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525.

48 *Ringrow Pty Ltd v BP Australia Pty Ltd* [2005] HCA 71; (2005) 224 CLR 656, [21].

49 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525.

50 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [26] (Kiefel J, with whom French J agreed), [161] (Gageler J), [256] (Keane J).

51 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [320].

52 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [57], [29].

53 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [270].

54 *Interstar Wholesale Finance Pty Ltd v Integral Home Loans Pty Ltd* [2008] NSWCA 310, [151]; *Zachariadis v Allforks Australia Pty Ltd* [2009] VSCA 258; (2009) 26 VR 47, [142]. Cf Peden and Carter, "Agreed Damages Clauses — Back to the Future?" (2006) 22 *Journal of Contract Law* 189, 196.

55 *Ringrow Pty Ltd v BP Australia Pty Ltd* [2005] HCA 71; (2005) 224 CLR 656, [32].

The approach in *Dunlop*

[28.40] The leading authority on distinguishing an agreed damages clause setting out a sum payable on breach from a penalty has traditionally been *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd*.[56] The approach set out in this case was affirmed by the High Court in *Ringrow Pty Ltd v BP Australia Pty Ltd*.[57] In *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* Lord Dunedin stated:

(1) Though the parties to a contract who use the words 'penalty' or 'liquidated damages' may prima facie be supposed to mean what they say, yet the expression used is not conclusive. The court must find out whether the payment stipulated is in truth a penalty or liquidated damages …

(2) The essence of a penalty is a payment of money stipulated as in terrorem of the offending party; the essence of liquidated damages is a genuine covenanted pre-estimate of damage …

(3) The question whether a sum stipulated is penalty or liquidated damages is a question of construction to be decided upon the terms and inherent circumstances of each particular contract, judged of as at the time of the making of the contract, not as at the time of the breach …

(4) To assist this task of construction various tests have been suggested, which if applicable to the case under consideration may prove helpful, or even conclusive. Such are:

   (a) It will be held to be penalty if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach …

   (b) It will be held to be a penalty if the breach consists only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid …

   (c) There is a presumption (but no more) that it is penalty when 'a single lump sum is made payable by way of compensation, on the occurrence of one or more or all of several events, some of which may occasion serious and others but trifling damage' …

   On the other hand:

   (d) It is no obstacle to the sum stipulated being a genuine pre-estimate of damage, that the consequences of the breach are such as to make precise pre-estimation almost an impossibility. On the contrary, that is just the situation when it is probable that pre-estimated damage was the true bargain between the parties.[58]

To the extent that Lord Dunedin's statement suggests on comparing the amount of compensatory damages that might be awarded for the breach with the agreed sum in the contract, the approach is too narrow. In *Paciocco* the High Court held that agreed damages clauses may legitimately protect a broader interest, namely the parties' interest in performance of the contract.[59] In *Paciocco*, the High Court affirmed the significance of Lord Dunedin's

56 *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* [1915] AC 79, 86–7.

57 *Ringrow Pty Ltd v BP Australia Pty Ltd* [2005] HCA 71; (2005) 224 CLR 656.

58 *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* [1915] AC 79, 86–7.

59 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525.

statement in *Dunlop*.[60] However, Kiefel J stated that the approach in *Dunlop* "whilst useful, should not be understood as a limiting rule".[61] In particular, Lord Dunedin's approach in *Dunlop* did not mean that if no pre-estimate of loss was made at the time the contract was entered into, the stipulated sum was a penalty. Nor did it mean that "a sum reflecting, or attempting to reflect, other kinds of loss or damage to a party's interests beyond those directly caused by the breach will be a penalty".[62]

Illustrations

[28.45] The courts' approach in determining whether an agreed damages clause is invalid as a penalty is illustrated by the decision of the High Court in *Ringrow Pty Ltd v BP Australia Pty Ltd*.[63] This case concerned the sale of a service station site by a fuel distributor to its operator. The parties entered into an agreement under which the site was to be operated under the distributor's brand. If the operator breached the agreement, the distributor was entitled to terminate it and claim liquidated damages. Liquidated damages were to be calculated by reference to the expected profits of the distributor over the balance of the term of the agreement. By a deed executed at the same time as the agreement, the operator granted the distributor an option to re-purchase the site on termination of the agreement. The price was to be the market value of the site calculated without reference to goodwill. The agreement provided that if the option was exercised, liquidated damages for the breach were not payable. In breach of the agreement, the operator bought fuel from a third party. The distributor terminated the agreement and gave notice of its intention to exercise the option. The operator claimed that the relevant provision of the option deed was void and unenforceable because it operated as a penalty for breach of the agreement. Both the Federal Court and the Full Federal Court held that the provision was not invalid as a penalty. In the High Court, Gleeson CJ, Gummow, Kirby, Hayne, Callinan and Heydon JJ dismissed the appeal.[64]

The High Court held that a suspicion the business might be worth more than the price paid for it was not sufficient to establish the provision in question as a penalty. "The comparison calls for something 'extravagant and unconscionable' in the value of what is transferred compared to the price to be received."[65] The operator had failed to establish that the goodwill was of any significant value. Thus, it could not be said that "the cumulative imposition of the option on the liquidated damages clause … is oppressive, or was extravagant and unconscionable in comparison with the loss which flowed from the breach of the [contract]".[66]

60 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [29].

61 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [30]. See also Gageler J noting that Lord Dunedin's statements in *Dunlop* should not be treated as having quasi statutory status at [152].

62 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [30]. See also *Arab Bank Australia Ltd v Sayde Developments Pty Ltd* (2016) 93 NSWLR 231.

63 *Ringrow Pty Ltd v BP Australia Pty Ltd* [2005] HCA 71; (2005) 224 CLR 656, [32].

64 *Ringrow Pty Ltd v BP Australia Pty Ltd* [2005] HCA 71; (2005) 224 CLR 656.

65 *Ringrow Pty Ltd v BP Australia Pty Ltd* [2005] HCA 71; (2005) 224 CLR 656, [21].

66 *Ringrow Pty Ltd v BP Australia Pty Ltd* [2005] HCA 71; (2005) 224 CLR 656, [25]. For an example of a case where the purpose of the sum payable on breach was to punish was was therefore penal see *Melbourne Linh Son Buddhist Society Inc v Gippsreal Ltd* [2017] VSCA 161.

Paciocco v Australia and New Zealand Banking Group Ltd[67] arose out a class action challenging bank fees on certain accounts. In question were provisions in credit card account contracts that allowed the bank to charge honour, dishonor, over limit and late payment fees. Paciocco claimed that the terms constituted penalties in law and at equity. The primary judge found that the late payment fees constituted penalties. The Full Federal Court held that the trial judge was correct in characterising the late payment fee as payable upon breach of contract. It was therefore capable of being penal. The late payment fee was not a fee for additional credit service but a fee for late payment.[68]

The Full Federal Court held that the late payment fee was not a penalty because it was not exorbitant and extravagant in comparison with the greatest loss that could conceivably follow from the breach, as opposed to a genuine pre-estimate of loss. Here, the Full Federal Court found that the primary judge erred in having had undertaken an ex post enquiry into actual damage sustained by reasons of the customers breach in assessing whether the late payment fee was penal, as opposed to a forward looking or ex ante inquiry.[69] In assessing whether the quantum of the fee was extravagant or unconscionable so as to amount to a penalty, the Full Federal Court considered that the bank was entitled to take into account its economic interests to be protected, including provisioning costs, regulatory capital costs and an element for infrastructure, and not merely the immediate costs of enforcement.[70] In these circumstances, the court concluded that "given the nature of the relationship, the legitimate interest of ANZ and the correct analytical perspective, the fees were not demonstrated to be extravagant, exorbitant or unconscionable".[71]

The decision of the Full Federal Court was affirmed in the High Court (Nettle J dissenting). Kiefel J concluded it had not been shown that the late payment fee was out of all proportion to ANZ's interest in receiving timeous payment.[72] Gageler J held that the late payment fee was not "grossly disproportionate" to the commercial interests of ANZ.[73] Keane J held that the late payment fee was "readily characterised' by the legitimate purpose of ensuring "ANZ's revenues are maintained at the level of profitability required by its shareholders".[74] Gageler J and Keane J held that the late payment fee did not contravene any statutory prohibitions on unconscionable conduct, unjust transactions or unfair terms. French J agreed with Keane J on the statutory claims.

As noted above at [28.25], the approach of the High Court to determining whether a stipulation is a penalty is similar to that adopted by the Supreme Court in England in *Makdessi v Cavendish Square Holdings BV* (*ParkingEye*).[75] *ParkingEye* concerned an £85 charge for exceeding the maximum stay in a car park at a shopping centre. [76] The payments

67 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525.
68 *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, [87].
69 *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, [117].
70 *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, [167]–[169], [177].
71 *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, [187].
72 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [69].
73 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [173].
74 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [216].
75 *Makdessi v Cavendish Square Holdings BV* [2015] UKSC 67; [2016] AC 1172.
76 *Makdessi v Cavendish Square Holdings BV* [2015] UKSC 67; [2016] AC 1172, [99].

in *ParkingEye* were reviewable but did not amount to penalties. The charges protected a legitimate interest of the car park owner in managing the space for the benefit of people using the shopping centre.[75]

Equipment lease cases

[28.50] Many of the earlier cases in the High Court concern equipment leases. These cases demand quite a close correlation between the sum stipulated under the contract and the probable damages payable in compensation for breach in order for the contractual term to be valid. For example, in *AMEV-UDC Finance Ltd v Austin*,[77] the High Court held that a purported agreed damages clause was a penalty.[78] The case concerned a lease of equipment. The lessee defaulted in paying a rental instalment. The lessor exercised its contractual power to terminate the arrangement and repossess and sell the equipment. The lessor also claimed, pursuant to a clause in the contract, the instalments due under the unexpired term of the arrangement. The clause relied on by the lessor was penal because it required the lessee to pay the balance of the instalments without any rebate for the accelerated payment of future instalments and without the lessor having to account to the lessee for the proceeds from the sale of the equipment.[79] It might be queried whether the clause would be held invalid as a penalty under the current approach, which recognizes the value of protecting the innocent party's interest in performance and only strikes down a clause that is out of all proportion to the interest protected.[80]

Esanda Finance Corp Ltd v Plessnig[81] concerned similar facts to *AMEV-UDC Finance Ltd v Austin*. However, in this case, the High Court held that the sum claimed by the lessor was not a penalty.[82] The clause reduced the amount of outstanding rent claimed to take into account the benefits accruing to the lessor by reason of the lease being terminated. The possibility that the amount recoverable under the clause might in some circumstances exceed the lessor's actual loss did not prevent the clause from being valid.[83]

Penalties and termination under a term of the contract

[28.55] The decision of the High Court in *Esanda Finance Corp Ltd v Plessnig*[84] suggests that a plaintiff may, under an agreed damages clause, recover an amount equivalent to the total price payable under the contract, otherwise known as *loss of bargain damages*. Such a clause, suitably discounted to account for the present valid of the payment and any gains on termination to the lessor, will not amount to a penalty. By contrast, in *Shevill v Builders Licensing Board*,[85] the High Court held that loss of bargain damages are not available as

77 *AMEV-UDC Finance Ltd v Austin* (1986) 162 CLR 170. See also *O'Dea v Allstates Leasing System (WA) Pty Ltd* (1983) 152 CLR 359; *Zachariadis v Allforks Australia Pty Ltd* [2009] VSCA 258; (2009) 26 VR 47.

78 Compare the valid provision in *Esanda Finance Corp Ltd v Plessnig* (1989) 166 CLR 131.

79 *AMEV-UDC Finance Ltd v Austin* (1986) 162 CLR 170, 171, 180–1.

80 Carter, Courtney and Tolhurst, 'Assessment of Contractual Penalties: Dunlop Deflated' (2017) 34 *Journal of Contract Law* 4, 17.

81 *Esanda Finance Corp Ltd v Plessnig* (1989) 166 CLR 131.

82 *Esanda Finance Corp Ltd v Plessnig* (1989) 166 CLR 131, 141, 148–9, 154.

83 *Esanda Finance Corp Ltd v Plessnig* (1989) 166 CLR 131, 142, 152, 155.

84 *Esanda Finance Corp Ltd v Plessnig* (1989) 166 CLR 131.

85 *Shevill v Builders Licensing Board* (1982) 149 CLR 620.

general law damages where a contract is terminated pursuant to a term in the contract, rather than by relying on a right to terminate conferred by the common law.[86] In the *Esanda* case, Brennan J recognised an incongruity in the law taking these two positions and suggested that it may be appropriate for the court to reconsider the incongruity in some later case.[87] As yet this has not occurred.

When is an obligation to pay a sum of money not conditioned on a breach of contract a penalty?

[28.60] In *Andrews v Australia and New Zealand Banking Group Pty Ltd*[88] the High Court held that the critical issue in deciding whether a contractual term requiring the payment of an agreed sum that is not conditioned on a breach of contract is a penalty is "whether the sum agreed was commensurate with the interest protected by the bargain".[89] An amount that is "excessive or unconscionable" having regard to interests of the party relying on the clause will be a penalty.[90] Most of cases involve an assessment in the context of breach of contract, but in a general sense, the considerations discussed in that context will be similar. The principles as to what constitutes a penalty do not relevantly differ according to whether the doctrine has been triggered by a breach of contract or an accessorial stipulation securing satisfaction of a primary stipulation.[91]

Evidence admissible in characterising a term as a penalty

[28.65] In *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd*, Lord Dunedin stated that:

> The question whether a sum stipulated is penalty or liquidated damages is a question of construction to be decided upon the terms and inherent circumstances of each particular contract, judged of as at the time of the making of the contract, not as at the time of the breach … [92]

In *Paciocco v Australia and New Zealand Banking Group Ltd*, Kiefel J noted Lord Dunedin's reference to construction and reaffirmed the role of the surrounding circumstances in making the assessment.[93] Some courts have described the process as one of characterisation rather than construction.[94] Under this approach, the extrinsic evidence of the circumstances in which the contract was made will not be precluded by the parol evidence rule because this evidence will be used in determining whether the clause was out of proportion to the interests protected or imposed in terrorem rather than in construing its meaning.[95]

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86 See [27.130].

87 *Esanda Finance Corp Ltd v Plessnig* (1989) 166 CLR 131, 147.

88 *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205.

89 *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205, [75].

90 See above [28.35].

91 *Arab Bank Australia Ltd v Sayde Developments Pty Ltd* [2016] NSWCA 328, [73]–[74], [315].

92 *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* [1915] AC 79, 86–7.

93 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [31].

94 *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, [187].

95 *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, [209]; *Spiers Earthworks Pty Ltd v Landtec Projects Corporation Pty Ltd (No 2)* [2012] WASCA 53, [26].

Whether the sum is exorbitant and extravagant involves a forward looking, or ex ante assessment. It is not to be assessed ex post, or after the event, in the manner of damages.[96] In *Spiers Earthworks Pty Ltd v Landtec Projects Corporation Pty Ltd (No 2)*,[97] the developer of a parcel of land entered into contract with a contractor for various earth and road works to be carried out on the land. The contract required the contractor to complete the work by a specified date. The contractor did not complete the work until almost a month and a half after this date. The contract provided that liquidated damages at the rate of $13,846 per week would be payable by the contractor to the developer if the work was not completed by the specified date. The contractor claimed that the liquidated damages clause was unenforceable because it was a penalty.

The approval for the development of the land granted by the relevant local government body, the shire, was conditional on the development of a part of the land, known as "Curtis Lane", occurring in the first stage of the project. The developer was required to have completed this development in order to receive any revenue from the first stage of the development on which the contractor was working. At the time of entry into the first contract, the developer had taken no steps to ensure that the condition would be satisfied. The Court held that, against that background, the liquidated damages clause could not be characterised as a genuine pre-estimate of the losses suffered by the developer through delay by the contractor. The Court of Appeal explained that:

> Delay in performance of the first contract was incapable of causing any relevant financial loss to the developer until condition 25 was satisfied or its performance deferred (or waived) by the shire.[98]

Thus, the sum stipulated in the contract with the contractor was extravagant in amount, in comparison with the greatest loss that could potentially be suffered by delay under that contract.

WHAT ARE THE CONSEQUENCES OF A TERM BEING A PENALTY?

[28.70] The consequence in law of a term providing for a sum payable in event of breach being a penalty is that it is void. The party relying on the term must instead seek common law damages as compensation for any losses arising from the breach. The consequence of a stipulation providing for the payment of money on the failure of a condition in equity is that the term is voidable to the extent of the invalidity. This is confirmed by the High Court's approach in *Andrews v Australia and New Zealand Banking Group Pty Ltd*. The High Court stated that a penalty provision is not wholly unenforceable.

> If compensation can be made to the second party for the prejudice suffered by failure of the primary stipulation, the collateral stipulation and the penalty are enforced only to the extent of that compensation. The first party is relieved to that degree from liability to satisfy the collateral stipulation.[99]

96 *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, [147].

97 *Spiers Earthworks Pty Ltd v Landtec Projects Corporation Pty Ltd (No 2)* [2012] WASCA 53.

98 *Spiers Earthworks Pty Ltd v Landtec Projects Corporation Pty Ltd (No 2)* [2012] WASCA 53, [40].

99 *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205, [10].

This analysis means, as the Full Federal Court explained in *Paciocco v Australia and New Zealand Banking Group Ltd*, that if the sum stipulated as payable by a term is a penalty, then the stipulation is unenforceable to the extent that it exceeds "the greatest loss that could conceivably be proved to have been sustained by the breach, or the failure of the primary stipulation upon which the stipulation was conditioned".[100] In such a case, the party relying on the stipulation may only "enforce the stipulation to the extent of that party's provided loss".[101]

It is unclear whether the pro tanto relief available in equity can also apply to cases where a term providing for the payment of money in the event of a breach of contract has been characterised as a penalty,[102] or if different outcomes apply to the different categories of case.[103] This uncertainty and apparent disjunction between the approaches in law and equity is far from desirable. A more coherent integrated response would serve contracting parties far better.[104]

REASONS FOR THE RULE AGAINST PENALTIES

[28.75] The High Court in *Ringrow Pty Ltd v BP Australia Pty Ltd*[105] and *Paciocco v Australia and New Zealand Banking Group Ltd*[106] recognised that the penalty doctrine curtailed freedom of contract and considered that it should accordingly be kept within bounds. Nonetheless, the rule still represents somewhat of an anomaly on the law of contract. There are a number of doctrines which, in various ways, also restrict the bargain parties can make; vitiating factors, discussed in Pt X are good examples. The rule against penalties is unusual in that it involves courts looking not merely at the process through which the parties have made their contract but also the substance of that contract.

One possible rationale for the intervention in parties' contracts imposed by the rule against penalties might be based on substantive fairness. This rationale would suggest that the rule against penalties protects a defendant from having to make a payment, which would be unfair because it represents a greater amount than the defendant would have to pay under an award of damages. Lanyon has argued that this rationale is not convincing because there are no general principles for evaluating the fairness of the bargain between contracting parties.[107]

100 *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, [20], appeal successful on a different point in *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205. Also *Cedar Meats (Aust) Pty Ltd v Five Star Lamb Pty Ltd* [2014] VSCA 32, [55]–[56].

101 *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, [20], appeal successful on a different point in *Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205.

102 See Tiverios, "A Restatement of Relief Against Contractual Penalties (I): Underlying Principles in Equity and at Common Law" (2017) 11 *Journal of Equity* 1 and "A Restatement of Relief Against Contractual Penalties (II): A Framework for Applying the Australian and English Approaches" (2017) 11 *Journal of Equity* 185: suggesting a unified approach.

103 Carter, Courtney and Tolhurst, "Assessment of Contractual Penalties: Dunlop Deflated" (2017) 34 *Journal of Contract Law* 4, 7.

104 See also Eldridge, "The New Law of Penalties: Mapping the Terrain" [2018] *Journal of Business Law* 637, 648.

105 *Ringrow Pty Ltd v BP Australia Pty Ltd* [2005] HCA 71; (2005) 224 CLR 656, [31]–[32].

106 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [220].

107 Lanyon, "Equity and the Doctrine of Penalties" (1996) 9 *Journal of Contract Law* 234, 237–8.

In particular, courts will not examine the adequacy of the consideration provided by the parties.[108]

A related possible rationale for the rule against penalties might be that it would be unfair for a plaintiff to threaten to use an agreed damages clause to compel performance, when common law damages would be of a lesser amount. Alternatively, it might be said that, as a matter of policy, courts should refuse to enforce an agreed damages clause where common law damages would be of a lesser amount. Lanyon points out that these types of rationale may be criticised as overly paternalistic.[109] Why shouldn't the parties be able to agree to pay damages in excess of common law damages? Goetz and Scott argue that agreed damages clauses might reduce transaction costs where the parties consider that the cost of negotiating the clause is less than the expected cost of litigation on breach.[110] An agreed damages clause may also be intended to allow a plaintiff to recover losses which would not be compensated in damages, but result from the idiosyncratic value the parties place on performance of the contract.[111]

A different rationale might be that the rule against penalties is concerned with procedural unfairness, as are most of the vitiating factors discussed in Pt X.[112] This rationale is based on the view that contracting parties will not generally agree to pay damages which exceed the losses compensated by common law damages. A clause providing for agreed damages significantly in excess of what would be recovered as common law damages may indicate that there has been some form of unfairness in the process through which the contract was made. Such procedural unfairness might occur where there was a difference in the bargaining power of the parties, perhaps where one party was a large corporation and the other party a small business or consumer. In these sorts of cases, Rea explains that "one party may not have realised the implications of the damages clause".[113] The rationale of promoting procedural fairness through the rule against penalties would be consistent with a general objective of promoting fairness in contracting. It would also be consistent with a concern with economic efficiency; the emphasis in economic analysis on giving effect to the parties' own preferences is premised on the bargaining process being voluntary and informed.[114]

Lanyon argues that, under the procedural fairness rationale, the existence of a penalty clause should create a presumption of unfairness in forming the contract. However, she suggests that the presumption should be capable of being rebutted by evidence of a fair process.[115] Certainly, in *AMEV-UDC Finance Ltd v Austin*, Mason and Wilson JJ considered that the nature of the relationship between the contracting parties was a "factor relevant to the unconscionability of

108 See [4.45].

109 Lanyon, "Equity and the Doctrine of Penalties" (1996) 9 *Journal of Contract Law* 234, 239.

110 Goetz and Scott, "Liquidated Damages, Penalties and the Just Compensation Principle: Some Notes on an Enforcement Model and a Theory of Efficient Breach" (1977) 77 *Columbia Law Review* 554.

111 Goetz and Scott, "Liquidated Damages, Penalties and the Just Compensation Principle" (1977) 77 *Columbia Law Review* 554; Ham, "The Rule Against Penalties in Contract: An Economic Perspective" (1990) 17 *Melbourne University Law Review* 649, 660.

112 Rea, "Efficiency Implications of Penalties and Liquidated Damages" (1984) 13 *Journal of Legal Studies* 147, 160; Lanyon, "Equity and the Doctrine of Penalties" (1996) 9 *Journal of Contract Law* 234, 239.

113 Rea, "Efficiency Implications of Penalties and Liquidated Damages" (1984) 13 *Journal of Legal Studies* 147; Lanyon, "Equity and the Doctrine of Penalties" (1996) 9 *Journal of Contract Law* 234, 239.

114 Lanyon, "Equity and the Doctrine of Penalties" (1996) 9 *Journal of Contract Law* 234, 241.

115 Lanyon, "Equity and the Doctrine of Penalties" (1996) 9 *Journal of Contract Law* 234, 242.

the plaintiff's conduct in seeking to enforce the term".[116] However, little was made of this kind of consideration in *Paciocco v Australia and New Zealand Banking Group Ltd*.[117]

Insights from the statutory regime setting aside unfair contract terms suggest that the reasons for the rule against penalties may lie in concerns that substantively unfair terms may undermine the institution of contract and should be subject to scrutiny for this reason. Terms imposing a sum payable on breach for the non-satisfaction of a condition that is exorbitant or unconscionable impose a punitive threat to perform that is arguably inconsistent with the consensual nature of contract. Chen-Wishart argues that, like statutory regimes against unfair terms, contract law places at least some limits on parties' ability to contract out of its constituent rules.[118] The rule against penalties prevents the parties from usurping contract law's jurisdiction over fair and proportionate redress for breach.[119] As Kiefel J stated in *Paciocco*, the policy of the rule against penalties is that "a sum may not be stipulated for payment on default if it is stipulated as a threat over the person obliged to perform; it may not be stipulated where the purpose and effect of requiring payment is to punish the defaulting party".[120]

116 *AMEV-UDC Finance Ltd v Austin* (1986) 162 CLR 170, 193.

117 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525.

118 See Chen-Wishart, "Regulating Unfair Terms" in Gullifer and Vogenaur (eds), *English and European Perspectives on Contract and Commercial Law* (2015), p 119.

119 See Chen-Wishart, "Regulating Unfair Terms" in Gullifer and Vogenaur (eds), *English and European Perspectives on Contract and Commercial Law* (2015), p 124.

120 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [32].

CHAPTER **29**

Actions for debt

ADVANTAGES OF AN ACTION FOR DEBT

[29.05] In some cases, it may be possible for a contracting party to claim money owing under the contract through an action for a debt (sometimes also called an *action for a liquidated sum*) following termination of the contract other than through a claim for damages. For example, a party who has performed his or her obligations under a contract might be able to claim as a debt the contract price, that is, the amount specified as payable for that performance under the contract.

The action to recover a debt is distinct from an action for damages. As the High Court explained in *Young v Queensland Trustees Ltd*, "the common law does not and never did conceive of indebtedness in a sum certain for an executed consideration as a mere breach of contract: it is rather the detention of a sum of money".[1]

There are a number of significant differences between debt and damages which may make the action in debt a useful remedy.[2] A party may be entitled to recover a debt even where that party has breached the contract and where the contract has been terminated in response to the breach. Whereas a party claiming damages must prove that there has been a breach of contract and a loss has been suffered, in an action for debt it is for the party against whom the debt is being claimed to prove any defence of payment. The principle of mitigation of loss applicable to a claim for damages does not apply to the recovery of a debt. In the case of a party not in breach of contract, the action in debt may be brought as an alternative to, or in conjunction with, an action for damages. Regardless of how the action is framed, the same sum cannot be recovered twice.

1 *Young v Queensland Trustees Ltd* (1956) 99 CLR 560, 567 per Dixon CJ, McTiernan and Taylor JJ.
2 See further Carter, *Contract Law in Australia* (7th ed, 2018), [37-01]–[37-04].

REQUIREMENTS OF AN ACTION FOR A DEBT

When does the right to a debt accrue?

[29.10] There are two main requirements for a party to bring an action to recover a debt:

1. the contract must impose an obligation to pay a certain or ascertainable sum of money; and
2. the right to payment of the sum must have "accrued".[3]

A debt will accrue where the consideration for the payment in question — whether that is the whole or part of the contract price — has been provided. Generally, for the right to a payment under the contract to have accrued, the party claiming the debt must have earned the payment by performing the obligations to which the payment relates.[4] What amounts to sufficient performance to entitle a party to claim payment under the contract as a debt depends on a distinction between entire and divisible obligations and on the doctrine of substantial performance.[5]

Entire obligations

[29.15] An *entire* obligation is one that must be wholly performed for a party to be entitled to payment for that performance.[6] In other words, under an entire contract, entire or complete performance is a condition precedent to payment.[7] Whether an obligation is entire is a question of construction. Examples of contracts which have been found to be entire include building contracts for a lump sum[8] and employment contracts for a specific period of time.[9] A party who has only partly performed an entire contract will not be entitled to payment of the contract price or any part of the price. Courts will not apportion the contract price in respect of the work that has been done.

Divisible obligations

[29.20] A *divisible* or *severable obligation* is one in which the parties have intended the contract price and contract performance to be divided into corresponding parts.[10] Such an arrangement may be found in contracts for the sale of goods to be delivered and paid for in instalments,[11] in building contracts which provide for progress payments to be made to the builder as the work proceeds[12] and in technology contracts with specified "milestones".[13]

3 See also *Westralian Farmers Ltd v Commonwealth Agricultural Service Engineers Ltd (in liq)* (1936) 54 CLR 361.
4 *McDonald v Dennys Lascelles Ltd* (1933) 48 CLR 457, 475; *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32. See also *Sale of Goods Act 1954* (ACT), s 52(1); *Sale of Goods Act 1923* (NSW), s 51(1); *Sale of Goods Act* (NT), s 51(1); *Sale of Goods Act 1896* (Qld), s 50(1); *Sale of Goods Act 1895* (SA), s 48(1); *Sale of Goods Act 1896* (Tas), s 53(1); *Goods Act 1958* (Vic), s 55(1); *Sale of Goods Act 1895* (WA), s 48(1).
5 *Steele v Tardiani* (1946) 72 CLR 386, 401; *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 350, 374, 384.
6 See *Cutter v Powell* (1795) 6 Term Rep 320; 101 ER 573; *Steele v Tardiani* (1946) 72 CLR 386, 401; *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 350.
7 *Phillips v Ellinson Brothers Pty Ltd* (1941) 65 CLR 221, 233.
8 *Sumpter v Hedges* [1898] 1 QB 673.
9 See, eg, *Phillips v Ellinson Brothers Pty Ltd* (1941) 65 CLR 221; *Cutter v Powell* (1795) 6 TR 320; 101 ER 573.
10 See, eg, *Steele v Tardiani* (1946) 72 CLR 386.
11 See, eg, *Mersey Steele and Iron Co Ltd v Naylor Benzon & Co* (1884) 9 App Cas 434.
12 See, eg, *Hyundai Heavy Industries Co Ltd v Papadopoulos* [1980] 1 WLR 1129.
13 *GEC Marconi Systems Pty Ltd v BHP Information Technology Pty Ltd* [2003] FCA 50; (2003) 128 FCR 1.

Where a contract is divisible, a party will be entitled to payment of each instalment of the contract price for which the required performance has been given. However, each divisible part of the contract may be "entire", or at least require substantial performance[14] in the sense that, under the contract,[15] a party will only be entitled to payment for those parts of the work that are completed.[16]

In *Steele v Tardiani*[17] the plaintiffs were employed to cut timber for the defendant. No particular amount of timber was specified; the plaintiffs were to be paid for each ton of wood cut. The contract required the timber to be cut into lengths each six feet long and six inches in diameter. The plaintiffs had cut 1500 tons of wood at lengths varying from six to 15 inches in diameter. The defendant refused to pay for the work, and the plaintiffs sued to recover some payment. The High Court found that the contract did not employ the plaintiffs to do a single piece of work for a lump sum under an entire contract. The contract was instead "infinitely divisible".[18] The plaintiffs were entitled to recover the contract price in respect of those tons of firewood which qualified by substantial compliance with the contract specifications.[19]

Assessing whether a contract is entire or divisible

[29.25] Whether a contract is entire or divisible is a matter of construction depending on the presumed intentions of the parties and the circumstances of each particular case.[20] A contract will be entire if it appears that the parties intended only exact and complete performance would be accepted.[21] A contract is more likely to be construed as entire where it provides for a single sum of money payable on completion of performance, but this factor is not conclusive.[22] A contract will generally be construed as divisible where payment and services are divided into instalments, although once again this factor is not conclusive.[23]

In some cases, legislation provides for a right to payment on a more generous basis than allowed under the contract. For example, legislation provides that: "[a]ll rents, annuities, dividends, and other periodical payments in the nature of income … shall, like interest on money lent, be considered as accruing from day to day, and shall be apportionable in respect of time accordingly".[24] These apportionment provisions may be excluded by express stipulation. The provisions only apply to payments which are periodical, that is, they do not apply to lump sum payments.[25]

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14 See discussion of substantial performance at [29.30].

15 But see the effect of statute at [29.25].

16 See *Steele v Tardiani* (1946) 72 CLR 386.

17 *Steele v Tardiani* (1946) 72 CLR 386.

18 *Steele v Tardiani* (1946) 72 CLR 386, 401.

19 *Steele v Tardiani* (1946) 72 CLR 386, 401. The plaintiffs recovered payment of a reasonable sum for the remainder of the work done under the principles of restitution. See further at [10.75].

20 *Purcell v Bacon* (1914) 19 CLR 241, 249, 265 (reversed on other grounds: *Bacon v Purcell* (1916) 22 CLR 307); *Hoenig v Isaacs* [1952] 2 All ER 176, 178.

21 See also Greig and Davis, *The Law of Contract* (1987), pp 1224–5.

22 *Hoenig v Isaacs* [1952] 2 All ER 176, 178, 181.

23 See, eg, *Smith v Jones* (1924) 24 SR (NSW) 444.

24 *Civil Law (Property) Act 2006* (ACT), s 250; *Conveyancing Act 1919* (NSW), s 144(1); *Law of Property Act* (NT), s 212(1); *Property Law Act 1974* (Qld), s 232(1); *Law of Property Act 1936* (SA), s 64; *Apportionment Act 1871* (Tas), s 2; *Supreme Court Act 1986* (Vic), s 54; *Property Law Act 1969* (WA), s 131. On the application of the legislation, see, eg, *Nemeth v Bayswater Road Pty Ltd* [1988] 2 Qd R 406, 418–9.

25 *Re South Kensington Co-operative Stores* (1881) 17 Ch D 161, 165.

Substantial performance

[29.30] The doctrine of substantial performance allows a party to recover the contract price, even though the contract has not been fully performed, in circumstances where the performance which has been rendered is nonetheless substantial. As the party claiming payment will be in breach of contract for rendering incomplete performance, the other party, though liable to pay the contract price, will have a right to compensation for the cost of remedying the defects in the performance. The doctrine of substantial performance may apply to divisible contracts so that substantial performance of each part of the contract may entitle a performing party to the price allocated for that part.[26]

In assessing whether or not a contract has been substantially performed, courts will consider the performance rendered and the nature of the defects in that performance. Has the work contracted for been done, albeit with defects of a minor or trivial nature, or is the contract substantially unperformed?

Two English cases are useful in illustrating the courts' approach. In *Hoenig v Isaacs*[27] the defendant employed the plaintiff, an interior decorator and furniture designer, to decorate and furnish the plaintiff's one-bedroom flat. Payment was a sum of £750, paid in instalments as the work proceeded, with the balance due on completion. When the plaintiff finished the work, the defendant refused to pay the balance owing of £350, complaining of faulty design and bad workmanship. The cost of remedying the defects was assessed at some £55. The English Court of Appeal held that the plaintiff had substantially performed the contract. The plaintiff was accordingly entitled to payment of the remainder of the contract price, with a deduction for the cost of remedying the defects.

By contrast, in *Bolton v Mahdeva*,[28] the plaintiff agreed to install a combined heating and hot water system in the defendant's home for a price of £560. The work was improperly done. The cost of remedying the defects was £174. The English Court of Appeal considered that the contract had not been substantially performed. The Court was influenced by the cost of the defects to the defendant and the proportion between the cost of the defects and the contract price.[29] It was also influenced by the nature of the defects. The flue was defective, which meant the heating system did not work adequately and affected the quality of the air in the living room. Accordingly, the plaintiff was not entitled to payment for the work that had been done.[30]

Substantial performance and entire obligations

[29.35] The relationship between the doctrines of entire obligations and substantial performance has not been settled. Some courts have assumed that the doctrine of substantial performance does apply to entire obligations.[31] On this view, the doctrine of

26 See, eg, *Steele v Tardiani* (1946) 72 CLR 386, 401. But compare, in relation to employment contracts, *Wiluszynski v Tower Hamlets London BC* [1989] ICR 493.

27 *Hoenig v Isaacs* [1952] 2 All ER 176.

28 *Bolton v Mahdeva* [1972] 1 WLR 1009.

29 *Bolton v Mahdeva* [1972] 1 WLR 1009, 1013.

30 See also *Williamson v Murdoch* (1912) 14 WALR 54; *Lemura v Coppola* [1960] Qd R 308.

31 See, eg, *Phillips v Ellinson Brothers Pty Ltd* (1941) 65 CLR 221, 246; *Steele v Tardiani* (1946) 72 CLR 386, 401.

substantial performance operates as an exception to the principle that entire obligations require complete performance for the price to be recovered.[32]

The more principled approach would seem to be that the doctrine of substantial performance should not apply where a contract is entire.[33] This is because an entire contract is one where the parties have intended that nothing less than complete performance of the contract will earn a contractual right to payment. Under this approach, there is a category of contract which, although not divisible, is not entire and for which substantial performance will be sufficient to entitle the party performing to recover the contract price.[34]

Reasons for requiring complete or substantial performance

[29.40] As we have seen, if a party has not substantially performed his or her obligations under a contract, that party will not be entitled to payment of the contract price for the work that he or she has done.[35] As a result, it may seem that the other party has received a windfall benefit. For example, in *Bolton v Mahdeva*,[36] the defendant received a hot water system worth some £560 with only £174 to pay for the cost of remedying the defects in the plaintiff's work. It might therefore be suggested that there should be some method of giving a party who has partly performed his or her obligations under a contract a pro-rata payment for the work done. On the other hand, the harshness of denying that party recovery of any of the contract price must be balanced against the need to maintain an incentive for parties to fully perform their contractual obligations. Such an incentive is provided by the rule that there is only a right to payment upon entire or substantial completion of performance.

Payment independent of performance

[29.45] The parties to a contract may make the payment of a particular sum of money independent of performance of the contract.[37] Where payment is independent of performance, the sum will be owing as a debt as soon as the time for payment arises. It will not be necessary to analyse whether or not the required performance for that sum has been given. Perhaps the main example of a payment made independent of performance is a contract for the sale of property that requires instalments towards the purchase price to be paid prior to the transfer of ownership of the property. The instalment will be owing as a debt from the time when payment is due.[38] Nonetheless, there is a qualification on the right of a vendor to retain or claim payment of the instalments that have become owing. Courts have considered that the right of the vendor to retain the payments is conditional on the vendor completing the contract.[39] If the contract is not completed, the purchaser will be able to make a claim in

32 See Greig and Davis, *The Law of Contract* (1987), p 1234.

33 Greig and Davis, *The Law of Contract* (1987), pp 1234–6.

34 See also Greig and Davis, *The Law of Contract* (1987), pp 1234–6, who refer to this category as "lump sum" contracts.

35 On a claim by the plaintiff in restitution, see Carter, "Discharged Contracts: Claims for Restitution" (1997) 11 *Journal of Contract Law* 130.

36 *Bolton v Mahdeva* [1972] 1 WLR 1009.

37 See also *Hyundai Heavy Industries Co Ltd v Papadopoulos* [1980] 1 WLR 1129.

38 See *McDonald v Dennys Lascelles Ltd* (1933) 48 CLR 457, 476.

39 See *McDonald v Dennys Lascelles Ltd* (1933) 48 CLR 457, 470, 476–9.

restitution for return of the payments on the ground of total failure of consideration.[40] The basis for the claim is that the purchaser contracted to receive the property. If the contract is terminated, the purchaser may not have received the bargained for consideration.[41] If, in such a case, the contract expressly provides that instalment payments will be forfeited should the transaction not be completed, relief against forfeiture of those payments may be available.[42]

DEPOSITS

[29.50] Perhaps the primary kind of payment that is considered independent of performance of the contract so as to constitute a debt owing is a deposit. A deposit is a percentage of the overall purchase price payable by a purchaser on entering into a contract of sale. A deposit is paid as a guarantee of the purchaser's genuine intention to perform the contract in return for the vendor entering into the transaction. In *Yardley v Saunders*[43] Kennedy J explained that a deposit "has variously been described as 'an earnest to bind the bargain' ",[44] "a guarantee that the purchaser means business"[45] and as "a security arranged to ensure the due performance of the contract".[46]

If the transaction does not proceed

[29.55] The parties will commonly specify in their contract what is to happen to the deposit in the event that the transaction does not proceed. The usual arrangements are as follows. If the transaction goes ahead, the deposit is treated as part of the purchase price. If the vendor, in breach of or having repudiated the contract, does not complete the transaction, the purchaser will be entitled to recover the deposit. If the transaction is not completed by reason of the default of the purchaser, the vendor will retain the deposit.[47] Courts have confirmed that a vendor's right to retain a deposit following breach by the purchaser is not conditional upon the subsequent completion of the transaction.[48] The consideration for which the deposit is paid is the vendor entering into the contract.[49]

If there is no express provision in the contract as to what is to happen to the deposit should the transaction not proceed, the matter is determined as a matter of construction of the contract based on the parties' presumed intentions.[50] Where a deposit is not excessive, but represents a reasonable sum, a deposit will typically be treated as subject to the principles specified above. This is because parties are unlikely to have intended for a vendor to retain a deposit in a case where the vendor refused to proceed with the contract.[51] This commonly

40 See [10.25].

41 For a variation on the usual scenario, see *Sharma v Simposh* [2011] EWCA Civ 1383; [2013] Ch 23.

42 See *McDonald v Dennys Lascelles Ltd* (1933) 48 CLR 457, 478; *Tropical Traders v Goonan* (1964) 111 CLR 41.

43 *Yardley v Saunders* [1982] WAR 231, 236. See also *Brien v Dwyer* (1978) 141 CLR 378, 385, 386, 406; *NLS Pty Ltd v Hughes* (1966) 120 CLR 583, 589; *Farrant v Leburn* [1970] WAR 179, 184.

44 *Howe v Smith* [1884] 27 Ch D 89, 101.

45 *Soper v Arnold* [1889] 14 AC 429, 435.

46 *Watson v Healy Lands Limited* [1965] NZLR 511, 516.

47 *McDonald v Dennys Lascelles Ltd* (1933) 48 CLR 457, 470, 478.

48 *Bot v Ristevski* [1981] VR 120, 123.

49 *Farrant v Leburn* [1970] WAR 179, 184.

50 *Howe v Smith* (1884) 27 Ch D 89, 97–8.

51 *CCP Australian Airships Ltd v Primus Telecommunications Pty Ltd* [2004] VSCA 232, [9].

understood treatment of a deposit will apply even where a deposit is expressed to be "non-refundable".[52] Thus, it seems likely that very clear words by the parties will be required before a deposit is treated as forfeited to a vendor regardless of whether that vendor is willing and able to complete the transaction.

Deposit paid to vendor in breach

[29.60] As just noted, the purchaser will be entitled to recover the deposit from the vendor if, having breached or repudiated the contract, the vendor does not perform its obligations under that contract. As noted, restitution of the deposit may be sought on the basis of total failure of consideration.[53]

Deposit not paid by purchaser in breach

[29.65] What if the deposit, although due, has not actually been paid when a vendor terminates the contract for reason of the purchaser's breach? There are some authorities which suggest that the vendor has no right to recover the unpaid deposit as a debt.[54] The better view is that if there is an unconditional right on the part of the vendor to recover and retain the deposit before the contract is discharged, that right survives the termination of the contract. Accordingly, if the purchaser has not paid the deposit before the contract is terminated, the vendor may recover the deposit from the purchaser.[55]

Deposits and penalties

[29.70] As discussed in Chapter 28, a penalty is a sum payable on breach which is "extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach".[56] A deposit is not usually treated as a penalty, even though it is forfeited on breach and may not be a genuine pre-estimate of damages.[57] Nonetheless, courts retain a discretion to grant relief against the forfeiture of a deposit that is excessive where the payment is properly described as a penalty.[58]

In *Coates v Sarich*, Hale J explained that:

> If the deposit is surprisingly large and if there is no express forfeiture clause the question may arise as a matter of interpretation whether the parties when using the word 'deposit' meant that the payment in question was in truth to have the normal incidents of a deposit of whether there was merely an error of nomenclature. Secondly, if that question is answered that there was no error of expression, or if there is an express forfeiture clause, a question may still arise whether what the parties have contracted for is in truth a penalty, and in the latter context the question whether the sum is a true deposit becomes the question whether it is a reasonable deposit or

52 *CCP Australian Airships Ltd v Primus Telecommunications Pty Ltd* [2004] VSCA 232.

53 See [10.20]. Also *Foran v Wight* (1989) 168 CLR 385, 438.

54 See, eg, *Lowe v Hope* [1970] Ch 94, 98.

55 See *Farrant v Leburn* [1970] WAR 179; *Bot v Ristevski* [1981] VR 120. See also *Ashdown v Kirk* [1999] 2 Qd R 1; *Russell v Adwon Pty Ltd* [2000] ACTSC 90; (2001) 144 ACTR 1.

56 *Dunlop Pneumatic Tyre Co Ltd v New Garage & Motor Co Ltd* [1915] AC 79; *O'Dea v Allstates Leasing System (WA) Pty Ltd* (1983) 152 CLR 359, 367–8, 399; *AMEV-UDC Finance Ltd v Austin* (1986) 162 CLR 170, 190.

57 *NLS Pty Ltd v Hughes* (1966) 120 CLR 583, 588–9; *Workers Trust and Merchant Bank Ltd v Dojap Investment Ltd* [1993] AC 573, 578.

58 *NLS Pty Ltd v Hughes* (1966) 120 CLR 583, 588; *Workers Trust and Merchant Bank Ltd v Dojap Investment Ltd* [1993] AC 573, 579–80; *Cloud Top Pty Limited v Toma Services Pty Limited* [2008] NSWSC 568.

whether it is so unreasonable a sum to be forfeited that it should be treated as a penalty against which relief should be granted.[59]

In *Workers Trust and Merchant Bank Ltd v Dojap Investment Ltd*[60] the Privy Council suggested that the customary amount for a deposit was 10 per cent of the purchase price and that an amount in excess of 10 per cent may be considered excessive unless special circumstances are shown.[61] Similar views have been expressed in Australia, at least in relation to the sale of land.[62]

A deposit of more than 10 per cent may not be a penalty if justified by the circumstances of the case. For example, in *Yardley v Saunders*,[63] a deposit of 20 per cent was paid in relation to the sale of a taxi licence. The court considered that the deposit represented a reasonable sum to protect the vendor, over the six-month period before the full purchase price was paid, against the risk of mismanagement and destruction of the business sold.[64] Conversely, a sum of no more than 10 per cent may be a penalty if, although termed as a deposit, it is only payable in event of breach by the purchaser.[65] The general law on deposits is also qualified in New South Wales and Victoria by legislation regulating the sale of land, which allow a court to order repayment of a deposit to a purchaser in certain circumstances.[66]

MITIGATION AND THE ACTION FOR DEBT

[29.75] The principles of mitigation do not apply to an action for a debt due under a contract.[67] If one party is faced with a repudiation, he or she has a choice whether to accept the repudiation or to affirm the contract, which would then continue in full effect. Thus, at least in principle, in a case where a party is to perform a specified service in return for payment of the contract price, that party may choose not to accept the repudiation by the other party and instead complete the performance of his or her obligations under the contract and sue in debt for the contract price.

White & Carter (Councils) Ltd v McGregor

[29.76] This principle was applied by the House of Lords in *White & Carter (Councils) Ltd v McGregor*.[68] In this case, the parties entered into a contract for the display of advertisements for the defendant's garage by the plaintiff on litter bins for a period of three years. On the same day that he entered into the contract, the defendant informed the plaintiff that he did not wish to go ahead with the contract after all. The plaintiff did not accept this repudiation. Instead,

59 *Coates v Sarich* [1964] WAR 2, 15.

60 *Workers Trust and Merchant Bank Ltd v Dojap Investment Ltd* [1993] AC 573.

61 *Workers Trust and Merchant Bank Ltd v Dojap Investment Ltd* [1993] AC 573, 580.

62 See, eg, *Freedom v AHR Constructions Pty Ltd* [1987] 1 Qd R 59; *Luong Dinh Luu v Sovereign Developments Pty Ltd* [2006] NSWCA 40; *Golden Oceans (NSW) Pty Ltd v Evewall Pty Ltd* [2009] NSWSC 674.

63 *Yardley v Saunders* [1982] WAR 231, 238.

64 *Yardley v Saunders* [1982] WAR 231, 238. See also *Re Hoobin* [1957] VR 341; *Coates v Saruta* (1964) WAR 2, 6, 15.

65 See *Luong Dinh Luu v Sovereign Developments Pty Ltd* [2006] NSWCA 40; (2006) 12 BPR 98,203; *Iannello v Sharpe* [2007] NSWCA 61; (2007) 69 NSWLR 452.

66 *Conveyancing Act 1919* (NSW), s 55; *Property Law Act* 1958 (Vic), s 49(2).

67 *White and Carter (Councils) Ltd v McGregor* [1962] 2 AC 413.

68 *White & Carter (Councils) Ltd v McGregor* [1962] 2 AC 413.

the plaintiff performed its obligations under the contract and sued for the full contract price. The House of Lords found in favour of the plaintiff.

Despite being consistent with principle, the result in *White & Carter (Councils) Ltd v McGregor* may not seem entirely satisfactory.[69] As the House of Lords itself noted, it was perhaps "unfortunate" that the defendant had been saddled "with an unwanted contract causing an apparent waste of time and money".[70] However, Lord Reid explained:

> It might be, but it never has been, the law that a person is only entitled to enforce his contractual obligations in a reasonable way, and that a court will not support an attempt to enforce them in an unreasonable way. One reason why that is not the law is, no doubt, because it was thought that it would create too much uncertainty to require the court to decide whether it is reasonable or equitable to allow a party to enforce his full rights under a contract.[71]

The approach may be contrasted with that taken in the United States, where a party faced with a repudiation is required to mitigate his or her losses regardless of whether or not that party elects to accept the repudiation by terminating the contract.[72] It remains to be seen which approach will be preferred by the High Court of Australia.

Limitations on the White & Carter principle

[29.78] The principle illustrated in *White & Carter (Councils) Ltd v McGregor*[73] — that a party may choose to affirm a contract following repudiation, complete his or her obligations and sue in debt for the contract price — is subject to two main limitations.[74]

The first limitation is that the party claiming payment must be able to completely fulfil his or her obligations under the contract without the cooperation of the other party.[75] This was the case in *White and Carter (Councils) Ltd v McGregor*[76] itself where the plaintiff could go ahead and place the advertisements on litter bins without any assistance from the defendant. In other cases, the ability of one party to complete performance without the assistance of the other party may be more limited. For example, a party is less likely to be able to complete performance and sue for the price where that party requires the use of the land or goods of the other party to perform his or her obligations under the contract.[77] A seller of goods will usually not be able to sue for the price of the goods unless the buyer accepts delivery of them.[78]

The second limitation on the principle illustrated in *White & Carter (Councils) Ltd v McGregor* is that a party that is continuing performance and suing for a debt following

69 See also Goodhart, "Measure of Damages when a Contract is Repudiated" (1962) 78 *Law Quarterly Review* 263.

70 *White and Carter (Councils) Ltd v McGregor* [1962] 2 AC 413, 445.

71 *White and Carter (Councils) Ltd v McGregor* [1962] 2 AC 413, 430.

72 *Clea Shipping Corp v Bulk Oil International Ltd (The "Alaskan Trader") (No 2)* [1984] 1 All ER 129, 137.

73 *White and Carter (Councils) Ltd v McGregor* [1962] 2 AC 413.

74 See generally Carter, Phang and Phang, "Performance Following Repudiation: Legal and Economic Interests" (1999) 15 *Journal of Contract Law* 97.

75 *White & Carter (Councils) Ltd v McGregor* [1962] 2 AC 413, 430, 432, 439.

76 *White and Carter (Councils) Ltd v McGregor* [1962] 2 AC 413.

77 See, eg, *Houndslow London Borough Council v Twickenham Garden Developments Ltd* [1971] Ch 233, 253–4.

78 *Automatic Fire Sprinklers Pty Ltd v Watson* (1946) 72 CLR 435, 464.

repudiation by the other party must have a *legitimate interest* in pursuing that course of action.[79] The limitation was articulated by Lord Reid as follows:

> It may well be that, if it can be shown that a person has no legitimate interest, financial or otherwise, in performing the contract rather than claiming damages, he ought not to be allowed to saddle the other party with an additional burden with no benefit to himself.[80]

This statement has been applied in a number of subsequent English cases. Yet it is not clear how a legitimate interest in performance is assessed. One factor identified in these cases as relevant to whether a party has a legitimate interest in continuing with performance relates to the calculation of damages for the repudiation or breach giving rise to the party's right to terminate the contract. A party may have a legitimate interest in continuing with the contract and suing for the price where damages would be difficult to assess and continuing with the contract would be unreasonable.[81] It has also been suggested that a party may have a legitimate interest in continuing with performance if it is not plain beyond all argument that the other party is repudiating the contract.[82]

PENALTIES AND THE ACCELERATION OF A DEBT

[29.80] The distinction between an agreed damages clause and a penalty, discussed in Chapter 28, will not apply to a contractual provision which provides for the full or immediate payment of a debt if certain specified conditions — relating to payment of interest or repayment on time of instalments of the debt or part of the debt — are not met. The position was explained in *O'Dea v Allstates Leasing System (WA) Pty Ltd* by Gibbs CJ:

> If a sum of money is payable by instalments, and it is provided that in the event of one instalment not being punctually paid the whole sum shall immediately become payable, the acceleration of payment is not a penalty … Similarly there is no penalty where it is agreed to charge a certain rate of interest on condition that if payment is made punctually the rate will be reduced … or where a creditor agrees to accept payment of part of his debt in full discharge if certain conditions are met but stipulates that if the conditions are not met he will be entitled to recover the original debt …[83]

Gibbs CJ explained that the issue of a penalty did not arise because:

> In all the cases of this kind there is a present debt, which, by reason of an indulgence given by the creditor, is payable either in the future, or in a lesser amount, provided that certain conditions are met. The failure of the conditions does not mean that the creditor becomes entitled to damages; the consequence is that the sum which was always owed, but which the debtor was allowed to pay by instalments or a smaller amount, becomes recoverable at once or in full.[84]

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79 See further Carter, "White & Carter v McGregor — How Unreasonable" (2012) 118 Law Quarterly Review 490; Liu, "The White & Carter Principle: A Restatement" (2011) 74 *Modern Law Review* 171.

80 *White and Carter (Councils) Ltd v McGregor* [1962] 2 AC 413, 431.

81 See further, *Attica Sea Carriers Corp v Ferrostaal Poseidon Bulk Reederei GmbH* [1976] 1 Lloyd's Rep 250; *Clea Shipping Corp v Bulk Oil International Ltd (The "Alaskan Trader") (No 2)* [1983] 2 Lloyd's Rep 646. Also *Isabella Shipowner SA v Shagang Shipping Co Ltd (The "Aquafaith")* [2012] EWHC 1077.

82 *Stocznia Gdanska SA v Latvian Shipping Co* [1996] 2 Lloyd's Rep 132, 139, varied without reference to this point [1998] 1 WLR 574.

83 *O'Dea v Allstates Leasing System (WA) Pty Ltd* (1983) 152 CLR 359, 366–7, also 382, 386, cf 403. See also *Acron Pacific Ltd v Offshore Oil NL* (1985) 157 CLR 514, 518.

84 *O'Dea v Allstates Leasing System (WA) Pty Ltd* (1983) 152 CLR 359, 367.

Courts will look to the substance of the provisions in question to see whether or not they genuinely involve the payment of an existing debt or represent a sum imposed as a penalty for non-performance.[85] This emphasis on substance not form is consistent with the decision of the High Court in *Andrews v Australia & New Zealand Banking Group Ltd*.[86]

RESTRICTIONS ON THE RECOVERY OF A DEBT

[29.85] There are several doctrinal limitations on the recovery of a sum as a debt. A party resisting payment of a debt under a contract may sometimes be entitled to make a claim for restitution of a sum paid under a contract on the basis of total failure of consideration.[87] In other cases, a party may be granted equitable relief against penalties[88] or relief against forfeiture.[89] Statute may also sometimes be relevant.[90]

85 See, eg, *O'Dea v Allstates Leasing System (WA) Pty Ltd* (1983) 152 CLR 359. Also *Cameron v UBS AG* [2000] VSCA 222, [22]; *Lachlan v HP Mercantile Pty Ltd* [2015] NSWCA 130, [38]–[58].

86 *Andrews v Australia & New Zealand Banking Group Ltd* [2012] HCA 30; (2012) 247 CLR 205.

87 See generally Mason, Carter and Tolhurst (eds), *Restitution Law in Australia* (3rd ed, 2016).

88 See Chapter 28.

89 See [25.125].

90 See, eg, the discussion of statutory prohibitions on unconscionable conduct in Chapter 38.

CHAPTER **30**

Specific performance and injunctions

THE NATURE OF EQUITABLE REMEDIES

[30.05] The courts in common law jurisdictions will not usually order a party to perform a contractual obligation in specie (in its own form) but instead will order payment of the monetary equivalent of performance, in the form of damages. The reason damages are favoured as a contractual remedy in the common law world is historical and results from the distinction between the common law and equity. The right to performance of a contract is a common law right, which the common law enforces through the remedy of damages. The limited effectiveness of the remedy of damages in some cases was one of the causes of dissatisfaction with the common law courts that led to the development of equity in the Court of Chancery.[1] Because equity acts in personam (against the person, rather than against property), a court exercising equitable jurisdiction has power to order parties to perform their contractual obligations or refrain from acting in breach of contract.

We are concerned in this chapter with the granting of the equitable remedies of specific performance and injunction to give effect to common law rights arising under contracts. Equitable remedies will be granted in aid of common law rights only when the remedy available at common law will not be adequate in the circumstances to compensate the plaintiff. This is because equity acts only as a supplement to the common law and will intervene only where it is necessary to do so because common law rights and remedies are inadequate. Accordingly, the principal remedy for breach of contract is the legal remedy of damages. It is only where damages will not provide an adequate remedy for the plaintiff that equity will supplement the common law by providing specific relief in the form of decrees of specific performance and injunctions. A defendant who knowingly disobeys such an order is in contempt of court and the court can use its powers to compel compliance with the order or punish disobedience.[2] Those powers include the imprisonment of the defendant, the sequestration of his or her property and the issuing of fines.[3]

1 See [2.50]–[2.55].
2 See *Australian Consolidated Press Ltd v Morgan* (1965) 112 CLR 483, 498.
3 Spry, *The Principles of Equitable Remedies* (9th ed, 2014), pp 381–6.

An important difference between damages and equitable remedies is that while damages are available as of right to a plaintiff who can establish a breach of contract, equitable remedies are available on a discretionary basis.[4] A court may, in the exercise of its discretion, require the plaintiff to submit to terms as a condition of obtaining equitable relief. Where a plaintiff seeking specific performance has himself or herself breached the contract, for example, the court may require the plaintiff to compensate the defendant for loss caused by the breach as a condition of obtaining equitable relief.[5] The court may also exercise its discretion by refusing to grant an injunction or specific performance. This is not an unfettered discretion but is exercised according to well-established principles that govern the considerations taken into account by the court.[6]

SPECIFIC PERFORMANCE

[30.10] Specific performance in its narrow or "proper" sense was defined by Dixon J in *JC Williamson Ltd v Lukey and Mulholland* as "a remedy to compel the execution in specie of a contract which requires some definite thing to be done before the transaction is complete and the parties' rights are settled and defined in the manner intended".[7] An example of a contract that requires some definite thing to be done is a contract for the sale of land, which requires the execution of a conveyance or transfer of the land before the transaction is complete. The expression "specific performance" is commonly used in a broader sense to describe any order of the court directing a party to perform his or her obligations under a contract. Little turns on the distinction. The discussion following covers both types of specific performance.[8]

Specific performance in its "proper sense" presupposes an executory contract (ie, one where the parties' obligations under the contract remain to be performed). However, courts may grant relief analogous to specific performance with respect to executed contracts.[9]

Essential requirements

[30.15] Where a contract is suitable for a decree of specific performance, the plaintiff may commence proceedings as soon as the defendant threatens to refuse performance or breaches the contract by failing to perform when the time for performance arrives.[10] In seeking a decree of specific performance, there are certain things the plaintiff must establish: the contract in question must be enforceable at common law, the plaintiff must have provided valuable consideration and damages must be an inadequate remedy in the circumstances. There are also several factors the court will take into account in deciding whether to exercise its discretion to award or refuse specific performance. The most important of those factors will be discussed following, after we have considered the essential requirements.

4 See, eg, *Dowsett v Reid* (1912) 15 CLR 695, 705–6.
5 See, eg, *Mehmet v Benson* (1965) 113 CLR 295.
6 *Goldsbrough Mort & Co Ltd v Quinn* (1910) 10 CLR 674, 697–8; *Fullers' Theatres Ltd v Musgrove* (1923) 31 CLR 524, 549.
7 *JC Williamson Ltd v Lukey and Mulholland* (1931) 45 CLR 282, 297.
8 On the significance of the distinction, see Heydon, Leeming and Turner, *Meagher, Gummow and Lehane's Equity – Doctrines and Remedies* (5th ed, 2015), [20-015] and Hepburn, "Specific Performance", in Parkinson (ed), *The Principles of Equity* (2nd ed, 2003), [1702].
9 See *Waterways Authority of NSW v Coal and Allied (Operations) Pty Ltd* [2007] NSWCA 276, [55]–[71].
10 *Turner v Bladin* (1951) 82 CLR 463, 472.

Consideration

[30.20] A court of equity will only grant specific performance of a contract which has been made for valuable consideration.[11] This principle illustrates the equitable maxim that "equity will not assist a volunteer". While the common law will enforce promises made without consideration if they are made under seal,[12] deeds are not accorded any special status in equity. Accordingly, specific performance of a deed will not be decreed unless consideration has been given by the plaintiff. The common law principles as to the sufficiency of consideration are generally applied for this purpose, although the English courts have occasionally adopted a broader notion of consideration.[13]

Enforceability

[30.25] Specific performance will not be decreed if a contract is invalid at law, such as where it has been made for an illegal purpose. Nor will it be decreed if the contract is liable to be rescinded because of some unfair conduct on the part of the plaintiff, such as misrepresentation or duress. Generally, specific performance will not be granted in respect of a contract that is unenforceable because of a failure to comply with a statutory requirement of writing. Specific performance will be granted, however, where it is considered inequitable or unconscionable to rely on the statute under the equitable doctrines of part performance or equitable estoppel. The remedy of specific performance is routinely granted to give effect to the doctrine of part performance[14] and is occasionally granted to give effect to equitable estoppel.[15]

Relative inadequacy of damages

[30.30] The principal restriction on the availability of specific performance is the requirement that damages must be an inadequate remedy for breach. The relevant principle is that: "The Court gives specific performance instead of damages, only when it can by that means do more perfect and complete justice."[16] The court's concern is not so much with the adequacy of damages as with superiority of specific performance in the circumstances. The remedy of specific performance will be refused if performance of the obligation would not put the plaintiff in a better position than the payment of damages. As noted above, the reason for this requirement is that equity acts only as a supplement to the common law. When the common law provides an adequate remedy, there is no need for equity to intervene. Dixon J explained in *Dougan v Ley* that proceedings in the Court of Chancery would be dismissed if a remedy was available to the plaintiff at common law:

> Though in earlier times the absence of an adequate theory of simple contract had led to the interposition of Chancery on wider grounds, by the seventeenth century, if not before, it had come to be "taken for a good cause of dismission" of a bill "in most causes, to say that he" the plaintiff "hath remedy at the common law".[17]

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11 *Jefferys v Jefferys* (1841) Cr & Ph 138; 41 ER 443.

12 See [4.120].

13 See Spry, *The Principles of Equitable Remedies* (9th ed, 2014), pp 59–61.

14 See, eg, *Regent v Millett* (1976) 133 CLR 679.

15 See, eg, *Waltons Stores (Interstate) Ltd v Maher* (1988) 164 CLR 387.

16 *Wilson v Northhampton and Banbury Junction Railway Co* (1874) 9 Ch App 279, 284, quoted with approval in *Dougan v Ley* (1946) 71 CLR 142, 150.

17 *Dougan v Ley* (1946) 71 CLR 142, 150, quoting (circa 1602) Cary 20; 21 ER 11.

Specific performance is most commonly granted in the case of contracts for the sale of land. Because each parcel of land is unique, it is assumed to have a special value for the purchaser; accordingly, damages are not seen as an adequate remedy if the vendor refuses to complete the contract.[18] The presumption that damages will always be an inadequate remedy for a purchaser of land has been abandoned in Canada. The Supreme Court of Canada held in *Semelhago v Paramadavam*[19] that specific performance of a contract for the sale of land should be decreed only where the plaintiff proves that the land is unique, in the sense that a substitute is not readily available. Canadian courts may therefore refuse to grant specific performance to the purchaser of vacant land if lots of similar size and aspect are available nearby. It is probably now impossible for a purchaser of an investment or development property to obtain a decree of specific performance – even if the land has unique and highly desirable characteristics – because the loss of an investment can always be compensated in damages. In a recent case, the purchaser of a development property was refused specific performance on that basis even though no properties with similar characteristics were available.[20] Because the purchaser sought specific performance, rather than terminating the contract and purchasing another development property, the purchaser was held to have failed to take reasonable steps to mitigate its loss and was awarded nominal damages of $1, even though its expectation loss (a 60 per cent chance of earning $3.2m in profit from the development) was almost $2m.[21]

Specific performance is not available in respect of contracts for the sale of personalty, such as chattels or shares, if the thing contracted for is readily obtainable from another source. If, for example, the seller of shares listed on the stock exchange refused to complete the contract, the buyer could simply purchase identical shares on the market, and damages would compensate the buyer for any additional cost incurred in doing so. On the other hand, where there is no available market for shares, or they have a special value to the buyer, specific performance will be ordered even if the purchaser is buying the shares with the intention of reselling them at a profit.[22]

In *Dougan v Ley*,[23] the subject matter of the contract was a taxi and a licence to operate the taxi. The seller argued that specific performance should not be decreed in favour of the buyer because damages provided an adequate remedy. The buyer was, in fact, able to buy another taxi and licence shortly before the hearing. The High Court confirmed that specific performance will not be decreed where damages will provide an adequate remedy for the plaintiff and this is generally the case where the subject matter is an item of personal property.[24] In this case, however, specific performance was appropriate because the number of taxi licences was limited, they were in great demand and the licence represented a substantial proportion of the sale price. Where property is of such a nature that specific performance is available, the purchase of similar property will not affect the purchaser's rights.[25]

18 *Dougan v Ley* (1946) 71 CLR 142, 150.

19 *Semelhago v Paramadavam* [1996] 2 SCR 415.

20 *Southcott Estates Inc v Toronto Catholic District School Board* 2009 CanLII 3567 (ON SC), [125]–[127].

21 *Southcott Estates Inc v Toronto Catholic District School Board* 2012 SCC 51; [2012] 2 SCR 675, discussed by McInnes, "Specific Performance and Mitigation in the Supreme Court of Canada" (2013) 129 *Law Quarterly Review* 165.

22 *ANZ Executors and Trustees Ltd v Humes Ltd* [1990] VR 615.

23 *Dougan v Ley* (1946) 71 CLR 142.

24 *Dougan v Ley* (1946) 71 CLR 142, 150–1, 153.

25 *Dougan v Ley* (1946) 71 CLR 142.

Specific performance will not generally be decreed in favour of a party whose claim is simply for the payment of money, since specific performance would put the plaintiff in precisely the same position as the payment of the debt or damages. A lender of money could not, for example, obtain specific performance of the borrower's obligation to repay. Where the subject matter of a contract is such that a purchaser would be entitled to a decree of specific performance on the ground of inadequacy of damages, however, it is clear that the seller will also be entitled to a decree.[26] A seller of land or unique goods will therefore have a prima facie entitlement to a decree of specific performance. This may be justified on the basis of mutuality (ie, that the seller should be entitled to a remedy which would be available to the buyer) or on the basis that divestment of ownership, as well as payment of the purchase price, is necessary to give the seller an adequate remedy.[27]

It is not only the subject matter of the contract that can make damages an inadequate remedy. Damages may be regarded as inadequate because the plaintiff's losses are difficult to prove or quantify.[28] The defendant's insolvency, and consequent inability to comply with an order to pay damages, may also justify a decree of specific performance,[29] although the courts may refuse specific performance where it would give the plaintiff an unfair advantage over other creditors.[30] Damages will generally provide an inadequate remedy to enforce a contract that confers a benefit on a third party. Specific performance will therefore be granted, even if the relevant obligation is simply to pay money.[31]

Discretionary factors

[30.35] The distinction between essential requirements and discretionary factors is not entirely settled. Some situations falling within the discretionary categories below will always result in a refusal to order specific performance. Nevertheless, all of the factors listed below as discretionary can involve questions of degree and, in those situations, the factors indicating that specific performance should be refused must be balanced against the injustice to the plaintiff in being restricted to a remedy in damages.

Supervision

[30.40] An important factor the courts take into account in deciding whether to decree specific performance is the extent to which the continued supervision of the court would be necessary to ensure the fulfilment of the contract. A contract requiring the performance of a single act, such as the execution of a document transferring an interest in land to the plaintiff, requires very little supervision on the part of the court. The defendant either has or has not performed the act. A contract requiring the performance of building works, on the other hand, may give rise to difficulties of supervision. A decree of specific performance would require the

26 *Turner v Bladin* (1951) 82 CLR 463.

27 Spry, *The Principles of Equitable Remedies* (9th ed, 2014), pp 64–5.

28 *ANZ Executors and Trustees Ltd v Humes Ltd* [1990] VR 615. For an example, see *Diagnostic X-Ray Services Pty Ltd v Jewel Food Stores Pty Ltd* [2001] VSC 9; (2001) 4 VR 632, [30.40].

29 See, eg, *Associated Portland Cement Manufacturers Ltd v Tigland Shipping A/S ("The Oakworth")* [1975] 1 Lloyd's Rep 581, where an injunction was granted on the basis of the defendant's inability to meet a claim for damages.

30 See Spry, *The Principles of Equitable Remedies* (9th ed, 2014), pp 70–2.

31 *Beswick v Beswick* [1968] AC 58; *Coulls v Bagot's Executor and Trustee Co Ltd* (1967) 119 CLR 460, 478, 503. See further [11.60]–[11.70].

defendant to undertake a series of acts over a long period of time. There is far greater scope for disputes to arise between the parties as to whether the order has been complied with, and for repeated applications to the court to adjudicate on those disputes.

It has been said that specific performance will not, as a rule, be granted where the continued supervision of the court would be required to ensure fulfilment of the contract.[32] The extent to which supervision might be required is, however, more accurately described as a consideration to be taken into account, rather than an absolute rule.[33] Questions of degree are necessarily involved and the extent to which the court might be required to make further orders must be balanced against other considerations, particularly the hardship to the plaintiff if specific relief is refused.[34] An important factor to be weighed in the balance is the certainty with which the parties' obligations have been defined. The parties and the court must be able to judge whether performance has taken place in accordance with the contract, and the less precisely defined the parties' obligations are, the more likely the court is to refuse a decree.[35]

The operation of those principles can be seen in the decision of the House of Lords in *Co-operative Insurance Society Ltd v Argyll Stores (Holdings) Ltd*.[36] The defendant operated a supermarket in a shopping centre owned by the plaintiff. The terms of the lease required the defendant to keep the supermarket open during the usual hours of business. In breach of that obligation, the defendant closed the supermarket because it was operating at a loss. The plaintiff sought specific performance of the agreement on the basis that the supermarket, as the "anchor tenant" in the shopping centre, played an important role in attracting customers to the centre. The trial judge refused specific performance in accordance with the "settled practice" that the courts would not make orders requiring a defendant to operate a business. The Court of Appeal allowed an appeal, but the trial judge's decision was restored by the House of Lords. Lord Hoffmann, with whom the other members of the House of Lords agreed, drew a distinction between orders that require the defendant to carry on an activity over an extended period of time, such as running a business, and orders requiring a defendant to achieve a particular result.[37] In the former case, there is a real risk of repeated applications to the court for rulings on compliance. In the latter case, even if the thing to be done is complicated, the court ultimately has only to determine whether the thing has been done. Lord Hoffmann also regarded the obligation to trade as insufficiently precise to be capable of specific performance.[38] He noted that a contractual obligation may not be sufficiently precise to be specifically enforced, even though it is not void for uncertainty and might be relied upon in support of a claim for damages.[39]

In *Diagnostic X-Ray Services Pty Ltd v Jewel Food Stores Pty Ltd*,[40] on the other hand, Beach J was prepared to grant an interlocutory injunction requiring the anchor tenant of a

32 *JC Williamson Ltd v Lukey and Mulholland* (1931) 45 CLR 282, 292–3, 297–8.

33 See *Patrick Stevedores Operations No 2 Pty Ltd v Maritime Union of Australia* [1998] HCA 30; (1998) 195 CLR 1.

34 Spry, *The Principles of Equitable Remedies* (9th ed, 2014), p 108.

35 See, eg, *Joseph v National Magazine Co Ltd* [1959] Ch 14.

36 *Co-operative Insurance Society Ltd v Argyll Stores (Holdings) Ltd* [1998] AC 1.

37 *Co-operative Insurance Society Ltd v Argyll Stores (Holdings) Ltd* [1998] AC 1, 13.

38 *Co-operative Insurance Society Ltd v Argyll Stores (Holdings) Ltd* [1998] AC 1, 16–7.

39 *Co-operative Insurance Society Ltd v Argyll Stores (Holdings) Ltd* [1998] AC 1, 14.

40 *Diagnostic X-Ray Services Pty Ltd v Jewel Food Stores Pty Ltd* [2001] VSC 9; (2001) 4 VR 623. As to mandatory injunctions, see [30.95].

shopping centre to operate a petrol station. The defendant leased a supermarket and petrol station in a suburban shopping centre and operated them for seven years.[41] Following a restructure of its business, the defendant sub-let the supermarket and, when it could not sub-let the petrol station on satisfactory terms, simply abandoned it. The petrol station had played an important role in attracting patrons to the centre and its closure caused significant detriment to the other tenants. Beach J said this was an exceptional case. Since the defendant had operated the petrol station for seven years, there was no reason why it could not continue to do so without the supervision of the court. Beach J distinguished *Co-operative Insurance Society Ltd v Argyll Stores (Holdings) Ltd* on the basis, among other things, that this was not a case where a venture had "turned sour": it was always clear that the petrol station would need to be subsidised by the supermarket business. Following its business restructure, the defendant was seeking to find a new tenant for the petrol station. There was no reason why the defendant should not continue to operate the petrol station until a new tenant was found. The loss caused by the defendant's breach was substantial but would be very difficult to quantify. Accordingly, damages would not provide an adequate remedy.

Personal services

[30.45] The remedy of specific performance is granted in respect of contracts of personal service only in "exceptional circumstances".[42] Apart from the obvious difficulties involved in supervision of such contracts, it is considered undesirable for a court to force a person to perform a contract of personal service, particularly where the relationship of trust and confidence between the parties has broken down.[43] The courts will usually also refuse to decree specific performance of contracts requiring continual co-operation between the parties, such as partnership[44] and share-farming[45] contracts.

Mutuality

[30.50] A court making an order for specific performance must be able to ensure that the plaintiff, as well as the defendant, performs his or her obligations.[46] Accordingly, the courts will not decree specific performance in favour of a plaintiff if, in the circumstances, such relief would not be available to the defendant. Where the defendant would be denied a decree because, for example, the plaintiff's obligations include an element of personal service or would require the constant supervision of the court, the plaintiff will also be denied a decree. The mutuality principle is exemplified by *JC Williamson Ltd v Lukey and Mulholland*.[47] The defendants, who were lessees of a theatre, granted the plaintiffs a licence to sell confectionery in the theatre for a period of five years in return for a promise by the plaintiffs to pay a weekly

41 The lease must have included a provision requiring the defendant to keep the supermarket and petrol station open on specified days, although this is not actually mentioned in the judgment. The term of the lease was 15 years.

42 *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 428.

43 *Tradition Australia Pty Ltd v Gunson* [2006] NSWSC 298; (2006) 152 IR 395, [27]. See also Saprai, "The Principle against Self-enslavement in Contract Law" (2009) 26 *Journal of Contract Law* 25.

44 *Douglas v Hill* [1909] SALR 28, 31; *Renowden v Hurley* [1951] VLR 13.

45 *Dudgeon v Chie* (1955) 92 CLR 342.

46 *JC Williamson Ltd v Lukey and Mulholland* (1931) 45 CLR 282, 298.

47 *JC Williamson Ltd v Lukey and Mulholland* (1931) 45 CLR 282.

fee. It was implied in the agreement that the plaintiffs were obliged to employ a sufficient number of staff, whose uniforms and behaviour would be under the control of the defendants, and to maintain a supply of confectionery of the kind and quality of usually sold in the theatre. Before the term of the licence expired, the defendants repudiated the agreement and granted the exclusive right to sell confectionery in the theatre to a third party. A decree of specific performance was refused. The plaintiffs' obligations involved repeated acts and might have required constant supervision. It was held to be unjust to bind the defendants to perform their obligations by a decree of specific performance, while leaving the defendants to a remedy in damages in the event of a breach by the plaintiffs.[48]

Delay in seeking relief

[30.55] A plaintiff seeking to assert an equitable right or obtain an equitable remedy, such as specific performance, may be prevented from doing so by the equitable defence of laches. Laches operates where the plaintiff has been guilty of unreasonable delay, and this delay has caused prejudice to the defendant which cannot adequately be compensated.[49] The defendant may, for example, be prejudiced by the disposition of property or the loss of access to documents necessary to defend against the claim.[50]

Breach

[30.60] Whether the plaintiff is in breach of the contract is an important factor for the court to consider in determining whether to grant the decree. A breach of contract will not, however, necessarily bar a plaintiff from a decree of specific performance. Where the plaintiff has breached an inessential term, specific performance will generally be granted, provided the plaintiff is ready and willing to perform the essential terms.[51] Where the plaintiff has breached an essential term, an order for specific performance will be made only in exceptional circumstances, such as where the defendant has caused or contributed to the plaintiff's breach.[52]

Readiness and willingness to perform

[30.65] A court will consider whether a plaintiff seeking specific performance is ready, willing and able to perform all of his or her obligations under the contract.[53] It will usually be inappropriate to decree specific performance in favour of a plaintiff who is unable or unwilling to perform an essential term.[54] An unwillingness or unreadiness to comply with an inessential term will not of itself necessarily bar relief but will be relevant to the exercise of the court's discretion.[55]

48 *JC Williamson Ltd v Lukey and Mulholland* (1931) 45 CLR 282, 298.

49 See *Fitzgerald v Masters* (1956) 95 CLR 420.

50 See *Hourigan v Trustees Executors and Agency Co Ltd* (1934) 51 CLR 619.

51 See *Mehmet v Benson* (1965) 113 CLR 295.

52 See *Legione v Hateley* (1983) 152 CLR 406; *Ciavarella v Balmer* (1983) 153 CLR 438; *Tanwar Enterprises Pty Ltd v Cauchi* [2003] HCA 57; (2003) 217 CLR 315. See further [25.125]–[25.155].

53 See *Mehmet v Benson* (1965) 113 CLR 295.

54 See *Bahr v Nicolay (No 2)* (1988) 164 CLR 604.

55 See *Mehmet v Benson* (1965) 113 CLR 295, 308; *Green v Sommerville* (1979) 141 CLR 594.

Hardship

[30.70] The court may also refuse specific performance on the basis that specific relief would cause hardship to the defendant that would not be caused by an award of damages. The court must weigh up any hardship that the defendant would suffer if the decree were granted against the detriment the plaintiff would suffer if he or she were confined to a remedy in damages.[56] A good example of hardship which justified refusal of the decree is provided by *Norton v Angus*,[57] which involved a contract for the purchase of two selections of Crown leasehold land held under the *Land Acts 1910–1924* (Qld). The two selections together exceeded the maximum area of land that one person was allowed to hold in the relevant district and the purchaser risked forfeiture of the land if forced to accept a transfer. Accordingly, the court by majority refused to order specific performance against the purchaser and ordered an inquiry into damages instead.

Unfairness

[30.75] Where the transaction has been affected by unfair conduct on the part of the plaintiff, such as undue influence, unconscionable dealing or misrepresentation, which entitles the defendant to a decree of rescission, then specific performance will clearly be refused. If the circumstances of formation of a contract do not justify rescission, but render it unfair to require the defendant to carry out his or her obligations, this may also justify a refusal of specific performance, particularly in conjunction with other factors. A unilateral mistake on the part of the defendant, which has not been induced by the plaintiff, for example, will justify a refusal of specific performance if the remedy would cause hardship to the defendant.[58] In these circumstances, the plaintiff would still be entitled to the legal remedy of damages. In *Blomley v Ryan*,[59] for example, Fullagar J noted that where the judgment of the defendant at the time of making the contract was, to the knowledge of the plaintiff, seriously affected by alcohol, equity will generally refuse specific performance, leaving the plaintiff to "pursue a remedy at law".[60]

Impossibility, illegality and futility

[30.80] A court will not decree specific performance of a contract which cannot be performed, such as a contract for the sale of land which is no longer owned by the vendor.[61] A risk of illegal conduct in performance may also lead the court to refuse specific performance.[62] The remedy may also be refused where it is likely to be futile, in the sense that the defendant's performance of the contract is unlikely to confer any real benefit on the plaintiff. It has, for example, been said that a court would refuse specific performance of an agreement to execute

56 Spry, *The Principles of Equitable Remedies* (9th ed, 2014), pp 204–8.

57 *Norton v Angus* (1926) 38 CLR 523. See also *Dowsett v Reid* (1912) 15 CLR 695, 706–7.

58 See *Goldsbrough Mort & Co Ltd v Quinn* (1910) 10 CLR 674; *Slee v Warke* (1949) 86 CLR 271; *Fragomeni v Fogliani* (1968) 42 ALJR 263.

59 *Blomley v Ryan* (1956) 99 CLR 362.

60 *Blomley v Ryan* (1956) 99 CLR 362, 405.

61 See *Ferguson v Wilson* (1866) LR 2 Ch App 77, 91.

62 See *Pottinger v George* (1967) 116 CLR 328, 337; *Norton v Angus* (1926) 38 CLR 523.

a deed creating a partnership which is terminable at will and might therefore be terminated by the defendant immediately after the deed is signed.[63]

Should specific performance be the usual remedy?

The civil law approach

[30.85] It is clear from the earlier discussion that the award of damages is the usual remedy for breach of contract in the common law system, while specific performance is exceptional. Orders for specific performance play a more prominent role in civil law systems. In German law, specific performance is the normal remedy for breach of contract, with damages constituting the exception. Although the general rule is that performance will be required, there are several exceptions, and it is said that in practice these exceptions are more important than the general rule.[64] The practical significance of specific performance is also diminished by the fact that commercial parties usually prefer to claim damages in cases where their losses can easily be quantified.[65] The difference between the common law and civil law approaches is not, therefore, as dramatic as their respective starting positions might suggest.[66] Nevertheless, the German approach to specific performance provides an interesting contrast with that of common law jurisdictions.

Essential to the notion of an obligation in German law is that a "creditor" can bring a claim for performance of the obligation and obtain a judgment ordering the "debtor" to perform it.[67] This enforceable right to performance of legal obligations in contract and tort is enshrined in § 241 of the *Bürgerliches Gesetzbuch* (BGB), which provides that legal obligations entitle the creditor to claim performance by the debtor. Although German courts have discretionary power to order payment of damages instead of performance, this power is not usually invoked where one party prefers performance.[68] Performance will be required provided it has not become impossible and would not require unreasonable effort or expense on the part of the debtor.[69]

The way in which orders for performance will be enforced in German law depends on the nature of the obligation in question. Where land or goods are to be transferred, a bailiff will take possession of the property and deliver it to the creditor. Where a debtor promises to do something that does not require his or her particular talents (such as building works), the court will order the thing to be done at the debtor's expense. Where the act promised can only be performed by the debtor, and depends exclusively on his or her will, the court will threaten the debtor with a fine or imprisonment. The German courts will grant judgments requiring

63 *Henry v Birch* (1804) 9 Ves 357; 32 ER 640. But see Spry, *The Principles of Equitable Remedies* (9th ed, 2014), pp 139–40; *Renowden v Hurley* [1951] VLR 13, 22.

64 Treitel, *Remedies for Breach of Contract: A Comparative Account* (1988), p 53.

65 Treitel, *Remedies for Breach of Contract: A Comparative Account* (1988), p 71; Zweigert and Kötz, *Introduction to Comparative Law* (3rd ed, 1998), pp 472, 484.

66 Treitel, *Remedies for Breach of Contract: A Comparative Account* (1988), p 71.

67 Zweigert and Kötz, *Introduction to Comparative Law* (3rd ed, 1998), p 472; Markesinis, Lorenz and Dannemann, *The German Law of Obligations* (1997), Vol 1, pp 29–30.

68 Dawson, "Specific Performance in France and Germany" (1959) 57 *Michigan Law Review* 494, 529–30.

69 Zweigert and Kötz, *Introduction to Comparative Law* (3rd ed, 1998), pp 472–3; Treitel, *Remedies for Breach of Contract: A Comparative Account* (1988), pp 52–3.

employees to perform contracts of service but will not enforce these judgments against the employee.[70]

A compromise between the common law and civil law approaches to specific performance has been adopted in the *UNIDROIT Principles of International Commercial Contracts 2016* (UPICC).[71] Article 7.2.2 provides that one party may "require performance" by the other unless performance is impossible, unreasonably burdensome, reasonably obtainable from another source, exclusively personal or has not been required within a reasonable time. Although the starting point under Art 7.2.2 is the civil law notion of a right to performance of a contractual obligation, the exception available where performance is "reasonably obtainable from another source" could be interpreted in a similar way to the inadequacy of damages requirement. The UPICC also confers on an aggrieved party a right to damages, "either exclusively or in conjunction with any other remedies".[72]

Economic analysis

[30.90] These comparative perspectives raise the question whether the remedy of specific performance should be more widely available than it is under the common law system. This question has received considerable attention, particularly from law and economics scholars in the United States.[73] Alan Schwartz has argued that specific performance should be routinely available because awards of damages undercompensate the plaintiff; they do not include the true cost of entering into a substitute transaction and may underestimate the plaintiff's loss as a result of inherent difficulties of prediction.[74] Plaintiffs are likely to seek specific performance only when damages are unlikely to be fully compensatory because there are strong economic incentives to sue for damages rather than specific performance.[75] It will normally be quicker and cheaper to obtain a substitute performance and sue for damages than to sue for specific performance and monitor performance by a reluctant promisor. Accordingly, Schwartz argues specific performance should be generally available, and plaintiffs, rather than the courts, should decide whether damages are adequate.

The economic argument against specific performance is that the law should encourage efficient breaches of contract. We have already seen that a breach of contract is efficient if the contract breaker's profit from the breach is likely to be greater than the innocent party's loss.[76] The contract breaker can then afford to compensate the innocent party for his or her loss and still be better off than he or she would have been had the contract been performed. If A must breach a contract with B in order to perform more profitably for C, then A should do this because her resources will be employed where they are most valuable. A remedy of expectation damages, rather than specific performance, facilitates and encourages efficient breaches by contracting parties such as A.[77] Ian Macneil has argued that it is not necessary for A to breach

70 Zweigert and Kötz, *Introduction to Comparative Law* (3rd ed, 1998), p 474.

71 See [1.180].

72 *UNIDROIT Principles of International Commercial Contracts 2016* Art 7.4.1.

73 See Morgan, *Great Debates in Contract Law* (2nd ed, 2015), Ch 9; Markovits and Schwartz, "The Myth of Efficient Breach: New Defenses of the Expectation Interest" (2011) 97 *Virginia Law Review* 1939, for discussion of recent contributions.

74 Schwartz, "The Case for Specific Performance" (1979) 89 *Yale Law Journal* 271, 276.

75 Schwartz, "The Case for Specific Performance" (1979) 89 *Yale Law Journal* 271, 277.

76 See [26.130].

77 Posner, *Economic Analysis of Law* (9th ed, 2014), § 4.10.

the contract with B in order to ensure efficient use of her resources: non-performance is all that is required and this can be achieved by B releasing A from the contract.[78] If specific performance is available to B, then A will need to negotiate a release from the contract. Since A is able to pay B more than the amount of B's loss from non-performance, we can assume they will make a deal.[79] Thus, neither damages nor specific performance prevents efficient non-performance by a contracting party.

Ultimately, the relative efficiency of the remedies will depend on the relative transaction costs of operating under each rule. These may include not only the cost of negotiating a release from the inefficient contract between A and B and the cost of negotiating a substitute contract between B and an alternative supplier but also the cost of litigation and the cost of A's loss of reputation.[80] In most cases, Macneil suggests these transaction costs under either rule are likely to exceed the gross efficiency gains of abandoning the transaction between A and B. The extent of the transaction costs in either case may depend on the timeliness of A's communication with B and, in particular, whether A actually breaches or threatens to breach the contract.[81]

Macneil has also pointed out that the idea that a contracting party should breach, rather than renegotiate, the contract where it is efficient to do so is based on an unco-operative model of contracting behaviour. The neo-classical economic model underlying the principle of efficient breach ignores the fact that the parties are engaged in complex social relations that affect their behaviour and may reward co-operation.[82] Co-operative behaviour will often be in the interests of a party seeking to avoid performance of a contractual obligation. Early communication and a co-operative approach are likely to minimise the cost of non-performance to the promisee, as well as enhancing the likelihood of preserving an economically valuable relationship between the parties.[83]

Macneil suggests that the theory of efficient breach might equally well be used to justify efficient theft. Assume A delivers widgets to B in accordance with their contract and passes property in the widgets to B. C then offers A a sum of money for the widgets, that would be sufficient to compensate B for the loss of the widgets and still allow A to make a profit. If A was to steal the widgets from B and sell them to C, this could be seen as efficient, since it would shift the resources to a more highly valued use. It has been argued, however, that economic considerations support the property rules that protect B's interest in the widgets.[84] A could have negotiated a voluntary transfer of the widgets from B, and only a voluntary transfer would provide an accurate indication of the worth of the widgets to B. An award of damages would represent only an approximation of the value B places on the widgets, and so

78 Macneil, "Efficient Breach of Contract: Circles in the Sky" (1982) 68 *Virginia Law Review* 947.

79 Macneil, "Efficient Breach of Contract: Circles in the Sky" (1982) 68 *Virginia Law Review* 947, 952.

80 See Macneil, "Efficient Breach of Contact: Circles in the Sky" (1982) 68 *Virginia Law Review* 947, 957–60 for a full discussion. Some of these costs are analysed by Schwartz, "The Case for Specific Performance" (1979) 89 *Yale Law Journal* 271, 278–96.

81 Macneil, "Efficient Breach of Contract: Circles in the Sky" (1982) 68 *Virginia Law Review* 947, 958.

82 See further Macneil "Economic Analysis of Contractual Relations: Its Shortfalls and the Need for a 'Rich Classificatory Apparatus'" (1981) 75 *Northwestern University Law Review* 1018.

83 See Macneil, "Efficient Breach of Contract: Circles in the Sky" (1982) 68 *Virginia Law Review* 947, 959.

84 Calebresi and Melamed, "Property Rules, Liability Rules and Inalienability: One View of the Cathedral" (1972) 85 *Harvard Law Review* 1089, 1125.

allowing A to steal the widgets and pay damages would not necessarily result in an efficient allocation of resources.

The question for contract law, then, is whether those economic considerations also justify protecting the promisee's right to performance of a contractual obligation through the remedy of specific performance. Anthony Kronman has argued that they do, but only where the subject matter of the contract is unique.[85] Where the subject matter is not unique, the court will be able to identify a substitute for the subject matter and can ensure that the damages award covers the cost of obtaining that substitute. The more developed the market, the better the evidence of substitutability and thus the lower the risk of undercompensation. Where the subject matter is unique, the court does not have a reliable way of knowing what the plaintiff regards as an acceptable substitute for the promised subject matter and therefore runs a much greater risk of undercompensating the plaintiff. Where the goods are unique, the plaintiff is also likely to incur greater transaction costs in seeking a substitute.[86] The approach taken in common law jurisdictions – of granting specific performance in the case of unique goods but not in the case of goods readily available on the market – can therefore be said to be justified by economic considerations.

INJUNCTIONS

[30.95] An injunction is an order of the court forbidding or commanding the performance of an act. A decree of specific performance is a form of injunction, but is treated separately because a discrete body of principle has developed governing the circumstances in which it is granted. The distinction between a decree of specific performance and other injunctions to enforce contractual terms is not clear. The best explanation is that specific performance is usually granted in respect of the whole of an agreement, while an injunction will be granted to ensure compliance with a particular term of a contract. This explanation is not entirely satisfactory, however, because, although it is sometimes said that specific performance will not be granted in respect of only part of an unseverable contract,[87] there are exceptions to this rule.[88]

An injunction is usually granted to restrain the breach of a negative stipulation in a contract, that is, a contractual undertaking not to do something. It is said that "[i]f … a clear legal duty is imposed by contract to refrain from some act, then, prima facie, an injunction should go to restrain the doing of that act".[89] Courts are far less willing to grant mandatory injunctions requiring compliance with positive obligations under contracts.[90] In determining whether a contractual obligation is negative or positive, the court looks to the substance of the obligation, rather than the form in which it is expressed. An

85 Kronman, "Specific Performance" (1978) 45 *University of Chicago Law Review* 351.

86 Kronman, "Specific Performance" (1978) 45 *University of Chicago Law Review* 351, 363–4.

87 *JC Williamson Ltd v Lukey and Mulholland* (1931) 45 CLR 282, 294.

88 See Spry, *The Principles of Equitable Remedies* (9th ed, 2014), pp 113–17; Heydon, Leeming and Turner, *Meagher, Gummow and Lehane's Equity – Doctrines and Remedies* (5th ed, 2015), [20-130]–[20-135].

89 *JC Williamson Ltd v Lukey and Mulholland* (1931) 45 CLR 282, 299. See also *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [12].

90 For an example of a case in which the Court was prepared to grant a mandatory injunction, at least until trial, see *Diagnostic X-Ray Services Pty Ltd v Jewel Food Stores Pty Ltd* [2001] VSC 9; (2001) 4 VR 632, [30.40].

obligation will be regarded as negative only if inactivity would constitute compliance with the term.[91]

Inadequacy of damages

[30.97] The courts will grant an injunction requiring performance of a positive obligation only when the plaintiff shows that damages would be inadequate.[92] In the case of a negative obligation, the inadequacy of damages has tended to be treated as a consideration to be taken into account, rather than a strict requirement. A test which has been applied in determining whether to grant an injunction to restrain a breach of a negative obligation is whether it is just to confine the plaintiff to his or her remedy in damages.[93] In *Lucas Stuart Pty Ltd v Hemmes Hermitage Pty Ltd*, however, Campbell JA observed that a court of equity has no jurisdiction to grant a remedy for breach of a common law obligation unless the common law remedy is inadequate.[94] Although in most cases the inadequacy of a common law remedy will be made out where an injunction is sought to restrain a breach of a negative contractual stipulation, "this is an empirical generalisation, not a legal principle".[95] As a matter of principle, the inadequacy of damages is a requirement that must be satisfied.[96]

In *AB v CD*, the English Court of Appeal considered whether the existence of an exclusion or limitation of liability clause could be taken into account in determining whether damages would provide an adequate remedy for the innocent party. The Court held that it could and should be taken into account. The clause in question would have entirely excluded liability with respect to the breach sought to be restrained by the injunction, and it was argued that the granting of the injunction would therefore upset the commercial expectations of the parties.[97] The Court of Appeal rejected that argument on the basis that the commercial expectation of the parties must be that the parties' contractual obligations will be performed.[98] The expectation created and given force by a limitation or exclusion clause concerned the recoverability of damages, not performance.[99] Underhill LJ said:

> The primary obligation of a party is to perform the contract. The requirement to pay damages in the event of a breach is a secondary obligation, and an agreement to restrict the recoverability of damages in the event of a breach cannot be treated as an agreement to excuse performance of that primary obligation.[100]

91 *Administrative and Clerical Officers Association v Commonwealth* (1979) 26 ALR 497.

92 *Sky Petroleum Ltd v VIP Petroleum Ltd* [1974] 1 WLR 576.

93 *Evans Marshall & Co Ltd v Bertola SA* [1973] 1 WLR 349, 379–80; *Sanderson Motors (Sales) Pty Ltd v Yorkstar Motors Pty Ltd* [1983] 1 NSWLR 513, 516; *AB v CD* [2014] EWCA Civ 229; [2015] 1 WLR 771.

94 *Lucas Stuart Pty Ltd v Hemmes Hermitage Pty Ltd* [2010] NSWCA 283, [5]; see also [62] (Young JA).

95 *Lucas Stuart Pty Ltd v Hemmes Hermitage Pty Ltd* [2010] NSWCA 283, [8].

96 See also *AB v CD* [2014] EWCA Civ 229; [2015] 1 WLR 771, [30] (inadequacy of damages "opens the door to the exercise of the court's discretion").

97 *AB v CD* [2014] EWCA Civ 229; [2015] 1 WLR 771, [23].

98 *AB v CD* [2014] EWCA Civ 229; [2015] 1 WLR 771, [28].

99 *AB v CD* [2014] EWCA Civ 229; [2015] 1 WLR 771, [27].

100 *AB v CD* [2014] EWCA Civ 229; [2015] 1 WLR 771, [27] (Underhill LJ, with whom Ryder and Laws LJJ agreed).

Injunctions tantamount to specific performance

[30.98] The courts are reluctant to grant an injunction which would be tantamount to a decree of specific performance in circumstances where such a decree would be unavailable, such as where the plaintiff's obligations involve personal service or would require supervision by the court, or for reasons of mutuality.[101] A particular difficulty arises when a plaintiff seeks an injunction to restrain a breach of a negative stipulation in an employment contract. In the famous case of *Lumley v Wagner*,[102] an injunction was granted to restrain a singer from breaching a contractual promise that she would not "use her talents at any other theatre" during the season for which she was contracted to the plaintiff. The decision has been distinguished in situations where the injunction sought would force the defendant to perform the contract for personal services or be put out of work altogether.[103] In *Page One Records Ltd v Britton*,[104] Stamp J refused to grant an interlocutory injunction restraining music group "The Troggs" from using a rival manager or music publisher. The fact that the agreement had four years left to run may have been the decisive factor.[105] Stamp J distinguished the case from *Lumley v Wagner* on the basis that here an injunction would effectively compel The Troggs to continue to employ the plaintiff and would thus indirectly require performance of a contract for personal services.[106]

A different approach was taken in *Buckenara v Hawthorn Football Club Ltd*,[107] where Buckenara agreed not to take part in any football match other than for the Hawthorn Football Club for two years. When Buckenara wanted to leave Hawthorn to play for a rival club, Hawthorn sought an injunction to enforce the contractual promise. Crockett J considered that enforcement of the contractual restraint would effectively have forced Buckenara to play with Hawthorn and so he granted an injunction which was limited to preventing Buckenara from playing for rival clubs for the relevant period.[108]

DAMAGES UNDER LORD CAIRNS' ACT

[30.100] In all Australian jurisdictions, legislative provisions allow the courts to award damages either in addition to, or in lieu of, specific performance or an injunction.[109] These provisions are modelled on English legislation known as *Lord Cairns' Act*.[110] The rationale for this legislation is historical, but the provisions retain an important practical role. *Lord Cairns'*

101 *JC Williamson Ltd v Lukey and Mulholland* (1931) 45 CLR 282. See also Saprai, "The Principle against Self-enslavement in Contract Law" (2009) 26 *Journal of Contract Law* 25.

102 *Lumley v Wagner* (1852) 1 De GM & G 604; 42 ER 687.

103 See, eg, *Heine Bros (Aust) Pty Ltd v Forrest* [1963] VR 383.

104 *Page One Records Ltd v Britton* [1968] 1 WLR 157.

105 *Curro v Beyond Productions Pty Ltd* (1993) 30 NSWLR 337, 348.

106 *Page One Records Ltd v Britton* [1968] 1 WLR 157, 166–7.

107 *Buckenara v Hawthorn Football Club Ltd* [1988] VR 39.

108 For another attempt to balance the interests of the parties, see *Tradition Australia Pty Ltd v Gunson* [2006] NSWSC 298.

109 *Supreme Court Act 1933* (ACT), ss 26, 27, 34; *Supreme Court Act 1970* (NSW), ss 58, 68; *Civil Proceedings Act 2011* (Qld), s 8; *Supreme Court Act* (NT), ss 14(1)(b), 62, 63 (see also *Brooks v Wyatt* (1994) 99 NTR 12, 27–8); *Supreme Court Act 1935* (SA), ss 21, 30; *Supreme Court Civil Procedure Act 1932* (Tas), s 11(13); *Supreme Court Act 1986* (Vic), s 38; *Supreme Court Act 1935* (WA), s 25(10).

110 *Chancery Amendment Act 1858* (Imp) 21 & 22 Vict c 27.

Act was passed before the Judicature Acts, when equity was administered separately from the common law, in the Court of Chancery. The Court of Chancery gave monetary awards, known as *equitable compensation*, only in very limited circumstances and certainly not in aid of legal rights under contracts. Accordingly, when a plaintiff sought specific performance or an injunction in respect of a valid contract, but the Court of Chancery refused the remedy on discretionary grounds, the plaintiff had to institute proceedings in the common law courts to obtain damages. By giving the Court of Chancery the power to award damages in these circumstances, *Lord Cairns' Act* allowed the matter to be resolved in the Court of Chancery and saved the plaintiff from having to continue the litigation in the common law courts.

The provisions are still regularly used today to award damages in three situations: first, where specific performance or an injunction is refused on discretionary grounds; secondly, where it is more convenient to award damages rather than specific relief; and thirdly, where it is necessary to award damages in addition to specific performance in order to compensate the plaintiff for some loss suffered as a result of the defendant's breach. The provisions are of the utmost importance in situations in which no damages are recoverable at law, such as where a contract fails to comply with a statutory requirement of writing,[111] and specific performance must be refused on discretionary grounds. In such a situation, the only remedy available to the plaintiff is damages under *Lord Cairns' Act*.

Most of the *Lord Cairns' Act* legislation gives a court power to award equitable damages only where the court has "jurisdiction" to grant specific performance or an injunction. This means that the essential requirements for obtaining a decree of specific performance or an injunction outlined above must be established, including the requirement that damages at common law will not provide an adequate remedy. The fact that the court would have refused specific performance or an injunction on discretionary grounds will not deprive the court of the power to award equitable damages. The power to award equitable damages can be exercised "where a plaintiff has made out a case for equitable relief by way of injunction or specific performance, and has either got it, or for some equitable or discretionary reason, been refused it".[112] The court exercises a discretion in awarding equitable damages and the exercise of that discretion involves slightly different considerations from those governing the granting of specific performance and injunctions. Some discretionary grounds for refusing specific relief will also result in a refusal of equitable damages, such as where the plaintiff has not been ready, willing and able to perform his or her obligations.[113] Other discretionary defences to specific relief, such as hardship[114] or delay,[115] will not operate as a bar to the award of equitable damages.

Equitable damages awarded in aid of common law rights are generally assessed in the same way as common law damages.[116] When awarded in lieu of specific performance, equitable damages are to be assessed according to the same compensatory principle as common law damages, "ie, that the innocent party is to be placed, so far as money can do, in the same

111 See [7.65].

112 *Madden v Kevereski* [1983] 1 NSWLR 305, 307.

113 *King v Poggioli* (1923) 32 CLR 222.

114 *Norton v Angus* (1926) 38 CLR 523.

115 *Shaw v Applegate* [1977] 1 WLR 970.

116 *Wenham v Ella* (1972) 127 CLR 454, 460.

position as if the contract had been performed".[117] The court clearly has some discretion in determining the appropriate method of assessment. The legislation in most jurisdictions provides that damages "may be assessed in such manner as the court shall direct". Despite such language, it has been held in England that damages awarded in substitution for specific performance must constitute a true substitute for specific performance.[118]

117 *Johnson v Agnew* [1980] AC 367, 400.

118 *Wroth v Tyler* [1974] Ch 30; *Johnson v Agnew* [1980] AC 367.

VITIATING FACTORS: MISINFORMATION

PART XIA

[PtXIA.05] A party to a contract may seek relief on the basis that he or she entered the contract under the influence of *mistake*; that is, under an erroneous belief. This mistake may be *self-induced* or *induced by the other party* to the contract.

If the mistake is self-induced, generally no relief is available unless the contract itself, expressly or by implication, provides otherwise. The common law in particular holds out little hope to the victim of a self-induced mistake. Equity, on the other hand, is somewhat more accommodating, especially if the enforcement of common law rights would be unconscionable in the circumstances. The topic of self-induced mistake as a basis for relief is considered in Chapter 31.

If a party's error is induced by the other party to the contract, one avenue for relief is *misrepresentation*. In essence, a misrepresentation is a false statement of fact made expressly or impliedly by one party (the *representor*) to another (the *representee*), whereby the latter is misled and induced to enter into a contract with the former. We consider the elements of misrepresentation under the general law (common law and equity) in Chapter 32.

There are also important statutory provisions dealing with misrepresentation. These provisions, which prohibit "misleading or deceptive conduct in trade or commerce" are found in the *Australian Consumer Law*.[1] We consider the elements of these provisions and the remedies available if they are breached in Chapter 33.

The remedies available at general law for victims of misinformation are covered in Chapter 32 and Part C (Chapter 39). Under the general law, the possible remedies are rescission and damages. Rescission involves setting the contract aside and returning the parties to the position they were in before the contract was made. Equivalent remedies, and a variety of additional remedies, are available under the legislation that prohibits misleading or deceptive conduct (see Chapter 33).

A pre-contractual representation of fact that proves to be false may give rise to a number of possible consequences, some of which we have examined in earlier chapters, and others of which we examine in this part (Part X). So as not to lose sight of the general picture, here is a list of the possible legal consequences of a pre-contractual representation of fact:

1 See further [2.75].

1. There may be no legal consequences (if the statement is a mere *puff*).[2]
2. The representee may be entitled to recover damages for breach of contract (if the representor can be said to have made a *contractual promise* that the fact is true).[3]
3. The representor may be entitled to rescind the contract (if the representation was made by the other party to the contract and the representee entered into the contract in reliance on the representation).[4]
4. The representee may be entitled to recover damages in tort (if, in making the statement, the representor committed the tort of *negligence* or the tort of *deceit*).[5]
5. The representee may be entitled to damages, rescission and other remedies under the *Australian Consumer Law* (if the statement constituted *misleading or deceptive conduct in trade or commerce*).[6]
6. In exceptional circumstances an estoppel may arise. Estoppel will only be relevant where, after the contract is made, the representor seeks to assert rights that are inconsistent with the representation. It is only where the representor behaves inconsistently that estoppel will play a role and, in the misrepresentation context, this very rarely happens. The representee's loss almost always arises as a result of the representation proving untrue, rather than as a result of inconsistent conduct on the part of the representor.[7]

2 See [32.15] and [33.50].
3 See Chapters 12, 18 and 26.
4 See Chapters 32 and 39.
5 See Chapter 32.
6 See Chapter 33.
7 See further at [9.230].

CHAPTER **31**

Mistake

OVERVIEW

Types of mistake

[31.05] After a contract has been formed, one of the parties may discover that he or she entered the contract under the influence of a mistake. Often, indeed usually, such mistakes are induced by the *misrepresentation* or *misleading conduct* of the other party. The law relating to such deceptive conduct is considered in Chapters 32 and 33. In this chapter, we are not concerned with mistakes induced by another party, but rather with mistakes which may be described as self-induced or spontaneous.

The law distinguishes between different categories of mistake based first on who is mistaken and secondly on the kind of mistake that has been made. The first distinction is between *common mistake* (where both parties are mistaken), *mutual mistake* (where the parties are at cross purposes) and *unilateral mistake* (where only one party is mistaken).[1]

The second distinction is between mistakes relating to the *terms* of the contract, mistakes relating to the *identity* of the other contracting party (which are obviously always unilateral) and mistakes relating to the existence or a quality of the *subject matter* of the contract. A mistake as to terms might arise, for example, where as a result of clerical error the weekly

1 Note that *common mistake* (ie, where a mistake is shared by the parties) is also sometimes referred to as *mutual mistake*; see, eg, *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377, 408 and *Bell v Lever Bros Ltd* [1932] AC 161, 224.

rental in a written lease is specified as $100 instead of $1000 as the parties had previously agreed. The mistake would be a common mistake if neither party noticed the error, and a unilateral mistake if the tenant noticed the error but remained silent about it. A mistake as to the existence of the subject matter occurs if parties contract for the sale of a painting without knowing that it was destroyed by fire overnight. A mistake as to a quality of the subject matter occurs if the parties contract for the sale of an item which is believed to be an antique but is in fact an imitation.

A mistake can have the effect that a contract is *void* (ie, no valid contract was ever formed), *voidable* (ie, a contract was formed but is liable to be set aside or rescinded at the option of one of the parties) or able to be *rectified* (ie, a court of equity can correct an error in a contractual document).

How does the law respond to mistakes?

[31.10] Three different approaches to mistakes are evident in the case law: constructionist, civilian and unconscionability. The first two approaches involve the application of common law principles, while the unconscionability approach involves the application of equitable principles.

Common law

[31.11] Under a constructionist approach, mistakes made by the contracting parties are solved by applying the rules of contract law relating to contract formation and the construction of contract terms.[2] Familiar rules relating to offer and acceptance, certainty and express and implied terms are employed to determine who bears the risk of the mistake. The application of these rules may result in a finding that no contract was formed, or a finding that a contract was formed but the parties are released from the contract because of a failure of a contingent condition. Although such findings would result in mistaken parties facing no contractual liability, this is not because the law has particular rules dealing with problems arising from mistakes. Rather, the finding flows from the application of ordinary contractual principles.

Under the constructionist approach, mistakes as to the *identity* of the other contracting party are resolved by construing the relevant offer and acceptance. Mistakes about the existence of the *subject matter* are resolved by construing the contract to determine whether the promise to supply was unqualified or conditional. For example, it may be held that the seller promised that the subject matter existed (with the result that there is a contract and the seller is liable), that the purchaser took the risk that the subject matter existed (in which case there is a contract and the purchaser is liable) or that there was an implied condition precedent that the subject matter existed (in which case there is no contract, because the instrument did not exist). If it cannot be objectively determined what the parties agreed to, then the issue is one of certainty. In *McRae v Commonwealth Disposals Commission*,[3] discussed at [31.35], the High Court preferred to resolve a common mistake problem on a constructionist basis. *Hartog v Colin & Shields*,[4] discussed at [31.85], provides an example of a unilateral mistake case resolved on the basis of ordinary formation principles.

2 See, eg, *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377, [31.80].
3 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377.
4 *Hartog v Colin & Shields* [1939] 3 All ER 566.

The civilian approach, deriving from Roman law, presents a distinct doctrine of mistake which is influenced by the notion of *consensus*. On this view, a fundamental error destroys the consent and consensus ad idem which are essential to contract and that justifies a finding that the contract is rendered void by the mistake.[5] In order to determine whether a mistake is fundamental, it is necessary to identify the substance of the contract and to determine whether the mistake relates to that substance or merely to some collateral matter, such as a quality or attribute of the subject matter. *Bell v Lever Brothers Ltd*,[6] discussed at [31.50], is the leading example of the influence of civilian theory on the common law principles that apply to common mistake. As we will see, the principle recognized in that case has a limited scope of application.

Equity

[31.12] If a constructionist approach leads to the conclusion that a mistaken party is bound notwithstanding his or her mistake, and the limited circumstances in which the common law holds contracts void for mistake do not apply, the contract may nevertheless be voidable or able to be rectified in equity. Equity's jurisdiction to set aside and rectify contracts on the basis of mistake allows it to fulfil its broader role of ensuring that the enforcement of common law rights is not unconscionable.[7]

Remedies and consequences

Contracts void

[31.15] A conclusion that a contract is void may cause great inconvenience to the parties if performance of the contract has already commenced or has already been completed. More importantly, the interests of *third parties* may be adversely affected. For example, if A, under the influence of an operative mistake, sells goods to B, and B sells the goods to C, no title to the goods will pass to C if the contract is held to be void at common law for mistake. This is because no title passes under the contract to B, so B has no title to pass on to C. The applicable principle is *nemo dat quod non habet* (one cannot give what one does not have). In this example, we assume that B has not paid A and has vanished with the money received from C. The inconvenient result is that C has lost money and does not own the goods. In fact, C is liable to A in conversion (a tort) for having exercised dominion over A's goods – however unwittingly. The drastic consequences of finding a contract void ab initio, and the inconveniences that follow, provide another explanation for the narrow scope of the circumstances in which a contract will be void ab initio for common mistake at common law, which will be considered at [31.50].

Contracts voidable

[31.17] In certain circumstances, contracts that are valid at common law are able to be rescinded in equity on the basis of mistake. A contract that is liable to be rescinded is said to be voidable. Rescission may be granted on terms which aim at achieving fairness between the parties, and thus the equitable response to mistake is more flexible than the "all-or-nothing"

5 See, eg, *Solle v Butcher* [1950] 1 KB 671, discussed at [31.100].
6 *Bell v Lever Brothers Ltd* [1932] AC 161.
7 See MacMillan, *Mistakes in Contract Law* (Hart, 2010), Ch 3.

approach of the common law. Moreover, title can pass under a voidable contract because such a contract is valid and effective until it is "avoided" (rescinded). So, in the example we just considered involving A, B and C, title will pass to C provided A has not already rescinded the contract between A and B. After C obtains title, the contract between A and B cannot be rescinded. Rescission is not usually available in equity if the parties cannot be restored substantially to the positions they were in before the contract was made or if third party rights (such as C's) have intervened.[8] In such a case, equity, like the common law, also takes an "all-or-nothing" approach, except this time it is A who loses all. Rescission is not the only form of relief available in equity. A court of equity can refuse to grant specific performance on the ground of mistake or grant specific performance on terms.[9] We will explore, at [31.55] and [31.95], the circumstances in which a court of equity will grant rescission for common mistakes and unilateral mistakes respectively.

Rectification

[31.20] A party that entered a contract under the influence of mistake may not wish to be released from the contract. Instead, he or she may prefer that the contract is corrected or *rectified*. The remedy of rectification is available in equity in respect of agreements which have been mistakenly recorded. Rescission and rectification are entirely different remedies. In the case of the former, the court sets aside the contract and restores the parties to their original positions. In the latter case, the court corrects the contract to reflect the parties' actual agreement. The fact that a rectification order keeps a contract on foot might justify the application of a less demanding test in cases of rectification vis-à-vis rescission. We will return to this issue later.

COMMON MISTAKE

[31.25] In this section, we are concerned with the situation in which the parties have reached agreement, but they make the same false assumption in respect of some matter. There are two ways of dealing with common mistake at common law. The first involves *construing* the contract, in accordance with ordinary principles of contractual interpretation, to determine where the risk of the mistake lies. The second involves a principle of law which recognises that the contract may be *void* for common mistake in certain circumstances. Although the High Court expressed a preference for the former in *McRae v Commonwealth Disposals Commission*,[10] it did not rule out the possibility that the Australian common law includes a doctrine that renders contracts void on the basis of common mistake. If such a doctrine is part of Australian law, it will have an extremely limited application.

Whether a contract that is valid at common law may be rescinded in equity on the basis of common mistake is now a controversial question, as will be discussed at [31.55]–[31.60]. Where contracting parties enter into a contract under a common mistake as to terms, it is clear that rectification can be granted if certain requirements are met, as will be discussed at [31.65].

It is also possible that the effect of the mistake will be governed by legislation. For example, *Sale of Goods* legislation includes a provision that states: "[W]here there is a contract for the

8 For a detailed discussion of rescission, see Chapter 39.
9 See Chapter 30.
10 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377.

sale of specific goods, and the goods without the knowledge of the seller have perished at the time when the contract is made the contract is void."[11] Where parties contract for the sale of goods on the mistaken basis that the goods are in existence, the contract is void because of the statutory provision rather than any common law rule.

Construing the contract

[31.30] The application of the constructionist approach to a mistake problem may result in one of three findings. First, where parties are at cross purposes, the court may conclude that it is not possible to determine, based on ordinary principles of interpretation,[12] which party is correct and which party is mistaken. If a misunderstanding of this kind relates to an essential term, no contract will have been formed because of a lack of certainty.[13] Secondly, the party or parties will be relieved from a contract if the contract is found to be subject to an implied condition that the facts are as the mistaken party or parties understood them to be at the time of formation. To quote Lord Atkin in *Bell v Lever Brothers Ltd*, "[o]ne term may be that unless the facts are or are not of a particular nature, or unless an event has or has not happened, the contract is not to take effect".[14] Thirdly, the court might decide that the parties' promises are unconditional and therefore binding irrespective of the mistake.[15] It should be noted, however, that where the mistake results in absurdity or inconsistency, the issue may be resolved at common law by a process of construction. The mistake itself, and the nature of the correction required to overcome absurdity or inconsistency, must be obvious.[16]

The promise is unconditional

[31.35] In *McRae v Commonwealth Disposals Commission*,[17] the leading authority on the constructionist approach to mistake, the court found that the contractual promises were unconditional despite the common mistake. As a result, the promises were binding despite the fact that the parties contracted on a mistaken basis. The defendant Commission invited tenders for the purchase of an oil tanker described as being wrecked at a certain location in Papua. The Commission accepted a tender submitted by the plaintiffs, who intended to salvage the tanker. The plaintiffs incurred expenses in mounting a salvage operation, only to discover that there was no tanker anywhere in the vicinity of the alleged location. The Commission had sold the tanker to the plaintiffs on the basis of a rumour, having made just a few inquiries. The trial judge, Webb J, held that, since there was no tanker to sell, the contract for the sale of the tanker was void and there could be no claim for damages for breach of contract. Webb J considered that the well-known case of *Couturier v Hastie*[18] compelled him to reach this conclusion. In *Couturier v Hastie*, A contracted to sell corn to B. Unbeknown to

11 *Sale of Goods Act 1954* (ACT), s 11; *Sale of Goods Act 1923* (NSW), s 11; *Sale of Goods Act* (NT), s 10; *Sale of Goods Act 1896* (Qld), s 9; *Sale of Goods Act 1895* (SA), s 6; *Sale of Goods Act 1896* (Tas), s 11; *Goods Act 1958* (Vic), s 11; *Sale of Goods Act 1895* (WA), s 6.

12 See Chapter 13.

13 See Chapter 6, especially [6.15] in relation to essential terms. The leading example of this is the well-known case *Raffles v Wichelhaus* (1864) 2 H&C 906; 159 ER 375, discussed at [31.75].

14 *Bell v Lever Brothers Ltd* [1932] AC 161, 225.

15 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377.

16 *Noon v Bondi Beach Astra Retirement Village Pty Ltd* [2010] NSWCA 202, [179]–[191].

17 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377.

18 *Couturier v Hastie* (1856) 5 HL Cas 673.

the parties, before the contract was formed, the ship transporting it had encountered heavy weather and the corn had became heated and fermented. The cargo was found to be unfit to be carried further and was sold at a local port. An action brought by the seller of the corn was unsuccessful. Webb J took *Couturier v Hastie* to set up a rule that non-existence of the subject matter at the time of formation renders a contract void.

Webb J's decision was appealed to the High Court. The High Court held that there was a contract and the defendant was in breach of it.[19] The defendant was held to have impliedly promised that there was a tanker in the position specified and was liable for breach of that promise. The High Court dealt with *Couturier v Hastie* by noting that, although the case has been explained in contract text books on the basis of mistake, it was in fact decided on the basis of construction. The question was not whether the contract was void but whether the buyer had agreed to buy particular goods in existence or to pay for "goods lost or not lost". Because the buyer had agreed to pay on presentation of the shipping documents, the seller argued that the buyer had taken the risk that the goods might have been lost during the voyage. The High Court held in *McRae* that the correct understanding of *Couturier v Hastie* was that the buyer not liable because, as a matter of construction, the buyer was liable to pay only if the goods were in existence and capable of delivery at the time the contract was made.[20] The question whether the contract was void did not arise.[21]

Implied condition

[31.40] The High Court accepted in *McRae v Commonwealth Disposals Commission* that in a case where the subject matter of the contract did not exist it was necessary to ask whether the contract was subject to an implied condition that the subject matter existed. If the contract was subject to such a condition, the parties would be released from the obligation to perform. On the facts of *McRae*, it was impossible to imply such a term.[22] The terms of the contract and the surrounding circumstances, the court said:

> clearly exclude any such implication. The buyers relied upon, and acted upon, the assertion of the seller that there was a tanker in existence. It is not a case in which the parties can be seen to have proceeded on the basis of a common assumption of fact so as to justify the conclusion that the correctness of the assumption was intended by both parties to be a condition precedent to the creation of contractual obligations.[23]

On different facts, a mistake relating to the existence of the subject matter could be resolved by implying a condition precedent that the subject matter continues to exist at the time the contract is made.[24] This would be likely, for example, where the parties are equally well-placed to know whether the subject matter exists. If the seller is the one with the means of knowledge, which will usually be the case, then he or she is likely to be taken as promising that the subject matter exists. In *McRae v Commonwealth Disposals Commission*, Dixon and Fullagar JJ (with whom McTiernan J agreed) noted that "[p]rima facie, one would think, there would be no such implied condition precedent, the position being simply that the vendor promised that

19 On the question of assessment of damages, see [26.60].

20 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377, 405.

21 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377, 406–7, 409.

22 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377, 409.

23 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377, 409.

24 See *Goldsbrough Mort & Co Ltd v Carter* (1914) 19 CLR 429, 437.

the goods *were* in existence".[25] *Couturier v Hastie*, discussed above, provides an example of a case resolved on the basis of an implied condition precedent.

Relief based on interpretation

[31.45] Where a mistake results in absurdity or inconsistency, the issue may be resolved at common law by a process of construction. Both the mistake itself and the nature of the correction required to overcome absurdity or inconsistency must be obvious.[26] In *Fitzgerald v Masters*,[27] clause 8 of a contract of sale provided that "[t]he usual conditions of sale in use or approved of by the Real Estate Institute of New South Wales … shall so far as they are inconsistent herewith be deemed to be embodied herein". It was clear that an error had been made. Why would the parties wish to incorporate terms inconsistent with those upon which they had expressly agreed? Dixon CJ and Fullagar J stated that "[w]ords may generally be supplied, omitted or corrected, in an instrument, where it is clearly necessary to avoid absurdity or inconsistency".[28] As a matter of construction, the court read the word "inconsistent" as "consistent". McTiernan J, Webb J and Taylor J noted that "the rejection of repugnant words, the transposition of words and the supplying of omitted words"[29] are all justified by "the rule that the intention of the parties is to be ascertained from the instrument as a whole and that this intention when ascertained will govern its construction".[30]

The relief granted in *Fitzgerald v Masters* looks similar to rectification, a concept we will come to. Rectification, however, involves the correction of an instrument to reflect the parties' actual intentions, whereas the decision in *Fitzgerald v Masters* was reached by determining the intention objectively manifested by the contract itself.

Contracts void for mistake at common law

[31.50] As noted earlier, civilian theory, influenced by the notion of consensus, suggests that in certain circumstances, the common law of contract should hold that a contract is void because of common mistake. While such a doctrine (admittedly one with a limited scope of operation) is well-established in the English common law, there is uncertainty as to whether it forms part of the Australian common law.

In *Bell v Lever Brothers Ltd*,[31] the House of Lords recognised that, in limited circumstances, a contract may be void at common law for common mistake. Bell was appointed chairman of a company controlled by Lever Brothers for a term of five years. After two years, the company wanted to terminate Bell's services. They entered into a contract with him under which he was paid £30,000 as compensation for the termination of his services. It was then discovered that Bell had committed breaches of duty when he was chairman that would have justified his dismissal without any compensation. The court accepted that Bell had forgotten about these breaches of duty at the time of the compensation agreement. Lever Brothers sought to recover the £30,000 on the basis that the compensation agreement was void for fundamental mistake.

25 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377, 407.

26 *Noon v Bondi Beach Astra Retirement Village Pty Ltd* [2010] NSWCA 202, [179]–[191].

27 *Fitzgerald v Masters* (1956) 95 CLR 420, discussed in the context of construction at [13.72].

28 *Fitzgerald v Masters* (1956) 95 CLR 420, 426–7.

29 *Fitzgerald v Masters* (1956) 95 CLR 420, 437.

30 *Fitzgerald v Masters* (1956) 95 CLR 420, 437.

31 *Bell v Lever Brothers Ltd* [1932] AC 161.

The mistake related to a quality of the subject matter – the contract of service – in that the parties thought that that contract was not terminable at will, whereas in fact it was terminable at will by Lever Brothers.

The House of Lords held, by a majority, that the compensation agreement was not void for mistake, as it related to a quality of the subject matter that was not fundamental. Lord Atkin said that the common mistake must be "as to the existence of some quality which makes the thing without the quality *essentially different* from the thing as it was believed to be".[32] Applying this test to the facts at hand, Lord Atkin asked the question: "Is an agreement to terminate a broken contract different in kind from an agreement to terminate an unbroken contract, assuming that the breach has given the one party the right to declare the contract at an end?"[33] He gave a negative answer to this question, explaining:

> [T]he contract released is the identical contract in both cases, and the party paying for the release gets exactly what he bargains for. It seems immaterial that he could have got the same result another way, or that if he had known the true facts he would not have entered the bargain.[34]

Lord Atkin mentioned some basic examples that made clear the limits of the principle.[35] Where A buys a horse from B which both wrongly believe to be sound, A cannot recover the price. A buyer who pays a high price for a painting which buyer and seller believe is an old master, but is in fact a modern copy, also has no remedy unless the seller made a representation or gave a contractual warranty. The situation is no different if A contracts to buy a service station beside a highway when construction is about to begin on a bypass which will divert all of the traffic away from the business.

Lord Atkin did consider the potential application of the constructionist approach, which he described as "the alternative mode of expressing the result of a mutual mistake."[36] The relevant question was whether the compensation agreement was subject to an implied condition that the contract of service could not be terminated until the end of the five-year term. Applying the business efficacy test for the implication of terms,[37] Lord Atkin said that "a condition would not be implied unless the new state of facts makes the contract (of service) something different in kind from the contract in the original state of facts."[38] In other words, whether the court applied a civilian or a constructionist approach to the mistake issue, the result was the same.

The minority in *Bell v Lever Brothers Ltd* considered that the mistake the contracting parties made was one which, having regard to the fact that they were negotiating about compensation to be paid for the premature termination of the service agreement, "was as fundamental to the bargain as any error one can imagine".[39] In fact, the conclusion could be drawn from the majority's reasoning that a mistake as to quality will almost never be regarded as sufficient to render a contract void at common law. There have, however, been cases in

32 *Bell v Lever Brothers Ltd* [1932] AC 161, 218 (emphasis added).
33 *Bell v Lever Brothers Ltd* [1932] AC 161, 223.
34 *Bell v Lever Brothers Ltd* [1932] AC 161, 223–4.
35 *Bell v Lever Brothers Ltd* [1932] AC 161, 224.
36 *Bell v Lever Brothers Ltd* [1932] AC 161, 224.
37 See [14.15]–[14.45].
38 *Bell v Lever Brothers Ltd* [1932] AC 161, 226.
39 *Bell v Lever Brothers Ltd* [1932] AC 161, 208.

which, on the application of the principle, mistakes as to quality have been found to render contracts void at common law.[40]

In *Solle v Butcher*, a case concerned with the equitable jurisdiction to set aside contracts on the basis of common mistake considered at [31.55], Denning LJ concluded that the common law did not provide relief for common mistake. His Lordship said of *Bell v Lever Bros*:

> The correct interpretation of that case, to my mind, is that, once a contract has been made, that is to say, once the parties, whatever their inmost states of mind, have to all outward appearances agreed with sufficient certainty in the same terms on the same subject matter, then the contract is good unless and until it is set aside for failure of some condition on which the existence of the contract depends, or for fraud, or on some equitable ground. Neither party can rely on his own mistake to say it was a nullity from the beginning, no matter that it was a mistake which to his mind was fundamental, and no matter that the other party knew that he was under a mistake. A fortiori, if the other party did not know of the mistake, but shared it. The cases where goods have perished at the time of sale, or belong to the buyer, are really contracts which are not void for mistake but are void by reason of an implied condition precedent, because the contract proceeded on the basic assumption that it was possible of performance.[41]

In *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd (The Great Peace)*,[42] however, the English Court of Appeal rejected Denning LJ's interpretation of *Bell v Lever Bros* and confirmed the existence of a common law jurisdiction as found in *Bell v Lever Bros*. The court in *The Great Peace* considered the principle identified in *Bell v Lever* Brothers – by which contracts are rendered void for common mistake – to be analogous to the doctrine of frustration. In each case, it is recognised that no obligation arises if the parties have agreed to do something that is impossible to perform.[43] On the basis of the frustration analogy, the Court suggested that:

> the following elements must be present if common mistake is to avoid a contract: (i) there must be a common assumption as to the existence of a state of affairs; (ii) there must be no warranty by either party that that state of affairs exists; (iii) the nonexistence of the state of affairs must not be attributable to the fault of either party; (iv) the non-existence of the state of affairs must render performance of the contract impossible; (v) the state of affairs may be the existence, or a vital attribute, of the consideration to be provided or circumstances which must subsist if performance of the contractual adventure is to be possible.[44]

Whether Australian law includes a principle of the kind recognised in *Bell v Lever Bros* and the *Great Peace* remains unresolved. In *McRae v Commonwealth Disposals Commission*,[45] the High Court displayed a preference for resolving issues of mistake on a constructionist basis by focusing on an interpretation of what the promisor can really be understood to have promised.[46] The court did not, however, expressly rule out the possibility that the Australian

40 See, eg, *Associated Japanese Bank (International) Ltd v Credit du Nord SA* [1989] 1 WLR 255 and *HWG Holdings Pty Ltd v Fairlie Court Pty Ltd* [2015] VSC 519, discussed below.

41 *Solle v Butcher* [1950] 1 KB 671, 691.

42 *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* [2003] EWCA Civ 1407; [2003] QB 679.

43 *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* [2003] EWCA Civ 1407; [2003] QB 679, [73].

44 The second and third elements were said (*Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* [2003] EWCA Civ 1407; [2003] QB 679, [77]) to be "exemplified by the decision of the High Court of Australia in *McRae v Commonwealth Disposals Commission* (1951) 84 CLR 377".

45 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377.

46 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377, 407.

common law includes a principle rendering contracts void for common mistake. The High Court's response to Lord Denning's suggestion that the common law provides no relief against mistake was qualified. Dixon and Fullagar JJ noted that, although they were "not prepared to assent to everything that is said by Denning LJ",[47] they agreed with his Lordship's suggestion that "the theorisings of the civilians about 'mistake'"[48] are not relevant to determining whether the contract is void at common law because of the mistake. While this comment could be interpreted to mean that the common law resolves mistake solely on a constructionist basis, their Honours went on to say that Lord Denning's view that no mistake, no matter how serious or fundamental, can render a contract void may not be "wholly or strictly correct".[49] Dixon and Fullagar JJ said in *McRae v Commonwealth Disposals Commission* that, if such a doctrine exists at common law, it will not apply "where the mistake consists of a belief which is, on the one hand, entertained by him without any reasonable grounds, and, on the other hand, deliberately induced by him in the mind of the other party".[50] To put it another way, we cannot read too much into the fact that the High Court did not find the contract under consideration void for mistake. After all, the case was brought against a careless seller who was unable to deliver what it had promised. Further, the appellant was only mistaken because of information provided to it by the respondent. This was hardly a compelling case in which to provide relief against mistake.

In *HWG Holdings Pty Ltd v Fairlie Court Pty Ltd*,[51] Sifris J understood the principle identified in *Bell v Lever Brothers* to form part of Australian law and found a contract to be void at common law for common mistake. Sifris J held that a share buy-back agreement was void because the parties had made a "very serious mistake" about the tax consequences which constituted the entire purpose of the agreement.[52] His Honour said that "performance of the buy-back agreement as specifically contemplated and intended by the parties is impossible" because "the subject matter of the contract is essentially and radically different from the subject matter of the contract which the parties believed to exist."[53] The case is analogous to the frustration case of *Krell v Henry*:[54] the parties could perform their obligations, but the foundation and purpose of the contract as mutually understood did not exist. Sifris J observed that:

> Courts do not lightly declare or find contracts to be void ab initio for common mistake. However, it is ultimately a matter of construction of the particular contract made by the parties, particularly in relation to which party is to bear the risk. In the unusual case where the contract is silent, gap filing mechanisms are not available, there is no misrepresentation or misleading conduct, and the breach is serious, the result in a particular case may well be the stated narrow common law position, namely that the contract is void ab initio. This is such a case.[55]

47 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377, 407.
48 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377, 407.
49 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377, 408.
50 *McRae v Commonwealth Disposals Commission* (1950) 84 CLR 377, 408.
51 *HWG Holdings Pty Ltd v Fairlie Court Pty Ltd* [2015] VSC 519.
52 *HWG Holdings Pty Ltd v Fairlie Court Pty Ltd* [2015] VSC 519, [57].
53 *HWG Holdings Pty Ltd v Fairlie Court Pty Ltd* [2015] VSC 519, [57].
54 *Krell v Henry* [1903] 2 KB 740, discussed at [15.40].
55 *HWG Holdings Pty Ltd v Fairlie Court Pty Ltd* [2015] VSC 519, [56] (footnote omitted).

Rescission in equity

[31.55] Whether a contract which is not subject to an implied condition or void at common law for common mistake may nonetheless be voidable in equity is an issue on which Australian courts are divided. The leading case on this point is (or was) *Solle v Butcher*,[56] a decision of the English Court of Appeal. Although *Solle v Butcher* has been cited with approval by the High Court of Australia,[57] the English Court of Appeal recently held the case to have been wrongly decided.[58] Views differ as to whether there remain circumstances in which a contract will be rescinded in equity for common mistake in Australian law.

In *Solle v Butcher*, a flat which had undergone alterations was let by the lessor to the lessee for seven years at a fixed and fair rent of £250 pa. Both parties mistakenly thought that, because of the alterations to the flat, it was not governed by the rent-control legislation. The controlled rent was only £140 pa. If the lessor had known that the flat was subject to the legislation, he could, before granting the lease, have simply given appropriate notice in order to have the rent increased to £250; but this could not be done after the lease was executed. The lessee, after being in possession for two years, sued the lessor claiming restitution of amounts overpaid and claiming a declaration that he could remain on as tenant at the lower rent. The lessor for his part claimed that the lease should be set aside on the ground of mistake. He argued that it was unfair that for the next five years he should receive a rent of only £140 pa. The English Court of Appeal held, by a majority, that the lease was voidable on terms laid down by the Court.

First, relying on the interpretation of *Bell v Lever Bros Ltd*[59] quoted above, Denning LJ found that the contract was not void ab initio at common law, even though he considered the mistake to be fundamental. In reaching this conclusion, Denning LJ appears to have been influenced by concerns that, if the contract were a nullity, the tenant would have no right to remain in the premises, and tenants generally would be fearful of seeking to have their rent reduced to the permitted amounts under the legislation.[60]

Second, Denning LJ held that a contract could be set aside in equity:

> if the parties were under a common misapprehension either as to facts or as to their relative and respective rights, provided that the misapprehension was fundamental and that the party seeking to set it aside was not himself at fault.[61]

Here, the Court of Appeal considered the misapprehension to be fundamental, in the sense that it related to a matter of great importance. Further, the tenant as a surveyor employed by the defendant landlord had himself advised the defendant on the rents payable. Now he "quite unashamedly" wanted to take advantage of the mistake to which he had contributed in order to avoid paying a fair rent.

The Court ordered that the lease should be set aside, on terms that the landlord should complete the notice required to take the rent outside legislative control, and then the tenant,

56 *Solle v Butcher* [1950] 1 KB 671.

57 *Taylor v Johnson* (1983) 151 CLR 422, 431.

58 *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* [2003] EWCA Civ 1407; [2003] QB 679.

59 *Bell v Lever Brothers Ltd* [1932] AC 161.

60 *Solle v Butcher* [1950] 1 KB 671, 692.

61 *Solle v Butcher* [1950] 1 KB 671, 693.

who in the meantime could stay on as a licensee, should be offered a new lease for the balance of the original term at a rental of £250 pa.[62]

In *Svanosio v McNamara*, Dixon CJ and Fullagar J observed that "it is difficult to conceive any circumstance in which equity could properly give relief by setting aside the contract unless there has been fraud or misrepresentation or a condition can be found expressed or implied in the contract."[63] In the later decision of the High Court in *Taylor v Johnson*, Mason ACJ, Murphy and Deane JJ agreed with that statement on the assumption that Dixon CJ and Fullagar J "were referring to 'fraud' in the wide equitable sense which includes unconscionable dealing".[64] Mason ACJ, Murphy and Deane JJ noted in *Taylor v Johnson* that "the reported cases, including *Solle v Butcher* itself, readily provide concrete examples" of circumstances in which equity would intervene to prevent unconscionable conduct in the mistake context.[65] Thus, the majority of the High Court in *Taylor v Johnson* appears to have approved the decision in *Solle v Butcher*, justifying it as an instance in which the Court intervenes to prevent unconscionable conduct.[66]

The Great Peace

[31.60] As already noted, *Solle v Butcher* is no longer regarded as good law in England. In *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* (*The Great Peace*),[67] a bulk carrier called the Cape Providence suffered serious structural damage during a voyage in the Southern Indian Ocean. The nearest tug was five to six days away in Singapore. The defendants were told by a third party (a weather forecasting service) that the claimants' ship (the Great Peace) was 35 miles away from the Cape Providence. The defendants contracted with the claimants to charter the Great Peace to stand by the Cape Providence until the tug arrived in case it became necessary to rescue the crew. The fee was $16,500 per day, with a minimum of "5 days due and earned upon Great Peace altering direction, being $82,500". The Great Peace changed course to rendezvous with the Cape Providence, but the defendants very soon became aware that the ships were actually 410 miles apart. The defendants did not cancel the arrangement immediately, but did so within a few hours, once they had located and made arrangements with a closer ship. The defendants resisted the claim for payment under the contract on the basis of a common mistake. The English Court of Appeal held that, contrary to Lord Denning's view in *Solle v Butcher*, the common law will grant relief against common mistake, provided the test in *Bell v Lever Bros Ltd* is made out.

The Court of Appeal held that the defendants would have had an arguable case that the contract was void (at common law) for common mistake if the distance between the two vessels had been "so great … as to render the contractual adventure impossible of performance".[68] The Court of Appeal noted that such circumstances "would have given them an arguable

62 See further *Magee v Pennine Insurance Co Ltd* [1969] 2 WLR 1278.

63 *Svanosio v McNamara* (1956) 96 CLR 186, 196.

64 *Taylor v Johnson* (1983) 151 CLR 422, 431. The fourth member of the court, Dawson J, dissented.

65 *Taylor v Johnson* (1983) 151 CLR 422, 431. As *Taylor v Johnson* was a unilateral mistake case, it remains unresolved whether the High Court's approach in that case is applicable to cases of common mistake: see Seddon, "Contract: Mistake Mistake" (2006) 80 *Australian Law Journal* 95.

66 The *Solle v Butcher* principle was applied in *Classic International Pty Ltd v Lagos* [2002] NSWSC 1155; (2002) 60 NSWLR 241, although in that case no reference was made to unconscionable conduct.

67 *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* [2003] EWCA Civ 1407; [2003] QB 679.

68 *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* [2003] EWCA Civ 1407; [2003] QB 679, [162].

case that the contract was void under the principle in *Bell v Lever Bros Ltd*".[69] As it was, however, the Great Peace was able to "arrive in time to provide several days of escort service" before the tug arrived.[70] Thus, the services the Great Peace was in a position to provide were not essentially different from those envisaged by the parties, and the defendant's failure to cancel the contract immediately upon learning of its position was a telling indication of this. The defendant was therefore bound by the contract and was obliged to pay the stipulated cancellation fee.

The Court of Appeal also held that there was no equitable jurisdiction to set contracts aside for common mistake. The existence of an equitable jurisdiction to set aside contracts made on the basis of a "fundamental" common misapprehension (the test from *Solle v Butcher*) could not be reconciled with the existence of the common law principle recognised in *Bell v Lever Bros Ltd*. That common law principle holds void a contract made under a "mistake as to quality which 'makes the thing [contracted for] essentially different from the thing [that] it was meant to be' ".[71] The Court of Appeal said that it was not possible to distinguish a mistake that is "fundamental" and attracts equitable relief, from a mistake that makes the thing "essentially different" and thus attracts the operation of the common law doctrine.[72] Thus, although the decision in *Solle v Butcher* had stood for more than 50 years and had been followed in a number of cases, the equitable jurisdiction identified by Denning LJ in that case "was a chimera".[73]

The position in Australia

[31.62] In *Australia Estates Pty Ltd v Cairns City Council*, two members of the Queensland Court of Appeal expressed their approval of *The Great Peace* and maintained that in Australian law there is no equitable jurisdiction to set aside, on the ground of common mistake, an agreement which is valid and enforceable at common law.[74] Atkinson J (with whom Jerrard J agreed) accepted the approach adopted in *The Great Peace* because of the persuasiveness of the court's reasoning in that case, because of negative references to *Solle v Butcher* in *Harris v Digital Pulse Pty Ltd*,[75] and because of what Atkinson J described as the "somewhat qualified approach taken to *Solle v Butcher* by the High Court".[76] Since the Court of Appeal found that no mistake had been made in *Australia Estates Pty Ltd v Cairns City Council*, Atkinson J's comments on the availability of rescission for common mistake were made by way of obiter dicta. They have, however, since received some support.[77]

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69 *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* [2003] EWCA Civ 1407; [2003] QB 679, [162].

70 *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* [2003] EWCA Civ 1407; [2003] QB 679, [165].

71 *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* [2003] EWCA Civ 1407; [2003] QB 679, [154], quoting *Bell v Lever Bros Ltd* [1932] AC 161, 218.

72 *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* [2003] EWCA Civ 1407; [2003] QB 679, [153].

73 *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* [2003] EWCA Civ 1407; [2003] QB 679, [131].

74 *Australia Estates Pty Ltd v Cairns City Council* [2005] QCA 328, [52], [64] (Atkinson J, with whom Jerrard J agreed; McMurdo P noting at [11] that it was unnecessary to consider the question).

75 In *Harris v Digital Pulse Pty Ltd* [2003] NSWCA 10; (2003) 56 NSWLR 298, [455], Heydon JA disparagingly cited *Solle v Butcher* as an example of equity's supposed "creativity" and "dynamism" that had since been overruled.

76 *Australia Estates Pty Ltd v Cairns City Council* [2005] QCA 328, [52].

77 *Manna v Manna* [2008] ACTSC 10, [51] ("there are serious doubts about the application of the rule in *Solle v Butcher* or some like equitable principle enabling the setting aside of a contract") and *Menegazzo v PriceWaterhouseCoopers (A Firm)* [2016] QSC 94, [117]–[124].

The view expressed in *Australia Estates Pty Ltd v Cairns City Council* has been criticised by a respected Australian contract scholar on two grounds: first, because it is inconsistent with the approach taken by the High Court in *Taylor v Johnson*; and, secondly, because the *Solle v Butcher* principle provides much-needed flexibility in dealing with common mistakes and allows third party rights to be protected.[78] In *Rees v Rees*,[79] McMillan J declined to follow what was said in *Australia Estates Pty Ltd v Cairns City Council* and granted rescission of a settlement deed on the basis of a common mistake. The deed was made between brother and sister to compromise litigation concerning their father's will. The settlement deed was entered into on the basis of common mistakes relating to the identity and value of land to be transferred pursuant to the deed. McMillan J held that rescission could be granted for common mistake under Australian law: the High Court confirmed its availability in *Taylor v Johnson* and several decisions since had proceeded on that basis.[80] Another noteworthy decision in this context is the pre-*Taylor v Johnson* case of *Lukacs v Wood*,[81] in which rescission of a contract of sale was granted because of a common mistake as to the identity of the land being sold.

As things stand, the weight of authority and opinion favours the view that, despite *The Great Peace*, rescission in equity for common mistake remains available in Australian law in some circumstances.[82]

Rectification for common mistake

[31.65] Sometimes when parties reduce their agreement to writing, they fail to record their intentions accurately. In such circumstances, a court exercising equitable jurisdiction may "rectify" or rewrite the contractual document so that it reflects the true intentions of the parties. As Campbell JA noted in *Franklins Pty Ltd v Metcash Trading Ltd*, equity permits rectification in such circumstances because "it is unconscientious for a party to a contract to seek to apply the contract inconsistently with what he or she knows to be the common intention of the parties at the time that the written contract was entered".[83] For example, the parties may orally agree to the sale of a house and all its furniture and accessories (excluding the carpets and curtains) for $500,000. When the contract is recorded in writing and signed, the document mistakenly states that the sale includes all the furniture and accessories. At common law, the parol evidence rule will most likely apply, and evidence could not be received to vary the written agreement[84] or influence the interpretation of the contract.[85] However, it would clearly be unconscionable for the purchaser to rely on his or her strict legal rights in such a situation and claim that the carpet and curtains were included in the sale. Accordingly,

78 Seddon, "Contract: Mistake Mistake" (2006) 80 *Australian Law Journal* 95. See also *Errichetti Nominees Pty Ltd v Paterson Group Architects Pty Ltd* [2007] WASC 77, [60]–[62]; Swain, "Common Mistake in Equity: Some Unanswered Questions" (2015) 40 *Australian Bar Review* 124; Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [12.25]; Heydon, *Heydon on Contract* (2019), [15.200].

79 *Rees v Rees* [2016] VSC 452, [103].

80 *Rees v Rees* [2016] VSC 452, [103].

81 *Lukacs v Wood* (1978) 19 SASR 520.

82 For discussion of the circumstances in which equitable relief is available, see Heydon, *Heydon on Contract* (2019), [15.200].

83 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407, [448]. See further McLauchlan, "The 'Drastic' Remedy of Rectification for Unilateral Mistake" (2008) 124 *Law Quarterly Review* 608.

84 See Chapter 12.

85 See Chapter 13.

the document may be rectified so that it expresses the true intentions of the parties. Even a provision stipulating that the document constitutes the "entire agreement" and "supersedes and cancels all prior arrangements and understandings" would not preclude the reception of evidence to prove that the written contract was not in accord with the true intentions of the parties.[86] If rectification is ordered, it is retrospective to the date of the execution of the document.

The party seeking rectification must provide "clear and convincing proof" of the common intention that is said not to be reflected in the contract.[87] Further, this common intention must continue up to the time of execution of the contract in question.[88] If a court is persuaded to grant rectification, it will make an order that identifies any words of the contract that are to be struck out and/or any words that are to be inserted into the contract. Thus, any term amended by rectification must have sufficient certainty to be contractually enforceable.[89] The contract will be rewritten only to the extent necessary to ensure that it expresses the parties' common intention at the time of contracting.[90] However, "[e]ven if a mistake in the expression of the document is able to be read in the correct (ie, the intended) sense as a matter of construction, nevertheless rectification can be granted"[91] to overcome any remaining uncertainty.

In *Maralinga Pty Ltd v Major Enterprises Pty Ltd*,[92] Major Enterprises put up land for sale by auction. The auctioneer announced that the purchaser would be allowed a mortgage back to the vendor for $64,500 for three years at eight per cent. The property was knocked down to Maralinga for $155,000. The draft contract provided for the payment of the balance of the purchase price on completion but did not contain a provision for any part of the price to remain on mortgage. Maralinga signed the contract knowing of this omission, as did Major Enterprises. Maralinga apparently thought it could still have the benefit of the auctioneer's promise regarding the mortgage. It later sought rectification of the written instrument on the basis that, at the end of the auction, there was an agreement (albeit unenforceable for lack of writing) and that the written instrument did not conform with that agreement.

The High Court, by a majority, refused to order rectification. No mistake had been made as to what the written contract contained. Both parties knew the written instrument differed from the terms of the antecedent bargain. Mason J said:

> [T]he court must be satisfied that the instrument does not reflect the true agreement of the parties. It cannot be so satisfied unless the writing was intended to record the earlier agreement and by mistake of the parties it fails to do so. If the plaintiff fails to establish these elements he does not displace the hypothesis arising from the execution of the written instrument, namely, that it is the true agreement of the parties.[93]

86 *MacDonald v Shinko Australia Pty Ltd* [1999] 2 Qd R 152.

87 *Pukallus v Cameron* (1982) 180 CLR 447, 452; *Ryledar Pty Ltd v Euphoric Pty Ltd* [2007] NSWCA 65; (2007) 69 NSWLR 603, [161].

88 *Pukallus v Cameron* (1982) 180 CLR 447, 452; *Ryledar Pty Ltd v Euphoric Pty Ltd* [2007] NSWCA 65; (2007) 69 NSWLR 603, [259].

89 On certainty see Chapter 6.

90 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407, [448].

91 *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407, [539], see also [26]–[27], [48].

92 *Maralinga Pty Ltd v Major Enterprises Pty Ltd* (1973) 128 CLR 336.

93 *Maralinga Pty Ltd v Major Enterprises Pty Ltd* (1973) 128 CLR 336, 351; cf *Winks v WH Heck & Sons Pty Ltd* [1986] 1 Qd R 226.

Although this quotation might give the impression that rectification requires a concluded agreement between the parties that precedes the execution of the written instrument, Mason J noted elsewhere in his judgment that an "antecedent agreement" between the parties is not required. Rectification may be granted in cases where "the instrument sought to be rectified constitutes the only agreement between the parties, but does not reflect their common intention".[94]

[31.67] Rectification for common mistake involves the correction of an instrument to accord with the common intention actually held by the parties. In *Simic v NSW Land and Housing Corporation* the High Court confirmed that the common intention that must be established for rectification is an intention actually or subjectively held by the parties, rather than an intention objectively manifested by their conduct.[95] It is sometimes said that the parties' intentions must be manifested by their words or conduct, but this is only a matter of discharging the burden of proof relating to the parties' actual, subjectively held intentions.[96] The parties' intentions may be ascertained not only from evidence as to their words or conduct but also from evidence given by the parties themselves as to their subjective states of mind.[97] The subjective approach is appropriate because equity acts on the conscience of the party denying the relevant common intention.[98] Tobias JA noted in *Ryledar Pty Ltd v Euphoric Pty Ltd* that where objective evidence establishes the necessary common intention, an assertion by the party opposing rectification that he or she did not subjectively have such an intention is unlikely to trump the intention objectively manifested by his or her conduct.[99] That is because the party's evidence is unlikely to be accepted, not because the Court is precluded from hearing evidence as to the subjective intentions of the parties.[100]

It is sometimes said that, for rectification to be granted, there must be an "some outward expression of accord"[101] between the parties or that the relevant intention must have been "communicated by one side to the other".[102] Kiefel J suggested in *Simic v NSW Land and Housing Corporation* that these are not requirements in themselves, but just go to whether the burden of proving the actual common intentions of the parties has been discharged.[103] Her Honour said that it is "to be expected that proof to the necessary standard will usually require some manifestation of the intention of each party by their words or conduct and that the requisite common intention will be a matter of inference for the court from that evidence".[104] In *Ryledar Pty Ltd v Euphoric Pty Ltd*, however, Campbell JA argued persuasively that it is necessary for the parties to "know enough of each other's intentions for it to be said that there

94 *Maralinga Pty Ltd v Major Enterprises Pty Ltd* (1973) 128 CLR 336, 350; see also *Pukallus v Cameron* (1982) 180 CLR 447, 452 and *Simic v NSW Land and Housing Corporation* [2016] HCA 47; (2016) 260 CLR 85, [32], [41], [117].

95 *Simic v NSW Land and Housing Corporation* [2016] HCA 47; (2016) 260 CLR 85, [19] (French CJ), [41]–[46] (Kiefel J), [104] (Gageler, Nettle and Gordon JJ).

96 *Simic v NSW Land and Housing Corporation* [2016] HCA 47; (2016) 260 CLR 85, [42] (Kiefel J).

97 *Ryledar Pty Ltd v Euphoric Pty Ltd* [2007] NSWCA 65; (2007) 69 NSWLR 603, [182]–[187].

98 *Ryledar Pty Ltd v Euphoric Pty Ltd* [2007] NSWCA 65; (2007) 69 NSWLR 603, [187].

99 *Ryledar Pty Ltd v Euphoric Pty Ltd* [2007] NSWCA 65; (2007) 69 NSWLR 603, [185].

100 See also *Simic v NSW Land and Housing Corporation* [2016] HCA 47; (2016) 260 CLR 85, [42].

101 *Joscelyne v Nissen* [1970] 2 QB 86, 98.

102 *Lovell & Christmas Ltd v Wall* [1911] 104 LT 85, 93.

103 *Simic v NSW Land and Housing Corporation* [2016] HCA 47; (2016) 260 CLR 85, [43]–[46].

104 *Simic v NSW Land and Housing Corporation* [2016] HCA 47; (2016) 260 CLR 85, [43]; see also [46].

is a common intention".[105] What underlies and justifies rectification is the notion that it is unconscientious to take advantage of a common mistake by insisting on the terms of a document that does not accurately record the parties' common intention.[106] The parties' intentions must therefore have been sufficiently disclosed to one another that they can be understood to have had a *common* intention. This does not mean that each party must have directly stated his or her intention. Rather, the parties may come to know of each other's intention through various means, including conscious and deliberate inference. According to Campbell JA, this "need for disclosure fills the role of being a limitation on the types of subjective intention that can be enforced through the remedy of rectification".[107] His Honour said:

> If two negotiating parties each had a particular intention about the agreement they would enter, and their intentions were identical, but that intention was disclosed by neither of them, and they later entered a document that did not accord with that intention, what would be the injustice or unconscientiousness in either of them enforcing the document according to its terms?

In *Chartbrook Ltd v Persimmon Homes Ltd* the House of Lords took the view that rectification is concerned with the objectively manifested intentions of the parties and not their subjective intentions. An exchange of letters between the parties in that case indicated that they were in agreement as to the method of calculation of a fee payable under the terms of the contract by Persimmon to Chartbrook. On the basis of oral evidence given by the directors of Chartbrook, however, the trial judge accepted that the objective appearance was misleading, that Chartbrook's understanding was in fact consistent with the contract as written, and that there was no common mistake. The House of Lords held that rectification was nevertheless available because the relevant question was "what an objective observer would have thought the intentions of the parties to be."[108] That conclusion was expressed by way of obiter dicta, however, because the House of Lords concluded that the same result could be reached applying ordinary principles of contract interpretation.[109] A reasonable person would conclude that something had gone wrong with the language of the written contract and would understand it to have a meaning that did not reflect "what the words would conventionally have been understood to mean" but which happened to be consistent with the view expressed by the parties in the exchange of letters.[110]

In *FSHC Group Holdings Ltd v Glas Trust Corporation Ltd*[111] the English Court of Appeal declined to follow the approach taken by the House of Lords in *Chartbrook*. The Court of Appeal held that it was bound by its own pre-*Chartbrook* decisions to require an actual, subjective common intention for rectification. Moreover, their Lordships held, a subjective approach is consistent with the underlying justification for rectification, which is that it is against conscience to enforce terms of a written contract that are "inconsistent with what both parties in fact intended (and mutually understood each other to intend) those terms to be

105 *Ryledar Pty Ltd v Euphoric Pty Ltd* [2007] NSWCA 65; (2007) 69 NSWLR 603, [281].

106 *Ryledar Pty Ltd v Euphoric Pty Ltd* [2007] NSWCA 65; (2007) 69 NSWLR 603, [310]–[315].

107 *Ryledar Pty Ltd v Euphoric Pty Ltd* [2007] NSWCA 65; (2007) 69 NSWLR 603, [316]. Cf *Tipperary Developments Pty Ltd v Western Australia* [2009] WASCA 126, [279]–[280].

108 *Chartbrook Ltd v Persimmon Homes Ltd* [2009] UKHL 38; (2009) 1 AC 1101, [60].

109 *Chartbrook Ltd v Persimmon Homes Ltd* [2009] UKHL 38; (2009) 1 AC 1101, [26]–[27].

110 *Chartbrook Ltd v Persimmon Homes Ltd* [2009] UKHL 38; (2009) 1 AC 1101, [15]–[26].

111 *FSHC Group Holdings Ltd v Glas Trust Corporation Ltd* [2019] EWCA Civ 1361.

when the document was executed".[112] Leggatt LJ, giving the judgment of the Court, also noted that the subjective approach was supported by the careful analysis of Campbell JA in *Ryledar Pty Ltd v Euphoric Pty Ltd* and the approach taken by the High Court in *Simic v New South Wales Land and Housing Corp*, both of which were discussed above.[113]

[31.68] Rectification may not be granted where parties would have used a different form of words had they known the true facts. In *Pukallus v Cameron*,[114] a written agreement was made for the sale of land described as "Subdivision 1 of Portion 1154". Both parties believed that Subdivision 1 included a bore and an area of cultivated land which they had inspected together before the contract was signed. After the sale was completed, the purchaser discovered that the area of land in question was part of Subdivision 2. The purchaser sought rectification of the contract. The trial judge ordered that the contract be rectified so that the description of the property would include the land in question. This order was overturned on appeal. The High Court held that the written contract did embody the intention of the parties, which was to transfer Subdivision 1 of Portion 1154. Although the parties erroneously believed the bore and cultivated area to be included in that parcel, there was no evidence of an intention to transfer land other than Subdivision 1.[115] Moreover, to obtain rectification, the purchaser would need to prove the precise term that was agreed between the parties and mistakenly omitted from the written contract.[116] Brennan J said that rectification could only be granted "upon proof that the parties intended that a further parcel of land, precisely identified, was to be included in the sale".[117]

The decision in *Pukallas v Cameron* should not be understood to mean that, for rectification to be granted, the mistake must relate to the words used by the parties rather than their legal effect.[118] The authorities were extensively reviewed by the New South Wales Court of Appeal in *Commissioner of Stamp Duties v Carlenka Pty Ltd*.[119] In that case, an amendment to a trust deed was intended to permit the distribution of income to a particular beneficiary. The words used had the additional unintended effect of entitling the beneficiary to share in the capital of the trust, and this had adverse stamp duty consequences. The trial judge rectified the document by adding words that prevented the distribution of capital to the beneficiary. The Court of Appeal upheld the order for rectification, notwithstanding that the party signing the document intended to execute it in that form. The Court concluded that rectification overcomes "mistaken expression of the true agreement"[120] and is available where the parties

112 *FSHC Group Holdings Ltd v Glas Trust Corporation Ltd* [2019] EWCA Civ 1361, [146].

113 *FSHC Group Holdings Ltd v Glas Trust Corporation Ltd* [2019] EWCA Civ 1361, [168]–[169].

114 *Pukallus v Cameron* (1982) 180 CLR 447.

115 *Pukallus v Cameron* (1982) 180 CLR 447, 453.

116 *Pukallus v Cameron* (1982) 180 CLR 447, 453.

117 *Pukallus v Cameron* (1982) 180 CLR 447, 457.

118 *Winks v W H Heck & Sons Pty Ltd* [1986] 1 Qd R 226; *Commissioner of Stamp Duties v Carlenka Pty Ltd* (1995) 41 NSWLR 329.

119 *Commissioner of Stamp Duties v Carlenka Pty Ltd* (1995) 41 NSWLR 329.

120 *Commissioner of Stamp Duties v Carlenka Pty Ltd* (1995) 41 NSWLR 329, 340. This states the test in broad terms and suggests that rectification may be available where there is a mistaken expression of the true agreement brought about by a mistake about the true facts. In *Mander Pty Ltd v Clements* [2005] WASCA 67; (2005) 30 WAR 46, [15] Murray J (dissenting) was prepared to rectify a contract to overcome a mistake the parties had made about the true owner of the premises subject to the agreement in question, even though this was a mistake about the true facts. Murray J pointed to *Commissioner of Stamp Duties v Carlenka Pty Ltd* (1995) 41 NSWLR 329 to support his reasoning.

have deliberately "used words which, when properly construed, do not express their true intention".[121] Rectification is available where the parties are mistaken as to the meaning or effect of the words they have used. The crucial requirement is that there must be a lack of correspondence between the form of the document and the common intention of the parties.[122]

Mistake and frustration

[31.70] Where a mistake relates not to facts existing at the time the contract was formed, but to *subsequent* events, the question becomes one of possible discharge of the contract by reason of frustration. The topic of frustration is dealt with in Chapter 15. As discussed at [31.50], the rules of common mistake and frustration are related.[123] The tests of mistake and frustration are often defined in similar terms; that is, as requiring the emergence or development of a factual situation radically different from that by reference to which the parties made their agreement.[124] A short difference in time may determine which set of rules applies. Take the example of a contract for the hire of a concert hall for a performance where, without the knowledge or fault of either party to the contract of hire, the hall burnt down shortly before or shortly after the contract is signed. In the former situation, the issue is one of mistake; in the latter, it is one of frustration. When the coronation procession of Edward VII was cancelled owing to the king's illness, contracts for the hire of rooms for viewing the procession were dealt with as cases either of frustration or of mistake, depending on whether the particular contract was made before or after the decision to postpone the procession.[125]

MUTUAL MISTAKE

[31.75] If A offers B a painting for US$5,000 and B accepts the offer, mistakenly thinking the price is AUD$5,000, there is no *actual* coincidence of offer and acceptance. The mistakes are *mutual* in the sense that, assuming A did not know of B's mistake about the price, the parties are mistaken about each other's intentions. As we have seen, however, the expression "mutual mistake" is also sometimes used as a synonym for common mistake. The effect of the parties being at cross purposes tends to be resolved by common law construction principles. Adopting the objective approach used to construe contracts, the question becomes: "Did B appear to accept the US$5,000 offer?" If B did, then there would be a valid contract on A's terms despite B's mistake. If B then refuses to complete because she was mistaken, she will be in breach of the contract.

However, there are situations where principles of contractual interpretation cannot establish that one party was correct and the other mistaken. In *Raffles v Wichelhaus*,[126] the defendant agreed to purchase 125 bags of cotton "to arrive ex Peerless from Bombay". When the cotton arrived in London, the defendant refused to accept delivery. His defence was that

121 *Commissioner of Stamp Duties v Carlenka Pty Ltd* (1995) 41 NSWLR 329, 343, citing *NSW Medical Defence Union Ltd v Transport Industries Insurance Co Ltd* (1986) 6 NSWLR 740.

122 *Club Cape Shanck Resort Co Ltd v Cape Country Club Pty Ltd* [2001] VSCA 2; (2001) 3 VR 526, [39].

123 See *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337, 360.

124 See *Bell v Lever Brothers Ltd* [1932] AC 161, 226–7.

125 See *Krell v Henry* [1903] 2 KB 740, a frustration case, discussed at [15.25]. For an example of mistake in the same context, see *Griffith v Brymer* (1903) 19 TLR 434.

126 *Raffles v Wichelhaus* (1864) 2 H&C 906; 159 ER 375.

he had been ready to receive cotton from the Peerless that sailed from Bombay in October, but the plaintiff proffered cotton from a different ship of the same name that left Bombay in December. The court gave judgment for the defendant but did not explain its reasons for doing so. It apparently accepted the argument that as each party intended a different ship, there was no consensus. It appears that no common intention could be objectively inferred from the conduct of the parties and the words of their agreement – the contract did not clearly identify which ship the goods were to be transported on other than by name. Because of the ambiguity, the agreement failed to meet the certainty requirement.[127] Thus, no contract was formed. The mistaken party was not bound by the contract but this does not mean the court provided relief against mistake. Rather, under the ordinary principles of contract formation, no contract was formed.

Equity follows the law with regard to mutual mistakes. As the non-mistaken party is unaware of the mistake, there is no equitable basis for interfering with the common law outcome.

UNILATERAL MISTAKE

[31.80] Where the parties, subjectively speaking, are not in agreement, but the understanding of one of the parties accords with what a reasonable person would think was intended (ie, that party's understanding reflects the correct objective interpretation of the contract), the mistake is described as unilateral. A unilateral mistake may be made in relation to the *terms* of the contract, a quality of the *subject matter* or the *identity* of the other contracting party. A unilateral mistake as to terms may render a contract void, voidable or provide grounds for rectification, as will be discussed below. Whether and when unilateral mistakes as to identity will render contracts void or voidable will also be discussed.

No relief is provided in where a party makes a unilateral mistake as to a quality of the subject matter or a factor influencing his or her decision to enter into the contract. In *Statoil ASA v Louis Dreyfus Energy Services LP (The Harriette N)*,[128] one of the contracting parties had made a serious mistake about the value of the subject matter of the contract. It was clear to the other party's representative that a mistake had been made, but he chose not to correct it. Aikens J held that the contract was binding. He said:

> The general rule at common law is that if one party has made a mistake as to the terms of the contract and that mistake is known to the other party, then the contract is not binding. … However, if one party has made a mistake about a fact on which he bases his decision to enter into the contract, but that fact does not form a term of the contract itself, then, even if the other party knows that the first is mistaken as to this fact, the contract will be binding. That was the effect of the decision of the Court of Queen's Bench, on appeal from the County Court, in *Smith v Hughes* [1871] LR 6 QB 597, see particularly at 603 per Cockburn CJ, and 607 per Blackburn J. The correctness of that decision and the analysis in it has never been doubted.[129]

127 See Chapter 6.

128 *Statoil ASA v Louis Dreyfus Energy Services LP (The Harriette N)* [2008] EWHC 2257 (Comm); see Cartwright, "Unilateral Mistake in the English Courts: Reasserting the Traditional Approach" [2009] *Singapore Journal of Legal Studies* 226.

129 *Statoil ASA v Louis Dreyfus Energy Services LP (The Harriette N)* [2008] EWHC 2257 (Comm), [87]–[88].

Unilateral mistake as to terms

Common law: no agreement

[31.85] A contract will only be "void" at common law for unilateral mistake if it can be concluded that there was no agreement as to terms and, therefore, no contract was formed. In *Hartog v Colin & Shields*,[130] the defendant offered to sell Argentine hare skins to the plaintiff, but by mistake quoted to sell the skins at a price per pound instead of per piece. All of the verbal negotiations and correspondence between the parties involved discussions of price per piece. Moreover, Argentine hare skins were commonly priced by the piece in the trade, and the quoted price per pound was equal to approximately one third of the normal price. Singleton J concluded that "anyone with any knowledge of the trade must have realised that there was a mistake" and the buyer "could not reasonably have supposed that the offer contained the offeror's real intention."[131] The buyer's action for damages was unsuccessful, but Singleton J did not say whether the contract was void or voidable. One explanation is that, since a reasonable person in the buyer's position would have understood that the seller had made a mistake, on an objective approach to formation there was no valid acceptance of the offer, no agreement and therefore no contract.[132]

The Singapore Court of Appeal recently found that a contract entered into in similar circumstances was void at common law on the basis that it could be inferred that the buyer had actual knowledge of the mistake.[133] In *Chwee Kin Keong v Digiland.com Pte Ltd*,[134] the respondent had mistakenly posted the price of commercial laser printers on its website. It advertised the printers at $66 when in fact the model in question typically sold for well over $3,000. The description of the printer simply read "55". The appellants placed, between them, orders over the internet for 1,606 commercial laser printers in the course of a single night. The appellants' orders were processed by the respondent's automated system and order confirmations were despatched to the appellants within a few minutes of the orders being placed. When the respondent became aware of the mistake it informed all customers who had placed orders that it would not be meeting the orders. The respondent unsuccessfully argued that the contract was conditional upon the printers being available. However, the respondent's argument that the contract was void at common law by reason of mistake was successful. Chao Hick Tin JA (who delivered the judgment of the Singaporean Court of Appeal) noted that this finding involved a departure from the objective approach employed by the common law to determine whether a contract has come into being. His Honour justified this departure by noting that:

> The reason behind this exception is self-evident, as a party who is aware of the error made by the other party cannot claim that there is *consensus ad idem*. The law should not go to the aid of a party who knows that the objective appearance does not correspond with reality. It would go against the grain of justice if the law were to deem the mistaken party bound by such a contract.[135]

130 *Hartog v Colin & Shields* [1939] 3 All ER 566.

131 *Hartog v Colin & Shields* [1939] 3 All ER 566, 568.

132 Burrows, *A Restatement of the English Law of Contract* (2016), p 175 stipulates in s 35(4) that there will be no contract if the non-mistaken party "knows or ought reasonably to know" of the mistake.

133 Hannen J's judgment in *Smith v Hughes* [1871] 6 QB 597, 610 was also cited in support.

134 *Chwee Kin Keong v Digiland.com Pte Ltd* [2005] SGCA 2; [2005] 1 SLR 502.

135 *Chwee Kin Keong v Digiland.com Pte Ltd* [2005] SGCA 2; [2005] 1 SLR 502, [31].

Chao Hick Tin JA made it clear that it is only where the court finds that there is actual knowledge (which was held to include wilful blindness) that the case comes within the ambit of what his Honour describes as "the common law doctrine of unilateral mistake".[136] Where the non-mistaken party does not have actual knowledge of the mistake, there is no reason to displace the objective principle.[137] Cases involving constructive knowledge only can be dealt with in equity and intervention is only likely if such knowledge is coupled with sharp practice on the part of the non-mistaken party. As the trial judge's finding that the appellants had actual knowledge of the respondent's mistake was upheld, and the other elements listed met, the contract was held to be void at common law. It was also made clear that only sufficiently serious or fundamental mistakes as to terms would vitiate a contract under this approach.

The approach adopted by the High Court in *Taylor v Johnson*[138] provides a strong indication that these cases involving the "snapping up" of offers would be dealt with in equity in Australia, and the contracts treated as voidable rather than void. Although the seller in *Taylor v Johnson* was mistaken as to the contract price, it was not clear to the buyer at the time the contract was made whether the vendor was mistaken as to the contract price or as to the value of the land.[139] The situation was therefore slightly different from the two cases just discussed. Significantly for present purposes, however, Mason ACJ, Murphy and Deane JJ rejected the idea that the vendor could rely on her own mistake to support a conclusion that there was no contract at common law, even though this had been argued on behalf of the seller.[140]

In *Taylor v Johnson*, Mason ACJ, Murphy and Deane JJ affirmed the objective approach to contract formation and quoted with apparent approval the statement of Denning LJ that "once the parties, whatever their innermost states of mind, have to all outward appearances agreed on the same terms … then the contract is good unless it is set aside for failure of some condition … or on some equitable ground."[141] That is consistent with a conclusion that no contract was formed in *Hartog v Collin & Shields*: the parties in that case had not "to all outward appearances agreed on the same term" because a reasonable person would understand that the seller was mistaken and there was no agreement. But Mason ACJ, Murphy and Deane JJ twice quoted a further passage from Denning LJ that "Neither party can rely on his own mistake to say it [the contract] was a nullity from the beginning … no matter that the other party knew he was under a mistake."[142] Mason ACJ, Murphy and Deane JJ accepted that statement as "applicable to a case, such as the present where the mistake is as to the existence or content of a term in a formal written contract".[143] The only question, then, was whether relief was available in equity.[144] Seddon and Bigwood therefore seem right to suggest that, if *Hartog v Colin & Shields* was decided in Australia today, the contract would not be

136 *Chwee Kin Keong v Digiland.com Pte Ltd* [2005] SGCA 2; [2005] 1 SLR 502, [53].

137 *Chwee Kin Keong v Digiland.com Pte Ltd* [2005] SGCA 2; [2005] 1 SLR 502, [53].

138 *Taylor v Johnson* (1983) 151 CLR 422, discussed further at [31.95].

139 *Taylor v Johnson* (1983) 151 CLR 422, 427.

140 *Taylor v Johnson* (1983) 151 CLR 422, 424.

141 *Taylor v Johnson* (1983) 151 CLR 422, 429, quoting *Solle v Butcher* [1950] 1 KB 671, 691.

142 *Solle v Butcher* [1950] 1 KB 671, 691, quoted at *Taylor v Johnson* (1983) 151 CLR 422, 429, 430.

143 *Taylor v Johnson* (1983) 151 CLR 422, 431.

144 *Taylor v Johnson* (1983) 151 CLR 422, 431.

considered void at common law but voidable in equity because of the unconscionable conduct of the buyer.[145]

Common law: non est factum

[31.90] In the 16th century, it was held that if a person who could not read executed a deed after it had been incorrectly read over to him or her, the deed would not be binding. The defence also applied where the signature or seal had been forged. It could be claimed on behalf of the illiterate, blind or victimised person: non est factum (it is not his/her deed).[146] Accordingly, if a person in these circumstances proves that he or she signed a document, believing it to be a document fundamentally different from what it was, he or she is not bound by the signature. Because of the absence of genuine consent to the contractual obligations apparently undertaken, the contract is void at common law. Relief may be available even if the person seeking it acted carelessly.

The rule in modern times has been clarified by the House of Lords in *Saunders (Executrix of the Will of Gallie) v Anglia Building Society*[147] and by the High Court in *Petelin v Cullen*.[148] The following qualifications have been emphasised. First, the class of persons who can avail themselves of the rule is limited to those who cannot read owing to blindness or illiteracy or who through no fault of their own are unable to have any understanding of the purport of a particular document,[149] for example, a migrant with little knowledge of English or a person suffering from mental infirmity.[150] Persons of full capacity will rarely qualify.[151] The rule will apply where the person seeking to invoke it does not have the capacity to form any relevant belief about the character of the document.[152] Secondly, the signer must sign the document in the belief that it was radically or fundamentally different from what it was in fact.[153] A distinction in earlier cases requiring that the mistake relate to the character or nature of the document, as distinct from its terms or contents, has been rejected as unsound. A mistake as to contents of a document can be just as radical as a mistake as to its character. Thirdly, at least where the defence is asserted against an innocent person, the failure to read and understand the document must not be due to carelessness on the part of the signer. The signer must take reasonable precautions to understand the document. Whether reasonable precautions have been taken is to be assessed by reference to the circumstances of the signer.[154] Fourthly, there is a heavy burden on a person who seeks to rely on the defence.[155] However, the person who

145 Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [12.48]. See also Heydon, *Heydon on Contract* (2019), [15.260] ("Whatever the position elsewhere, unilateral mistake of this kind [ie, as to terms] leads to the contract being voidable, not void".)

146 The full plea was Scriptum predictum non est factum suum.

147 *Saunders (Executrix of the Will of Gallie) v Anglia Building Society* [1971] AC 1004.

148 *Petelin v Cullen* (1975) 132 CLR 355.

149 *Petelin v Cullen* (1975) 132 CLR 355, 359–60.

150 *PT Ltd v Maradona Pty Ltd* (1992) 25 NSWLR 643. Cf the equitable jurisdiction to set aside contracts of mentally infirm persons, discussed at [36.35].

151 *Saunders (Executrix of the Will of Gallie) v Anglia Building Society* [1971] AC 1004, 1015.

152 *Ford v Perpetual Trustees Victoria Ltd* [2009] NSWCA 186; (2009) 75 NSWLR 42, [38].

153 *Petelin v Cullen* (1975) 132 CLR 355, 360.

154 *Ford v Perpetual Trustees Victoria Ltd* [2009] NSWCA 186; (2009) 75 NSWLR 42, [39], [89].

155 *Petelin v Cullen* (1975) 132 CLR 355, 360.

seeks to rely on the defence does not need to establish that the other party had knowledge of the incapacity that led to the signing of the contract.[156]

When the plea of non est factum is raised against a person who induced the signing and was aware of the mistake or had reason to suspect it, the issue of the signer's carelessness or otherwise does not arise.[157] In *Petelin v Cullen*,[158] Cullen presented Petelin with a document for signature and told him it was a receipt for $50 he had previously sent him. Petelin, who spoke little English, signed the document. In fact it was an extension of an option (in favour of Cullen) to buy land owned by Petelin. Cullen exercised the option, but Petelin refused to sign the contract of sale. When Cullen sued him for specific performance, Petelin raised the defence of non est factum.

The High Court allowed the defence. In this case, the signer's carelessness or otherwise was irrelevant. Cullen was not an innocent person who had relied on a signature with no reason to doubt its validity. He had misrepresented the nature of the document to Petelin and knew of his language problem. In any event, Petelin was not careless. He could not read English and he had a choice of either relying on Cullen or incurring the expense of a solicitor's advice. The document he signed, a contractually binding document, was radically different from what he believed it to be, a receipt for a payment he thought he was entitled to.[159] Accordingly, the option was void. It should be noted that this type of case is an instance of unilateral mistake and if the contract was found to be valid at common law, Petelin could have invoked equity to have the contract set aside.[160]

Equity: rescission

[31.95] A contract valid at common law may be *voidable* in equity because of a unilateral mistake as to a fundamental term of the contract. As noted above, the equitable jurisdiction is not enlivened solely on the basis that a *unilateral mistake* has been made, even if the mistake is serious and entry into the contract has serious, negative consequences for the mistaken party. It must be shown that it would be unconscionable to uphold the bargain, a requirement that is often met by showing that the non-mistaken party had actual or constructive knowledge of the mistake.

The leading Australian case on the equitable jurisdiction to set aside a contract on the basis of unilateral mistake is *Taylor v Johnson*.[161] Mrs Johnson granted an option to Mr Taylor to purchase two lots of land, each comprising five acres, for a total purchase price of $15,000. The option was exercised by Taylor, and Johnson entered into a written contract for the sale of the land. The purchase price was $15,000 as provided in the option. Subsequently, however, Johnson declined to perform the contract on the ground that she had mistakenly believed that the agreements provided for a price of $15,000 per acre of the subject land. At the time the contract was made, Taylor believed that Johnson was under some serious mistake or misapprehension as to either the terms (the price) or the subject matter (its value) of the

156 *Perpetual Trustees Victoria Ltd v Ford* [2008] NSWSC 29; (2008) 70 NSWLR 611, [84] (affirmed on appeal: *Ford v Perpetual Trustees Victoria Ltd* [2009] NSWCA 186; (2009) 75 NSWLR 42).

157 *Petelin v Cullen* (1975) 132 CLR 355, 360.

158 *Petelin v Cullen* (1975) 132 CLR 355.

159 Cf *Lee v Ah Gee* [1920] VLR 278.

160 *Taylor v Johnson* (1983) 151 CLR 422, discussed at [31.95].

161 *Taylor v Johnson* (1983) 151 CLR 422.

transaction. He deliberately set out to ensure that she did not become aware of her mistake or misapprehension. He refrained from mentioning the price and wrongly stated that he did not have a copy of the option to make available to her. Johnson sought an order setting aside the contract of sale. The High Court held (3-1) that the contract should be set aside.

As noted above, Mason ACJ, Murphy and Deane JJ found that it could not be claimed that the contract was a nullity at common law.[162] Instead, the matter was resolved in equity. The particular proposition of law which Mason ACJ, Murphy and Deane JJ saw as appropriate to dispose of the present case in favour of Mrs Johnson was "narrowly stated" as follows:

> [A] party who has entered into a written contract under a serious mistake about its contents in relation to a fundamental term will be entitled in equity to an order rescinding the contract if the other party is aware that circumstances exist which indicate that the first party is entering the contract under some serious mistake or misapprehension about either the content or subject matter of that term and deliberately sets out to ensure that the first party does not become aware of the existence of his mistake or misapprehension.[163]

Applying this statement, the contract was held to be voidable in equity. In subsequent decisions the view has been taken that the passage quoted above was not intended as a comprehensive statement of the circumstances in which mistake by a contracting party would attract equitable relief.[164] Ultimately the question to be determined is more general in nature; namely, whether it would be unconscionable for the non-mistaken party to take advantage of the mistaken party's mistake. The non-mistaken party may be said to have acted unconscionably even if he or she did not engage in deliberate acts of concealment.[165] In *Smith v Smith*,[166] Barrett J held that a party will be found to have deliberately set out to ensure that the mistaken party does not become aware of the existence of the mistake when they have either engaged in positive acts or omitted bringing the mistake to the mistaken party's attention.[167] Barrett J said:

> The essential elements are, first, that one person enters into a contract under a serious mistake about its content in relation to a fundamental matter; second, that the other party is aware that circumstances exist indicating that the first person is entering into the contract under a serious mistake about the content or subject matter of that aspect of the contract; and, third, that the second party deliberately sets out to ensure that the first party does not become aware of the existence of the mistake, either by positive acts or omitting to bring it to their attention.[168]

It has been held that the principle applied in *Taylor v Johnson* does not extend beyond mistakes relating to fundamental terms of a contract and does not apply to mistakes relating to factors influencing a party's decision to enter into a contract.[169] That is consistent with the discussion at [31.80] about mistakes relating to qualities of the subject matter. It is also

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162 *Taylor v Johnson* (1983) 151 CLR 422, 430–1.

163 *Taylor v Johnson* (1983) 151 CLR 422, 432.

164 See, eg, *Tutt v Doyle* (1997) 42 NSWLR 10, 14; *Blackley Investments Pty Ltd v Burnie City Council* [2010] TASSC 48, [64]; *Chwee Kin Keong v Digilandmall.com Pte Ltd* [2004] SGHC 71; [2004] 2 SLR 594, [73].

165 *Taylor v Johnson* (1983) 151 CLR 422, 433.

166 *Smith v Smith* [2004] NSWSC 663.

167 *Smith v Smith* [2004] NSWSC 663, [50]. See also *Moobi Pty Ltd v Les Gunn Properties Pty Ltd* [2008] NSWSC 719, [55] is another recent decision of the New South Wales Court in which it was held that failure to inform appears to have sufficed to satisfy the requirement that the non-mistaken party deliberately set out to ensure that the mistaken party did not become aware of the mistake.

168 *Smith v Smith* [2004] NSWSC 663, [50].

169 *Blackley Investments Pty Ltd v Burnie City Council (No 2)* [2011] TASFC 6, [12]–[23].

consistent with the discussion immediately below as to why the law draws a sharp distinction between mistakes as to price and mistakes as to value.

An insight from economic theory

[31.100] As a general rule, a mistake as to value of the subject matter, albeit serious and known to the other party, has no vitiating effect. For example, if A offers B a television set for $600, and B accepts the offer thinking the set is only six months old, when it is in fact four years old, there is a contract and the terms are that A is to sell that particular television to B for that particular price. Even if A is aware of B's mistake, the offer and acceptance coincide and the contract would normally stand, although A's awareness of B's mistake may see the contract rescinded in equity.

Why are courts prepared to set aside contracts on the ground of mistake concerning *price*, but generally not prepared to do so on the ground of mistake concerning *value*? We saw that the mistake in *Taylor v Johnson*[170] was basically a unilateral pricing error: Mrs Johnson, the vendor, thought the contract provided for a price per acre and Mr Taylor, the purchaser, knew that it did not. What of the situation where Taylor knew of a mine on Johnson's estate and, knowing that Johnson was ignorant of this fact, contracted for the purchase of the estate at half its real value? This would be a unilateral valuation error, and it seems that equity would not intervene to protect the seller.[171] Such a difference in approach is not easy to justify, although one judge has said that the non-disclosure of a valuation error is simply an example of free enterprise bargaining, while the non-disclosure of a pricing error is "just a shabby trick and indubitably unconscionable".[172]

Duggan has suggested that the distinction between the two instances is more readily understood from an economic perspective.[173] Drawing on the seminal work of Kronman,[174] he points to two competing efficiency considerations:

1. the desirability of preventing mistakes in the contracting process; and
2. the need to preserve incentives for the discovery and exploitation of economically useful information.

If issue (1) above were the only consideration, courts should compel any party who knows of the other party's error to correct the error, regardless of whether it related to pricing or valuation. However, issue (2) above is a countervailing consideration. If economically useful information, such as the mining potential of land, has to be disclosed in the interests of mistake prevention, then such information might remain undiscovered. This is because the lower the anticipated gains from exploration and discovery, the less likely it is that the exploration and discovery will actually take place. Valuable resources would be less likely to be exploited. On the other hand, a rule which favoured non-disclosure would allow the explorer to enjoy the gains derived from investment in exploration, thereby encouraging the investment. If issue (1) were given priority, information would be more evenly shared, but the cost would be less

170 *Taylor v Johnson* (1983) 151 CLR 422.

171 See [31.80].

172 *Deputy Commissioner of Taxation v Chamberlain* (1990) 26 FCR 221, 233 (Wilcox J).

173 Duggan, "Is Equity Efficient?" (1997) 113 *Law Quarterly Review* 601, 609–11. For a general discussion of economic analysis of law, see above [1.30]–[1.65].

174 Kronman, "Mistakes, Disclosure, Information, and the Law of Contracts" (1978) 7 *Journal of Legal Studies* 1.

information available in the first place. Note, however, that such reasoning rests on certain unspoken but significant assumptions, such as the parties' knowledge of the law and their propensity to act rationally in response to that law.[175]

Information involved in pricing error cases, such as *Taylor v Johnson*, is not economically valuable. Taylor's superior information was not wealth creating. It would merely have effected a redistribution of wealth, making Taylor wealthier at Johnson's expense. It would not cause the reallocation of the land to a more economically productive use.

So the question becomes one of mistake prevention: Which contracting party is the lower cost-information gatherer – the mistaken party or the party who knows the truth? Generally it will be the former, as reading the contract more carefully costs little and requiring the party who knows the truth to disclose it would encourage the mistaken party to be careless. Also, the informed person may be put to expense in uncovering the mistake or passing on the information. However, in the case of unilateral mistake, the informed person already knows of the other party's mistake, so that it would usually be cheaper for that party to correct the error. This, concludes Duggan, is why equity in such cases requires disclosure of pricing errors.[176]

Equity: rectification

[31.105] We have seen the courts have equitable power to *rectify* a contractual document where the document does not accurately record the *common intention* of the parties. In such a case, rectification cures *common mistake* by amending the contract. Rectification is also granted in cases of *unilateral mistake* where it would be unconscionable for the non-mistaken party to enforce the contract according to its terms. Unconscientious behaviour on the part of the non-mistaken party prior to the formation of the contract must be shown.

Leibler v Air New Zealand Ltd (No 2)[177] concerned an agreement for the sale by Ninth Astjet Pty Ltd (NAPL) to a subsidiary of Air New Zealand (ANZ) of shares comprising a half-interest in Jetset, a company that operated a travel agency. NAPL was a company controlled by Leibler. Clause 10.9 of the draft agreement gave Air New Zealand a right of pre-emption in respect of the remaining shares in the event that Leibler should die or become incapacitated. During further negotiations, it was agreed that the right of pre-emption would not be triggered by Leibler's death or incapacitation, but only by the Leibler family ceasing to control NAPL (which would, after the sale, retain half of the issued shares in Jetset). The parties agreed that clause 10.9 would be amended accordingly, but the purchaser's solicitors mistakenly deleted the clause entirely.[178] The trial judge (Hansen J) found that Leibler and NAPL knew of the mistake and "deliberately refrained from drawing the mistaken deletion to the attention of ANZ, because the deletion of the clause was seen as beneficial to their interests."[179] Hansen J held that the agreement should be rectified to include a right of pre-emption in the form of clause 10.9 with the amendments the parties had agreed would be made to that clause before

175 See further [9.245], where unspoken assumptions behind proposals for an efficient doctrine of estoppel are adumbrated. These assumptions are equally applicable in the present context.

176 See further Duggan, Bryan and Hanks, *Contractual Non-Disclosure* (1994), pp 148–57.

177 *Leibler v Air New Zealand Ltd (No 2)* [1999] 1 VR 1.

178 The headnote in the Victorian Reports mistakenly records that the purchaser's solicitors asked the vendor's solicitors to delete the clause.

179 *Leibler v Air New Zealand Ltd (No 2)* [1999] 1 VR 1, [65].

it was accidentally deleted. On appeal, Kenny JA (Winneke P and Philips JA agreeing) stated the principles which govern rectification for unilateral mistake as follows:

> If (1) one party, A, makes an agreement under a misapprehension that the agreement contains a particular provision which the agreement does not in fact contain; and (2) the other party, B, knows of the omission and that it is due to a mistake on A's part; and (3) lets A remain under the misapprehension and concludes the agreement on the mistaken basis in circumstances where equity would require B to take some step or steps, depending on those circumstances, to bring the mistake to A's attention; then (4) B will be precluded from relying upon A's execution of the agreement to resist A's claim for rectification to give effect to A's intention.[180]

The Court of Appeal held that the trial judge was entitled to conclude that these requirements were met, along with the additional requirement (omitted from the above list) that before the mistake was made the parties must have reached a consensus as to the provision to be included in the agreement.[181] The "unusual" circumstances of the case required the vendor to bring the mistake to the attention of the purchaser.[182] Those circumstances included the complexity of the transaction, the degree of trust involved, the fundamental importance of the omitted term and the fact that the deletion of the clause was totally inconsistent with the tenor of the negotiations.[183]

In line with the approach taken in relation to common mistake, the Australian cases also require a party seeing rectification for unilateral mistake to provide "convincing proof" of the mistake that is sought to be corrected.[184] In *Leibler v Air New Zealand Ltd (No 2)*, this requirement was met by reference to detailed evidence of the parties' negotiations regarding the clause.

Because cases of rectification for unilateral mistake are relatively uncommon, there is some uncertainty as to the elements that must be established to justify the granting of the remedy. The English Court of Appeal has observed that the precise scope of the principle "remains controversial".[185] The Court noted that rectification for unilateral mistake is at least available in a situation where the parties had a common intention which they communicated to one another, but "one party before executing the contract realised that the document did not give effect to that intention and changed their mind without telling the other party."[186] A particularly controversial question is whether it is necessary that, before the mistake was made, the parties had reached a consensus as to the provision which was the subject of the mistake. If there was no antecedent consensus then the effect of rectification is to hold the non-mistaken party to a bargain to which he or she did not assent.[187] This has been justified on the basis that it "is simply a consequence of the [non-mistaken party's] attempt to take

180 *Leibler v Air New Zealand Ltd (No 2)* [1999] 1 VR 1, [36].

181 *Leibler v Air New Zealand Ltd (No 2)* [1999] 1 VR 1, [70]–[73].

182 *Leibler v Air New Zealand Ltd (No 2)* [1999] 1 VR 1, [67].

183 *Leibler v Air New Zealand Ltd (No 2)* [1999] 1 VR 1, [67].

184 *Leibler v Air New Zealand Ltd (No 2)* [1999] 1 VR 1, [38]. *Sande v Medsara Pty Ltd* [2004] NSWSC 147, [6], following *Pukallus v Cameron* (1982) 180 CLR 447, 452.

185 *FSHC Group Holdings Ltd v Glas Trust Corporation Ltd* [2019] EWCA Civ 1361, [104].

186 *FSHC Group Holdings Ltd v Glas Trust Corporation Ltd* [2019] EWCA Civ 1361, [104], noting that these were the circumstances in which rectification was granted in *Thomas Bates & Son Ltd v Wyndham's (Lingerie) Ltd* [1981] 1 WLR 505.

187 Cf McLauchlan, "The 'Drastic' Remedy of Rectification for Unilateral Mistake" (2008) 124 *Law Quarterly Review* 608.

advantage of the [mistaken party's] blunder".[188] A number of textbook writers favour the view that an antecedent agreement on the issue in question is not required.[189] If that is the case then rectification for unilateral mistake is properly considered a "drastic" remedy,[190] the availability of which must be strictly limited.[191]

MISTAKE AS TO IDENTITY

[31.110] The cases involving mistake as to identity clearly lend themselves to an offer and acceptance analysis. Nevertheless, this area of law is unsettled. In fact, the cases in this area have been described as "either irreconcilable or decided on the basis of fine distinctions that are a reproach to the law".[192]

The case law dealing with the specific issue of mistaken identity is mainly English and quite old. To some extent, this limits its utility as the principles may reflect a different understanding of contract law to the predominantly objective approach adopted today. In fact, some claim that mistakes regarding identity are today resolved by applying the more general principles outlined above than the specific case law below.[193] When reading through the descriptions of the facts and outcomes in the cases below, consider whether the outcome would be the same applying the approaches outlined above.

The case law in this area may be conveniently divided into two categories:

1. cases where the parties are not face to face; and
2. cases where the parties are face to face (*inter praesentes*).

Parties not face to face

[31.115] In *Cundy v Lindsay*,[194] a rogue called Alfred Blenkarn sent an order for handkerchiefs to Messrs Lindsay, giving his address as 37 Wood Street, Cheapside. He signed his name in such a way as to make it look like Blenkiron & Co, a firm known to Lindsay and located at 123 Wood Street, was ordering the goods. Lindsay sent the goods to Blenkiron & Co at 37 Wood Street. Blenkarn took possession of the goods. He did not pay for them and sold them to Cundy. Lindsay sued Cundy in conversion. The House of Lords held that the action should succeed. The issue was resolved at common law – it was held that there was no contract between Lindsay and Blenkarn. Lindsay intended to deal with Blenkiron, not Blenkarn. They knew nothing of Blenkarn. As there was no contract between Blenkarn and Lindsay, no title in the handkerchiefs passed to Blenkarn. Blenkarn, in turn, could pass no title to Cundy. Cundy therefore had no right to possess the handkerchiefs, and Lindsay's action in conversion was successful.

188 *Littman v Aspen Oil (Broking) Limited* [2005] EWCA Civ 1579, [24].

189 See, eg, Hodge, *Rectification: The Modern Law and Practice Governing Claims for Rectification for Mistake* (2010), [4-89]–[4-91]; Peel, *The Law of Contract* (14th ed, 2015), [8-070]; Heydon, *Heydon on Contract* (2019), [30.490]–[30.500].

190 *Agip SpA v Navigazion Alta Italia SpA (The "Nai Genova")* [1984] 1 Lloyd's Rep 353, 365.

191 See, eg, Heydon, *Heydon on Contract* (2019), [30.530] (arguing that rectification will not be granted merely because one party has entered into a contract knowing that the other party is mistaken).

192 McLauchlan, "Mistake of Identity and Contract Formation" (2005) 21 *Journal of Contract Law* 1, 1.

193 *Halsbury's Laws of Australia*, [7.2.700].

194 *Cundy v Lindsay* (1878) 3 App Cas 459.

The opposite conclusion was reached in *Kings Norton Metal Co Ltd v Edridge Merrett & Co*.[195] A rogue called Wallis wrote to the plaintiffs on impressive note paper bearing the name Hallam & Co, asking for a quotation of prices for brass rivet wire. The prices were quoted and "Hallam & Co" ordered the wire, which was delivered, but not paid for. In fact, Hallam & Co did not exist and was only a cloak for Wallis. The wire was sold by Wallis to the defendant and the plaintiff sued the defendant in conversion. The trial judge held there was a contract between the plaintiff and the person who wrote the letters and, under this contract, property in the goods passed. When Wallis sold the goods to the defendant, the defendant received a good title as the sale took place before the plaintiff rescinded the contract between itself and Wallis. The Court of Appeal upheld this decision. AL Smith LJ said the question was:

> With whom … did the plaintiffs contract to sell the goods? Clearly with the writer of the letters. If it could have been shown that there was a separate entity called Hallam & Co and another entity called Wallis, then the case might have been within the decision in *Cundy v Lindsay*.[196]

In an earlier case, there was no rogue involved. The defendant in *Boulton v Jones*[197] sent an order to Brocklehurst for some pipe hose. At the time Brocklehurst, who had dealings with Jones before, owed Jones money. Brocklehurst had just sold his business to Boulton, his foreman. Boulton sent the goods and Jones used them. However, when an invoice was later sent to Jones, he refused to pay. The court held he was justified. Jones intended to contract with Brocklehurst, and Boulton had misled him by executing the order. The judges stressed that the identity of the supplier was important here because the supplier owed the defendant money; the defendant could have claimed a set-off against a claim by Brocklehurst but not against a claim by Boulton.

In a more recent House of Lords decision, *Shogun Finance Ltd v Hudson*,[198] a rogue dishonestly obtained the driver's licence of a Mr Durlabh Patel and used it to acquire a car on hire-purchase from Shogun. The transaction was arranged through a car dealer who sent to Shogun an application form (on which the rogue had forged Patel's signature) and a copy of Patel's driver's licence. Shogun checked Patel's credit and employment records before approving the transaction and authorising the dealer to deliver the car to the rogue. The rogue sold the car to Hudson and then disappeared. Shogun claimed that it remained the owner of the car on the basis that the rogue was not able to pass title to Hudson under the *nemo dat quod non habet* rule (one cannot give what one does not have). Hudson was entitled to the benefit of a statutory exception to the nemo dat rule if he could establish that a contract (even a voidable contract) had been made between the rogue and Shogun. The House of Lords held (3-2) that the contract was void and so Hudson did not obtain title to the car. First, as a matter of construction, the contract was clearly expressed to be one made between Patel and Shogun. In a consumer credit agreement such as this, the identity of the consumer is fundamental, since credit is given on the basis of the consumer's credit rating. Extrinsic evidence was not admissible to show that the contract was in fact made with the rogue. Secondly, there was no consensus ad idem between Shogun and the rogue. Shogun intended

195 *Kings Norton Metal Co Ltd v Edridge Merrett & Co* (1897) 14 TLR 98.

196 *Kings Norton Metal Co Ltd v Edridge Merrett & Co* (1897) 14 TLR 98, 99.

197 *Boulton v Jones* (1858) 27 LJ Ex 117; 157 ER 232.

198 *Shogun Finance Ltd v Hudson* [2003] UKHL 62; [2004] 1 AC 919. For detailed analysis of this case and the earlier authorities, see McLauchlan, "Mistake of Identity and Contract Formation" (2005) 21 *Journal of Contract Law* 1.

to contract only with Patel and the rogue had no contractual intention at all. Lord Nicholls and Lord Millett dissented on the basis that *Cundy v Lindsay* was wrongly decided and the law should recognise the formation of a contract whenever two parties agree on terms, even if they do not meet face to face. On this view, a voidable contract would have been formed between Shogun and the rogue.

Parties face to face (inter praesentes)

[31.120] When parties are face to face, and one party has assumed a false name, it will be presumed that the mistaken party is intending to contract with the person physically present. In *Lewis v Averay*,[199] Lewis owned a car which he wanted to sell. He showed it to a rogue who came to his flat and claimed to be Richard Greene, a well-known actor. The parties agreed on a price, but when the rogue wrote out a cheque, Lewis was unwilling to hand over the car until the cheque was cleared. He asked the rogue for proof of identity, and the rogue produced a photographic pass from a film studio. Lewis was satisfied and handed over the car, but the cheque was later dishonoured. The rogue sold the car to Averay, an innocent purchaser. Lewis claimed the car was still his and sued Averay for conversion. The action failed.

The Court of Appeal held that there was a contract between Lewis and the rogue, under which property passed to the rogue and later to Averay. Lord Denning MR stated his view as follows:

> When two parties have come to a contract – or rather what appears on the face of it to be a contract – the fact that one party is mistaken as to the identity of the other does not mean there is no contract, or that the contract is a nullity and void from the beginning. It only means that the contract is voidable, that is liable to be set aside at the instance of the mistaken party, so long as he does so before third parties have in good faith acquired rights under it.[200]

Lord Denning rejected certain distinctions which had found some favour in this area of law. First, he rejected the distinction between mistake as to identity and mistake as to attributes – the former rendering the contract void, the latter not. A person's name, he said, is an attribute and, at the same time, a key to the person's identity. Secondly, he rejected the distinction between a contract of sale concluded just before the rogue's fraudulent misrepresentation was made (property passes) or just after (property does not pass). His Lordship considered that a third party's rights should not depend on such refinements. It was the original owner, the plaintiff, who let the rogue have the goods and enabled him to dupe the defendant, an innocent purchaser. The plaintiff should therefore not be able to recover.

Of the other judges in this case, Megaw LJ came to exactly the same conclusion as Lord Denning using the identity/attributes distinction. The mistake here, he held, was as to an attribute, namely creditworthiness, not as to identity. The plaintiff intended to contract with the person physically before him. The identity of the buyer was not in itself of vital importance to the plaintiff's decision to contract. Rather, confirmation of identity was sought only as an aid to assess the creditworthiness of the purchaser. Therefore, property passed. The third judge, Phillimore LJ, said, "I do not think there was anything which could displace the prima facie presumption that Mr Lewis was dealing with the gentleman present there in the flat – the rogue".[201]

199 *Lewis v Averay* [1972] 1 QB 198.

200 *Lewis v Averay* [1972] 1 QB 198, 207.

201 *Lewis v Averay* [1972] 1 QB 198, 208.

Lewis v Averay was preceded by two other cases which were factually very similar, but in which the results varied. In *Phillips v Brooks*,[202] a rogue who posed as Sir George Bullough of St James's Square induced a jeweller to let him take away a ring in exchange for a cheque. In *Ingram v Little*,[203] a rogue who posed as PGM Hutchinson of Caterham induced three people to deliver over their car in exchange for a cheque. In both cases, the cheque was subsequently dishonoured and the claim of the duped owners was made against an innocent third party – in the first case a pawnbroker and in the second case a car dealer. In *Phillips v Brooks* (like *Lewis v Averay*), the claim failed, whereas in *Ingram v Little* (by a majority), the claim succeeded.

Considerable ingenuity has been expended by scholars and students in reconciling these contrasting results. The distinctions deprecated by Lord Denning have been invoked for this purpose – mistake as to attributes in *Phillips v Brooks* as against mistake as to identity in *Ingram v Little* or fraudulent misrepresentation as to identity made by the rogue just after offer made and contract concluded in *Phillips v Brooks* but just before final offer made and contract concluded in *Ingram v Little*.[204] It has been suggested that the innocent third party in *Ingram v Little* (car dealer) was a superior loss bearer.[205]

In the House of Lords decision in *Shogun Finance v Hudson*,[206] a majority of the House of Lords confirmed that, where parties are dealing face to face, there is at least a strong presumption that they intend to contract with one another. Accordingly, a majority either expressly or implicitly took *Ingram v Little* to have been wrongly decided[207] and preferred the approach adopted in *Phillips v Brooks Ltd*. This is consistent with the approach taken in a recent South Australian case, where *Lewis v Averay* was followed.[208] A similar approach was adopted by the New South Wales Court of Appeal in *MacMillian v Mumby*.[209] The plaintiff loaned money to a non-existent company, Appliance Sales & Rentals, which he thought was owned by the respondents. In fact, Appliance Sales & Rentals was a business name used by a company owned by the respondents. The Court of Appeal found for the plaintiff on the basis that it was clear that the respondent had intended to invest money in the business that was being operated by the respondents and that the name of the company was not important to him.

In his dissenting judgment in *Ingram v Little*, Devlin LJ adopted a different approach and stated that the relevant question in this sort of case is not whether the original contract is void or voidable, but which of two innocent parties shall suffer for the fraud of a third. His view was:

> [T]he loss should be divided between them in such proportion as is just in all the circumstances. If it be pure misfortune, the loss should be borne equally; if the fault or imprudence of either party has caused or contributed to the loss, it should be borne by that party in the whole or in the greater part.[210]

202 *Phillips v Brooks* [1919] 2 KB 243.

203 *Ingram v Little* [1961] 1 QB 31.

204 Greig and Davis, *The Law of Contract* (1987), pp 902–3.

205 Adams and Brownsword, *Understanding Contract Law* (5th ed, 2007), p 67.

206 *Shogun Finance v Hudson* [2003] UKHL 62; [2004] 1 AC 919, [36], [80], [170].

207 *Shogun Finance v Hudson* [2003] UKHL 62; [2004] 1 AC 919, [87], [185]; McLauchlan, "Mistake of Identity and Contract Formation" (2005) 21 *Journal of Contract Law* 1.

208 *Papas v Bianca Investments Pty Ltd* [2002] SASC 190; (2002) 82 SASR 581.

209 *MacMillian v Mumby* [2006] NSWCA 74.

210 *Ingram v Little* [1961] 1 QB 31, 73–4.

However, the English Law Reform Committee, shortly after *Ingram v Little* was handed down, opted in favour of the innocent third party: "Where goods are sold under mistake as to the buyer's identity, the contract should, so far as third parties are concerned, be voidable and not void."[211] This reform, which would have reversed *Cundy v Lindsay*,[212] has not been implemented.

What if a rogue C induces A by means of impersonation to believe that he is B, the registered proprietor of land, and induces A to lend him money secured by a forged mortgage on B's land? In such a case, a particular attribute (ownership of land) would be important in determining to whom the offer of loan was made. Would the resultant contract be void? In *Porter v Latec Finance (Qld) Pty Ltd*,[213] Windeyer J expressed the opinion that such a contract of loan was void "only with (B) could the contract proposed, a loan on mortgage of his land, have been made".[214] So also Kitto J, even assuming C appeared in person before A, "[t]he grant of the loan … was implicitly if not expressly on the condition precedent that the recipient was identical with the registered proprietor".[215]

Barwick CJ, on the other hand, drew a distinction between an agreement to lend, which would be void, and an executed loan. In the latter instance, "the borrower, if sued by the lender, could not escape liability for money lent and for performance of the terms of the loan by asserting he did not agree to repay and on the agreed terms".[216]

The presumption of dealing with the person present might also be rebutted where a rogue pretends to be acting as an agent for a principal. There will be no contract with the rogue, as the duped person would have had no intention to contract with him or her personally. Nor will there be a contract with the principal, as the agent would have no authority to bind the principal.[217]

MISTAKES IN ELECTRONIC TRANSACTIONS

[31.125] Commonwealth legislation, as well as legislation in the States and Territories, may provide relief where a natural person makes an "input error" in the course of a transaction with an automated system.[218] Where the system provides no opportunity to correct an "input error", the person making the error is entitled to "withdraw the portion of the communication in which the input error was made", provided he or she does so as soon as possible after learning of the error, and provided he or she has not received any material benefit from goods or services provided by the other party. The legislation specifically provides that the right

211 Twelfth Report (Cmnd 2958, 1966).

212 *Cundy v Lindsay* (1878) 3 App Cas 459.

213 *Porter v Latec Finance (Qld) Pty Ltd* (1964) 111 CLR 177.

214 *Porter v Latec Finance (Qld) Pty Ltd* (1964) 111 CLR 177, 201.

215 *Porter v Latec Finance (Qld) Pty Ltd* (1964) 111 CLR 177, 194.

216 *Porter v Latec Finance (Qld) Pty Ltd* (1964) 111 CLR 177, 183.

217 *Hardman v Booth* (1863) 1 H&C 803; 158 ER 1107; *Roache v Australian Mercantile Land & Finance Co Ltd* [1965] NSWR 1015.

218 *Electronic Transactions Act 2001* (ACT), s 14D; *Electronic Transactions Act 1999* (Cth), s 15D; *Electronic Transactions Act 2000* (NSW), s 14D; *Electronic Transactions (Northern Territory) Act* (NT), s 14D; *Electronic Transactions (Queensland) Act 2001* (Qld), s 26D; *Electronic Communications Act 2000* (SA), s 14D; *Electronic Transactions Act 2000* (Tas), s 12D; *Electronic Transactions (Victoria) Act 2000* (Vic), s 14D; *Electronic Transactions Act 2011* (WA), s 20. See also [3.41].

to withdraw a portion of an electronic communication is not a right to rescind a contract. The consequences of withdrawal of the relevant portion of the communication are to be determined in accordance with applicable legal rules, but clearly in some circumstances, this will undermine the validity of the contract. If, for example, a consumer booking a ticket for air travel over the Internet accidentally booked a flight for the wrong date and was not given an opportunity to correct the error, the withdrawal of that portion of the communication would undermine the validity of the contract, since the withdrawn communication identified the subject matter of the contract.

CHAPTER **32**

Misrepresentation

OVERVIEW AND CONTEMPORARY RELEVANCE

[32.05] A misrepresentation is a false statement made expressly or impliedly by one party (the *representor*) to another (the *representee*) that acts as an inducement to the latter to enter into a contract with the former. As a general rule, in order to obtain relief, the representee must show that he or she was misled by and relied on a positive misrepresentation of fact by the representor. In an appropriate case, the representee can claim either rescission of the contract or damages and, in some cases, both forms of relief. These remedies are available under the general law, that is, at common law or in equity.

Rescission is the principal remedy for misrepresentation. Rescission means the contract is set aside ab initio (from the beginning). The parties are restored to the status quo ante (the position they were in before the contract was entered into). There are, however, various limits to this form of relief. In particular, substantial restoration of the parties to their pre-contractual positions is required and may not be impossible, or a third party may have acquired property rights in the subject matter of the contract.

Damages are available at common law only if a tort is established. The relevant torts are deceit and negligence. These torts require proof of culpability in the making of the false statement: fraud in the case of deceit, carelessness in breach of a duty of care in the case of negligence. They also require proof of other elements including reliance and actual damage.

If the representor sues the representee seeking specific performance, then the representee may rely on the misrepresentation as a defence.

In this chapter, we examine the elements of misrepresentation under the general law. The remedy of rescission is discussed in Chapter 39.

General law misrepresentation is not as important to contracting parties today as it was in the past. In recent years, statutory law has become the most important source of relief

for representees.[1] Section 18(1) of the *Australian Consumer Law* (ACL) prohibits *misleading or deceptive conduct in trade or commerce*. Representees who suffer loss as a result of a contravention of these provisions have access to a wide range of remedies under the legislation, including, but not restricted to, damages and rescission. The relevant law is examined in Chapter 33. There has been a veritable flood of reported decisions under the legislation. As French CJ and Kiefel J recently noted in *Miller & Associates Insurance Broking Pty Ltd v BMW Finance Australia Limited*, the frequent invocation of the statutory prohibition "reflects its simplicity relative to the torts of negligence, deceit and passing off".[2]

Although the general law of misrepresentation has been somewhat overshadowed by the legislation and the litigation it has generated, it remains important for at least three reasons. First, the legislation only applies where the person who engaged in misleading conduct did so "in trade or commerce". Thus, the general law may be the only source of relief for a representee who has been induced to enter into a contract outside the commercial and consumer contexts. Secondly, concepts formulated in the context of the general law are often adopted or adapted by judges in their interpretation of the legislative provisions. Thirdly, in practice, general law misrepresentation is routinely relied upon by litigants as an alternative to misleading or deceptive conduct and relief is sometimes granted under the general law, even where the ACL applies.[3]

POSITIVE MISREPRESENTATION OF FACT

Misrepresentation of fact

[32.10] The cases in this area of law are widely regarded as supporting a general rule that for a representee to succeed in an action based on misrepresentation, the representation must be a statement of existing or past fact.[4] This general rule applies whether the representation is written, oral or implied by conduct. The requirement of existing or past *fact* excludes other types of statements, such as mere puffs, statements of opinion or future intent and representations of law.

The rationale of the general rule appears to be that only facts are true or untrue at the time a statement is made and that while it is reasonable to rely on statements of fact, it is not reasonable to rely on other kinds of statement. *Puffs* are just sales talk and not meant to be taken seriously. A person's *opinion* should not be relied on unless that person is prepared to warrant its accuracy and give it contractual force. The same could be said of statements of *future intention*. As for statements of *law*, it is sometimes said, with little conviction, that everyone is presumed to know the law. Alternatively, and with slightly more conviction, it could be argued that, as everyone has access to the law and legal advice, no-one should rely on another person's statement (at least a layperson's statement) as to what the law is. A final argument might be that the law is so uncertain that no statement about its content can be taken as anything more than an expression of opinion.

1 See [2.75] and Chapter 33.
2 *Miller & Associates Insurance Broking Pty Ltd v BMW Finance Australia Limited* [2010] HCA 31; (2010) 241 CLR 357, [5].
3 See, eg, *Vadasz v Pioneer Concrete (SA) Pty Ltd* (1995) 184 CLR 102, discussed at [39.45].
4 *Given v Pryor* (1979) 39 FLR 437, 441.

The restriction of the concept of misrepresentation to representations of fact has often proved to be unsatisfactory. The courts have frequently found it necessary to unearth implied statements of fact lurking behind expressions of opinion and expressions of future intention. Moreover, the law of torts relating to negligent statements rejects the distinction between statements of fact and those of opinion. It covers both untrue information and unsound advice. As for the distinction between fact and law, it no longer commands respect and is being increasingly abandoned by the courts.[5]

It can be argued that, instead of asking whether a representor made a statement of fact, the appropriate question is whether the conduct of the representor was such as might reasonably be relied upon by the representee.[6] This test avoids drawing awkward distinctions between statements of fact and other types of statement. Certainly, in the tort of negligence, the reasonableness of the representee's reliance is a crucial element, rather than the nature of the careless statement as one relating to fact. On the other hand, in the tort of deceit, the nature of the statement as one relating to fact remains crucial.

If a statement is ambiguous, it will first have to be determined what it means before it can be determined whether it is false. In such a case: "[T]he sense in which a representation would be understood by a reasonable person in the position of the representee is prima facie the sense relevant to the question whether the representation is false."[7]

Where the representation is made directly to the representee, the experience of the representee will be considered to determine how the representation is likely to be understood. Thus, the same statement made directly to several specific representees may be treated as having a different meaning in different contexts.[8] When determining whether a representation is false, the intentions of the representor are not relevant. The representor's intentions are relevant to determining whether he or she acted fraudulently.

Puffs and opinions

[32.15] A statement of opinion may be mere sales talk or it may be a statement of belief. Alternatively, it may involve a statement of fact. Sales talk is characterised by extravagant and colourful language that no reasonable person would take literally. To say of a house that it is "charming and located in an area much sought after by people of discriminating taste" is an example of a mere puff.[9]

In *Mitchell v Valherie*,[10] the Court considered whether the statements "Cosy – Immaculate Style" and "Nothing to Spend – Perfect Presentation" contained in a brochure advertising the sale of a home amounted to misrepresentations. The purchaser of the house unsuccessfully argued that these words, in particular the words "Nothing to Spend", represented to prospective buyers that there were no serious faults at the date of inspection. White J held that the words could not be understood as conveying such a representation of fact for several reasons. First, their true nature was a pithy promotion of the property. Secondly, the phrase "Nothing to Spend – Perfect Presentation" had to be read as a whole. The words "Nothing to

5 See [32.25].
6 Greig and Davis, *The Law of Contract* (1987), p 827.
7 *Krakowski v Eurolynx Properties Ltd* (1995) 183 CLR 563, 576–7.
8 *Vickers v Taccone* [2005] NSWSC 514, [11], applying the majority judgment in *Butcher v Lachlan Elder Realty Pty Ltd* [2004] HCA 60; (2004) 218 CLR 592.
9 *Simplex commendatio non obligat* (a simple commendation does not bind).
10 *Mitchell v Valherie* [2005] SASC 350; (2005) 93 SASR 76.

Spend" take their colour from the words "Perfect Presentation", which was clearly a phrase of puffery. Thirdly, the words were used in circumstances where some hyperbole is commonplace. A reasonable purchaser would not understand the words to convey a representation about the structural integrity of the property.[11] Layton J was prepared to recognise that the phrase "Nothing to Spend" amounted to a representation of fact. However, the only representation that was made by the phrase was that a buyer could move in with no need to spend money on improving the presentation of the house. The phrase said nothing about whether the house was structurally sound.[12] However, if a statement, albeit extravagant, is characterised by precise or specific assertions, or proves to be blatantly false, it may be classified as a statement of fact. The more specific the words are, the less likely it is that they will be regarded as mere puffery.[13] That said, even words that appear quite general in nature may amount to a representation. In *Pryor v Given*,[14] the Court held that although the statement "A wonderful place to live" contained in an advertisement for land was probably intended as mere puffery (in so much as it involved the use of exaggerated sales talk), it nevertheless conveyed the impression that the land was zoned for urban use and that constituted a statement of fact.

A statement of opinion may be merely a statement of belief. This is particularly so where the person making the statement, to the knowledge of the person to whom the statement is made, has no personal knowledge of facts upon which the belief is based; in other words, where both parties are in a position to draw their own conclusions. In *Bisset v Wilkinson*,[15] Bisset was selling a holding in New Zealand to Wilkinson. The holding had not been used as a sheep farm and Wilkinson knew this. The Court held that a statement by Bisset that the land would support 2000 sheep, albeit wrong, was merely a statement of opinion.

A statement of opinion may imply a statement of fact. A person who states an opinion always implies that he or she in fact holds that opinion.[16] If the opinion is not held, there is a misrepresentation of fact. For example, if a person who has no belief about the age of a house, or alternatively believes it is 14 years old, says, "I believe that house is 10 years old", there is a misrepresentation as to the person's belief in both instances. Where the facts upon which the opinion is based are particularly within the knowledge of the person expressing the opinion, there is a representation that he or she has knowledge or reasonable grounds to justify holding the opinion. For example, in *Smith v Land & House Property Corp*,[17] a vendor described a tenant as "a most desirable tenant" when the tenant was in fact in arrears of rent. The vendor's statement implied that he had grounds that justified his opinion. He had no such grounds and his statement was held to be a misrepresentation.

Statement as to the future

[32.20] A statement or promise that something will happen in the future is not a misrepresentation simply because that thing does not happen. However, every promise,

11 *Mitchell v Valherie* [2005] SASC 350; (2005) 93 SASR 76, [79]–[81].

12 *Mitchell v Valherie* [2005] SASC 350; (2005) 93 SASR 76, [119]–[121].

13 *Eveready Australia Pty Ltd v Gillette Australia Pty Ltd (No 4)* [1999] FCA 1824, [59].

14 *Pryor v Given* (1980) 30 ALR 189.

15 *Bisset v Wilkinson* [1927] AC 261.

16 *Fitzpatrick v Michel* (1928) 28 SR (NSW) 285, 288–9.

17 *Smith v Land & House Property Corp* (1884) 28 Ch D 7. See further *Ritter v North Side Enterprises Pty Ltd* (1975) 132 CLR 301.

whether contractual or pre-contractual, implies a representation of fact, namely that there is a present intention to fulfil the promise. If there is no such intention, a misrepresentation is established.[18] For example, in *Edgington v Fitzmaurice*,[19] the directors of a company said that money lent to the company would be used to complete alterations to the company's buildings. In fact, the directors intended to use the money to pay off the company's debts. It was held that they had misstated a fact: the state of their intentions. Bowen LJ made the following oft-quoted comment:

> [T]he state of a man's mind is as much a fact as the state of his digestion. It is true that it is very difficult to prove what the state of a man's mind at a particular time is, but if it can be ascertained it is as much a fact as anything. A misrepresentation as to the state of a man's mind is therefore a misstatement of fact.[20]

Sometimes a statement expressed in terms of the future is really a representation of fact. In *Balfour v Hollandia Ravensthorpe NL*, Bray CJ illustrated this point:

> If I say that a department store is selling certain goods at 15 per cent discount, that is a statement in the present tense and a representation of an existing fact; if I say "if you go to that department store, they will sell you the goods in question at a discount of 15 per cent", that is a statement in the future tense, but it is none the less a representation of an existing fact. It means exactly the same as the first statement.[21]

Statements of law

[32.25] The exclusion of misstatements of law from the concept of misrepresentation is difficult to justify. The exclusion has been undermined by the ruling of the High Court in *David Securities Pty Ltd v Commonwealth Bank of Australia*[22] that in a restitutionary claim for recovery of money paid under mistake it is no bar to recovery that the mistake was one of law. If mistake of law provides a basis for a restitutionary claim, a misrepresentation of law should equally provide a basis for rescission. Moreover, in reference to the doctrine of estoppel, it has been stated that the distinction between assumptions as to law and as to fact "is artificial and elusive … So it would be productive only of confusion and arid technicality to restrict the operation of the doctrine so as to exclude from its scope an assumption as to a purely legal state of affairs".[23] In England, it has been recognised that a misrepresentation of law is now actionable.[24] Since the two rules developed together, the "misrepresentation of law" rule in contract could not survive the demise of the "mistake of law" rule in restitution.[25]

In any event, a fraudulent misrepresentation of law is recognised as providing a basis for relief. This can be explained on the basis that a statement of law implies a representation

18 *Beach Petroleum NL v Johnson* (1993) 43 FCR 1, 40.

19 *Edgington v Fitzmaurice* (1885) 29 Ch D 459.

20 *Edgington v Fitzmaurice* (1885) 29 Ch D 459, 483.

21 *Balfour v Hollandia Ravensthorpe NL* (1978) 18 SASR 240, 252.

22 *David Securities Pty Ltd v Commonwealth Bank of Australia* (1992) 175 CLR 353, 376, discussed at [10.95].

23 *Commonwealth v Verwayen* (1990) 170 CLR 394, 413.

24 *Pankhania v London Borough of Hackney* [2002] EWHC 2441 Ch, [58], quoted with approval in *Brennan v Bolt Burdon* [2004] EWCA Civ 1017; [2005] QB 303, [10].

25 *Pankhania v London Borough of Hackney* [2002] EWHC 2441 Ch, [58], quoted with approval in *Brennan v Bolt Burdon* [2004] EWCA Civ 1017; [2005] QB 303, [10].

of fact, that is, that the person professing to expound the law believes it to be as stated.[26] Moreover, the rule excluding misrepresentations of law, if it still operates, appears to apply only to misrepresentations about the general law. Representations as to private rights, such as the powers possessed by a company under a private Act of Parliament, or as to a person's title to land, appear to be treated as misrepresentations of fact.[27] Further, representations as to foreign law are classified as representations of fact.[28]

Positive misrepresentation

[32.30] As a general rule, there is no duty imposed on one contracting party to disclose material facts to the other prior to the contract. Silence is not a basis for relief. In the absence of a positive misrepresentation, the *caveat emptor* (let the buyer beware) rule applies.[29] This rule represents the spirit of individualism in contract law. It places a high value on the self-reliance of the individual. It provides an economic incentive for investment in the acquisition of skill and knowledge. A person who has invested in the acquisition of skill and knowledge should be able to use those advantages when negotiating a contract. However, the economic investment argument is not always appropriate. A person may acquire information by chance, rather than by research. Further, the personal relationship between parties may be such as to render the incentive argument inappropriate. Nevertheless, it has been argued that while theories that emphasise informed consent and greater information sharing in the interests of fairness are relevant in explaining and moulding the law of non-disclosure, such theories are likely to result in reduced information production.[30]

There are important qualifications to the general rule of non-disclosure. First, there are instances when a failure to speak creates a false impression in the circumstances. Secondly, a duty of disclosure may arise by virtue of the special relationship between the parties or by virtue of the nature of the proposed contract.

False impressions

[32.35] Although a person may say nothing, a false impression may be created by conduct. For example, signing a cheque implies that the cheque is good for the amount stated, even though this may not be true. In certain circumstances, a mere nod, smile or wink may amount to an implied positive misrepresentation.[31]

There is a duty of disclosure in the following situations:

1. Although a person makes a statement that is literally true, it may create a false impression by telling only half the truth. The statement may imply, falsely, that there are no other facts that qualify the statement. For example, a vendor of land who tells a purchaser that

26 *Public Trustee v Taylor* [1978] VR 289.

27 *Derry v Peek* (1889) 14 App Cas 337; *West London Commercial Bank v Kitson* (1884) 13 QBD 360.

28 *Andre & Cie v Ets Michel Blanc & Fils* [1979] 2 Lloyds LR 427, 430–1.

29 *Smith v Hughes* (1871) LR 6 QB 597, 604, 606; *W Scott Fell and Co Ltd v FH Lloyd* (1906) 4 CLR 572.

30 For an in-depth examination of this topic, see Duggan, Bryan and Hanks, *Contractual Non-disclosure* (1994). See also [31.125].

31 *Walters v Morgan* (1861) 3 De GF & J 718, 723–4; 45 ER 1056.

all the farms on the land are "fully let", but fails to add that the tenants have given notice to quit, has clearly created a false impression.[32]

2. Events that occur subsequently to the making of a statement, but before the contract is entered into, may affect the characterisation of the statement.
   (a) A representation which was true when made may be falsified, to the knowledge of the representor, by later events.
   (b) A representation believed to be true when made, may later be discovered by the representor to be false.

In both instances (a) and (b), the silence of the representor cannot be justified and a duty to disclose the truth to the representee arises.[33]

In *Jones v Dumbrell*,[34] Dumbrell represented to Jones in September that he desired to purchase his shares in a company in which they both held shares. He indicated that he did not intend to resell the shares as he proposed to conduct the company's business for the benefit of his family. Jones, who did not wish to sell to an outsider, sold the shares to Dumbrell at an undervalue. Dumbrell did not disclose to Jones that from November until the completion of the sale he intended to purchase the share in order to resell them at a profit. The Court held that Dumbrell was liable for damages in deceit. Although his original statement of intention in September was not proved to be false, it had become false to his knowledge by the time the contract was concluded.

Even if a representor does not know that new developments have falsified an earlier statement, a court may be able to give relief to the representee by implying a condition in the offer that there has been no change in the situation.[35]

Special contracts and relationships

Contracts of insurance

[32.40] A contract of insurance is classified as a contract *uberrimae fidei* (of utmost good faith).[36] There are statutory provisions dealing with the duties of disclosure owed by insured persons to insurers.[37] A duty is imposed on a person applying for insurance to disclose all material facts[38] known to him or her.[39] This duty is imposed in order to ensure that the parties enter the contract on a reasonably equal footing. An insurance company may well have substantial resources and expertise, but its knowledge of the risks relating to a particular applicant for insurance is based on information provided by the applicant. It needs this knowledge in order to determine whether to take the risk or not and how to set the premium.

32 *Dimmock v Hallett* (1866) LR 2 Ch App 21. For another example, see *Curtis v Chemical Cleaning and Dyeing Co* [1951] 1 KB 805, [12.15].

33 *Davies v London & Provincial Marine Insurance Co* (1878) 8 Ch D 469, 475; *Jones v Dumbrell* [1981] VR 199, 203.

34 *Jones v Dumbrell* [1981] VR 199.

35 See *Financings Ltd v Stimson* [1962] 1 WLR 1184, [3.60].

36 The development of a general duty of good faith is examined in Chapter 14.

37 See *Marine Insurance Act 1909* (Cth), s 24; *Insurance Contracts Act 1984* (Cth), s 21.

38 The matters that must be disclosed are more precisely defined in the *Insurance Contracts Act 1984* (Cth), s 21(1).

39 In relation to marine insurance the duty of disclosure extends to what *should* be known: *Marine Insurance Act 1909* (Cth), s 24(1).

Contracts of guarantee

[32.45] Contracts of guarantee are not contracts *uberrimae fidei* in the sense of requiring full disclosure of all material facts, but a limited duty of disclosure is imposed.[40] Contracts of guarantee arise out of a three-party situation. There is a creditor, debtor and guarantor. The contract is between two of the parties – the guarantor and the creditor. The guarantor promises the creditor to make good the defaults of the debtor and, in return, the creditor confers a benefit, such as an increase in credit or an extension of time to repay, on the debtor. Generally, the creditor does not go to the guarantor and explain the risk to be run. The guarantor often gives the guarantee from motives of friendship to the debtor and knows the risk or can find out what the risk is from the debtor.[41] An insurer, on the other hand, is exclusively dependent on the insured for knowledge of circumstances that affect the risk.

The rule concerning contracts of guarantee:

> requires disclosure of facts only if concealment of those facts would otherwise misrepresent the transaction which the guarantor is undertaking to guarantee. In general, it would only be the non-disclosure of those circumstances *which were not naturally to be expected* which would misrepresent the material features of that transaction.[42]

In *Westpac Banking Corporation v Robinson*,[43] it was held that the bank was under no duty to disclose to a prospective guarantor of a customer's account that the account had been overdrawn. Where a guarantee is required, it is "naturally to be expected" that the bank is not satisfied with the customer's credit. On the other hand, in *Commercial Bank of Australia v Amadio*,[44] it was held by Gibbs CJ that the bank was bound to reveal to the guarantors that the overdraft limit extended to the debtor was especially temporary and that the bank had participated with the debtor in the selective dishonouring of the debtor's cheques. These were matters occurring in the relationship between the bank and the debtor which the guarantor "would not expect to exist".

Fiduciary relationships

[32.50] A fiduciary relationship gives rise to a duty of disclosure. The duty is imposed on the *fiduciary* in favour of the person to whom fiduciary obligations are owed (the *beneficiary*). In *Hospital Products Ltd v United States Surgical Corp*, Gibbs CJ stated:

> The archetype of a fiduciary is of course the trustee, but it is recognised by the decisions of the courts that there are other classes of persons who normally stand in a fiduciary relationship to one another – eg, partners, principal and agent, director and company, master and servant, solicitor and client, tenant for life and remainderman. There is no reason to suppose that these categories are closed. However, the difficulty is to suggest a test by which it may be determined whether a relationship, not within one of the accepted categories, is a fiduciary one.[45]

40 *Goodwin v National Bank of Australia Ltd* (1968) 117 CLR 173.

41 *Seaton v Heath* [1899] 1 QB 782, 793.

42 *Westpac Banking Corporation v Robinson* (1993) 30 NSWLR 668, 689 (emphasis added).

43 *Westpac Banking Corporation v Robinson* (1993) 30 NSWLR 668.

44 *Commercial Bank of Australia v Amadio* (1983) 151 CLR 447. The majority in this case found for the guarantor on the basis of unconscionable dealing by the bank. See [36.15].

45 *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41, 68.

A fiduciary is a person who undertakes to act in the interests of another (the beneficiary) and not in the interests of himself or herself.[46] The primary obligations of a fiduciary are to avoid a conflict of interest between the duty to the beneficiary and the interests of the fiduciary and not to profit from the position of trust enjoyed by the fiduciary.[47] If the fiduciary is entering into a contract with the beneficiary, a "most ample disclosure of everything" will be demanded.[48]

In *McKenzie v McDonald*,[49] the plaintiff, a widow with pressing financial and family problems, engaged the defendant estate agent to sell her farm and to find her a suitable home in the city. The agent, who knew of the plaintiff's circumstances, was told by an experienced land valuer in the district that the farm was worth the price asked. This information was not passed on to the plaintiff. The agent in fact suggested the plaintiff accept a lower price for the farm and later suggested she exchange the farm for a dwelling he owned on terms advantageous to him and correspondingly disadvantageous to her. The plaintiff agreed to this scheme, and the defendant later sold the farm to a third party for an increased price.

Dixon J held that the defendant was under a duty to the plaintiff to make full disclosure of all that he knew about the farm. Although not every person described in popular language as an "agent" stands in a fiduciary relationship with a principal, this agent did. He undertook the function of advising and assisting the plaintiff and assumed a position of confidence towards her. He was furnished with an intimate knowledge of her financial position and family needs. He offered her counsel as to the value of the farm and as to the obtaining of finance. He accordingly came under a duty of disclosure. He failed to discharge that duty as he did not furnish the plaintiff with all the information he himself possessed. On the contrary, he misled her.

A fiduciary's duties extend beyond disclosure of material facts, to giving advice about the wisdom of entering into a particular contract. Failure to give suitable advice where appropriate may be just as much a breach of duty as a failure to disclose material facts.[50]

Breach of fiduciary duty overlaps with areas of law examined elsewhere in this book, such as undue influence, unconscionable dealing and mistake. Some relationships, such as that of solicitor and client, are not only fiduciary relationships but are also "relationships of influence" for purposes of the law relating to undue influence.[51] The relationship in *McKenzie v McDonald*,[52] we noted, was characterised as a fiduciary relationship (principal and agent). However, it could also have been characterised as "a relationship of influence in fact", given that it was a case in which one person placed confidence and trust in another and relied on the other for guidance. The trusted person was clearly in a position to exercise persuasive influence over and take unfair advantage of the trusting person, as indeed he did.

Contracts for the sale of land

[32.55] Contracts for the sale of land are not contracts *uberrimae fidei*. A vendor of land comes under no duty of general disclosure. It is up to the purchaser to discover whether the drains are leaking or the timber-work is rotting. Holland J stated the position as follows:

46 *Pilmer v Duke Group Ltd (in liq)* [2001] HCA 31; (2001) 207 CLR 165, 196.

47 See [2.60].

48 *Davies v London & Provincial Marine Insurance Co* (1878) 8 Ch D 469, 474.

49 *McKenzie v McDonald* [1927] VLR 134.

50 *Haywood v Roadknight* [1927] VLR 512.

51 See Chapter 35.

52 *McKenzie v McDonald* [1927] VLR 134.

> It seems to me the general rule in contracts of sale and purchase is still undoubtedly caveat emptor … No doubt there is a duty on the vendor to disclose presently existing latent defects of title … But the existence of a possibility which might or does affect the value only has not been held to impose on the vendor any such duty.[53]

A purchaser, equally, comes under no such duty. The position is of course different if a fiduciary relationship exists between the parties.[54] Further, the concept of a latent defect in title is quite broad, covering physical encumbrances, such as an underground drain. A duty of disclosure applies in respect of such defects even if the vendor is ignorant of them.

Duty of care

[32.60] If the representor is under a duty of care to the representee, the discharge of this duty in a particular case may involve an obligation of disclosure. The representor must be careful in providing information and advice. A failure to reveal a relevant fact or to advise on a pertinent matter may constitute a breach of the duty of care giving rise to a possible claim in negligence.[55]

Statute

[32.65] There are many statutory provisions that expressly impose duties of disclosure on specific contracting parties. Examples include corporations laws, consumer credit laws, trade description laws, food-labelling laws and land laws. These provisions cannot be examined here, but it is important to understand that in any particular contractual situation the caveat emptor rule may be modified by statutory provision.

Another point to note is that the general rule of non-disclosure may be bypassed by the statutory imposition of implied terms. For example, it may be true to say that a seller of goods is generally under no duty to disclose defects in the goods to the purchaser. However, in most cases, there will be a statutory guarantee that the goods are of merchantable quality, so that a duty of disclosure is unnecessary.[56] Moreover, the seller is liable even if ignorant of the defects which render the goods unmerchantable. The non-disclosure rule becomes important, however, in the case of a sale not governed by legislation, such as the private sale of a second-hand item.

CULPABILITY

[32.70] A misrepresentation may be culpable or innocent. There are two types of culpable misrepresentation: fraudulent and negligent. Both may permit rescission. The presence or absence of culpability may determine whether rescission is available under the common law or in equity. The presence or absence of culpability is also relevant to determining whether a tort has been committed. We noted at the beginning of this chapter that if the tort of deceit or the tort of negligent misstatement has been committed by the representor, the representee can claim damages.

53 *Dormer v Solo Investments Pty Ltd* [1974] 1 NSWLR 428, 432–3. See further *Kadissi v Jankovic* [1987] VR 255.

54 *McKenzie v McDonald* [1927] VLR 134. See further *Pedashenko v Blacktown City Council* (1996) 39 NSWLR 189.

55 See, eg, *Norwest Refrigeration Services Pty Ltd v Bain Dawes (WA) Pty Ltd* (1984) 157 CLR 149.

56 See Chapter 16.

Fraudulent misrepresentation

[32.75] Fraud on the part of a representor means knowledge of the falsity or absence of belief in the truth of the representation. Fraud in this sense forms the basis of the tort of deceit. Deceit may be defined as a false representation of fact made by a representor, without belief in its truth, with the intention that the representee should act in reliance on the representation, and which causes damage to the representee as a consequence of the latter's reliance.

In the leading case on the meaning of fraud, *Derry v Peek*, Lord Herschell stated:

> fraud is proved when it is shown that a false representation has been made: (1) knowingly or (2) without belief in its truth or (3) recklessly, careless whether it be true or false. Although I have treated the second and third as distinct cases, I think the third is but an instance of the second, for one who makes a statement under such circumstances can have no real belief in the truth of what he says. To prevent a false statement being fraudulent, there must, I think, always be an honest belief in its truth.[57]

This means that if a representor honestly believed in what he or she stated, however careless the representor may have been in coming to that belief, the representor could not be guilty of deceit. As Isaacs ACJ once put it, "negligence, however great, is consistent with honesty, and is not equivalent to fraud".[58]

When a representation is ambiguous, we noted earlier that the sense in which the representation would be understood by a reasonable person in the position of the representee is the sense relevant to determining whether the representation is false. However, this test is not appropriate for determining whether the representation was made fraudulently. Rather, "the sense in which the representor intended the representation to be understood is relevant to the question whether the representation was fraudulently made".[59] Thus, if a car dealer represents as "new" a car manufactured 18 months previously, this would not be a fraudulent misrepresentation if the car had not been previously sold and the dealer honestly meant "not second-hand".[60]

A disclaimer of responsibility by a representor, even though communicated to the representee, will not be effective in respect of a fraudulent misrepresentation.[61]

Negligent misrepresentation

[32.80] In the first half of the 20th century, it was widely thought that a person claiming damages for misrepresentation, at least in respect of pure economic loss, was restricted to suing in deceit.[62] Lord Moulton in *Heilbut Symon & Co v Buckleton* declared that there could be "no damages for innocent misrepresentation".[63] In 1964, however, the House of Lords held in *Hedley Byrne & Co Ltd v Heller & Partners Ltd*[64] that there could be liability

57 *Derry v Peek* (1889) 14 App Cas 337, 374–5.

58 *Haye v CML Assurance Soc Ltd* (1924) 35 CLR 14, 30.

59 *Krakowski v Eurolynx Properties Ltd* (1995) 183 CLR 563, 577; cf [32.15].

60 See *McGrath Motors (Canberra) Pty Ltd v Applebee* (1964) 110 CLR 656.

61 *Commercial Banking Co of Sydney Ltd v RH Brown & Co* (1972) 126 CLR 337; see also *HIH Casualty and General Insurance Ltd v Chase Manhattan Bank* [2003] UKHL 6.

62 One exception was compensation in equity for breach of a fiduciary duty.

63 *Heilbut Symon & Co v Buckleton* [1913] AC 30, 49.

64 *Hedley Byrne & Co Ltd v Heller & Partners Ltd* [1964] AC 465.

for damages for a negligent misstatement.[65] A plaintiff in a negligence action has to establish that the defendant owed him or her a duty of care and that a breach of that duty caused him or her damage. The duty in this context is to take reasonable care that information provided is accurate and that advice given is sound.

In determining whether a duty of care is owed in respect of a statement, the courts have not simply applied the well-known "neighbour test" enunciated by Lord Atkin in *Donoghue v Stevenson*,[66] a test which employs the notion of "reasonably foreseeable possibility" of damage in respect of careless acts (or statements) causing personal injury. A more restrictive approach has been taken in respect of statements causing economic loss. Economic loss is readily recognised as a head of damage in the law of negligence when it flows from physical injury (such as loss of earning capacity) or damage to property (such as the cost of repairs). It is not so readily recognised when it is pure economic loss and this is not linked with physical injury or damage. For example, a person who acts upon another person's unsound statement about a financial matter, and makes a bad investment, suffers pure economic loss.

The more restrictive approach requires a special relationship or nexus between the maker of the statement and the recipient of it. In *Mutual Life & Citizens' Assurance Co Ltd v Evatt*,[67] Barwick CJ has enunciated the elements of the special relationship or nexus. It will be established where the speaker realises or ought to realise that the recipient intends to or is likely to act on the statement in respect of a matter of consequence and it is reasonable for the recipient to so act in all the circumstances. The relevant circumstances would include the nature of the subject matter, the occasion of the interchange and the identity and relative positions of the parties as regards knowledge and capacity.[68] The maker of the statement must know of or foresee the type of purpose for which the recipient intends to use the information or advice.[69]

At one stage, the Privy Council ruled that the duty of care was only imposed on persons who have or claim to have professional or business skill and competence in the subject matter of the representation.[70] However, the High Court has rejected this limitation, as have the English courts.[71] As Gibbs CJ said in *Shaddock & Assocs Pty Ltd v Parramatta City Council*, the duty should extend to "persons who, on a serious occasion, give considered advice or information concerning a business or professional transaction".[72] Although special skill is no longer a separate requirement in itself, it remains a factor relevant to determining whether the recipient's reliance on the information was reasonable.

The negligence principle is applicable to pre-contractual statements.[73] It is not restricted to misstatements of fact but covers both information and advice. The advice may take the form of an opinion as to the future. "The exercise of judgment so often involves an element of prognosis."[74]

65 The approach in *Hedley Byrne & Co Ltd v Heller & Partners Ltd* [1964] AC 465 was first adopted by the Australian High Court in *Mutual Life & Citizens' Assurance Co Ltd v Evatt* (1968) 122 CLR 556.

66 *Donoghue v Stevenson* [1932] AC 562.

67 *Mutual Life & Citizens' Assurance Co Ltd v Evatt* (1968) 122 CLR 556.

68 *Mutual Life & Citizens' Assurance Co Ltd v Evatt* (1968) 122 CLR 556, 569–72.

69 *Tepko Pty Ltd v Water Board* [2001] HCA 19; (2001) 206 CLR 1.

70 *Mutual Life & Citizens' Assurance Co Ltd v Evatt* [1971] AC 793.

71 See *Howard Marine & Dredging Co Ltd v A Ogden & Sons (Excavations) Ltd* [1978] QB 574.

72 *Shaddock & Assocs Pty Ltd v Parramatta City Council* (1981) 150 CLR 225, 234.

73 *Esso Petroleum Co Ltd v Mardon* [1976] QB 801; *Ellul v Oakes* (1972) 3 SASR 377.

74 *Mutual Life & Citizens' Assurance Co Ltd v Evatt* (1968) 122 CLR 556, 573.

The maker of a statement may effectively disclaim responsibility for the statement at the time of making it and thereby avoid a duty of care.[75] However, a disclaimer is likely to be read restrictively in an appropriate case, in much the same way as an exemption clause would be.[76]

Innocent misrepresentation

[32.85] A statement inducing a contract may be entirely innocent; that is, it is neither fraudulent nor negligent. This means, as we have seen, that no claim in tort for damages is possible. It does not mean that no relief is available, as the representee may be entitled to rescind the contract.

There are statutory provisions in South Australia[77] and the Australian Capital Territory[78] which confer upon representees a right to damages for a misrepresentation which induces entry into a contract.[79] These provisions cover innocent misrepresentations. However, the representor has a defence of reasonable belief in the truth of the representation. So if the representor proves that the representation was innocent (in the sense of not negligent), the representee's right to damages is lost. This contrasts with the tort of negligence, where the representee, as plaintiff, has the burden of proving want of reasonable care on the part of the representor. Under the legislation, however, if the misrepresentation is innocent (in the sense that the representor's belief in its truth was reasonable), the court has a discretion to award damages in lieu of rescission.

RELIANCE BY THE REPRESENTEE

[32.90] A representee who is seeking relief, whether rescission or damages, must establish a causal and a not-too-remote link between the misrepresentation and the representee's entry into the contract. This link is established by proof of *reliance* on the misrepresentation. There are issues to be considered here about the actuality and materiality of the reliance and about the nexus between the representor and representee.

Actuality of reliance

[32.95] Did the representee actually rely on the misrepresentation? Sometimes the answer to this question will be clear. For example, if the claimant did not even know of the misrepresentation, there can hardly be reliance on it, nor if the representee knew that the representation was false.[80] Yet Hutley JA in *Gipps v Gipps* stated that the representee will only be defeated:

75 *Hedley Byrne & Co Ltd v Heller & Partners Ltd* [1964] AC 465.

76 See, eg, *BT Australia Ltd v Raine & Horne Pty Ltd* [1983] 3 NSWLR 221; *Burke v Forbes Shire Council* (1987) Aust Torts Reps 80-122.

77 *Misrepresentation Act 1972* (SA), s 7.

78 *Civil Law (Wrongs) Act 2002* (ACT), s 174.

79 The model for these provisions was the *Misrepresentation Act 1967* (UK), c 7.

80 Note, however, that in England it has been held that an action for deceit can be maintained if the representee acts on the representation, even if the representee did not believe the representation to be true: *Zurich Insurance Co plc v Hayward* [2016] UKSC 48; [2017] AC 142.

> if the knowledge is such as to destroy the effects of the misrepresentations as inducements. Only if knowledge is of the falsity of the representations, and that knowledge is accepted as true so that the false belief is wholly dissipated does knowledge defeat misrepresentation.[81]

If the representee was influenced by other factors as well as the representation, this will not defeat a claim. Most people who enter contracts are influenced by a variety of factors. In *Gould v Vaggelas*,[82] the High Court confirmed that a representation need not be the sole inducement. It is sufficient that it plays some part in contributing to the formation of the contract. For example, in *Edgington v Fitzmaurice*,[83] a case referred to earlier in this chapter, the plaintiff advanced money on debentures relying on a false statement in the defendant directors' prospectus as to how the money would be spent. He also mistakenly thought he would have a charge on the company's assets. The Court rejected the defendants' argument that it was the plaintiff's mistaken notion, not the misstatement, which really induced the plaintiff to advance the money. Cotton LJ said: "If he acted on that misstatement, though he was influenced by an erroneous supposition, the defendants will still be liable."[84]

If the representee makes his or her own investigations and relies solely on the results of that investigation, rather than the representor's false statement, the representee's claim will be defeated.[85] What then would be the result if the representee is given an opportunity to discover the truth and does not take it? In *Redgrave v Hurd*,[86] a solicitor, Redgrave, stated that his business brought in £300 pa. He produced summaries showing a business of about £200 pa. Hurd, the prospective purchaser, asked how the difference was made up, and Redgrave referred to papers which he said related to other businesses. In fact, these papers showed only trifling returns. If Hurd had examined them, he would have discovered the truth. The Court nevertheless found in favour of Hurd, as he had been misled by Redgrave's statement. The mere fact that Hurd had an opportunity to investigate and ascertain whether the representation was true did not affect his rights. Jessel MR said: "Nothing can be plainer … than that the effect of a false representation is not got rid of on the ground that the person to whom it was made has been guilty of negligence."[87]

If the representor intends to induce reliance by the representee, the courts draw an inference that the representee was in fact induced to rely on the representation. In *Gould v Vaggelas*,[88] the High Court held that in such circumstances, there is an evidentiary onus on the representor to rebut the factual inference of inducement, but the ultimate burden of proving inducement rests upon the representee. This ruling was made in the context of fraudulent misrepresentation, but if an innocent misrepresentor intends to induce reliance, the same inference of actual inducement should arise. Note that if the meaning of a representation is ambiguous, "the

81 *Gipps v Gipps* [1978] 1 NSWLR 454, 460.

82 *Gould v Vaggelas* (1985) 157 CLR 215.

83 *Edgington v Fitzmaurice* (1885) 29 Ch D 459, discussed at [32.20].

84 *Edgington v Fitzmaurice* (1885) 29 Ch D 459, 481.

85 See *Holmes v Jones* (1907) 4 CLR 1692.

86 *Redgrave v Hurd* (1881) 20 Ch D 1.

87 *Redgrave v Hurd* (1881) 20 Ch D 1. Today if Hurd sued Redgrave for *negligence*, any damages he received might be reduced on account of his contributory negligence, under apportionment legislation. See [27.110] and [33.145]. An award of damages for misleading or deceptive conduct under the ACL may also be reduced. See [33.140] and [33.200].

88 *Gould v Vaggelas* (1985) 157 CLR 215.

sense in which [it] is understood by the representee is relevant to the question whether the representation induced the representee to act upon it".[89]

Materiality of misrepresentation

[32.100] The issue here is whether the representation must be "material" in the sense that it would induce a reasonable person to enter the contract.

If the representor *intends* that the representee should act on the representation, and the representee does so act, it should not matter that a reasonable person would not have so acted. This appears to be the case when the claim is based upon a fraudulent misrepresentation. In *Nicholas v Thompson*,[90] the representees were induced to purchase the representor's interest in a speculative venture by the representor's fraudulent misrepresentation that he had been offered a very large sum of money for his interest but had refused to sell. The representor argued that the representation could not be regarded as material as it was not such as would induce a reasonable person, as distinct from the particular representees, to enter the contract. The Full Court held that it was not necessary to prove that the representation was material in this sense. As McArthur J said: "If the defendant makes the statement for the purpose of inducing, and the plaintiff is thereby induced, that, I think is sufficient."[91]

On the other hand, if the claim is in respect of a negligent misrepresentation, there is in effect a requirement of materiality. As we have seen, the imposition of a duty of care in giving information or advice requires that the reliance of the recipient be reasonable in all the circumstances.[92] In *Shaddock v Parramatta City Council*, Gibbs CJ said:

> A person should be under no duty to take reasonable care that advice or information which he gives to another is correct, unless he knows, or ought to know that the other relies on him to take such reasonable care and may act in reliance on the advice or information which he is given, and unless it would be reasonable for that other person so to rely or act.[93]

If this is the case in respect of negligent misrepresentation, then with stronger reason it would appear to be the case in respect of an innocent misrepresentation. Why should a representor be liable if the misrepresentation is innocent and is not such as would induce a reasonable person to act in reliance on it? On the other hand, if a representor intends the representee to act on the representation and the representee does so act, should the representor be heard to say that a reasonable person would not have so acted?

In the case of deceit, it is an element of the tort that the representor intends the representee to act on the representation. While this may not strictly speaking be a requirement of the tort of negligence, the misrepresentor will often in fact so intend. Equally, an innocent misrepresentor may in fact so intend. In such circumstances, a representee who is induced to enter a contract arguably has a claim for rescission, even though a reasonable person would not have been so induced. However, it appears that no damages could be claimed through an action in negligence, given the basic elements of that tort.

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89 *Krakowski v Eurolynx Properties Ltd* (1995) 183 CLR 563, 577.

90 *Nicholas v Thompson* [1924] VLR 554.

91 *Nicholas v Thompson* [1924] VLR 554, 576. See further *Australian Steel & Mining Corp Pty Ltd v Corben* [1974] 2 NSWLR 202, 207.

92 *Tepko Pty Ltd v Water Board* [2001] HCA 19; (2001) 206 CLR 1.

93 *Shaddock & Assocs Pty Ltd v Parramatta City Council* (1981) 150 CLR 225, 231. See, eg, *Ta Ho Ma Pty Ltd v Allen* [1999] NSWCA 202; [1999] 47 NSWLR 1.

One area where materiality is important is in cases involving a duty of disclosure. Materiality is essential in cases such as insurance. A person under a duty of disclosure cannot be expected to disclose everything he or she knows. There is only a duty to disclose material facts.

In instances where materiality of the misrepresentation is not an element, this does not mean that materiality is irrelevant. Clearly it is easier for a representee to prove actual reliance if the representation is such as would influence a reasonable person. When a representee enters a contract following such a representation, the discharge of the representee's burden of proof is assisted by an inference of fact that the representation induced the entry.[94]

Reliance by whom?

[32.105] A representee who claims relief must prove reliance on the misrepresentation. Who then is a representee? A representee may be defined as a person to whom a representation is made. If the representation is made to a class of persons, all the members of the class are representees. In such cases, the nexus between the representor and the representee(s) is clear and there is no issue of remoteness.

A difficulty may arise, however, if the person who relies on the representation is not the immediate recipient of the representation but receives it indirectly through an intermediary. A may make a statement to B (eg, that his car, which is up for sale, was once owned by a certain celebrity) and B brings the statement to C's attention. C may be induced by the statement to enter into a contract with A to purchase the car. If the statement is false, and B is not A's agent, may C seek relief from A? This problem has not been explored in the cases. There are, however, cases dealing with a different but related situation; that is, where on the basis of A's statement B or C enters into a contract with yet another person D. Assume, for example, that A tells B, falsely, that D is creditworthy, and B tells C. On the basis of the statement, B or C may enter into a contract with D under which credit is unwisely extended to D. Is A liable to B or C?[95] The problem is to determine what degree of knowledge or foresight on the part of the representor is required in respect of the person who acts on the representation and the transaction into which he or she enters.

A fraudulent representor will be liable in deceit if he or she intended the other party to act on the representation in the way the other party did, even though that party may not be the immediate recipient of the representation.[96] In negligence, the problem takes the form of asking whether a duty of care is owed to the person who acted on the statement in the way in which he or she did so act. As we have noted, a duty of care will only be imposed when there is a special or proximate relationship between the person who makes the statement and the person who acts on it. In *Esanda Finance Corp v Peat Marwick Hungerfords*, Brennan CJ stated:

> The uniform course of authority shows that mere foreseeability of the possibility that a statement made or advice given by A to B might be communicated to a class of which C is a member and that C might enter into some transaction as a result thereof and suffer financial

94 *Gould v Vaggelas* (1985) 157 CLR 215, 236.

95 See, eg, *Commercial Banking Co of Sydney Ltd v RH Brown & Co* (1972) 126 CLR 337; *Hedley Byrne & Co Ltd v Heller & Partners Ltd* [1964] AC 30.

96 *Commercial Banking Co of Sydney Ltd v RH Brown & Co* (1972) 126 CLR 337; *Ramsey v Vogler* (1999) 44 IPR 153, 157.

> loss in that transaction is not sufficient to impose on A a duty of care owed to C in the making of the statement or the giving of the advice.[97]

A problem which has particularly troubled the courts and commentators alike is whether an auditor who reports on the financial state of a company owes a duty of care beyond the company itself to others, such as financiers and creditors, who rely on the auditor's report in dealing with the company. The courts have taken a restrictive approach to the imposition of a duty of care in this situation, no doubt fearful of opening the floodgates.[98] For example, Brennan CJ declared:

> [It] is necessary for the plaintiff to allege and prove that the defendant knew or ought reasonably to have known that the information or advice would be communicated to the plaintiff, either individually or as a member of an identified class, that the information or advice would be so communicated for a purpose that would be very likely to lead the plaintiff to enter into a transaction of the kind that the plaintiff does enter into and that it would be very likely that the plaintiff would enter into such a transaction in reliance on the information or advice and thereby risk the incurring of economic loss if the statement should be untrue or the advice should be unsound.[99]

Reasoning of this restrictive kind may well be applicable where a representee who is not the immediate recipient of the representor's statement is nonetheless induced by the statement to enter into a contract with the representor.

97 *Esanda Finance Corp Ltd v Peat Marwick Hungerfords* (1997) 188 CLR 241, 251.

98 *Candler v Crane Christmas* [1951] 2 KB 164; *Caparo Industries plc v Dickman* [1990] 2 AC 605; *Esanda Finance Corp Ltd v Peat Marwick Hungerfords* (1997) 188 CLR 241.

99 *Esanda Finance Corp Ltd v Peat Marwick Hungerfords* (1997) 188 CLR 241, 251–3.

CHAPTER **33**

Misleading or deceptive conduct

STATUTES PROHIBITING MISLEADING OR DECEPTIVE CONDUCT

[33.05] Misleading or deceptive conduct is prohibited by s 18(1) of the *Australian Consumer Law* ("*ACL*"), which provides that:

> [a] person shall not, in trade or commerce, engage in conduct that is misleading or deceptive or is likely to mislead or deceive.[1]

An equivalent prohibition is found in s 12DB of the *Australian Securities and Investments Commission 2001* (Cth).

Section 18 creates a statutory norm or standard of conduct in trade or commerce. A person who has suffered loss by conduct that breaches s 18 is entitled to damages to compensate them for that loss: s 236 of the *ACL*. The court is also given the power to grant any other order it thinks fit to prevent loss being suffered as a result of a breach of s 18, including a declaration that a contract is void or is to be varied or that a person should refund money or return property: ss 237 and 243 of the *ACL*. Section 18 of the *ACL* has a very wide reach. It can be

1 See further Paterson, *Corones' Australian Consumer Law* (4th ed, 2019), Ch 3.

relied upon not only by consumers but also by commercial entities. As a result, it is almost routinely invoked in litigation between commercial parties.

The prohibition in s 18 of the *ACL* is complemented by a number of prohibitions on more specific forms of false or misleading conduct set out in ss 29, 30, 31, 33, 34 and 37 of the *ACL*.[2] These prohibitions on specific kinds of conduct have proved to be very important in the enforcement work of the regulators because they carry potential liability for criminal and civil pecuniary penalties.[3] Regulators have used the prohibitions on specific kinds of misleading conduct to promote compliance with other parts of the *ACL*, such as safety standards in Div 1 of Pt 3-3[4] and the mandatory nature of the consumer guarantees in Pt 3-2.[5] This chapter focuses on the prohibition on misleading or deceptive conduct in s 18 of the *ACL*. Courts typically use the analysis for identifying conduct that misleads developed under the s 18 prohibition in applying the sections dealing with more specific kinds of misleading conduct.[6]

THE LAW PRIOR TO THE INTRODUCTION OF THE *ACL*

[33.10] The provisions of the *ACL* considered in this chapter came into force on 1 January 2011. Prior to the introduction of the *ACL*, s 52 of the *Trade Practices Act 1974* (Cth) ("*TPA*")[7] contained a prohibition, equivalent to s 18 of the *ACL*, on corporations from engaging, in trade or commerce, in conduct that is misleading or deceptive or likely to mislead or deceive. Equivalent provisions in all States and Territories applied to *persons* who engaged in misleading or deceptive conduct in trade or commerce.[8]

Section 52 of the *TPA* and its equivalents were repealed when the *ACL* was enacted. However, the case law identified under these provisions remains relevant in applying the regime in the *ACL*. The following table identifies the key provisions of the TPA which are referred to in the cases considered and identifies the equivalent provisions in the *ACL*.

Nature of provision	Former regime (TPA)	New Regime
Prohibition against misleading or deceptive conduct	s 52	*ACL*, s 18
Definition provisions		
"Engaging in conduct"	s 4(2)	*ACL*, s 2(2)
"involved in"	s 75B	*ACL*, s 2(1)
Deeming provision: future representations	s 51A	*ACL*, s 4 (note: this provision is not identical to *TPA*, s 51A)[9]
Injunction	s 80	*ACL*, s 232

2 See further Paterson, *Corones' Australian Consumer Law* (4th ed, 2019), Ch 6.
3 See further Paterson, *Corones' Australian Consumer Law* (4th ed, 2019), Ch 14.
4 See, eg, *ACCC v Woolworths Limited* [2016] FCA 44; *ACCC v Thermomix in Australia Pty Limited* [2018] FCA 556.
5 See, eg, *Valve Corporation v ACCC* [2017] FCAFC 224; (2017) 258 FCR 190.
6 *ACCC v Coles Supermarkets Australia* [2014] FCA 634, [40] (Allsop CJ).
7 The *Trade Practices Act 1974* (Cth) has since been renamed the *Competition and Consumer Act 2010* (Cth).
8 The relevant statutes and the sections that reproduced s 52 were: *Fair Trading Act 1992* (ACT), s 12; *Fair Trading Act 1987* (NSW), s 42; *Consumer Affairs and Fair Trading Act* (NT), s 42; *Fair Trading Act 1989* (Qld), s 38; *Fair Trading Act 1987* (SA), s 56; *Fair Trading Act 1990* (Tas), s 14; *Fair Trading Act 1999* (Vic), s 9; *Fair Trading Act 1987* (WA), s 10.
9 See [33.70].

Nature of provision	Former regime (TPA)	New Regime
Damages	s 82	*ACL*, s 236
Other orders	s 87	*ACL*, ss 237 and 243
Reduction of damages for failure to take reasonable care	s 82(1B)	*CCA*, s 137B (note there is no equivalent provision in the State and Territory application laws)[10]

TO WHOM DOES THE PROHIBITION AGAINST MISLEADING OR DECEPTIVE CONDUCT APPLY?

[33.15] The *ACL* applies both as a law of the Commonwealth and as a law of all the States and Territories. As a result, corporations, unincorporated entities and individuals are all caught by the prohibition against engaging in misleading or deceptive conduct in trade or commerce. Government entities are also caught to the extent they are carrying on business.[11]

THE "IN TRADE OR COMMERCE" LIMITATION

[33.25] In order to be caught by the statutory prohibition, misleading or deceptive conduct must occur "in trade or commerce". Misleading conduct that does not occur in trade or commerce may still be actionable under the general law governing misrepresentation.[12] The concept of "in trade or commerce" is, as Davies J has stated:

> a complex one and the precise limits of what is or is not trade or commerce or what act is in or is not in trade or commerce cannot be definitively stated … In marginal cases, the circumstances of the case must be considered and many factors must be taken into account.[13]

The High Court considered the limitations imposed by the phrase in *Concrete Constructions (NSW) Pty Ltd v Nelson*.[14] In that case, a worker who was injured on a building site claimed a contravention of the prohibition against misleading or deceptive conduct in trade or commerce on the basis that he had received incorrect information from a foreman as to the safety of grates on air-conditioning shafts.[15] The High Court held that there was no contravention of the section. A majority of the judges so held on the basis that the conduct of the foreman was not "in trade or commerce".

A distinction was drawn by the judges between conduct that is of the essence of a corporation's trade or commerce and conduct that is merely incidental to it. The conduct in this case was an internal communication by one employee to another in the course of their ordinary activities in the construction of a building. The conduct was not itself an aspect or element of activities or transactions which of their nature bore a trading or commercial character. It was undertaken merely in the course of, or incidental to, the carrying on of a trading or commercial business. The word "in" in the phrase "in trade or commerce" indicated

10 See [33.140].

11 See [2.75]–[2.85].

12 See Chapter 32.

13 *Plimer v Roberts* (1997) 80 FCR 303, 305.

14 *Concrete Constructions (NSW) Pty Ltd v Nelson* (1990) 169 CLR 594.

15 In relying on the prohibition against misleading or deceptive conduct in trade or commerce, the worker sought to overcome limitations on recovery imposed by the relevant State workers' compensation legislation.

that the conduct must be directed towards persons with whom the corporation had dealings of a trading or commercial character, such as (but not limited to) consumers. As Toohey J put it, "[t]he question is not whether the conduct engaged in was in connection with trade or commerce or in relation to trade or commerce. It must have been in trade or commerce".[16]

However, there is no need to show that the conduct is part of the corporation's ordinary business activities. In *Bevanere Pty Ltd v Lubidineuse*[17] it was held that the sale of a cosmetic clinic by a company that was not in the business of selling such capital assets was still a transaction "in trade or commerce".[18]

It is well accepted that the phrase "in trade or commerce" excludes from the reach of s 18 the conduct of those who act not in a business capacity, but in a purely private capacity. Thus, the sale by an individual of a non-business asset like the family home would not be caught. In *O'Brien v Smolonogov*,[19] it was held that representations preceding a private sale of land by an individual were not made "in trade or commerce" unless arising in a business context. Such a business context was not created by resort to the press for advertisement or to the telephone for negotiations. The mere use of facilities commonly employed in commercial transactions cannot transform a dealing which lacks any business character into something done "in trade or commerce". However, in such a case, if the vendor engages a real estate agent, the agent's conduct may well occur "in trade or commerce".[20]

The sale by an individual of property or assets used for a business activity has been held to be in trade or commerce.[21] In *Havyn Pty Ltd v Webster*,[22] the New South Wales Court of Appeal upheld the trial judge's finding that the sale of a block of six residential units that had been let out by the respondent occurred in trade or commerce. The nature of the statement and the context in which it was made is more important than the nature of the facilities or methods used to communicate the statement, as illustrated by *Madden v Seafolly Pty Ltd*.[23] In this case, the appellant made statements claiming that the respondent had copied its swimwear designs. Statements to this effect were made on the appellant's personal Facebook page, her business' Facebook page and in emails to media outlets. As the statements went to the way in which Seafolly, one of the appellant's competitors, conducted its business, all statements, including those made on the appellant's personal Facebook page, were held to have occurred in trade or commerce.

It is not necessary to show that the person engaged in the conduct was acting in "trade or commerce" in their own right. Thus, an individual acting on behalf of her employer may herself breach the prohibition against misleading or deceptive conduct, even though she engaged in the conduct on behalf of her employer. This point is illustrated by *Houghton*

16 *Concrete Constructions (NSW) Pty Ltd v Nelson* (1990) 169 CLR 594, 614. Negotiations for an employment contract may be in "trade or commerce": *Rakic v Johns Lyng Insurance Building Solutions (Vic) Pty Ltd (Trustee)* [2016] FCA 430.

17 *Bevanere Pty Ltd v Lubidineuse* (1985) 7 FCR 325.

18 *Bevanere Pty Ltd v Lubidineuse* (1985) 7 FCR 325, 330. See further *Hosmer Holdings Pty Ltd v CAJ Investments Pty Ltd* (1995) 57 FCR 45.

19 *O'Brien v Smolonogov* (1983) 53 ALR 107. See further *Franich v Swannell* (1993) 10 WAR 459.

20 *Argy v Blunts & Lane Cove Real Estate Pty Ltd* (1990) 26 FCR 112; *Pricom Pty Ltd v Sgarioto* [1994] ATPR (Digest) 46-135.

21 *Bevanere Pty Ltd v Lubidineuse* (1985) 7 FCR 325.

22 *Havyn Pty Ltd v Webster* [2005] NSWCA 182, [100].

23 *Madden v Seafolly Pty Ltd* [2014] FCAFC 30.

v Arms.[24] Mr Arms engaged WSA Online to provide website design services. Two of WSA Online's employees, Mr Houghton and Mr Student, told Arms that a particular web-based payment system could be set up easily. Arms set up a web-based wine-selling business in reliance on these representations. As a result of the falsity of the representations, Arms was required to restructure his business. This resulted in the business running at a loss for a period of time. Arms sought to recover that loss from Houghton and Student on the basis that they had engaged in misleading or deceptive conduct. The statements made to Arms were found to have been made "in trade or commerce". The High Court held that:

> It is not to the point that Mr Houghton and Mr Student themselves were not business proprietors or that their activities were an aspect or element of the trade or commerce of WSA … Mr Houghton and Mr Student nevertheless engaged in conduct in the course of trade or commerce.[25]

TCN Channel Nine Pty Ltd v Ilvariy Pty Ltd[26] provides a useful example of how the decision in *Houghton v Arms* has further expanded the scope of the "in trade or commerce" requirement. The New South Wales Court of Appeal, relying on *Houghton v Arms*, held that a representation can be made in trade or commerce even though it is not in the trade or commerce of the person making the representation, so long as it is in the trade or commerce of the person to whom the representation is made. Employees of Channel Nine's "A Current Affair" program purported to be interested in building a home in order to gain access to premises of a building company whose practices they were investigating. The false representations were held to be in trade or commerce as they were in the trade of the building company to which the representations were made.[27]

There are limits to the application of this approach in the context of dealings with government bodies. Thus, the approach was not followed in *Wentworth Shire Council v Bemax Resources Ltd*.[28] The applicant, a local council, allegedly reneged on a rates agreement it had reached with the respondents, who held two mining leases that were subject to the increased rate charges. The negotiation of, and subsequent agreement regarding the rates agreement was held not to have occurred in trade or commerce. Instead it was held to involve conduct of an administrative nature. This was so even though such conduct concerned the respondent's trade or commerce.

Professional activity

[33.28] Professional activities, such as the provision of professional advice, have been held to be "in trade or commerce".[29] In *Bond Corporation Pty Ltd v Thiess Contractors Pty Ltd*,[30] French J held that the giving of professional advice by a consulting engineer was conduct in trade or commerce. Further, the introduction of the *ACL* makes it more likely that professional

24 *Houghton v Arms* [2006] HCA 69; (2006) 225 CLR 553.

25 *Houghton v Arms* [2006] HCA 69; (2006) 225 CLR 553, [35].

26 *TCN Channel Nine Pty Ltd v Ilvariy Pty Ltd* [2008] NSWCA 9; (2008) 71 NSWLR 323.

27 *TCN Channel Nine Pty Ltd v Ilvariy Pty Ltd* [2008] NSWCA 9; (2008) 71 NSWLR 323, [48]–[49].

28 *Wentworth Shire Council v Bemax Resources Ltd* [2013] NSWSC 1047. See also *Mid Density Development Pty Ltd v Rockdale Municipal Council* (1992) 39 FCR 579.

29 See *Bond Corp Pty Ltd v Thiess Contractors Pty Ltd* (1987) 14 FCR 215.

30 *Bond Corp Pty Ltd v Thiess Contractors Pty Ltd* (1987) 14 FCR 215.

activities will be viewed as occurring "in trade or commerce". This is because the definition of the phrase "trade or commerce" under the *ACL* is broader than the definition that was previously contained in s 4(1) of the *TPA*. Section 2(1) of the *ACL* provides that the phrase "trade or commerce" means:

> (a) trade or commerce within Australia; or
>
> (b) trade or commerce between Australia and places outside Australia;
>
> and includes any business or professional activity (whether or not carried on for profit).

The words "and includes any business or professional activity (whether or not carried on for profit)" were not included in s 4(1) of the *TPA*. Some of the now repealed State and Territory consumer protection regimes included a reference to "business or professional activity" in the definition of "trade or commerce".[31] Cases decided in those jurisdictions provide some guidance about the extent to which the reference to "any business or professional activity" may make it easier for a claimant to show that certain types of conduct occurred in trade or commerce. *Shahid v Australasian College of Dermatologists*[32] involved a claim brought under both the *TPA* and the now repealed *Fair Trading Act 1987* (WA). The definition of the phrase "trade or commerce" in the Western Australian legislation included a reference to "any business or professional activity". Jessup J noted that the phrase "any professional activity" is an expression of "potentially wide application".[33] The expression "any professional activity" does not refer to everything done by a professional. Purely instrumental or administrative functions, even if engaged in by a professional, will continue to fall outside of the definition of "trade or commerce". However, once conduct is classified as "professional activity", it is not necessary to show that the professional activity bears a trading or commercial character.[34]

THE RELEVANT AUDIENCE

[33.30] In order to assess whether conduct is misleading or deceptive it is necessary to identify its likely effect on the audience to whom the conduct is directed. As the High Court noted in *Butcher v Lachlan Elder Realty Pty Ltd*:

> Questions of allegedly misleading conduct … can be analysed from two points of view. One is employed in relation to 'members of a class to which the conduct in question [is] directed in a general sense'.[35] The other … is employed where the objects of the conduct are 'identified individuals to whom a particular misrepresentation has been made or from whom a relevant fact, circumstance or proposal has been withheld';[36] they are considered quite apart from any class into which they fall.[37]

31 *Fair Trading Act 1987* (NSW), s 4(1); *Consumer Affairs and Fair Trading Act* (NT), s 4; *Fair Trading Act 1989* (Qld), s 5(1); *Fair Trading Act 1987* (WA), s 5(1).

32 *Shahid v Australasian College of Dermatologists* [2008] FCAFC 72; (2008) 168 FCR 46.

33 *Shahid v Australasian College of Dermatologists*[2008] FCAFC 72; (2008) 168 FCR 46, [191].

34 *Shahid v Australasian College of Dermatologists* [2008] FCAFC 72; (2008) 168 FCR 46, [190]. Cf *Prestia v Aknar* (1996) 40 NSWLR 165.

35 *Campomar Sociedad Limitada v Nike International Ltd* [2000] HCA 12; (2000) 202 CLR 45, [103].

36 *Campomar Sociedad Limitada v Nike International Ltd* [2000] HCA 12; (2000) 202 CLR 45, [103].

37 *Butcher v Lachlan Elder Realty Pty Ltd* [2004] HCA 60; (2004) 218 CLR 592, [36].

Conduct directed at the public at large

[33.35] Conduct is often directed to the public at large (or a section of the public, such as television viewers[38] or addressees of a prospectus[39]). Advertisements for, or representations associated with, the mass marketing of products provide a good example of such conduct. In *Campomar Sociedad Limitada v Nike International Limited*,[40] Campomar began selling a sports fragrance labelled "NIKE SPORT FRAGRANCE".[41] Nike International alleged that Campomar's marketing and distribution of the product was misleading or deceptive. The High Court held that:

> Where the persons [to whom the conduct is directed] are not identified individuals to whom a particular misrepresentation has been made … but are members of a class to which the conduct in question was directed in a general sense, it is necessary to isolate by some criterion a representative member of that class.[42]

Isolating the ordinary or reasonable member of the class involves an objective attribution of certain characteristics. The ordinary or reasonable member is expected to take reasonable care of his or her own interests.[43] Furthermore, extreme or fanciful reactions to the conduct will not be attributed to the ordinary or reasonable member.

Applying these principles to the facts at hand, the High Court held that Campomar had engaged in misleading or deceptive conduct. Placing the "NIKE SPORT FRAGRANCE" product on store shelves next to other sports fragrances sold under the names of other sportswear manufacturers, such as Adidas, was likely to mislead or deceive reasonable and ordinary members of the public into thinking that the "NIKE SPORTS FRAGRANCE" was in some way promoted or distributed by Nike International itself or with its consent or approval.

It is implicit in the High Court's finding in *Campomar Sociedad Limitada v Nike International Limited* that a failure to pay close attention to small print on the packaging of the Nike fragrance that disclosed that it was produced and distributed by Campomar did not constitute a failure by the ordinary or reasonable member of the class to take reasonable care. However, where the product in question is of a higher value, the ordinary or reasonable member may be treated as having paid closer attention to labels. In *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd*,[44] a manufacturer of a couch that was very similar in design to a more expensive couch distributed by the manufacturer's competitor was held not to have engaged in misleading or deceptive conduct on the basis that, owing to the price of the product in question, and the relaxed environment in which the product was presented, the reasonable consumer would have paid close attention to the brand of the couch and any labels attached.

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38 *R & C Products Pty Ltd v SC Johnson & Son Pty Ltd* [1994] ATPR 41-364.

39 *Fraser v NRMA Holdings Ltd* (1995) 55 FCR 452.

40 *Campomar Sociedad Limitada v Nike International Ltd* [2000] HCA 12; (2000) 202 CLR 45.

41 At the time of the trial, the trademark "Nike" was registered in Campomar's name in respect of perfume products and all kinds of essential oils.

42 *Campomar Sociedad Limitada v Nike International Ltd* [2000] HCA 12; (2000) 202 CLR 45, [103]. This observation was recently approved by French CJ in *Campbell v Backoffice Investments Pty Ltd* [2009] HCA 25; (2009) 238 CLR 304, [35].

43 *Campomar Sociedad Limitada v Nike International Ltd* [2000] HCA 12; (2000) 202 CLR 45, [102], citing *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* (1982) 149 CLR 191, 199.

44 *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* (1982) 149 CLR 191.

Some of the High Court's statements in *Campomar Sociedad Limitada v Nike International Limited* suggest that the effect or likely effect of the conduct is determined by considering the response of a single representative hypothetical member of the class identified. However, as Greenwood J (Tracey J agreeing) noted in *Peter Bodum A/S v DKSH Australia Pty Ltd*,[45] there are Full Court of the Federal Court authorities which determine whether conduct is misleading by asking whether a "not insignificant" number of reasonable or ordinary people in the target audience would be misled. Greenwood J acknowledged that Nike may require the conclusion that retail customers as a class, tested by reference to the hypothetical representative member of the class, would be misled. However, his Honour concluded that the appropriate test to apply was to ask "whether a not insignificant number of persons within the relevant section of the public would be misled or be likely to be misled".[46] It should also be noted that this approach seems consistent with Gibbs CJ's view in *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* that "consideration must be given to the class of consumers likely to be affected by the conduct [which] may include the inexperienced as well as the experienced, and the gullible as well as the astute".[47]

Whether one is to focus on the effect of the conduct on the class or a representative member of the class, the approach adopted in *Campomar Sociedad Limitada v Nike International Limited* suggests that the representative member or members of the relevant class would have defining characteristics that exclude from the group being considered some members of the general public.[48] For example, the comments in *Campomar Sociedad Limitada v Nike International Limited* led a judge considering a misleading conduct claim relating to the marketing of men's suits to identify the relevant class as "a potential purchaser of men's suits from a retail store in or near the Melbourne CBD".[49]

The hypothetical member of the relevant class may also be treated as having some background knowledge of the subject matter to which the potentially misleading conduct relates.[50] In *Australian Competition and Consumer Commission v TPG Internet Pty Ltd*,[51] the ACCC argued that TPG's marketing methods were misleading. TPG published advertisements that prominently displayed an attractive monthly flat rate for broadband services and, much less prominently, disclosed that the rate in question was only available when broadband services were bundled with a TPG landline service (costing $30 per month). The primary judge, whose approach on this issue was upheld by the High Court, identified the relevant class as "the broad class of Australian consumers around mainland capital cities who were users or potential users of broadband internet services".[52] This group included first-time users but excluded those who knew little or nothing about broadband internet services. The primary judge found that such a group would be aware that such services can be sold bundled or

45 *Peter Bodum A/S v DKSH Australia Pty Ltd* [2011] FCAFC 98.

46 *Peter Bodum A/S v DKSH Australia Pty Ltd* [2011] FCAFC 98, [209].

47 *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* (1982) 149 CLR 191, [9].

48 See also *Crescent Funds Management (Aust) Ltd v Crescent Capital Partners Management (Aust) Ltd* [2017] FCAFC 2; *Homart Pharmaceuticals Pty Ltd v Careline Australia Pty Ltd* [2017] FCA 403.

49 *Heritage Clothing Pty Ltd trading as Peter Jackson Australia v Mens Suit Warehouse Direct Pty Ltd trading as Walter Withers* [2008] FCA 1775, [17].

50 See also *Novartis Pharmaceuticals Australia Pty Ltd v Bayer Australia* [2015] FCA 35 where the relevant class had specialist expertise (ophthalmologists).

51 *Australian Competition and Consumer Commission v TPG Internet Pty Ltd* [2013] HCA 54; (2013) 250 CLR 640.

52 *Australian Competition and Consumer Commission v TPG Internet Pty Ltd* [2011] FCA 1254.

unbundled and would not have a starting assumption as to whether there would be a bundling condition. Given the prominence of the dominant message about unlimited broadband services for a competitive monthly price, a reasonable member of the class identified would conclude that no conditions were attached.[53]

Conduct directed at identified individuals or identified groups

[33.40] Often conduct will be addressed to specific individuals or identified groups of individuals. In such circumstances, an assessment of whether the conduct is likely to mislead is made by reference to the individual or identified group's position.[54] *Butcher v Lachlan Elder Realty Pty Ltd*[55] involved a claim by a purchaser of property against a real estate agent. The purchaser (Butcher) argued that the agent had engaged in misleading conduct by including an inaccurate survey diagram in the brochure it produced to market the property. The brochure included the following disclaimer: "All information contained herein is gathered from sources we believe to be reliable. However, we cannot guarantee it's [sic] accuracy and interested parties should rely on their own enquiries".

The majority (Gleeson CJ, Hayne and Heydon JJ) held that, in order to determine whether the conduct was misleading, it was necessary to consider the nature of the parties, the character of the transaction contemplated and what each party knew about the other as a result of the dealings to determine what effect the conduct would have. The majority characterised the purchasers as intelligent, shrewd and self-reliant business people who could be assumed to respond to the representation in question in a reasonable manner.[56] The real estate agent was characterised as a business with a small staff that did not hold itself out as possessing the means of independently verifying title details of property. Such matters are complex and need to be dealt with by specialists.

With respect to the character of the transaction, the majority noted that it involved the purchase of a very expensive property and that Butcher was assisted throughout the transaction by professional advisers. Given the nature of the parties, the nature of the transaction and the presence of the disclaimer, the majority concluded that the conduct was not misleading or deceptive — the disclaimer made it clear that the real estate agent was not representing that the diagram in question was accurate. In his dissenting judgment, McHugh J adopted a different approach. His Honour asked whether the conduct was likely to mislead "persons in the class identified as reasonable potential purchasers of waterfront properties in the price range of over $1 million".[57] However, McHugh imputed many of Butcher's subjective

53 Compare *Australian Competition and Consumer Commission v Jetstar Airways Pty Ltd* [2015] FCA 1263, [168] in which Foster J found that the relevant target audience was not the public at large as the ACCC contended but a narrower class consisting of members of the public who had internet access and possessed some level of knowledge and experience in navigating the internet and using online booking services, including an understanding of the use of hyperlinks to navigate particular web.

54 *Bathurst Regional Council v Local Government Financial Services Pty Ltd (No 5)* [2012] FCA 1200.

55 *Butcher v Lachlan Elder Realty Pty Ltd* [2004] HCA 60; (2004) 218 CLR 592.

56 *Butcher v Lachlan Elder Realty Pty Ltd* [2004] HCA 60; (2004) 218 CLR 592, [41]. At [50], the majority notes that, had the case involved a purchaser of limited means acting without professional advice, it might be more appropriate to ask what the purchaser actually made of the agent's behaviour, rather than whether they were acting reasonably. This once again illustrates how the characteristics of the parties may affect the analysis of whether conduct is misleading or deceptive.

57 *Butcher v Lachlan Elder Realty Pty Ltd* [2004] HCA 60; (2004) 218 CLR 592, [129].

characteristics to members of the class he identified. For example, his Honour held that such members would have the benefit of professional advice and be aware that it was not part of a selling agent's function to obtain or verify a survey plan. As a result, his Honour's approach is not as different as it first seems. Rather, McHugh J dissented because he took a broader view of what constituted the relevant conduct. His Honour noted that "[i]t invites error to look at isolated parts of the [impugned] conduct. The effect of the relevant statements or actions or any silence or inaction occurring in the context of a single course of conduct must be deduced from the whole course of conduct".[58] Applying this principle, McHugh J held that the relevant conduct extended beyond incorporating the inaccurate diagram into the brochure it prepared for marketing purposes and distributing that brochure.

During an inspection at which Mr Elder was present, Mr Butcher had a conversation with his architect about the possibility of moving the pool to create a larger entertainment area. During this conversation, which Mr Elder heard, Mr Butcher made it clear that he was relying on the accuracy of the survey diagram. Although Mr Elder indicated that he was sceptical about the proposed renovations, everything he said to Butcher at the inspection was premised on the pool being within the freehold land. McHugh J held that in order to be effective, the disclaimer had to modify the effect of all the conduct engaged by Lachlan Elder (including the distribution of the brochure and Mr Elder's conduct at the inspection) so that it was not misleading. His Honour held that the disclaimer did not operate to overcome the misleading nature of the course of conduct engaged in by the real estate agent.

Kirby J also dissented. His Honour appeared to accept that Butcher's personal characteristics were relevant to determining whether the conduct was misleading or deceptive. He also agreed that the Butcher was an intelligent, shrewd and self-reliant businessperson. However, these characteristics would not have made Butcher alert to the nuances of land law. Lachlan Elder's conduct, including the inclusion of the inaccurate diagram in the marketing brochure and the fact that Mr Elder gave no oral reinforcement of the disclaimer at the inspection, was misleading. Kirby J held that the disclaimer was ineffective because of its miniscule size and because he thought giving effect to disclaimers subverted the policy goals of the Act.

Despite the attention devoted to the issue, the Butcher's personal characteristics did not factor heavily in the reasoning of either the majority or the minority. However, as Barker J noted in *Australian Competition and Consumer Commission v Breast Check Pty Ltd*, "the identification of the target audience — whether an individual or a section of the public — is important because, for example, conduct which may not mislead or deceive an individual with whom a respondent has had dealings, may possibly mislead or deceive a representative member of the public in a setting devoid of personal dealings".[59] The ACCC alleged that a pamphlet published by Breast Check and made available to customers in its waiting room contained misleading statements about the ability of a particular form of breast imaging to detect cancer. Breast Check argued that the pamphlet was not misleading as it was directed to a specific group of people, those interested in breast imaging services from Breast Check. That group was said to have "special knowledge that would prevent the alleged misrepresentations

58 *Butcher v Lachlan Elder Realty Pty Ltd* [2004] HCA 60; (2004) 218 CLR 592, [109]. This statement was referred to with approval by Gummow, Hayne, Heydon and Kiefel JJ in *Campbell v Backoffice Investments Pty Ltd* [2009] HCA 25; (2009) 238 CLR 304, [102].

59 *Australian Competition and Consumer Commission v Breast Check Pty Ltd* [2014] FCA 190, [10].

arising".[60] Barker J refused to define the group so narrowly because the brochures in question were freely available to anyone who entered the well-signed clinic. Instead he identified the relevant class as females interested in the Breast Check service, a group including women who may have seen only the brochure and had no other dealings with Breast Check.

WHAT TYPE OF CONDUCT MAY BE MISLEADING?

[33.45] Conduct is regarded as "misleading" if it has the capacity to lead into or cause error.[61] Error occurs when a person is led to believe things that are not true or correct.[62] The courts have not attempted to define the words "misleading or deceptive" any further, and in *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd*, Lockhart J stated that "there is no need or warrant to search for other words to replace those used in the section itself".[63] In *Demagogue Pty Ltd v Ramensky*, Black CJ set out the approach to be adopted when determining whether conduct is misleading or deceptive:

> [C]onsistently with regard to the natural meaning of the terms of s 52 [now *ACL*, s 18], the question is whether in light of all the relevant circumstances constituted by acts, omissions, statements or silence, there has been conduct which is or is likely to be misleading or deceptive. Conduct answering that description may not always involve misrepresentation.[64]

In order to determine whether conduct is misleading or deceptive, it is important to pay close attention to the context in which the conduct occurred. As Gibbs CJ noted in *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd*:

> The conduct of a defendant must be viewed as a whole. It would be wrong to select some words or act which, alone, would be likely to mislead if those words or acts, when viewed in their context, were not capable of misleading.[65]

The context in which the representation is made will also be important to determining the appropriate level of analysis expected of the persons to whom the conduct was directed. For example, the effects of representations contained in television advertisements are assessed on an impressionistic basis. In *Pacific Dunlop Ltd v Hogan*,[66] Beaumont J noted that television advertisements "should not be seen as setting off a logical train of thought in the minds of television viewers".[67] Beaumont J acknowledged that the reasonable member is unlikely to pay close attention to the details of the advertisement. In assessing the impact of an advertisement, therefore, courts should focus on the general impression the advertisement is likely to leave with the viewer. The advertisement in that case was found to be misleading because of its overall impression, even though, on a line-by-line analysis, it said nothing that was literally false. In other circumstances, the reasonable person will be expected to pay close attention to the representations made. In *Butcher v Lachlan Elder Realty Pty Ltd*,[68] a majority of the

60 *Australian Competition and Consumer Commission v Breast Check Pty Ltd* [2014] FCA 190, [37].
61 *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546, 554–555.
62 *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* (1982) 149 CLR 191, 199.
63 *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546, 555.
64 *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31, 41.
65 *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* (1982) 149 CLR 191, 199.
66 *Pacific Dunlop Ltd v Hogan* (1989) 23 FCR 553.
67 *Pacific Dunlop Ltd v Hogan* (1989) 23 FCR 553, 583.
68 *Butcher v Lachlan Elder Realty Pty Ltd* [2004] HCA 60; (2004) 218 CLR 592, [79].

High Court held that the importance and brevity of the information contained in the brochure given to prospective purchasers of land meant that the reasonable person in the position of the purchaser would have paid close attention to the details of the brochure and read it in its entirety.

There is no requirement in s 18 that the misleading conduct be culpable in the sense of being fraudulent, reckless or negligent. As Gibbs CJ said in *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd*, "a corporation which has acted honestly and reasonably may … nevertheless be rendered liable".[69] Accordingly, a perfectly innocent misrepresentation may contravene s 18.[70]

However, culpability is sometimes relevant. In the case of promises, statements of opinion or statements as to the future, the speaker's state of mind may be relevant in establishing misleading conduct.[71] Moreover, as a result of s 4, a representation with respect to a future matter will be taken to be misleading or deceptive unless the representor leads evidence that he or she had reasonable grounds for making the representation.[72] At least where it is not coupled with other conduct, silence must be "otherwise than inadvertent" to constitute conduct.[73] Finally, as noted, individuals are only taken to be "involved in a contravention" if they have knowledge of all the relevant circumstances, including the falsity of the representations.[74]

Puffs

[33.50] It is quite common for advertisements or parties engaged in negotiations to make exaggerated claims in order to attract attention. The courts have accepted that a certain degree of puffery or exaggeration is to be expected in the ordinary course of business.[75] Nonetheless, simply proving that the statement was exaggerated does not preclude it from being misleading. The effect of exaggerated claims will ultimately be determined by asking whether the statement was capable of leading the representee into error. Whether representations are actionable or merely in the nature of puffery depends on the particular facts of the case at hand, considered "in the light of the ordinary incidents and character of commercial behaviour".[76] The nature of the audience to whom the representation was directed will need to be identified[77] so that the effect of the representation on an ordinary and reasonable member of that class can be determined.

Where the correctness of what is being represented can be tested objectively in a sensible manner, it is more likely to be viewed as a form of conduct which, if inaccurate, constitutes misleading or deceptive conduct.[78] In *Byers v Dorotea Pty Ltd*,[79] Pincus J rejected an argument

69 *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* (1982) 149 CLR 191, 197.

70 See, eg, *Greco v Bendigo Machinery Pty Ltd* [1985] ATPR 40-521; *Consolidated Bearing Co (SA) Pty Ltd v Molnar Engineering Pty Ltd* [1994] ATPR (Digest) 46-122.

71 See [33.90].

72 See [33.70].

73 See [33.65].

74 See [33.15].

75 *General Newspapers Pty Ltd v Telstra Corporation* (1993) 45 FCR 164, 178.

76 *General Newspapers Pty Ltd v Telstra Corporation* (1993) 45 FCR 164, 178; *Australian Competition and Consumer Commission v Kaye* [2004] FCA 1363, [122].

77 See [33.30].

78 *Downey v Carlson Hotels Asia Pacific Pty Ltd* [2005] QCA 199, [92].

79 *Byers v Dorotea Pty Ltd* (1986) 69 ALR 715.

that a statement by a vendor of off-the-plan apartments that the apartments would be "bigger and better" than those located in another close-by building was puffery. Although the words "bigger and better" sound like exaggerated sales talk, in this context they conveyed a clear and false impression that the units were on a grander scale than those located in the other building. If the vendor had simply said these apartments will be the "biggest and the best", without comparing the units to another specific building, the Court may have been more willing to dismiss the statement as mere puffery, because such a general statement is far less likely to lead the representee into error than a statement with some degree of specificity.[80] Similarly, in *Petty v Penfold Wines Pty Ltd*,[81] a statement that Petty was getting Penfold's "best discount" was held to be not mere puffery, but a statement of specific fact.

Silence

[33.55] Silence, or the failure to disclose information, will sometimes constitute misleading conduct. A half-truth, for example, is misleading conduct, just as it is a misrepresentation under the general law.[82] Equally so is a failure to disclose an alteration of circumstances after a statement has been made,[83] or a failure to correct a statement where the maker later acquires knowledge which shows that the statement was inaccurate.[84]

Reasonable expectation of disclosure

[33.60] The prohibition on misleading conduct is not limited in responding to silence by the categories recognised by the general law.[85] "Mere silence" on its own is unlikely to be misleading conduct contrary to the statutory prohibition. However, silence or a failure to speak may be misleading where it is accompanied by an "expectation of disclosure" on behalf of the recipient. In *Kimberley NZI Finance Ltd v Torero Pty Ltd*, French J explained that:

> [U]nless the circumstances are such as to give rise to the reasonable expectation that if some relevant fact exists it would be disclosed, it is difficult to see how mere silence could support the inference that the fact does not exist.[86]

This approach to silence and the role of a reasonable expectation of disclosure was endorsed by the Full Federal Court in *Demagogue Pty Ltd v Ramensky*.[87] Gummow J stated that the main question is "whether in the light of all the circumstances constituted by acts, omissions, statements or silence, there has been conduct which is … misleading or deceptive".[88] Black CJ stated that the question to be asked is whether the circumstances were such as to give rise to a reasonable expectation that certain information would be disclosed. The decision in *Demagogue Pty Ltd v Ramensky* has been interpreted in later cases as prescribing a reasonable

80 *Eveready Australia Pty Ltd v Gillette Australia Pty Ltd* [1999] FCA 1824, [59].

81 *Petty v Penfold Wines Pty Ltd* (1994) 49 FCR 282.

82 *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546.

83 *Collier v Electrum Acceptance Pty Ltd* (1986) 66 ALR 613.

84 *Heidelberg Graphics Equipment Ltd v Andrew Knox & Associates Pty Ltd* [1994] ATPR 41-326.

85 *Rhone-Poulenc Agrochimie SA v UIM Chemical Services Pty Ltd* (1986) 12 FCR 477, 489.

86 *Keen Mar Corporation Pty Ltd v Labrador Park Shopping Centre Pty Ltd* [1989] ATPR (Digest) 46-054, 53,195.

87 *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31.

88 *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31, 41.

expectation test for assessing the likelihood of silence to mislead or deceive.[89] The reasonable expectation test was also accepted by members of the High Court as "an approach which can be taken to the characterisation … of conduct consisting of, or including, non-disclosure of information".[90]

Just as the misleading quality of positive conduct is determined by the audience at whom the conduct is directed,[91] so too should the reasonable expectation test allow for the expectations of the ordinary and reasonable members of the class of possible victims or, where the conduct is directed at an individual, the expectations of that individual.[92] Whether there is a reasonable expectation of disclosure is very much a matter of context.[93] For example, where one party is under a duty of confidentiality, it may mean that another person cannot reasonably expect disclosure,[94] although it may be possible to act in a manner that avoids engaging in misleading conduct without breaching an obligation of confidence.[95]

A good illustration of what would now be seen as an application of the reasonable expectation approach to assessing whether silence in the circumstances is misleading is *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd*.[96] In this case, a vendor of a restaurant business informed the purchaser that the restaurant seated 128 persons without disclosing that the restaurant was in fact only authorised by the local authority to seat 84.[97] The vendor's failure to disclose the true position with respect to the limitations on seating capacity was held to constitute misleading conduct. In *Demagogue Pty Ltd v Ramensky*,[98] Mr and Mrs Ramensky entered into a contract with Demagogue to purchase a unit. During the course of the negotiations, the Ramenskys asked about access to the property. They were informed by a representative of Demagogue that "of course there will be access". At a later stage, they were also shown a plan of development that showed a driveway that ran between their property and the road. However, Demagogue failed to inform the Ramenskys that the driveway was a public road and that the Ramenskys would be required to obtain, at a fee, a licence in order to be able to use the driveway. The failure to disclose the requirement to obtain a licence was held to be misleading.

Misleading conduct, silence and commercial negotiations

[33.63] Courts have repeatedly emphasised that in the ordinary course of commercial negotiations there will be little scope for a reasonable expectation of disclosure of sensitive

89 See Robertson, "Silence as Misleading Conduct: Reasonable Expectations in the Wake of Demagogue Pty Ltd v Ramensky" (1994) 2 *Competition and Consumer Law Journal* 1.

90 *Miller & Associates Insurance Broking Pty Ltd v BMW Australia Finance Limited* [2010] HCA 31; (2010) 241 CLR 357, [19].

91 See [33.30].

92 Robertson, "Silence as Misleading Conduct: Reasonable Expectations in the Wake of Demagogue Pty Ltd v Ramensky" (1994) 2 *Competition & Consumer Law Journal* 1, 7–9.

93 *Nagy v Masters Diary Ltd* (1996) 150 ALR 273, 273, 291.

94 See, eg, *Winterton Constructions Pty Ltd v Hambros Australia* (1993) 39 FCR 97.

95 See *EK Nominees Pty Ltd v Woolworths Ltd* [2006] NSWSC 1172, [155].

96 *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546. Although Lockhart J employed the duty of disclosure test, rather than the reasonable expectation of disclosure test that has now found favour, the factual outcome in this case is sound.

97 See also *Nagy v Masters Dairy Ltd* (1996) 150 ALR 273.

98 *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31.

information relevant to the bargaining process.[99] Thus, in *General Newspapers Pty Ltd v Telstra Corporation*, the Full Federal Court stated:

> The common understanding of commercial people must … be taken into account in determining what is misleading or deceptive or likely to be so … [Section 18] does not require arm's length negotiations to be completely open or require full disclosure at all times. The particular facts of the case must be considered in light of the ordinary incidents and character of commercial behaviour.[100]

In *Poseidon Ltd v Adelaide Petroleum NL*, Burchett J commented that:

> I do not think it has ever been suggested that s 52 [now *ACL*, s 18] strikes at the traditional secretiveness and obliquity of the bargaining process. Traditional bargaining may well be hard, without being in the statutory sense misleading or deceptive. No one expects all the cards to be put on the table. But the bargaining process is not therefore to be seen as a licence to deceive.[101]

The sentiments expressed in the cases referred to in the preceding paragraphs were endorsed by the High Court of Australian in *Miller & Associates Insurance Broking Pty Ltd v BMW Australia Finance Limited*.[102] Miller & Associates Insurance Broking Pty Ltd (Miller), an insurance broker, negotiated an insurance premium funding loan with BMW Australia Finance Limited (BMW Finance) on behalf of its client Consolidated Timber Holdings Ltd (CTH). When CTH defaulted on the loan, BMW Finance sought to recover its losses from Miller. During the course of negotiations, Miller provided BMW Finance with a memorandum and certificate of insurance and the loan policy document. BMW Finance alleged that the memorandum and certificate was misleading as it conveyed the misrepresentation that the policy covered property and was assignable and cancellable (features which would have made the insurance policy a better form of security). In addition, BMW Finance alleged that Miller's failure to disclose that the policy was neither assignable nor cancellable amounted to misleading or deceptive conduct.

French CJ and Kiefel J referred with approval to Burchett J's observation in *Poseidon Ltd v Adelaide Petroleum NL* and noted that, as a general proposition, the prohibition against misleading or deceptive conduct in trade or commerce "does not require a party to commercial negotiations to volunteer information which will be of assistance to the decision-making of the other party".[103] In particular, a party is not required to "volunteer information in order to avoid the consequences of careless disregard … of another party of equal bargaining power and competence".[104] Heydon, Crennan and Bell JJ stressed that a reasonable expectation of disclosure does not arise simply because one party knows that a particular matter is likely

99 See also *Australian Competition and Consumer Commission v LG Electronics Australia Pty Ltd* [2018] FCAFC 96: no reasonable expectation of disclosure in a case involving consumers.

100 *General Newspapers Pty Ltd v Telstra Corporation* (1993) 45 FCR 164, 177–178.

101 *Poseidon Ltd v Adelaide Petroleum NL* (1991) 105 ALR 25, 26. See also *Lam v Austotel Investments Australia Pty Ltd* (1989) 97 FLR 458, 475.

102 *Miller & Associates Insurance Broking Pty Ltd v BMW Australia Finance Limited* [2010] HCA 31; (2010) 241 CLR 357.

103 *Miller & Associates Insurance Broking Pty Ltd v BMW Australia Finance Limited* [2010] HCA 31; (2010) 241 CLR 357, [22].

104 *Miller & Associates Insurance Broking Pty Ltd v BMW Australia Finance Limited* [2010] HCA 31; (2010) 241 CLR 357, [22].

to be of importance to the other party.[105] Applying these principles, the High Court rejected BMW Finance's argument that Miller had engaged in misleading conduct. Miller had supplied BMW Finance, an experienced premium lender, with a copy of the policy. Miller's failure to draw BMW Finance's attention to a circumstance disclosed by the policy document was not misleading or deceptive within the meaning of the statutory prohibition contained in the predecessor to s 18(1) of the *ACL*.[106]

Silence may amount to misleading conduct in commercial negotiations where there is other conduct that, without correction, is likely to mislead and therefore gives rise to a reasonable expectation of disclosure. In *EK Nominees Pty Ltd v Woolworths Ltd*,[107] White J held that Woolworths' failure to disclose that it was negotiating with another potential landlord constituted misleading conduct. Woolworths was interested in opening a supermarket in the Auburn area. It had originally hoped to open a store in Queen St. When negotiations for the Queen St site failed, it entered into an in principle agreement with the owner of a site in Auburn Road (EK Nominees). EK Nominees was aware that Woolworths had been interested in opening a store at the Queen St site and sought an assurance from Woolworths that its interest in the Auburn Rd site was genuine. Woolworths gave this assurance, and there was nothing to suggest the assurance was not genuine at the time it was given. On 5 December 2000, Woolworths made an offer to take a lease of a supermarket to be constructed at the Auburn Rd site, subject to Woolworths' board's approval and to the execution of lease documentation. Board approval was obtained on 18 July 2001. It was clear that, despite the absence of a binding agreement, Woolworths expected EK Nominees to commit itself to the project.

From mid-2001, EK Nominees expended significant amounts of money developing the site, including obtaining council approval and undertaking renovation works. During this time, Woolworths provided EK Nominees with various plans and specifications it required the site to comply with. The parties' solicitors also began to negotiate the terms of the lease. On 10 January 2002, Woolworths became aware that the Queen St site (which it had originally been interested in) was being developed. It then entered into confidential negotiations with the new owner of the Queen St site. Over the course of the negotiations it became clear that Queen St was Woolworths' preferred site. Woolworths did not inform EK Nominees that it was negotiating with the owners of the Queen St site. In fact, it continued negotiating with EK Nominees about the terms of the lease.

EK Nominees continued to work on the project until 6 May 2002, when one of EK Nominees' electrical subcontractors asked whether Woolworths was going elsewhere. EK Nominees then contacted Woolworths and was informed that no decision had been made whether to open to a supermarket at the Auburn Rd site, the Queen St site or both. EK Nominees stopped work on the project. On 4 June 2002, Woolworths resolved not to proceed with the agreement for lease of the Auburn Rd site. EK Nominees claimed that Woolworths had engaged in misleading or deceptive conduct by failing to disclose its negotiations with the owners of the Queen St site, thus impliedly representing that there had been no material change to the likelihood of entry by

105 *Miller & Associates Insurance Broking Pty Ltd v BMW Australia Finance Limited* [2010] HCA 31; (2010) 241 CLR 357, [95].

106 See also *General Newspapers Pty Ltd v Telstra Corporation* (1993) 45 FCR 164; *NB2 Pty Ltd v PT Ltd* [2018] NSWCA 10, [75] (Macfarlan, Meagher, Gleeson JJA).

107 *E K Nominees Pty Ltd v Woolworths Ltd* [2006] NSWSC 1172.

Woolworths into a lease at the Auburn Rd site. Woolworths argued that it was not reasonable to expect it to inform EK Nominees of the alternative opportunity that had presented itself. White J disagreed. This was not merely a case in which parties were negotiating with a view to entering into a lease. EK Nominees had spent, and continued to spend, substantial sums of money on the project with Woolworths' knowledge and encouragement. In this context, EK Nominees could reasonably have expected that if a new proposal arose in relation to the Queen St site, it would be told about it or at least told that Woolworths was reconsidering its decision to open a site in Auburn Rd. Although the negotiations with the owner of the Queen St site were confidential, Woolworths could have disclosed that it was reconsidering its decision to continue with the Auburn Rd site lease without breaching confidence. Woolworths was held to have engaged in misleading or deceptive conduct and was held liable for EK Nominees' wasted expenditure on the project.[108]

Deliberateness

[33.65] Although it is generally not necessary to show that the party engaging in the allegedly misleading conduct intended to mislead the other party, there is authority that suggests that silence must be *deliberate* if it is to contravene the section. This possibility stems from the inclusion of the words "otherwise than inadvertently" in the definition of conduct in s 2(2) of the *ACL*. Section 2(2) provides as follows:

> In this Schedule:
>
> …
>
> (b) a reference to conduct, when that expression is used as a noun … is a reference to the doing of or the *refusing to do any act* …;
>
> (c) a reference to *refusing to do an act* includes a reference to —
>
> (i) refraining (*otherwise than inadvertently*) from doing that act …

The impact of this section in assessing misleading conduct contrary to s 18 of the *ACL* in cases involving silence on the part of the defendant is unsettled. In many cases it is not discussed, in others the conclusions are contradictory.

In *Rhone-Poulenc Agrochimie SA v UIM Chemical Services Pty Ltd*,[109] the appellants argued that the respondents engaged in misleading conduct by failing to disclose that the product being sold by the respondents had not been registered as required by law. Bowen CJ held that although s 4(2) of the *TPA* (now s 2(2) of the *ACL*) recognises that whilst an omission to do an act may constitute "engaging in conduct", that will only be so where there has been a deliberate refraining from doing the act (such as disclosing information). This was because the words "refuse" and "refrain" clearly connote that the omission to do an act must be deliberate. This conclusion was reinforced by the phrase "otherwise than inadvertently" in the predecessor to s 2(2)(c)(i).

In *Demagogue Pty Ltd v Ramensky*, Gummow J said:

> 'Conduct' within the meaning of s 52 [now *ACL*, s 18] includes refusing to do an act, and refusal to do an act includes a reference to 'refraining (otherwise than inadvertently) from doing that act': s 4(2) [now *ACL*, s 2(2)]. But in any case, where a failure to speak is relied upon, the question must be whether in the particular circumstances the silence constitutes or is part of the misleading or deceptive conduct. The expanded meaning given by s 4(2) [now

108 See also the discussion of this issue in the estoppel context at [9.175].

109 *Rhone-Poulenc Agrochimie SA v UIM Chemical Services Pty Ltd* (1986) 12 FCR 477, 489.

> *ACL*, s 2(2)] to 'conduct' should not distract attention from the fundamental issue in the case at hand.[110]

This statement suggests that the core inquiry is into whether there has been conduct that is misleading, of which silence may be a part. In such circumstances, whether a decision to withhold information was deliberate is not at issue. However, at a later point in the judgment, Gummow J stated that the trial judge's finding that the silence was the result of a deliberate decision by the vendor "indicates that the disclosure to the respondents which the appellant refrained from making was otherwise than inadvertent, and thus 'conduct' within the terms of s 4(2) [now *ACL*, s 2(2)]".[111]

Gummow J's judgment in *Demagogue Pty Ltd v Ramensky* has been cited both in support of and against there being a requirement that silence be deliberate. In *Costa Vraca Pty Ltd v Berrigan Weed & Pest Control Pty Ltd*[112] a farmer suffered the loss of his tomato crop after the crop was sprayed by an agricultural spraying company. The loss was caused by a small concentration of a harmful chemical left in the spraying rig and hoses. The misleading conduct alleged was a failure to inform the farmer that the rig had been used to spray the chemical on occasions prior to spraying the tomato crop. Given that the farmer had expressed concerns about the use of chemicals, there was a reasonable expectation that if relevant facts existed, they would be disclosed. By failing to inform the farmer about the prior use of chemicals the vendor of the rig misled him to form the erroneous view that it was safe to use the spraying rig. However, Finkelstein J held that, although a reasonable expectation of disclosure arose on the facts, the prohibition against misleading or deceptive conduct in trade or commerce had not been breached as the information had not been deliberately withheld. His Honour referred to Gummow J's second comment (quoted above) in *Demagogue Pty Ltd v Ramensky* in support of this conclusion.[113]

By contrast, in *Nagy v Masters Dairy Ltd*[114] Nicholson J interpreted Gummow J's first comment (quoted above) in *Demagogue Pty Ltd v Ramensky* to mean that silence need not be deliberate.[115]

In *Johnson Tiles Pty Ltd v Esso Australia*[116] Merkel J noted that silence has been recognised as justifying a claim of misleading or deceptive conduct in two situations. The first situation is where it is an element which, together with other circumstances of the case, renders other conduct engaged in misleading or deceptive. In such circumstances, the silence need not be deliberate as silence is simply part of a broader range of conduct which may become misleading because of the non-disclosure. The second situation is where silence alone constitutes misleading or deceptive conduct. This situation arises by reason of the extended definition of "conduct" in s 2(2) of the *ACL*. Therefore, where silence alone is relied on as constituting misleading or deceptive conduct, it must be deliberate.[117] This apparently neat

110 *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31, 40.

111 *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31, 42.

112 *Costa Vraca Pty Ltd v Berrigan Weed & Pest Control Pty Ltd* (1998) 155 ALR..

113 *Costa Vraca Pty Ltd v Berrigan Weed & Pest Control Pty Ltd* (1998) 155 ALR 714, 722.

114 *Nagy v Masters Dairy Ltd* (1996) 150 ALR 273.

115 See also *CCP Australian Airships Ltd v Primus Telecommunications Pty Ltd* [2004] VSCA 232.

116 *Johnson Tiles Pty Ltd v Esso Australia* [1999] FCA 477.

117 *Johnson Tiles Pty Ltd v Esso Australia* [1999] FCA 477, [4]–[5]. See also *Noor Al Houda Islamic College Pty Ltd v Bankstown Airport Ltd* [2005] NSWSC 20, [177]–[192].

distinction is inconsistent with Black CJ's observation in *Demagogue Pty Ltd v Ramensky* that "there is in truth no such thing as 'mere silence' because the significance of silence always falls to be considered in the context in which it occurs".[118]

In *CCP Australian Airships Ltd v Primus Telecommunications Pty Ltd*,[119] the Victorian Court of Appeal considered the definition of conduct when deciding whether silence needed to be deliberate but reached the opposite conclusion to that reached by Bowen CJ in *Rhone-Poulenc Agrochimie SA v UIM Chemical Services Pty Ltd*. The appellants promised to lease an airship to the respondent for advertising purposes. The appellants were unable to finance the purchase of the airship and were thus unable to honour the lease. As an alternative to its claim for breach of contract, the respondents argued that the appellant's failure to inform the respondent as soon as the appellant knew it did not have the funds available to source the airship was misleading. The appellants argued that silence was only caught by the prohibition against misleading conduct if it was intentional. The appellant also argued that it lacked the requisite intention because, at the time of the allegedly misleading silence, it believed sufficient funding would become available. It thus could not be said to have deliberately remained quiet about a lack of finance. Nettle JA (with whom Batt JA and Vincent JA agreed) stated, in response to the appellant's argument that silence had to be deliberate because of the definition of conduct in s 4(2)(c) of the *TPA* (now s 2(2) of the *ACL*):

> As to the law, the misleading and deceptive quality of remaining silent inheres in the non-disclosure of information; not in any refusal to provide it. Consequently, it does not follow from the fact that a failure to act must be intentional in order to be actionable, that silence must be intentional in order to be actionable. It is plain in principle and authority that it is not necessary that silence be intentional in order that it may constitute misleading and deceptive conduct for the purposes of s 52.[120]

This statement suggests a holistic approach to assessing misleading conduct which considered the whole of the context and is therefore consistent with earlier authority such as that in *Demagogue Pty Ltd v Ramensky* that "the significance of silence always falls to be considered in the context in which it occurs".[121]

By contrast, in *Owston Nominees No 2 Pty Ltd v Clambake Pty Ltd*,[122] McLure P, after noting the difficulties in this area, suggested that where the role of the defendant's silence is merely to establish that there is no evidence to contradict a misleading impression created by other conduct, the silence need not be deliberate. But where silence is a part of the conduct relied to establish a contravention of the s 18 prohibition, that conduct must be linked to the defendant through the requirement of deliberateness. McLure P explained:

> Thus, the identification of the defendant's contextual conduct and what it conveys or communicates to the persons to whom it is directed must be assessed having regard to all relevant surrounding circumstances. Not all surrounding circumstances are relevant in the identification process. In particular, conduct cannot be attributed to the defendant unless it had actual or constructive knowledge of the circumstances that affect its content. … When identifying the defendant's contextual conduct, regard can and should be had to all the

118 *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31, 32.

119 *CCP Australian Airships Ltd v Primus Telecommunications Pty Ltd* [2004] VSCA 232.

120 *CCP Australian Airships Ltd v Primus Telecommunications Pty Ltd* [2004] VSCA 232, [34].

121 *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31, 32.

122 *Owston Nominees No 2 Pty Ltd v Clambake Pty Ltd* [2011] WASCA 78; (2011) 248 FLR 183.

> actual conduct of the defendant which encompasses acts and omissions (including silence). Ordinarily, the role of silence is negative in the sense that it confirms there is nothing to prevent a representation arising, as in *Fraser, Demagogue* and *Henjo*. If the surrounding circumstances alter what the actual conduct would otherwise convey, it is the defendant's contextual conduct that must satisfy the definition of 'engage in conduct' in s 4(2).[123]

The issue of whether or when silence must be deliberate to be misleading is yet to be resolved by the High Court.

Representations about future matters

[33.70] Statements about the future are governed by s 4 of the *ACL*. Section 4 is an evidentiary provision rather than a substantive provision. It provides:

> (1) If
>
> (a) a person makes a representation with respect to any future matter (including the doing of, or the refusing to do, any act); and
>
> (b) the person does not have reasonable grounds for making the representation;
>
> the representation shall be taken to be misleading.
>
> (2) For the purposes of applying subsection (1) in relation to a proceeding concerning a representation made with respect to a future matter by:
>
> (a) a party to the proceeding; or
>
> (b) any other person;
>
> the party or other person is taken not to have had reasonable grounds for making the representation, unless evidence is adduced to the contrary.
>
> (3) To avoid doubt, subsection (2) does not:
>
> (a) have the effect that, merely because such evidence to the contrary is adduced, the person who made the representation is taken to have had reasonable grounds for making the representation; or
>
> (b) have the effect of placing on any person an onus of proving that the person who made the representation had reasonable grounds for making the representation.
>
> (4) Subsection (1) does not limit by implication the meaning of a reference in [the *ACL*] to:
>
> (a) a misleading representation; or
>
> (b) a representation that is misleading in a material particular; or
>
> (c) conduct that is misleading or is likely to mislead;
>
> and, in particular, does not imply that a representation that a person makes with respect to any future matter is not misleading merely because that person has reasonable grounds for making the representation.

Section 4(1) provides that a representation as to a future matter is misleading unless the representor had reasonable grounds for making the representation. Although it is not expressly stated, s 4(2) requires the representor to adduce evidence showing that he or she had reasonable grounds for making the representation. Section 4(3) is a new provision that is intended to resolve the uncertainty that surrounded the interpretation of s 4(2)'s predecessor, s 51A(2) of the *TPA*.[124] Contrary views had been expressed about the effect of s 51A(2) in the

123 *Owston Nominees No 2 Pty Ltd v Clambake Pty Ltd* [2011] WASCA 78; (2011) 248 FLR 183, [62], [64].

124 See Duke, "Representations as to the Future Under the Proposed Australian Consumer Law" (2009) 33 *Melbourne University Law Review* 454; Gillies, "Misrepresentations as to Future Matters — Current

cases. On one view, s 51A(2) placed the burden of proof upon the representor who made a representation about a future matter to show, on the balance of probabilities, that there were reasonable grounds for making the representation.[125] On the other, s 51A(2) did not have the effect of placing the burden of proof on the representor.[126] Rather, provided the representor adduced some evidence "to the contrary", the deeming provision would not operate and it was then for the representee to establish, on the balance of probabilities in the ordinary way, that the representor did not have reasonable grounds for making the representation.[127]

Section 4(3) provides that s 4(2) does not have the effect of placing the onus of proving reasonable grounds on any person. Thus, it rules out the first view described in the previous paragraph. Where the representor leads no evidence of reasonable grounds, the representation will be deemed to be misleading: s 4(1).[128] Where the representor leads "some evidence that it had reasonable grounds",[129] he or she will have discharged the evidential onus imposed by s 4(2). The matter will thereafter be dealt with under s 4(1) and "the obligation will be on the [representee] to establish that the representor did not have reasonable grounds for making the representation".[130] Section 4(4) is also a new provision that, at the time of writing, had not been considered by the courts. It provides that s 4(1) "does not imply that a representation that a person makes with respect to any future matter is not misleading merely because that person has reasonable grounds for making the representation". This had, however, been recognised by the courts prior to the introduction of s 4(4).[131]

We will return to the operation of s 4 when discussing the circumstances in which promises will be viewed as misleading conduct.

When will a representation be about the future?

[33.75] A representation as to a future matter will often imply that the representor was of a particular state of mind at the time the representation was made. For example, a representation that sales will reach a particular level implies that, at the time of making the statement, the representor genuinely believed that sales would reach that level and that there were reasonable

Issues in Interpretation" (2009) 17 *Trade Practices Law Journal* 25; Gillies, "Representations as to the Future: Section 51A of the Trade Practices Act 1974 — Plaintiff's Sword or Defendant's Shield?" (2005) 7 *University of Notre Dame Australia Law Review* 99.

125 This view has been adopted in many cases; see, eg, *Ting v Blanche* (1993) 118 ALR 543, 552; *Lewarne v Momentum Productions Pty Ltd* [2007] FCA 1136, [82]; *DIB Group Pty Ltd v Ventouris Enterprises Pty Ltd* [2011] NSWCA 300, [31]. For a review of the relevant authorities see Allsop J's judgment in *McGrath v Australian Naturalcare Products Pty Ltd* [2008] FCAFC 2; (2008) 165 FCR 230, [177]–[191].

126 The latter view recently received strong obiter support from Allsop J and Emmett J in *McGrath v Australian Natural Products Pty Ltd* [2008] FCAFC 2; (2008) 165 FCR 230, [44] (Emmett J), [192] (Allsop J), [76] (Stone J). Stone J, however, thought that determination of the issue was better left to a court that had the benefit of full argument in a matter where the outcome depends on the view taken of s 51A(2). See also *Australian Competition and Consumer Commission v Universal Sports Challenge Ltd* [2002] FCA 1276, [47]; *North East Equity Pty Ltd v Proud Nominees Pty Ltd* [2010] FCAFC 60.

127 *North East Equity Pty Ltd v Proud Nominees Pty Ltd* [2010] FCAFC 60, [25].

128 *Futuretronics Pty Ltd v Gadzhis* [1992] 2 VR 217.

129 *North East Equity Pty Ltd v Proud Nominees Pty Ltd* [2010] FCAFC 60, [33].

130 *North East Equity Pty Ltd v Proud Nominees Pty Ltd* [2010] FCAFC 60, [33]; see also *Hadgelias Holdings Pty Ltd v Seirlis* [2014] QCA 177.

131 See, eg, in *Hatt v Magro* [2007] WASCA 124; (2007) 34 WAR 256, Steytler P noted that s 51A (s 4(4)'s predecessor) was intended to provide an additional avenue by which an applicant might prove that conduct involving a representation with respect to a future matter was misleading. See also [33.95].

grounds for this belief. In *Ting v Blanche*,[132] Hill J held that it is not correct to treat a representation as to an event or conduct in the future as not being a representation with respect to a future matter *merely* because it implies a representation as to the representor's present state of mind. Thus, a representation made to purchasers of a commercial property that they could rent the premises out for a particular amount was held to be a representation as to the future.

However, just because a statement has a future element to it does not mean that it will automatically be treated as a representation as to the future. Ultimately, whether a statement is with respect to a future matter depends on its proper characterisation in the context in which it is made.[133] In *Miba Pty Ltd v Nescor Industries Group Pty Ltd*,[134] the applicants alleged that the respondents made misleading representations about the likely takings of the franchise business the respondents were selling. The applicants relied on the contents of a letter in which the respondents detailed the takings of a similar franchise and adjusted those takings to take account of the location of the franchise being sold to the applicants to reach the estimation of the likely takings of the business being sold. Merkel J held that, although the estimation necessarily has a future element in it, that did not make the estimation a representation as to a future matter. Rather, the estimation was properly characterised as a statement of present belief because the letter referred to the respondents believing that the projected takings would be received and because the letter set out the grounds on which the projections were made.

The approach adopted in *Miba Pty Ltd v Nescor Industries Group Pty Ltd*[135] was firmly rejected by the New South Wales Court of Appeal in *Digi-Tech (Australia) Pty Ltd v Brand*.[136] Sheller, Ipp and McColl JJA did not accept that the statement of the grounds on which a forecast was based prevented it from being characterised as a representation as to a future matter. Moreover, they held that even a statement explicitly made as an expression of belief may nevertheless be a representation as to a future matter: "It all depends on the words used and the general context."[137]

Promises

[33.80] The making of a promise or commitment to do something in the future can be viewed as containing two representations; first, that the promisor currently intends and is able to perform the promise or honour the commitment and, secondly, that the promise or commitment will be honoured in the future.

The making of a misleading contractual promise may, in certain circumstances, constitute misleading conduct.[138] Section 2(2)(a) of the *ACL* provides:

> A reference to engaging in conduct is a reference to doing or refusing to do any act, including:
>
> (i) the making of, or the giving effect to a provision of, a *contract* or arrangement; or
>
> (ii) the arriving at, or the giving effect to a provision of an understanding; or
>
> (iii) the requiring of the giving of, or the giving of, a *covenant*. [emphasis added]

132 *Ting v Blanche* (1993) 118 ALR 543, 553.

133 *Sykes v Reserve Bank of Australia* (1998) 88 FCR 511, 521.

134 *Miba Pty Ltd v Nescor Industries Group Pty Ltd* (1996) 141 ALR 525.

135 *Miba Pty Ltd v Nescor Industries Group Pty Ltd* (1996) 141 ALR 525.

136 *Digi-Tech (Australia) Ltd v Brand* [2004] NSWCA 58.

137 *Digi-Tech (Australia) Ltd v Brand* [2004] NSWCA 58, [102].

138 See Cornwell-Jones, "Breach of Contract and Misleading Conduct: A Storm in a Teacup?" (2000) 24 *Melbourne University Law Review* 249; Skapinker and Carter, "Breach of Contract and Misleading and Deceptive Conduct in Australia" (1997) 113 *Law Quarterly Review* 294.

In *Holt v Biroka Pty Ltd*,[139] it was argued by the defendants that the prohibition against misleading or deceptive conduct in trade or commerce does not apply to contractual promises and that promises to perform contractual obligations cannot constitute conduct which is misleading under s 52 of the *TPA* (now s 18 of the *ACL*). However, Kearney J held that the definition of "engaging in conduct" in s 4(2)(a) of the *TPA* (now s 2(2)(a) of the *ACL*) envisaged acts of a contractual nature as being capable of constituting misleading conduct.

Parties may need to rely on the *ACL* where a promise is not contractual in nature (because, for example, it is not supported by consideration).[140] It may also be necessary to rely on the *ACL* to enforce a contractual promise if that promise is unenforceable (because, for example, it does not comply with *Statute of Frauds* requirements)[141] or if a third party (who will be precluded from enforcing the contractual promise by the doctrine of privity)[142] wishes to enforce the promise. However, it is worth noting from the outset that the making of a contractual promise does not necessarily amount to a representation that the promisor will necessarily fulfil the promise. As Ormiston J noted in *Futuretronics Pty Ltd v Gadzhis*,[143] contractual obligations are usually qualified by some reciprocal obligation. It is therefore necessary to carefully consider, given the circumstances, exactly what representation is made by the giving of a contractual promise.

Promises about a present state of affairs

[33.85] A contractual promise may purport to affirm a presently existing state of affairs. A contractual promise as to an existing fact or state of affairs is sometimes called a *warranty*. A promisor may, for example, warrant that the promisor's house is free of termites or that the promisor is the sole beneficial owner of copyright in a computer program. If the promised state of affairs does not exist, the making of the promise may result in liability for misleading conduct. In *Accounting Systems 2000 (Developments) Pty Ltd v CCH Australia Ltd*,[144] Accounting Systems entered into a contract under which it assigned copyright interests in computer software to Castle Douglas. Accounting Systems provided Castle Douglas with a warranty that it was the rightful owner of the copyright assigned. Castle Douglas then granted a licence to use the software to CCH. As it turned out, Accounting Systems was not the rightful copyright owner. CCH argued that the warranties contained in the contract between Accounting Systems and Castle Douglas were misleading and sought to be compensated for loss in the form of money it expended on a licence from Castle Douglas on the faith of the false warranty. Lockhart and Gummow JJ held that:

> Section 4(2) [now *ACL*, s 2(2)] provides significant support for … the general proposition that the making of a statement as to a presently existing state of affairs, if false, may be engaging in misleading or deceptive conduct, where the statement is embodied as a provision of a contract. In many cases, there will have been pre-contractual conduct which itself contravenes s 52 [now *ACL*, s 18]. The present case is a striking one because it was presented on a narrow basis, and concerned the giving of the warranties in the contract itself.[145]

139 *Holt v Biroka Pty Ltd* (1988) 13 NSWLR 629.

140 See Chapter 4.

141 See Chapter 7.

142 See Chapter 11.

143 *Futuretronics Pty Ltd v Gadzhis* [1992] 2 VR 217.

144 *Accounting Systems 2000 (Developments) Pty Ltd v CCH Australia Ltd* (1993) 42 FCR 470.

145 *Accounting Systems 2000 (Developments) Pty Ltd v CCH Australia Ltd* (1993) 42 FCR 470, 505–6.

The approach adopted in *Accounting Systems 2000 (Developments) Pty Ltd v CCH Australia Ltd* was endorsed by French CJ in *Campbell v Backoffice Investments Pty Ltd*.[146]

Promises about future conduct

[33.90] As noted at [33.80], contractual promises as to the future can be analysed in two ways. First, whether or not a promise to do something in the future is misleading can be analysed by deriving implied representations of current fact from the making of the promise. Secondly, the making of a promise may give rise to a representation that it will be honoured in the future.

In *Futuretronics Pty Ltd v Gadzhis*,[147] the plaintiff's property was knocked down to the defendant at an auction, but the defendant refused to sign the contract and pay the deposit as required under the conditions of sale. The contract was unenforceable for failure to comply with Victoria's *Statute of Frauds* legislation.[148] As the contract could not be sued upon, the plaintiff sought a remedy by alleging that the defendant engaged in misleading or deceptive conduct by bidding at the auction. The plaintiff argued that the defendant's bid constituted a representation to the plaintiff that the bid was genuine and that he intended to be bound by the auction conditions. The plaintiff claimed that both of these representations were untrue. Ormiston J agreed that whether or not the promise was misleading could be analysed in this way.[149] However, he noted that, as a result of s 10A of the *Fair Trading Act 1985* (Vic) (now s 4 of the *ACL*), the inquiry is no longer limited to considering implied representations about the promisee's intention and ability to perform the contract at the time the promise was made.[150] The inquiry is now broader and the courts must inquire whether at the relevant time the promisor had reasonable grounds for making the implicit representation that he or she intended to perform the promise in the future.[151] As noted, s 4(2) provides that a representation as to the future will be deemed to be misleading unless evidence of reasonable grounds is adduced. As Gadzhis failed to tender evidence that he had reasonable grounds for making the representation, his representation was taken to be misleading. However, in this case, no demonstrable loss flowed from the defendant's misleading conduct as there was no competing genuine bidder at the auction. It could not be shown that the error into which the plaintiff's auctioneer had been led resulted in the loss of a sale.

A more restrictive approach was adopted in *Concrete Constructions Group Ltd v Litevale Pty Ltd*.[152] In that case, Mason P said that, while a contractual promise might readily convey an implicit representation as to the promisor's intention to perform, it is far more difficult to argue that a contractual promise conveys an implicit representation as to the promisor's capacity to perform.[153] Before applying s 51A (now s 4 of the *ACL*) the Court must, he said, first determine whether a representation has been made and should exercise restraint in doing so since the promisee may well have relied on nothing more than the contractual rights

146 *Campbell v Backoffice Investments Pty Ltd* [2009] HCA 25; (2009) 238 CLR 304, [35].

147 *Futuretronics Pty Ltd v Gadzhis* [1992] 2 VR 217.

148 See Chapter 7.

149 *Futuretronics Pty Ltd v Gadzhis* [1992] 2 VR 217, 239.

150 *Futuretronics Pty Ltd v Gadzhis* [1992] 2 VR 217, 239.

151 See also *Wright v TNT Management Pty Limited* (1989) 15 NSWLR 679, 690.

152 *Concrete Constructions Group Ltd v Litevale Pty Ltd* (2002) 170 FLR 290.

153 *Concrete Constructions Group Ltd v Litevale Pty Ltd* (2002) 170 FLR 290, [167]–[168].

arising from the promise.[154] Mason P also took a generous approach to what constitutes "reasonable grounds". Even if one could say that the promisor company in that case had made a representation as to its capacity to perform, account must be taken of the fact that the promisor was a limited liability company with limited resources and that the promisee knew that there were risks associated with the transaction.[155]

Not all judges share Mason P's concerns. In *Body Bronze International Pty Ltd v Fehcorp Pty Ltd*,[156] the appellant franchisor reneged on a pre-contractual promise (which was held to have contractual force) to provide finance if fit-out costs exceeded $250,000. Macaulay AJA (with whom Harper JA and Hansen JA agreed) unreservedly found that the appellant's promise "carried with it the implication that Body Bronze had a present intention to lend the moneys if the fit-out cost exceeded $250,000, and had the means to make good that undertaking".[157] Both of these representations were found to be true. Macaulay AJA held that this finding also established that the appellant had reasonable grounds for the purposes of s 51A.

Circumventing the parol evidence rule

[33.92] It is not uncommon for one party to make a pre-contractual promise that is inconsistent with the terms of the contract ultimately entered into. Common law principles relating to contract terms provide that where the contract is wholly in writing, the terms of the contract override any inconsistent pre-contractual promises. In these circumstances, the parol evidence rule prevents extrinsic evidence being giving to add to, vary or contradict the terms of a contract as they appear in the written document.[158] However, a party misled by such a pre-contractual promise may be able to seek a remedy under the *ACL* if he or she is able to establish that the pre-contractual promise was misleading. In *Italform Pty Ltd v Sangain Pty Ltd*,[159] Sangain entered into a contract to purchase two tower cranes from Italform. During contractual negotiations, Italform's managing assured Sangain's managing director that the cranes could be supplied within a period of eight weeks. However, the resulting contract stated "Delivery: Approx. 90–150 days". The New South Wales Court of Appeal endorsed the trial judge's observation that "[t]he fact that a contractual remedy is denied to a plaintiff cannot be determinative of whether a remedy is available under s 52 [now *ACL*, s 18]".[160] Italform's managing director was therefore held to have engaged in misleading or deceptive conduct. The parties had a long-standing commercial and social relationship which explained why the effect of the verbal assurance was not overcome by the terms of the resulting contract.

By contrast, in *Wedgewood Road Hallam (No 1) v Diamond*,[161] Bell J found that the terms of the resulting agreement overcame the otherwise potentially misleading nature of a pre-contractual promise. The defendant agreed to purchase land from the plaintiff. The defendant made it very clear that he required the lot purchased to be level with the warehouse on his adjacent property. The plaintiff promised the level of the lot would be adjusted to ensure this

154 *Concrete Constructions Group Ltd v Litevale Pty Ltd* (2002) 170 FLR 290, [171]–[173].

155 *Concrete Constructions Group Ltd v Litevale Pty Ltd* (2002) 170 FLR 290, [176].

156 *Body Bronze International Pty Ltd v Fehcorp Pty Ltd* [2011] VSCA 196; (2011) 34 VR 536.

157 *Body Bronze International Pty Ltd v Fehcorp Pty Ltd* [2011] VSCA 196; (2011) 34 VR 536, [50].

158 See Chapter 12.

159 *Italform Pty Ltd v Sangain Pty Ltd* [2009] NSWCA 427.

160 *Italform Pty Ltd v Sangain Pty Ltd* [2009] NSWCA 427, [37].

161 *Wedgewood Road Hallam (No 1) v Diamond* [2013] VSC 447.

was the case. The defendant refused to settle when the elevation of the lot was not level with his warehouse. The contract of sale did not include a special condition reflecting the plaintiff's promise. In fact, it included a clause (cl 15) that allowed the plaintiff to change the plan of subdivision provided it notified the defendant. If the defendant objected to the change, he had 14 days from the date of notification to rescind the contract. The defendant was notified but did not exercise his right to rescind. Bell J rejected the defendant's claim that the plaintiff's promise was misleading. Applying what is now s 4 of the *ACL*, Bell J held that at the time the plaintiff made the promise it had reasonable grounds. Bell J was also of the view that the reasonable person in Diamond's position would have understood the promise to ensure the ground was level in light of cl 15, a contractual provision which gave the vendor the right to alter the plan of subdivision (and in turn the level).

Statement of opinions, belief and law

The approach at common law

[33.95] Before the introduction of a statutory prohibition against misleading or deceptive conduct, statements of opinion, belief or law were actionable under the common law doctrine of misrepresentation,[162] even though the doctrine only applied to representations of fact. The courts overcame this limitation by finding representations of fact implicit in the making of the statement. For example, if A stated that an agreement was contractually binding (a statement of law), A would be viewed as impliedly representing that A genuinely believes the agreement in question to be contractual and that there was a reasonable basis for her opinion, perhaps because A has a legal qualification or has received legal advice on the matter. A similar approach has typically been taken in identifying misleading conduct contrary to the statutory prohibition.

Statements of opinion

[33.96] The approach adopted in *Global Sportsman Pty Ltd v Mirror Newspapers Pty Ltd* provides an example of a court employing the common law approach to determine whether the statutory prohibition against misleading conduct had been breached. The Full Federal Court set out the principles that apply when determining whether an opinion about a past or current matter is misleading:

> An expression of opinion which is identifiable as such conveys no more than that the opinion expressed is held and perhaps that there is a basis for the opinion. At least *if those conditions are met*, an expression of opinion, *however erroneous, misrepresents nothing*.[163]

This approach has been adopted in several other cases involving the allegedly misleading giving of opinions.[164]

Thus, for example, whether an opinion can be misleading has arisen in relation to valuations of property, commonly used as the basis for making and entering into a loan. Courts have held that a valuation will be misleading and deceptive if the opinion as to value was not based on reasonable grounds, was not the product of due care and skill and

162 See Chapter 32.

163 *Global Sportsman Pty Ltd v Mirror Newspapers Pty Ltd* (1984) 2 FCR 82, 88 (emphasis added).

164 See, eg, *Johnson & Johnson Pacific Pty Ltd v Unilever Australia (No 2)* [2006] FCA 1646, [117]; *Hatt v Magro* [2007] WASCA 124; (2007) 34 WAR 256, [33].

could not reasonably be held on the basis of information available to the person making the valuation.[165]

Statements of belief

[33.97] Courts have also analysed statements of belief by deriving implied statements of fact that the statement of belief is genuine and has a reasonable foundation. In *Havyn Pty Ltd v Webster*,[166] the purchaser of a block of six flats alleged that a statement in a brochure that each flat was approximately 63 square metres in area was misleading because it overstated the average size of the flats by approximately 5 per cent. The statement was analysed as a statement of belief. The real estate agent arrived at the estimation in question by "pacing out" one of the units. As the method of estimation was so crude, it was held that there was no adequate foundation upon which the real estate agent could have had a rational belief that each flat was approximately 63 square metres in area. The statement of belief contained an implied factual representation that the real estate agent has a reasonable basis for the statement. As the implied factual representation was false, the statement of belief was held to be misleading or deceptive.

Statements of law

[33.98] A misstatement of law may constitute misleading conduct. The expertise or the knowledge of the person making the statement will be relevant to determining whether a misstatement of law constitutes misleading or deceptive conduct. In *Inn Leisure Industries Pty Ltd v DF McCloy Pty Ltd*,[167] the purchaser of a boating launch told the vendor erroneously that the intended use of the launch for game fishing attracted an exemption from sales tax. An audit by the Australian Taxation Office resulted in the vendor being obliged to pay tax and a penalty. The vendor sought to recover the amounts paid on the basis that the purchaser's statement was misleading or deceptive. In the course of his judgment, French J said:

> A representation of law may be made in different ways which send different messages to the recipient. It may do no more than convey what is, on the face of it, the untutored opinion of the representor. As such it would be unlikely, if wrong, to constitute misleading or deceptive conduct … Expert advice as to the law may convey the representation that it is based upon an underlying body of knowledge, experience or expertise possessed by the person proffering it or to which that person has access. The situations in which advice, expert or otherwise, as to the law may be misleading or deceptive for the purposes of s 52 [now *ACL*, s 18] will depend upon the context and circumstances in which it is proffered and the representations implied or expressed that accompany it.[168]

French J's approach also focused on the implied representations drawn from the expertise of the representor. His Honour held that the purchaser had done no more than express an inexpert opinion. The purchaser gave evidence that its statement was based on advice it received from its accountants. There was nothing to suggest that the opinion was not honestly held or that the advice had not been given. Therefore, although the opinion turned

165 *MGICA (1992) Ltd (formerly MGICA Ltd) v Kenny & Good Pty Ltd* (1996) 140 ALR 313, 356–7 (Lindgren J); *Bathurst Regional Council v Local Government Financial Services Pty Ltd (No 5)* [2012] FCA 1200, [2164], [2416] (Jagot J); *Chowder Bay Pty Ltd v Paganin* [2017] FCA 332, [31] (Besanko, Markovic, Lee JJ).

166 *Havyn Pty Ltd v Webster* [2005] NSWCA 182.

167 *Inn Leisure Industries Pty Ltd v DF McCloy Pty Ltd* (1991) 28 FCR 151.

168 *Inn Leisure Industries Pty Ltd v DF McCloy Pty Ltd* (1991) 28 FCR 151, 167.

out to be inaccurate, the conduct was held not to breach the prohibition against misleading or deceptive conduct.

Where a party holds itself out as having expertise, statements about law are more likely to be viewed as misleading. In *SWF Hoists and Industrial Equipment Pty Ltd v State Government Insurance Commission*,[169] the Commission provided advice about workers' compensation insurance to SWF Hoist. Von Doussa J held that the Commission had represented that the policy in question would cover SWF Hoist if an employee was injured or killed whilst performing his or her employment interstate. Even though the making of the statement involved a mistake or misunderstanding as to the law by the Commission, von Doussa J held that the statement was one of fact as to the content of packages of insurance offered to SWF Hoist policy.[170] As the Commission held itself out as an expert in the matter of insurance, the Commission's conduct was held to be misleading. Von Doussa J noted that the distinction between fact and law is often very difficult to draw and observed that, even if the relevant statements were characterised as statements of law, the advice would still have been an actionable form of misleading or deceptive conduct.[171]

Overall assessment is whether the conduct is misleading or likely to mislead

[33.99] Despite this tendency in the case law to analyse statements of opinion, belief and law by reference to whether they contain an implied representation of belief or expertise, the overall issue is whether, in the circumstances, the conduct is misleading or likely to mislead.

In *Forrest v Australian Securities and Investments Commission*,[172] the High Court was critical of analysing statements of the kind under discussion by analysing the accuracy of statements of fact said to be implicit in such statements. The Australian Securities and Investments Commission (ASIC) alleged that Fortescue Metals Group Ltd (the second appellant) breached s 1041H of the *Corporations Act*. Fortescue's Chairman and Chief Executive, Mr Forrest (the first appellant), was said to be "involved in" the breach. Section 1041H prohibits misleading and deceptive conduct in relation to financial products or services. ASIC identified 13 different communications said to have involved contravention of s 1041H. In a letter to the Australian Stock Exchange (ASX) and in a media release, both sent on 23 August 2004, Fortescue announced it had entered a "binding contract" with Chinese Railway Engineering Corporation (CREC) to build and finance the railway component of a particular project. ASIC alleged that communications in question represented a false statement of fact, namely that agreements binding under Australian law had come into existence. This was not the case as the agreements lacked the requisite degree of certainty because they did not provide for the subject matter, scheduling or price for the works to be done, nor a mechanism for determining such matters. ASIC also pleaded that Fortescue had implicitly, but still falsely, represented it had a "genuine and reasonable basis" for making the statement. ASIC explained the inclusion of this argument in its pleadings as a pre-emptive strike against an argument it believed the appellants may make, namely that the statements in question were statements of opinion.

169 *SWF Hoists and Industrial Equipment Pty Ltd v State Government Insurance Commission* [1990] ATPR 41-043.

170 *SWF Hoists and Industrial Equipment Pty Ltd v State Government Insurance Commission* [1990] ATPR 41-043, 51,607.

171 *SWF Hoists and Industrial Equipment Pty Ltd v State Government Insurance Commission* [1990] ATPR 41-043, 51,608.

172 *Forrest v Australian Securities and Investments Commission* [2012] HCA 39; (2012) 247 CLR 486.

Heydon J's judgment is the more traditional. His Honour found the statement was one of opinion. The statement would, therefore, be held to be misleading if Fortescue did not hold that opinion. Heydon J described the question of whether the giving of an opinion implies there is some basis for that opinion as "controversial".[173] His Honour then notes that the court in *Global Sportsman Pty Ltd v Mirror Newspapers Pty Ltd* said that an expression of opinion conveys the impression that the opinion was held and "*perhaps* that there is basis for the opinion".[174] Heydon J made the point that whether there is a representation that the opinion has a basis will very much depend on the circumstances, including the identity of the person giving the opinion and those hearing it. Anything said along with the opinion would also be relevant. Heydon J held that Fortescue's remarks were directed at a section of the public who were not a naive audience. This audience was conscious of the difficulties associated with mining projects and would understand that in the circumstances it may never be possible to enforce a contract against CREC.

French CJ, Gummow, Hayne and Kiefel JJ held that it did not matter whether the appellants had a genuine or reasonable basis for making the statement, noting:

> It is ultimately unprofitable to attempt to classify the statement according to some taxonomy, no matter whether that taxonomy adopts as its relevant classes fact and opinion, fact and law, or some mixture of these classes. It is necessary instead to examine more closely and identify more precisely what it is that the impugned statements conveyed to their audience.[175]

The intended audience was held to include present and possible future investors and some wider section of the business community. The ultimate question was what members of this group would have understood the statement that "binding contracts" had been reached to mean. It was held that this group would take the statement "as a statement of what the parties to the agreements understood that they had done and *intended* would happen in the future".[176] The statement conveyed that Fortescue and the CREC entered into agreements they intended to keep. Such a statement would not be interpreted by reasonable members of the identified class as a representation as to the legal enforceability of the agreements in an Australian court. As a result, the conduct was not misleading.

Passing on information

[33.100] One way in which a respondent may be able to negate a claim that it engaged in misleading conduct is to make it clear that it is merely passing on the misleading information — that it was a mere "conduit".[177] In *Yorke v Lucas*, the High Court said that, although a corporation that acts honestly and reasonably may nonetheless engage in conduct that is misleading, it is doubtful whether this conclusion should be drawn "if the circumstances are such as to make it apparent that the corporation is not the source of the information and that

173 *Forrest v Australian Securities and Investments Commission* [2012] HCA 39; (2012) 247 CLR 486, [94].

174 *Global Sportsman Pty Ltd v Mirror Newspapers Pty Ltd* (1984) 2 FCR 82, 88 (emphasis in original).

175 *Forrest v Australian Securities and Investments Commission* [2012] HCA 39; (2012) 247 CLR 486, [33].

176 *Forrest v Australian Securities and Investments Commission* [2012] HCA 39; (2012) 247 CLR 486, [37] (emphasis in original).

177 For a review of the relevant authorities, see *Borzi Smythe Pty Ltd v Campbell Holdings (NSW) Pty Ltd* [2008] NSWCA 233, [34]–[50].

it expressly or impliedly disclaims any belief in its truth or falsity, merely passing it on for what it is worth".[178]

In some instances, the person who passes on information does so with a disclaimer attached that expressly disclaims authorship of the information and knowledge of the accuracy of the statement. These types of cases are discussed under the heading "disclaimers" at [33.210]. In other cases, the court has found that despite the fact that there is no express disclaimer, it would nevertheless be apparent to the relevant audience that the person was simply passing on information. In *Google Inc v Australian Competition and Consumer Commission*[179] the respondents (the ACCC) alleged that Google was liable for misleading advertisements displayed as sponsored links (paid placements). Under its AdWords campaign, advertisers bid on key words or phrases and are able to ensure that their sponsored links are displayed when, for example, a Google searcher enters the name of one of the advertiser's competitors. Google allows the advertiser to draft the text of the advertisement. The potential for this to result in misleading conduct is evidenced by the following sponsored link placed by STA Travel at issue in the case. STA bid on the name of one of its competitors, "Harvey Travel", which triggered the display of the following advertisement by STA Travel:

Harvey Travel
Unbeatable deals on flights, Hotel & Pkg's Search, Book & Pack Now!
www.statravel.com.au

If the top or bottom line of the advertisement was clicked on, the Google user would be taken through to STA Travel's website.

By the time the matter got to the High Court, Google accepted that the advertisement created a misleading impression of association between Harvey Travel and STA Travel and that STA Travel had breached s 18. However, the ACCC wanted the case to force Google to change its practices so as to nip such misleading advertising strategies in the bud. The trial judge drew analogies with cases in which newspaper publishers were held to have merely passed on information and concluded that the reasonable Google user would understand that the advertiser was the author of the information. The Full Court upheld the ACCC's appeal. It found that because sponsored links were "Google's response to a user's insertion of a search term into Google's search engine",[180] the newspaper cases were distinguishable. Google was found, along with the advertiser itself, to have engaged in the misleading conduct by publishing the sponsored link under its AdWords policy. The High Court restored the trial judge's finding. It held that Google merely published or displayed the advertisements. The High Court also endorsed the trial judge's conclusion that ordinary and reasonable "Google searchers" would understand that the advertiser had paid for the advertisement to be placed where it is and also that the advertiser, not Google, drafted the text of the advertisement. To put it simply, the High Court found that Google merely "passed on" the information.

178 *Yorke v Lucas* (1985) 158 CLR 661, 666.

179 *Google Inc v Australian Competition and Consumer Commission* [2013] HCA 1; (2013) 249 CLR 435.

180 *Australian Competition and Consumer Commission v Google Inc* [2012] FCAFC 49; (2012) 201 FCR 503, [96].

REMEDIES

[33.105] A range of remedies is available for breach of s 18 of the *ACL*. Under s 236, a person who has suffered loss as a result of a contravention is entitled to damages to compensate him or her for that loss. Under s 237, the court is given power to grant any other orders it thinks appropriate to prevent loss or likely loss being suffered as a result of a contravention. Section 243 sets out a non-exhaustive list of the types of orders that can be made under s 237. Included on the list are declarations that a contract is void, or is to be varied, or that a person should refund money or return property. Section 232 gives the court the power to grant injunctions to restrain breaches and attempted contraventions of s 18. We will focus our attention on ss 236 and 237 as they are most commonly relied upon by persons who have been misled in the contractual context.

In order to be entitled to a remedy under s 236 or s 237 for misleading or deceptive conduct, it is necessary to establish that:

1. there has been a contravention of s 18;[181]
2. "loss or damage" has been (or is likely to be) suffered;[182] and
3. there is a causal connection between the 'loss or damage' suffered or likely to be suffered and the contravention.[183]

We will begin our discussion by determining the kinds of "loss or damage" that are compensable under ss 236 and 237. We will then consider how the courts determine whether there is a causal connection between this "loss or damage" and the breach. In the following discussion, the person seeking relief is called the *applicant* and the person against whom relief is sought is called the *respondent*.

Loss or damage under s 236

[33.110] Section 236(1) of the *ACL* provides that:

> If
>
> (a) a person (the *claimant*) suffers loss or damage because of the conduct of another person; and
>
> (b) the conduct contravened a provision of Chapter 2 or 3;
>
> the claimant may recover the amount of the loss or damage by action against that other person, or against any person involved in the contravention.

For these purposes, it should be noted that s 18, which prohibits misleading or deceptive conduct, is found in Ch 2 of the *ACL*. Chapter 2 also contains the provisions which prohibit unconscionable conduct.[184] Note also that the phrase "involved in a contravention" is defined by s 2(1) to include persons who have aided or abetted, or have been knowingly concerned in, a contravention.[185] A person will be found to be knowingly concerned if they participate in the

181 See [33.05]–[33.100].
182 See [33.110]–[33.165].
183 See [33.170]–[33.200].
184 See Chapter 38.
185 See [33.15].

misleading conduct and were aware of the conduct's false or misleading nature.[186] However, they need not have appreciated that the misleading conduct constituted a contravention of the law.[187]

Loss or damage is one of the elements that must be proved to bring an action under s 236. It also provides the measure of damages recoverable.[188]

Tort analogy: reliance loss

[33.115] Damages under s 236 of the ACL are often calculated on a reliance basis, by drawing analogies with damages that would have been available as compensatory damages in an action at common law for deceit or negligent misstatement. In *Kizbeau Pty Ltd v WG & B Pty Ltd*, for example, in the context of the purchase of a business induced by a misleading statement, the High Court summarised the principles relating to the assessment of damages for deceit and added: "All these principles are appropriate to the assessment of damages under s 82 [now *ACL*, s 236] where a breach of s 52 [now *ACL*, s 18] has induced a person to purchase a business."[189]

The damages awarded in such a case will be the difference (if any) between the price paid and the "fair" or "real" value of the business or asset, plus damages for consequential loss (if any) directly attributable to the misleading conduct.[190] In assessing the "real" value of the business, subsequent events may be looked at to the extent that they reveal the value of the business at the date of acquisition.[191] Consequential damages would include losses incurred in the running of an unprofitable business, provided damages are mitigated where reasonably possible.[192] Further, there is no need to show that the consequential losses were related to the subject matter of the alleged misrepresentation. In *North East Equity Pty Ltd v Proud Nominees Pty Ltd*,[193] the appellant purchased equipment from the respondent. The appellant sought damages on the basis that the respondent had made misrepresentations about the equipment and that these misrepresentations induced the appellant to purchase the equipment. Inter alia, the appellant claimed to be entitled to damages to compensate it for additional power costs it incurred in operating the new machinery. The trial judge had refused to bring the additional power costs to account because the respondent had not made representations about power costs. The Full Court of the Federal Court found that the trial judge ought to have brought the additional power costs into account because those costs arose directly out of the operation of the equipment acquired in reliance on the respondent's misrepresentations, even though none of these misrepresentations related to power costs.[194]

Such consequential damages would certainly be reasonable if the applicant would not have bought the business *at all* had the true facts been known.[195] However, if the purchaser would

186 *Yorke v Lucas* (1985) CLR 661, 670.

187 *Yorke v Lucas* (1985) CLR 661, 670.

188 *Havyn Pty Ltd v Webster* [2005] NSWCA 182, [113].

189 *Kizbeau Pty Ltd v WG & B Pty Ltd* (1995) 184 CLR 281, 291.

190 See *HTW Valuers (Central Qld) Pty Ltd v Astonland Pty Ltd* [2004] HCA 54; (2004) 217 CLR 640; *North East Equity Pty Ltd v Proud Nominees Pty Ltd* [2010] FCAFC 60, [130]–[131].

191 *Anya Holdings Pty Ltd v Idohage Pty Ltd* [2006] FCA 1531, [187].

192 *Gould v Vaggelas* (1985) 157 CLR 215.

193 *North East Equity Pty Ltd v Proud Nominees Pty Ltd* [2010] FCAFC 60.

194 *North East Equity Pty Ltd v Proud Nominees Pty Ltd* [2010] FCAFC 60, [176].

195 *Henville v Walker* [2001] HCA 52; (2001) 206 CLR 459, [132] (McHugh J).

have been content to buy the business at a lower price in such circumstances, it may be that the only damage the purchaser has suffered is the immediate damage of the difference between the price paid and the true value of the business.[196] Such reasoning involves the application of the but for test of causation to the assessment of damages.

In *Gates v City Mutual Life Assurance Society Ltd*,[197] the applicant alleged that before he applied for a total disability clause to be added to an existing life policy, the respondent insurance company's agent assured him that policy benefits would apply if he could not attend to his occupation for 90 days. In fact, the clause denied benefits to the applicant if he was able to attend to *any* gainful occupation, not just *his* occupation. The applicant sustained injury and could not attend to his occupation as a builder for 90 days. The respondent refused to pay the policy benefits on the basis that the conditions of the disability clause were not satisfied.

The applicant's claim for damages under the equivalent of s 236 of the *ACL* failed. The issue of compensation in this case could be approached in a number of ways. The court adopted the torts (reliance) measure to determine whether the applicant had suffered any loss. The applicant was therefore entitled to the difference between the value of what he paid by way of premiums and the value of the total disability clause in the policy. As there was no evidence that the cover was not worth what he paid for it, the applicant was not entitled to any damages on that basis. Another way of giving the applicant relief would have been to rescind the policy and direct a refund of the premiums paid. But the applicant did not claim relief on that basis. Instead, he claimed the benefits that were payable according to the agent's assurance. This was a contract (expectation) measure of damages for expectation loss and such a measure was not considered by the High Court to be an appropriate method for determining loss or damage in this context.[198]

Loss of opportunity

[33.120] In order to obtain damages, the applicant must sustain a prejudice or disadvantage as a result of altering his or her position in reliance on the misleading conduct.[199] In order to restore an applicant to the position he or she would have been in had it not be for the contravention, it may be necessary to compensate the application for opportunities lost as a result of the contravention.[200] For example, damages may be claimed under s 236 for *loss of an opportunity* to enter or continue a profitable contract with another party.[201] The applicant in *Gates v City Mutual Life Assurance Society Ltd* would have been entitled to damages on this basis if he had been able to prove that had it not been for the insurance agent's misrepresentation, he could and would have entered into a contract of insurance that would have covered him in the event that he could not work in his profession.[202] Such damages for opportunities foregone resemble the expectation element in contract damages. However, as the applicant must prove that, in reliance on the misleading conduct, he or she missed the opportunity to enter into a different contract on terms similar to the represented

196 *Corbridge v Bakery Fun Shop Pty Ltd* [1984] ATPR 40-493, 45,688.

197 *Gates v City Mutual Life Assurance Society Ltd* (1986) 160 CLR 1.

198 But see *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388.

199 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [46].

200 See, eg, *Jospin Pty Ltd v Copulos Venture Capital Pty Ltd* [1994] ATPR 41-295.

201 *Sellars v Adelaide Petroleum NL* (1994) 179 CLR 332.

202 *Gates v City Mutual Life Assurance Society Ltd* (1986) 160 CLR 1, 14–15.

terms, such damages are more accurately viewed as compensating for reliance loss. The expectation measure of loss may also coincide with the reliance measure where goods with the represented qualities could have been purchased from another supplier. In *Wakefield Trucks Pty Ltd v Lach Transport Pty Ltd*,[203] a "Western Star" truck was purchased on the faith of representations that it would achieve fuel consumption of 4.5–4.8 miles per gallon. The Western Star truck did not achieve that fuel consumption, and as a result of purchasing the Western Star truck, the buyer lost the opportunity to buy another truck then available (a "Scania") which was capable of achieving that fuel consumption. The cost difference between the fuel consumption as represented and that achieved was recoverable as loss flowing from reliance on the representation.[204]

In *Sellars v Adelaide Petroleum NL*,[205] the High Court considered the problem of proof of damage and assessment of damages in a case where the applicant seeks to show loss of an opportunity or chance to obtain a commercial advantage or benefit. Such a claim is problematic as it is based on a past *hypothetical* fact situation. The High Court decided that it is not necessary for the applicant in such a case to prove *on the balance of probabilities* that a benefit would have been derived from the opportunity had it not been lost. Nor is it necessary to establish the extent of that benefit. Rather, it is sufficient for the applicant to show, by reference to the degree of possibilities and probabilities, that there was *some* prospect of deriving a benefit from the opportunity had it not been lost. If this is shown, the Court will then ascertain the value of the opportunity or benefit by reference to such possibilities and probabilities. In other words, the Court assesses the degree of probability that an event might have occurred and adjusts its award of damages to reflect that degree of probability.[206] The High Court affirmed that this approach is appropriate whether the loss of opportunity results from a tort, a breach of contract or a contravention of s 18.

Contract analogy: expectation loss

[33.125] In Chapter 26, we saw that "expectation damages" are typically awarded for breach of contract. The aim of such damages is to put the promisee, who had a legal right to performance of the contract, in the position he or she would have been in if the contract had been performed. Could "the amount of the loss or damage" which provides the measure of damages for claims under s 236 comprise expectation loss in the contractual sense or is the concept of "loss or damage" limited by analogy to reliance-based loss? This depends on whether expectation loss can be regarded as having been caused by misleading or deceptive conduct.

In *Marks v GIO Australia Holdings Ltd*, McHugh, Hayne and Callinan JJ said:

> [T]here is nothing in s 82 [now *ACL*, s 236]… which suggests … that the amount that may be recovered under s 82(1) … should be limited by drawing some analogy with the law of contract, tort or equitable remedies. Indeed, the very fact that [the section] may be applied to widely differing contraventions of the Act, some of which can be seen as inviting analogies with torts such as deceit (eg s 52 [now *ACL*, s 18]) or with equity (eg s 51AA [now *ACL*, s 20(1)]) but others of which find no ready analogies in the common law or equity, shows

203 *Wakefield Trucks Pty Ltd v Lach Transport Pty Ltd* [2001] SASC 168; (2001) 79 SASR 517.

204 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (2001) 79 SASR 517, [5], [46].

205 *Sellars v Adelaide Petroleum NL* (1994) 179 CLR 332.

206 See also *Walker v Citigroup Global Markets Pty Ltd* [2005] FCA 1678; (2005) 226 ALR 114, [128]–[140].

> that it wrong to limit the apparently clear words of the Act by reference to one or other of these analogies.'[207]

As Gummow J put it: "Analogy … is a servant not a master."[208] However, Gleeson CJ has noted that, although common law analogies "are not controlling … they represent an accumulation of valuable insight and experience which may be useful in applying the Act".[209]

Given that the aims of the *ACL* include fair trading and consumer protection, one way of maintaining adequate levels of commercial propriety and protecting the interests of consumers would be to recognise and enforce legitimate expectations. However, there may be a logical difficulty in allowing expectation damages under s 236 for misleading conduct. Consider the following example. A promises B to deliver a car on Saturday, cash of $10,000 to be paid on delivery. The car is worth $12,000. A fails to deliver. Assuming A's conduct can be characterised as misleading, there must be proof of loss under s 236, and that loss must be a consequence of the misleading conduct. If the action was for breach of contract, the expectation loss would be $2,000, representing the difference between the contract price and the value of the car. This is the benefit B expected to gain from the contract. But can it be said that such loss results from misleading conduct for purposes of a claim under s 236?

Colvin has argued that it cannot.[210] He finds it difficult to see how the loss of the value of the performance of a promise is caused by the promisee being misled as to whether it will be performed. The value of the performance of the promise has only been lost if the promisee was *entitled* to performance. Section 236 does not confer such entitlement. It only allows a claim for loss or damage caused by being misled as to whether a promise will be performed, not for loss or damage caused by failure to perform the promise.

The New Zealand Court of Appeal in *Cox & Coxon Ltd v Leipst*,[211] a case concerned with s 43(1) of the *Fair Trading Act 1986* (NZ), stated that a representation can give rise to a claim for a lost benefit or loss of expectation only where there is an obligation to perform the representation. McHugh J approved this opinion in *Henville v Walker*[212] and pointed out that the wrong which s 52 (now s 18 of the *ACL*) prohibits is the making of, not the failure to honour, the false representation. However, in the same decision, McHugh J also noted that "general principles for assessing damages may have to give way altogether in particular cases to solutions best adopted to give the injured claimant an amount which will most fairly compensate for the wrong suffered".[213]

The High Court's decision in *Murphy v Overton Investments Pty Ltd*[214] provides an example of a case where the Court was prepared to depart from measuring loss on a reliance basis. The High Court held that an applicant suffers compensable loss when, as a result of misleading conduct, he or she undertakes financial obligations which prove to be more onerous than he or she had been led to believe. The applicants purchased a leasehold interest in a unit in a retirement village operated by the respondent. The leases of units in the village

207 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [38], also [15]–[17] (Gaudron J).

208 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [103].

209 *Henville v Walker* [2001] HCA 52; (2001) 206 CLR 459, [18].

210 Colvin, "Tales of the Unexpected: Damages for Lost Expectations" (1997) 5 *Trade Practices Law Journal* 17.

211 *Cox & Coxon Ltd v Leipst* [1999] 2 NZLR 15.

212 *Henville v Walker* [2001] HCA 52; (2001) 206 CLR 459, [132].

213 *Henville v Walker* [2001] HCA 52; (2001) 206 CLR 459, [131].

214 *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388.

required the tenants to pay, each month, a proportion of the "outgoings" of the village (that is, the costs of owning and operating the village). Before they entered into the transaction in 1992, the applicants were provided with an estimate of the amount they would be charged in relation to outgoings. The estimate was misleading because it did not take into account all of the outgoings then being incurred in the operation of the village, which the respondent was entitled to charge under the terms of the lease. In 1996, the respondent began charging the full amount of outgoings payable under the terms of the lease. The applicants sought relief under the predecessor to s 236 of the *ACL*.

The trial judge held that the applicants did not establish that they had suffered any loss or damage as a result of the misleading conduct. There was no evidence of any difference between the price they had paid and the value of the property acquired (even once the value of the property had been adjusted to take account of the increased liability to pay outgoings). Furthermore, there was no evidence that the applicants were not receiving value for the maintenance fees they were paying. In other words, there was no evidence of any reliance loss. In the Full Court of the Federal Court, Branson and RD Nicholson JJ said that the applicants could have claimed damages if they had shown that, had it not been for the respondent's misleading conduct, they would have entered into a less onerous transaction with another retirement village.[215] A lost opportunity such as this would have been a compensable reliance loss, but there was no evidence to support such a claim. Accordingly, a majority of the Full Court upheld the conclusion of the trial judge that no relief was available under the *TPA*.

The High Court allowed an appeal. In a joint judgment, the High Court observed that "the difference between price and value will often be an important element in assessing the damage suffered by a person who, by a misrepresentation, has been induced to buy an item of property".[216] But the High Court also noted that that is not the only kind of damage that may be suffered in a case such as this. In this case, the applicants may have suffered loss by undertaking financial obligations that "proved to be larger than the respondent's misleading conduct led them to believe".[217]

When the respondent started to charge all of the outgoings it was entitled to charge, the appellants suffered a loss. The amount of that loss was not to be determined, as the majority of the Full Court held, only by comparing the financial position of the appellants according to whether they entered into this lease or took some other accommodation. The appellants suffered loss because the continuing financial obligations they undertook when they took the lease proved to be larger than they had been led to believe.[218]

The High Court remitted the case to the trial judge to assess the damages on that basis. The conclusion of the High Court in this case was that the applicants suffered a loss merely by undertaking a contractual obligation that was more onerous than the respondent's conduct led them to believe it was. This is an expectation loss. This decision seems to contradict much of what was said by the High Court in its 1998 decision in *Marks v GIO Australia Holdings*

215 *Murphy v Overton Investments Pty Ltd* [2001] FCA 500; (2001) 112 FCR 182.

216 *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388, [31] (Gleeson CJ, McHugh, Gummow, Kirby, Hayne and Callinan JJ).

217 *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388, [74].

218 *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388, [66].

Ltd,[219] including repeated references to calculating loss by comparing the value of the rights obtained to what was paid,[220] and the following statement made by McHugh, Hayne and Callinan JJ, which was central to the decision:

> The bare fact that a contract has been made which confers rights or imposes obligations that are different from what one party represented to be the case does not demonstrate that the party that was misled has suffered loss or damage … A party that is misled suffers no prejudice or disadvantage unless it is shown that that party could have acted in some other way (or refrained from acting in some way) which would have been of greater benefit or less detriment to it than the course in fact adopted.[221]

The High Court in *Murphy v Overton Investments Pty Ltd*[222] justified the conclusion it reached by reference to statements in earlier cases, such as *Marks v GIO Australia Holdings Ltd*, that relief under s 82 (now s 237 of the *ACL*) should not be confined by analogy.[223] However, the Court's reasoning appears to be inconsistent with the approach to measuring "loss or damage" outlined in the above quotation in the very same case.

Some courts have relied on *Murphy v Overton Investments Pty Ltd*[224] to award damages for expectation loss. Expectation-based damages were awarded in *Dalecoast Pty Ltd v Guardian International Pty Ltd*.[225] The applicant purchased a grafitti-removal franchise from the respondent. The respondent was held to have engaged in misleading or deceptive conduct by representing to the applicant that it would have an indefinite supply of a grafitti-removal product, when in fact the applicant only had the right to an indefinite supply of a grafitti-coating product. Although the applicants had not sustained an operating loss, McKechnie J awarded damages calculated by reference to the profits that would have been made from the distribution and application of the grafitti-removal product on the basis that the applicant did not "receive all that it bargained for".[226] Although this is an expectation measure of loss, McKechnie J held it was appropriate to award damages calculated on this basis because of the reasoning in *Murphy v Overton Investments Pty Ltd*, which made it clear that there is a compensatory element and a public interest element in the assessment of damages for breach of the prohibition against misleading or deceptive conduct in trade or commerce.

In *Callander v Ladang Jalong (Australia) Pty Ltd*,[227] the respondent represented that it would advance money to a business and that the applicant would be appointed CEO of that business at a certain salary. These representations were held to be misleading. On the basis of these representations, the applicant joined the company and worked in the expectation he would be paid a particular salary. Loss or damage was calculated by reference to the amount the claimant expected to be paid less the amount he had received, rather than on the basis of

219 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, discussed at [33.160].

220 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [49]–[51], see also [13], [87].

221 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [47]–[48].

222 *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388.

223 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [15]–[17] (Gaudron J), [38] (McHugh, Hayne and Callinan JJ), [103] (Gummow J), [152] (Kirby J).

224 *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388.

225 *Dalecoast Pty Ltd v Guardian International Pty Ltd* [2004] WASC 82.

226 *Dalecoast Pty Ltd v Guardian International Pty Ltd* [2004] WASC 82, [71].

227 *Callander v Ladang Jalong (Australia) Pty Ltd* [2005] WASC 159.

salary payments foregone, which is the reliance measure of damage.[228] McKechnie J of the Supreme Court of Western Australia decided both of these cases.

In several other cases, the courts have resisted recognising expectation loss as a compensable form of loss under the predecessor to s 236 of the *ACL*. In *Warwick Entertainment Centre Pty Ltd v Alpine Holdings Pty Ltd*,[229] the applicant claimed loss of profits it had hoped to earn by conducting a business it had been induced to purchase on the basis of misleading conduct. The Western Australian Court of Appeal distinguished *Murphy v Overton Investments Pty Ltd*[230] on the basis that the loss claimed by the applicant had not actually been suffered. All that had happened was that an expectation which it had been led to hold had failed. A similar conclusion was reached in *Slinger v Southern White Pty Ltd*[231] in which the Full Court of the Supreme Court of South Australia also noted that awarding the claimant the difference between the price paid for the business and the value received as well as lost profits would result in double recovery.[232]

In *Sumy Pty Ltd v Southcorp Wines Pty Ltd*[233] the applicant bought a block of land that had been advertised as being 100 acres in area. When it discovered that the land was in fact only 80 acres in area, the applicant argued that it would not have entered into the contract at the particular price had it known the area was only 80 acres. It claimed to have suffered loss calculated as a dollar figure per deficient acre. Bergin J distinguished *Murphy v Overton Investments Pty Ltd* and dismissed the applicant's claim on the basis that the amount paid for the land was not higher than the land's real or fair value. A similar claim was made in *Bonnett v Barron & Dowling Property Group*.[234] The applicant argued that because he did not receive the area of land he expected to receive, he had suffered "loss or damage" according to the reasoning of *Murphy v Overton Investments Pty Ltd*. This was said to be because the loss was unexpected and generated by misleading conduct. The applicant also argued that his case was stronger because, unlike the applicants in *Murphy v Overton Investments Pty Ltd*, he had not received what he paid for. Bergin J again held that the relevant loss was the difference between the price paid for the property and its value at settlement.

Unfortunately, it is not possible to be certain about the effect of the decision in *Murphy v Overton Investments Pty Ltd*. Whilst the decision has been interpreted in some cases as allowing for loss to be measured on an expectation basis, more commonly courts have interpreted the decision narrowly and confined it to its facts.

Exemplary damages

[33.130] Because an award of damages under s 236 is to compensate for "loss or damage", exemplary damages, which are aimed at *punishing* the respondent for contumelious disregard

228 Cf *Nikolich v Goldman Sachs JB Were Services Pty Ltd* [2006] FCA 784, [305]. Wilcox J refused to classify expected income as a loss as there was no evidence that the claimant would have embarked on a more profitable course had he not relied on the misleading conduct.

229 *Warwick Entertainment Centre Pty Ltd v Alpine Holdings Pty Ltd* [2005] WASCA 174; (2005) 224 ALR 134.

230 *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388.

231 *Slinger v Southern White Pty Ltd* [2005] SASC 267; (2005) 92 SASR 303.

232 In reaching this conclusion, *Murphy v Overton* [2004] HCA 3; (2004) 216 CLR 388 was not cited.

233 *Sumy Pty Ltd v Southcorp Wines Pty Ltd* [2004] NSWSC 1000.

234 *Bonnett v Barron & Dowling Property Group* [2006] NSWSC 975; (2006) 67 NSWLR 475.

for the victim's rights and *deterring* repetition of such conduct, cannot be awarded.[235] At common law, exemplary damages are not available for breach of contract but may be awarded for flagrant instances of deceit.[236]

Damages for disappointment and distress

[33.133] Section 13 of the *ACL* provides that a reference to an amount of loss or damage includes references to damages in respect of an injury. Thus, s 236 is not limited to compensating for economic loss. In principle, an applicant may recover damages for distress caused by the misleading or deceptive conduct.[237] This possibility is illustrated by the result in *New South Wales Lotteries Corporation Pty Ltd v Kuzmanovski*.[238] The respondent was given an "instant lottery" ticket. The instructions on the ticket stated that "[i]f the word shown in any one Game matches the picture shown in the same Game, you win the prize shown for the game". When the respondent scratched the ticket, he found the word "BATHE" and a picture of a person swimming in the same Game. The appellant refused to recognise the ticket as a winning ticket. The Court held that the terms of the ticket misled consumers as its inherent characteristics and the trial judge's award of $20,000 to compensate for disappointment, anger and frustration as a result of the appellant's misleading conduct was upheld.

However, the circumstances in which such an award may be available are severely limited under the *ACL*. Section 137C of the *Competition and Consumer Act 2010* (Cth) ("*CCA*") provides that plaintiffs cannot bring actions for personal injury damages under s 236 of the *ACL* to the extent that they relate to misleading or deceptive conduct,[239] or unfair practices,[240] where they do not relate to smoking or use of tobacco products.[241] Limitations for damages on personal injury also exist under the State and Territory Civil Liability Acts. For the purposes of this legislation, disappointment has been classified as a form of personal injury, which means that the statutory limitations apply to claims for disappointment and distress.[242]

Apportionment of damages

[33.135] An applicant's loss may be caused by a number of factors in addition to conduct in contravention of the s 18. A damages award under s 236 may be reduced where the loss has been caused partly by the applicant's own failure to take reasonable care and also where the acts or omissions of two or more persons contributed to the loss or damage.

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235 *Musca v Astle Corporation Pty Ltd* (1988) 80 ALR 251, 262; *Nixon v Philip Morris (Australia) Ltd* [1999] FCA 1107; (1999) 95 FCR 453, [97]; *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [9] (Gaudron J).

236 *Musca v Astle Corp Pty Ltd* (1988) 80 ALR 251, 263–8.

237 See, eg, *Walker v Citigroup Global Markets Pty Ltd* [2005] FCA 1678; (2005) 226 ALR 114, [138].

238 *New South Wales Lotteries Corporation Pty Ltd v Kuzmanovski* [2011] FCAFC 106.

239 *Australian Consumer Law* ("*ACL*"), Pt 2-1.

240 *ACL*, Pt 3-1.

241 *Competition and Consumer Act 2010* (Cth), s 137E imposes a similar limitation on the award of compensation orders under *ACL*, s 237.

242 *Insight Vacations Pty Ltd v Young* [2010] NSWCA 137; *Flight Centre v Louw* [2011] NSWSC 132. See Walker and Lewins "Dashed Expectations? The Impact of Civil Liability Legislation on Contractual Damages for Disappointment and Distress" (2014) 42 *Australian Business Law Review* 465.

Claimant's failure to take reasonable care

[33.140] Section 137B of the *CCA* (which is contained in the Part of the *CCA* that applies the *ACL* as a law of the Commonwealth)[243] requires the reduction of an award of damages under s 236(1) where the loss or damage in question has been caused partly by the claimant's failure to take reasonable care and partly by conduct that contravenes s 18. Section 137B only applies to claims for damages in respect of economic loss or damage to property caused by a contravention of s 18.[244] The provision does not apply where the respondent intentionally or fraudulently caused the loss or damage.[245]

Where s 137B is applicable, and the loss has been caused partly by the claimant's failure to take reasonable care and partly as a result of conduct in contravention of s 18, then:

> [T]he amount of loss or damage that the claimant may recover under subsection 236(1) of the *Australian Consumer Law* is to be reduced to the extent to which a court thinks just and equitable having regard to the claimant's share in the responsibility for the loss or damage.[246]

Where those criteria are not met, and the claimant's failure to take reasonable care does not sever the causal connection between the misleading conduct and the loss,[247] the claimant will be entitled to recover the full amount of the loss from the respondent.[248]

Although decided before the introduction of s 137B, *I & L Securities Pty Ltd v HTW Valuers (Brisbane) Pty Ltd*[249] provides a good illustration of its likely operation. The respondent, a valuer, gave an incorrect valuation of a property owned by a third party. The applicant, a financier, lent money to the third party in reliance on the valuation. The third party defaulted and the applicant suffered a loss of $661,481 when the property was sold. The trial judge, Williams J, held that there were two independent causes of the applicant's loss: (1) the respondent's inaccurate valuation and (2) the carelessness of the applicant in failing to make reasonable inquiries as to the third party's creditworthiness before making the loan. Williams J awarded the applicant damages of $440,987 under s 82 of the *TPA* (now s 236 of the ACL), representing two-thirds of the loss. The Queensland Court of Appeal upheld the trial judge's ruling, but based its decision on s 87 of the *TPA* (now s 237 of the *ACL*).

The High Court held (6-1) that apportionment of the loss was not justified under either s 82 or s 87. There was, they said, nothing in s 82 to "to suggest that a claimant's carelessness may be taken into account to reduce the amount of the loss or damage which the claimant is entitled to recover".[250] Callinan J suggested that "urgent steps should be taken to amend the Act to prevent a recurrence of the unjust result that the application of the Act … dictates here".[251] Such steps were indeed soon taken through the introduction of s 137B's predecessor (s 82(1B) of the *TPA*) in 2004.[252]

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243 See [xxx].

244 *Competition and Consumer Act 2010* (Cth), s 137B(a), (b).

245 *Competition and Consumer Act 2010* (Cth), s 137B(d).

246 *Competition and Consumer Act 2010* (Cth), s 137B.

247 See [33.200].

248 *I & L Securities Pty Ltd v HTW Valuers (Brisbane) Pty Ltd* [2002] HCA 41; (2002) 210 CLR 109.

249 *I & L Securities Pty Ltd v HTW Valuers (Brisbane) Pty Ltd* [2002] HCA 41; (2002) 210 CLR 109.

250 *I & L Securities Pty Ltd v HTW Valuers (Brisbane) Pty Ltd* [2002] HCA 41; (2002) 210 CLR 109, [50], following *Henville v Walker* [2001] HCA 52; (2001) 206 CLR 459.

251 *I & L Securities Pty Ltd v HTW Valuers (Brisbane) Pty Ltd* [2002] HCA 41; (2002) 210 CLR 109, [211].

252 Section 82(1B) only applies to causes of action that arose on or after 26 July 2004: *APF Properties Pty Ltd v Kestrel Holdings Pty Ltd (No 2)* [2007] FCA 1561, [366]–[377].

Section 137B would now justify the approach taken by Williams J. The applicant's economic loss was caused partly by its own carelessness and partly by the valuer's misleading conduct (which was not fraudulent and was not intended to cause loss). Accordingly, the damages a person in the applicant's position may recover would now be reduced to the extent the court thinks just and equitable having regard to the applicant's share in the responsibility for the loss or damage.

Limits to the application of s 137B

[33.143] Section 137B has no application to claims made for compensation pursuant to other provisions contained in the *ACL*. Thus, a claim based on a contravention of one of prohibitions on specific forms of misleading conduct, such as under ss 29, 30, 31, 33 or 37, will not be susceptible of reduction under s 137B.[253]

The application laws of the States and Territories do not contain a provision equivalent to s 137B of the *CCA*. Thus, damages cannot be reduced in the manner described above under the State and Territory application laws.[254] An applicant concerned about the possibility of having his or her damages reduced on the basis of a failure to take reasonable care would therefore be advised to bring a claim under the State or Territory application laws.

Multiple wrongdoers and proportionate liability

[33.145] Part VIA of the *CCA* provides for the apportionment of damages awarded under the Commonwealth application laws where loss or damage has been caused by the acts or omissions of two or more persons, acting independently or jointly. Similar provisions apply to actions for damages under the State and Territory application laws in respect of economic loss or property damage caused by misleading conduct.[255] Prior to the introduction of such provisions, wrongdoers were jointly and severally liable to the claimant. Now, the claimant can recover from each wrongdoer only the proportion of the loss or damage for which the wrongdoer is responsible.[256]

The various apportionment regimes vary slightly. Part VIA of the *CCA* will now be discussed by way of example. Part VIA applies to a claim for damages under s 236 in respect of economic loss or property damage caused by conduct in breach of s 18, provided the respondent did not intentionally or fraudulently cause the loss or damage.[257] Provided these conditions are met, the claim brought in respect of the breach of s 18 is an "apportionable claim" and the persons who caused the loss are "concurrent wrongdoers".[258] This means that the liability of a respondent "is limited to an amount reflecting that proportion of the damage or loss claimed that the court considers just having regard to the extent of the defendant's

253 *Vero Lenders Mortgage Insurance Ltd v Taylor Byrne Pty Ltd* [2006] FCA 1430, [186].

254 *Perpetual Trustee Company Ltd v Milanex Pty Ltd (in liq)* [2011] NSWCA 367, [86]–[88].

255 See *Civil Law (Wrongs) Act 2002* (ACT), Ch 7A; *Civil Liability Act 2002* (NSW), Pt 4; *Proportionate Liability Act* (NT); *Civil Liability Act 2003* (Qld), Pt 2; *Law Reform (Contributory Negligence and Apportionment of Liability) Act 2001* (SA), Pt 3; *Civil Liability Act 2002* (Tas), Pt 9A; *Wrongs Act 1958* (Vic), Pt IVAA; *Civil Liability Act 2002* (WA), Pt 1F.

256 *Shrimp v Landmark Operations Ltd* [2007] FCA 1468; (2007) 163 FCR 510, [58].

257 *Competition and Consumer Act 2010* (Cth), ss 87CB(1), 87CC(1).

258 In *Shrimp v Landmark Operations Ltd* [2007] FCA 1468; (2007) 163 FCR 510, it was held that a party is not a concurrent wrongdoer simply because his or her acts or omissions caused the loss or damage that is the subject of the claim. It is also necessary to show that the party is liable to the claimant for that loss.

responsibility for the damage or loss".[259] It does not matter that the claims against the "concurrent wrongdoers" are based on different causes of action[260] or that other "concurrent wrongdoers" are insolvent.[261] The court must also exclude any part of the loss or damage caused by the applicant's contributory negligence.[262]

These provisions apply "to all apportionable claims, whether or not all concurrent wrongdoers are parties to the proceedings".[263] A defendant is required to notify a plaintiff if the defendant has reasonable grounds to believe that a particular person may be a concurrent wrongdoer.[264]

Assume, for example, that A contracts to buy a restaurant from B Pty Ltd on the faith of a representation by B that the restaurant "seats 100". Although the restaurant has 100 seats, it is only licensed to seat 50. A engages a solicitor, C, to act for her in relation to the purchase. In breach of his duty of care, C fails to make inquiries in relation to the licence. A goes ahead and buys the restaurant and suffers loss. Assume, then, that A's loss has been caused partly by misleading conduct in trade or commerce on the part of B and partly by negligence on the part of C. A's claim against B is an "apportionable claim" under Pt VIA. Damages awarded against B under s 236 are therefore limited to an amount the court considers just, having regard to the extent of B's responsibility for A's loss or damage.

Loss or damage under s 237

[33.150] Section 237 makes provision, in the words of Mason P, for a veritable "remedial smorgasbord"[265] of orders.

Section 237 provides that:

> (1) A court may:
>
> (a) on application of a person (the *injured person*) who has suffered, or is likely to suffer, loss or damage because of the conduct of another person that:
>
> (i) was engaged in a contravention of a provision of Chapter 2, 3 or 4; or
>
> …
>
> (b) on the application of the regulator made on behalf of one or more such injured persons;
>
> make such order or orders as the court thinks appropriate against the person who engaged in the conduct, or a person involved in that conduct.
>
> (2) The order must be an order that the court considers will:
>
> (a) compensate the injured person, or any such injured persons, in whole or in part for the loss or damage; or
>
> (b) prevent or reduce the loss or damage suffered, or likely to be suffered, by the injured person or any such injured persons.

259 *Competition and Consumer Act 2010* (Cth), s 87CD(1).

260 *Competition and Consumer Act 2010* (Cth), s 87CB(2).

261 *Competition and Consumer Act 2010* (Cth), s 87CB(5).

262 *Competition and Consumer Act 2010* (Cth), s 87CD(3).

263 *Competition and Consumer Act 2010* (Cth), s 87CD(4).

264 *Competition and Consumer Act 2010* (Cth), s 87CE.

265 *Akron Securities Ltd v Iliffe* (1997) 41 NSWLR 353, 364. See generally Skapinker, "'Other Remedies' under the Trade Practices Act — The Rise and Rise of Section 87" (1995) 21 *Monash University Law Review* 189. For the history of the section, see *Tenji & Associates v Henneberry Pty Ltd* [2000] FCA 550; (2000) 98 FCR 324, [6]–[11].

Before setting out the "orders", a number of points should be noted. First, s 18, which prohibits misleading or deceptive conduct, is found in Ch 2 of the *ACL*. Chapter 2 also contains the provisions which prohibit unconscionable conduct.[266] Secondly, the phrase "a person who was involved in the contravention" is defined by s 2(1) to include persons who have aided or abetted, or have been knowingly concerned in a contravention.[267] Thirdly, unlike s 236, which is concerned only with compensation for actual loss or damage, s 237 extends to the prevention and reduction of loss or damage which is "likely to be suffered". Fourthly, the orders granted under s 237 are at the court's discretion, whereas under s 236, there is an entitlement to compensation for loss or damage caused by a contravention. Finally, the relief for which s 237 makes provision is available as a stand-alone remedy.

Section 243 sets out a non-exhaustive list of the types of orders that can be made under s 237. The orders mentioned in s 243 are, in brief, to the following effect: (a) declaring a contract void in whole or in part; (b) varying a contract; (c) refusing to enforce all or any of the provisions of the contract; (d) directing refund of money or return of property; (e) directing payment to the person who suffered loss or damage the amount of the loss or damage; (f) directing repair of, or provision of spare parts for, goods; (g) directing the supply of specified services; and (h) directing variation of, or termination of, an instrument creating or transferring an interest in land.[268]

Discretion and analogies

[33.155] The High Court has pointed out that once a causal connection has been identified between the loss and damage that allegedly has been or is likely to be suffered and the contravening conduct, there is nothing in s 237, or elsewhere in the *ACL*, which suggests that the orders that may be made under the section should be limited by drawing some analogy with the law of contract, tort or equitable remedies.[269] In particular, in granting a remedy under s 237, the court is not restricted by limitations which apply under the general law to relief in the form of rescission, such as the bar to rescission of "executed" contracts.[270]

Nevertheless, in exercising its discretion, the court may seek guidance from general law principles, as it does in assessing damages under s 236. In *Chint Australasia Pty Ltd v Cosmoluce Pty Ltd*, Einstein J said that "[t]he power of the Court to make orders in the nature of rescission under the Trade Practices Act [now *ACL*] is guided (but not controlled by) the same considerations as affect the availability of rescission in equity".[271] These principles are discussed in Chapter 39.

The Court will consider the conduct of the parties after the misleading nature of the respondent's conduct has been revealed.[272] The question whether there has been a disaffirmation or a positive affirmation of the contract, for example, will generally be relevant.[273]

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266 See Chapter 38.

267 See [33.15].

268 Cf *Contracts Review Act 1980* (NSW), s 7, see [38.90].

269 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [38].

270 *Henjo Investment Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546, 564; *Akron Securities Ltd v Iliffe* (1997) 41 NSWLR 353, 366.

271 *Chint Australasia Pty Ltd v Cosmoluce Pty Ltd* [2008] NSWSC 635, [130]. See also *Akron Securities Ltd v Ilife* (1997) 41 NSWLR 353, 367E; *Campbell v BackOffice Investments Pty Ltd* [2008] NSWCA 95, [105] (Giles JA).

272 *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546, 564.

273 *Tenji & Associates v Henneberry Pty Ltd* [2000] FCA 550; (2000) 98 FCR 324, [19].

In *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd*,[274] the applicant purchased a licensed restaurant business from the respondent. The respondent gave the impression that the seating for 128 was approved by the local council, whereas in fact the approval only extended to seating for 84. This misleading conduct was one of the factors that induced the applicant to buy the business. The business fared badly, even though in fact about 128 seats were used. The applicant commenced proceedings against the respondent, but the proceedings were not actively prosecuted by it and it had the proceedings adjourned while it sought approval from the council for increased seating. In the meantime, the management of the business changed for the worse. The applicant originally sought damages, but later sought rescission under s 87 of the *TPA* (now s 237 of the *ACL*). The majority of the Court held that rescission was not appropriate in the circumstances. In exercising its discretion, the Court took into account the delay of two years or so in bringing the case to Court and the adverse changes in the business which were not related to the misleading conduct. Damages were awarded instead.

In *Tenji & Associates v Henneberry Pty Ltd*,[275] the applicant purchased a service station from the respondent induced by misstatements as to the value of the property, the adequacy of the rent paid by the current lessee and the quantity of fuel sold per year. The trial judge refused to declare the contract void under s 87 of the *TPA* (now s 237 of the *ACL*), but awarded $10,000 instead. He considered that the applicant had not significantly overpaid for the service station and it was possible that the applicant would have offered $10,000 less than the asking price if apprised of the falsity of the misstatements. On appeal, however, the contract was declared void. It was pointed out that the question of what the applicant would have done in the absence of the misleading conduct had not been pursued at the trial. "It was not appropriate", according to Carr J, "having found that the misleading or deceptive conduct caused the [applicant] to enter the contract, to subdivide that causal effect into the effect upon the very decision to buy and the effect as to how much to pay".[276] Further, as French J said, although avoidance under s 87 (now s 237 of the *ACL*) must serve a compensatory purpose, it may serve other purposes in doing justice between the parties. An applicant may be compensated in damages, "but is left nonetheless with a continuing burden of unforeseen risk, a transaction soured by the events that surrounded it and a property, once the repository of hope for the future that is now an albatross around its neck".[277]

The requirement of "loss or likely loss"

[33.160] A person may be induced to enter a contract by misleading conduct, but not suffer any loss or likely loss. The 1998 decision of the High Court in *Marks v GIO Australia Holdings Ltd*[278] has been regarded as the leading case on this issue. The decision must now be treated with caution, however, because much of what was said in *Marks v GIO Australia Holdings Ltd* is inconsistent with the 2004 decision of the High Court in *Murphy v Overton Investments Pty Ltd*.[279] The applicants in *Marks v GIO Australia Holdings Ltd* were borrowers

274 *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546.

275 *Tenji & Associates v Henneberry Pty Ltd* [2000] FCA 550; (2000) 98 FCR 324.

276 *Tenji & Associates v Henneberry Pty Ltd* [2000] FCA 550; (2000) 98 FCR 324, [123].

277 *Tenji & Associates v Henneberry Pty Ltd* [2000] FCA 550; (2000) 98 FCR 324, [20].

278 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494.

279 *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388, discussed at [33.125].

who entered into loan facilities with the respondent, a public company financier. They relied on a written representation that the interest would be at a specified base rate plus a margin "set" at 1.25 per cent per annum. They all drew down funds under the facilities. Contrary to the representations that had been made, the loan contract itself enabled the respondent to vary the margin on giving 90 days' notice. The respondent in fact later notified the applicants that in 90 days' time the margin would be varied to 2.25 per cent per annum. The respondent gave the applicants an opportunity to withdraw from the loan contracts without penalty. The applicants did not take up this opportunity. Instead they brought proceedings against the respondent alleging misleading conduct. They sought an order under s 87 (now s 237 of the *ACL*) varying the loan contracts to make good the representation or damages under s 82 (now s 236 of the *ACL*).

At trial, the applicants did not claim that, if they had known the truth about the variation clause, they would not have borrowed at all or would have sought to make alternative arrangements. In fact, they conceded that even with the increased margin, the loan facility was more beneficial to them than any other such facility in the market.

The trial judge awarded damages calculated on the difference between the interest payable where a margin of 1.25 per cent prevailed and the interest payable if the margin were 2.25 per cent. This award was overturned on appeal and a further appeal was brought to the High Court. A majority of that Court (Gaudron, McHugh, Gummow, Hayne and Callinan JJ) held that no relief was available under either s 87 or s 82 (now ss 237 and 236, respectively).

Under s 87 (now s 237 of the *ACL*), relief can only be awarded if the applicant suffers or is likely to suffer loss or damage. According to McHugh, Hayne and Callinan JJ in a joint judgment, the applicants in this case had not suffered and were not likely to suffer loss or damage. This also ruled out damages under s 82 (now s 236 of the *ACL*). Merely entering into a contract which is different from the one represented does not demonstrate loss or damage.[280] Such loss or damage will only be demonstrated if the applicant could have acted in some other way (or refrained from acting in some way) which would have been of greater benefit or less detriment to the applicant than the course adopted.[281] In the present case, there was no cheaper loan available on the market, even taking into account the increased margin. The judges asked:

> If a person agrees to pay interest at the rate of 10% for a loan which the lender falsely represents would ordinarily command interest at the rate of 15% but which in fact would ordinarily command interest at 12%, what loss has the borrower who is misled suffered by agreeing to borrow (… assuming no more is known)?[282]

Although the operation of s 237 extends to cases where loss is *likely* to be sustained (as opposed to actually sustained), in making a compensation order, the inquiry remains one about whether it is likely that as a result of the contravention the applicant will suffer some prejudice or disadvantage.[283] McHugh, Hayne and Callinan JJ conceded, however, that it will

280 But see *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388, discussed at [33.125].

281 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [47]. Again, this point seems to be inconsistent with the later decision of the High Court in *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388, discussed at [33.125].

282 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [50].

283 *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31 was held to be wrong to the extent that it held to the contrary. However, as Gummow J points out (*Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196

be a rare case where the difference between what was represented and what was given will not be reflected in some difference in value or other manifestation of actual loss, either now or in the future.[284]

Gummow J was prepared to assume that "in an appropriate case, the exercise by one party of a contractual power to increase the legal obligations of another party may be an injury to the second party, which answers the description 'loss or damage' … in s 82 [now *ACL*, s 236]".[285] In this case, a cause of action under s 82 could not have arisen until the expiration of the 90 days. However, the applicants had been given an opportunity (before that date) to escape the imposition of what would otherwise have been an increased contractual liability. So, the imposition of the higher rate of interest was a result of their own choice not to take up the respondent's offer to let them withdraw from the loan agreement. This meant that no causal link could be established between the respondent's contravention and the applicants' loss or damage. Further, it was not an appropriate exercise of the discretion conferred on the court by s 87(1A) of the *TPA* (now s 237 of the *ACL*) to direct a variation of the loan facility to the effect that the margin was fixed at 1.25 per cent, given that the respondent had not sought to hold the applicants to their contracts.

Kirby J, dissenting, thought it was an extremely odd result that the respondent could walk away scot-free "given the character of the contraveners as a group of major financial organisations, the gravity of the contravention found, the wide variety of remedies provided by Parliament together with the public as well as the private purposes which the TPA [now *ACL*] is designed to uphold".[286]

As discussed at [33.125], in *Murphy v Overton Investments Pty Ltd*,[287] the High Court held that an applicant will suffer a loss where he or she is induced by misleading conduct to undertake obligations that prove to be larger than he or she is led to believe. This seems to contradict the reasoning of at least McHugh, Hayne and Callinan JJ in *Marks v GIO Australia Holdings Ltd*.[288] But the only reference to *Marks v GIO Australia Holdings Ltd* in the High Court's judgment in *Murphy v Overton Investments Pty Ltd* is the following statement:

> Particular attention was given, both in the reasons of the Full Court and in the arguments advanced in this court, to analysing this court's reasons in *Marks v GIO Australia Holdings Ltd* concerning the identification of loss or damage. In the end, however, the resolution of this appeal does not depend on identifying the nature or extent of any differences there may be between the separate reasons given in Marks. It depends on the application of the Act according to its terms.[289]

The decisions in *Murphy v Overton* and *Marks v GIO Australia Holdings Ltd* can be reconciled on the basis that the applicants in *Marks v GIO Australia Holdings Ltd* were given the opportunity to withdraw from the loan agreement and refinance their borrowings without

CLR 494, [104]) in *Demagogue Pty Ltd v Ramensky* it was found that the applicants would not have entered the contract in question if they had been aware of the falsity of the misleading conduct.

284 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [55].

285 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [111].

286 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [155].

287 *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388.

288 See the explanation given by RD Nicholson J in the Full Court of the Federal Court in *Murphy v Overton Investments Pty Ltd* [2001] FCA 500; (2001) 112 FCR 182, [85]–[89].

289 *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388, [43] (footnote references omitted).

penalty, rather than pay the increased rate of interest. In *Murphy v Overton Investments Pty Ltd*, the applicants were given no such opportunity to withdraw. Furthermore, the trial judge made a finding of fact that if the truth about the outgoings had been revealed, the Murphys would not have entered into the lease.[290] While the Murphys could have sold their leasehold interest in the retirement unit when the full amount of outgoings began to be charged, they would have incurred some cost in doing so and would have to pay the increased outgoings until the unit was sold.[291] In other words, *Murphy v Overton* can be reconciled with *Marks v GIO Australia Holdings Ltd* if the reasoning of Gummow J in *Marks v GIO Australia Holdings Ltd* is preferred to the reasoning of the other members of the majority in that case.[292] Even Gummow J, though, said in *Marks v GIO Australia Holdings Ltd* that it was an error "to treat GIO as obliged to make good its representations".[293]

Apportionment of damages

Claimant's failure to take reasonable care

[33.163] As discussed in [33.140], s 137B of the *CCA* (which is contained in the Part of the *CCA* that applies the *ACL* as a law of the Commonwealth)[294] requires the reduction of an award of damages under s 236(1) where the loss or damage in question has been caused partly by the claimant's failure to take reasonable care and partly by conduct that contravenes s 18. Section 137B is not expressed to apply to claims for compensation under s 237.[295] Although s 237(2) allows the court to award compensation "in whole or in part" for the loss or damage, the High Court has previously held that this does not allow the Court to award compensation for only part of the loss.[296] For example, in *I & L Securities Pty Ltd v HTW Valuers (Brisbane) Pty Ltd*, McHugh J said:

> [N]othing in [the predecessor to s 237] suggests that the amount of a compensable loss may be reduced. Nor does anything in the section suggest the grounds upon which such a reduction might be made. Rather, the insertion of the words, 'in whole or in part for the loss' emphasises the availability of remedies under [the predecessor to s 237] in situations where [other available remedies] are not appropriate, or are not sufficient, to remedy the loss or damage brought about or that may be brought about by the contravening conduct.[297]

290 *Murphy v Overton Investments Pty Ltd* [2000] FCA 801, [203] (cited by High Court at *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388, [23]).

291 See *Murphy v Overton Investments Pty Ltd* [2004] HCA 3; (2004) 216 CLR 388, [70].

292 McHugh, Hayne and Callinan JJ at *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [23] also accepted that the result might have been different if the borrowers had not been given the opportunity to refinance, but only if the new rate charged by GIO exceeded prevailing rates, so that the borrowers might be said to have lost the opportunity to make more beneficial arrangements with other lenders.

293 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [110].

294 See [33.08]–[33.15].

295 Under the Commonwealth application laws, an award of damages under *ACL*, s 236(1) will be reduced where the loss or damage in question has been caused partly by the claimant's failure to take reasonable care and partly by conduct that contravenes s 18: *Competition and Consumer Act 2010* (Cth), s 137B (see [33.140]). In *Vero Lenders Mortgage Insurance Ltd v Taylor Byrne Pty Ltd* [2006] FCA 1430, [186], Greenwood J confirmed that the predecessor to the *Competition and Consumer Act 2010* (Cth), s 137B had no application to a claim for compensation under the predecessor to the *ACL*, s 237.

296 *I & L Securities Pty Ltd v HTW Valuers (Brisbane) Pty Ltd* [2002] HCA 41; (2002) 210 CLR 109, [120].

297 *I & L Securities Pty Ltd v HTW Valuers (Brisbane) Pty Ltd* [2002] HCA 41; (2002) 210 CLR 109, 120.

Gaudron, Gummow and Hayne JJ agreed, noting that "the words 'in whole or in part' do not suggest that the combination of orders that a court makes should do less than provide full compensation for all loss and damage".[298]

I & L Securities Pty Ltd v HTW Valuers (Brisbane) Pty Ltd was decided before the introduction of provisions that allow for the reduction of damages under s 236 of the *ACL* where the claimant[299] shares responsibility for the loss or damage.

In *Khoury v Sidhu*,[300] an interlocutory decision, the Full Federal Court suggested that the introduction of these provisions may be relevant to the way in which the Court exercises its discretion under s 237 of the *ACL*. The Full Court agreed with the trial judge's observation that:

> In determining what order might be appropriate under [the predecessor to s 237] to compensate the applicants for the amount of the economic loss they suffered (and might further suffer), it is relevant to consider whether the *same* claim … if framed under [the predecessor to s 236] would be susceptible of just and equitable reduction having regard to Mr and Mrs Khoury's share in the responsibility for the loss.
>
> That consideration arises not because [the predecessor to s 237] expressly provides for a reduction of compensation … but rather, the discretion under [the predecessor to s 237] is a broad discretion to frame and make orders which provide compensation for the amount of the loss suffered as the Court considers appropriate, in all the circumstances, that is, *as justice requires*. If recovery of the entire amount of the loss, if made the subject of a claim under [the predecessor to s 236], is constrained by the factors discussed, the exercise of the discretion as to whether and if so in what amount, compensation might be payable to the applicants under [the predecessor to s 237], for the amount of the same economic loss, ought to take into account as a factor, the extent to which Mr and Mrs Khoury share in the responsibility for that loss.[301]

Concurrent wrongdoers

[33.166] As discussed at [33.145], Pt VIA of the *CCA* provides for the apportionment of damages awarded under the Commonwealth application laws where loss or damage has been caused by the acts or omissions of two or more persons, acting independently or jointly. The apportionment provisions do not apply to a claim for compensation under s 237 of the *ACL* or for a contravention of a substantive prohibition other than s 18 of the *ACL*.[302]

Causation

[33.170] Sections 236 and 237 provide that the claimant must suffer "loss or damage" *because of* the conduct of the respondent. The loss or damage must directly result from or be caused by the respondent's conduct. In most cases, the requisite causal connection is established by showing that the claimant suffered loss because he or she acted or failed to act in reliance on the misleading conduct.

298 *I & L Securities Pty Ltd v HTW Valuers (Brisbane) Pty Ltd* [2002] HCA 41; (2002) 210 CLR 109, [53].

299 See [33.140].

300 *Khoury v Sidhu* [2011] FCAFC 71.

301 *Khoury v Sidhu* [2011] FCAFC 71, [70]–[71] (emphasis in original). See also *BHPB Freight Pty Ltd v Cosco Oceania Chartering Pty Ltd (No 3)* [2009] FCA 1087, [62].

302 *Bennett v Elysium Noosa Pty Ltd (in liq)* [2012] FCAFC 120; (2012) 202 FCR 72, [275]; *Selig v Wealthsure Pty Ltd* (2015) HCA 18; (2015) 255 CLR 661, [29]–[30] (French CJ, Kiefel, Bell and Keane JJ) in relation to the equivalent proportionate liability provisions of *Corporations Act 2001* (Cth); *ABN AMRO Bank NV v Bathurst Regional Council* (2014) [2014] FCAFC 65; 224 FCR 1, 307–8; *Williams v Pisano* [2015] NSWCA 177; (2015) 90 NSWLR 342, [59]–[62].

The previous regime under the TPA contained the words "loss or damage *by* conduct". The meaning of the word "by" in this context was considered by the High Court in *Wardley Australia Ltd v Western Australia*. The majority of the Court said:

> 'By' is a curious word to use … But the word clearly expresses the notion of causation without defining or elucidating it. In this situation s 82(1) [now *ACL*, s 236(1)] should be understood as taking up the common law practical or common sense concept of causation … except in so far as that concept is modified or supplemented expressly or impliedly by the provisions of the Act.[303]

In *Henville v Walker*, Gaudron J noted that the "common-sense approach requires no more than that the act or event in question should have materially contributed to the loss or injury suffered".[304] Although common law concepts of causation are applicable, such concepts will not be applied rigidly or mechanically without regard to the terms or objects of the *ACL*. It is relevant to note that the remedial provisions apply to quite different types of contraventions, such as misleading or deceptive conduct and unconscionable conduct. Moreover, the objects of the *ACL* support an interpretation that promotes fair trading and protection of consumers.[305]

The same approach should be applied to the requirement that loss or damage arise *because of* the conduct of the defendant under ss 236 and 237 of the *ACL*.

Reliance

[33.175] Most of the cases dealing with causation concern applicants who enter contracts following misleading conduct. In that context, as under the general law relating to misrepresentation, causation is established by proving *actual reliance* on the misleading conduct in entering the contract.[306]

Misleading conduct does not necessarily cease to have causative effect merely because the applicant makes his or her own enquiries. In *Como Investments Pty Ltd v Yenald Nominees Pty Ltd*, the Court said that "the making of independent enquiries, which did not reveal reason to doubt the truth of what had been represented, does not require the conclusion that the representation itself had ceased to have any effect".[307] The fact that the applicant has some doubts about representations made to him or her does not necessarily negate a finding of reliance.[308] However, if a person who makes independent enquiries entirely discounts what the respondent said, then the misleading conduct may cease to have any operative effect.[309]

Inference of inducement

[33.180] The applicant has the burden of proving causation. However, the applicant's burden of proof may be lightened by an inference of inducement. In *Gould v Vaggelas*, a deceit case,

303 *Wardley Australia Ltd v Western Australia* (1992) 175 CLR 514, 525.

304 *Henville v Walker* [2001] HCA 52; (2001) 206 CLR 459, [61].

305 *Henville v Walker* [2001] HCA 52; (2001) 206 CLR 459, [96].

306 It is not essential that the claimant establish that he or she suffered loss in reliance on the misleading conduct. Where the misleading conduct has caused others to act to the detriment of the claimant (e.g. where misleading conduct causes others to purchase from a competitor of the applicant), the requisite causative link will still be established: *Ford Motor Company of Australia Ltd v Arrowcrest Group Pty Ltd* [2003] FCAFC 313; (2003) 134 FCR 522. See [33.110].

307 *Como Investments Pty Ltd v Yenald Nominees Pty Ltd* [1997] ATPR 41-550, 43,619.

308 *Transglobal Capital Pty Ltd v Yolarno Pty Ltd* [2005] NSWCA 68.

309 *Elitegold Pty Ltd v CM Holdings Pty Ltd* [1995] ATPR 41-422.

Wilson J stated that "[i]f a material representation is made which is calculated to induce the representee to enter into a contract and that person in fact enters into the contract there arises a fair inference of fact that he was induced to do so by the representation".[310] In *Ricochet Pty Ltd v Equity Trustees Executor & Agency Co Ltd*, the Full Federal Court applied Wilson J's statement and noted that it "provides a practical guide to the way in which inferences can and should be drawn in" misleading conduct cases.[311] In *Como Investments Pty Ltd v Yenald Nominees Pty Ltd*, the Full Court of the Federal Court applied this principle to a claim for damages for misleading conduct. The court stated the position as follows:

> Where a representation is relevant to the decision in question, and in its nature persuasive to induce the making of the decision, it accords with legal notions of causation to hold that it has a causative effect. And where a respondent, who may be taken to know his own business, has thought it was in his interests to misrepresent the situation in a particular respect, the Court may infer that the misrepresentation was persuasive. These inferences arise from the making of the representation followed by the respondent doing the thing it was calculated to induce him to do. All this is a matter of common sense.[312]

The Court went on to point out that, although the inference may be rebutted, in the absence of rebuttal, the conclusion inferred will stand.

The decision of the High Court in *Campbell v Backoffice Investments Pty Ltd*[313] signals the need for caution in applying an inference of inducement — stressing that the all of the circumstances of the case must be taken into account. Mr Campbell sold Backoffice an interest in a company called Healthy Water. Mr Weeks, who controlled Backoffice, claimed that Mr Campbell had provided him with information that overstated sales revenue and EBIT (earnings before interest and tax) of Healthy Water. Mr Weeks also gave evidence that had he knew of *both* the overstatement of sales revenue and the overstatement of EBIT he would not have purchased an interest in Healthy Water from Campbell. However, as the overstatement of EBIT was not proved, the Court needed to determine whether Backoffice would have proceeded with a purchase of shares had Mr Weeks known that sales revenue alone had been overstated. The Court of Appeal, relying on the statement in *Gould v Vaggelas*, found that Mr Weeks had been induced, by the misrepresentation about the sales revenue alone, to purchase the interest in Healthy Water. On appeal to the High Court, Gummow, Hayne, Heydon and Keifel JJ made three points about the proposition set out in *Gould v Vaaggelas*:

> First, it is a proposition expressed in relation to the law of deceit, not the operation of statutory provisions for the award of damages suffered by contravention of consumer protection provisions proscribing misleading or deceptive conduct. Secondly, the proposition carries within it a number of subsidiary questions, such as what is a 'material' representation, and when is a material representation 'calculated' to induce entry into a contract. Thirdly, because the proposition is directed to the drawing of inferences, consideration of its application must always attend closely to all of the evidence that is adduced that bears upon the question being examined.[314]

310 *Gould v Vaggelas* (1985) 157 CLR 215, 236.

311 *Ricochet Pty Ltd v Equity Trustees Executor & Agency Co Ltd* (1993) 41 FCR 229, 234.

312 *Como Investments Pty Ltd v Yenald Nominees Pty Ltd* [1997] ATPR 41-550, 43,619; see also; *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546, 558.

313 *Campbell v Backoffice Investments Pty Ltd* [2009] HCA 25; (2009) 238 CLR 304.

314 *Campbell v Backoffice Investments Pty Ltd* [2009] HCA 25; (2009) 238 CLR 304, [143].

Their Honours then went on to note:

> What is important in the present case is that the evidence that was given by Mr Weeks about what he would have done if he had known more than he did was expressed in a way that distinguished between cases where knowledge of *either* of two matters would have meant he would not proceed and cases where he attached significance to knowledge of *both* of two matters. This being the only direct evidence on the subject it was not open to the Court of Appeal to infer, from its own assessment of the materiality of the representation and its own assessment of whether the representation was calculated to induce entry into a contract, that Mr Weeks would not have proceeded with the share purchase.[315]

In *MWH Australia Pty Ltd v Wynton Stone Australia Pty Ltd (in liq)*[316] disagreement was expressed about the effect of Gummow, Hayne, Heydon and Kiefel JJ's comments in *Campbell v Backoffice Investments Pty Ltd*. Wynton Stone contracted to provide consultancy services to MWH Australia. When Wynton Stone merged with another company, MWH Australia executed a deed of novation which released Wynton Stone from its obligations under the consultancy contract. Clause 4 of the novation deed contained a warranty given by Wynton Stone that the services it had performed prior to the date of the novation deed had been performed in accordance with the terms of the consultancy agreement. MWH Australia alleged that the warranty was misleading, that the giving of the warranty induced MWH Australia to enter into the novation deed and that MWH Australia suffered loss as a consequence of its decision to enter the novation deed. MWH Australia led no evidence from the individuals involved in executing the novation deed. Instead, it relied on Wilson J's statement in *Gould v Vaggelas* and argued that the requisite causative link could be inferred from the materiality of the statement and the fact that MWH Australia actually entered into the deed. Warren CJ noted that the evidence adduced on reliance was minimal. Her Honour refused to make the inference MWH Australia invited her to make because doing so would see the matter resolved on a speculative basis. In reaching this conclusion, her Honour was influenced by Gummow, Hayne, Heydon and Kiefel JJ's comments in *Campbell v Backoffice Investments Pty Ltd*. Buchanan JA and Nettle JA acknowledged that Gummow, Hayne, Heydon and Kiefel JJ "adopted what may be seen as a more demanding approach to the proof of causation in cases of misleading or deceptive conduct".[317] However, their Honours went on to note that they saw "nothing in Campbell which runs counter to the reasoning of the Full Federal Court in *Ricochet*" and that *Ricochet Pty Ltd v Equity Trustees Executor & Agency Co Ltd* remains as an authoritative statement that "Wilson J's approach in *Gould v Vaggelas* provides a practical guide to the way in which inferences can and should be drawn in cases of this kind".[318] Buchanan JA and Nettle JA then concluded that, in light of the relevant surrounding facts and circumstances including the course of conduct leading up to the execution of the novation deed, a fair inference arose that the warranty operated as an inducement. In *Lord Buddha Pty Ltd v Harpur*, the Full Court of the Victorian Supreme Court agreed with Buchanan JA and Nettle JA that "the approach in *Gould v Vaggelas*, while it is not to be taken as an exhaustive rule, remains as a guide to resolving questions of fact which may arise in cases of this kind".[319]

315 *Campbell v Backoffice Investments Pty Ltd* [2009] HCA 25; (2009) 238 CLR 304, [147] (emphasis in original).

316 *MWH Australia Pty Ltd v Wynton Stone Australia Pty Ltd (in liq)* [2010] VSCA 245.

317 *MWH Australia Pty Ltd v Wynton Stone Australia Pty Ltd (in liq)* [2010] VSCA 245, [103].

318 *MWH Australia Pty Ltd v Wynton Stone Australia Pty Ltd (in liq)* [2010] VSCA 245, [105].

319 *Lord Buddha Pty Ltd v Harpur* [2013] VSCA 101; (2013) 41 VR 159, [158].

In *Australian Competition and Consumer Commission v TPG Internet Pty Ltd*,[320] French CJ, Crennan, Bell and Keane JJ stated: "[i]t has long been recognised that, where a representation is made in terms apt to create a particular mental impression in the representee, *and is intended to do so*, it may be inferred that it has had that effect".[321] *Gould v Vaggelas* is cited in support of this "long recognised" proposition of law. No reference is made to Gummow, Hayne, Heydon and Kiefel JJ's comments in *Campbell v Backoffice Investments Pty Ltd*.

The but for test

[33.185] The *but for* test of causation is often considered a useful threshold test to determine whether loss was caused by the misleading conduct. Applying the test in the context of misleading conduct, the question is: "Would the applicant have entered the contract with the respondent *but for* the respondent's misleading conduct?" If the answer is "no", this establishes a causal link between the misleading conduct and the act of entering the contract. If the answer is "yes, the applicant would still have entered the contract even in the absence of the misleading conduct", this may suggest that there is no causal link between the misleading conduct and the act of entering the contract.

However, the but for test is no longer regarded as comprehensive or exclusive. In *Marks v GIO Australia Holdings Ltd* McHugh, Hayne and Gummow JJ noted that "[a]nalysing the question of causation only by reference to … a 'but for' test has been found wanting in other contexts and it may well be found that it is not an exclusive test of causation".[322] As will be discussed below, the courts have been prepared to hold that loss was caused by misleading conduct even where the but for test has not been satisfied.

In the past, the courts have stated that the but for test must be applied in a common sense way. It had also been recognised that the outer bounds of liability may be determined by policy considerations and value judgments as to whether the respondent ought to be taken to have caused the loss in question.[323] However, the recent High Court decision of *Travel Compensation Fund v Tambree*[324] calls into question the common sense qualification and the relevance of broad policy considerations when determining causation under the *ACL*. Gummow and Hayne JJ expressed doubt as to whether there is any "common sense" notion of causation that can provide a useful legal norm.[325] Gummow and Hayne JJ also held that it was inappropriate to determine causation by reference to the broad question of whether the respondent ought to be held liable for the loss in question. While policy is relevant, it is only the policy underpinning the particular cause of action that should be considered.[326] Gleeson CJ also noted that when determining whether "loss or damage is 'by' misleading or deceptive conduct

320 *Australian Competition and Consumer Commission v TPG Internet Pty Ltd* [2013] HCA 54; (2013) 250 CLR 640, [55] (emphasis added). See also *Lord Buddha Pty Ltd v Harpur* [2013] VSCA 101; (2013) 41 VR 159, [159].

321 *Lord Buddha Pty Ltd v Harpur* [2013] VSCA 101; (2013) 41 VR 159, [159]. See also *Hanave Pty Ltd v LFOT Pty* [1999] FCA 357.

322 *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494, [42].

323 *March v Stramare Pty Ltd* (1991) 171 CLR 506; *Chappel v Hart* [1998] HCA 55; (1998) 195 CLR 232, [22]–[26]; *Ruddock v Taylor* [2003] NSWCA 262; (2003) 58 NSWLR 269, [88].

324 *Travel Compensation Fund v Tambree* [2005] HCA 69; (2005) 224 CLR 627.

325 *Travel Compensation Fund v Tambree* [2005] HCA 69; (2005) 224 CLR 627, [45].

326 *Travel Compensation Fund v Tambree* [2005] HCA 69; (2005) 224 CLR 627, [46]–[47].

… it is in the purpose of the statute, as related to the particular circumstances of the case, that the answer to the question of causation is to be found".[327] Although Callinan J opined that it would be "delusion to think that a disputed question of causation can be resolved according to an invariable scientific formula, and without acknowledgement of common sense",[328] he agreed that the scope and objects of the statute are of critical importance to determining causation. Kirby J did not oppose the consideration of broader policy questions and believed that common sense must also have a role to play in determining causation.

The New South Wales Court of Appeal in *Abigroup Contractors Pty Ltd v Sydney Catchment Authority (No 3)*[329] held that there was a causative link between the applicant's loss and the respondent's misleading conduct, despite the fact that the but for test was not satisfied on the facts. The applicant contractor successfully tendered to construct a spillway for a dam for the respondent authority. The authority represented that no plans were available of an outlet pipe. In fact, such plans were available and, had the applicant seen those plans, it would have known that the project would require significantly more excavation work. The applicant sued for the cost of doing the additional work. Although it assumed all risks for any additional costs, the applicant argued that it would not have entered into the contract on the terms that it did if the respondent had disclosed the relevant plans. The respondent argued that the loss was not caused by its misleading conduct. It argued that, but for the statement that there were no plans of the outlet pipe, the applicant would nevertheless have entered into the contract because it still would not have known about the further excavation work that would be required. The respondent argued that the relevant question was not whether the applicant would have acted differently if it had been told that there was a plan of the outlet pipe available. The respondent's argument was described as an exemplification of the but for test. The Court of Appeal rejected the respondent's argument and held that s 82 (now s 236 of the *ACL*) does not operate so simplistically.[330]

Referring to *Travel Compensation Fund v Tambree*, the Court noted that the approach to determining causation is to be found in the purpose of the statute. The Court observed that the purpose of the statutory prohibition against misleading conduct is to provide relief for persons who suffered loss by contravening conduct. Against this background, the question of causation is not answered by asking what the applicant would have done but for the misleading representation. Rather, it is necessary to determine what would have had to occur for the principal not to have engaged in conduct that was misleading. This would have required the plans to be disclosed. The loss was held to have been caused by the misleading conduct because if the applicant had seen the plans, it would have put in a different tender that took account of the need to do the additional excavation work.[331]

Several inducing factors

[33.190] The misleading conduct need not be the only factor that influences the applicant's behaviour. It need only be a cause or factor. As Hayne J says: "[s]eldom, if ever, will contravening

327 *Travel Compensation Fund v Tambree* [2005] HCA 69; (2005) 224 CLR 627, [30].

328 *Travel Compensation Fund v Tambree* [2005] HCA 69; (2005) 224 CLR 627, [81].

329 *Abigroup Contractors Pty Ltd v Sydney Catchment Authority (No 3)* [2006] NSWCA 282; (2006) NSWLR 341.

330 *Abigroup Contractors Pty Ltd v Sydney Catchment Authority (No 3)* [2006] NSWCA 282; (2006) NSWLR 341, [56].

331 See also *Lockyer Investment Co Pty Ltd v Smallacombe* (1994) 50 FCR 358.

conduct be the *sole* cause of a person suffering loss. Other factors will always be capable of identification as a cause of the person suffering loss".[332] In *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd*, Lockhart J confirmed the view that "recovery … is founded by the applicant's actual reliance upon the misleading or deceptive conduct of the respondent although that conduct was not the only factor in the applicant's decision to enter a particular agreement".[333] The position is the same under the general law.[334]

But must the misleading conduct be significant as an inducing factor? In *Metcalfe v NZI Securities Australia Ltd* Sackville J said that the applicant "must show, on the balance of probabilities, that the misrepresentation played some part — beyond the trivial — in inducing him or her to enter the contract".[335] In *Gould v Vaggelas*[336] a case involving fraudulent misrepresentation, Wilson J said it was sufficient if the representation "plays some part even if only a minor part in contributing to the formation of the contract".[337]

Some judges, however, prefer a more restrictive test requiring substantial or essential cause.[338] In *Como Investments Pty Ltd v Yenald Nominees*,[339] for example, the Full Federal Court acknowledged that while people are often swayed by several considerations influencing them to varying extents, "the law attributes causality to a single one of those considerations, provided it had some substantial rather than negligible effect".[340] In *Henville v Walker*, McHugh J adopted the view that, provided the defendant's breach materially contributed to the damage,

> it will be regarded as a cause of the damage, despite other factors or conditions having played an even more significant role in producing the damage. As long as the breach materially contributed to the damage, a causal connection will ordinarily exist even though the breach without more would not have brought about the damage.[341]

Effect of subsequent discovery of misleading conduct

[33.195] An applicant who learns of the misleading nature of the respondent's conduct may not always be able to claim damages in respect of losses subsequently incurred. In *Baillieu Knight Frank (Gold Coast) Pty Ltd v Susan Pender Jewellery*, the Court gave the following example:

> If a lessee who has entered into a lease in reliance on a misrepresentation subsequently learns that the representation was false, but nonetheless consciously chooses to continue in possession, a court might conclude that any further losses were caused by the decision to retain possession rather than by the original representation. Whether such a conclusion is to be drawn in a particular case depends on the circumstances.[342]

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332 *Henville v Walker* [2001] HCA 52; (2001) 206 CLR 459, [163].

333 *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546, 558–9.

334 See [32.95].

335 *Metcalfe v NZI Securities Australia Ltd* [1995] ATPR 41-418, 40,672.

336 *Gould v Vaggelas* (1985) 157 CLR 215.

337 *Gould v Vaggelas* (1985) 157 CLR 215, 236.

338 See cases referred to in *Australian Protective Electronics Pty Ltd v Pabflow Pty Ltd* [1996] ATPR 41-524, 42,737.

339 *Como Investments Pty Ltd v Yenald Nominees Pty Ltd* [1997] ATPR 41-550.

340 *Como Investments Pty Ltd v Yenald Nominees Pty Ltd* [1997] ATPR 41-550, 43,619.

341 *Henville v Walker* (2001) 182 ALR 37, 61.

342 *Baillieu Knight Frank (Gold Coast) Pty Ltd v Susan Pender Jewellery* [1997] ATPR 41-542, 43,525.

However, proceeding to settlement of a contract after learning of the misleading nature of the respondent's conduct does not necessarily negate the causal connection between the misleading conduct and loss subsequent on settlement. As the Court said in *Como Investments Pty Ltd v Yenald Nominees Pty Ltd*:

> There is all the difference in the world between a would be investor, who is free to make or not to make an offer, and the situation of a party bound by contract who discovers that, at the date of settlement although not (so far as he is aware) at the date of contract, a default exists. It is not easy to extricate oneself from a binding contract just prior to settlement. Extrication, even if possible, is unlikely to come without cost.[343]

In *Warwick Entertainment Centre Pty Ltd v Alpine Holdings Pty Ltd*[344] the Court focussed on whether the decision to proceed with the transaction in question was reasonable. As the applicants had expended a considerable sum in establishing the business, their decision to complete the contract rather than terminate it did not sever the causal connection between the loss suffered and the misleading conduct.[345]

Failures by the applicant

[33.200] An applicant may fail to make appropriate investigations regarding the accuracy of a respondent's misleading statement. Such failure has generally not been regarded as negating the causal link between the misleading conduct and the applicant's loss.[346] As Santow JA explained in *Havyn Pty Ltd v Webster*:

> [w]here a misrepresentation is in fact relied upon by an innocent party to induce him or her to enter a contract it is … difficult to see how that very reliance can be treated as cancelling out the causative effect of the misrepresentation because of some supposed carelessness by the party in so relying.[347]

Although reliance need not be reasonable,[348] it has been suggested that an applicant's neglect may be so extreme that it negates the causal link.[349] In *Argy v Blunts and Lane Cove Real Estate Pty Ltd*, the Court said:

> A case can perhaps be imagined where the applicant is so negligent in protecting his interest that there will be a finding of fact that the representation complained of was not in the circumstances a real inducement to his entering into a contract. In such a case the element of causation between the misrepresentation and damage will have been severed by the intervention of the negligence of the applicant.[350]

The negating of causation by events intervening between breach and damage is likely to be exceptional, and restricted, in the words of McHugh J, to cases involving an "abnormal event".[351]

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343 *Como Investments Pty Ltd v Yenald Nominees Pty Ltd* [1997] ATPR 41-550, 43,620.

344 *Warwick Entertainment Centre Pty Ltd v Alpine Holdings Pty Ltd* [2005] WASCA 174; (2005) 224 ALR 134.

345 *Warwick Entertainment Centre Pty Ltd v Alpine Holdings Pty Ltd* [2005] WASCA 174; (2005) 224 ALR 134, [74]–[75].

346 *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546, 558; *Marks v GIO Australia Holdings Ltd* [1998] HCA 69; (1998) 196 CLR 494.

347 *Havyn Pty Ltd v Webster* [2005] NSWCA 182, [122].

348 *Sykes v Reserve Bank of Australia* (1998) 88 FCR 511, 522.

349 *Munchies Management Pty Ltd v Belperio* (1988) 58 FCR 274, 286–7.

350 *Argy v Blunts and Lane Cove Real Estate Pty Ltd* (1990) 26 FCR 112, 191.

351 *Henville v Walker* [2001] HCA 52; (2001) 206 CLR 459, [106].

Although an applicant's failure to take care of his or her own interests will almost invariably not negate a causal connection existing between the respondent's contravention and the applicant's loss, under the Commonwealth application legislation only, damages available under s 236 for breach of s 18 may be reduced where the loss or damage is partly attributable to the applicant's failure to take reasonable care.[352] The provision is clearly applicable where the applicant's failure to take care is independent of the misleading conduct.[353] It remains to be seen whether the applicant's damages will be reduced where he or she has failed to take reasonable care to discover the falsity of a respondent's representation.

The courts have taken the view that it is no answer to a claim for damages for loss or damage that the applicant "should have made its own inquiries and that, if it had done so, it would have found out the true position".[354] In such circumstances, it may well be said that the loss or damage is caused partly by the misleading conduct and partly by the applicant's failure to take reasonable care. An alternative interpretation of the Commonwealth provision allowing for the reduction of damages mentioned in the previous paragraph is that it only requires a reduction of damages where the applicant's failure to take care is independent of the misleading conduct.[355]

Causation without reliance

[33.203] Direct reliance by a plaintiff on the impugned misleading conduct is not the only way to establish causation. Where there are a series of transactions or events and intermediaries are involved — for example, the misleading conduct of the respondent induces an innocent party to act in some way, and the innocent party's act causes the applicant's loss — it will be necessary to plead an "indirect" theory of causation. For example, where the respondent makes an untrue statement about the applicant's products which results in the applicant losing sales, the applicant's "loss or damage" will be determined by reference to the consequent loss of profits.[356] *Larrikin Music Publishing Pty Ltd v EMI Songs Australia Pty Ltd*[357] provides an interesting example. Larrikin owns the copyright in the iconic Australian round "Kookaburra sits in the old gum tree" (Kookaburra song). When similarities between the Kookaburra song and Men at Work's 1981 song "Down Under" were revealed on the music quiz show "Spicks and Specks", Larrikin brought proceedings against the owners of copyright in the words and music of "Down Under" (the respondents). Larrikin framed its claim for a share of sales royalties on copyright infringement laws. However, it could not rely on these laws when claiming a share in performance income because Larrikin assigned its performance rights in the Kookaburra song to the Australian Performing Right Association (APRA), a collecting agency that administers public performance and communication rights in works. APRA licences the

352 *Competition and Consumer Act 2010* (Cth), s 137B. See further [33.140].

353 An example of carelessness that is independent of the misleading conduct is provided by the facts of *I & L Securities Pty Ltd v HTW Valuers (Brisbane) Pty Ltd* (2002) 210 CLR 109, discussed at [33.140].

354 *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546, 558, following the approach taken in *Redgrave v Hurd* (1881) 20 Ch D 1 in relation to the right to rescind in equity for innocent misrepresentation: see [32.95].

355 As was the case in *I & L Securities Pty Ltd v HTW Valuers (Brisbane) Pty Ltd* (2002) 210 CLR 109, discussed at [33.140].

356 *Snyman v Cooper* (1990) 24 FCR 433; *Janssen-Gilag Pty Limited v Pfizer Pty Limited* (1992) 37 FCR 526, 529.

357 *Larrikin Music Publishing Pty Ltd v EMI Songs Australia Pty Ltd* [2010] FCA 29.

works to those who wish to use the music and remits part of the licence fee collected to the copyright owners. The past performances of "Down Under" did not constitute copyright performance right infringement because APRA, the owner of the performance rights in the both songs, had authorised the songs to be played. As it could not rely on copyright laws with respect to lost performance payments, Larrikin made a claim against the respondents under the predecessor to s 236 of the *ACL*. Jacobson J found for Larrikin. The respondents had represented to APRA that it was entitled to 100 per cent of the performance income and that "Down Under" did not infringe copyright in any other work. These representations were misleading or deceptive. In reliance on these representations, APRA paid 100 per cent of the performance income to the respondents, something it would not have done but for the respondent's misrepresentations. This caused Larrikin loss that was compensable under s 82 of the *TPA* (now s 236 of the *ACL*) even though Larrikin had not itself relied on the misleading representations.[358]

Indirect or market causation

[33.204] A second category of indirect causation involves reliance on the intermediary of the market to represent an accurate price. Initially it was thought this form of indirect reliance was not available in Australia. This was suggested by cases involving reliance on a valuation by a third party.

In *Digi-Tech (Australia) Ltd v Brand*[359] the appellants (investors) submitted that it was not necessary for a party seeking to recover damages to show direct reliance upon misleading conduct by the representor. The appellants relied upon an independent valuation report based on alleged misleading profit forecasts provided by Digi-Tech. They submitted that the misleading conduct might cause other persons to act in a way that led to the loss suffered by a plaintiff. The New South Wales Court of Appeal rejected the "indirect causation theory" as a test of causation because it had not been pleaded in the original statement of claim.

By way of obiter the Court stated that in cases of misrepresentation inducing a transaction, where plaintiffs claim to have suffered loss because they are induced by misleading representations of other persons, they must themselves have relied on the misleading statements.[360] This reasoning was approved by the New South Wales Court of Appeal in *Ingot Capital Investments Pty Ltd v Macquarie Equity Capital Markets Ltd*[361] noting parties who know the truth of a representation or are indifferent to it will not be misled.[362]

A different conclusion has been reached in subsequent raising "indirect" or "market-based" causation where the misleading conduct has led to shares being overvalued by the market and in this way causing loss to investors. Under this kind of claim, the argument is that where misleading conduct leads to distortions in the market price, that distortion will cause loss to the plaintiffs who acquire the shares at a wrongly inflated price.

358 The quantum of damages was determined in a separate proceeding: see *Larrikin Music Publishing Pty Ltd v EMI Songs Australia Pty Ltd (No 2)* [2010] FCA 698.

359 *Digi-Tech (Australia) Ltd v Brand* [2004] NSWCA 58 (Sheller JA, Ipp JA and McColl JA).

360 *Digi-Tech (Australia) Ltd v Brand* [2004] NSWCA 58, 62 [159].

361 *Ingot Capital Investments Pty Ltd v Macquarie Equity Capital Markets Ltd* (2008) 73 NSWLR 6531; (2008) 73 NSWLR 653, [12]–[13] (Giles JA), [616]–[618] (Ipp JA).

362 *Ingot Capital Investments Pty Ltd v Macquarie Equity Capital Markets Ltd* (2008) 73 NSWLR 6531; (2008) 73 NSWLR 653, [12]–[13] (Giles JA), [616]–[618] (Ipp JA).

In *Re HIH Insurance Ltd (in liq)*,[363] the plaintiffs were shareholders in HIH. They acquired their shares following the publication by HIH of its financial results over the period 1998–2000, which overstated the company's financial position. The results contravened what is now s 18 of the *ACL*. The plaintiffs did not seek to prove that they had acquired their shareholdings in reliance on HIH's misrepresentations. Instead the plaintiffs argued that they had acquired the shares on the Australian Stock Exchange (ASX) at a market price that had been artificially inflated through the misrepresentations which "conveyed to the market an overoptimistic impression of HIH's financial position and prospects".[364]

Brereton J distinguished *Digi-Tech (Australia) Pty Ltd v Brand* and *Ingot Capital Investments Pty Ltd v Macquarie Equity Capital Markets Ltd*.[365] His Honour held that reliance by the claimant on the contravening conduct was not a necessary element for a claim for damages under the equivalent of s 236 of the *ACL* (previously s 82 of the *TPA*):

> The ultimate issue posed by TPA s 82 (and its equivalents) is one of causation, not one of reliance, and reliance is not a substitute for the fundamental question of causation. The word 'by' signifies no more than that the loss or damage has to have been brought about by virtue (or reason) of the contravening conduct. As a matter of principle, if causation — 'by conduct of' — can otherwise be established, it cannot matter that reliance is not established. Thus, the statutory cause of action does not, *per se*, include reliance as a necessary material fact (although that is not to say that it will not be one, as a matter of fact, in the context of many, if not most, individual cases).[366]

It was sufficient that somewhere in the chain of causation, someone, not necessarily the claimant, had relied on the contravening conduct.[367] Brereton J explained that:

> In those circumstances, I do not see how the absence of direct reliance by the plaintiffs on the overstated accounts denies that the publication of those accounts caused them loss, if they purchased shares at a price set by a market which was inflated by the contravening conduct: the contravening conduct caused the market on which the shares traded to be distorted, which in turn caused loss to investors who acquired the shares in that market at the distorted price. In the absence of any suggestion that any of the plaintiffs knew the truth about, or were indifferent to, the contravening conduct, but proceeded to buy the shares nevertheless. I conclude that 'indirect causation' is available and direct reliance need not be established.[368]

Therefore, "indirect causation" was available to found a claim under s 236 of the ACL and direct reliance need not be established.[369] To make their case the plaintiffs would need to establish, by evidence and/or inference, that the contravening conduct distorted the market price so as to cause the shares to trade at an inflated price.[370] As Brereton J indicates, it is also

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363 *Re HIH Insurance Ltd (in liq)* [2016] NSWSC 482; (2016) 335 ALR 320. See Legg and Harkin, "Judicial Recognition of Indirect Causation and Shareholder Class Actions" (2016) 44 *Australian Business Law Review* 429.

364 *Re HIH Insurance Ltd (in liq)* [2016] NSWSC 482; (2016) 335 ALR 320, [38].

365 *Re HIH Insurance Ltd (in liq)* [2016] NSWSC 482; (2016) 335 ALR 320, [72].

366 *Re HIH Insurance Ltd (in liq)* [2016] NSWSC 482; (2016) 335 ALR 320, [42], [50].

367 *Re HIH Insurance Ltd (in liq)* [2016] NSWSC 482; (2016) 335 ALR 320, [56].

368 *Re HIH Insurance Ltd (in liq)* [2016] NSWSC 482; (2016) 335 ALR 320, [77].

369 See also *Caason Investments Pty Ltd v Cao* [2015] FCAFC 94; (2015) 236 FCR 322, [85]–[86] (Gilmour and Foster JJ), [187] (Edelman J); *Grant-Taylor v Babcock & Brown Ltd (in liq)* [2016] FCAFC 60; (2016) 245 FCR 402, [219]–[220]; *TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited* [2019] FCA 1747, [1634]–[1672] (Beach J).

370 *Re HIH Insurance Ltd (in liq)* [2016] NSWSC 482; (2016) 335 ALR 320, [78].

possible that market-based causation would be denied in circumstances where an investor knew or was indifferent to the true state of affairs and did not rely on the market price as a signal of the value of the shares.[371]

EXCLUSION CLAUSES AND DISCLAIMERS

[33.205] A variety of devices have been employed in an attempt to avoid the statutory prohibition against misleading or deceptive conduct.

Contracting parties often seek to limit liability by including an "entire agreement" or an "acknowledgment clause" in a contractual document. An entire agreement clause (which is also sometimes referred to as a *merger clause*) purports to limit a party's duties to the terms set out in the written document and will often include a declaration that the agreement represents the entire understanding reached between the parties.[372] Under an acknowledgment clause, one party declares that, in entering into the contract, it has not relied on any representations made by the other contracting party.[373] It is also common for one party to include in a non-contractual document a disclaimer about the accuracy of information provided.[374]

It is not possible to exclude the statutory liability that arises from a contravention of s 18 of the *ACL* by force of contractual provision or disclaimer alone. As Gummow, Hayne, Heydon and Kiefel JJ noted in *Campbell v Backoffice Investments Pty Ltd*:

> [O]f itself, neither the inclusion of an entire agreement clause in an agreement nor the inclusion of a provision expressly denying reliance upon pre-contractual representations will necessarily prevent the provision of misleading information before a contract was made constituting a contravention of the prohibition against misleading or deceptive conduct by which loss or damage was sustained … [W]hether conduct is misleading or deceptive is a question of fact to be decided by reference to all of the relevant circumstances, of which the terms of the contract are but one.[375]

Accordingly, disclaimer or contractual provision can only affect statutory liability if:

1. it has the effect that the relevant conduct cannot be properly characterised as misleading or deceptive; or
2. it has the effect that the claimant cannot successfully establish that it reasonably relied on the misleading or deceptive conduct and, therefore, is unable to prove that the conduct caused the loss.

In *Poulet Frais Pty Ltd v The Silver Fox Company Pty Ltd*,[376] the respondent used a disclaimer at the time of providing information, required the applicant to sign an acknowledgment clause and included a merger clause in the resulting contract. During the course of negotiations

371 See also *TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited* [2019] FCA 1747, [1668] (Beach J).

372 See, eg, Special Condition 7 in *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546, 550.

373 See, eg, Special Condition 6 in *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546, 549–550.

374 See, eg, the disclaimer included on the marketing brochure in *Butcher v Lachlan Elder Realty Pty Ltd* [2004] HCA 60; (2004) 218 CLR 592, [7], [10].

375 *Campbell v Backoffice Investments Pty Ltd* [2009] HCA 25; (2009) 238 CLR 304, [130]. See also *Guirguis Pty Ltd v Michel's Patisserie System Pty Ltd* [2017] QCA 83; [2017] 1 Qd R 132.

376 *Poulet Frais Pty Ltd v The Silver Fox Company Pty Ltd* [2005] FCAFC 131.

about a potential franchise agreement, the respondent provided the applicant with disclosure documents. These disclosure documents included estimates about the likely level of sales and profitability of a franchise. However, the documents also made it clear that the respondent was providing no guarantee that the estimates would be achieved and that the applicant should make its own enquiries and form its own view about the likelihood that the projected sales would be achieved. The document also stated that the applicant should seek legal advice about the effect of the transaction and financial advice on the franchise proposition before signing the franchise agreement. The respondent also required the applicant to sign a statement in which it acknowledged that it had or would undertake its own investigations, that independent advice would be sought and that it had not relied and would not rely on the material in the disclosure statements. The resulting contract itself also included a clause whereby the applicant acknowledged that no representations or warranties about the likely success of the franchise had been given and that, in deciding to enter into the contract, the applicant had relied on its own personal assessments.

Even though the estimates of the level of sales and profitability of the franchise were not met, the respondent was held not to be liable for misleading or deceptive conduct. No reasonable person in the position of the claimants who had read and considered the documentary material provided by the respondent could have been under the illusion that the respondent was representing that the sales projections would necessarily be achieved. The Court also noted that it was "not easy to see how [the respondent] could have made more clear than it did that it was making no representations … touching on the likely profitability of [the franchise]".[377] The Court also observed that even if the methods used by the respondent did not negate a misleading impression created by the disclosure documents, the claimants would not have been able to establish that they relied on the information provided by the respondents. The respondents also represented that they carefully selected potential franchise sites. As the disclaimer and acknowledgements related to the profit representations, they would not have protected the respondent had this representation been held to be misleading. However, the Court made a factual finding that the respondent had, in fact, carefully selected the site for the applicant's franchise.

Given the various methods employed by the respondent, the Court's conclusion in this case is not surprising. In the sections that follow, we consider cases in which the parties have relied on one particular method of excluding or limiting liability.

Disclaimers

[33.210] An appropriately worded disclaimer, if sufficiently prominent and contemporaneous with the alleged misconduct, may prevent the alleged misconduct from being misleading or make it difficult for a fully informed person to show actual reliance.[378] For a disclaimer to negate potentially misleading conduct, it must be worded unambiguously and feature prominently, and it must be communicated to the reader that the disclaimer is relevant to the information it is seeking to qualify.[379]

377 *Poulet Frais Pty Ltd v The Silver Fox Company Pty Ltd* [2005] FCAFC 131, [79].

378 *Kewside Pty Ltd v Warman International Ltd* [1990] ATPR (Digest) 46-059, 53,222. See also *BMD Major Projects Pty Ltd v Victorian Urban Development Authority* [2009] VSCA 221.

379 *Medical Benefits Fund of Australia v Cassidy* [2003] FCAFC 289; (2003) 135 FCR 1, [37]–[41].

In *Butcher v Lachlan Elder Realty Pty Ltd*[380] a brochure produced by the respondent real estate agent contained a diagram that inaccurately depicted the boundaries of the property. The brochure included the following disclaimer: "All information contained herein is gathered from sources we believe to be reliable. However, we cannot guarantee it's [sic] accuracy and interested parties should rely on their own enquiries." The majority (Gleeson CJ, Hayne and Heydon JJ) held that:

> it is important that the agent's conduct be viewed as a whole. It is not right to characterise the problem as one of analysing the effect of its 'conduct' divorced from 'disclaimers' about that 'conduct' and divorced from other circumstances which might qualify its character. Everything the agent did up to the time when the purchasers contracted to buy the … land must be taken into account.[381]

The majority held that the disclaimer was effective to prevent the agent's conduct from being misleading. A variety of considerations led to this conclusion, including the nature of the parties involved and the short length of the marketing brochure. The claimants were sophisticated buyers who had access to legal and other professional advice. The respondent agent, on the other hand, was a small local real estate agent who did not hold itself out as having the means to independently verify title details about the property. Furthermore, the brochure consisted of only two pages and the disclaimer was there to be read. It was therefore held by the majority that the disclaimer had the effect of changing the nature of the representation made by the agent. The brochure conveyed the message that, although the agent believed the information to be accurate, it was not guaranteeing its accuracy. The conduct was, on this basis, held not to be misleading or deceptive. McHugh J dissented. He held that the disclaimer did not operate to overcome the misleading nature of the course of conduct engaged in by the real estate agent. This conduct included the fact that the agent's representative did not reinforce the disclaimer at a site inspection when Butcher had discussions with his architect which made it clear that Butcher's renovation plans were dependent upon the accuracy of the boundaries depicted in the brochure. Kirby J also dissented. He held that the tiny typeface used for the disclaimer suggested that the information was not important. He believed it required "a large measure of judicial self-deception to say that the purchasers should have read the written disclaimers invoked here".[382]

A disclaimer may also be effective, even if the person seeking to rely on it makes it clear that they are the source of the information, provided the Court is satisfied that it removes any misleading character the conduct may otherwise have had.[383] For example, the respondent may deny expertise about a particular subject matter or advise the other party that it has only made very limited enquiries.[384] Whether or not a disclaimer is effective in such circumstances involves consideration of the particular circumstances of the case and the representation made by the disclaimer. *Havyn Pty Ltd v Webster*[385] also involved the misdescription of real estate. A brochure produced to sell a block of six units stated that each flat was approximately

380 *Butcher v Lachlan Elder Realty Pty Ltd* [2004] HCA 60; (2004) 218 CLR 592, discussed at [33.40].

381 *Butcher v Lachlan Elder Realty Pty Ltd* [2004] HCA 60; (2004) 218 CLR 592, [39].

382 *Butcher v Lachlan Elder Realty Pty Ltd* [2004] HCA 60; (2004) 218 CLR 592, [217].

383 See discussion of *Poulet Frais Pty Ltd v The Silver Fox Company Pty Ltd* [2005] FCAFC 131, [33.205].

384 *NEA Pty Ltd v Magneta Mining Pty Ltd* [2007] WASCA 70, [118].

385 *Havyn Pty Ltd v Webster* [2005] NSWCA 182.

63 square metres in area. The brochure included a disclaimer which said, "the information contained herein … has been supplied to us and we have no reason to doubt its accuracy, however we cannot guarantee it". The representation about the approximate area of each flat was incorrect and had been determined by the real estate agent "pacing out" part of one of the units in the block and calculating the estimate from that. The Court held that the disclaimer did not negate the misleading representation about the approximate area of the flats.

This case was distinguished from *Butcher v Lachlan Elder Realty Pty Ltd* on the basis that, unlike complex title information, the area of a flat could easily be determined by a real estate agent. Furthermore, the disclaimer itself was misleading. The information had not been supplied to the agent and, given the haphazard method used by the agent to calculate the approximate area of the flats, the proposition that the agent had no reason to doubt its accuracy was untrue. The disclaimer was therefore held to be ineffective and itself misleading.

Exclusion clauses

[33.215] The application legislation in some States provides that there can be no contracting out of the *ACL*.[386] In any event, there is ample authority for the view that attempts to exclude liability by way of an exclusion clause are unlikely to succeed.[387] In *Bowler v Hilda Pty Ltd*, Heerey J referred to:

> what is now a substantial body of authority … which holds that exclusionary … clauses cannot override the statutory prohibition against misleading or deceptive conduct or prevent the grant of appropriate statutory relief where loss or damage is, as a matter of fact, caused by a contravention of the statute.[388]

His Honour referred to a review of the authorities by Burchett J in *Lezam Pty Ltd v Seabridge Australia Pty Ltd*.[389]

Section 18 is, apart from anything else, a consumer protection provision aimed at protecting the public from misleading conduct. It would be contrary to public policy for a clause to effectively oust a statutory remedy.[390] This is certainly true in respect of a clause that purports to exclude a statutory liability that has already arisen, for example, in respect of pre-contractual representations. In such a case, the misleading conduct has already been engaged in by the time the contract is signed.[391] But it is equally true of attempts to prevent statutory liability from arising. For example, if the retainer between a professional consultant and a client contained an exclusion clause that purported to exclude liability for any misleading conduct contravening s 18, such a clause would be ineffective.

In *NEA Pty Ltd v Magenta Mining Pty Ltd*[392] the respondent stated that crushing equipment it hired to the applicant was fit for the purpose of crushing ore stockpiled by the applicant. The contract for hire included clause 8, which provided "that no warranty or condition expressed

386 *Fair Trading Act 1989* (Qld), s 107; *Fair Trading Act 1987* (SA), s 96; *Fair Trading Act 2010* (WA), s 13 (but see s 105).

387 As to the effect of exclusion clauses on misrepresentation under the general law, see [32.75] and [32.80].

388 *Bowler v Hilda Pty Ltd* (1998) 80 FCR 191, 207.

389 *Lezam Pty Ltd v Seabridge Australia Pty Ltd* (1992) 35 FCR 535, 556–7.

390 *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546, 561.

391 *Byers v Dorotea Pty Ltd* (1986) 69 ALR 715; *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31.

392 *NEA Pty Ltd v Magneta Mining Pty Ltd* [2007] WASCA 70.

or implied is given by the owner as to the condition of the plant or as to the suitability or fitness of the plant for any purpose". Aside from the inclusion of clause 8 in the contract, nothing else had been said to the applicant to dispel the representation that the equipment was fit for the relevant purpose. Martin CJ noted that it is important to differentiate between a factual situation where one party makes it clear to the other party (by way of disclaimer) that information provided may not be reliable and the situation in which there is nothing more than a contractual provision which attempts to limit liability. Exclusion clauses have no independent force of their own.[393] Clause 8 was held to do no more than preclude any term being incorporated into the contract relating to the condition of the equipment. It did not negate the misleading or deceptive nature of the representation made by the respondent.

Acknowledgment clauses

[33.220] It is common for parties to include an "acknowledgement" or "no reliance" clause in their contract. As noted earlier, such clauses typically involve one or both parties declaring that, in entering into the contract, no reliance was placed on any representations made by the other contracting party. The effect of such clauses was recently discussed by the High Court in *Campbell v Backoffice Investments Pty Ltd*.[394] French CJ summarised the relevant principles as to the significance of such clauses as follows:

> Where the impugned conduct comprises allegedly misleading pre-contractual representations, a contractual disclaimer of reliance will ordinarily be considered in relation to the question of causation. For if a person expressly declares in a contractual document that he or she did not rely upon pre-contractual representations, that declaration may, according to the circumstances, be evidence of non-reliance and of the want of a causal link between the impugned conduct and the loss or damage flowing from entry into the contract. In many cases, such a provision will not be taken to evidence a break in the causal link between misleading or deceptive conduct and loss. The person making the declaration may nevertheless be found to have been actuated by the misrepresentations into entering the contract. The question is not one of law, but of fact.[395]

A practice has arisen in the shopping centre context of requiring lessees to sign a separate deed of acknowledgment stating that no representation of the lessor has been relied upon by the lessee in entering into the lease. This was an attempt to overcome the problem created by the fact that the contract including the acknowledgment term may be rescinded because of the misleading conduct. In *Waltip Pty Ltd v Capalaba Park Shopping Centre Pty Ltd*[396] a deed of acknowledgment in this form was held to be ineffective. Pincus J held that the execution of the deed of acknowledgment did not alter the fact that the tenant had been misled by a misleading floor plan it had been shown by the landlord.[397] While such deeds may have some effect in an evidentiary sense, they will not easily survive the scrutiny of the courts.

393 See also *Benlist Pty Ltd v Olivetti Australia Pty Ltd* [1990] ATPR 41-043, 51,590.

394 *Campbell v Backoffice Investments Pty Ltd* [2009] HCA 25; (2009) 238 CLR 304.

395 *Campbell v Backoffice Investments Pty Ltd* [2009] HCA 25; (2009) 238 CLR 304, [31] (footnotes omitted). See also *Venerdi Pty Ltd v Anthony Moreton Group Funds Management Ltd* [2015] QSC 219; [2015] 1 Qd R 214; *Chowder Bay Pty Ltd v Paganin* [2018] FCAFC 25, [62].

396 *Waltip Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* [1989] ATPR 40-975.

397 Pincus J treated the deed of acknowledgment as equivalent to an exclusion clause and supported his conclusion by reference to the following cases: *Clark Equipment Australia Ltd v Covcat Pty Ltd* (1987) 71

In *IOOF Australia Trustees (NSW) Ltd v Tantipech*[398] the applicant entered into a lease of a shop in a shopping centre and signed a separate deed of acknowledgment. The misleading conduct comprised statements by the respondent landlord's agent that the centre was 80 per cent leased and that the shops surrounding the applicant's shop had already been leased or were about to be leased. Both the lease and the deed contained statements purporting to exclude any representations or warranties. By clause 1 of the deed the applicant confirmed that, except for those specified in clause 2, the respondent had made no statements which had induced him to enter the contract. Clause 2 identified two representations, neither of which related to the number or proportion of leases or proposed leases which had or were likely to be entered into. The applicant agreed to indemnify the respondent against any claim he might make in respect of statements other than those set out in clause 2. He also agreed that if any such claim were made, production of the deed by the respondent would be a complete bar to the claim. The respondent argued that the deed was in a different position from that of the lease because there was no evidence that the applicant had been induced to enter the deed, as distinct from the lease, by any representation about the leasing of surrounding shops.

All this ingenuity of the respondent's lawyers came to nil. The Full Federal Court said that:

> the public policy which lies behind the court's refusal to allow a party to contract out of liability under s 52 of the Act [now *ACL*, s 18] is not exhausted by application to the case of an exculpatory provision which is contained in a document into which the complainant has been induced to enter by a misrepresentation. It must extend to any document which purports to excuse a misrepresentor from liability for contravention of s 52 [now *ACL*, s 18].[399]

The Court acknowledged that the fact that an applicant stated that he was *not* induced to enter into an agreement in reliance on representations may bear on the question whether he should be believed when he asserts that the representations *were* an inducement. However, in this case, the applicant did not understand that the deed related to representations about the occupancy of surrounding shops and was *in fact* induced by the misleading conduct. Therefore, the deed could not have the effect of barring the claim.

By contrast, in *Jewelsnloo Pty Ltd v Sengos* the NSW Court of Appeal found that a "No Reliance" provision in the contract for purchase of business precluded a claim of misleading conduct, in circumstances where the bargain was made on the basis that the purchaser would pay a "severely discounted price to reflect the fact that it was not able to rely upon the accuracy of [sales figures provided by the seller and covered by the non-reliance clause]".[400]

ALR 367, 371; *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd* (1988) 39 FCR 546, 559–61; *Keen Mar Corporation Pty Ltd v Labrador Park Shopping Centre Pty Ltd* [1989] ATPR (Digest) 46,048, 53,146.

398 *IOOF Australia Trustees (NSW) Ltd v Tantipech* (1998) 156 ALR 470.

399 *IOOF Australia Trustees (NSW) Ltd v Tantipech* (1998) 156 ALR 470, 479.

400 *Jewelsnloo Pty Ltd v Sengos* [2016] NSWCA 309 (Beazley ACJ, Macfarlan JA and Payne JA).

VITIATING FACTORS: ABUSE OF POWER

PART XIB

[PtXIB.05] In Part XIA (Misinformation), we saw that a party to a contract (the *plaintiff*) who has entered into a contract on the basis of misinformation may, in certain circumstances, obtain relief from the courts. Such misinformation may derive from a spontaneous mistake (Chapter 31) or from misrepresentation by or misleading conduct on the part of the other party (the *defendant*) (Chapters 32 and 33). In such cases, the original consent of the plaintiff is impaired in the sense that it is based on an erroneous belief.

In this Part, we look at some further categories of cases in which a party's consent or judgment is impaired. In these instances, the impairment results from the abuse or exploitation of a position of influence or advantage by the defendant at the expense of the plaintiff.[1] The following chapters consider the doctrines of duress (Chapter 34), undue influence (Chapter 35) and unconscionable dealing (Chapter 36). A person who is induced to enter into a contract by abusive conduct which falls within one or more of these categories can, in appropriate circumstances, have the contract set aside (rescinded) by the courts. This relief is justified on the basis that it would be unconscionable for the defendant to retain any benefits obtained under the contract, given his or her improper behaviour and the resultant impairment of the plaintiff's consent. In some cases, the relief may be sought by the plaintiff, even though the improper conduct in question is that of a third party, that is, a person who is not a party to the contract (Chapter 37).

Relevant to this discussion is a distinction sometimes drawn in contract law between *procedural unfairness* and *substantive unfairness*.[2] The former is concerned with unfairness in the way in which the contract was brought about (eg, by misleading conduct), the latter with unfairness of the terms of the contract itself (eg, harsh and one-sided terms as discussed in Chapter 16). Judge-made law has generally been concerned with procedural unfairness. As Toohey J pointed out in *Louth v Diprose*, the courts "are not armed with a general power to set

1 See generally Bigwood, *Exploitative Contracts* (2003).

2 The distinction was first enunciated in Leff, "Unconscionability and the Code – The Emperor's New Clause" (1967) 115 *University of Pennsylvania Law Review* 485, 487.

aside bargains simply because, in the eyes of the judge, they appear to be unfair, harsh or unconscionable".[3] The abuse of power categories which we look at in this Part were created by judges and generally represent instances of "procedural" unfairness. Nevertheless, it is clear that substantive unfairness may be evidence of procedural unfairness. In the words of Lord Brightman: "Contractual imbalance may be so extreme as to raise a presumption of procedural unfairness, such as undue influence or some other form of victimization."[4]

There has been significant *legislative* development in the areas which form the subject matter of this part. In Chapter 38 (Statutory unconscionability), we will consider two legislative schemes: Pt 2-2 of the *Australian Consumer Law* (ACL) which deals with "unconscionable conduct" and the *Contracts Review Act 1980* (NSW) which deals with "unjust contracts". The impugned conduct may occur before contractual formation as a vitiating factor or during performance. Various forms of relief are available in addition to rescission, such as variation of the contract and compensation for loss. The remedies available under the ACL are considered in Chapter 33 in respect of the prohibition on misleading and deceptive conduct. The same provisions apply to breaches of the prohibition on unconscionable conduct under the ACL.

3 *Louth v Diprose* (1992) 175 CLR 621, 654.
4 *Hart v O'Connor* [1985] 1 AC 1000, 1018.

CHAPTER **34**

Duress

OVERVIEW

[34.05] The doctrine of duress provides relief from a contract where illegitimate pressure has been applied by one party (the *defendant*) to induce the other party (the *plaintiff*) in making his or her decision to enter into or modify the contract. The focus of inquiry in duress is into the kind of pressure exerted and its effect on the plaintiff.[1] Threats involving unlawful acts will usually amount to illegitimate pressure. Some courts have suggested that duress also covers threats of lawful action which nonetheless amount to illegitimate pressure for the purposes of duress. There is considerable debate about whether this category of duress should be recognised or whether its concerns are better addressed through the doctrine of unconscionable dealing. Lawful act duress is discussed at [34.47].

Duress also covers threats to pay money, which is part of the law of restitution. Many of the cases on this topic are also relevant to the contractual claims discussed in this chapter. Conduct by a defendant that pressures a plaintiff to enter into a contract may also give rise to claims in undue influence (Chapter 35) and in unconscionable dealing (Chapter 36), as well as under the *Australian Consumer Law* on grounds of unconscionable conduct under s 21 or undue harassment under s 50 (Chapter 38).

Duress in law and in equity

[34.10] Historically the common law recognised duress only in cases of duress to the person and then duress to goods. The equitable jurisdiction developed in recognition of other forms

1 *Westpac Banking Corporation v Cockerill* [1998] FCA 43; (1998) 152 ALR 267, 289 (Kiefel J, Lindgren J agreeing); *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [26] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

of illegitimate pressure.[2] The distinction between duress in law and in equity is no longer treated as significant by courts.[3] Edelman and Bant note that the "jurisdictional origin" of the doctrine commonly pays no part in the analysis of the court.[4] Consistently, relief for duress makes the contract voidable rather than void.[5]

The rationale for relief: impaired consent

[34.15] It is sometimes said that duress "negates", "vitiates" or "destroys" consent and renders the plaintiff's actions non-voluntary.[6] If this were literally true, the resultant contract would be *void*. The generally accepted view is that a contract procured by duress is not void (except perhaps in very extreme cases), but *voidable* at the discretion of the plaintiff. On this view, the justification for duress is that the will of the plaintiff is impaired, inhibited or deflected, rather than destroyed or negated.[7] The plaintiff does consent to the defendant's terms, but the consent is given because there is no other practical choice open. As recognised by McHugh JA in *Crescendo Management Pty Ltd v Westpac Banking Corporation*, "the overbearing of the will theory of duress should be rejected. A person who is the subject of duress usually knows only too well what he is doing. But he chooses to submit to the demand or pressure rather than take an alternative course of action."[8]

Basic elements

[34.20] There are two elements involved in assessing duress:

1. "whether any applied pressure induced the [plaintiff] to enter into the contract"; and
2. "whether that pressure went beyond what the law is prepared to countenance as legitimate".[9]

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2 *Barton v Armstrong* [1976] AC 104, 118 (Lord Cross).

3 See, eg, *Halpern v Halpern (Nos 1 & 2)* [2007] EWCA Civ 291; [2008] QB 195, [69] (Lord Carnwath).

4 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 200.

5 *Barton v Armstrong* [1973] 2 NSWLR 598, 617 (Mason JA); *Pao On v Lau Yiu Long* [1979] UKPC 2; [1980] AC 614, 629 (Lord Scarman); *Universe Tankships Inc of Monrovia v International Transport Workers Federation* [1983] 1 AC 366, 383 (Lord Diplock), 400 (Lord Scarman).

6 *Pao On v Lau Yiu Long* [1979] UKPC 2; [1980] AC 614, 635 (Lord Scarman); *Westpac Banking Corporation v Cockerill* [1998] FCA 43; (1998) 152 ALR 267, 289–90 (Kiefel J).

7 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [26] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

8 *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 NSWLR 40, 45–6 (McHugh JA (Samuels and Mahoney JJA agreeing)). See also *Universe Tankships Inc of Monrovia v International Transport Workers Federation* [1983] 1 AC 366, 400 (Lord Scarman); *Equiticorp Finance Ltd (in liq) v Bank of New Zealand* (1993) 32 NSWLR 50, 149–50 (Clarke and Cripps JJA).

9 *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 NSWLR 40, 46 (McHugh JA (Samuels and Mahoney JJA agreeing)). See also *Universe Tankships Inc of Monrovia v International Transport Workers Federation* [1983] AC 366, 400 (Lord Scarman); *Progress Bulk Carriers Ltd v Tube City IMS LLC (The Cenk Kaptanoglu)* [2012] EWHC 273 (Comm), [21]–[35] (Cooke J); *Electricity Generation Corporation (t/as Verve Energy) v Woodside Energy Ltd* [2013] WASCA 36, [24] (McLure P); *Doggett v Commonwealth Bank of Australia* [2015] VSCA 351; (2015) 47 VR 302, [73] (Whelan JA); *Ukraine v Law Debenture Corporation PLC* [2018] EWCA Civ 2026, [157] (Lady Gloster, Lord Sales and Lord Richards).

No reasonable alternative?

[34.25] In England, it has been suggested that duress also requires the absence of a reasonable alternative available to the defendant,[10] although this has not been universally accepted.[11] The absence of a reasonable alternative is not an established requirement of duress in Australia.[12] Thus, Heydon reaches the conclusion that this element is required.[13] Edelman and Bant reach the contrary view.[14]

Even if the absence of a reasonable alternative is not an element of duress, it may have considerable evidential value. The absence of a reasonable alternative may be evidence that the pressure applied by the defendant influenced the decision of the plaintiff, supporting the inquiry into causation.[15] Conversely, the presence of a reasonable alternative available to the plaintiff may support the conclusion that that the pressure was not an operative reason affecting his or her decision.[16]

The possibility of a plaintiff successfully litigating to protect his or her position does not establish a reasonable alternative to submitting to the pressure applied by a defendant.[17] In *Adam Opel GmbH v Mitras Automative (UK) Ltd*,[18] the likelihood that the plaintiff would have obtained an injunction compelling performance was not sufficient to preclude a claim of duress to recover payments made to the defendant in response to its threat of breach. David Donaldson QC J who rejected the argument that the existence of alternatives should preclude relief on grounds of duress. David Donaldson QC J stated that to accept such an approach would have the "Alice in Wonderland" outcome that "the more blatantly unjustified and illegal the action threatened, the more readily the defendant would escape liability in duress".[19]

It has additionally been suggested that a lack of a "good faith" or honest belief on the part of the defendant in the legitimacy of his or her conduct is an element of the action.[20] State of mind is better seen as a relevant but not essential consideration.[21] A threat to do something unlawful may amount to illegitimate pressure even where the person making the threat believes he or she is lawfully entitled to do it.[22]

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10 See, eg, *Huyton SA v Peter Cremer GmbH & Co* [1998] EWHC 1208 (Comm); [1999] 1 Lloyds Rep 620, 636 (Mance J); *DSND Subsea Ltd v Petroleum Geo-Services ASA* [2000] EWHC 185, [131] (Dyson J); *Carollion Construction Ltd v Felix (UK) Ltd* [2001] BLR 1, relying on the statement of Lord Scarman in *Pao On v Lau Yiu Long* [1979] UKPC 2; [1980] AC 614.

11 *Kolmar Group AG v Traxpo Enterprises PVT Ltd* [2010] EWHC 113, [92] (Clarke J); *Borrelli v Ting* [2010] UKPC 21.

12 See, eg, *Lactos Fresh Pty Ltd v Finishing Services Pty Ltd (No 2)* [2006] FCA 748, [97] (Weinberg J).

13 Heydon, *Heydon on Contract* (2019), [16.10]. Compare Seddon and Bigwood, *Cheshire and Fifoot's Law of Contract* (11th Aust ed, 2017), [13.1].

14 See Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 207.

15 *Kolmar Group AG v Traxpo Enterprises PVT Ltd* [2010] EWHC 113, [92] (Clarke J); Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 223.

16 *Huyton SA v Peter Cremer GmbH & Co* [1998] EWHC 1208 (Comm); [1999] 1 Lloyd's Rep 620, 638 (Mance J).

17 Heydon, *Heydon on Contract* (2019), [16.310].

18 *Adam Opel GmbH v Mitras Automative (UK) Ltd* [2007] EWHC 3205 (QB).

19 *Adam Opel GmbH v Mitras Automative (UK) Ltd* [2007] EWHC 3205 (QB), [32] (Donaldson QC).

20 *Mitchell v Pacific Dawn Pty Ltd* [2011] QCA 98, [51] (Fraser JA).

21 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), pp 215–16; Heydon, *Heydon on Contract* (2019), [16.120] and [16.280].

22 *Beerens v Bluescope Distribution Pty Ltd* [2012] VSCA 209; (2012) 39 VR 1, [46] (Nettle JA); *Electricity Generation Corporation (t/as Verve Energy) v Woodside Energy Ltd* [2013] WASCA 36, [30] (McLure P), [184] (Murphy J), appeal allowed on different issue in *Electricity Generation Corporation v Woodside Energy Ltd* [2014] HCA 7; (2014) 251 CLR 640.

WHETHER THE PRESSURE INDUCED THE PLAINTIFF TO ENTER INTO THE CONTRACT

[34.30] The first established element in assessing a claim for relief on grounds of duress is whether the pressure applied by the defendant induced the plaintiff to enter into or vary the contract. This is a question of causation.[23] In Australia, it is clear that illegitimate pressure must only have been *a* factor influencing the plaintiff's decision to enter into the contract. [24] The illegitimate pressure need not be the *sole* or even *substantial* reason for this conduct.

This approach was initially applicable in cases of duress exherted through threats to the person.[25] In Australia the approach also applies more widely. In *Crescendo Management Pty Ltd v Westpac Banking Corporation*, McHugh JA said:

> It is unnecessary … for the [plaintiff] to prove that the illegitimate pressure was the sole reason for him entering into the contract. It is sufficient that the illegitimate pressure was one of the reasons for the person entering into the agreement. Once the evidence establishes that the pressure exerted on the [plaintiff] was illegitimate, the onus lies on the person applying the pressure to show that it made no contribution to the [plaintiff] entering into the agreement …[26]

By contrast, in England a more stringent test of causation for duress has been applied outside threats to person or property, requiring the pressure to be a "significant" cause of the plaintiff's conduct.[27]

Courts have identified a number of factors that may be relevant in assessing whether the illegitimate pressure caused the plaintiff to enter into the contract. These factors include whether the plaintiff protested, whether there were reasonable alternatives and whether the plaintiff took expeditious steps to set aside the contract after entering into it.[28]

These matters must be assessed in the light of the pressure that occurred. The more serious the threat, the less the plaintiff will be expected to do by way of protest and the fewer the alternatives that will be available to him or her.[29] For example, failure to protest when threatened with a gun or knife would be of little or no significance. Threats to life, physical integrity or liberty, as such, leave no practical alternative to the plaintiff. Where the threat is to economic interests, more must be done to show that the pressure was a cause of the plaintiff's decision, such as that there were no practical or realistic alternatives but to submit, as discussed at [34.35].[30]

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23 Cf Bigwood, who argues that there is also a normative question of whether the plaintiff had a reasonable alternative to entering into the contract: Bigwood, *Exploitative Contracts* (2003), pp 351–2.

24 *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 NSWLR 40, 46; *Electricity Generation Corporation (t/as Verve Energy) v Woodside Energy Ltd* [2013] WASCA 36, [24].

25 *Barton v Armstong* [1976] AC 104.

26 *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 NSWLR 40, 46 (McHugh JA (Samuels and Mahoney JJA agreeing)).

27 *Dimskal Shipping Co SA v International Transport Workers Federation (The Evia Luck) (No 2)* [1992] 2 AC 152, 165. See further Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), pp 221-222.

28 *Pao On v Lau Yiu Long* [1979] UKPC 2; [1980] AC 614, 635 (Lord Scarman); *DSND Subsea Ltd v Petroleum Geo-Services ASA* [2000] EWHC 185, [131] (Dyson J).

29 See *Adam Opel GmbH v Mitras Automotive (UK) Ltd* [2007] EWHC 3205 (QB), [34] (Donaldson QC).

30 *Universe Tankships Inc of Monrovia v International Transport Workers Federation* [1983] 1 AC 366, 383–4 (Lord Diplock), 400 (Lord Scarman); *Huyton SA v Peter Cremer GmbH & Co* [1998] EWHC 1208 (Comm); [1999] 1 Lloyd's Rep 620, 636 (Mance J).

Once it is established that there is illegitimate pressure on the plaintiff, this pressure is treated as having induced the plaintiff to enter into the contract. The onus then lies on the defendant to prove that the threat made no contribution to the plaintiff's decision to enter into the agreement.[31]

WHETHER THE PRESSURE WAS ILLEGITIMATE

[34.32] The second element in assessing duress is whether the pressure that was applied to a plaintiff to enter into a contract, or to modify an existing contract, was illegitimate. The assessment involves considering "what might count as morally or socially unacceptable in the context in which [the parties] interact with each other".[32]

As discussed at [10.100] in relation to pressure justifying a restitutionary claim, there are three categories of pressure that may be considered illegitimate for the purposes of relief.[33] These categories are:

1. a threat to harm a person;
2. a threat to harm property; and
3. a threat to infringe a person's legal rights, sometimes called *economic duress*.

Threats in categories 1 and 2 are highly intrusive and will usually amount to illegitimate pressure for the purposes of duress. The boundaries of category 3 are more difficult to define.[34] The prime example of a threat to infringe a person's legal rights involves a threat to breach a contract unless the plaintiff accedes to a demand made by the defendant. As discussed further at [34.45], this kind of threat may amount to duress or be merely a negotiating strategy resulting in a valid contractual modification.

Threats to a person

[34.35] A threat to harm the plaintiff or the family of the plaintiff unless the plaintiff enters into a contract will constitute illegitimate pressure giving rise to duress.[35] In *Barton v Armstrong*,[36] the defendant sought to coerce the plaintiff into executing a deed relating to the sale of certain companies by threatening to have him murdered. Although the plaintiff took the threats seriously, there were also good business reasons for executing the deed. It was held that the plaintiff should succeed in obtaining relief, even though he could not prove that, but for the threats, he would not have signed the deed. Relief was available if the threats contributed to the decision to sign or, in other words, were *one* of the reasons for signing, even though the plaintiff might well have signed even if no threat had been made.

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31 See *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 NSWLR 40, 46 (McHugh JA (Samuels and Mahoney JJA agreeing)). Cf Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 220.

32 *Ukraine v Law Debenture Corporation PLC* [2018] EWCA Civ 2026, [160] (Lady Gloster, Lord Sales and Lord Richards).

33 See also *Smith v William Charlick Ltd* [1924] HCA 13; (1924) 34 CLR 38, 56 (Issacs J).

34 *Times Travel (UK) Ltd v Pakistan International Airlines Corporation* [2019] EWCA Civ 828, [1] (Lord Richards).

35 See, eg, *Barton v Armstrong* [1976] AC 104; *Al Nehayan v Kent* [2018] EWHC 333 (Comm).

36 *Barton v Armstong* [1976] AC 104. Although this case was apparently pleaded as *common law* duress, the action began in the *equity* division of the New South Wales Supreme Court and, on appeal, the Privy Council applied equitable principles.

Threats to property

[34.40] In the 19th century, there was some authority for the view that if a person promised to pay money in order to obtain the release of goods unlawfully taken or retained, then, provided consideration was given, such a promise was enforceable and the contract could not be set aside on the basis of duress. *Skeate v Beale*[37] concerned a promise to pay money for the return of goods detained and threatened to be sold for alleged arrears of rent. The promisor failed to pay the money, arguing that the promise to pay was induced by duress. This defence failed. Lord Denman CJ stated that "an agreement is not void because made under duress of goods … the fear that goods may be taken or injured does not deprive anyone of his free agency".[38]

This opinion, however, stood uneasily with the recognised right to recover money paid to prevent the unlawful seizure of goods or to obtain goods actually seized. In such an instance, a claim could be made in restitution for money had and received.[39] This apparent distinction between contract and restitution, if accepted, "leads to the absurd result that if A paid money under duress of goods he could recover the money paid but if he entered into a contract to pay money under similar duress he could not avoid the contract and would be obliged to pay the moneys due thereunder".[40]

Today it is accepted that threatened unlawful detention or seizure of goods, or threatened damage to goods, is within the scope of duress in contract law. As Kerr J said in *Occidental Worldwide Investment Corporation v Skibs A/S Avanti (The "Siboen" and The "Sibotre")*, "if I should be compelled to sign a lease or some other contract … under imminent threat of having my house burnt down or a valuable picture slashed, though without any threat of physical violence to anyone, I do not think the law should uphold the agreement."[41] The contrary result in *Skeate v Beale* might perhaps be explained on the basis that the plaintiff in that case, when subjected to the threat to sell the goods, had a real alternative to submission – an action in court – which he chose not to pursue. It might also be inferred that the parties' agreement constituted a settlement of their dispute. Where a person is withholding a chattel under a bona fide claim of right, a contract to pay for its return may constitute a valid compromise of the claim.

The modern approach to duress to goods is illustrated by *Hawker Pacific Pty Ltd v Helicopter Charter Pty Ltd*.[42] In that case, the plaintiff had a helicopter which needed repainting. The defendant agreed to do the job for $5,200. The work was not done to the plaintiff's satisfaction. Further work on the helicopter was done on the basis that the price became $5,550. Again, the plaintiff was dissatisfied, and the helicopter was returned to the defendant for rectification work. When the plaintiff's representative finally went to collect the helicopter, he was asked to sign a document in which the plaintiff agreed to pay $4,300 on delivery and to release the defendant from any further liability. The plaintiff's representative took the helicopter away, but the $4,300 was not paid. The plaintiff commenced proceedings in which it submitted that

37 *Skeate v Beale* (1841) 11 Ad & E 983; 113 ER 688.

38 *Skeate v Beale* (1841) 11 Ad & E 983; 113 ER 688, 690 (Lord Denman CJ).

39 *Astley v Reynolds* (1731) 2 Str 915; 93 ER 939.

40 *Hawker Pacific Pty Ltd v Helicopter Charter Pty Ltd* (1991) 22 NSWLR 298, 306 (Clarke JA).

41 *Occidental Worldwide Investment Corporation v Skibs A/S Avanti (The "Siboen" and The "Sibotre")* [1976] 1 Lloyd's Rep 293, 335 (Kerr J).

42 *Hawker Pacific Pty Ltd v Helicopter Charter Pty Ltd* (1991) 22 NSWLR 298.

the agreement in the document was voidable on grounds of duress. The Court upheld this submission. The plaintiff believed the defendant would prevent the helicopter being taken away unless the document was signed, and needed the helicopter urgently for a charter that day. The defendant knew of this urgency. The concept of duress, it was held, applied not only where money was paid but also where promises were made to retrieve detained goods.

Threats to breach a contract

[34.45] Illegitimate pressure giving rise to duress may involve a threat to a person's rights. In contract law, the main example of this kind of pressure is sometimes termed *economic* duress.[43] The category most commonly applies where the defendant threatens to breach a contract unless the plaintiff enters into a modified or new contract on terms more favourable to the defendant.

As was seen in Chapter 4, contractual modifications, to be binding, must be supported by consideration.[44] If this is the case, then the further question is whether the modification was the result of a genuine response to changed circumstances or procured under duress.

Assessing when a contract variation is the result of duress is not straightforward. On the one hand, it might be argued that if a defendant has faced unforeseen hardship that makes performance of the contract more difficult or expensive than anticipated, the defendant should be compensated at least partially for that hardship. On the other hand, it might be argued that the defendant assumed the risk of such difficulties when making the contract. In such circumstances, the defendant should not be permitted to take advantage of its stronger bargaining position once work under the contract has commenced by demanding changes to the contract. Courts faced with these alternatives consider the circumstances of the case to determine whether the modification was a genuine re-negotiated arrangement or the result of illegitimate pressure.[45] Edelman and Bant argue that a key question in in making this determination is whether or not the conduct of the defendant amounted to a threat, as opposed to an offer or request, in initiating re-negotiation of a contract.[46]

In *North Ocean Shipping Co Ltd v Hyundai Construction Co Ltd*,[47] a shipbuilding company contracted to build a tanker for prospective owners at a fixed price in US dollars, with payment to be made in five instalments. After the owners had paid the first instalment, the US dollar was devalued by 10 per cent. The shipbuilder, without legal justification, claimed an increase of 10 per cent in the remaining instalments. It declined the owner's suggestion that the claim be referred to arbitration and said that if the owners did not agree to pay the extra money, it would terminate the contract and return the first instalment. The owners, who had already entered into a lucrative agreement to charter the tanker upon completion, said they were convinced they were not obliged to pay, but would do so "in order to maintain an amicable relationship and without prejudice to our rights".[48] At the owner's request, the company increased an existing letter of credit (a security for repayment of instalments in the

43 See also [10.100].

44 See [4.65]ff.

45 See also *North Ocean Shipping Co Ltd v Hyundai Construction Co Ltd* [1979] QB 705; *Borrelli v Ting* [2010] UKPC 21; *Progress Bulk Carriers Ltd v Tube City IMS LLC (The Cenk Kaptanoglu)* [2012] EWHC 273 (Comm).

46 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), pp 202–3.

47 *North Ocean Shipping Co Ltd v Hyundai Construction Co Ltd* [1979] QB 705.

48 *North Ocean Shipping Co Ltd v Hyundai Construction Co Ltd* [1979] QB 705, [21] (Mocatta J).

event of default in building the tanker). After paying the final instalment "in full and final settlement", the owner took delivery in November 1974. They claimed return of the 10 per cent excess in July 1975.

The Court held that by increasing the letter of credit, the shipbuilding company had provided consideration for the promise to pay the extra 10 per cent, but that the agreement to pay was made under duress in the form of economic pressure – a threat by the shipbuilder to break the original contract. The shipbuilding company had been adamant in insisting on the increase. The Court considered it would have been unreasonable to expect the owners to claim damages in arbitration, with all the inherent uncertainties of litigation, given that they were already contracted to charter the tanker upon completion. The shipbuilding contract would therefore have been voidable, given the illegitimate pressure the shipbuilding company had applied. However, the Court went on to hold that the owners had *affirmed* the varied contract by their overt acts: their failure to protest when final payment was made and their delay of eight months after delivery of the tanker in putting forward a claim. The owners had no reason to believe that if they had made a protest in the protocol of delivery and acceptance, the shipbuilders would have refused to deliver the vessel.

LAWFUL ACT DURESS

[34.47] The categories of cases discussed above have involved unlawful acts of varying severity. An unresolved issue in Australian and English contract law is whether lawful threats may give rise to duress. The possibility of lawful act duress was recognised in *R v Attorney General for England and Wales* in which Lord Hoffmann, delivering the majority judgment for the Privy Council, said that "the fact that the threat is lawful does not necessarily make the pressure legitimate".[49] The reason for recognising the potential for lawful threats, nonetheless, to amount to duress is that otherwise "those who devise outrageous but technically lawful means of compulsion must always escape restitution until the legislature declares the abuse unlawful".[50] In assessing when a threat of otherwise lawful action will be illegitimate for the purposes of duress, an important consideration will be the existence of a threat, as opposed to a mere request. A second consideration is the relationship between the threat and the demand. If "the pressure is lawful, it may be illegitimate if there is no reasonable or justifiable connection between the pressure being applied and the demand which that pressure supports".[51] Edelman and Bant explain that this is essentially an inquiry into proportionality.[52] A threat involving lawful conduct is more likely to amount to duress where there is no reasonable relationship between the lawful threat and "the defendant's legitimate interest in the demand it supports".[53]

49 *R v Her Majesty's Attorney-General for England and Wales* [2003] UKPC 22; [2004] 2 NZLR 577, [16] Lord Hoffman).

50 Birks, *An Introduction to the Law of Restitution* (1989), p 177, quoted in *CTN Cash and Carry Ltd v Gallaher* [1994] 4 All ER 714, 718 (Lord Steyn).

51 *Electricity Generation Corporation (t/as Verve Energy) v Woodside Energy Ltd* [2013] WASCA 36, [25] (McLure P) but cf [176] (Murphy JA), appeal allowed on different issue in *Electricity Generation Corporation v Woodside Energy Ltd* [2014] HCA 7; (2014) 251 CLR 640. See also *Universe Tankships Inc of Monrovia v International Transport Workers Federation* [1983] 1 AC 366, 401 (Lord Scarman); *R v Her Majesty's Attorney-General for England and Wales* [2003] UKPC 22; [2004] 2 NZLR 577, [15]–[20] (Lord Hoffman).

52 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 212.

53 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 212, adopted in *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [71] (Nettle J).

Blackmail and threats to prosecute

[34.48] One example of a threat involving a lawful act that may nonetheless amount to duress is a threat by a blackmailer to report a crime to the police.[54] The threat is lawful in itself, but the demand for money may render the threat illegitimate. Even if there is no question of blackmail, a threat to prosecute may be coercive and illegitimate. In *Mutual Finance Ltd v John Wetton & Sons Ltd*,[55] a family company promised to guarantee the payment of money owed by a family member to a creditor. The guarantee was knowingly induced by a threat of the creditor to prosecute the family member for the alleged crime of forging a previous guarantee. Relief was given in this case. Such a prosecution would have put the family member's liberty, and his father's health, at risk. Hence, it could be said that the threat of such prosecution was illegitimate pressure.

In a different situation, a threat to prosecute might not be enough in itself to justify relief. For example, a promisor may promise to pay a sum of money, which is already allegedly *owed by that person* to the promisee. The promisor may have been guilty of a misappropriation of the promisee's funds to the extent of the amount promised. In such a case, some other element of impropriety beyond the promisee's threat to prosecute is apparently needed to justify relief to the promisor. Such impropriety may be found in an actual agreement (express or implied) not to proceed with the prosecution in return for a promise to repay the money.[56]

Refusal to contract

[34.50] Lawful act duress has been raised in relation to a *refusal to contract*. In *CTN Cash and Carry Ltd v Gallaher*[57] the defendant supplied cigarettes to the plaintiff company on a regular basis and arranged credit facilities. Each supply was under a separate contract and the defendant was not obliged either to make further supplies or to provide credit facilities. It invoiced the plaintiff for a consignment that had been stolen before it reached the correct delivery address. The defendant did so wrongly believing that it was entitled to payment. When the plaintiff refused to pay the invoice, the defendant terminated its credit facilities and refused to reinstate them unless the invoice was paid. Against this pressure, the plaintiff paid the invoice but subsequently brought proceedings to recover the payment on the grounds that it had been the result of economic duress.

The claim was rejected by the English Court of Appeal. Lord Steyn identified three relevant factors regarding the dispute. First, it did not involve a protected relationship or arise in a course of dealings between a consumer and a supplier. Secondly, the defendant was entitled to refuse to enter into further supply contracts with the plaintiff. Thirdly, "the defendants bona fide thought that the goods were at the risk of the plaintiffs and that the plaintiffs owed the defendants the sum in question".[58] Lord Steyn concluded that "courts have wisely not

54 *Universe Tankships Inc of Monrovia v International Transport Workers Federation* [1983] 1 AC 366, 401 (Lord Scarman). See also *Thorne v Motor Trade Association* [1937] AC 797, 806 (Lord Atkin).

55 *Mutual Finance Ltd v John Wetton & Sons Ltd* [1937] 2 KB 389.

56 *Scolio Pty Ltd v Cote* (1992) 6 WAR 475. Such an agreement to stifle a prosecution is also unenforceable as an illegal contract: see [42.35]. See also *Tsarouchi v Tsaroushi* [2009] FMCAfam 126.

57 *CTN Cash and Carry Ltd v Gallaher* [1994] 4 All ER 714.

58 *CTN Cash and Carry Ltd v Gallaher* [1994] 4 All ER 714, 718 (Lord Steyn), see also 719 (Lord Nicholls).

accepted any general principle that a threat not to contract with another, except on certain terms, may amount to duress".[59]

State of mind and unreasonableness

[34.53] It has been argued at [34.25] that the honest or good faith belief of the defendant is a relevant but not essential consideration in assessing whether pressure is illegitimate for the purposes of duress involving an unlawful act. The good faith belief of the defendant may play a more significant role in assessing lawful act duress. It has been suggested that a lawful claim made with a good faith belief in the legitimacy of the claim is less likely to involve duress, whereas pressure to concede to a claim to which the defendant does not consider itself entitled may be a factor supporting a conclusion of duress.[60] Thus, in *Beerens v Bluescope Distribution Pty Ltd*, Nettle JA (Redlich JA agreeing) in the Victorian Court of Appeal suggested that it would not normally be illegitimate pressure for a creditor to threaten to bring bankruptcy proceedings to persuade a debtor to pay.[61] However, where a creditor threatens proceedings which the creditor "knows to be groundless or for an improper purpose", that threat may be sufficient to vitiate a transaction.[62]

It has sometimes been suggested that a claim that is objectively unreasonable may also be open to challenge as involving duress. This proposition was rejected by the English Court of Appeal in *Times Travel (UK) Ltd v Pakistan International Airlines Corporation*.[63] Lord David Richards, with whom Lord Moylan and Lord Asplin agreed, surveyed the relevant authorities and concluded that:

> the doctrine of lawful act duress does not extend to the use of lawful pressure to achieve a result to which the person exercising pressure believes in good faith it is entitled, and that is so whether or not, objectively speaking, it has reasonable grounds for that belief. The common law and equity set tight limits to setting aside otherwise valid contracts. In this way undesirable uncertainty in a commercial context is reduced.[64]

Times Travel was a travel agency in Birmingham. It was appointed as an agent for PIAC, an important trading partner, for any travel agent selling airline tickets to the Pakistani community in the United Kingdom. In 2008, the parties were in dispute over the commissions. In 2010, Times Travel became aware that other travel agents were asserting claims against PIAC about commissions and threatening legal proceedings. PIAC advised Times Travel not to get involved with this course of action. In 2012, PIAC sent a notice of termination to Times Travel, and all other agents in the United Kingdom, terminating its appointment with effect from 31 October 2012. The notice offered terms of re-appointment, which reduced Times Travel's fortnightly allocation of tickets from 300 to 60. This reduction in ticket allocation would have a major impact on Times Travel's business.

59 *CTN Cash and Carry Ltd v Gallaher* [1994] 4 All ER 714, 717–8 (Lord Steyn), 719 (Lord Nicholls).

60 *CTN Cash and Carry Ltd v Gallaher* [1994] 4 All ER 714, 718 (Lord Steyn); *Times Travel (UK) Ltd v Pakistan International Airlines Corporation* [2019] EWCA Civ 828, [62] (Lord Richards).

61 *Beerens v Bluescope Distribution Pty Ltd* [2012] VSCA 209; (2012) 39 VR 1, [43] (Nettle JA), [151] (Tate JA).

62 *Beerens v Bluescope Distribution Pty Ltd* [2012] VSCA 209; (2012) 39 VR 1, [46] (Nettle JA); Cf *Australian Building and Construction Commissioner v Construction, Forestry, Mining and Energy Union* [2017] FCA 157; (2017) 267 IR 130, [47] (Reeves J): no mental element required in establishing illegitimate pressure.

63 *Times Travel (UK) Ltd v Pakistan International Airlines Corporation* [2019] EWCA Civ 828.

64 *Times Travel (UK) Ltd v Pakistan International Airlines Corporation* [2019] EWCA Civ 828, [105] (Lord Richards).

In September 2012, Times Travel signed a new agreement with PIAC. This new agreement was expressed to replace with immediate effect the previous arrangements and to be "the sole, exclusive and entire agreement" between the parties. Times Travel's ticket allocation was then restored to its usual level. Under the new agreement, Times Travel released PIAC from all claims to commission or remuneration on any basis other than as set out in that agreement.

Times Travel argued the agreement was a result of economic duress on the part of PIAC. This argument was accepted by the trial judge. The judge found that the initial ticket reallocation would effectively mean that Times Travel's agency would come to an end and so would be unable to sell PIAC tickets. This decision was reversed by the Court of Appeal. The conduct of PIAC was not unlawful. Lord David Richards, with whom Lord Moylan and Lord Asplin agreed, held there was "little or no support in other authorities for the extension of lawful act duress in a commercial context to cover a demand which is made in good faith but unreasonably".[65] While PIAC was able to apply pressure as a result of its position at that time as a monopoly supplier of tickets for direct flights between the United Kingdom and Pakistan, "the common law has always rejected the use, or abuse, of a monopoly position as a ground for setting aside a contract, leaving it to be regulated by statute".[66]

Lawful act duress, undue influence and unconscionable dealing

[34.54] While English courts have, typically as obiter, recognised duress arising from illegitimate pressure applied through a lawful act,[67] the status of this category of duress in Australia is more uncertain. Some Australian courts have acknowledged the possibility of lawful act duress.[68] Other Australian courts have rejected it,[69] preferring instead to characterise such cases as raising issues of unconscionability.[70]

In *Crescendo Management Pty Ltd v Westpac Banking Corporation*,[71] unconscionable dealing was utilised as a way of analysing the kinds of lawful acts that may amount to illegitimate pressure for the purposes of duress. McHugh JA said:

> The proper approach in my opinion is to ask whether any applied pressure induced the victim to enter into the contract and then ask whether that pressure went beyond what the law is prepared to countenance as legitimate? Pressure will be illegitimate if it consists of unlawful threats or amounts to unconscionable conduct. But the categories are not closed. Even overwhelming pressure, not amounting to unconscionable or unlawful conduct, however, will not necessarily constitute economic duress.[72]

65 *Times Travel (UK) Ltd v Pakistan International Airlines Corporation* [2019] EWCA Civ 828, [72] (Lord Richards), dismissing obiter comments of Lord Leggatt in *Al Nehayan v Kent* [2018] EWHC 333 (Comm).

66 *Times Travel (UK) Ltd v Pakistan International Airlines Corporation* [2019] EWCA Civ 828, [107] (Lord Richards).

67 See in particular *Times Travel (UK) Ltd v Pakistan International Airlines Corporation* [2019] EWCA Civ 828.

68 *Electricity Generation Corporation (t/as Verve Energy) v Woodside Energy Ltd* [2013] WASCA 36, [25] (McLure P) but cf [176] (Murphy JA), appeal allowed on different issue in *Electricity Generation Corporation v Woodside Energy Ltd* [2014] HCA 7; (2014) 251 CLR 640.

69 *Australia & New Zealand Banking Group Ltd v Karam* [2005] NSWCA 344; (2005) 64 NSWLR 149, [66]–[67] (Beazley, Ipp and Basten JJA); *Canon Australia Pty Ltd v Patton* [2007] NSWCA 246, [3] (Basten JA).

70 See also Heydon, *Heydon on Contract* (2019), [16.40].

71 *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 NSWLR 40.

72 *Crescendo Management Pty Ltd v Westpac Banking Corporation* (1988) 19 NSWLR 40, 45–6 (McHugh JA).

This statement has received wide support from courts in Australia.[73]

Conversely, it has been suggested that lawful act duress might better be seen as part of the doctrines of undue influence and unconscionable dealing – a view expressed by Kirby P in *Equiticorp Finance Ltd (in liq) v Bank of New Zealand*.[74] In *Australia & New Zealand Banking Group v Karam*, Beazley, Ipp and Basten JJA said:

> The vagueness inherent in the terms "economic duress" and "illegitimate pressure" can be avoided by treating the concept of "duress" as limited to threatened or actual unlawful conduct. The threat or conduct in question need not be directed to the person or property of the victim, narrowly identified, but can be to the legitimate commercial and financial interests of the party. Secondly, if the conduct or threat is not unlawful, the resulting agreement may nevertheless be set aside where the weaker party establishes undue influence (actual or presumptive) or unconscionable conduct based on an unconscientious taking advantage of his or her special disability or special disadvantage, in the sense identified in *Commercial Bank of Australia Ltd v Amadio*. Thirdly, where the power to grant relief is engaged because of a contravention of a statutory provision such as s 51AA, s 51AB or s 51AC of the *Trade Practices Act* (Cth), [now ACL, ss 20–22] the Court may be entitled to take into account a broader range of circumstances than those considered relevant under the general law.[75]

In *Thorne v Kennedy*,[76] the High Court declined to address the questions about whether duress required an unlawful act or whether lawful act duress added anything to the existing doctrine of unconscionable conduct.[77]

RELIEF

[34.55] The consequence of duress is that the contract is *voidable*.[78] This means that the plaintiff of duress can elect to have the contract set aside or *rescinded*. If the defendant makes a claim for specific performance, this will be denied. Rescission may not be available if substantial restoration of the parties to their original positions is impossible (although courts may be flexible in this regard) or if the plaintiff has chosen to ratify or affirm the contract after the illegitimate pressure has been lifted.[79]

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73 *McKay v National Australia Bank Ltd* [1998] 4 VR 677, 690 (Tadgell JA); *Sholl Nicholson Pty v Chapman* [2001] VSC 430, [31] (Balmford) J); *Denmeade v Stingray Boats* [2003] FCAFC 215, [14] (Whitlam, Kiefel and Dowsett JJ); *Maher v Millennium Markets Pty Ltd* [2004] VSC 174, [125] (Osbourne J); *Australia & New Zealand Banking Group Ltd v Karam* [2005] NSWCA 344; (2005) 64 NSWLR 149.

74 *Equiticorp Finance Ltd (in liq) v Bank of New Zealand* (1993) 32 NSWLR 50, 106 (Kirby P).

75 *Australia & New Zealand Banking Group Ltd v Karam* [2005] NSWCA 344; [2005] 64 NSWLR 149, [66]–[67] (Beazley, Ipp and Basten JJA), cited with approval in *May v Brahmbhatt* [2013] NSWCA 309, [38]–[40] (Beazley P, Basten JA and Bergin CJ).

76 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85.

77 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [29] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ), see also [71]–[74] (Nettle J expressing a preference for including illegitimate pressure through a lawful act within the concept of duress).

78 *Barton v Armstrong* [1973] 2 NSWLR 598, 617 (Mason JA); *Pao On v Lau Yiu Long* [1979] UKPC 2; [1980] AC 614, 629 (Lord Scarman); *Universe Tankships Inc of Monrovia v International Transport Workers Federation* [1983] 1 AC 366, 383 (Lord Diplock), 400 (Lord Scarman); *Borrelli v Ting* [2010] UKPC 21, [38] (Lord Saville); *Electricity Generation Corporation (t/as Verve Energy) v Woodside Energy Ltd* [2013] WASCA 36, [31] (McLure J).

79 For a detailed discussion of rescission, see Chapter 39.

CHAPTER **35**

Undue influence

OVERVIEW

[35.05] Undue influence arises from circumstances where one party (the *defendant*) or, as discussed in Chapter 37, a third party, exercises such ascendency or influence over another (the *plaintiff*) that he or she ceases to exercise a free will in entering into a transaction.[1] In these circumstances, the doctrine is concerned with "the quality of the consent or assent of the weaker party".[2] A plaintiff who has been induced to enter into a transaction by the undue influence of the defendant is entitled to set that transaction aside as against the defendant and also any other person who has notice of the undue influence.[3] The doctrine applies to both contracts and gifts.

Undue influence may be established or arise by presumption

[35.15] There are two different ways to prove the existence of undue influence.[4] First, undue influence may be established through the circumstances of the particular transaction.[5] Secondly, undue influence may be proved by presumption on the basis of the relationship between the parties to the transaction. The law recognises a number of categories of relationship that give rise to a presumption that a resulting transaction was not the free will of the party concerned.[6]

1 See further Duggan, "Undue Influence", in Parkinson (ed), *The Principles of Equity* (2nd ed, 2003); Bigwood, "Undue Influence in the House of Lords: Principles and Proof" (2002) 65 *Modern Law Review* 435; Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016) ch 10.

2 *Commercial Bank of Australia Ltd v Amadio* (1983) 151 CLR 447, 474; *Bridgewater v Leahy* (1998) 194 CLR 457, [74].

3 See Chapter 37.

4 See *Barclays Bank plc v O'Brien* [1994] 1 AC 180.

5 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [45] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

6 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [46] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

The presumption may also be raised by proof that "the history of the particular relationship involved one party occupying a similar position of ascendency or influence and the other a corresponding position of dependency or trust".[7]

Rationale

[35.17] Different views have been expressed as to the underlying rationale of the doctrine of undue influence.[8] One approach sees the undue influence as based on the fiduciary-like responsibilities of a party in a position of influence.[9] Under this approach, the relationship of influence giving rise to the presumption of undue influence arises out of one party's trust in and dependence on the other. This relationship gives rise to a duty on the defendant to act in the interests of the plaintiff. As explained by Dixon J in *Johnson v Buttress*, the principle of presumed undue influence applies whenever "one party occupies or assumes towards another a position naturally involving an ascendancy or influence over that other, or a dependence or trust on his part".[10] Certain responsibilities then follow:

> One occupying such a position falls under a duty in which fiduciary characteristics may be seen. It is his duty to use his position of influence in the interest of no one but the man who is governed by his judgment, gives him his dependence and entrusts him with his welfare. When he takes from that man a substantial gift of property, it is incumbent upon him to show that it cannot be ascribed to the inequality between them which must arise from his special position.[11]

Another variant of a defendant focused view, prevalent in England, is that undue influence is concerned with impropriety on the part of the stronger party,[12] a position that may in part reflect the absence of a robust doctrine of unconscionable dealing in that jurisdiction.[13]

The other perspective for considering undue influence focuses on the impaired consent of the plaintiff. As described by Deane J in *Commercial Bank of Australia Ltd v Amadio*:

> The equitable principles relating to relief against unconscionable dealing and the principles relating to undue influence are closely related. [They] are, however, distinct. Undue influence, like common law duress, looks to the quality of the consent or assent of the weaker party … Unconscionable dealing looks to the conduct of the stronger party in attempting to enforce, or retain the benefit of, a dealing with a person under a special disability in circumstances where it is not consistent with equity or good conscience that he should do so.[14]

This rationale for undue influence was affirmed in *Thorne v Kennedy*.[15] The majority emphasised that the inquiry was into whether the plaintiff acted "freely", in which case the

7 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [34] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).
8 See further discussion in *Anderson v McPherson (No 2)* [2012] WASC 19, [240].
9 *Johnson v Buttress* (1936) 56 CLR 113, 134–6 (Dixon J). See also Bigwood, "Undue Influence: 'Impaired Consent or Wicked Exploitation'?" (1996) 16 *Oxford Journal of Legal Studies* 503.
10 *Johnson v Buttress* (1936) 56 CLR 113, 134–5; see, eg, *Courtney v Powell* [2012] NSWSC 460.
11 *Johnson v Buttress* (1936) 56 CLR 113, 135; see, eg, *Courtney v Powell* [2012] NSWSC 460.
12 See *Royal Bank of Scotland plc v Etridge (No 2)* [2001] UKHL 44; [2002] 2 AC 773, [32]. Also Capper, "The Unconscionable Bargain in the Common Law World" (2010) 126 *Law Quarterly Review* 403.
13 See Capper, "The Unconscionable Bargain in the Common Law World" (2010) 126 *Law Quarterly Review* 403.
14 *Commercial Bank of Australia Ltd v Amadio* (1983) 151 CLR 447, 474, see also 461 (Mason J); see also *Anderson v McPherson (No 2)* [2012] WASC 19.
15 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [29], [57] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

transaction would stand, or had "substantially subordinated" his or her will to that of the other party, in which case the doctrine of undue influence would be invoked.[16]

UNDUE INFLUENCE ESTABLISHED IN FACT

[35.20] Lack of free choice

For undue influence to be established "in fact" from the circumstances of the impugned transaction, "it is necessary for the [plaintiff] to prove affirmatively that the [defendant] exerted undue influence on the [plaintiff]".[17] The facts must show that the "transaction was the outcome of such an actual influence over the mind of the [plaintiff] that it cannot be considered a free act".[18] The High Court in *Thorne v Kennedy* explained:

> The question whether a person's act is "free" requires consideration of the extent to which the person was constrained in assessing alternatives and deciding between them. Pressure can deprive a person of free choice in this sense where it causes the person substantially to subordinate his or her will to that of the other party. It is not necessary for a conclusion that a person's free will has been substantially subordinated to find that the party seeking relief was reduced entirely to an automaton or that the person became a "mere channel through which the will of the defendant operated". Questions of degree are involved. But, at the very least, the judgmental capacity of the party seeking relief must be "markedly sub-standard" as a result of the effect upon the person's mind of the will of another.[19]

The influence exercised to coerce agreement for the purposes of undue influence may involve physical, financial or emotional pressure. In *Farmers' Co-Operative Executors & Trustees Ltd v Perks*,[20] a wife transferred her interest as tenant in common in a farming property, jointly owned by herself and her husband, to the husband. The evidence demonstrated a long history of brutal violence perpetrated by the husband against the wife, which ended in his murdering her. It was held that a relationship of influence existed and the presumption that the wife transferred the property as a result of her husband's undue influence was not rebutted. It was held there was evidence establishing that the transfer resulted from *actual* undue influence. Accordingly, the transfer was set aside by the judge.

Thorne v Kennedy[21] involved prenuptial and postnuptial agreements between Ms Thorne, an Eastern European woman, and Mr Kennedy, a wealthy Australian property developer. The parties met online on a website for potential brides. Thorne was induced to come to Australia to marry Kennedy. The trial judge noted this meant that "[i]f the relationship ended, she would have nothing. No job, no visa, no home, no place, no community".[22]

16 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [32] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ). See criticism of the uncritical adoption of this perspective in Bigwood, "The Undue Influence of 'Non-Australian' Undue Influence Law on Australian Undue Influence Law: Farewell, *Johnson v Buttress?* Part 1" (2018) 35 *Journal of Contract Law* 56.

17 *Barclays Bank plc v O'Brien* [1994] 1 AC 180, 189.

18 *Johnson v Buttress* (1936) 56 CLR 113, 134.

19 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [32].

20 *Farmers' Co-Operative Executors & Trustees Ltd v Perks* (1989) 52 SASR 399.

21 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85.

22 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [47] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

Kennedy arranged for Thorne to obtain independent legal advice about the prenuptial agreement 10 days before their wedding. Thorne had not previously been aware of the contents of the prenuptial agreement. The solicitor advised Thorne not to sign the prenuptial agreement. In particular, under the agreement, if the parties separated after at least three years of marriage, Thorne would receive a payment of $50,000, described by her solicitor as "piteously small".[23] Kennedy told Thorne that the wedding would not go ahead unless she signed the agreements, despite the wedding arrangements being well progressed. The agreement was signed four days before the wedding, and the postnuptial agreement shortly after the wedding. Slightly less than four years into the marriage, the parties separated, and Thorne began proceedings to set aside the agreements.

The trial judge found that the agreement was signed in vitiating circumstances and found for Thorne. The Full Court of the Family Court of Australia set aside those findings. They were upheld by the High Court.

The High Court held that, in considering undue influence, the unfair and unreasonable terms in the prenuptial and postnuptial agreements were relevant to assessing whether they were vitiated on grounds of undue influence.[24] Other relevant factors were:

> (i) whether the agreement was offered on a basis that it was not subject to negotiation; (ii) the emotional circumstances in which the agreement was entered including any explicit or implicit threat to end a marriage or to end an engagement; (iii) whether there was any time for careful reflection; (iv) the nature of the parties' relationship; (v) the relative financial positions of the parties; and (vi) the independent advice that was received and whether there was time to reflect on that advice.[25]

These factors should be assessed in context and should not be treated as an exercise of "mathematical precision".[26]

The trial judge found that Thorne considered she had no choice other than to enter into the agreements and was unable to exercise a calm and considered judgment.[27] Accordingly, it was open to the trial judge to conclude that the agreements were the result of the undue influence of the defendant. Moreover, the agreements were liable to be set aside on ground of unconscionable conduct, discussed in Chapter 36.[28]

The trial judge had focused on Thorne's lack of free will rather than whether Kennedy's actions amounted illegitimate pressure. Accordingly, the Court held that it was not necessary to address duress.[29]

Overlap with duress

[35.30] As noted in Chapter 34, there is considerable potential overlap between undue influence and duress. In *Thorne v Kennedy*, the High Court noted that the boundaries,

23 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [8] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

24 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [56] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

25 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [60] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

26 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [62] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

27 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [59] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

28 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [63]–[65] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ); [75] (Nettle J); [119]–[123] (Gordon J).

29 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [29], [57] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ), also [70] (Nettle J). See also Chapter 34.

particularly between these doctrines, "are blurred".[30] One difference between the doctrines is that a broader range of conduct by the defendant will be relevant in assessing undue influence than for duress. In particular, illegitimate pressure or a threat are not required for undue influence.[31]

These differences arise because, as Edelman and Bant explain, the effect of the pressure or influence on the plaintiff's decision making is very different in undue influence and in duress:

> Plaintiffs in undue influence cases are typically over-eager and unwilling to enter the transaction, without considering their own interests. By contrast, plaintiffs in illegitimate pressure cases typically are only too aware of their own interests and are loathe to succumb to "some coercion from outside, some overreaching, some form of cheating".[32]

UNDUE INFLUENCE ARISING BY PRESUMPTION

[35.35] Applies to particular relationships

Undue influence may also be proved by presumption. The High Court explained in *Thorne v Kennedy* that:

> Common experience gives rise to a presumption that a transaction was not the exercise of a person's free will if (i) the person is proved to be in a particular relationship, and (ii) the transaction is one, commonly involving a "substantial benefit" to another, which cannot be explained by "ordinary motives", or "is not readily explicable by the relationship of the parties".[33]

This presumption represents a shift of the evidential burden.[34] In such cases, the plaintiff does not have to prove that undue influence was actually exerted by the defendant. Undue influence by the defendant is presumed by virtue of the relationship between the parties. The defendant will then have the burden of disproving undue influence by showing that the plaintiff freely consented to the transaction.

Overlap with undue influence established by fact

[35.37] There may be an overlap between undue influence established on the facts of the case and undue influence established through the presumption. In some cases, courts may find for the plaintiff on both grounds.[35] In other cases, judges may differ in their interpretation of the conduct. In *Johnson v Buttress*,[36] discussed below, Starke J held there was sufficient evidence to infer that actual undue influence had been exercised.[37] Dixon J held that there was

30 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [28] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

31 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [30] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

32 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 201, Quoting *Allcard v Skinner* (1887) 36 Ch D 145, 181.

33 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [34] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

34 See *Royal Bank of Scotland plc v Etridge (No 2)* [2001] UKHL 44; [2002] 2 AC 773.

35 See, eg, *Farmers' Co-Operative Executors & Trustees Ltd v Perks* (1989) 52 SASR 399.

36 *Johnson v Buttress* (1936) 56 CLR 113, discussed at [35.45].

37 *Johnson v Buttress* (1936) 56 CLR 113, 126.

insufficient evidence of actual undue influence but that the facts disclosed a relationship of influence sufficient to attract the presumption.[38]

Presumed relationships of influence

[35.40] Equity deems certain relationships to be relationships of influence: parent over child,[39] guardian over ward,[40] religious adviser over disciple,[41] solicitor over client[42] and doctor over patient.[43] In all of these relationships, the first named person (the *defendant*) is presumed to have unduly influenced the second named person (the *plaintiff*) in any contract between them or in any gift given by the plaintiff to the defendant. In these categories, the very fact of the relationship is sufficient to raise the presumption of undue influence and to place on the defendant the burden of disproving excessive influence.

In *Hartigan v International Society for Krishna Consciousness Inc*, the plaintiff was a member of the Krishna Consciousness Movement. The plaintiff gave her house and farm to the defendant corporation that held property for the movement. The plaintiff had misunderstood the religious teaching of the Movement and wrongly thought it required her to give up all worldly possessions. At the time of the transaction, the plaintiff had three small children and no other housing. Bryson J found that the transaction gave rise to a presumption of undue influence entitling the plaintiff to relief. The case illustrates the importance of the presumption of undue influence in triggering the application of the doctrine. There was no suggestion of deliberate wrongdoing by the defendant. Bryson J held that there was "nothing in the nature of a deliberate attempt by the defendant or by anyone in the Krishna Consciousness Movement to get the better of the plaintiff, to overbear her or deceive her, or to deprive her of the opportunity of making up her own mind".[44] However, the nature of the relationship was such that there was a risk that the plaintiff had not brought a fully consenting mind to the transaction. This presumption of influence was not rebutted. The transaction was highly disadvantageous to the plaintiff and could not be explained by reference to ordinary motives of "generosity, charity or religious feeling".[45]

Relationships which are not deemed to be relationships of influence include the relationship of accountant (or financial adviser) and client and fiancé and fiancée.[46] Even relationships of a fiduciary kind do not per se fall within the category, as not all fiduciary relationships (such as principal and agent, and trustee and beneficiary) are regarded as relationships of influence. No presumption of influence arises from the relationship of husband and wife. It might be thought that this identical treatment of husband and wife stems from a policy of promoting equality. However, in *Yerkey v Jones*,[47] Dixon J stated that the reason for the denial

38 *Johnson v Buttress* (1936) 56 CLR 113, 133-4, 138.

39 *Lanchashire Loans Ltd v Black* [1934] 1 KB 380; *Westmelton (Vic) Pty Ltd v Archer and Schulman* [1982] VR 305.

40 *Hylton v Hylton* [1754] 28 ER 349.

41 *Wright v Carter* [1903] 1 Ch D 27.

42 *Allcard v Skinner* (1887) 36 Ch D 145.

43 *Mitchel v Homfray* (1881) 8 QBD 587.

44 *Hartigan v International Society for Krishna Consciousness Inc* [2002] NSWSC 810, [32].

45 *Hartigan v International Society for Krishna Consciousness Inc* [2002] NSWSC 810, [37].

46 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [36] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ). See also Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 232.

47 *Yerkey v Jones* (1939) 63 CLR 649, 675.

of the presumption was that "there is nothing unusual or strange in a wife from motives of affection or even of prudence conferring a large proprietary or pecuniary benefit upon her husband". The policy, it seems, is to encourage altruism between married partners, rather than to promote equality in marital relationships.[48] However, in the same case, Dixon J stated that the relationship had never been completely divested of "equitable presumptions of an invalidating tendency" in favour of the wife.[49] Chapter 37 discusses the special principles to protect wives who guarantee their husbands' business borrowings.[50] In any event, the fact that one party is the spouse of the other is not to be ignored in determining whether a relationship of influence exists *in fact*.[51]

Proof of a relationship of influence

[35.45] If the relationship between the plaintiff and the defendant does not fall into one of the recognised classes of deemed relationships of influence, the plaintiff may prove that there is such a relationship. Once a relationship of influence is shown, the presumption that any transaction was the result of undue influence of the defendant over the plaintiff arises. There is no closed list of relationships of influence, and the facts of the particular case must be thoroughly scrutinised. For example, the relationship of banker and customer may be found to be a relationship of influence on the facts of one case,[52] but not on the facts of another.[53]

To establish a relationship of influence from which undue influence can be presumed, it will not be sufficient that the plaintiff consulted the defendant in making a decision. If this was the case, then transactions between friends and family could rarely stand. Courts have explained that "more is required than the 'influence' that any person might have on another by making [a] recommendation or giving advice".[54] Rather a relationship of influence "is one which involves ascendancy and influence on the part of the dominant party, or dependence, reliance, trust and confidence on the part of the weaker party".[55]

The leading Australian case on presumed undue influence is *Johnson v Buttress*.[56] In this case, Mr Buttress gave his land and cottage to Mrs Johnson three years before he died because she had been very good to his wife and he was very fond of her. The administrator of his will challenged the transfer. The High Court held that it should be set aside. Dixon J considered that, although there was no positive proof that the transfer was procured by improper exercise of an actual ascendancy gained by Mrs Johnson over the deceased, there was evidence of an antecedent relationship of influence over Mr Buttress. Mr Buttress was described by the

48 *Yerkey v Jones* (1939) 63 CLR 649, 675.

49 See Otto, "A Barren Future? Equity's Conscience and Women's Inequality" (1992) 18 *Melbourne University Law Review* 808, 819.

50 See Chapter 37.

51 See, eg, *Farmers' Co-Operative Executors & Trustees Ltd v Perks* (1989) 52 SASR 399, considered at [35.20].

52 See *Lloyds Bank v Bundy* [1975] QB 326.

53 See *National Westminster Bank plc v Morgan* [1985] 1 AC 686.

54 *Tulloch (deceased) v Braybon (No 2)* [2010] NSWSC 650, [51]; *Lee v Chai* [2013] QSC 136, [197].

55 *Tulloch (deceased) v Braybon (No 2)* [2010] NSWSC 650, [38]. See also *Johnson v Buttress* (1936) 56 CLR 113, 134–5. *Courtney v Powell* [2012] NSWSC 460, [38]; *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [34].

56 *Johnson v Buttress* (1936) 56 CLR 113. See also *Courtney v Powell* [2012] NSWSC 460, [40].

Court as illiterate, ignorant of financial affairs and a person of strange disposition.[57] He did not understand he had disposed of the property irrevocably. Mrs Johnson knew him for more than 20 years and had rendered assistance to his wife before she died. She visited him, allowed him to live in a shack on her property and sent necessaries to him from time to time. Dixon J considered that Mrs Johnson had the burden of rebutting a presumption of undue influence which she had failed to discharge. She could not show that the transfer was the result of the free exercise of the donor's independent will.

An interesting contrast is *Lee v Chai*.[58] Mr Lee purchased an apartment and a Porsche motor vehicle for Ms Chai, with whom he was having an affair. Mr Lee later argued that the gift of both items of property should be set aside as the result of undue influence. The claim was dismissed. Mr Lee and Ms Chai were not in a relationship of influence that would attract the operation of the equitable doctrine.[59] Mr Lee was described as an intelligent and well-educated man with substantial experience in business affairs.[60] Ms Chai had a less forceful personality and less experience in business.[61] Mr Lee was emotionally dependent on Ms Chai, but this was not considered to affect his judgment in business affairs.[62]

Need the transaction be disadvantageous?

[35.47] In Australia, it has not been a requirement for relief against undue influence that the transaction has been disadvantageous to the plaintiff, although this factor will be relevant in assessing whether there has been such influence.[63] By contrast, in England in *National Westminster Bank plc v Morgan*,[64] Lord Scarman said that, to obtain relief for undue influence, a plaintiff must show that the transaction was *manifestly disadvantageous* to the plaintiff.[65] In *CIBC Mortgages plc v Pitt*,[66] this requirement was held not to apply to cases of actual undue influence, only to cases of presumed undue influence. In *Royal Bank of Scotland plc v Etridge (No 2)*, Lord Nicholls affirmed that to raise a presumption of undue influence, it was necessary to look not just at the relationship between the parties but also at the nature of the transaction.[67] This requirement was a necessary limitation upon the doctrine. Lord Nicholls said that:

> It would be absurd for the law to presume that every gift by a child to a parent, or every transaction between a client and his solicitor or between a patient and his doctor, was brought about by undue influence unless the contrary is affirmatively proved. Such a presumption would be too far-reaching.[68]

57 *Johnson v Buttress* (1936) 56 CLR 113, 137.

58 *Lee v Chai* [2013] QSC 136.

59 *Lee v Chai* [2013] QSC 136, [208].

60 *Lee v Chai* [2013] QSC 136, [200].

61 *Lee v Chai* [2013] QSC 136, [201].

62 *Lee v Chai* [2013] QSC 136, [203].

63 See, eg, *Baburin v Baburin* [1990] 2 Qd R 101. Contra *Farmers' Co-Operative Executors & Trustees Ltd v Perks* (1989) 52 SASR 399.

64 *National Westminster Bank plc v Morgan* [1985] 1 AC 686, 704.

65 *National Westminster Bank plc v Morgan* [1985] 1 AC 686, 704.

66 *National Westminster Bank plc v Morgan* [1994] 1 AC 200, 209.

67 *Royal Bank of Scotland plc v Etridge (No 2)* [2001] UKHL 44; [2002] 2 AC 773, Lord Bingham and Lord Clyde concurring.

68 *Royal Bank of Scotland plc v Etridge (No 2)* [2001] UKHL 44; [2002] 2 AC 773, [24].

Lord Nicholls rejected manifest disadvantage as a test for identifying presumed undue influence.[69] Lord Nicholls proposed instead that there must be evidence the transaction in question was "explicable only on the basis that undue influence had been exercised to procure it".[70]

In *Thorne v Kennedy*,[71] the High Court apparently adopted a similar approach to the English requirements for controlling the scope of the doctrine, stating that, for a presumption of undue influence, the transaction must be one "involving a 'substantial benefit' to another, which cannot be explained by 'ordinary motives', or 'is not readily explicable by the relationship of the parties' ".[72] The requirement that the transaction be not readily explained by other reasons has a function of establishing a causal link between the presumed influence and the outcome, suggesting that the influence was a factor in the plaintiff's decision.[73]

REBUTTING THE PRESUMPTION

[35.50] When a relationship of influence gives rise to a presumption of influence, the court must determine whether the presumption has been rebutted. This requires establishing both that the plaintiff "knew and understood what he or she was doing, and that he or she was acting independently of the influence of the dominant party".[74] It is not sufficient that the plaintiff understood the transaction; the plaintiff must be "emancipated" from the influence of the impugned relationship.[75] One influential factor in deciding whether a plaintiff was acting independently is whether the plaintiff was given competent advice by an independent and well-informed adviser. The advice is often given by a solicitor but need not be. The important factors are the quality of the advice and its effect on the plaintiff's capacity for making an independent decision.[76]

In *Badman v Drake*,[77] the defendants were a couple who befriended the plaintiff, a socially isolated and lonely older woman. When the couple fell into financial difficulties, the older women used her savings to purchase the couple's home for them. Solicitors acting for both sets of parties were concerned about the potential for equitable fraud and advised that a number of steps be followed to safeguard the interests of the plaintiff. The defendants refused to accept this advice because they were anxious to finalise the transaction. They obtained the advice of a doctor that the plaintiff had the capacity to enter into the agreement, but the plaintiff was not given independent legal advice. The transaction was held to have been tainted by undue influence, and a charge was levied against the home for repayment of the money that had been

69 *Royal Bank of Scotland plc v Etridge (No 2)* [2001] UKHL 44; [2002] 2 AC 773, [29], quoting *National Westminster Bank plc v Morgan* [1985] 1 AC 686, 704.

70 *Royal Bank of Scotland plc v Etridge (No 2)* [2001] UKHL 44; [2002] 2 AC 773, [25].

71 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85.

72 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [34] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

73 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 237.

74 *Tulloch (deceased) v Braybon (No 2)* [2010] NSWSC 650, [40]. See also *Watkins v Combes* (1922) 30 CLR 180; *Quek v Beggs* (1990) 5 BPR 11,761.

75 Edelman and Bant, *Unjust Enrichment* (2nd ed, 2016), p 238.

76 *Royal Bank of Scotland plc v Etridge (No 2)* [2001] UKHL 44; [2002] 2 AC 773, [20]. See also *Inche Noriah v Shaik Allie Bin Omar* [1929] AC 127, 135–6.

77 *Badman v Drake* [2008] NSWSC 1366.

contributed by the plaintiff. The Court considered that the solicitors' advice, if followed, may have been sufficient to rebut the presumption of undue influence. The Court explained that:

> There is no doubt that an elderly person may, if she wishes, deal with her property in any way she likes including making gifts to friends. However, as most lawyers know and as [the solicitors acting for the parties] appreciated in the present case, where there is doubt about a person's capacity, the transaction is always in some danger of being attacked unless it can be shown that the action was a free will action of the elderly person.[78]

The Court continued:

> Had the transaction been properly explained and had there been independent advice, it may well be that there would have been sufficient material together with Dr Lowe's advice to show that the plaintiff had capacity to do what she wanted to do. However, the transaction did not happen in the way in which the lawyers proposed it happen and it is not at all clear from the material that the plaintiff did anticipate that she would be giving away the whole of the $378,623.19 to the first and second defendants.[79]

While independent advice is a matter of vital importance in most cases, there is no rule of law that, in order to rebut a presumption of undue influence, the plaintiff must be shown to have received such advice.[80] The recipient of a benefit may prove, by other means, that the plaintiff exercised an informed judgment. An independent judgment is not established by showing that the proposal came from the plaintiff.[81] Rather the Court will consider the circumstances of the case and the age, character and experience of the plaintiff.[82] In some cases, the presumption may be rebutted by reference to the purpose of the transaction, which was not produced by any influence of the recipient.[83]

In *Westmelton (Vic) Pty Ltd v Archer and Shulman*,[84] the plaintiff was a solicitor who advised the defendant development company. He continued to do the company's legal work after he was appointed as director and chairman of the board. When he presented a bill of costs to the extent of $25,000 for legal work rendered, he suggested to one of the directors that it could be reduced in return for a share in the company's profits. He left the directors' meeting when this matter was discussed and, when he came back, he accepted a proposal that, in return for reducing the bill by $10,000, he should thereafter be entitled to 7.5 per cent of the defendant's profits before tax. The defendant paid the reduced bill but refused to pay the profits. It was held the contract was enforceable. Although there was a solicitor–client relationship between the parties (ie, a deemed relationship of influence), this was not a case where the presumption of influence could only be rebutted by proof that the solicitor had advised the directors of the defendant to obtain separate legal advice on the nature of the proposed contract. The Court said:

> The extent and weight of the burden cast upon the person in whom the confidence was reposed, and the matters (where the presumption applies) of which the court will require to be satisfied

78 *Badman v Drake* [2008] NSWSC 1366, [80].

79 *Badman v Drake* [2008] NSWSC 1366, [80].

80 *Inche Noriah v Shaik Allie Bin Omar* [1921] AC 127, 136; *Union Fidelity Trustee Co of Australia Ltd v Gibson* [1971] VR 573, 577.

81 *Spong v Spong* (1914) 18 CLR 544, 549.

82 *Johnson v Buttress* (1936) 56 CLR 113, 119. See also *Courtney v Powell* [2012] NSWSC 460.

83 See, eg, *ANZ Banking Group Ltd v Alirezai* [2004] QCA 6, [75]; *Daunt v Daunt* [2015] VSCA 58, [77]–[79].

84 *Westmelton (Vic) Pty Ltd v Archer and Schulman* [1982] VR 305.

> before it will regard the presumption as having been negatived, must vary enormously with all the circumstances of the case …[85]

In this case, the company had more expertise in commerce and finance than most solicitors. Once the Court was satisfied that the plaintiff solicitor dealt fairly and honestly with a well-informed and sophisticated corporate client and that the client was in no way relying upon any confidence or expectation of legal advice, then it was possible to conclude that there was no duty to advise the client further. Alternatively, this kind of scenario might now be dealt with by considering whether the transaction said to be procured by undue influence could be explained by reference to the commercial relationship of the parties, as discussed at [35.47].

RELIEF

[35.55] The relief available to victims of undue influence is the same as that available to those who have been induced by duress or coercion to enter into the contract. The contract may be rescinded.[86] If the defendant seeks specific performance of the contract, this will be denied.

85 *Westmelton (Vic) Pty Ltd v Archer and Schulman* [1982] VR 305, 312.

86 For a detailed discussion of rescission, see Chapter 39.

CHAPTER **36**

Unconscionable dealing

OVERVIEW

[36.05] The equitable doctrine of unconscionable dealing "looks to the conduct of [the *defendant*] in attempting to enforce, or retain the benefit of, a dealing with a person under a special disability [the *plaintiff*] in circumstances where it is not consistent with equity or good conscience that he should do so".[1] It is unconscionable for a defendant to take advantage of a plaintiff's position of special disadvantage in circumstances in which the defendant "knew, or ought to have known, of the existence and the effect of the disadvantage".[2]

Historical background

[36.10] The origins of the doctrine of unconscionable dealing lie in the protection extended by courts to "expectant heirs", that is people who expected to inherit property on the death of another. Before they came into possession on the death of the other person, expectant heirs had a "reversionary interest" in the property, which they could sell, sometimes at a gross undervalue. The protection extended to expectant heirs reached the point by the mid-19th century where an expectant heir could obtain relief from the courts simply on the basis that an inadequate price had been paid for the property. This jurisdiction was modified in England when the *Sales of Reversions Act 1867* was passed. The relevant provision in Australia is found in property and conveyancing legislation. For example, in Victoria, s 175 of the *Property Law Act 1958* (Vic) states:

1 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 474 (Deane J). See also *Bridgewater v Leahy* [1998] HCA 66; (1998) 194 CLR 457.

2 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [38] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

(1) No acquisition made in good faith, without fraud or unfair dealing, of any reversionary interest in real or personal property, for money or money's worth, shall be liable to be opened or set aside merely on the ground of under value …

(2) This section shall not affect the jurisdiction of the Court to set aside or modify unconscionable bargains.

The courts also traditionally gave relief in respect of bargains characterised by exorbitant terms entered into by poor, sick, weak-minded or inexperienced persons who lacked the advantage of independent advice. Thus, in *Fry v Lane*, Kay J said:

> The result of the decisions is that where a purchase is made from a poor and ignorant man at a considerable undervalue, the vendor having no independent advice, a court of equity will set aside the transaction. This will be done even in the case of property in possession, and a fortiori if the interest be reversionary. The circumstances of poverty and ignorance of the vendor, and the absence of independent advice, throw upon the purchaser, when the transaction is impeached, the onus of proving, in Lord Selborne's words, that the purchase was "fair, just and reasonable".[3]

Modern applications

[36.15] These grounds of relief form the basis of the modern doctrine of unconscionable dealing. The modern doctrine in Australian law has developed from the decisions in *Blomley v Ryan*[4] and *Commercial Bank of Australia Ltd v Amadio* (*Amadio*).[5]

In *Blomley v Ryan*, the plaintiff sought specific performance of a contract under which the defendant agreed to sell to the plaintiff a grazing property for £25,000. The defendant resisted this order. The property had been sold significantly under value and upon terms highly favourable to the plaintiff. A bottle of rum was taken to the negotiations by a colleague of the plaintiff's agent and drunk by the already inebriated plaintiff. The trial judge described and found that at the time the contract was signed:

> the defendant was an old man, whose health and faculties had been impaired by habitual drinking to excess over a long period, who was at the material time in the middle of a prolonged bout of heavy drinking of rum, and who was utterly incapable of forming a rational judgment about the terms of any business transaction. … [the trial judge] also held that the defendant's condition must have been patent to the plaintiff's father, who acted as the plaintiff's agent.[6]

The High Court refused to order specific performance and set aside the contract on grounds of unconscionable dealing. In the circumstances of the case such an unfair advantage had been taken of the defendant that the contract could not be allowed to stand.

[36.20] In *Amadio*[7] Mr and Mrs Amadio signed a mortgage under which they agreed to pay the bank on demand any moneys owed to the bank, presently or in the future, by a land development company which was controlled by their son Vincenzo. They mortgaged an office block they owned as security for the payment. When their son's company went into liquidation, the bank proposed to exercise its power of sale under the mortgage. Mr and

3 *Fry v Lane* (1888) 40 Ch D 312, 322.
4 *Blomley v Ryan* (1956) 99 CLR 362.
5 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447.
6 *Blomley v Ryan* (1956) 99 CLR 362, 408.
7 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447.

Mrs Amadio attacked the validity of the guarantee/mortgage and in the High Court they succeeded in having the transaction set aside.[8]

The jurisdiction to relieve against unconscionable contracts was described by Deane J as follows:

> The jurisdiction is long established as extending generally to circumstances in which (i) a party to a transaction was under a special disability in dealing with the other party with the consequence that there was an absence of any reasonable degree of equality between them and (ii) that disability was sufficiently evident to the stronger party to make it prima facie unfair or "unconscientious" that he procure, or accept, the weaker party's assent to the impugned transaction in the circumstances in which he procured or accepted it. Where such circumstances are shown to have existed, an onus is cast upon the stronger party to show that the transaction was fair, just and reasonable: "the burthen of shewing the fairness of the transaction is thrown on the person who seeks to obtain the benefit of the contract".[9]

The judges in majority held that the Amadios were under a special disability in dealing with the bank because of a combination of factors: their respective ages (76 and 71), their limited grasp of written English, the circumstances in which the bank presented them with the document for signature and their lack of knowledge and understanding of that document. The Amadios knew nothing of the financial difficulties of their son's company, which was repeatedly and substantially in excess of its overdraft limit. Nor did they know that the bank selectively dishonoured cheques drawn by the company in order to maintain the company's façade of prosperity. They were told by Vincenzo, on whom they relied for advice, that they were being asked to guarantee up to $50,000 for six months, whereas in fact there were no such limits. When Virgo, the bank's representative, went to the Amadios' home to obtain their signatures, they agreed in the kitchen to sign the relevant document, which they had not read, and which was not explained to them. When Mr Amadio said the mortgage was for six months, Virgo indicated that there was no such limit, but he did not disabuse him about the amount the Amadios thought they were guaranteeing.

The special disability of the Amadios was sufficiently evident to the bank (through Virgo) to make it prima facie unconscientious of the bank to procure the execution of the guarantee/mortgage in the circumstances in which it was procured. Virgo knew that Vincenzo was the dominant member of the family, that his company could not meet its debts and that he could not have explained the mortgage document to his parents. Virgo simply "closed his eyes" to the Amadios' vulnerability.

The onus cast on the bank to show that the transaction was fair and reasonable was not discharged given the circumstances in which the Amadios' assent had been procured. There was a significant difference between a potential liability of up to $50,000 under a guarantee of a financially successful company and a potentially unlimited liability under a guarantee of a financially unsuccessful company. The Amadios would not have executed the transaction if they had known of the financial troubles their son's company was experiencing.

8 Deane, Wilson and Mason JJ set the transaction aside on the basis that it was procured by unconscionable dealing. Gibb CJ held there was no unconscionable dealing, but that the transaction should still be set aside on the basis that the bank had failed in a duty of disclosure. Dawson J dissented.

9 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 474 (Deane J).

THE ELEMENTS OF THE DOCTRINE

[36.25] As *Amadio* illustrates, the doctrine of unconscionable dealing operates where:

1. "in entering into a transaction the plaintiff was under a special disability in dealing with the defendant, with the consequence that there was an absence of any reasonable degree of equality between them"; and
2. "the disability was sufficiently evident to the defendant to make it prima facie unfair or 'unconscientious' that he or she procure, or accept, the plaintiff's assent to the impugned transaction in the circumstances in which he or she procured or accepted it".[10]

Where these elements are established, there is an equitable presumption to the effect that the improvident transaction was a consequence of the special disadvantage, and that the defendant has unconscientiously taken advantage of the opportunity presented by the disadvantage.[11] The onus is then on the defendant to show that the transaction was fair, just and reasonable.[12]

Adequacy of consideration

[36.30] In most cases of unconscionable dealing, there is an inadequate consideration moving from the defendant. However, it is not essential that this should be so. A transaction may still be unfair and unreasonable from the point of view of the person under a special disability, even though adequate consideration has moved from the defendant. This could clearly be the case, for example, where the consideration moved not to the plaintiff, but to some third party, for example, where the plaintiff is a guarantor.[13] On the other hand, inadequacy of consideration may be important in supporting an inference that a disability existed and in showing that unfair advantage was taken of it.[14] In *Blomley v Ryan*, Fullagar J explained:

> It does not appear to be essential in all cases that the party at a disadvantage should suffer loss or detriment by the bargain. … But inadequacy of consideration, while never of itself a ground for resisting enforcement, will often be a specially important element in cases of this type. It may be important in either or both of two ways—firstly as supporting the inference that a position of disadvantage existed, and secondly as tending to show that an unfair use was made of the occasion.[15]

SPECIAL DISADVANTAGE

[36.35] The situations that may constitute a special disadvantage for the purposes of unconscionable dealing cannot be comprehensively defined. The traditional starting point is the statement of Fullagar J in *Blomley v Ryan*.[16] Fullagar J said that the circumstances which may place a person under a special disability include:

10 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 474 (Deane J).

11 *Turner v Windever* [2005] NSWCA 73, [2], [105]; *Lampropoulos v Kolnik* [2010] WASC 193, [389].

12 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 474 (Deane J).

13 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 475.

14 *Blomley v Ryan* (1956) 99 CLR 362, 405. See also *Elkofairi v Permanent Trustee Co Ltd* [2002] NSWCA 413.

15 *Blomley v Ryan* (1956) 99 CLR 362, 405.

16 *Blomley v Ryan* (1956) 99 CLR 362.

> poverty or need of any kind, sickness, age, sex, infirmity of body or mind, drunkenness, illiteracy or lack of education, lack of assistance or explanation where assistance or explanation is necessary. The common characteristic seems to be that they have the effect of placing one party at a serious disadvantage vis-à-vis the other.[17]

Although sex is mentioned in Fullagar J's list, it has not been recognised by subsequent courts as forming the basis of a special disability for the purpose of unconscionable dealing.[18] This may be seen as a recognition of gender equality or as a failure to recognise the inequalities of power associated with relations between the sexes.[19]

Courts have also stressed the importance of the disadvantage being "special". As Mason J explained in *Amadio*:

> I qualify the word "disadvantage" by the adjective "special" in order to disavow any suggestion that the principle applies whenever there is some difference in the bargaining power of the parties …[20]

A difference in bargaining power is not on its own sufficient to place the plaintiff at a special disadvantage in relation to the defendent.[21] The disadvantage must be one that "seriously affects the ability of the innocent party to make a judgment as to his [or her] own best interests".[22] The factors identified in Fullagar's judgment are considerations that in the circumstances of the case may lead to the plaintiff being disadvantaged in this manner. A good example is *Amadio*,[23] discussed earlier in this section. In this case, the Amadios were under a special disability due to the combination of circumstances that they faced. In particular, the Amadios had only a limited understanding of written English and were under a misapprehension as to the nature and implications of the transaction into which they were entering.[24]

In *Thorne v Kennedy* Gordon J[25] and again in *Australian Securities and Investments Commission v Kobelt* Nettle and Gordon JJ[26] described the test as being whether the special disadvantage seriously affected the plaintiff's ability to *safeguard* his or her own interests, as opposed to *judge* his or her own interests. This is a subtle but significant extension of the doctrine. In *Thorne v Kennedy*, discussed below at [36.55], the plaintiff had received legal advice that a prenuptial agreement did not favour her interests. She nonetheless signed the agreement because she considered she had no other choice.[27] The problem was therefore the plaintiff's inability to safeguard, as opposed to judge, her best interests.

It is clear that the special disadvantage must affect ability of the plaintiff to decide whether to enter into the relevant transaction, rather than merely evidence ongoing adverse

17 *Blomley v Ryan* (1956) 99 CLR 362, 405 (Fullagar J).

18 See, however, the special principles developed by the courts to protect wives who guarantee their husbands' business debts: see Chapter 37.

19 See Otto, "A Barren Future? Equity's Conscience and Women's Inequality" (1992) 18 *Melbourne University Law Review* 808, 815, fn 39.

20 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 462.

21 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 462.

22 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 462.

23 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447.

24 See also *Permanent Mortgages Pty Ltd v Vandenbergh* [2010] WASC 10, [235]–[236].

25 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [113].

26 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [147] (Nettle and Gordon JJ) (footnotes omitted).

27 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [63]–[64], [74].

circumstances. *Kakavas v Crown Melbourne Ltd* (*Kakavas*)[28] concerned a claim by Harry Kakavas, for compensation for some $20 million lost while gambling at Crown Casino in Melbourne between 2004 and 2006 on the basis of unconscionable conduct by Crown. The claim was made under s 51AA of the *Trade Practices Act 1974* (Cth), now s 20 of the ACL, which provides a statutory remedy for the equitable doctrine of unconscionable dealing. The Supreme Court of Victoria rejected Kakavas' claim to recover the $20 million. This decision was upheld by the Court of Appeal. Kakavas was then granted special leave to appeal the Full Court's decision to the High Court. Kakavas' actions in the Supreme Court of Victoria were based on the argument that Crown had engaged in unconscionable conduct in attempting to entice the custom of Kakavas. In the High Court, the claim was changed and based instead on alleged unconscionable conduct in Crown failing to respond to Kakavas' inability to make worthwhile decisions for himself whilst at the gaming table.

The High Court (French CJ, Hayne, Crennan, Kiefel, Bell, Gageler and Keane JJ) was unanimous in rejecting the claim. On the question of whether Kakavas suffered a "special disability", necessary for a finding of unconscionable conduct, the Court accepted the factual findings of the trial judge that Kakavas was a problem (even pathological) gambler. Nonetheless, the court concluded these findings did not demonstrate that Kakavas was unable to control the urge to gamble, which was the trigger for the losses incurred.[29] The was not the end of the inquiry. The circumstances in which the transaction under challenge occurred and the relationship between the parties had to be considered. Even assuming Kakavas was a compulsive gambler, this did not place him at a relevant disadvantage in his dealings with the Casino. It was Kakavas who made the decision to enter the gaming venue.[30] Kakavas had chosen to enter the Casino, when he could have made a different decision.[31] Care needed to be taken in assessing any aspect of the relationship between gambler and casino because the very nature of that relationship was that one party sought to inflict losses on the other.[32]

Emotional dependence

[36.55] In *Louth v Diprose*,[33] discussed further at [36.95], the High Court accepted that emotional dependence, in combination with other factors, may amount to a special disability for the purpose of unconscionable dealing.[34] A person who is emotionally dependent on another may be vulnerable to exploitation or abuse by that other. In the case before the Court, the victim was a male solicitor. He was held to have been manipulated by a woman with whom he was utterly infatuated. Her manipulation was said to take the form of falsely manufacturing situations of personal crisis and threatening suicide. His gift of a property to her was set aside.[35]

The recognition of emotional dependence as a disability in need of protection gives rise to problems. Emotional dependence is difficult to assess, both in terms of its cogency and

28 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [135].
29 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [135].
30 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [23].
31 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [135].
32 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [25].
33 *Louth v Diprose* (1992) 175 CLR 621. See also *Truran v Cortorillo* [2011] VSC 488.
34 See also *Bridgewater v Leahy* [1998] HCA 66; (1998) 194 CLR 457, esp [115].
35 This case is considered in more detail at [36.80].

its potency. It is also difficult to assess how far a gift or contract is actually influenced by an emotional dependence as opposed to feelings of love, altruism or responsibility, which are qualities it might be thought do not justify legal intervention. In *MacKintosh v Johnson*,[36] a case also dealing with a gift given by an older man infatuated by a younger woman, Buchanan and Wheelan JJA and Hargrave AJA held that:

> Something more than mere infatuation and consequent foolish action based on clouded judgment was required to establish that the [plaintiff's] ability to make decisions in his own best interests was so seriously affected as to amount to a special disability or disadvantage.[37]

Moreover, it was not exploitation for the woman with whom the gift donor was infatuated to conceal her true feelings; this "was the stuff of ordinary human relationships".[38]

Pressure and manipulation of a relationship of dependence was evident in *Thorne v Kennedy*,[39] a case raising undue influence and discussed at [35.20]. The case concerned prenuptial and postnuptial financial agreements. The parties had met online on a website for potential brides and Thorne, a woman from eastern Europe, was induced by Kennedy, a wealthy and much older property developer, to come to Australia to be married. Just 10 days before the wedding and after her family had flown to Australia, Kennedy asked Thorne to sign a prenuptial agreement unfavourable to her interests. Thorne was given legal advice and this advice was not to sign the agreements. Thorne nonetheless signed the agreements after Kennedy advised the wedding would not proceed unless this happened. Slightly less than four years into the marriage, the parties separated. Thorne sought to set aside the prenuptial agreements. The High Court agreed with the trial judge that the agreements should be set aside because they were procured through undue influence and unconscionable conduct. Thorne was at a special disadvantage relative to Kennedy; she was powerless, with what she saw as no choice but to enter the agreements.[40] This special disadvantage was known to the respondent and had been, in part, created by him.[41] "He created the urgency with which the pre-nuptial agreement was required to be signed and the haste surrounding the post-nuptial agreement and the advice upon it."[42]

Inequality of bargaining power

[36.60] As discussed in the introduction to Part VII, the expression *inequality of bargaining power* refers to a disparity in information, experience, expertise and resources between parties to a contract. While a principle of relief based on inequality of bargaining power was proposed by Lord Denning in *Lloyds Bank v Bundy*,[43] this principle has not received general judicial support.[44] In *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty*

36 *MacKintosh v Johnson* [2013] VSCA 10.

37 *MacKintosh v Johnson* [2013] VSCA 10, [77].

38 *MacKintosh v Johnson* [2013] VSCA 10, [84]. See also *BOM v BOK* [2018] SGCA 83.

39 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85.

40 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [64] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

41 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [65] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ), [74] (Nettle J), [118]– [112] (Gordon J).

42 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [64] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

43 *Lloyds Bank v Bundy* [1975] QB 326, 339.

44 *National Westminster Bank v Morgan* [1985] 1 AC 686, 708.

Ltd,[45] the High Court dismissed the possibility of inequality of bargaining power amounting to a special disability for the purposes of relief against unconscionable dealing.[46] Gleeson CJ stated that:

> A person is not in a position of relevant disadvantage, constitutional, situational, or otherwise, simply because of inequality of bargaining power. Many, perhaps even most, contracts are made between parties of unequal bargaining power, and good conscience does not require parties to contractual negotiations to forfeit their advantages, or neglect their own interests.[47]

Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd concerned a lease by Mr and Mrs Roberts from a shopping centre of a shop from which the Roberts conducted a business. In 1990, a number of tenants at the shopping centre, including the Roberts, became concerned at some of the charges levied under the terms of their leases and brought legal action against the lessor. The Roberts estimated alleged overpayments of approximately $50,000 which they were interested in recovering from the owners.

The lease for the shop was due to expire on 14 February 1997. The Roberts had made it known to the manager of the shopping centre that they were anxious to sell their business and that if they could negotiate a new lease term, which they could then assign to the purchaser, that would assist them. As a condition of renewal of the lease, the lessor required the Roberts to consent to the dismissal of any current legal proceedings against the owners. The Roberts' solicitor advised against consenting to this proposal. However, the Roberts decided that they had little option but to agree and the business was eventually sold. It turned out that if the Roberts had participated in Supreme Court proceedings settled in November 1998, they would have been entitled to around $3000, much less than they expected.

In legal action against the lessors, the Australian Competition and Consumer Commission alleged that the lessor's conduct contravened s 51AA of the *Trade Practices Act 1974* (Cth). This claim was dismissed in the High Court by the majority of Gleeson CJ, Gummow, Hayne and Callinan JJ, Kirby J dissenting. Although an action under statute, the case was conducted on the basis that it fell within the well-established principles of unconscionable dealing.[48]

The majority accepted that lessees were in a difficult bargaining position. However, "there was neither a special disadvantage on the part of the lessees, nor unconscientious conduct on the part of the lessors".[49] The case merely concerned a situation where one party had a bargaining advantage which they used with the consequence that the other party was required to forego a financial interest. Gleeson CJ explained:

> all the people involved in the transaction were business people, concerned to advance or protect their own financial interests. The critical disadvantage from which the lessees suffered was that they had no legal entitlement to a renewal or extension of their lease; and they depended

45 *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd* [2003] HCA 18; (2003) 214 CLR 51.

46 References to unequal bargaining power are found in unconscionable contracts legislation: see further Chapter 38.

47 *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd* [2003] HCA 18; (2003) 214 CLR 51, [11]. See also *Rose v Sakkara Properties Pty Limited* [2009] FCA 304, 163; *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [65] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

48 *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd* [2003] HCA 18; (2003) 214 CLR 51, [17].

49 *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd* [2003] HCA 18; (2003) 214 CLR 51, [15], [57].

> upon the lessors' willingness to grant such an extension or renewal for their capacity to sell the goodwill of their business for a substantial price … They were at a distinct disadvantage, but there was nothing "special" about it … Good conscience did not require the lessors to permit the lessees to isolate the issue of the lease from the issue of the claims. It is an everyday occurrence in negotiations for settlement of legal disputes that, as a term of a settlement, one party will be required to abandon claims which may or may not be related to the principal matter in issue.[50]

KNOWLEDGE

[36.65] The second element of the doctrine of unconscionable dealing is that:

> the disability was sufficiently evident to [the defendant] to make it prima facie unfair or "unconscientious" that he procure, or accept, [the plaintiff's] assent to the impugned transaction in the circumstances in which he procured or accepted it.[51]

This requirement of *knowledge* is central to the doctrine of unconscionable dealing. It is the defendant's knowledge of the special disadvantage of the plaintiff and, in the face of this knowledge, the defendant's failure to take any steps to protect the interests of the plaintiff, which taints the conscience of the defendant so as to justify the courts setting aside the transaction.[52]

Knowledge and active and passive wrongdoing

[36.70] In many cases of unconscionable dealing, the defendant will *actively* have engaged in conduct that "is capable of clear moral or ethical criticism–cheating, trickery, extortion or plain dishonesty".[53] In these cases it will usually be patently apparent that the defendant knows of the special disability of the plaintiff. The jurisdiction to grant relief for unconscionable dealing has traditionally also arisen in cases of *passive* wrongdoing, where a defendant has proceeded with a transaction with a plaintiff operating under a position of special disadvantage and doing nothing to ensure that the interests of the vulnerable plaintiff are protected. In *Johnson v Smith*, Allsop P explained:

> what lies at the heart of the doctrine is that advantage is taken of the special disadvantage. This may occur because of the unconscientious use of power arising or existing in the circumstances or (as here) the unconscientious attempt to retain the benefit obtained from the person with the special disadvantage.[54]

Similarly Young JA said:

> There are situations where a person who has no active intention of doing another down may still be guilty of unconscientious conduct if he or she accepts "the benefit of an improvident bargain by an ignorant person acting without independent advice which cannot be shown to be fair".[55]

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50 *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd* [2003] HCA 18; (2003) 214 CLR 51, [15]–[16].

51 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 474.

52 See Bigwood, *Exploitative Contracts* (2003), p 249; Duggan, "Unconscientious Dealing" in Parkinson (ed), *The Principles of Equity* (2nd ed, 2003), pp 146–8.

53 *Johnson v Smith* [2010] NSWCA 306, [5].

54 *Johnson v Smith* [2010] NSWCA 306, [5].

55 *Johnson v Smith* [2010] NSWCA 306, [101], citing *Nichols v Jessup* [1986] 1 NZLR 226, 234. Also *Bridgewater v Leahy* [1998] HCA 66; 194 CLR 457.

In this second category of case it may not be clear that the defendant actually knew of the plaintiff's disadvantage and the question arises as to whether some form of constructive knowledge is sufficient

The degree of knowledge required in establishing unconscionable dealing

[36.75] The most straightforward way to satisfy the knowledge requirement is through *actual knowledge* by the defendant of the plaintiff's disability. *Wilful ignorance* – the defendant shutting his or her eyes to the obvious vulnerability of the plaintiff – will also be sufficient. In *Amadio*, Mason and Deane JJ both quoted with approval a statement that "wilful ignorance is not to be distinguished in its equitable consequences from knowledge".[56]

Constructive knowledge arises where the defendant is aware of facts which would lead a reasonable person to know of the vulnerable party's special disability. It appears that constructive knowledge – requiring only that the defendant ought reasonably to have known that the plaintiff was not in a position to look after his or her own interests – may be sufficient to establish unconscionable dealing, although this approach has been criticised by some commentators.[57] In *Amadio*, Mason J stated that it would be sufficient "if, instead of having actual knowledge of [the special disability], [the defendant] is aware of the possibility that that situation may exist or is aware of facts that would raise that possibility in the mind of any reasonable person".[58] This statement has been applied in a number of subsequent cases.[59]

However, in *Kakavas*, the High Court held that the knowledge element of unconscionable dealing required the stronger party to have actual knowledge, not constructive notice of the other party's position of special disadvantage in the transaction in question.[60] On the facts of the case, discussed at [36.35], the High Court found that, even if Kakavas did suffer from a special disability, Crown did not have the knowledge of this disadvantage required to taint its conduct in its dealings with Kakavas as unconscionable. The Court highlighted that Kakavas did not present himself as someone incapable of making worthwhile decisions for himself.[61] Kakavas appeared to be a successful businessman whose finances were in good shape,[62] and he appeared to be making his own choices about whether and where to gamble.[63] Crown knew Kakavas had suffered problems with gambling in the past but had subsequently been given a report by a psychologist to the effect that Kakavas was in control of his gambling.[64]

Kakavas argued that it would be sufficient if Crown had constructive notice, in the sense of being "aware of the possibility that [a] situation [of special disadvantage] may exist or [was]

56 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 467, 479, quoting *Owen and Gutch v Horman* (1853) 4 HL Cas 997, 1035; 10 ER 752.

57 See, eg, Duggan, "Unconscientious Dealing", in Parkinson (ed), *The Principles of Equity* (2nd ed, 2003).

58 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 467.

59 See, eg, *Lopwell Pty Ltd v Clarke* [2009] NSWCA 165, [54]–[56]; *Kenneth Charles Ward v Brian Charles* [2011] NSWSC 107, [33]; *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [38] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

60 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [150]–[162].

61 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [146].

62 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [31].

63 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [33].

64 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [143].

aware of facts that would raise that possibility in the mind of any reasonable person".[65] The High Court dismissed this approach. The Court stated that constructive notice was a doctrine that applied "to the resolution of disputes as to priority of [property] interests as between a legal interest and a prior competing equitable interest"[66] and was inapplicable to the scenario addressed by unconscionable conduct.

In the *Amadio* case itself there was no proof that the bank had actual knowledge of the special disability of the Amadios. However, the majority held that the special disability of the Amadios would have been evident to any reasonable person. Mason J explained that:

> Mr Virgo was aware that the respondents [the Amadios] were Italians, that they were of advanced years and that they did not have a good command of English. He knew that Vincenzo had procured their agreement to sign the mortgage guarantee. He had no reason to think that they had received advice and guidance from anyone but their son … Mr Virgo also knew that, in the light of the then financial condition of the company, it was vital to Vincenzo to secure his parents' signature to the mortgage guarantee so that the company could continue in business. It must have been obvious to Mr Virgo, as to anyone else having knowledge of the facts, that the transaction was improvident from the viewpoint of the respondents. In these circumstances it is inconceivable that the possibility did not occur to Mr Virgo that the respondents' entry into the transaction was due to their inability to make a judgment as to what was in their best interests, owing to their reliance on their son, whose interests would inevitably incline him to urge them to sign the instrument put forward by the bank.[67]

In *Kakavas*, the High Court saw no inconsistency between *Amadio* and their statement that constructive knowledge was insufficient to establish unconscionable dealing.[68] However, in *Thorne v Kennedy*, the High Court reaffirmed the approach in *Amadio* by defining unconscionable conduct to include circumstances of special disadvantage of which the defendant knew *or ought to have known*.[69]

Predatory state of mind?

[36.78] In addition to clarifying the type of knowledge on the part of the stronger party required for relief in equity for unconscionable dealing, the High Court in *Kakavas* indicated that there may be a further requirement of a "predatory state of mind". The Court stated that:

> Equitable intervention to deprive a party of the benefit of its bargain on the basis that it was procured by unfair exploitation of the weakness of the other party requires proof of a predatory state of mind.[70]

This statement suggests that not only must the stronger party know of the special disadvantage of the weaker party but also that the stronger party must have made some active decision to exploit that disadvantage for his or her conduct to be unconscionable in equity.[71] If such a

65 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [150]. See also *Australian Competition and Consumer Commission v Radio Rentals Ltd* (2005) 146 FCR 292, [21] (Finn J).

66 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [152].

67 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 466–7.

68 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [155].

69 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [38] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

70 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [161].

71 See *Bodapati & Anor v Westpac Banking Corporation* [2015] QCA 7, [75] (Peter Lyons J, Holmes and Gotterson JJA agreeing).

requirement does exist, it is inconsistent with earlier judicial statements recognising relief on grounds of unconscionable dealing may be given in response to the "active exhortation of a benefit" and also "the passive receipt of a benefit in unconscionable circumstances".[72] In cases of so-called "passive" exploitation, the stronger party may not have intended to act wrongfully by exploiting the special disability of the weaker party to the transaction. Instead the unconscionable dealing may be grounded in the stronger party's deliberate retention of a benefit in circumstances where, to the knowledge of the stronger party, the weaker party was in need of assistance to protect his or her own interests.[73]

For example, in *Amadio*, Deane J noted "in fairness" that "there is no suggestion that Mr Virgo [the bank's officer] or any other officer of the bank has been guilty of dishonesty or moral obliquity in the dealings between Mr and Mrs Amadio and the bank".[74] Rather the fault lay in the fact that he "simply closed his eyes to the vulnerability of Mr and Mrs Amadio and the disability which adversely affected them".[75] The High Court's statement that unconscionable conduct required proof of a predatory state of mind on the part of the stronger party was stated to apply in an "arm's length commercial transaction".[76] It is therefore possible that in different sorts of transactions, such as private sales or transactions between family or friends, it would not be necessary for a predatory state of mind to be shown in order for relief to be granted for conduct that is otherwise unconscionable under equity.

In *Thorne v Kennedy*[77] and again in *Australian Securities and Investments Commission v Kobelt*,[78] the High Court did not refer to any requirement of a predatory state of mind to establish unconscionable dealing in equity. Instead the Court described the doctrine as requiring "victimisation", "unconscientious conduct" or "exploitation".[79] This description is consistent with the *Amadio* doctrine and can accommodate both active and passive exploitation or advantage-taking.

REBUTTING THE PRESUMPTION

[36.80] Once it is established that a person is under a special disability, and that that disability is evident to the defendant, the defendant has the burden of proving that the transaction was fair, just and reasonable. In effect, this means there is a rebuttable presumption that the transaction is unfair. How then is that presumption rebutted?

72 *Hart v O'Connor* [1985] AC 1000, 1024; *Bridgewater v Leahy* (1998) 194 CLR 457, [76], quoting *Earl of Aylesford v Morris* (1873) LR 8 Ch App 484, 490–1. Also *Johnson v Smith* [2010] NSWCA 306, [5], [101]; *Aboody v Ryan* [2012] NSWCA 395, [65].

73 Bigwood, "Still Curbing Unconscionability: *Kakavas* in the High Court of Australia" (2013) 37 *Melbourne University Law Review* 463, 491.

74 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 478 (Deane J).

75 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 478 (Deane J).

76 *Kakavas v Crown Melbourne Ltd* [2013] HCA 25; (2013) 250 CLR 392, [161]. Compare *Humphreys v Humphreys* [2004] EWHC 2201 (Ch), [105]–[107] ("… the party benefiting from the transaction must have imposed the objectionable terms in a morally reprehensible manner").

77 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85.

78 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [15] (Kiefel CJ and Bell J), [118] (Keane J), [282] (Edelman J), also [81] (Gageler J) "exploitation" is sufficient, [258] (Nettle and Gordon JJ) affirming passive exploitation.

79 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85.

One obvious way of rebutting the presumption is to show that the terms of the transaction are fair. Proof of adequate consideration provided by the defendant will not necessarily be sufficient for this purpose. For example, in a contract of guarantee, the consideration moves from the creditor to the debtor, not to the guarantor. Even if the terms of a contract appear fair, they may be unfair *in the circumstances*. If the plaintiff was misled as to some significant feature of the contract and would not have entered the contract at all if properly informed, it can be said that that contract is unfair in the circumstances. In *Amadio*[80] it could be said the contract was unfair either because the Amadios obtained no benefit from the contract (the consideration moving from the bank to their son) or because they would never have entered that contract if they had been informed of its salient terms and the relevant circumstances surrounding it, such as the financial problems of their son's company.

Another way of attempting to rebut the presumption is to show that the victim was referred to an independent adviser. We have already seen how a presumption of undue influence may be rebutted in this way. In the present context, referral to an independent adviser would not prove that the contract was fair, but it might prove that the defendant did not take advantage of the plaintiff, at least if the defendant reasonably believed the advice would be adequate. Partial advice or advice given by the defendant's solicitor will not be sufficient.

In *Aboody v Ryan*[81] Mr Ryan, an elderly man on a veteran's disability pension, lived in a home owned by him. One daughter had spent time and effort caring for and assisting Mr Ryan, while he had fallen out with his other children. Mr Ryan was fond of this daughter. He also held an irrational fear that, should the Labor Party win the 2007 election, they would take his pension and his home. As a result, Mr Ryan transferred the interest in his home to the daughter and her husband, the Aboodys, by way of gift. At the time, the Aboodys attempted to obtain legal advice for Mr Ryan. Two years later, Mr Ryan changed his mind and commenced proceedings to set aside the gift. The NSW Court of Appeal upheld the decision of the trial judge setting aside the transaction on grounds of unconscionable dealing in equity. Allsop P (Bathurst CJ and Campbell JA agreeing) explained that the Aboodys knew about the characteristics of Mr Ryan that left him vulnerable in the transaction and the gift would leave him financially exposed to their charity or the support of the state.[82] Accepting and retaining the improvident gift in these circumstances was to take advantage of the known weakness and amounted to unconscionable dealing. The presence of legal advice was not sufficient to ensure that the transaction was fair, just and reasonable.[83] The solicitor giving the advice was not independent; he was the Aboodys' solicitor. He did not know of Mr Ryan's irrational motive for the transaction.[84] His advice did not extend to the financial consequences of the transaction, which were of crucial importance to an elderly man.[85]

Even independent legal advice will not be sufficient to relieve the impact of unconscionable conduct if the circumstances make it apparent that the plaintiff remained unable to exercise independent judgment. For example, in *Thorne v Kennedy*,[86] discussed at [35.20], a solicitor's

80 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447.

81 *Aboody v Ryan* [2012] NSWCA 395.

82 *Aboody v Ryan* [2012] NSWCA 395, [68].

83 *Aboody v Ryan* [2012] NSWCA 395, [68]–[69].

84 *Aboody v Ryan* [2012] NSWCA 395, [68].

85 *Aboody v Ryan* [2012] NSWCA 395, [78].

86 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85.

advice given before the prenuptial agreements were signed did not protect the agreements from being set aside on grounds of Kennedy's undue influence and unconscionable conduct. Gordon J explained that:

> The fact that Ms Thorne was willing to sign both agreements despite being advised that they were "terrible" serves to underscore the extent of the special disadvantage under which Ms Thorne laboured, and to reinforce the conclusion that in these circumstances, which Mr Kennedy had substantially created, it was unconscientious for Mr Kennedy to procure or accept her assent.[87]

RELIEF

[36.85] The relief available to victims of unconscionable dealing is the same as that available to victims of duress or undue influence. The contract may be rescinded, provided there are no bars to rescission.[88] If the defendant seeks specific performance of the contract, this will be denied.

UNCONSCIONABLE DEALING AND UNDUE INFLUENCE COMPARED

[36.90] We have seen that relief from the consequences of unconscionable dealing is relief from exploitation or victimisation. Courts hold that a stronger person should not be allowed to take advantage of a weaker one. By contrast, undue influence looks to the degree to which the plaintiff freely consented to the transaction. However, the same set of facts can give rise to the application of both doctrines. It could be said of the son in *Amadio*,[89] for example, that he influenced his parents them unduly and the bank had notice of this conduct.

In *Bridgewater v Leahy*,[90] Gaudron, Gummow and Kirby JJ explained the distinction between the doctrines in the following terms:

> each doctrine may be seen as a species of that genus of equitable intervention to refuse enforcement of or to set aside transactions which if allowed to stand, would offend equity and good conscience. However, there are conceptual and practical distinctions between them …

At the practical level, as we have seen, a special relationship of influence gives rise to a *presumption* that undue influence was exercised by the defendant and this presumption, which must be rebutted by the defendant, confers a forensic advantage on the plaintiff.[91] In an unconscionable dealing case, on the other hand, the plaintiff, in the absence of a relationship of influence, must prove the existence of exploitation on an ad hoc basis, that is, at the time of the particular transaction. Even in such a case, however, the plaintiff may be assisted by an evidentiary inference. In *Louth v Diprose*,[92] a case involving a substantial gift, Brennan J said, "[o]nce it is proved that substantial property has been given by a donor to a donee after the donee has exploited the donor's known position of special disadvantage, an inference may be drawn that the gift is the product of the exploitation." Nevertheless, if exploitation is proved,

87 *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [123].

88 For a detailed discussion of rescission, see Chapter 39.

89 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447.

90 *Bridgewater v Leahy* [1998] HCA 66; (1998) 194 CLR 457, 478 [73].

91 *Bridgewater v Leahy* [1998] HCA 66; (1998) 194 CLR 457, 478 [73].

92 *Louth v Diprose* (1992) 175 CLR 621, 632.

as seems to be indicated here, this may well be evidence of a relationship of influence which would give rise to a presumption of undue influence.

At the conceptual level, Deane J, after pointing out that the two doctrines are closely related, drew the following distinction between them:

> Undue influence, like common law duress, looks to the quality of the consent or assent of the plaintiff … Unconscientious dealing looks to the conduct of the defendant in attempting to enforce or retain the benefit of a dealing with a person under a special disability in circumstances where it is not consistent with equity or good conscience that he should do so.[93]

However, this distinction is, from one perspective, merely one of emphasis. On the one hand, the impaired consent in undue influence cases must be induced by wrongful conduct (*undue* influence). On the other hand, exploitation in unconscionable dealing cases will leave the victim's consent impaired.[94]

Should the two doctrines be merged? In *Australian Competition and Consumer Commission v Berbatis Holdings Pty Ltd (No 2)*,[95] French J said that "it is only a small step to classify both under the rubric of unconscionable conduct". There is certainly an argument that at least actual (as distinct from presumed) undue influence should be merged with unconscionable dealing. There does not seem to be any substantial difference between the two doctrines. If the latter doctrine is the broader of the two, the former could be subsumed under it. However, presumed undue influence, with its recognition of a relationship of influence, and the presumption that attends that relationship, should probably be kept separate.[96]

EQUITY'S USE OF ARCHETYPES

[36.95] The doctrine of unconscionable dealing is one which, as we have seen, aims at providing relief for people who, by virtue of a special disability, are vulnerable to, and in fact succumb to, exploitation. The list of potential victims and methods of exploitation is open-ended and cannot be conclusively catalogued. A court clearly must consider all the relevant facts of the particular case to determine issues of both "special disability" and "knowledge". In this context, however, a question arises as to how far archetypes may be invoked by a court to assist in the decision process. In our study of presumed relationships of influence in Chapter 35, we saw the express employment of archetypes in equity. For example, a child is presumed to be vulnerable to the influence of a parent, a religious disciple vulnerable to the influence of a religious leader.[97] These presumptions are beneficial, but there are dangers in the employment of archetypes. Unless due care is taken, reliance on an archetype may result in an inequitable outcome. First, the *validity* of the archetype may be wrongly taken for granted. Secondly, the archetype may be *subconsciously* adopted and not brought out in the open for critical scrutiny.

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93 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, 474, see also 461 (Mason J); *Thorne v Kennedy* [2017] HCA 49; (2017) 263 CLR 85, [40] (Kiefel CJ, Bell, Gageler, Keane and Edelman JJ).

94 See further Bigwood, "Undue Influence: 'Impaired Consent' or 'Wicked Exploitation'" (1996) 16 *Oxford Journal of Legal Studies* 504.

95 *Australian Competition and Consumer Commission v Berbatis Holdings Pty Ltd (No 2)* [2000] FCA 2; (2000) 96 FCR 491, 499 [15].

96 For a contrary argument, see Capper, "Undue Influence and Unconscionability: A Rationalisation" (1998) 114 *Law Quarterly Review* 479.

97 See Chapter 35.

A case in which, it has been argued, archetypes loomed large is *Louth v Diprose*.[98] This case, as we have seen, is authority for the proposition that emotional dependence in the form of infatuation may be a special disability and render the victim of it vulnerable to unconscientious exploitation. As the notion of "emotional dependence" between adults is quite mercurial, the use of archetypes to fill it out is tempting. Some commentators have argued cogently that in *Louth v Diprose*, the judges, wittingly or unwittingly, succumbed to this temptation to ill effect.[99]

Louis Diprose was a solicitor and Mary Louth a single mother with two children. They developed a relationship in Tasmania. When Louth went to Adelaide to live with her sister, Diprose followed her, even though she had said she could no longer go out with him. He sent her love poems and they began to see each other again. He gave her many gifts and eventually bought a property in her name. Later, he claimed that the last-mentioned gift was not absolute as it was intended that the property should be retransferred to him. He further argued that Louth had manipulated his infatuation for her, by deliberately manufacturing an atmosphere of crisis concerning her housing situation and by threatening suicide. Louth denied these allegations.

The trial judge, King CJ, although he did not believe Diprose's submission that the gift was not absolute, generally preferred his version of events and found in his favour. He found that Diprose was an utterly vulnerable person by reason of infatuation and was the victim of manipulation by Louth. On appeal to the Full Court, a majority upheld this ruling. On appeal to the High Court, a majority again upheld the ruling. Only one judge, Toohey J, dissented. He observed that the trial judge's use of colourful expressions such as "pathetic devotion" and "unrequited love" did not give a balanced picture of the parties' relationship, which was not one of complete emotional dependence. Diprose understood the unbalanced terms of the relationship and his dependence and improvidence were in fact self-induced. The evidence, Toohey J considered, did not support the conclusion that Louth had manufactured an atmosphere of crisis.

The case has been widely criticised. Heerey J, for example, assessed it as follows:

> The Mary-Louis transaction might be seen as no more than the private and domestic equivalent of a commercial and hard bargain where the better positioned bargainer came out on top. Louis' infatuation was a self-inflicted weakness and Mary took advantage of it. That might have been unfair, but the world is not always fair. Mary's conduct did not pass over the ill-defined border into that specially reprehensible and repellent unfairness which lawyers call unconscionability–something that shocks the conscience.[100]

The judges who found for Diprose seem to be implicitly adopting highly questionable archetypes. Louth is portrayed as a scheming temptress determined to grasp all that she can, while Diprose appears as a susceptible but generous male – a variant of the knight in shining armour. An educated male solicitor would not normally behave as Diprose did, according to the judges in the majority, so he must have been emotionally dependent and the innocent

98 *Louth v Diprose* (1992) 175 CLR 621.

99 See Hepburn, "Equity and Infatuation" (1993) 18 *Alternative Law Journal* 208; Haigh and Hepburn, "The Bank Manager Always Rings Twice: Stereotyping in Equity after Garcia" (2000) 26 *Monash University Law Review* 275, 300–1; Otto, "A Barren Future? Equity's Conscience and Women's Inequality" (1992) 18 *Melbourne University Law Review* 808, 823–5.

100 *Mulcahy v Hydro-Electric Commission* (1998) 85 FCR 170, 244.

victim of female exploitation. This view of the facts overlooks the influence that Diprose had over Louth, by virtue of his superior wealth and higher education. Louth was a single mother on a security pension, with no significant assets.

In a perceptive article, Lisa Sarmas has shown how the narratives adopted by the judges in this case reflect and reinforce dominant ideas, and stock stories, about gender and class.[101] She demonstrates that even the minority judges in the case make archetypical assumptions. Louth appears now not as an undeserving temptress, but as a pitiful victim (a damsel in distress) who should be able to keep the house given to her by a benign romantic suitor, even though she has done nothing to deserve it. Diprose was a grown professional man who should have known better. This account, like the majority accounts, is an official court story. But Sarmas points to another possible story – an unofficial one, hinted at in the transcripts. In this account, we are introduced to the idea that Louth might have experienced what the judges described as Diprose's romantic "infatuation" with her as sexual harassment, especially in the context of her past history of rape. But this is outside the court-sanctioned account according to which "women are either victims or conniving, manipulative, dangerous; advances by men who are sexually interested are romantic, they are not sexual harassment; social class does not exist; structural power based on gender does not exist".[102]

Progressive legal change requires that the unofficial or counter story be told and that the official narratives be challenged. But this presents a dilemma. It is not just that the court may not hear or understand the challenge, but also that as a strategy for winning a case it may be counter-productive. After all, Louth wanted to keep the property and she might have had a better chance of success as "a damsel in distress" than as a person who challenged a whole range of deep and disturbing prejudices.

101 Sarmas, "Storytelling and the Law: A Case Study of Louth v Diprose" (1994) 19 *Melbourne University Law Review* 701.

102 Sarmas, "Storytelling and the Law: A Case Study of Louth v Diprose" (1994) 19 *Melbourne University Law Review* 701, 722.

CHAPTER **37**

Impropriety by third parties

THREE-PARTY SITUATIONS

[37.05] Typically, a party (the *plaintiff*) who is seeking to be released from a contract on grounds of a vitiating factor, such as misrepresentation, duress, undue influence or unconscionable dealing, is seeking relief as against the party whose conduct gave rise to the circumstances supporting relief. This chapter is concerned with the category of cases where the plaintiff is seeking to have a contract set aside as against the other party to the contract (the *defendant*) on the basis of improper conduct by a person who is not a party to the contract (a *third party*).

The most common instance of this sort of claim arises where the plaintiff enters into a guarantee with a lender of a third party's debt. For example, the third party may need a loan from a lender, but the lender may require another person to guarantee repayment of the loan. The borrower may coerce the plaintiff into signing a contract of guarantee with the bank. The question may then arise as to whether the plaintiff can have the contract with the lender set aside on the basis of the borrower's duress or undue influence. Another variation concerns a loan taken out by the plaintiff to benefit a third person, typically a family member. Can the plaintiff seek to have the loan from the lender set aside on the basis of undue influence or other impropriety on the part of the family member benefiting from the loan?[1]

Possible grounds for relief

[37.10] For a plaintiff to have a contract with the defendant set aside on grounds of impropriety by a third person who is not a party to the contract, there must be some basis for showing that the defendant was in some way tainted by the improper conduct. There are five possible types of claim:

1. agency;
2. unconscionable dealing;

1 On these issues see further Paterson, "Knowledge and Neglect in Asset Based Lending: When is it Unconscionable or Unjust to Lend to a Borrower who cannot Repay" (2009) 20 *Journal of Banking and Finance Law and Practice* 1.

3. notice of undue influence;
4. in Australia, a special rule arising from the decision in *Yerkey v Jones*, also sometimes referred to as the *wives' special equity*; and
5. under statute, as discussed in Chapter 38.

AGENCY

[37.15] A defendant may rely on a third party to obtain the plaintiff's agreement to the transaction. An agent is a person who is authorised to act on behalf of a principal and can bind that principal when acting within authority. In such circumstances, the defendant may suffer the consequences of any relevant impropriety in the methods used by the third party if the third party was acting as the defendant's *agent* in obtaining the plaintiff's agreement.

In the case of third party guarantees, if the lender is held to have appointed the borrower to act as the defendant's agent for obtaining the consent of the guarantor to give a guarantee for the borrower's loan, then the guarantee may be set aside on the basis of wrong-doing by the borrower as agent for the lender. In the context of third-party guarantees, it has been said that the relationship of principal and agent between a lender and a debtor is not likely to be common.[2]

The issue of agency might also arise in transactions where a mortgage or loan is procured through a financial adviser or broker. The lender may have no direct dealings with the borrower and hence no knowledge of the circumstances under which the loan was made. By contrast, the broker may know of a special disability on the part of the borrowers which has been exploited by a third party or even have exploited the borrower's position of vulnerability itself. If the broker is the agent of the lender, the knowledge of the agent will be attributed to the lender. The loan may then be set aside on the basis that the lender is tainted by the misconduct used to obtain the borrower's consent to the loan. Courts have consistently held that a broker is the agent of the borrower not the lender.[3] Nonetheless, agency is a factual inquiry and hence it is possible that the facts of a particular case might establish an agency relationship between broker and lender.[4]

UNCONSCIONABLE DEALING

[37.20] In Australia, one of the most common grounds under which a plaintiff may challenge a contract entered into as a result of some third party impropriety is unconscionable dealing. As discussed in Chapter 36, to establish unconscionable dealing, the plaintiff must be under a special disadvantage and the defendant must have knowledge of that fact. One of the leading modern applications of the doctrine of unconscionable dealing, *Commercial Bank of Australia*

2 See *Barclays Bank plc v O'Brien* [1994] 1 AC 180, 195 (Lord Browne-Wilkinson).

3 See, eg, *Esanda Finance Corporation Ltd v Spence Financial Group Pty Ltd & Ors* [2006] WASC 177; *Perpetual Trustees Victoria Ltd v Ford* [2008] NSWSC 29; (2008) 70 NSWLR 611; *Perpetual Trustees Australia Ltd v Schmidt & Anor* [2010] VSC 67, [131] (Forrest J). Also *Morlend Finance Corporation (Vic) Pty Ltd v Westendorp* [1993] 2 VR 284; *Custom Credit Corporation Ltd v Lynch* [1993] 2 VR 469. By contrast, a mortgage aggregator has been found to be an agent of the lenders for which it acts: see, eg, *Permanent Mortgages Pty Ltd v Vandenbergh* [2010] WASC 10, [319] (Murphy J).

4 See, *Permanent Trustee Company Limited v O'Donnell* [2009] NSWSC 902, [359] (Price J); *David Benson Nominees Pty Ltd v Dicksons Ltd & Anor* [2005] SASC 97.

Ltd v Amadio,[5] arose in a situation where the plaintiffs, Mr and Mrs Amadio, had given a guarantee after being misled by their son, Vincenzo. The case might have been dealt with on the basis of undue influence by the son over his parents, the Amadios. However, it was pleaded as, and set aside on, the grounds of unconscionable dealing.

The difficulty in these sorts of cases will often be in showing that the defendant knew or ought to have known of the plaintiff's position of special disadvantage. For example, loan and mortgage contracts may be facilitated through a broker, rather than the lender itself. In such a scenario, the lender/defendant may have had no direct dealings with the borrower and hence no knowledge of the borrower's disability. In *Perpetual Trustees Victoria Limited v Ford*,[6] the borrower, Ford, suffered from a congenital intellectual impairment and was illiterate. Ford owned a house which had been inherited from his mother. In 2004, Ford entered into a loan agreement for $200,000 secured by a mortgage over the house. At the time of the transaction, Ford received a Disability Pension of $452.70 per fortnight. He had no capacity from his income or other resources to pay the interest on a loan of $200,000. The loan was arranged by Ford's son with whom Ford had, until recently, been estranged. The purpose of the loan was to purchase a cleaning business to be operated by the son. The business was purchased in Ford's name although he did not plan to operate the business and did not have the skills to do so. Ford did not receive any legal advice. Within 12 months of the date of the transaction, Ford had defaulted on his obligations to the lender and the lender sought to recover the principal sum and take possession of Ford's house.

In the Supreme Court of New South Wales, Harrison J held that the lender did not have knowledge of the borrower's disability for the purposes of the equitable doctrines of undue influence or unconscionable dealing. Ford's disability was so significant that the loan was found to be void on the ground of non est factum.[7]

NOTICE OF UNDUE INFLUENCE

[37.25] As discussed in Chapter 35, undue influence is concerned with a relationship of influence that affected the plaintiff's judgment in entering the contract.[8] A defendant will be tainted by a transaction involving undue influence between the plaintiff and a third party where the defendant had actual or constructive notice of that influence.[9] The defendant will have constructive notice where the defendant knows facts sufficient to put it on inquiry as to the possibility of undue influence between the plaintiff and the third party, but it fails to inquire.

In *Bank of New South Wales v Rogers*[10] a niece whose uncle's financial affairs were out of control charged all her property to a bank as security for her uncle's overdraft. The relationship between the uncle and niece, who resided together, was one of influence by the uncle over the niece. This relationship gave rise to a presumption that the uncle had influenced his niece in

5 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447, discussed at [36.20].

6 *Perpetual Trustees Victoria Limited v Ford* [2008] NSWSC 29; (2008) 70 NSWLR 611, appeal on a different point allowed in *Ford by his Tutor Beatrice Ann Watkinson v Perpetual Trustees Victoria Limited* [2009] NSWCA 186; (2009) 75 NSWLR 42.

7 See further discussion of the consequences of the contract being void, at [10.15].

8 See further Duggan, "Undue Influence" in Parkinson, *The Principles of Equity* (2nd ed, 2003); Bigwood, "Undue Influence in the House of Lords: Principles and Proof" (2002) 65 *Modern Law Review* 435.

9 See, eg, *Bank of New South Wales v Rogers* [1941] HCA 9; (1941) 65 CLR 42. See also *Verduci & Anor v Golotta* [2010] NSWSC 506; *Permanent Mortgages Pty Ltd v Vandenbergh* [2010] WASC 10, [180] (Murphy J).

10 *Bank of New South Wales v Rogers* [1941] HCA 9; (1941) 65 CLR 42.

the transaction. As the bank manager knew of the special relationship between the uncle and niece, there was an onus on the bank to rebut the presumption by proving that the charge was executed by the niece in a free and informed way. As the bank failed to discharge this onus, the charge was set aside.

The English approach to protecting non-commercial guarantors

[37.30] In England, the House of Lords has adopted a low threshold for the circumstances which will give rise to notice in third-party impropriety cases involving guarantees. In *Royal Bank of Scotland v Etridge (No 2)*[11] Lord Nicholls held that a lender was *put on inquiry* as to the risk of undue influence whenever a wife offered to guarantee her husband's debts or the debts of a company in which they both had a shareholding. Lord Nicholls held that a lender will also be put on inquiry in cases where the relationship between the borrower and the guarantor is one where the law presumes a relationship of trust and confidence (ie, a relationship of influence for the purposes of undue influence) and indeed in every case where the relationship between the parties is not "commercial".[12] A lender put on inquiry will be required to take steps to reduce the risk of the guarantor entering into the transaction under a misrepresentation or as a result of undue influence. If these steps are not taken, the bank will be deemed to have notice that the transaction was procured by undue influence or misrepresentation on the part of the borrower and the guarantee may be set aside.[13] This principle has not been adopted in Australia.[14]

YERKEY V JONES

The rule in *Yerkey v Jones*

[37.35] In 1939, in Australia, a unique two pronged rule responding to third party impropriety was recognised by the High Court in *Yerkey v Jones*.[15] This rule, sometimes known as the *wives' special equity*, provides protection for a wife who enters into a guarantee for her husband's debts without herself gaining any direct benefit from the transaction and where, either, the wife's entry into the guarantee was procured by the undue influence of her husband or, alternatively, the wife lacked understanding of the transaction. The rule in *Yerkey v Jones* was enunciated by Dixon J as follows:

> Although the relation of husband to wife is not one of influence, yet the opportunities it gives are such that if the husband procures his wife to become surety for his debt a creditor who accepts her suretyship obtained through her husband has been treated as taking it subject to any invalidating conduct on the part of her husband even if the creditor be not actually privy to such conduct.[16]
>
> …
>
> If a married woman's consent to become a surety of her husband's debts is procured by the husband and, without understanding its effect in essential respects, she executes an instrument

11 *Royal Bank of Scotland v Etridge (No 2)* [2001] UKHL 44; [2002] 2 AC 773, [44] (Lord Nicholls (Lord Bingham and Lord Clyde concurring)).

12 *Royal Bank of Scotland v Etridge (No 2)* [2001] UKHL 44; [2002] 2 AC 773, [86]–[87] (Lord Nicholls).

13 *Royal Bank of Scotland v Etridge (No 2)* [2001] UKHL 44; [2002] 2 AC 773, [87] (Lord Nicholls).

14 *Kranz & Anor v National Australia Bank Ltd* [2003] VSCA 92; (2003) 8 VR 310, [24], [31] (Charles JA).

15 *Yerkey v Jones* [1939] HCA 3; (1940) 63 CLR 649, 683 (Dixon J).

16 *Yerkey v Jones* [1939] HCA 3; (1940) 63 CLR 649, 678.

> of suretyship which the creditor accepts without dealing with her personally, she has a prima facie right to have it set aside.[17]

The effect of the rule was that to avoid having a guarantee given by a wife impeached, a lender would be obliged to take steps to ensure that it has reasonable grounds for believing that the consent of the guarantor was fairly obtained and that that consent, with the benefit of independent advice, was adequately informed.[18]

The rule in *Yerkey v Jones* had been criticised, and for some time, there was uncertainty about its status in Australian law.[19] However, the rule was re-affirmed by the High Court in *Garcia v National Australia Bank Ltd*[20] and has subsequently been expanded to cover other kinds of relationships.

Modern application: *Garcia v National Australia Bank Ltd*

[37.40] In 1979, Mrs Garcia (the plaintiff) and her husband signed a mortgage over their jointly owned matrimonial home in favour of the bank in order to secure loans made to them both. The mortgage secured all moneys which the Garcias might owe the bank, including money owing under future guarantees. The loans were repaid, but the mortgage was not discharged. In 1987, the plaintiff signed a guarantee in favour of the bank in respect of advances of $270,000 to a company controlled by her husband in operating his business as a foreign exchange dealer. The guarantee was signed in the presence of a bank officer. In 1990, the Garcias were divorced and the husband's interest in the property was transferred to the plaintiff subject to the mortgage. The plaintiff sought to have the guarantee set aside:

1. on the basis of *Commercial Bank of Australia Ltd v Amadio*[21] (unconscionable dealing); and
2. on the basis of the principles in *Yerkey v Jones*.[22]

The trial judge held that she could not succeed on the basis of *Commercial Bank of Australia Ltd v Amadio*, because, even if the husband had behaved unconscionably towards his wife, the bank did not know about it. But she did succeed on the basis of *Yerkey v Jones*. In the NSW Court of Appeal, the judges held that *Yerkey v Jones* no longer stated the law in Australia in cases of this kind. The relevant tests were now to be found in *Commercial Bank of Australia Ltd v Amadio*, and on the basis of those tests, the plaintiff failed.

The plaintiff finally succeeded in the High Court, where the majority of judges reaffirmed *Yerkey v Jones*. Under the principles in that case she could succeed because she did not understand that the guarantee was secured by the "all moneys" mortgage and she mistakenly believed her husband's claim that it was a guarantee of limited overdraft accommodation to be applied only in the purchase of gold bullion. She thought the transaction was "risk-proof" because there would be either "gold or money". Further, she was a volunteer. Although she was a director of and shareholder in the company controlled by her husband, she had no

17 *Yerkey v Jones* [1939] HCA 3; (1940) 63 CLR 649, 683.

18 See Duggan, "Undue Influence" in Parkinson, *Principles of Equity* (2nd ed, 2003), pp 422–4.

19 See *National Australia Bank Ltd v Garcia* (1996) 39 NSWLR 577.

20 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395, [31] (Gaudron, McHugh, Gummow and Hayne JJ).

21 *Commercial Bank of Australia Ltd v Amadio* [1983] HCA 14; (1983) 151 CLR 447.

22 *Yerkey v Jones* [1939] HCA 3; (1940) 63 CLR 649.

financial interest in the fortunes of that company and obtained no real benefit from entering the contract of guarantee.

The majority view in the High Court, as expressed in the joint judgment of Gaudron, McHugh, Gummow and Hayne JJ, was that the principles spoken by Dixon J in *Yerkey v Jones* were simply particular applications of accepted equitable principles which had as much relevance today as when uttered. It was not to the point that the role of women in Australian society had changed (although a significant number of women were in fact still in relationships marked by disparities of economic and other power), as the basis of the principles was the bond of trust and confidence between married partners.[23]

In a separate judgment, Callinan J upheld the *Yerkey v Jones* principles on the basis that, despite apparent changes in matrimonial relationships, many married women were still in need of the protection which the principle offered.

Kirby J considered that the *Yerkey v Jones* principles were outmoded.[24] Kirby J regarded the broader doctrines of equity expounded in *Commercial Bank of Australia Ltd v Amadio* as insufficiently meeting the particular problem of sureties who are emotionally vulnerable or dependent on the debtor. The *Amadio* case was not intended to cover the whole field of unconscionable conduct. The same set of facts could give rise to two types of liability in a lender: one deriving from the lender's own wrongful conduct (*Commercial Bank of Australia Ltd v Amadio*) and one deriving from the lender's notice of someone else's wrongful conduct. Kirby J was prepared to adopt a generous concept of when a lender will have notice of impropriety by the borrower in respect to the guarantor, similar to that adopted in England and discussed earlier in this chapter.[25]

Under Kirby J's formulation, the plaintiff still succeeded. She was the victim of misrepresentation by her husband, and the bank, which had constructive notice of her potential vulnerability, failed to take reasonable steps to satisfy itself that she entered her obligations freely and with knowledge of the relevant facts. Kirby J recognised that the principle he favoured would add a marginal cost to financial transactions and deprive some family businesses of the provision of capital. However, he considered that if the principle improved the quality of decisions of great importance to individuals, discouraged improvident risk taking and diminished litigious challenges, then the cost was well justified.[26]

The two limbs of *Yerkey v Jones*

[37.45] *Yerkey v Jones*, as affirmed in *Garcia v National Australia Bank Ltd*, identifies two bases for relief in transactions where a wife guarantees the debts of her husband. Under the first limb of the *Yerkey v Jones* principles, if the wife's consent is procured by the husband's undue influence, the wife will be entitled as against the lender to have the mortgage or guarantee set aside unless the lender can show that she received independent advice.[27] The reason for

23 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395, 403–4 (Gaudron, McHugh, Gummow and Hayne JJ).

24 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395, [66] (Kirby J).

25 See [37.30].

26 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395, 434 (Kirby).

27 *Yerkey v Jones* [1939] HCA 3; (1940) 63 CLR 649, 678 (Dixon J); Duggan, "Undue Influence" in Parkinson, *Principles of Equity* (2nd ed, 2003), p 420.

granting relief in these circumstances is that "to enforce that voluntary transaction against her when in fact she did not bring a free will to its execution would be unconscionable".[28]

Under the second limb of the principles in *Yerkey v Jones* if the wife fails to understand the effect of the document and the significance of giving a guarantee, she may be entitled as against the lender to have the transaction set aside unless the lender took steps to inform her about the transaction and reasonably supposed she understood.[29] In these circumstances, it would be unconscionable for the lender to enforce the guarantee:

> if the lender took no steps itself to explain the purport and effect to her or did not reasonably believe that its purport and effect had been explained to her by a competent, independent and disinterested stranger.[30]
>
> The bank carries the obligation of ensuring that the explanation as to the nature and effect of the transaction was adequate.[31]

Scope of the *Yerkey v Jones* principles

Limitation to volunteers

[37.50] The principles in *Yerkey v Jones* only apply if the wife is a "volunteer". A wife will be a volunteer if she does not benefit from the transaction, even though the transaction confers an important advantage on the husband or the company of the husband. To exclude a wife from the category of volunteer, in the sense discussed in *Garcia*, her gain from the transaction must be direct or immediate.[32] The possibility of some modest or speculative benefit is not sufficient.[33]

In *Garcia v National Australia Bank Ltd*,[34] the plaintiff was a director of and shareholder in the company controlled by her husband. The plaintiff was nonetheless a volunteer because she had no financial interest in the fortunes of that company and obtained no real benefit from entering the contract of guarantee.

Application to other relationships

[37.55] In *Garcia v National Australia Bank Ltd*,[35] the High Court left open the possible future application of the principles in *Yerkey v Jones*[36] to other long-term and publicly declared relationships short of marriage, between members of the same or opposite sex.[37] Different views have subsequently been expressed about the potential scope of the principles,

28 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395, 408 (Gaudron, McHugh, Gummow and Hayne JJ).

29 *Yerkey v Jones* [1939] HCA 3; (1940) 63 CLR 649, 683 (Dixon J); Duggan, "Undue Influence" in Parkinson, *Principles of Equity* (2nd ed, 2003), p 420.

30 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395, 408–9 (Gaudron, McHugh, Gummow and Hayne JJ).

31 *Schultz v Bank of Queensland* [2015] QCA 208, [40] (Boddice J).

32 *Cranfield Pty Ltd v Commonwealth Bank of Australia* [1998] VSC 140; *State Bank of New South Wales v Chia* [2000] NSWSC 552; (2000) 50 NSWLR 587.

33 *Agripay Pty Limited v Byrne* [2011] QCA 85; [2011] 2 Qd R 501, [11] (McMurdo P).

34 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395.

35 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395.

36 *Yerkey v Jones* [1939] HCA 3; (1940) 63 CLR 649.

37 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395, [22] (Gaudron, McHugh, Gummow and Hayne JJ).

which remains uncertain. Some courts initially took a restrictive view of the scope of the principles, holding them not even to apply to de facto couples.[38] However, this view seems to be changing. In *Agripay Pty Limited v Byrne*, McMurdo P said that:

> There seems to be no sound reason why these principles should be limited to wives entering into guarantees of their husbands' liabilities. Human weaknesses and unconscionable conduct are not limited to heterosexual marriage relationships. These legal principles should apply equally to all vulnerable parties in personal relationships.[39]

In *Kranz & Anor v National Australia Bank Ltd*, the Court of Appeal of the Supreme Court of Victoria held that the principles would apply where the lender was aware of a relationship of "trust and confidence" between the guarantor and the borrower.[40]

The broad application of the principles in *Yerkey v Jones* suggested in these statements has typically not been accepted by other courts. *Yerkey v Jones* has been applied to defacto partners.[41] Different views have been expressed about its application to elderly parents who guarantee the debts of a child. Some courts have rejected the extension.[42] In *Permanent Mortgages Pty Ltd v Vandenbergh*,[43] Murphy J said that he:

> would not see the burden of current authority as supporting an extension of the *Garcia* principles enunciated in the High Court by treating the relationship of aged parent/child as, in itself, synonymous with the husband/wife relationship for the purposes of the application of those principles.[44]

This view was based on the common desire of parents to assist their children, which should not be the subject of legal scrutiny without evidence of other factors to support a relationship of undue influence.[45] Nonetheless, subsequent courts have been open to the application of the principles in *Yerkey v Jones* to parent-child relationships.[46] There is some indication that courts would apply the principles to protect a husband guaranteeing his wife's debt.[47]

Application to other types of transaction

[37.58] In *Elkofairi v Permanent Trustee Co Ltd*, Santow JA, with whom Campell JA agreed, concluded that it was not permissible for an intermediate court of appeal to treat *Yerkey*

38 *State Bank of New South Wales Ltd v Hibbert* (2000) 9 BPR 17,543 [60] (Bryson J); *Hillston v Bar-Mordecai* [2003] NSWSC 89 [45]–[46] (Bryson J) (result reversed in part on other grounds: *Bar-Mordecai v Hillston* [2004] NSWCA 65).

39 *Agripay Pty Limited v Byrne* [2011] QCA 85; [2011] 2 Qd R 501, [4].

40 *Kranz & Anor v National Australia Bank Ltd* [2003] VSCA 92; (2003) 8 VR 310, [24]–[31] (Charles JA). See also *ANZ Banking Group Ltd v Alirezai*; *Alirezai v ANZ Banking Group Ltd* [2004] QCA 6, [115] (McMurdo J); *McIvor v Westpac Banking Corporation* [2012] QSC 404, [104] (Applegarth J).

41 *Lui v Adamson* [2003] NSWSC 74; *Hoult v Hoult* [2011] FamCA 1023.

42 *Permanent Mortgages Pty Ltd v Vandenbergh* [2010] WASC 10, [197] (Murphy J); *Watt v State Bank of New South Wales Ltd* [2003] ACTCA 7.

43 *Permanent Mortgages Pty Ltd v Vandenbergh* [2010] WASC 10.

44 *Permanent Mortgages Pty Ltd v Vandenbergh* [2010] WASC 10, [197].

45 *Permanent Mortgages Pty Ltd v Vandenbergh* [2010] WASC 10, [173] (Murphy J).

46 *State Bank of New South Wales Limited v Layoun* [2001] NSWSC 113; [2001] NSW ConvR 55-984, [74]–[76] (Levine J); *Siglin v Choules & Ors* [2002] WASCA 9; *Australian Regional Credit v Mula*; *Australian Regional Credit v Raphael* [2009] NSWSC 325, [138]–[139] (McCallum J); *McIvor v Westpac Banking Corporation* [2012] QSC 404, [104] (Applegarth J); *Alceon Group Pty Ltd v Rose* [2015] NSWSC 868.

47 *Commonwealth Bank of Australia v Starrs* [2012] SASC 222.

v Jones as capable of application or extension to transactions other than those involving a guarantee by a wife of her husband's business loan, even to a loan granted to the wife for the benefit of the husband.[48]

Are the *Yerkey v Jones* principles justified?

[37.60] There are some reasons for questioning the merits of the principles in *Yerkey v Jones*.[49] There is an issue, first, as to whether the special protection it provides for married women is consonant with the ideal of social and economic equality for spouses. Although that ideal has not been achieved, it has been questioned whether it is appropriate today to *assume* that the marriage relationship is one of dependence of the wife on the husband. In *Garcia v National Australia Bank Ltd*, Kirby J said:

> [t]he stereotype underlying *Yerkey* may hold true for some, perhaps even a significant number of wives. But this court should, where possible, refuse to "classify unnecessarily and over broadly by gender when more accurate and impartial"[50] principles can be stated.[51]

A second issue is whether the special protection provided by the principles discriminates against other people who are living in analogous circumstances but who are not equally protected, such as women who opt for a relationship outside marriage. Further, there is a danger that the provision of special protection for married women may render the matrimonial home economically sterile. In *Barclays Bank plc v O'Brien*, Lord Browne-Wilkinson warned:

> If the rights secured to wives by the law renders vulnerable loans granted on the security of the matrimonial home, institutions will be unwilling to accept such security thereby reducing the flow of loan capital to business enterprises.[52]

In *Garcia v National Australia Bank Ltd*, the High Court acknowledged criticism of the principles in *Yerkey v Jones* but defended its merits in modern society on grounds of the trust and confidence inherent in the relationship of husband and wife. Gaudron, McHugh, Gummow and Hayne JJ said:

> the rationale of *Yerkey v Jones* is not to be found in notions based on the subservience or inferior economic position of women. Nor is it based on their vulnerability to exploitation because of their emotional involvement …
>
> [*Yerkey v Jones*] is based on trust and confidence, in the ordinary sense of those words, between marriage partners. The marriage relationship is such that one, often the woman, may well leave many, perhaps all, business judgments to the other spouse. … Sometimes, with not the slightest hint of bad faith, the explanation of a particular transaction given by one to the other will be imperfect and incomplete, if not simply wrong. That that is so is not always attributable to intended deception, to any imbalance of power between the parties, or, even, the vulnerability of one to exploitation because of emotional involvement. It is, at its core, often a reflection of no more or less than the trust and confidence each has in the other.[53]

48 *Elkofairi v Permanent Trustee Co Ltd* [2002] NSWCA 413. See also Narain v *Euroasia (Pacific) Pty Ltd* [2009] VSCA 290; (2009) 26 VR 387.

49 *Yerkey v Jones* [1939] HCA 3; (1940) 63 CLR 649.

50 *Miller v Albright* 523 US 420, 460 (Ginsburg J).

51 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395, [66].

52 *Barclays Bank plc v O'Brien* [1994] 1 AC 180, 188 (Lord Browne-Wilkinson).

53 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395, [20]–[41], 403–4.

Feminist critiques

[37.65] In Chapter 1, we saw that although a general aim of feminism is to reveal and redress inequalities between men and women, a variety of approaches to the realisation of this aim have emerged. We examined three broad approaches in feminist legal analysis — the identical treatment approach, the difference approach and the subordination approach — and considered how these approaches might differ in their assessment of the High Court's treatment of the *Yerkey v Jones* principle in *Garcia v National Australia Bank Ltd*.[54]

One issue faced by courts dealing with issues of inequality is whether to adopt gender-specific or gender-neutral principles. Kirby J posed this issue in *Warburton v Whiteley*:

> Despite the advances in the status of women in recent years, it should not be assumed that all commentators are of the opinion that the law should immediately expunge every rule previously fashioned to distinguish the position of women (and wives) from men (and husbands or persons in other relationships). Thus some commentators suggest that the conferral of "special" rights upon women (and wives) enables them to exercise an "equal right" without which they will, effectively, be denied equal treatment by the law. See, for example, Thornton, "Feminist Jurisprudence: Illusion or Reality?" (1986) 3 *Australian Journal of Law and Society* 5 … Other commentators oppose any special treatment for women (including wives) as such. They recognise the limitations of strict equality in the treatment of women (and wives) on the one hand, and men (and husbands and others) on the other. But they contend that there are more dangers in special treatment. Thus, Williams in "The Equality Crisis: Some Reflections on Culture, Courts and Feminism" (1981) 7 *Women's Rights Law Reporter* 175 observes, relevant to special treatment rules that they: "absolve women of personal responsibility in the name of protection … do we not acquire a greater right to claim our share from society if we too share its ultimate jeopardies?"[55]

In *Garcia v National Australia Bank Ltd*, as we have seen, Kirby J firmly enunciated gender-neutral principles. Callinan J adopted gender-specific principles in confirming *Yerkey v Jones*.[56] The remaining judges, who delivered a joint judgment, confirmed *Yerkey v Jones*, but they restated its rationale in gender-neutral terms. Which of these approaches is the most effective in forwarding the cause of equality for women?

Kristie Dunn has argued that the danger of focusing on this question is that fundamental assumptions about primary and natural sexual differences between men and women may go unchallenged.[57] She argues that, despite the apparent variations between the judgments in *Garcia v National Australia Bank Ltd*, in fact they all rely, impliedly, if not expressly, on assumptions about women's *difference* to account for the fact that the problem of sexually transmitted debt primarily affects married women. Kirby J, for example, seems to imply that it is merely a matter of preference for women that in a substantial proportion of marriages they follow their husband's advice in financial matters. Further, the judges who delivered the joint judgment, after describing marriage as a relationship of mutual trust and confidence, indicate that it is often the woman who leaves business decisions to her spouse. As this phenomenon is unexplained, the statement allows readers to assume that men and women naturally occupy different roles in marriage in respect of business decisions. Callinan J, in stating that many

54 *Garcia v National Australia Bank Ltd* [1998] HCA 48; (1998) 194 CLR 395. See [1.95].

55 *Warburton v Whiteley* (1989) 5 BPR 11,628, 11,630.

56 *Yerkey v Jones* [1939] HCA 3; (1940) 63 CLR 649.

57 Dunn, "'Yakking Giants': Equality Discourse in the High Court" (2000) 24 *Melbourne University Law Review* 427. ("Yakking Giants" is an American voice-activated computer software interpretation of the words "*Yerkey v Jones*".)

married women still need special protection, seemingly relies on an assumption of female dependence within marriage. Thus, in all the judgments, the problem of sexually transmitted debt is located in some notion of women's "difference". And this difference translates into either choice (women's preference) or incapacity (women's dependence).

In challenging the assumptions of the High Court in *Garcia v National Australia Bank Ltd*, Dunn employs a "subordination" approach. This approach, as we saw in Chapter 1, largely originated with the work of Catherine MacKinnon.[58] Gender inequality is seen not as the product of gender difference but rather as the product of male dominance. Adopting this approach one can focus on the issue of structural inequality within marriage, especially economic inequality. This in turn would lead to a better understanding of the factors associated with married women's decisions to enter into security transactions at the behest of their husbands. In *Garcia v National Australia Bank Ltd*:

> the missing factor in all three judgments was an analysis of the structural gendered inequality and, in particular the economic factors, which contribute to the problem. Such an analysis is vital if we are to reach an understanding of why it is that sexually transmitted debt is a gendered phenomenon without "blaming the victim" or entrenching notions of women as inherently and uniformly "different".[59]

The recognition by the courts that credit-providers have a responsibility to potential guarantors to provide them with information, and to recommend the obtaining of independent advice, will no doubt assist many wives who are called on to be guarantors of their husband's debts. The information and advice will at least assist those who did not originally understand the proposed transaction or had been misled by their husbands. This assumes, of course, that the information is adequate and the advice independent of the interests of both credit-provider and debtor. Adequate advice, it has been suggested, normally includes a "clear explanation of the terms of the document, the effects of the transaction and the propriety of the surety entering the surety transaction".[60] However, even such measures do not adequately address the general problem of wives who act under the pressure of structural inequality in the marriage relationship. The balance of power in a marriage will rarely be changed by independent information and advice. As Dianne Otto has said:

> The idea that the receipt of independent advice or adequate information can transform the position of a weaker party to one of equality … totally misunderstands that inequality is created by social arrangements of power which cannot be compensated for by mere formal gestures.[61]

58 See, eg, MacKinnon, *Towards a Feminist Theory of the State* (1989).

59 Dunn, "'Yakking Giants': Equality Discourse in the High Court" (2000) 24 *Melbourne University Law* Review 427, 447.

60 Sneddon, "Unfair Conduct in Taking Guarantees and the Role of Independent Advice" (1990) *University of New South Wales Law Journal* 302, 320.

61 Otto, "A Barren Future? Equity's Conscience and Women's Inequality" (1992) 18 *Melbourne University Law Review* 808, 826.

CHAPTER **38**

Unconscionable conduct under statute

STATUTORY REGULATION OF UNCONSCIONABLE CONDUCT AND UNJUST CONTRACTS

[38.05] In 1986, the Commonwealth introduced a statutory prohibition on unconscionable conduct through s 52A of the *Trade Practices Act 1974* (Cth) (TPA). That prohibition evolved over time, and statutory regulation of unconscionable conduct in trade or commerce is now found in Pt 2-2 of the *Australian Consumer Law* (ACL).[1]

The legislative provisions regulating unconscionable conduct make available to a plaintiff a wider range of remedies than may be obtained under the general law.[2] The legislation also potentially extends to a wider range of conduct than the equitable doctrines of unconscionable dealing or undue influence. The legislation does not clearly distinguish between concerns relating to procedural fairness, the process through which the contract was made, and substantive fairness in the terms of the contract itself. However, to date, most cases have been decided on the basis of a combination of these concerns rather than purely on grounds of substantive fairness.[3]

1 On the *Australian Consumer Law* (*ACL*), see Chapter 2.

2 See Chapter 33.

3 But cf *Kowalczuk v Accom Finance Pty Ltd* [2008] NSWCA 343; (2008) 77 NSWLR 205 (higher "penalty" interest and provision for compounding interest were held to be unjust and unconscionable); *PSAL Ltd v Kellas-Sharpe* [2012] QSC 31, appeal dismissed in *Kellas-Sharpe v PSAL Ltd* [2012] QCA 371; [2013] 2 Qd R 233 (provision for compounding interest held to be unconscionable).

In New South Wales, additional protection against abuse of power in contracting is found in the *Contracts Review Act 1980*, which gives courts the power to grant relief against contracts that are "unjust". This provision has a slightly broader scope than the ACL prohibition on unconscionable conduct. Equally however, its primary use has been in response to procedural, as opposed to substantive, unfairness.

PART 2-2 OF THE AUSTRALIAN CONSUMER LAW

Trade and commerce

[38.15] The prohibitions on unconscionable conduct in Pt 2-2 of the ACL apply only to unconscionable conduct occurring in trade or commerce. The meaning of this phrase is discussed in Chapter 33 in relation to misleading or deceptive conduct. Transactions between individuals in their private capacity are not covered. This means, in particular, that transactions between family members where some form of equitable fraud is alleged, commonly the taking advantage of an elderly parent or relative, will not be regulated under the ACL and will instead proceed in equity.[4]

The ACL and the *Trade Practices Act 1974* (Cth)

[38.20] The ACL re-enacts prohibitions on unconscionable conduct in a similar form as under the TPA.[5] However, there are some important differences between the provisions. Under the ACL, the prohibition on unconscionable conduct applies to persons, not merely corporations as in the TPA. Importantly, unlike the TPA, the ACL does not distinguish between unconscionable conduct occurring in consumer transactions and unconscionable conduct occurring in business-to-business transactions. Case law dealing with the prohibitions on unconscionable conduct under the TPA may be useful in interpreting and applying the provisions regulating unconscionable conduct in the ACL, provided these differences in scope are borne in mind.

Financial services

[38.25] Section 131A provides that the ACL does not apply "to the supply, or possible supply, of services that are financial services, or of financial products." These products are regulated under the *Australian Securities and Investments Commission Act 2001* (Cth), where ss 12CA, 12CB and 12CC replicate ss 20, 21 and 22 of the ACL, respectively.

4 See Chapters 35 and 36.

5 Specifically:
- s 20 of the *ACL* replaces 51AA of the *TPA*
- s 21 of the *ACL* replaces s 51AB and 51AC of the *TPA* by removing the distinction between business to business and business to consumer transactions, and
- s 22 of the *ACL* contains the list of relevant factors previously found in ss 51AB and 51AC.

Redress and remedies

[38.30] Under the ACL, courts may order the payment of a civil pecuniary penalty for a contravention of the provisions precluding unconscionable conduct.[6] Remedies available for unconscionable conduct include: undertakings,[7] substantiation notices,[8] public warning notices,[9] injunctions,[10] damages,[11] compensatory orders,[12] redress for non-parties[13] and non-punitive orders.[14]

The remedies for violation of any of the three prohibitions of Pt 2-2 of the ACL are discussed in Chapter 33 in relation to the prohibition on misleading and deceptive conduct. While there is little case law on this issue, similar principles will apply to govern the application of the remedy provisions in the ACL to grant relief against unconscionable conduct.

SECTION 20: THE UNWRITTEN LAW

[38.35] Section 20 provides:

> (1) A person must not, in trade or commerce, engage in conduct that is unconscionable, within the meaning of the unwritten law from time to time.
>
> (2) This section does not apply to conduct that is prohibited by section 21.

Until 2018, s 21 applied to all transactions in trade or commerce other than those involving claims by a listed public company of unconscionable conduct. Section 20 would therefore apply in these situations. A party who can bring an action under s 20 will have access to the various remedies provided under the ACL. Section 20 also makes possible the involvement of the regulator, the Australian Competition and Consumer Commission (ACCC), in claims alleging unconscionable conduct within the meaning of the unwritten law.

In 2019, the ACL was amended to remove the limitation on s 21 applying to claims by a listed public company.[15] This amendment appears to have reduced considerably the scope of s 20; all claims of unconscionable conduct in trade or commerce will fall under s 21 and therefore be precluded under s 20(2).

Unconscionable conduct within the meaning of the unwritten law

[38.40] The phrase "unwritten law" in s 20 refers to judge-made law that is distinguished from enacted law in the form of legislation. It may be described in a general way as "common law". In this sense, it is an umbrella term to cover two historically distinctive sources of law: common law and equity.[16] The ACL does not define "unconscionable conduct" within

6 *ACL*, s 224.
7 *ACL*, Pt 5-1, Div 1.
8 *ACL*, Pt 5-1, Div 2.
9 *ACL*, Pt 5-1, Div 3.
10 *ACL*, s 232.
11 *ACL*, s 236.
12 *ACL*, Pt 5-2, Div 4, Subdiv A.
13 *ACL*, s 246.
14 *ACL*, Pt 5-2, Div 5, s 246.
15 *Treasury Laws Amendment (Australian Consumer Law Review) Act 2018*.
16 See [2.50]ff.

the meaning of the unwritten law. Equity's notion of unconscionable conduct can be understood at different levels of breadth. At a narrow level, the ACL could mean simply the unconscionable conduct (or unconscionable dealing) doctrine as recognised in those terms by the High Court in *Commercial Bank of Australia Ltd v Amadio*.[17] As we have seen, the notion of unconscionable conduct also informs a wide range of particular equitable doctrines, either expressly or impliedly, such as undue influence, duress, unconscionable dealing, equitable estoppel, relief from forfeiture and penalties, unilateral mistake and misrepresentation.[18] In *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd*, the High Court accepted that the proper construction of s 51AA of the TPA (now s 20 of the ACL) meant that it applied beyond unconscionable dealing in equity to broader "manifestations of equity's concern with unconscientious or unconscionable conduct", although the precise scope of the jurisdiction did not have to be decided in that case.[19]

SECTION 21: STATUTORY UNCONSCIONABLE CONDUCT

[38.45] Section 21 of the ACL provides that:

> A person must not, in trade or commerce, in connection with:
>
> (a) the supply or possible supply of goods or services to a person; or
>
> (b) the acquisition or possible acquisition of goods or services from a person;
>
> engage in conduct that is, in all the circumstances, unconscionable.

At one time, this general prohibition distinguished between business-to-consumer and business-to-small-business transactions.[20] However, in 2012, the distinction was removed and the prohibition now applies to all transactions in "trade or commerce" regardless of the identity of the parties.[21] In 2018, the restriction on listed public companies making use of the prohibition in s 21 was removed.[22]

Interpretative principles

[38.50] Unconscionable conduct under s 21 is not defined. Section 21(4) contains a set of interpretative principles that aim to assist in the application of the section. The principles confirm that the statutory prohibition is not confined by the unwritten law.[23] The principles also state that the "section is capable of applying to a system of conduct or pattern of

17 *Commercial Bank of Australia Ltd v Amadio* (1983) 151 CLR 447, see [36.20].

18 See *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd (No 2)* [2000] FCA 2; (2000) 96 FCR 491, [23].

19 *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd* [2003] HCA 18; (2003) 214 CLR 51, [40].

20 See the *Trade Practices Act 1974* (Cth), ss 51AB and 51AC.

21 *Competition and Consumer Legislation Amendment Act 2011* (Cth).

22 *Treasury Laws Amendment (Australian Consumer Law Review) Act 2018*.

23 *ACL* s 21(4)(a). A point already confirmed in a number of cases, see eg: *Australian Competition and Consumer Commission v Radio Rentals Ltd* [2005] FCA 1133; (2005) 146 FCR 292, [24]; *Australian Securities and Investments Commission v National Exchange Pty Ltd* [2005] FCAFC 226; (2005) 148 FCR 132, [30]; *Attorney-General (NSW) v World Best Holdings Ltd* [2005] NSWCA 261; (2005) 63 NSWLR 557, [21]; *Director of Consumer Affairs Victoria v Scully* [2013] VSCA 292, [38].

behaviour, whether or not a particular individual is identified as having been disadvantaged by the conduct or behaviour".[24]

Section 22: Factors to consider

[38.55] Section 22 contains a list of factors to which the court may have regard in deciding whether conduct is unconscionable.[25] Section 22(1) deals with the relationship between a customer (who may be a business or a consumer) and a supplier:

> Without limiting the matters to which the court may have regard for the purpose of determining whether a person (the *supplier*) has contravened section 21 in connection with the supply or possible supply of goods or services to a person (the *customer*), the court may have regard to:
>
> (a) the relative strengths of the bargaining positions of the supplier and the customer; and
>
> (b) whether, as a result of conduct engaged in by the supplier, the customer was required to comply with conditions that were not reasonably necessary for the protection of the legitimate interests of the supplier; and
>
> (c) whether the customer was able to understand any documents relating to the supply or possible supply of the goods or services; and
>
> (d) whether any undue influence or pressure was exerted on, or any unfair tactics were used against, the customer or a person acting on behalf of the customer by the supplier or a person acting on behalf of the supplier in relation to the supply or possible supply of the goods or services; and
>
> (e) the amount for which, and the circumstances under which, the customer could have acquired identical or equivalent goods or services from a person other than the supplier; and
>
> (f) the extent to which the supplier's conduct towards the customer was consistent with the supplier's conduct in similar transactions between the supplier and other like customers; and
>
> (g) the requirements of any applicable industry code; and
>
> (h) the requirements of any other industry code, if the customer acted on the reasonable belief that the supplier would comply with that code; and
>
> (i) the extent to which the supplier unreasonably failed to disclose to the customer:
>
> (i) any intended conduct of the supplier that might affect the interests of the customer; and
>
> (ii) any risks to the customer arising from the supplier's intended conduct (being risks that the supplier should have foreseen would not be apparent to the customer); and
>
> (j) if there is a contract between the supplier and the customer for the supply of the goods or services:
>
> (i) the extent to which the supplier was willing to negotiate the terms and conditions of the contract with the customer; and
>
> (ii) the terms and conditions of the contract; and

24 *ACL* s 21(4)(b). See also making this point *Australian Securities and Investments Commission v National Exchange Pty Ltd* [2005] FCAFC 226; (2005) 148 FCR 132.

25 *Australian Securities and Investments Commission v National Exchange Pty Ltd* [2005] FCAFC 226; (2005) 148 FCR 132, [40]. Also *Australian Competition and Consumer Commission v Simply No-Knead (Franchising) Pty Ltd* [2000] FCA 1365; (2000) 104 FCR 253, [31].

(iii) the conduct of the supplier and the customer in complying with the terms and conditions of the contract; and

(iv) any conduct that the supplier or the customer engaged in, in connection with their commercial relationship, after they entered into the contract; and

(k) without limiting paragraph (j), whether the supplier has a contractual right to vary unilaterally a term or condition of a contract between the supplier and the customer for the supply of the goods or services; and

(l) the extent to which the supplier and the customer acted in good faith.

Section 22(2) contains an equivalent list of considerations applying to transactions between a supplier of goods or services (who may be a business or consumer) and an acquirer of goods or services, in circumstances where it is alleged the acquirer has engaged in unconscionable conduct contrary to the statute.

Courts have stated that it is not appropriate to approach these lists as exhaustive of the circumstances that may give rise to unconscionable conduct; they are indicative of the kinds of factors that should be considered in determining whether conduct contravenes the prohibition.[26]

Determining whether there has been a contravention of the prohibition

[38.60] Courts have used different expressions for describing the threshold standard of wrongful conduct required for establishing unconscionable conduct contrary to the statutory prohibition. The presence of unequal bargaining power is not enough.[27] Courts have required conduct "not done in good conscience"[28] or conduct that offends "commonly held community values".[29] Unconscionable conduct has sometimes been described as a concept that requires "a high level of moral obloquy".[30] The use of this concept has also been subject to considerable criticism.[31] It was adopted by Gageler J in *Paciocco v Australia and New Zealand Banking Group Ltd*.[32] In *Australian Securities and Investments Commission v Kobelt*, Gageler J stated that the criticism was justified and his Honour regretted having mentioned moral obloquy.[33] Gageler J considered the phrase was "arcane terminology" and had the potential to be

26 *Australian Securities and Investments Commission v National Exchange Pty Ltd* [2005] FCAFC 226; (2005) 148 FCR 132, [40]. Also *Australian Competition and Consumer Commission v Simply No-Knead (Franchising) Pty Ltd* [2000] FCA 1365; (2000) 104 FCR 253, [31].

27 *Director of Consumer Affairs Victoria v Scully* [2013] VSCA 292, [43].

28 *Australian Competition and Consumer Commission v Lux Distributors Pty Ltd* [2013] FCAFC 90, [41]; *PT Ltd v Spuds Surf Chatswood Pty Ltd* [2013] NSWCA 446, [105].

29 *Australian Competition and Consumer Commission v Lux Distributors Pty Ltd* [2013] FCAFC 90, [23]. See also *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, (2015) 236 FCR 199, [296].

30 *Attorney-General (NSW) v World Best Holdings Ltd* [2005] NSWCA 261; (2005) 63 NSWLR 557, [121] (Spigelman CJ). See also *Canon Australia Pty Ltd v Patton* [2007] NSWCA 246, [55]; *Violet Home Loans Pty Ltd v Schmidt* [2013] VSCA 56; (2013) 44 VR 202, [58]; *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [188].

31 See Baxt, "Continuing 'Furore' Over Moral Obloquy and Unconscionability" (2017) 91 *Australian Law Journal* 809, 809–10; *Ipstar Australia Pty Ltd v APS Satellite Pty Ltd* (2018) 356 ALR 440, [194]–[195] and [275]–[278].

32 *Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28; (2016) 258 CLR 525, [188].

33 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [91] (Gageler J).

misleading by suggesting a requirement for "conscious wrongdoing".[34] By contrast, Keane J stated that the relevant judgment in determining whether conduct was unconscionable contrary to the statute was to "whether the impugned conduct exhibits the level of moral obloquy associated with predatory conduct".[35]

Courts have also emphasised that none of the alternative phrases used to describe conduct that will contravene the prohibition should be "used as a substitute for the statutory words".[36] The question is whether conduct is unconscionable having regard to the matters listed in the statutory prohibition and the values and normative standards embodied in it.[37]

Relationship with the equitable doctrine

[38.62] The prohibition on unconscionable conduct in s 21 of the ACL does not merely replicate the equitable doctrine of unconscionable dealing in statutory form. This is clear from this list of factors the court may consider and also from the existence of s 20, which provides a statutory remedy for conduct that is unconscionable within the meaning of the unwritten law. The precise nature of the relationship between the statutory prohibition and the equitable doctrine remains unclear. Should the equitable doctrine provide the framework for analysis or is the approach guided primarily by the statutory factors? The controversial decision in *Australian Securities and Investments Commission v Kobelt* showed different understandings of the influence of the equitable doctrine in determining whether a party has engaged in unconscionable conduct in contravention of the statutory prohibition.

In the majority, Kiefel CJ and Bell J considered that unconscionable conduct under s 12CB "requires not only that the innocent party be subject to special disadvantage, but that the other party must also unconscientiously take advantage of that special disadvantage".[38] These are the elements in the equitable doctrine of unconscionable dealing. The statutory prohibition with which *Australian Securities and Investments Commission v Kobelt*[39] was concerned does not refer to either "special disadvantage" or "advantage taking". Their Honours observed that this was standard for assessment presented by ASIC and that, in the circumstances, the appeal did not provide the occasion to consider the suggestion that the statute might not require the elements demanded in equity.[40]

Gageler J[41] and Edelman J[42] explicitly confirmed that the statutory prohibition on unconscionable dealing is not confined by the equitable doctrine. Gageler J also emphasised that the statutory doctrine should not be permitted to "dilute" the equitable conception of

34 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [91].

35 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [120] (Keane J).

36 *Ipstar Australia Pty Ltd v APS Satellite Pty Ltd* [2018] NSWCA 15; (2018) 329 FLR 149, [195]–[199] (Bathurst CJ), [275]–[278] (Leeming JA); *Australian Competition and Consumer Commission v Ford Motor Company of Australia Ltd* [2018] FCA 763, [25]; *Australian Competition and Consumer Commission v Medibank Private Ltd* [2017] FCA 1006, [240].

37 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [87] (Gageler J), [153] (Nettle and Gordon JJ); *Australian Competition and Consumer Commission v Lux Distributors Pty Ltd* [2013] FCAFC 90.

38 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [15], quoting *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50, (2015) 236 FCR 199, [296] (Allsop CJ).

39 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18.

40 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [48].

41 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [83], [93] (Gageler J).

42 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [279], [295] (Edelman J).

unconscionable conduct, involving exploitation of a special disadvantage.[43] Rather, regard must be had to the factors identified in the statute as relevant in assessing whether conduct has been unconscionable. Gageler J,[44] Nettle and Gordon JJ[45] and Edelman J[46] recognised that unconscionable conduct under s 12CB should be assessed primarily by reference to the values expressed by the statutory norm and as guided by the identified factors.

Australian Securities and Investments Commission v Kobelt[47] concerned an informal credit scheme known as "book-up" provided by Mr Kobelt to the Anangu, the indigenous residents of the remote South Australian APY Lands. The book-up scheme allowed Anangu customers to purchase goods and second-hand motor vehicles on credit at the store operated by Kobelt. In return, Kobelt required Anangu customers to provide him with their debit cards, PINs and details of their income, which he then used to withdraw of the whole of the customer's money from their bank account on or around the day they were paid. Around half of the withdrawn amount was used to pay down the debt on the second-hand motor vehicles, while the balance was intended to be used as credit for goods, cash advances or money orders for other stores. The credit charges for purchasing cars were not disclosed, and the credit provided was expensive. The records of the arrangements were unintelligible and chaotic. The customers were not provided with information about the transactions or statements of account.

At first instance, White J in the Federal Court held that the system was unconscionable.[48] The Full Federal Court (Besanko and Gilmour JJ and Wigney J) allowed an appeal by Mr Kobelt.[49] ASIC appealed to the High Court. The High Court (Kiefel CJ and Bell J; Gageler J and Keane J agreeing; Nettle and Gordon JJ dissenting; Edelman J dissenting) held that Kobelt's conduct did not contravene the statutory prohibition on unconscionable conduct.

Although recognising the vulnerable situation of the Anangu customers, the majority did not consider that Kobelt had taken unconscientious advantage of that situation. For the majority judges, the supply of the book-up credit to Kobelt's Anangu customers did not exploit or otherwise take advantage of their lack of education and financial literacy.[50] Book-up credit provided the Anangu customers with the ability to purchase motor vehicles, notwithstanding their low incomes and lack of assets with which to secure a loan.[51] The majority considered that the vast majority of the Anangu customers had a rudimentary but adequate understanding of the basic operation of Kobelt's book-up system.[52] This meant there was an element of choice in the use of the book-up system by the Anangu customers.[53] Moreover, Kobelt's book-up system provided benefits to its customers in the form of access

43 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [90]. Contrast [295] (Edelman J).

44 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [83] (Gageler J).

45 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [234] (Nettle and Gordon J).

46 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [268] (Edelman J).

47 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18.

48 *Australian Securities and Investments Commission v Kobelt* [2016] FCA 1327.

49 *Kobelt v Australian Securities and Investments Commission* [2018] FCAFC 18.

50 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [77], (Kiefel CJ and Bell J), [107] (Gageler J).

51 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [64]–[65] (Kiefel CJ and Bell J).

52 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [78] (Kiefel CJ and Bell J), [108] (Gageler J), [129] (Keane J).

53 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [107] (Gageler J).

to credit and a response to the problems of "humbugging" and "demand sharing", by which members of the community pressured those with funds to share their money[54] and to smooth out the "boom and bust" cycle of household expenditure which might otherwise exist.[55] The majority emphasised the role of cultural practices and choice as supporting their conclusion that the book-up scheme operated by Kobelt was not unconscionable.[56] Gageler J said:

> To say, as does ASIC, that the cultural considerations which fed into Mr Kobelt's Anangu customers' choice to maintain their relationship with Mr Kobelt and to continue to participate in his book-up system were amongst the very factors which made those customers vulnerable and that the operation of Mr Kobelt's book-up system 'would be patently unacceptable conduct elsewhere in modern Australian society' fails, in my opinion, to afford to the Anangu people the respect that is due to them within contemporary Australian society. Those of the Anangu people who chose to maintain their relationship with Mr Kobelt and to continue to participate in his book-up system evidently considered that continued participation in the book-up system suited the interests of them and their families having regard to their own preferences and distinctive cultural practices.[57]

By contrast, the minority judges held that the Kobelt had engaged in unconscionable conduct. Nettle and Gordon JJ said that Kobelt's

> customers were at such a special disadvantage relative to Mr Kobelt so as to be unable to make a decision in their own interests, and Mr Kobelt, knowing or in circumstances where he ought to have known of their incapacity to make a decision in their own interests, took advantage of that disadvantage to get them to agree to his terms.[58]

The minority did not consider it conclusive for establishing the validity of the transactions that that some of Kobelt's Anangu the customers may have understood the rudiments of the book-up system or regarded it as useful in alleviating demand sharing and entered the arrangement voluntarily. The position of the customers was such that they could not demand a superior system.[59] Moreover, Kobelt's system was not reasonably necessary to protect his legitimate interests – there were alternatives.[60] Edelman J concluded:

> As the Solicitor-General of the Commonwealth rightly said in oral submissions, in what is probably a significant understatement, the system of credit adopted by Mr Kobelt is one that would be unacceptable in mainstream Australian society. It is made less acceptable, not more acceptable, because it was the only form of credit offered, and thus accepted, in remote communities of highly vulnerable persons in need of credit.[61]

54 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [69] (Kiefel CJ and Bell J).

55 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [109] (Gageler J).

56 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [100] (Kiefel CJ and Bell J), [109]–[110] (Gageler J).

57 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [110] (Gageler J).

58 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [239] (Nettle and Gordon JJ).

59 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [240] (Nettle and Gordon JJ), [312] (Edelman J).

60 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [264] (Nettle and Gordon JJ) (Edelman J agreeing).

61 *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [313]. Also [260] (Nettle and Gordon JJ).

Business to consumer and business to business transactions

[38.65] Courts have referred to "dishonesty, trickery, predatory or overbearing behaviour, choice or the absence of choice, disadvantage, vulnerability and exploitation" as indicators of unconscionable conduct.[62] Many of the cases of unconscionable conduct contrary to s 21 of the ACL involve businesses whose sales strategy, established by evidence, relies on taking advantage of the position of vulnerability or a lack of understanding in a targeted consumer or small business group.[63]

Australian Competition and Consumer Commission v Lux Distributors Pty Ltd[64] involved a challenge by the Australian Competition and Consumer Commission to the sales strategy utilised by Lux for the sale of vacuum cleaners. The strategy involved a representative from Lux calling home owners and offering a free maintenance check of their existing vacuum cleaner. If the offer was taken up, a Lux representative, who was not a trained maintenance technician but a salesperson would visit the householder. During the visit to the householder's home, the sales representative would perform a very perfunctory check of the existing vacuum cleaner and then attempt to sell a new Lux vacuum cleaner, often staying at the premises longer than permitted under relevant door-to-door sales provisions. The Full Court of the Federal Court held that by utilising this strategy, Lux had contravened the statutory prohibition on unconscionable conduct. This finding was primarily based on the grounds that the sales strategy was premised on a "deceptive ruse", which breached consumer protection laws on door-to-door sales, and had the effect of taking advantage of elderly consumers living alone.[65] The court noted that:

> [t]he vulnerability of the consumer to the salesperson in her or his own home arises from the difficulty in putting an end to the sales process once the salesperson is in the home, especially after that person has spent time and undertaken persuasive effort in a sales process or 'pitch'. … Ingratiating solicitude, just as much as high-pressure bullying sales tactics, may lead to a feeling of necessitous acceptance, especially by a polite and accepting person.[66]

The prohibition on unconscionable conduct in s 21 of the ACL also applies to business-to-business transactions. In these cases, the offending conduct often involves a high degree of "bullying and thuggish behaviour".[67] *Australian Competition and Consumer Commission v Seal-A-Fridge*[68] arose from the operation of the Seal-A-Fridge franchise, which provided the on-site replacement of seals on refrigerators. Seal-A-Fridge charged franchisees a weekly fee for

62 *Kobelt v ASIC* (2018) 352 ALR 689, [192], [296]. This approach follows the categories of unconscionable conduct identified in *Tonto Home Loans Australia Pty Ltd v Tavares* [2011] NSWCA 389, [291]. See also *Paciocco v Australia and New Zealand Banking Group Ltd* [2015] FCAFC 50; (2015) 236 FCR 199, [296]; *Commonwealth Bank of Australia v Kojic* [2016] FCAFC 186; (2016) 249 FCR 421, [60]; *Australian Competition and Consumer Commission v Ford Motor Company of Australia Limited* [2018] FCA 763, [23].

63 On the need to establish this conduct by evidence see, eg, *Australian Competition and Consumer Commission v Woolworths Limited* [2016] FCA 1472; *Unique International College Pty Ltd v ACCC* [2018] FCAFC 155. Also *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18.

64 *Australian Competition and Consumer Commission v Lux Distributors Pty Ltd* [2013] FCAFC 90.

65 *Australian Competition and Consumer Commission v Lux Distributors Pty Ltd* [2013] FCAFC 90, [27], [34], [40], [42].

66 *Australian Competition and Consumer Commission v Lux Distributors Pty Ltd* [2013] FCAFC 90, [10], [64]. See also *Australian Securities and Investments Commission v Australian Lending Centre Pty Ltd (No 3)* [2012] FCA 43, [194], [199].

67 *Tonto Home Loans Australia Pty Ltd v Tavares* [2011] NSWCA 389, [291].

68 *Australian Competition and Consumer Commission v Seal-A-Fridge* [2010] FCA 525.

access to calls made by prospective consumers to the national 13-telephone franchise telephone number. This fee included a portion of profit to the franchisor. Seal-A-Fridge then demanded increases to this fee from franchisees, which significantly increased its own profit margin.

In the Federal Court, Logan J found that Seal-A-Fridge had contravened the prohibition on unconscionable conduct in s 51AC of the *Trade Practices Act 1974* (Cth). The fee increases demanded by Seal-A-Fridge were not permitted by the contract and instead amounted to a "unilateral profit gouge".[69] Seal-A-Fridge engaged in a range of objectionable conduct to support its demands for payment of the fee increase, which Logan J described as amounting to "misstatement, non-disclosure of information, threats and intimidation and abuse of Seal-A-Fridge's position of strength in relation to being able to cut off the phone number".[70] Logan J emphasised that merely taking advantage of a superior bargaining position will not amount to unconscionable conduct.[71] The complaint in this case was that Seal-A-Fridge had used its ability to cut off a service that was essential to the business of the franchisees to obtain additional profit to which it was not entitled.[72]

In *Ipstar Australia Pty Ltd v APS Satellite Pty Ltd*,[73] Ipstar supplied goods to APS Satellite. These goods failed to comply with the consumer guarantee of acceptable quality, exposing Ipstar to liability to compensate APS Satellite. Rather than doing this, Ipstar increased the price of the goods by an amount based on the estimated accrued liability. The Full Court of the Supreme Court of NSW concluded this conduct was not done in good faith and was contrary to the statutory prohibition on unconscionable conduct.[74]

CONTRACTS REVIEW ACT 1980 (NSW)

Scope of the power to give relief against an unjust contract

[38.75] The *Contracts Review Act 1980* was enacted in New South Wales in 1980, following a report by John Peden in 1976 on harsh and unconscionable contracts.[75] The *Contracts Review Act 1980* (NSW) is generally seen as beneficial remedial legislation. It has given rise to considerable litigation for over 20 years.[76] Section 7 of the *Contracts Review Act 1980* (NSW) confers on the court[77] power to grant various kinds of relief in respect of "a contract or a

69 *Australian Competition and Consumer Commission v Seal-A-Fridge* [2010] FCA 525, [133].

70 *Australian Competition and Consumer Commission v Seal-A-Fridge* [2010] FCA 525, [141].

71 *Australian Competition and Consumer Commission v Seal-A-Fridge* [2010] FCA 525, [150].

72 *Australian Competition and Consumer Commission v Seal-A-Fridge* [2010] FCA 525, [146] and [150]. See also *Australian Competition and Consumer Commission v Simply No-Knead (Franchising) Pty Ltd* [2000] FCA 1365; (2000) 104 FCR 253, [51]; *Australian Competition and Consumer Commission v Coles Supermarkets Australia Pty Ltd* [2014] FCA 1405; *Australian Competition and Consumer Commission v South East Melbourne Cleaning Pty Ltd* [2015] FCA 25; *Australian Competition and Consumer Commission v ACN 117 372 915 Pty Ltd (in liq)* [2015] FCA 368.

73 *Ipstar Australia Pty Ltd v APS Satellite Pty Ltd* [2018] NSWCA 15; (2018) 329 FLR 149.

74 *Ipstar Australia Pty Ltd v APS Satellite Pty Ltd* [2018] NSWCA 15; (2018) 329 FLR 149, [210].

75 See further Peden, *The Law of Unjust Contracts* (1982); Terry, "Unconscionable Contracts in New South Wales: The Contracts Review Act" (1982) 10 *Australian Business Law Review* 311.

76 For appraisals see Carlin, "The Contracts Review Act 1980 (NSW) – 20 Years On" (2001) 123 *Sydney Law Review* 125; Zipser, "Unjust Contracts and the Contracts Review Act 1980 (NSW)" (2001) 17 *Journal of Contract Law* 76.

77 "Court" means the Supreme Court and, within their jurisdictional limits, the District Court, the Local Court and the Fair Trading Tribunal.

provision of a contract" that the court finds to have been "unjust in the circumstances relating to the contract at the time it was made". The relief is given if the court "considers it just to do so, and for the purpose of avoiding as far as practicable an unjust consequence or result".

To what contracts does the Contracts Review Act apply?

[38.80] Section 6(1) of the *Contracts Review Act 1980* (NSW) restricts the parties who can claim relief under that Act. It excludes the Crown, public or local authorities and corporations (except home unit corporations: s 4(2)). Further, s 6(2) excludes contracts entered into "in the course of or for the purpose of a trade, business or profession … other than a farming undertaking".

Although s 6(2) places restrictions on the granting of relief, it has not been interpreted in a restrictive way. For example, it has been held that a contract for the sale of a business is not excluded by the subsection because such a sale is not "in the course of a business".[78] Further, it appears that a person who provides a guarantee in favour of a company through which that person conducts a business is not regarded as carrying on a business in giving the guarantee.[79] A contract granting quarrying operation rights over part of a landowner's land has been held to come within the "farming operation" exception and therefore is not excluded from the *Contracts Review Act 1980* (NSW).[80]

Relief

[38.85] The principal forms of relief available under the *Contracts Review Act 1980* (NSW) in respect of unjust contracts are set out in s 7(1): refusal to enforce all or any of the provisions of the contract, avoidance in whole or part, and variation. In addition, by virtue of s 8, Sch 1 has effect with respect to wide-ranging forms of ancillary relief. These include orders with respect to:

- the disposition of property;
- payment of money (by way of compensation or otherwise);
- compensation to a person who is not a party to the contract;
- the supply or repair of goods;
- the supply of services; and
- the creation of a charge on property.

In determining whether it is just to grant relief in respect of a contract found to be unjust, the court may have regard to the conduct of the parties in relation to the performance of the contract since it was made: s 9(5).

What is an unjust contract?

[38.90] The *Contracts Review Act 1980* (NSW) does not define "unjust" exclusively but states in s 4(1) that it includes "unconscionable, harsh or oppressive". Under s 9(1), the court must have regard to "the public interest and to all the circumstances of the case". Without detracting

78 *Coombs v Bahama Palm Trading Pty Ltd* (1991) ASC 56-097.

79 See *Australian Bank Ltd v Stokes* (1985) 3 NSWLR 174, 176.

80 *Ellison v Vukicevic* (1986) 7 NSWLR 104.

from the generality of this subsection, subsection (2) sets out a lengthy list of matters to which the court shall have regard, to the extent to which they are relevant to the circumstances, which are similar to the identified relevant considerations in assessing conscionable conduct under s 22 in the ACL. The court must not have regard to any injustice arising from circumstances that were not reasonably foreseeable at the time the contract was made: s 9(4).

Interpretation

[38.95] In *West v AGC (Advances) Ltd*,[81] McHugh J described the *Contracts Review Act 1980* (NSW) as "revolutionary legislation whose evident purpose is to overcome the common law's failure to provide a comprehensive doctrinal framework to deal with 'unjust' contracts". In *Sharman v Kunert*, Holland J said the *Contracts Review Act 1980* (NSW) called for

> a fresh and direct approach to the individual case, without preconceived notions of conditions on which the courts may set aside or vary a contract derived exclusively from established doctrines, whilst at the same time giving due recognition to the public interest in generally holding parties to their bargains.[82]

Although the jurisdiction extends to substantive unfairness, as with unconscionable dealing, the courts tend to look for procedural injustice before granting relief.[83] It has been said that:

> a contract may be unjust under the [Contracts Review] Act because its terms, consequences or effects are unjust. This is substantive injustice. Or a contract may be unjust because of the unfairness of the methods used to make it. This is procedural injustice. Most unjust contracts will be the product of both procedural and substantive injustice.[84]

A study of cases decided under the *Contracts Review Act 1980* (NSW) showed that most successful cases involved some measure of procedural unfairness; only a very small percentage of successful cases where held to be unjust on solely the basis of substantive unfairness.[85] The threshold for relief from an unjust contract is lower than in relation to a claim for relief from unconscionable dealing at general law[86] or unconscionable conduct under statute.[87] In particular, although courts have held that the defendant's knowledge of the injustice will be relevant to the exercise of the court's discretion to grant relief under the relevant legislation,[88] an absence of knowledge of the circumstances of injustice does not preclude a claim for relief.[89]

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81 *West v AGC (Advances) Ltd* (1986) 5 NSWLR 610, 621.

82 *Sharman v Kunert* (1985) 1 NSWLR 225, 231.

83 See Carlin, "The Contracts Review Act 1980 (NSW) – 20 Years On" (2001) 23 *Sydney Law Review* 125; Zipser, "Unjust Contracts and the Contracts Review Act" (2001) 17 *Journal of Contract Law* 76, 79.

84 *West v AGC (Advances) Ltd* (1986) 5 NSWLR 610, 620.

85 Carlin, "The Contract Review Act 1980 (NSW) – 20 Years On" (2001) 23 *Sydney Law Review* 133.

86 *Bakarich v Commonwealth Bank of Australia* [2007] NSWCA 169, [89]. Also *Robinson v ANZ Banking Group Ltd* [1990] ASC 55-979; *Elders Rural Finance Ltd v Smith* (1996) 41 NSWLR 296.

87 *Paciocco v Australia and New Zealand Banking Group Limited* [2015] FCAFC 50; (2015) 236 FCR 199, [356].

88 *Collier v Morlend Finance (Vic) Corporation Pty Ltd* [1989] ASC 55-716; *Beneficial Finance Corporation Ltd v Karavas* (1991) 23 NSWLR 256; *Nguyen v Taylor* (1992) 27 NSWLR 48; *Perpetual Trustee Co Ltd v Khoshaba* [2006] NSWCA 41, [77], [119]; *Verduci v Golotta* [2010] NSWSC 506, [52].

89 See, eg, *Robinson v ANZ Banking Group Ltd* [1990] ASC 55-979; *Elkofairi v Permanent Trustee Co Ltd* [2002] NSWCA 413; *St George Bank Ltd v Trimarchi* [2004] NSWCA 120; *Perpetual Trustee Co Ltd v Khoshaba* [2006] NSWCA 41.

Protection provided

[38.100] There is considerable overlap between the power to reopen unjust contracts in *Contracts Review Act 1980* (NSW) and the prohibition on unconscionable conduct in s 21 of the ACL. Courts have taken the view that one of the legislative purposes of the reopening provisions is to "protect persons who, for various reasons, are not able to look after their own interests, and who are preyed upon by dishonesty, trickery and other forms of predation".[90] As we have seen, the scope of the prohibition on unconscionable conduct has been described in similar terms.[91] Most of the cases under the *Contracts Review Act 1980* (NSW) have related to mortgage and guarantee contracts. However, relief has been sought in respect of a wide range of other contracts, such as contracts for the sale of land, option contracts, employment contracts, tenancy agreements and compromises.

In *Perpetual Trustee Co Ltd v Khoshaba*,[92] Mr and Mrs Khoshaba, who were pensioners and members of the Assyrian community in Sydney, became aware that many members of the Assyrian community were investing in a trolley-collecting business operated by Karl Suleman Enterprizes Pty Ltd (KSE) and decided to invest in the scheme on the basis of promised high returns. In fact, the business operated as an illegal pyramid investment scheme. False information about Mr Khoshaba's income was submitted to the lender, although the trial judge found that the Khoshabas were not aware of this. The lender's own guidelines for assessing the loan application were not followed. In particular, the lender did not verify the employment and income position of the applicants, nor the full details of the purpose of the loan. Under the loan agreement, the lender lent the Khoshabas $120,000 and took a mortgage over their family home. Eventually the scheme collapsed, leaving the Khoshabas without the expected flow of revenue and with a debt to the lender. In the New South Wales Court of Appeal, Spigelman CJ (Handley and Basten JJA agreeing) held that the contract was unjust.

Basten JA considered that the borrowers' background, including the fact that English was their second language and that they had limited formal education and no business experience, was a disadvantage that, while not constituting a special disadvantage or disability for the purposes of equitable principles of unconscionable dealing, "was sufficient in the circumstances of the case to satisfy the requirement of the public interest in concluding that the asset-based lending in that case was unjust".[93] The Court held that the lender had been indifferent to the purpose of the loan and had been content to lend on the value of the security. In the case, the statement of purpose in the loan application was left blank and the lender made no inquiry about that purpose. The Court considered that the "indifference" shown by the lender to the purpose of the loan, which indicated that it was "content to proceed on the basis of enforcing the security".[94] Basten JA explained that:

90 *Lauvan Pty Ltd v Bega* [2018] NSWSC 154, [283] (Gleeson JA). See also *Perpetual Trustee Co Ltd v Khoshaba* (2006) 14 BPR 26,639, [128] (Basten JA); *Kowalczuk v Accom Finance Pty Ltd* (2008) 77 NSWLR 205, [102] (Campbell JA, Hodgson and McColl JJA agreeing); *Provident Capital Ltd v Papa* (2013) 84 NSWLR 231, [7] (Allsop P, Sackville AJA agreeing); *Tonto Home Loans Australia Pty Ltd v Tavares* (2011) 15 BPR 29,699, [270].

91 *Tonto Home Loans Australia Pty Ltd v Tavares* [2011] NSWCA 389, [291]; *Paciocco v Australia and New Zealand Banking Group Limited* [2015] FCAFC 50, (2015) 236 FCR 199, [296]; *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18, [14].

92 *Perpetual Trustee Co Ltd v Khoshaba* [2006] NSWCA 41.

93 *Perpetual Trustee Co Ltd v Khoshaba* [2006] NSWCA 41, [131].

94 *Perpetual Trustee Co Ltd v Khoshaba* [2006] NSWCA 41, [92] (Spigelman CJ).

> To engage in pure asset lending, namely to lend money without regard to the ability of the borrower to repay by instalments under the contract, in the knowledge that adequate security is available in the event of default, is to engage in a potentially fruitless enterprise, simply because there is no risk of loss. At least where the security is the sole residence of the borrower, there is a public interest in treating such contracts as unjust, at least in circumstances where the borrowers can be said to have demonstrated an inability reasonably to protect their own interests.[95]

An example of the application of the legislation outside the area of loan contracts is *Baltic Shipping Company v Dillon*.[96] In that case, the plaintiff took an ill-fated shipping cruise in which the ship struck a rock and sank. She sustained personal injuries, loss of personal effects and loss of a proportion of the cruise. She later signed a release in settlement of all possible claims against the shipping company. She accepted a payment of $4,786. The majority of the Court of Appeal held that the release was "unjust" under the *Contracts Review Act 1980* (NSW) and should be declared void, even though the plaintiff had received advice from a solicitor. The plaintiff settled her claim for less than one-tenth of what it was worth. There was material inequality of bargaining power between the parties and the plaintiff's capacity to protect her interests was diminished, owing to her physical and emotional condition. In addition, as Gleeson CJ noted, the defendant confronted the plaintiff with the prospect of potentially enormous litigation which subjected her to a form of pressure. Kirby P expressed the opinion that a contract could be unjust even though it was not produced by unfair conduct on the part of one of the parties. A contract may be "unjust" because of the peculiarities inherent in the circumstances of one of the parties, of which the other party may be quite ignorant.[97]

95 *Perpetual Trustee Co Ltd v Khoshaba* [2006] NSWCA 41, [128].

96 *Baltic Shipping Company v Dillon* (1991) 22 NSWLR 1.

97 *Baltic Shipping Company v Dillon* (1991) 22 NSWLR 1, 20. See further *West v AGC (Advances) Ltd* (1986) 5 NSWLR 610, 620.

VITIATING FACTORS: RESCISSION

PART XIC

[PtXIC.05] In Part XIA (Misinformation) and Part XIB (Abuse of Power), we considered various forms of pre-contractual misbehaviour that make it unfair for one party to hold another to a contract. These forms of misbehaviour are recognised as such under the general law (common law and equity) and under statute. In this part, we examine the remedy available to a party who is a victim of one or more of these forms of misbehaviour, which is the remedy of rescission.

CHAPTER **39**

Rescission

NATURE AND METHOD OF RESCISSION

[39.05] Rescission is a form of relief which, in appropriate circumstances, is available to victims of the following vitiating factors: mistake,[1] misrepresentation,[2] duress,[3] undue influence,[4] unconscionable dealing,[5] breach of fiduciary duty,[6] and under the rule in *Yerkey v Jones*.[7] Although the person claiming relief (the *victim*) may have suffered loss, it is not a requirement of the remedy of rescission that the victim suffer loss of a kind for which a pecuniary award may be made.[8]

Purpose and effect

[39.10] The purpose and effect of rescission, as traditionally understood, is to set aside the contract and restore the parties to their original pre-contractual positions.[9] Rescission effects a restitutio in integrum (restoration to the original position). For example, if a contract for the sale of goods is rescinded, the seller returns the purchase money to the purchaser and the

1 See Chapter 31. Note that in some instances of mistake the contract is *void*, rather than *voidable*, and the issue of rescission does not arise.
2 See Chapter 32.
3 See Chapter 34.
4 See Chapter 35.
5 See Chapter 36.
6 See [2.60] and [32.50].
7 *Yerkey v Jones* (1940) 63 CLR 649. see Chapter 37.
8 *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31, 32.
9 The nature of rescission is thoroughly explored in O'Sullivan, Elliott, Zakrzewski, *The Law of Rescission* (2nd ed, 2014).

purchaser returns the goods to the seller. Note that restitutio in integrum is also the aim of damages awarded to the victim of a tort.

A contract which is vulnerable to rescission is said to be *voidable*. This means it is valid until it is "avoided", "rescinded" or "disaffirmed". The victim *elects* whether or not to rescind. The effect of a valid election to rescind is to render the contract void ab initio (a nullity from the beginning).

Termination of contract distinguished

[39.15] Rescission must be carefully distinguished from termination for breach of contract. We have seen that termination of a contract for breach absolves the parties from future obligations.[10] In such a case, the contract may be said to be determined in futuro rather than ab initio. There is no discharge of rights and obligations that have already accrued or of causes of action arising from breach.

> When a contract is rescinded by reason of a recognised vitiating factor, the contract, as just noted, is set aside from the beginning. In such a case there can be no claim for damages for breach of contract, because in such situations there is no contract. Equally, if a claim is made by the victim for damages for breach of contract, there can be no rescission of the contract as the victim has by suing for breach clearly elected not to rescind.[11]

Who rescinds?

[39.20] The issue here is whether rescission is effected by act of the party or by the court. This matter is in dispute. There is authority to support the view that, in the case of fraudulent misrepresentation, rescission is recognised at common law and is effected by the *act of the party*. Equity's jurisdiction in such a case is "concurrent" and equity follows the law. The victim's title to property transferred under the rescinded contract is automatically restored by rescission, even though curial action may be required to retrieve possession of the property.

In *Alati v Kruger*,[12] a case in which a purchaser claimed rescission for fraudulent misrepresentation, the High Court stated:

> It is not that equity asserts a power by its decree to avoid a contract which the defrauded party himself has no right to disaffirm, and to revest property the title to which the party cannot affect. Rescission for misrepresentation is always the act of the party himself … The function of a court in which proceedings for rescission are taken is to adjudicate upon the validity of a purported disaffirmance as an act avoiding the transaction ab initio, and, if it is valid, to give effect to it and make appropriate consequential orders …[13]

At what point in time will the rescission be effective? This is relevant in determining whether substantial restoration of the parties to their pre-contractual positions is possible. In Helsham J's opinion in *Kramer v McMahon*:

> [W]here the rescinding act of a party to the contract does not for one reason or another bring about restitutio in integrum (and it is necessary to have an order of the court to bring this about) then rescission will not be effective unless the court through its powers can order that which the party was unable by his own powers to effect.[14]

10 See [24.30].

11 *Alati v Kruger* (1955) 94 CLR 216, 222.

12 *Alati v Kruger* (1955) 94 CLR 216.

13 *Alati v Kruger* (1955) 94 CLR 216, 224.

14 *Kramer v McMahon* [1970] 1 NSWR 194, 207.

In other words, although rescission on this view is the act of the party, the effectiveness of the rescission depends on the ability of either the party or the court (if necessary) to make the necessary restoration. If restoration can only be achieved with the aid of the court, then the possibility of restoration has to be determined *at the time of the court's order* and not at the time of the party's notice of rescission.

The view that it is always the party who rescinds in the case of fraudulent misrepresentation is difficult to maintain given that the High Court has claimed an equitable jurisdiction in cases of fraudulent misrepresentation to grant rescission *on terms* or to grant *partial rescission* only.[15] Given this development, rescission in such cases, if not generally, is more accurately described as a discretionary remedy granted by decree of the court. The problem is evident in *Alati v Kruger*, where the court says at one point that the "defrauded purchaser is regarded by a court exercising equitable jurisdiction as entitled to rescind the purchase and obtain a decree, on proper terms, declaring and giving effect to the rescission as an avoidance of the transaction from the beginning" and then goes on to assert that "the remedy is discretionary" and that if the purchaser "had acted unconscientiously during the pendency of the action … the court might refuse relief".[16]

Method of rescission

[39.25] In order to rescind, the victim must, as a general rule, communicate his or her intention to rescind to the other party. The rescission may be stated and communicated to the other party for the first time in a writ claiming relief based on the rescission.[17]

Notice will not always be required, however. Where the guilty party, by absconding, deliberately puts it out of the power of the victim to communicate an intention to rescind, the victim may evince an intention to rescind by some overt means falling short of communication. In *Car & Universal Finance Co Ltd v Caldwell*,[18] Caldwell was the victim of a fraudulent misrepresentation. He sold his car to a rogue whose cheque was dishonoured. He immediately informed the police and the Automobile Association and asked for their assistance in finding the car. The car was subsequently sold to an innocent purchaser. It was held that Caldwell had done enough in the circumstances to rescind the contract and so the innocent purchaser did not obtain title to the car. The contract was rescinded, and title revested in Caldwell, before the subsequent sale to the innocent purchaser.

A decision the other way would have been hard on owners such as Caldwell, as it would deprive them of the right to rescind whenever a rogue vanished. However, the result is hard on innocent third parties.[19] It is uncertain whether a court would take the same approach in the case of innocent misrepresentation or other vitiating factors.[20]

15 *Vadasz v Pioneer Concrete (SA) Pty Ltd* (1995) 184 CLR 102 and see [39.45].

16 *Alati v Kruger* (1955) 94 CLR 216, 225.

17 *Academy of Health and Fitness Pty Ltd v Power* [1973] VR 254, 256; *Alati v Kruger* (1955) 94 CLR 216, 222.

18 *Car & Universal Finance Co Ltd v Caldwell* [1965] 1 QB 525.

19 The English Law Reform Committee recommended that *Car & Universal Finance Co Ltd v Caldwell* [1965] 1 QB 525 be reversed by legislation: Twelfth Report (1966, Cmnd 2958), [16].

20 Such an approach is adopted in Victoria in respect of contracts for the supply of goods: *Australian Consumer Law and Fair Trading Act 2012* (Vic), s 26. This provision operates wherever a purchaser purports to discharge or rescind such a contract.

RESTITUTIO IN INTEGRUM

Common law and equity

Precise restoration and substantial restoration

[39.30] As far as the common law is concerned, rescission is only allowed in cases of fraud and certain instances of duress or where there is a total failure of consideration. Further, the common law only recognises rescission if *precise* restoration is possible. Equity, on the other hand, recognises rescission not only for fraud and duress (where it exercises a "concurrent jurisdiction" with the common law), but also for a wide variety of other vitiating factors, such as innocent misrepresentation, mistake, undue influence, breach of fiduciary duty and unconscionable dealing. In these instances, equity has an "exclusive" or "auxiliary" jurisdiction. Further, equity recognises rescission even though precise restoration is not possible, provided *substantial* restoration is possible. It can unravel the contract and restore the status quo ante the contract by appropriate decrees and orders.[21]

In *Alati v Kruger*,[22] a purchaser bought a fruit business for £700. The written contract of sale stated that the average takings of the business were £100 per week. This statement was a misrepresentation by the seller when the contractual document was presented to the purchaser for signature and became a term of the contract (a "warranty") after the buyer signed the document. It was a fraudulent statement, as in fact the business produced no more than £40 per week, as the seller well knew. The business was conducted on leasehold property, and the lease was assigned to the purchaser.

In these circumstances, the High Court pointed out that the purchaser had a choice of three courses open to him.[23] First, he could sue for damages for breach of contract (the warranty). However, he could not do this and rescind the contract for misrepresentation. Secondly, he could sue to recover as damages for deceit the difference between the price he had paid and the fair value of the property at the time of the contract. This again would involve affirming the contract. Thirdly, provided he could restore to the seller substantially what he had received under the contract, he could rescind the contract and claim his purchase money back with interest, together with damages (in deceit) for any loss he may have suffered through carrying on the business in the meantime. In other words, the purchaser could sue in deceit for damages whether he rescinded the contract or not, although the measure of damages would depend on whether the contract was rescinded.

In this case, the purchaser adopted the third option and rescinded the contract. The question for the court was whether this rescission was valid and the answer to that question depended on whether restitutio in integrum was possible at the commencement of the action.

The High Court held that restitutio in integrum was possible. Equity, unlike common law, demands only substantial, not precise, restoration of the parties to their original positions. In the case before the court, this solved a number of issues. First, although the purchaser had taken possession of the premises, in equity a money payment could compensate for any difference between the rental value of the premises and the rent paid by the purchaser. Secondly, the title to the lease would revest in equity when the purchaser elected to rescind

21 *Alati v Kruger* (1955) 94 CLR 216, 223.

22 *Alati v Kruger* (1955) 94 CLR 216.

23 *Alati v Kruger* (1955) 94 CLR 216, 222.

and he was in a position to make a legal re-assignment with the landlord's consent. Thirdly, although the purchaser had taken over stock and could not restore it to the seller, he could pay its value. Fourthly, although the business itself had deteriorated, this was not due to any fault on the purchaser's part. Even at common law, it was not necessary to return the property in its original condition if changes occurred as a result of the inherent nature of the property or by reason of the purchaser's exercise of contractual rights. Finally, the purchaser did not lose his right to a decree giving effect to the rescission by discontinuing the business and leaving the premises before judgment was given. If the purchaser had acted unconscientiously, the court might refuse relief. For example, if the purchaser had caused loss of goodwill and a valuable leasehold by abandoning the premises without giving the seller a reasonable opportunity to take them back, the court might have refused relief. Nothing of the kind happened. The seller knew the issues of fact had gone against him at the trial and could have applied to the court for the appointment of a manager to preserve the property. He did not offer to take the property back and offered no solution to the purchaser. The purchaser was not under a duty to go on indefinitely, working for nothing and incurring losses.

If property that is the subject matter of a contract has been wholly or substantially destroyed by the party seeking rescission, there can be no rescission.

> But where the property has been improved or deteriorated by the act of the purchaser, and yet remains in substance what it was before the contract, equity adjusts the rights of the parties by awarding money compensation to one or the other, and so substantially putting each party in the position which he occupied before the contract was made.[24]

Undue influence and breach of fiduciary duty

[39.35] Equity's reluctance to apply the principle of restitutio in integrum with much rigour is particularly evident in cases where the contract is voidable on the basis of undue influence or breach of fiduciary duty.[25] In *O'Sullivan v Management Agency and Music Ltd*,[26] the plaintiff was a highly successful composer and performer. Before he became successful, he had signed management and performing contracts with the defendants. These contracts were procured by undue influence. The defendants argued that it was not possible to rescind the contracts, which had been in operation for some years, as restitutio in integrum was not possible. The English Court of Appeal rejected this argument. Dunn LJ said:

> [T]he court can achieve practical justice between the parties by obliging the wrongdoer to give up his profits and advantages while at the same time compensating him for any work he had actually performed pursuant to the transaction.[27]

Accordingly, the court ordered that the contracts be set aside and the copyright in the plaintiff's compositions be reassigned to him. The court also ordered an account of profits and payment of the sum found due on the taking of the account. In taking the accounts, the defendants were entitled to an allowance for reasonable remuneration, including a profit element, for all the work done in promoting the plaintiff and his compositions. However, according to Fox LJ (with whom Dunn LJ agreed), the allowance for profit "would not be at all as much as the

24 *Brown v Smitt* (1924) 34 CLR 160, 164.

25 See also *Hartigan v International Society for Krishna Consciousness Inc* [2002] NSWSC 810, discussed at [39.65].

26 *O'Sullivan v Management Agency and Music Ltd* [1985] QB 428.

27 *O'Sullivan v Management Agency and Music Ltd* [1985] QB 428, 458.

defendants might have obtained if the contracts had been properly negotiated between fully advised parties".[28]

The award of an indemnity

[39.40] Equity also has jurisdiction to award an indemnity. This is significant in the context of innocent misrepresentation. We noted earlier that at common law rescission is not available for innocent misrepresentation. Damages cannot be awarded for a purely innocent misrepresentation, that is, one which is neither fraudulent nor negligent. Equity, on the other hand, allows rescission for innocent misrepresentation and can also, as just noted, award an indemnity. This means it can require a representor to indemnify a representee against obligations created by the contract. This to some extent alleviates the impact of the rule that no damages can be awarded at common law for a purely innocent misrepresentation.

On this issue, the High Court has stated:

> [P]utting the parties in the position they were in before the contract, replacing them in status quo, does not involve replacing them in the same position in all respects, but only in respect of the rights and obligations created by the contract which is rescinded. A party in case of rescission, cannot ask the court to award him compensation for all collateral losses which he may have sustained by reason of the fact that he entered into the contract, such as losses incurred in carrying on a business … but only such compensation as will restore the status quo ante in relation to the subject matter of the contract. Such losses could only be recovered in an action of [tort].[29]

In *Whittington v Seale-Hayne*,[30] the Whittingtons, who were poultry breeders, negotiated with Seale-Hayne with a view to leasing a property. It was innocently represented to them that the premises were in a thoroughly sanitary condition. They entered into a lease, erected several buildings and stocked the premises with poultry. However, the water supply became poisoned by the unsanitary state of the premises. The poultry died and the local council required the drains and house to be put in order. There was a clause in the lease requiring the tenant to execute work ordered to be performed by the local council.

The Whittingtons claimed rescission of the lease and indemnification against a number of expenses, including the value of the stock lost, loss of profits on sales, loss of the breeding season, medical expenses, removal of storage, rent paid, rates and cost of repairs. The court held that the plaintiffs were entitled on rescission to recover the rent, rates and cost of repairs required by the council, but not the other expenses. The lease did not oblige the tenants to move in and set up a poultry-breeding business.

Partial rescission

Vadasz v Pioneer Concrete

[39.45] If rescission is regarded as requiring at least the possibility of substantial restitutio in integrum, as it traditionally is in equity, then the notion of partial rescission sounds like a contradiction in terms. Nevertheless, partial relief from liability under a contract may be granted in the exercise of "equity's general jurisdiction, in setting aside contracts and other

28 *O'Sullivan v Management Agency and Music Ltd* [1985] QB 428, 459.

29 *Brown v Smitt* (1924) 24 CLR 160, 165–6. See further *Newbigging v Adam* (1886) 34 Ch D 582, 592–3; *JAD International Pty Ltd v International Trucks Australia Ltd* (1994) 50 FCR 378, 391–2.

30 *Whittington v Seale-Hayne* (1900) 82 LT 49.

dealings on equitable grounds, to ensure the observance of the requirements of good conscience and practical justice".[31]

In *Vadasz v Pioneer Concrete (SA) Pty Ltd*,[32] Vadipile was a company carrying on the business of a foundation piling contractor. Mr Vadasz and his wife were the only shareholders in the company and Vadasz was one of its two directors. Another company, Pioneer Concrete (SA) (Pioneer), manufactured ready-mixed concrete and supplied Vadipile with concrete. Vadipile owed Pioneer $200,000. Pioneer said it would continue to supply concrete to Vadipile on credit only if Vadasz provided Pioneer with a personal guarantee. Before he signed the guarantee, Vadasz was told that the guarantee would only cover future debts of Vadipile. The guarantee in fact provided, as Pioneer intended, for the payment of "all monies which are now or may at any time" be owing by Vadipile. Pioneer made further deliveries and Vadipile incurred further debts. Pioneer finally sued Vadasz on the guarantee for $357,427, representing the total indebtedness of Vadipile. Vadasz claimed the guarantee was vitiated by the misrepresentation. The High Court held, however, that the guarantee should be set aside only in so far as it related to existing debts. Vadasz was left liable to Pioneer for debts incurred after the guarantee was signed.

The High Court pointed out that, in this case, a practical restoration of the status quo ante the guarantee would have involved not only a cancellation of Vadasz's obligations under the guarantee, but also either a return of the concrete subsequently supplied to his company or the actual payment of an amount equivalent to the value of that concrete. Vadasz was not prepared to ensure that the concrete was paid for, but he nonetheless wanted to be relieved of his obligations under the guarantee. In these circumstances, the court invoked its general jurisdiction in setting aside contracts to ensure the observance of "practical justice" and "good conscience" for both parties. This allowed for a partial rescission; that is, a rescission limited to the setting aside of the obligation to guarantee existing debts.

Two reasons were given in justification. First, it could not be maintained that Vadasz would not have entered into the guarantee had it been confined to the future indebtedness of Vadipile. On the contrary, the evidence was that he would have done so if only to ensure future supplies of concrete. In other words, this was a case where the victim would have accepted some part of the transaction even in the absence of any wrongdoing by the other party. The court said that in *Commercial Bank of Australia Ltd v Amadio*,[33] the reason why the mortgage was not set aside, only to the extent that it involved a liability in excess of $50,000 (the figure the Amadios thought represented the limit of their guarantee), was that the Amadios would not have entered the transaction at all had they known the true financial situation of their son.

Secondly, if Vadasz were given complete relief from obligations under the guarantee, he would enjoy the benefits of the transaction (the supply of concrete to his company) without accepting its burdens (the cost of that supply). The notion of unconscionability, the Court said, provides a justification not only for the setting aside of a transaction, but also for not setting it aside in its entirety or for doing so subject to conditions "so as to prevent one party obtaining an unwarranted benefit at the expense of the other".[34] Whoever seeks equity, the court affirmed, must do equity.

31 *Vadasz v Pioneer Concrete (SA) Pty Ltd* (1995) 184 CLR 102, 112.

32 *Vadasz v Pioneer Concrete (SA) Pty Ltd* (1995) 184 CLR 102.

33 *Commercial Bank of Australia Ltd v Amadio* (1983) 151 CLR 447, 481, discussed at [36.15].

34 *Vadasz v Pioneer Concrete (SA) Pty Ltd* (1995) 184 CLR 102, 114.

The High Court's judgment in *Vadasz* introduced a novel equitable remedy. It goes beyond the setting aside of contracts on terms.[35] It is somewhat analogous to rectification for unilateral mistake.[36] It has been interpreted in subsequent cases as authority for the following principle:[37]

1. Where a case has been made out for a contract to be set aside in equity, the court must consider what would have happened in the absence of the vitiating factor.
2. The court should set the contract aside in its entirety only if, had it not been for the vitiating factor, the victim would not have entered into the contract at all.
3. If the victim would have accepted some obligation in the absence of the vitiating factor, then partial rescission should be granted and the victim held to that obligation.

Will this principle be applied to other instances of misconduct when the equitable remedy of rescission is available? The High Court has stated that "the scope of the equity for rescission may be determined by the nature and extent of the conduct giving rise to the equity for rescission".[38] It is not immediately clear that the scope of the equity for fraudulent misrepresentation should be different from that for innocent misrepresentation, duress, undue influence, unconscionable dealing, unilateral mistake or the rule in *Yerkey v Jones*.[39] However, the High Court held in *Maguire v Makaronis*[40] that partial rescission is not an appropriate form of relief for breach of fiduciary duty. Breach of such a duty automatically generates an equity to have the whole contract rescinded.

Outstanding issues

[39.50] *Vadasz v Pioneer Concrete (SA) Pty Ltd*[41] raises a number of issues. First, it adopts an approach that is inconsistent with the commonly held view that in cases of fraudulent misrepresentation, the right to rescind is vested solely in the representee.[42] On this view, the common law recognised the right of a victim of fraudulent misrepresentation to rescind a contract and, in such an instance, equity's jurisdiction was concurrent. Equity would follow the law in affirming or denying the validity of the act of rescission, although it was more accommodating in recognising the possibility of restitutio in integrum. On the other hand, where equity had "exclusive" jurisdiction, such as in the case of innocent misrepresentation, rescission would be effected not by the representee but by the decree of the court. Such a decree is granted at the court's discretion and, in appropriate cases, on terms. The *Vadasz* ruling apparently rejects this dichotomy and reflects a more flexible approach to equitable relief in cases of fraudulent misrepresentation. Equity may by its own decree, and in its own

35 See, eg, *Solle v Butcher* [1950] 1 KB 671, discussed at [31.100]; and *O'Sullivan v Management Agency and Music Ltd* [1985] QB 428, discussed at [39.35].

36 See [31.160].

37 *Australia and New Zealand Banking Group Ltd v Petrik* [1996] 2 VR 638; *Cockerill v Westpac Banking Corporation* (1996) 142 ALR 227, 286–7; *NZI Capital Corporation Ltd v Poignand* [1997] ATPR 41-586, 44,098–44,099.

38 *Maguire v Makaronis* (1997) 188 CLR 449, 472.

39 Note that in *Vadasz v Pioneer Concrete (SA) Pty Ltd* (1995) 184 CLR 102 the High Court expressly left undecided the question whether the misrepresentation in that case was fraudulent.

40 *Maguire v Makaronis* (1997) 188 CLR 449, 472.

41 *Vadasz v Pioneer Concrete (SA) Pty Ltd* (1995) 184 CLR 102.

42 See O'Sullivan, "Partial Rescission for Misrepresentation in Australia" (1997) 113 *Law Quarterly Review* 16.

discretion, effect rescission, assessing the rights of litigants according to standards of practical justice and good conscience.

A second issue arising out of *Vadasz v Pioneer Concrete (SA) Pty Ltd* relates to the court's emphasis on the question: What would the representee have done in the absence of the misrepresentation? Would the representee have accepted any part of the transaction? This test raises, at the remedial stage, a question of causation that is inconsistent with the well-established approach to causation at the earlier stage of establishing an entitlement to relief on the basis of a fraudulent misrepresentation.[43] We have seen that, at the stage of establishing an entitlement to relief, the court considers only whether the misrepresentation contributed to the innocent party's decision to enter into the contract.[44] If it did, it is not relevant to ask what would have happened "but for" the misrepresentation. The same reasoning is applicable in establishing an entitlement to relief on the basis of duress.[45] The reason we cannot generally be sure what the innocent party would have done in the absence of the misrepresentation or the duress is that the wrongdoer has engaged in misconduct. A wrongdoer should not be able to speculate on what might have happened had it not been for his or her misconduct. By asking questions of this kind at a remedial level, the innocent party's entitlement is thrown into doubt. If the facts of *Barton v Armstrong*[46] occurred today, the result might be different. This is because the victim might well have signed the deed even if the wrongdoer had not threatened to have him murdered.

A third problem arising out of *Vadasz v Pioneer Concrete (SA) Pty Ltd* relates to the Court's emphasis on the fact that Vadasz had received a benefit from the transaction with Vadipile through the continued supply of concrete.[47] If this means some tangible *objective* benefit, like money or saleable property, there appears to be no convincing evidence in the case that Vadasz himself received any such benefit. If tangible benefit is the basis of partial rescission, it would need to be more carefully investigated.

On the other hand, benefit might mean subjective benefit to the victim, such as the lending of money to a third person. In this sense, Vadasz certainly received a benefit (goods delivered on credit to his company as he intended), just as the Amadios did (financial accommodation to their son as they intended). The question of such benefit is linked to the "but for" question, because that latter question helps us to identify the value the victim put on the conferral of benefit on the third person. Since Vadasz was prepared to guarantee future debts of Vadipile, he apparently valued the delivery of concrete to it at the price it agreed to pay Pioneer. This principle works well in a case like *Vadasz v Pioneer Concrete (SA) Pty Ltd*, because it involved a misrepresentation as to terms of a contract. It was easy to say what obligations Vadasz would have accepted had there been no misconduct and thereby identify the value he placed on the continued supply of concrete to Vadipile. In other cases of misconduct, it would be a matter of speculation what value the victim would have put on the conferral of a benefit on a third person. As discussed earlier in this chapter, a wrongdoer should not be entitled to speculate on what might have happened had there been no wrongdoing.

43 Robertson, "Partial Rescission, Causation and Benefit" (2001) 17 *Journal of Contract Law* 163, 168–75.

44 *Gould v Vaggelas* (1985) 157 CLR 215, discussed at [32.95].

45 *Barton v Armstrong* [1976] AC 104, discussed at [34.35].

46 *Barton v Armstrong* [1976] AC 104, discussed at [34.35].

47 See Robertson, "Partial Rescission, Causation and Benefit" (2001) 17 *Journal of Contract Law* 163, 176–9.

BARS TO RESCISSION

[39.55] Apart from impossibility of substantial restoration of the parties to their original positions, there are a number of specific bars to rescission. In some jurisdictions, the law relating to these matters has been changed or clarified by statute. Some bars have all but atrophied.[48]

Affirmation

[39.60] When a contract is voidable by reason of a vitiating factor, the victim of the relevant misconduct must elect whether to avoid or affirm the contract.[49] Generally, notice of avoidance or affirmation must be given to the other party.[50] This may be done expressly or impliedly by conduct that clearly manifests the relevant intention.[51] Words and conduct ordinarily required to constitute an election must be unequivocal in the sense that they are consistent only with the exercise of one of two sets of rights and are inconsistent with the exercise of the other.[52] An election, once made, is irrevocable.

Affirmation will not be inferred where the victim's knowledge or independence is still impaired by the vitiating factor, such as where duress or undue influence is still operative or the victim has not yet been apprised of the falsity of misrepresented facts. A party seeking to establish a case of affirmation must prove that, after the disabling effect of his or her misconduct was dispelled, the other party either elected not to avoid the contract or became estopped from asserting his or her right to avoid the contract.[53]

What if the victim has been freed of any improper pressure and apprised of relevant facts but does not know of the right to rescind?[54] One view is that knowledge of the right to rescind is not a necessary condition of an effective election. In *Re Hoffman*,[55] Pincus J said that knowledge of the facts giving rise to the right to elect is all that need to be proved. His Honour preferred to apply this principle, even in fraud cases, because it:

1. accorded with the general rule as to the relevance of knowledge of the law;
2. removed the necessity of an awkward examination, in many cases, of what legal advice had been received;
3. had the virtue of simplicity; and
4. did not altogether deprive the defrauded party of a remedy, as damages remained available.

48 For a critical examination of the bars to rescission and a recommendation that that a new scheme of "pecuniary rescission" be substituted, see Nahan, "Rescission: A Case for Rejecting the Classical Model?" (1997) 27 *University of Western Australia Law Review* 66.

49 The same election arises following a serious breach of contract: see [24.05].

50 Notice of avoidance may not be necessary if the wrongdoer has absconded: see [39.25].

51 See, eg, *North Ocean Shipping Co Ltd v Hyundai Construction Co Ltd* [1979] QB 705, discussed at [34.45].

52 *Sargent v ASL Developments Ltd* (1974) 131 CLR 634, 656, 646.

53 *Hawker Pacific Pty Ltd v Helicopter Charter Pty Ltd* (1991) 22 NSWLR 298, 304–5, 306–8.

54 This question is also raised in the contexts of the right to terminate a contract for breach and for non-fulfilment of a condition. See [25.55].

55 *Re Hoffman* (1989) 85 ALR 145. See further *Molotu Pty Ltd v Solar Power Ltd* (1989) NSW Conv R 55-490, 58,565.

The opposing view was adopted in *Coastal Estates Pty Ltd v Melevende*,[56] where Adam J said:

> Because the making of an election necessarily presupposes a knowledge that a choice between alternative courses is open, in general, no question of affirmation can arise in the absence of such knowledge. There appears, however, to be one important qualification upon this. If a representee, after discovery of the facts which entitle him to avoid a contract, exercises, in an unequivocal manner, rights under the contract adversely to the other party, he will in general be deemed to have elected to affirm it, although not aware of his right to elect.[57]

Sholl J, in the same case, gives the example of a purchaser of land, who, knowing of the vendor's misrepresentation, enters into possession of the property or accepts some other benefit from the vendor. This could be regarded as an exercise of rights adversely to the other party. But payments to the vendor, or payment of rates or negotiation for resale, would not.[58]

In *Hawker Pacific Pty Ltd v Helicopter Charter Pty Ltd*,[59] Priestley JA suggested that where election does not apply because the party with the right of election is ignorant of that right, an estoppel may operate. The party with the right of election may act in such a way as to represent to the other party that the contract was being affirmed and the other party may act in detrimental reliance on that representation. In the case before the court, a helicopter owner signed a contract under duress of goods.[60] There was a period following the contract in which the helicopter owner fobbed off the other party in respect of moneys owing under the contract. The court held that nothing that was done during the fobbing-off period had deprived the helicopter owner of its right to avoid the contract as it had not affirmed, nor was it estopped from asserting its right to avoid, the contract.

A person who has an election is not bound to elect immediately but may keep the question open so long as the delay does not cause prejudice to the other party. Affirmation may be inferred from lapse of time, but it is doubtful whether mere lapse of time is itself an independent bar to rescission. Delay as such will not be a bar to relief in equity; rather, it is relevant to the court's exercise of discretion.[61] The term "laches" in equity connotes delay of such a kind that, standing by itself or in association with other facts, it renders the granting of relief inequitable.[62] A court considers the length of time and the nature of any acts and events occurring in the interval. When a contract concerns a disposition of an interest in property of a fluctuating kind, such as shares in a company, greater expedition is appropriate than might otherwise be the case.[63]

Intervening third-party rights

[39.65] Rescission has traditionally been barred where a bona fide third party has acquired rights in the subject matter of a voidable contract. We have seen that a voidable contract stands until it is avoided. This means that the purchaser of goods who obtains those goods by

56 *Coastal Estates Pty Ltd v Melevende* [1965] VR 433.

57 *Coastal Estates Pty Ltd v Melevende* [1965] VR 433, 453.

58 *Coastal Estates Pty Ltd v Melevende* [1965] VR 433, 443.

59 *Hawker Pacific Pty Ltd v Helicopter Charter Pty Ltd* (1991) 22 NSWLR 298.

60 See [34.40].

61 *JAD International Pty Ltd v International Trucks Australia Ltd* (1994) 50 FCR 378, 387–8.

62 *Whereat v Duff* [1972] 2 NSWLR 147, 179–80.

63 *Barburin v Barburin* [1991] 2 Qd R 240.

misconduct, such as misrepresentation, duress or breach of fiduciary duty, obtains a voidable title. If that wrongdoer sells the goods to an innocent third party, before the contract is rescinded by the original victim, a good title passes. This means that restitutio in integrum between the original parties is impossible, and rescission has been held to be barred on this basis.[64] However, if the original victim rescinds the contract before the third party purports to buy the goods,[65] or if the original contract is void ab initio,[66] or if the purchaser is not bona fide, no title passes to the third party. This means the third party must return the goods to the original victim or pay damages for conversion.

Rescission of a contract may be allowed despite the intervention of third party rights in the subject matter of the contract if, by making ancillary orders, the court can ensure that the rescission does not cause injustice or loss to the third parties.[67] A more basic solution is to allow "pecuniary rescission" between the original parties.[68] In *Hartigan v International Society for Krishna Consciousness Inc*,[69] the plaintiff donated a rural property to the defendant in circumstances raising a presumption of undue influence, which the defendant was unable to rebut. The property was sold by the defendant before the plaintiff sought rescission and the proceeds used to reduce the defendant's indebtedness to a bank. The defendant argued that the plaintiff should be denied rescission on the ground that, the property having been sold by the defendant, restitutio in integrum was no longer possible.[70] Bryson J held that the remedies are available for undue influence:

> are not limited to remedies against specific assets; while specific assets will be restored if they still exist and can be identified, personal remedies are available against a donee which itself directly received the property from the donor.[71]

Bryson J held that the appropriate remedy was to order the defendant to pay to the plaintiff an amount equal to the proceeds of sale of the farm.[72]

Executed contracts

[39.70] A contract for the sale of land that is induced by a misrepresentation, and has been completed by a conveyance of the land, cannot be rescinded unless the misrepresentation is fraudulent. In other words, innocent misrepresentation (or common mistake) will not suffice as a basis for rescinding such an executed contract. The founding English authority for this rule is *Wilde v Gibson*,[73] and the rule has been adopted in Australia.[74] "Absent fraud, equity

64 *White v Garden* (1851) 10 CB 919; 138 ER 364. See also *McKenzie v McDonald* [1927] VLR 134, discussed at [32.50]; and *Lewis v Averay* [1972] 1 QB 198, discussed at [31.140].

65 See *Car & Universal Finance Co Ltd v Caldwell* [1965] 1 QB 525, discussed at [39.25].

66 *Cundy v Lindsay* (1878) 3 App Cas 459 and *Shogun Finance Ltd v Hudson* [2003] UKHL 62; [2004] 1 AC 919, discussed at [31.135].

67 *Water Motors Pty Ltd v Cratchley* (1963) 80 WN (NSW) 1165, 1177.

68 See Nahan, "Rescission: A Case for Rejecting the Classical Model?" (1997) 27 *University of Western Australia Law Review* 66.

69 *Hartigan v International Society for Krishna Consciousness Inc* [2002] NSWSC 810.

70 *Hartigan v International Society for Krishna Consciousness Inc* [2002] NSWSC 810, [25].

71 *Hartigan v International Society for Krishna Consciousness Inc* [2002] NSWSC 810, [98].

72 *Hartigan v International Society for Krishna Consciousness Inc* [2002] NSWSC 810, [104].

73 *Wilde v Gibson* (1848) 1 HL Cas 605; 9 ER 897.

74 See *Svanosio v McNamara* (1956) 96 CLR 186, discussed at [31.100].

would not order rescission of the contract of sale after conveyance."[75] The rationale of the rule is that the purchaser has the fullest opportunity to investigate title and conduct surveys of the land so that the vendor's representations can be tested.

Unfortunately, the rule (redefined as "no rescission for executed contracts induced by innocent misrepresentation") has been applied to contracts other than contracts for the sale of land. This is unfortunate for two reasons. First, the rationale for the rule does not apply to such other contracts. Secondly, it is often not clear what is meant by "executed" when applying the rule to such other contracts.

The rule has been applied to a contract for the sale of shares,[76] a lease[77] and the sale of a business.[78] When it has not been applied, the usual point of distinction is that the contract is "executory", rather than "executed". For this purpose, the courts have been keen to find "ongoing obligations" in the contractual relationship. On this basis, the rule has not been applied to a contract for the allotment of shares,[79] the purchase of shares in a business where the purchaser became partners with the seller in that business[80] and a hire-purchase contract.[81] The rule has also been held not to apply to contracts where the parties are in a fiduciary relationship.[82]

In other cases, the rule has simply not been followed. It was neither followed by Helsham CJ in *Leason Pty v Princes Farm Pty Ltd*[83] (sale of a horse), nor by Young J in *Baird v BCE Holdings Pty Ltd*[84] (transfer of shares), nor by Lord Denning in *Solle v Butcher*[85] (lease). Even the original rule may not be read so strictly today. When it is said that a contract for the sale of land can be set aside for fraud, "fraud" may be given its wide equitable meaning, including "unconscionable dealing".[86]

The extension of the original rule to cases other than the sale of land has been widely and effectively criticised by judges and commentators alike for decades.[87] Legislative reform or clarification was called for and has already taken place in some jurisdictions. Rescission of an executed contract for innocent misrepresentation is allowed in South Australia[88] and the Australian Capital Territory.[89] Similar reforms have taken place in Victoria in respect of contracts for the supply of goods[90] and in New South Wales in respect of sales of goods.[91]

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75 *Krakowski v Eurolynx Properties Ltd* (1995) 183 CLR 563, 585.

76 *Seddon v The Northern Eastern Salt Company Pty Ltd* [1905] 1 Ch 326.

77 *Angel v Jay* [1911] 1 KB 666.

78 *Vimig Pty Ltd v Contract Tooling Pty Ltd* (1986) 9 NSWLR 731.

79 *Grogan v "The Astor" Ltd* (1925) 25 SR (NSW) 409.

80 *Senanayake v Cheng* [1966] AC 63.

81 *Mihaljevic v Eiffel Towers Motors Pty Ltd and General Credits Ltd* [1973] VR 545.

82 *Armstrong v Jackson* [1917] 2 KB 822.

83 *Leason Pty v Princes Farm Pty Ltd* [1983] 2 NSWLR 381.

84 *Baird v BCE Holdings Pty Ltd* (1996) 40 NSWLR 374.

85 *Solle v Butcher* [1950] 1 KB 671, discussed at [31.100].

86 See [31.100].

87 See, eg, Hammelmann, "Seddon v North Eastern Salt Co" (1939) 55 *Law Quarterly Review* 90; MacFarlane and Willmott, "Rescission of an Executed Contract at Common Law for an Innocent Misrepresentation" (1998) 10 *Bond Law Review* 58.

88 *Misrepresentation Act 1971* (SA), s 6(1).

89 *Civil Law (Wrongs) Act 2002* (ACT), s 173(1)(b)(ii).

90 *Australian Consumer Law and Fair Trading Act 2012* (Vic), s 24.

91 *Sale of Goods Act 1923* (NSW), s 4(2A)(b).

Sale of goods

[39.75] There has been some doubt as to whether the equitable jurisdiction to rescind for innocent misrepresentation applies to sales of goods. One view is that there never was any such jurisdiction and that there is a provision in the *Sale of Goods Acts* which is declaratory of that state of the law. The provision is to this effect:

> The rules of the common law … and in particular the rules relating to the law of principal and agent and the effect of fraud misrepresentation, duress, or coercion, mistake, or other invalidating cause, shall continue to apply to contracts for the sale of goods.[92]

Even if rescission was available prior to this legislative provision, there is an argument that the reference to "common law" means common law in its technical sense, that is, as distinct from "equity". As the common law does not allow rescission for innocent misrepresentation, this means there is no such remedy for the sale of goods.

There is a decision of the Full Supreme Court of Victoria that adopts the view that the rules of equity in regard to misrepresentation never applied to contracts for the sale of goods and that "common law" in the legislative provision has a narrow connotation.[93]

The argument against this view is strong. First, the historical point is contentious and may be a misreading of the law as it stood when the original English *Sale of Goods Act 1893* (UK) was passed in 1893.[94] Secondly, the narrow reading of "common law" is doubtful. The Act is not a code as it does not purport to deal exhaustively with every aspect of sale of goods; for example, specific performance is not covered. The phrase "common law" arguably means "common law as distinct from statutory law" and therefore includes "equity". The section distinguishes "misrepresentation" from "fraud". But at common law, innocent misrepresentation did not render a contract voidable; therefore, the reference must be to the rules of equity. Further, there would be no remedy at all for an innocent misrepresentation that was not incorporated into the contract if the narrow view prevailed.

There is a decision of the Full Supreme Court of South Australia, *Graham v Freer*,[95] and other cases, that support the view that rescission of contracts for the sale of goods for innocent misrepresentation is available.[96] This is undoubtedly the better conclusion.

Rescission of contracts for the sale of goods for innocent misrepresentation is expressly permitted in New South Wales[97] and Victoria[98] by virtue of statutory reform.

Incorporation of representation in contract

[39.80] It has been said that when an innocent misrepresentation becomes a term of the contract, the representee is restricted to the *contractual* rights that thereby arise (that is, damages for breach of warranty or termination for breach of condition) and cannot rescind in

92 *Sale of Goods Act 1954* (ACT), s 62(1); *Sale of Goods Act 1923* (NSW), s 4(2); *Sale of Goods Act* (NT), s 4(2); *Sale of Goods Act 1896* (Qld), s 61(2); *Sale of Goods Act 1895* (SA), s 59(2); *Sale of Goods Act 1896* (Tas), s 5(2); *Goods Act 1958* (Vic), s 4(2); *Sale of Goods Act 1895* (WA), s 59(2).

93 *Watt v Westhoven* [1933] VLR 458.

94 See Greig and Davis, *The Law of Contract* (1987), p 881.

95 *Graham v Freer* (1980) 35 SASR 424.

96 *Goldsmith v Rogers* [1962] 2 Lloyd's Rep 249; *Leaf v International Galleries* [1950] 2 KB 86.

97 *Sale of Goods Act 1923* (NSW), s 4(2A).

98 *Australian Consumer Law and Fair Trading Act 2012* (Vic), s 24.

equity for misrepresentation.[99] Historically, equity intervened because the common law gave no remedy at all for an innocent misrepresentation that was not incorporated in the contract.

Why should the equitable right be lost merely because the representation is incorporated in the contract? It seems odd that the more drastic remedy of setting the contract asunder is available when the representation is not a term. In *Academy of Health and Fitness Pty Ltd v Power*,[100] Crockett J held in respect of a written contract relating to the use of the facilities of a health studio that the party induced to enter into it by an innocent misrepresentation did not lose the equitable right to rescind by reason of the representation having become a term of the contract that was at no time more than a warranty.[101]

This approach has been confirmed by statute in South Australia[102] and the Australian Capital Territory.[103] There is further statutory confirmation in respect of the sale of goods in New South Wales[104] and in respect of contracts for the supply of goods in Victoria.[105]

Exclusion clauses

[39.85] When a representee is claiming rescission in respect of a misrepresentation, a non-fraudulent misrepresentor may be protected against such a claim by an exclusion or limitation clause in the contract.[106] A clause may say, for example, that the representee has not relied on any pre-contractual statement.[107] In South Australia and the Australian Capital Territory, however, legislation provides that an exclusion or limitation clause in this context may be relied upon only if the court considers it "fair and reasonable in the circumstances" to do so.[108]

Statutory curtailments

[39.90] In South Australia and the Australian Capital Territory, in the case of a wholly innocent misrepresentation, where the representor had reasonable grounds for believing the representation was true, the court may, notwithstanding the representee's right to rescind, declare the contract subsisting and award damages. This discretion may be exercised by the court when it considers it reasonable and just to do so in the circumstances of the case.[109]

Under the *Insurance Contracts Act 1984* (Cth), there is an automatic right of rescission only in respect of certain fraudulent misrepresentations made by the insured. In other cases of misrepresentation, the insured's benefits are subject to reduction.[110] Even in the case of

99 The victim of a fraudulent misrepresentation is clearly not so restricted: *Alati v Kruger* (1955) 94 CLR 216, discussed at [39.30].

100 *Academy of Health and Fitness Pty Ltd v Power* [1973] VR 254.

101 See also *Simons v Zartom Investments Pty Ltd* [1975] 2 NSWLR 30, 36.

102 *Misrepresentation Act 1971* (SA), s 6(1)(a).

103 *Civil Law (Wrongs) Act 2002* (ACT), s 173.

104 *Sale of Goods Act 1923* (NSW), s 4(2A)(a).

105 *Australian Consumer Law and Fair Trading Act 2012* (Vic), s 24(2).

106 For exclusion clauses generally, see Chapter 13.

107 See *Byers v Dorotea Pty Ltd* (1986) 69 ALR 715.

108 *Misrepresentation Act 1971* (SA), s 8; *Civil Law (Wrongs) Act 2002* (ACT), s 176.

109 *Misrepresentation Act 1971* (SA), s 7(3); *Civil Law (Wrongs) Act 2002* (ACT), s 175.

110 *Insurance Contracts Act 1984* (Cth), s 28.

fraudulent misrepresentation, the court may disregard a rescission if it would be harsh and unfair not to do so.[111]

IS RESCISSION FOR INNOCENT MISREPRESENTATION JUSTIFIED?

[39.95] The reason for allowing rescission for fraudulent misrepresentation is clear. To allow a fraudster to retain the benefit he or she has obtained by virtue of a deliberate deceit would be to permit the continuation of the same deceit.[112] From an economic point of view, it is inefficient to encourage a cheat to invest resources in misleading the other party as the resources could be put to more productive use. The cheat makes gains from trade when the victim cannot assess the value of the contract.

What, then, is the reason for allowing rescission for innocent misrepresentation? Equity provides relief against various kinds of unconscionable behaviour. It is unconscionable for a representor to seek to retain a benefit, once the falsity of the representation has been exposed. In *Redgrave v Hurd*,[113] Jessel MR spoke of the "moral fraud" and "moral delinquency" of a person who seeks to take advantage of a contract induced by a statement made by that person and now known to be false.[114] However, another reason he gave as justification for equity's intervention was that a person who innocently makes a false statement ought to find out the truth of the matter before making the statement. This element of carelessness reinforces, and possibly explains, the moral delinquency argument. Jessel MR, it appears, was concerned to censure careless conduct.

Duggan has provided a useful economic explanation of equity's intervention in granting relief against innocent misrepresentation.[115] He points out that to say that a representor should have been more careful implies the existence of two conditions: first, that there were economic means available for discovering the truth; secondly, that it was cheaper for the representor to investigate the matter, rather than the representee. It is reasonable to assume that in most cases both these conditions will be met.

This analysis justifies rescission where the representor has been careless in the sense described. But what if the representor has not been careless in that sense? Duggan argues that the rule discourages carelessness in a secondary sense. It acts as an incentive to representors to be more circumspect in cases where they cannot be sure of their information. This they can do by making a disclaimer. Such a disclaimer will indicate to the representee either that there are no economical means available to discover the truth or that it would be cheaper for the representee to undertake the investigations. The risk of loss if the statement turns out to be untrue is thereby transferred to the representee, who must decide whether to proceed or not and, if so, on what terms or at what cost. The result is a minimisation of the risk of mistake.

Although the equitable rule allowing rescission for innocent misrepresentation is a rule of strict liability, representors can "opt out" of the rule by contracting around it in the manner suggested. The alternative is to have a no-liability rule for innocent misrepresentors, leaving

111 *Insurance Contracts Act 1984* (Cth), s 31.

112 Greig and Davis, *The Law of Contract* (1987), p 866.

113 *Redgrave v Hurd* (1881) 20 Ch D 1, discussed at [32.95].

114 *Redgrave v Hurd* (1881) 20 Ch D 1, 13.

115 Duggan, "Misrepresentation" in Parkinson (ed), *The Principles of Equity* (2nd ed, 2003), [605]–[606]; Duggan, "Is Equity Efficient?" (1997) 113 *Law Quarterly Review* 601, 606–9.

the representor to "opt in" to liability by contracting to guarantee the truth of the statement. It is true that both "opting in" and "opting out" inevitably involve transaction costs for the parties, but the aim of the law should be to minimise those costs. It does this by choosing a rule that represents the majority-preferred position. As the majority of parties would probably prefer an opt-out scheme, that scheme is likely to be the cheaper one.

So Duggan concludes that the equitable rule of strict liability for innocent misrepresentation in respect of rescission is an efficient rule. It is efficient because, in the normal case, the information relevant to test the truth of the representor's statement is likely to be accessible to the representor at lower cost than it would be to the representee.

VITIATING FACTORS: ILLEGALITY

PART XID

[PtXID.05] The topic of illegality is quite complex and challenging. The following overview of the main issues raised in this part of the book is offered to assist the reader.

Illegal contracts

[PtXID.10] In the interests of the community as a whole, the law exercises a certain degree of control over the subject matter and aims of contracts. This means that there are limits to what parties can legally agree to do or refrain from doing and to what objectives they may seek to achieve through contractual ventures.

In *Nelson v Nelson*,[1] Deane and Gummow JJ identified three ways in which a contract may be void for illegality. First, the making of a contract may be expressly prohibited by statute. Secondly, the making of a contract may be impliedly prohibited by statute if its formation or performance involves conduct prohibited by statute. Finally, even if a contract is not expressly or impliedly prohibited by statute it may nevertheless be invalid at common law if it offends "public policy". As Kirby J noted in *Fitzgerald v F J Leonhardt Pty Ltd*:

> [i]t is important to keep the interpretation and public policy questions separate. Logically, the interpretation question arises first. This is because if, as a matter of interpretation, the contract is illegal … it is void as to those parts affected by illegality. The secondary question of unenforceability for public policy reasons does not then arise.[2]

Contracts prohibited by statute

[PtXID.15] Contracts prohibited by statute are considered in detail in Chapter 40. As noted above, such statutory prohibition may be express or implied. As Gibbs ACJ stated in *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd*, the "question whether a statute … intends to vitiate a contract made in breach of its provisions, is one which must be determined in accordance with the ordinary principles that govern the construction of statutes".[3] The factors the court takes

1 (1995) 184 CLR 538.
2 (1997) 189 CLR 215, 245.
3 (1978) 139 CLR 410, 413.

into account when determining whether a statute expressly or impliedly prohibits a contract are considered in Chapter 40.

Moreover, a contract can be held illegal at common law (and therefore in the third category below) as a contract to commit a statutory crime. It should be noted that the classification of a contract as prohibited by statute, rather than by common law, has few if any, legal ramifications unless the statute actually lays down particular legal consequences in respect of contracts that violate its provisions.

Contracts prohibited at common law

[PtXID.20] Even if a contract is not prohibited by statute, it may nevertheless be void for illegality. Notwithstanding varying degrees of judicial support for a philosophy of freedom of contract, for centuries the common law courts have refused to enforce contracts that are against "public policy". To take an extreme example, a contract between A and B under which B agrees for $100,000 to murder C may be perfectly fair and balanced as between A and B, but obviously our law would not countenance such a nefarious contract. Any principle of freedom of contract must give way in appropriate circumstances to a collectivist principle – the dictates of "public policy".

The general philosophy underlying common law illegality may be summed up in the old maxim *ex turpi causa non oritur actio* (no action arises from a base cause). Another rendering is *ex dolo malo non oritur actio*.[4] The notion of a "base" or "unworthy" cause, whether it is expressed in English or Latin, is too broad and vague to be of much practical use. It is a background idea. And yet to be more specific is difficult. When considering whether to refuse to enforce a contract on the grounds of public policy, the courts are balancing a desire to uphold bargains against concerns associated with aiding the enforcement of agreements associated with illegal activity.

Public policy is concerned with basic community standards. Contracts which violate judicially recognised community standards are prohibited at common law. Contracts of this kind are considered in detail in Chapter 41. Examples for consideration include contracts to commit a crime or a tort, contracts which prejudice the administration of justice, contracts which promote corruption in public life, contracts promoting sexual immorality, contracts imposing servitude, contracts to defraud the revenue and contracts to breach the laws of a foreign country. Such contracts have generally been described as "illegal". That adjective seems appropriate in most of the examples, given the degree of turpitude attaching to the breach of relevant community standards. However, it should be noted that public policy changes. What was regarded as against public policy, or as base, at one time may not be so regarded at another time.

Certain other contracts have been seen by the courts as less offensive to public policy and often only offensive in respect of one particular term. Such contracts or terms are generally, but not consistently, described as "void", rather than "illegal". An example is a clause seeking to oust the jurisdiction of the courts. Covenants in unreasonable restraint of trade provide another example. It appears, however, that the classification of a contract as "void" rather than "illegal" in this context has few, if any, legal ramifications.

4 Yet another rendering is *allegans suam turpitudinem non est audiendus*.

Consequences of illegality

[PtXID.25] Contracts or contractual terms are variously, and sometimes interchangeably, described as unlawful, illegal, void, null and void, invalid or unenforceable. Such terminology might suggest that the contract, or the term, is of no legal effect at all. The legal position, however, is not as simple as that, as we shall see.

The topic of consequences is considered in detail in Chapter 42. Generally, it may be said that whatever terminology is used, and subject to a statutory indication to the contrary, the main consequence of a finding that a contact (or a contractual term) is "illegal" or "void" is that neither party can *enforce* the contract (or the relevant contractual term). A second consequence is that generally a claim in *restitution* for the return of money or property that has been paid or transferred under an illegal contract will fail.[5] The point is that a court does not wish to be seen as positively supporting illegal or other anti-social conduct or even as reversing the consequences of such conduct. Rather, courts wish to be seen as actively discouraging criminal or other anti-social behaviour.

However, the consequences of unenforceability and non-retrieval are often seen as too drastic and arbitrary. If a plaintiff cannot retrieve money paid or property transferred, an unworthy defendant may be left unjustly enriched. The plaintiff may be an innocent party or at least one who is not as guilty as the defendant (sometimes described as not *in pari delicto*). For example, the defendant may intend to and actually perform the contract in an illegal way, but the plaintiff may not have expected this or consented to it. The plaintiff may have been a victim of the defendant. To avoid unfairness in cases such as these, the courts have formulated qualifications to the general rules of unenforceability and non-restitution. In fact, the general rules themselves tend to be less frequently invoked and more restrictively applied, to avoid unfairness. This leads to complexity.

Before a contract, or a contractual term, is declared "illegal", it is important for a court to consider what the *consequences* of such a declaration are. The consequences are indeed often expressly considered by the courts. When determining whether or not a contract is prohibited by statute, consideration of the consequences of a finding of illegality allows the courts to consider whether parliament intended such an effect. When determining whether to find that a contract is void for illegality on public policy grounds, consideration of the consequences of a finding of illegality allows the courts to find a solution that does not undermine public policy and yet is reasonably just as between the parties in the circumstances of the case. To reason *forward* from a legal concept (such as "void contract" or "illegal contract") to a solution (such as "therefore the plaintiff cannot recover") gives the impression that the result is inevitable. To reason *backwards* ("should the plaintiff be able to recover?") to a conceptual conclusion ("the contract is – or is not – illegal or void") allows the real issues to be discussed. As Windeyer J said in *Brooks v Burns Philp Trustee Co Ltd*:

> it has always seemed likely to lead to error … to adopt first one of the familiar legal adjectives—"illegal", "void", "unenforceable"—and then having given an act a label, to deduce from that its results in law. That is to invert the order of inquiry, and by so doing to beg the question, and allow linguistics to determine legal rights.[6]

5 See further [10.85].
6 (1969) 121 CLR 432, 458.

How is the issue of illegality raised?

[PtXID.30] Illegality generally emerges in legal proceedings by way of a defence to a claim. It is a defence that may be raised in answer to a claimant's assertion of either common law or equitable rights.[7] However, a court may itself invoke illegality in certain circumstance, even though it has not been pleaded. In *Knowles v Fuller*, Jordan CJ stated that:

> a court will not entertain a defence of illegality which has not been pleaded, unless (1) the transaction sued upon is ex facie illegal, or (2) the plaintiff cannot prove his case without proving also that he is pleading under an illegal transaction, or (3) exceptionally, where a fact comes to light in the course of the trial which of itself shows that the transaction sued on is illegal on grounds which nothing could cure.[8]

Illegality may also be invoked in varying degrees in the context of claims outside of contract law, such as in torts, restitution and trusts. For example, in the context of negligence, a duty of care will not be owed by one bank robber to another in the course of jointly blowing up a safe. In the context of restitution, a claim against a contracted killer who has been paid in advance and has not performed may not succeed in retrieving the money, despite the total failure of consideration.

Reform

[PtXID.35] A study of illegality in contract law reveals considerable complexity and an apparent lack of coherence. Is drastic reform called for? If so, what form should it take? These questions are considered at the end of Chapter 42.

7 In equity there is also the maxim that "a person who comes to equity must come with clean hands". However, this maxim is concerned with the relationship between the parties to the action, rather than general public policy considerations. See *Nelson v Nelson* (1995) 184 CLR 538, 608–9.

8 *Knowles v Fuller* (1947) 48 SR (NSW) 243, 245. See also *Cohen v Cohen* (1929) 42 CLR 91, 95.

CHAPTER **40**

Contracts prohibited by statute

A QUESTION OF INTERPRETATION

[40.05] A statute may expressly prohibit a contract and expressly stipulate the consequences of that prohibition. If a statute expressly provides that a contract of a particular kind is void, then the matter is easily resolved.[1] Similarly, a statute may expressly provide that particular contractual terms are void.[2] Conversely, where the statute expressly provides that the consequence of non-compliance with the statute is that the contract is voidable at the discretion of one of the parties, this will suffice to show that it was not the intention of the legislature that such a contract be void on the basis of illegality.[3]

Where the statute does not expressly prohibit the making of the contract, but the contract as made or performed may involve the violation of a statutory provision, the court must determine whether the contract is impliedly prohibited by statute. Whether a contract is impliedly prohibited by statute is a question of construction that turns on the particular provisions and the scope and purpose of the statute.[4] This question will be answered by focusing on the policy underpinning the statute and, more specifically, by considering whether the legislature intended merely to penalise *specified conduct* (eg, by means of a fine) or to go further and deprive of legal effect a contract involving or associated with the prohibited conduct. If the latter, the court will also consider whether *both* parties should be deprived of the right to enforce the contract or only the party responsible for the violation.

Traditionally, the courts have adopted the general rule that contracts that are expressly or impliedly prohibited by statute are void and unenforceable. Gibbs ACJ noted in *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd* that "cases are likely to be rare in which a statute prohibits a contract but nevertheless reveals an intention that it shall be valid and enforceable, and in most cases it is sufficient to say … that the test is whether the contract is prohibited by statute".[5] Where the court concludes that the making of a contract is expressly or impliedly prohibited by statute, however, the court may nevertheless find that the contract

1 See, eg, *Ethnic Earth Pty Ltd v Quoin Technology Pty Ltd (in liq)* [2004] SASC 257; (2004) 89 SASR 337, 349–51.
2 See, eg, ACL, s 23, discussed in Chapter 16.
3 See, eg, *Ibrahim v Pham* [2007] NSWCA 215, [87].
4 *Yango Pastoral Company Pty Ltd v First Chicago Australia Ltd* (1978) 139 CLR 410, 425.
5 *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd* (1978) 139 CLR 410, 413. See also *Zullo Enterprises Pty Ltd v Sutton* [1998] QCA 417; [2000] 2 Qd R 196, [4].

itself is not prohibited by statute. In *Australian Competition and Consumer Commission v Baxter Healthcare Pty Ltd*, the majority noted that:

> when a statute contains a unilateral prohibition on entry into a contract, it does not follow that the contract is void. Whether or not the statute has this effect depends upon the mischief which the statute is designed to prevent, its language, scope and purpose, the consequences for the innocent party, and any other relevant considerations. Ultimately, the question is one of statutory construction.[6]

In *Tonkin v Cooma-Monaro Shire Council*,[7] the New South Wales Court of Appeal upheld the validity of a contract despite the fact that it was entered into in contravention of a regulation. The regulation in question provided that a council may enter into a contract of a certain kind only if certain requirements were complied with, including a tender process. Those requirements were not complied with. The question for the court was whether, in view of its scope and purpose, the statute disclosed an intention that a contract entered into in breach of its provisions should be unenforceable or an intention that the only sanctions for breach are those provided for in the legislation.[8] The court concluded that it was unlikely that the legislature intended that an innocent party was to be left with an unenforceable contract, especially since the statute provided a regime of penalties that operated in respect of non-compliance.[9]

Similarly, in *Gnych v Polish Club Ltd*,[10] the High Court upheld the validity of a lease (of a restaurant area within a licensed club), which was granted in breach of s 92(1) of the *Liquor Act 2007* (NSW). Section 92(1) provided that the holder of a liquor licence "must not lease or sublease any part of the licensed premises except with the approval of the [Liquor and Gaming] Authority". The statute imposed a penalty for breach of s 92 and also empowered the authority to cancel or suspend the licence or alternatively to take no action. The New South Wales Court of Appeal held that the policy of the Act (which included ensuring that licensees personally supervised and controlled licensed premises) could only be protected by holding the lease void. The High Court held that the policy of the Act was adequately protected through the supervisory role of the Authority. A conclusion that the lease was void would pre-empt the role of the Authority, which might decide to take no action on the basis that the lessees were fit and proper persons to operate the restaurant.[11] French CJ, Kiefel, Keane and Nettle JJ also took account of the adverse consequences for the innocent lessees.[12] Since it was the Club's responsibility as licensee to seek the approval of the Authority, the lessees bore no responsibility for the contravention. While coming to the same conclusion, Gageler J was reluctant to place much weight on the hardship to the innocent lessees in view of the "evident public interest" of the liquor licensing regime.[13]

6 *Australian Competition and Consumer Commission v Baxter Healthcare Pty Ltd* [2007] HCA 38; (2007) 232 CLR 1, 29.
7 *Tonkin v Cooma-Monaro Shire Council* [2006] NSWCA 50.
8 *Tonkin v Cooma-Monaro Shire Council* [2006] NSWCA 50, [72]
9 *Tonkin v Cooma-Monaro Shire Council* [2006] NSWCA 50, [90].
10 *Gnych v Polish Club Ltd* [2015] HCA 23; (2015) 255 CLR 414.
11 *Gnych v Polish Club Ltd* [2015] HCA 23; (2015) 255 CLR 414, [54], [83].
12 *Gnych v Polish Club Ltd* [2015] HCA 23; (2015) 255 CLR 414, [45].
13 *Gnych v Polish Club Ltd* [2015] HCA 23; (2015) 255 CLR 414, [81].

DRASTIC EFFECT OF PROHIBITION

[40.10] The potentially drastic effect of a ruling that a contract is prohibited by statute is illustrated by *Re Mahmoud and Ispahani*.[14] Under statutory regulation, no person was permitted to sell linseed oil except in accordance with the terms of a licence granted by the Government. The plaintiff had a licence to sell linseed oil and, under the terms of that licence, he could only sell to other persons holding a licence. The plaintiff sold linseed oil to the defendant, who said he had a licence to purchase, but in fact he had no such licence. This sale constituted an offence. The defendant refused to accept delivery and the plaintiff sued him for breach of contract. The defendant successfully pleaded illegality as a defence. The contract, it was held, was prohibited by statutory regulation. This ruling had drastic consequences. The plaintiff could not enforce the contract even though he was an innocent party, and the defendant was able to rely on his own illegal act. It could, however, have been worse for the plaintiff. If the defendant had accepted delivery of the linseed oil, but refused to pay for it, the defendant would have been enriched at the plaintiff's expense.

Such questionable results are said to be justified on grounds of public policy. As Lord Mansfield explained in *Holman v Johnson*:

> The objection that a contract is immoral or illegal as between the plaintiff and the defendant, sounds at all times very ill in the mouth of the defendant. It is not for his sake, however, that the objection is ever allowed, but it is founded in general principles of policy, which the defendant has the advantage of, contrary to the real justice, as between him and the plaintiff, by accident, if I may say so. The principle of public policy is this: ex dolo malo non oritur actio. No court will lend its aid to a man who founds his cause of action upon an immoral or illegal act.[15]

The idea to which Lord Mansfield adverts, that the defendant is advantaged by the policy of the law, is summed up in another maxim: in pari delicto potior est conditio defendentis (where there is equal fault, the defendant is in the stronger position). But was the plaintiff in *Re Mahmoud and Ispahani* as much at fault as the defendant? Seemingly not, and yet an inquiry into relative fault was apparently regarded as precluded in a case where the contract was prohibited by statute and the issue of enforcement of the contract was before the court.

In *Bradshaw v Gilberts (Australasian) Agency (Vic) Pty Ltd*,[16] the High Court endorsed the general rule that if a particular class of sale is prohibited by statute, a purported sale in breach of that prohibition is void. The statute in that case was s 25(1) of the *Price Regulation Act 1918* (Vic), which provided that no person should sell any declared goods at a greater price than the maximum price fixed under the statute. Subsection (2) provided that, in addition to any other penalty which might be imposed for contravention of subsection (1), the court could order the seller to refund to the purchaser the difference between the fixed maximum price and the contract price. The defendant agreed to purchase 127 tons of scrap lead from the plaintiff, the scrap lead being intended for export. The defendant repudiated the contract and the plaintiff claimed damages. The majority (Dixon CJ and Taylor J) held that the action could not be maintained. The contract was within the ambit of the legislation and, as it was in breach of s 25(1), it was void. Subsection (2) was not thought to contradict this conclusion, as that subsection imposed an obligation on the seller by way of additional penalty for violation

14 *Re Mahmoud and Ispahani* [1921] 2 KB 138.

15 *Holman v Johnson* (1775) 1 Cowp 431, 343; 98 ER 1120, 1121.

16 *Bradshaw v Gilberts (Australasian) Agency (Vic) Pty Ltd* (1952) 86 CLR 209.

of subsection (1). The relief thereby made available would not have been otherwise available to the purchaser, regardless of whether one took the view that a contract in contravention of subsection (1) was legal or illegal. The dissenting judge, McTiernan J, held that the statute did not apply to goods intended for export and therefore the contract was valid. However, he did not dissent from the majority as to the consequences that would ensue if the statute did apply to goods intended for export.

MODERN RELUCTANCE TO FIND PROHIBITION

[40.20] The cases discussed in the preceding section reflect a strict and relatively inflexible approach to the issue of whether a contract is void or unenforceable as a result of statutory illegality. In recent times, the courts have shown an increased reluctance to find that a contract is void on the basis that it is expressly or impliedly prohibited by statute.[17] In *Fitzgerald v FJ Leonhardt Pty Ltd*, Kirby J observed that:

> This reluctance probably grows out of a recognition of the multitude of legislative provisions, important and unimportant, which may nowadays indirectly impinge upon the contractual relations of parties and, if enforced with full rigour, cause harsh and unwarranted deprivation of rights. In part, this reluctance may be no more than a species of the general rule of statutory construction that legislation will not be interpreted to deprive parties of basic rights at common law without a clear expression of the legislative will to do so.[18]

As it is ultimately a matter of statutory construction, there are no hard and fast rules about when a contract will be void or enforceable on the basis of statutory illegality. In deciding whether a contract is expressly or impliedly prohibited, there are three key factors that the courts will consider. First, the courts will start by considering the language of the relevant statutory provision(s). Then, the courts will consider the object and context of the legislation. If the purpose of the statute can be fulfilled without finding that the contract is prohibited, the contract is more likely to be construed as valid.[19] In determining whether the purpose of the statute can be fulfilled without finding that the contract is prohibited, the courts will consider whether the statute said to invalidate the contract provides sanctions for non-compliance. Finally, the courts will also consider whether finding that the contract is unenforceable might adversely affect innocent parties. Where this is the case, the courts are less likely to find that parliament intended that the contract is unenforceable.[20]

Likely effect on innocent parties

[40.25] In *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd*,[21] the plaintiff lent the defendant money on mortgage and the defendant defaulted in repayment. The defendant pleaded that the loan transaction was impliedly prohibited by s 8 of the *Banking Act 1959* (Cth). The plaintiff was carrying on the business of banking contrary to the prohibition in

17 *Hurst v Vestcorp Ltd* (1988) 12 NSWLR 294, 411–2. But for a modern example of a contract illegal by statute, see *Burmic Pty Ltd v Goldview Pty Ltd* [2002] QCA 479; [2003] 2 Qd R 477.

18 *Fitzgerald v FJ Leonhardt Pty Ltd* (1997) 189 CLR 215, 243.

19 *Fitzgerald v FJ Leonhardt Pty Ltd* (1997) 189 CLR 215, 227.

20 *Tonkin v Cooma-Monaro Shire Council* [2006] NSWCA 50, [91]; *Master Education Services Pty Limited v Ketchell* [2008] HCA 38; (2008) 236 CLR 101, [39], [40]; *Gnych v Polish Club Ltd* [2015] HCA 23; (2015) 255 CLR 414, discussed at [40.05].

21 *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd* (1978) 139 CLR 410.

that section, and the loan transaction was entered into in the course of carrying on that banking business. In rejecting the defendant's illegality defence, the High Court paid close attention to the potential effect of holding that the contract was unenforceable on innocent parties. Gibbs ACJ and Mason J (in separate judgments) noted that if the statute were read as prohibiting contracts made by unauthorised bodies in the course of carrying on banking business, innocent depositors would be prejudiced rather than protected. They would be unable to recover moneys deposited with the person unlawfully carrying on banking business (ie, the wrongdoer). It could not be supposed by the court that the legislature intended to inflict such consequences on innocent depositors.[22] Further, to relieve the defendants of their obligation to repay their loans would jeopardise the plaintiff's ability to meet its own obligations to investors and creditors. The purpose of the statute was already adequately served by the statutory provision of a heavy penalty for contraventions of s 8. The case illustrates the process, referred to earlier (at [PtXID.25]), of reasoning backwards ("the plaintiff ought to be able to recover") to a conceptual conclusion ("therefore the contract is not prohibited").[23]

In *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd*, the Court assumed that if the contract was prohibited by statute, this would mean that *neither* party could enforce the contract. Rather than come to that conclusion, which would have had a drastic effect on innocent depositors and the bank, the court preferred to find that the contract itself was not prohibited. There is no reason why the court could not have found that the contract remained valid but could not be enforced by the plaintiff (the party responsible for the illegality). As the majority observed in *Australian Competition and Consumer Commission v Baxter Healthcare Pty Ltd*:

> there is nothing unusual about a circumstance in which making or giving effect to a contract involves an offence by one party to the contract but not the other. The consequences of such illegality for the rights of the parties will not necessarily be the same.[24]

Relevance of sanctions for non-compliance

[40.35] If sanctions for non-compliance (such as fines or penalties) appear to be sufficient to deal with the contravention of the legislation, courts are less likely to hold that a contract made in breach of the legislation is unenforceable.[25] Similarly, where the legislation systematically addresses the consequences of breach it is less likely that the legislation will be interpreted as prohibiting the contract.[26] In *Master Education Services Pty Ltd v Ketchell*,[27] Ketchell (a franchisee) claimed that its franchise agreement with Master Education Services Pty Ltd (Master Education) was unenforceable as Master Education had failed to comply with the Franchising Code of Conduct in breach of s 51AD of the *Trade Practices Act 1974* (Cth) (now

22 *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd* (1978) 139 CLR 410, 414 (per Gibbs ACJ), 427 (Mason J).

23 See [PtXID.30].

24 *Australian Competition and Consumer Commission v Baxter Healthcare Pty Ltd* [2007] HCA 38; (2007) 232 CLR 1, 28.

25 *Nelson v Nelson* (1995) 184 CLR 538, 612–3; *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd* (1978) 139 CLR 410, 413; *Fitzgerald v FJ Leonhardt Pty Ltd* (1997) 189 CLR 215, 244; *Elvidge Pty Ltd v BGC Construction Pty Ltd* [2006] WASCA 264, [53]–[55]; *Master Education Services Pty Limited v Ketchell* [2008] HCA 38; (2008) 236 CLR 101, [38].

26 *Dover Beach Pty Ltd v Geftine Pty Ltd* [2008] VSCA 248; (2008) 21 VR 442, [79], [96];

27 *Master Education Services Pty Ltd v Ketchell* [2008] HCA 38; (2008) 236 CLR 101.

Competition and Consumer Act 2010 (Cth)). In deciding that the contract was enforceable, the High Court was influenced by the range of remedies provided for in Pt VI of the Act which could be imposed on a party who had breached s 51AD.[28] The High Court was also influenced by the effects on innocent parties that might result from a finding that the contract was impliedly prohibited by statute.[29]

Moreover, a contract will not be impliedly prohibited, even where no penalty is imposed on the party breaching the statute, if the policy underpinning the statute is protected in another way.[30] In *Bondlake Pty Ltd v Owners – Strata Plan No 60285*,[31] an owners' corporation (an entity that manages the common property of a property development) incurred a debt by entering into a caretaker agreement with Bondlake during the early stages of the development at a time when it had no money in its administrative account. This breached s 113(1)(b) of the *Strata Schemes Management Act 1996* (NSW), which prohibited owners' corporations from incurring a debt for any amount that exceeded the funds available in the owners' corporation's administrative fund. The New South Wales Court of Appeal found that the object of the legislation was to protect future lot owners against liability for such expenses. Even though the legislation impliedly prohibited entry into the contract in question, it was held that the contract should nevertheless be enforceable. Although the statute imposed no penalty on owners' corporations that breach the provision, the statute provided that, in the event that s 113(1)(b) was breached, the owners' corporation could recover the amount of the debt from the original owner. The policy goals of the legislation could therefore be achieved without the need to render the contract with the caretaker unenforceable. The Court of Appeal also noted that finding that the contract was unenforceable would have been unfair to innocent parties who dealt with the owners' corporation.[32]

Invalidity on the grounds of public policy

[40.40] Even where the court concludes that the contract is not expressly or impliedly prohibited by statute, the court must then consider whether to refuse relief on public policy grounds. As discussed in Chapter 41,[33] a contract may be held to be unenforceable on the grounds of public policy if it could only be performed "in contravention of a statute or was intended to be performed illegally or for an illegal purpose".[34] There is considerable overlap between the factors the court considers when determining whether a contract is impliedly prohibited by statute and when determining whether to refuse to enforce a contract on the basis that it contemplates the commission of a breach of statute and is therefore contrary to public policy. In both instances, the court reasons backwards and first asks whether the plaintiff ought to be able to recover under the contract. If the court considers that enforcing the contract would undermine the legislative prohibition in question, then the contract will be held to be void or illegal.[35]

28 *Master Education Services Pty Ltd v Ketchell* [2008] HCA 38; (2008) 236 CLR 101, [28]–[30].

29 *Master Education Services Pty Ltd v Ketchell* [2008] HCA 38; (2008) 236 CLR 101, [39].

30 *Bondlake Pty Ltd v Owners – Strata Plan No 60285* [2005] NSWCA 35; (2005) 62 NSWLR 158, 166.

31 *Bondlake Pty Ltd v Owners – Strata Plan No 60285* [2005] NSWCA 35; (2005) 62 NSWLR 158.

32 *Bondlake Pty Ltd v Owners – Strata Plan No 60285* [2005] NSWCA 35; (2005) 62 NSWLR 158, 166–7.

33 See [41.10]–[41.30].

34 *Fitzgerald v FJ Leonhardt Pty Ltd* (1997) 189 CLR 215, 220.

35 See [PtXID.25].

CHAPTER **41**

Contracts prohibited at common law

PUBLIC POLICY

[41.05] In the introduction to this Part of the book, we saw that, traditionally, judges determined what constituted "public policy". We noted the various kinds of contracts held by judges to violate basic community standards. The judiciary has recognised, however, that the power to declare contracts illegal on grounds of public policy was fraught with danger and difficulty. Burrough J famously said in *Richardson v Mellish* that public policy "is a very unruly horse, and when once you get astride it you never know where it will take you".[1] In the context of vastly increased legislative activity in the 20th century, some judges took the view that it was not for the courts to create new heads of public policy. Their role was now seen as defining the scope of existing heads of public policy.[2] If this is so, it apparently allows for novel applications.[3] The more realistic view is that expressed by Jordan CJ: "New heads of public policy come into being and old heads undergo modification."[4]

When a contract by its express terms or by the tendency of its operation infringes a recognised principle of public policy so that its judicial enforcement would be injurious to

1 *Richardson v Mellish* (1824) 2 Bing 229, 252; 130 ER 294, 303.
2 See *Brooks v Burns Philp Trustee Co Ltd* (1969) 121 CLR 432, 451–2.
3 See *Naylor Benzon & Co v Krainische Industrie Gesellschaft* [1918] 1 KB 331, 341–2.
4 *Re Morris (dec'd)* (1943) 43 SR (NSW) 352, 355.

the community, the courts may refuse to give effect to the contract. As we have seen, a court's refusal to enforce a right in this context is said to be not for the sake of the defendant (whose failure to abide by the agreement may sometimes be quite dishonourable), but for the sake of the community at large.[5] In determining whether to support any particular head of public policy by means of non-enforcement of a contract, however, a court must weigh any opposing public interests in the balance.[6] A refusal to enforce a contractual right may cause more social harm than a decision to enforce it: "The court has to weigh the gravity of the anti-social act and the extent to which it will be encouraged by enforcing the right sought to be asserted against the social harm which will be caused if the right is not enforced."[7]

CONTRACTS INVOLVING THE COMMISSION OF A CRIME, TORT OR BREACH OF STATUTE

[41.10] A contract which obliges one or both of the parties to commit a crime, tort or breach of statute, or contemplates the possibility of such a commission, may be declared void or unenforceable on the basis that it is contrary to public policy. However, the rule against enforcement is not inflexible.[8] Whether the contract is declared unenforceable will depend upon the seriousness of the wrong in question and the consequences of declaring the contract unenforceable.[9]

In *North v Marra Developments Ltd*,[10] the plaintiff stockbroker was engaged by the defendant company to advise it on a reconstruction of its capital and on the takeover of another company. Following its own advice to the defendant, the plaintiff purchased shares in the defendant company on the stock exchange in order to set a market price for those shares. The market price of the shares had originally been $4.40, but following the plaintiff's purchases, the market price was set at $16.50. It was on the basis of this latter price that the defendant made its takeover bid. In statements made to the press and in the formal offer to the shareholders of the other company, $16.50 was referred to as "the market price". When the plaintiff later claimed remuneration from the defendant for services rendered, the defendant pleaded that the contract to pay the fees for the services was illegal by reason of contravention of s 70 of the *Securities Industry Act 1970* (NSW). That section prohibited the doing of anything calculated to create a false or misleading appearance with respect to the price of securities.

The High Court held that the action must fail, not because the contract was itself prohibited by the statute, but because the contract from the outset contemplated the possibility of a breach of s 70 as a means of carrying out the scheme to which the parties had agreed. As it happened, what was contemplated as a possibility became an actuality. The performance on which the plaintiffs relied in their claim for remuneration involved illegal conduct – the violation of s 70. The object of that section was to protect the securities market against artificial or managed manipulation. A majority of the High Court held further that the plaintiff's claim for remuneration failed on the additional ground that the parties had contemplated the possibility

5 *Wilkinson v Osborne* (1915) 21 CLR 89, 98.
6 *A v Hayden* (1984) 156 CLR 532, 559–60.
7 *Hardy v Motor Insurers' Bureau* [1964] 2 QB 745, 751.
8 *Fitzgerald v F J Leonhardt Pty Ltd* (1997) 189 CLR 215, 248 (Kirby J).
9 *Hayes v Cable* [1962] SR (NSW) 1, 6.
10 *North v Marra Developments Ltd* (1981) 148 CLR 42.

of perpetrating a fraud at common law. They had in fact made statements which they knew to be misleading with a view to deceiving the shareholders of the company which the defendant was planning to take over.

Knowledge of unlawfulness

[41.15] Generally, the parties to a contract will know that their proposed act is criminal or tortious. The deliberateness of the proposed act is relevant to determining whether or not the court will refuse to enforce the contract on public policy grounds.[11] The courts may not refuse relief where the claimant was ignorant of the illegality or where the illegality was induced by the defendant's fraud.[12] The courts have, however, been prepared to find that a contract is void for illegality even where neither party had knowledge of the illegality. In *JM Allan (Merchandising) Ltd v Cloke*,[13] the plaintiff leased to the defendant a roulette table and wheel to enable a certain game to be played. This game was unlawful under gaming legislation. It was held that no rent could be claimed under the contract, and it was no excuse that the parties were ignorant of the unlawfulness of the game which they both intended to be played.

Gravity of wrong

[41.20] If the crime or tort in question is of a minor nature, and cannot be characterised as in any sense heinous, a contract involving its commission, even an intentional commission, will not be held contrary to public policy.[14] A contract with the driver of a vehicle to park it illegally is clearly not as anti-social as a contract with the driver to perform a hit and run.

Illegal performance

[41.23] One of the parties to a legal contract may *perform* the contract in an illegal manner. The innocent party, if sued, may raise the defence of illegality: *ex turpi causa non oritur actio* (an action does not arise from a base cause). In such an instance, the innocent party is not arguing that the *contract* is illegal, as that might well rule both parties out of court as far as enforcement is concerned. Rather, the innocent party is saying that the claimant is *relying on an illegal act* in order to obtain relief in a contract action. As Devlin LJ once pointed out:

> If a contract can be performed in one of two ways, that is legally or illegally, it is not an illegal contract, though it may be unenforceable at the suit of the party who chooses to perform it illegally.[15]

This ex turpi rule is not, however, applied arbitrarily. The courts today will weigh various considerations of public policy for and against enforcing the contract, including the aims of any relevant statute. In *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd*,[16] we saw that the High Court held that the loan contract itself was not prohibited by the *Banking Act 1959* (Cth). The court also considered an argument by the defendant that the plaintiff was

11 *Fitzgerald v F J Leonhardt Pty Ltd* (1997) 189 CLR 215, 249.

12 *Nelson v Nelson* (1995) 184 CLR 538, 605.

13 *JM Allan (Merchandising) Ltd v Cloke* [1963] 2 QB 430.

14 See *Electric Appliance Pty Ltd v Doug Thorley Caravans (Australia) Pty Ltd* [1981] VR 799.

15 *Archbolds (Freightage) Ltd v S Spanglett* [1961] 1 QB 374, 391.

16 *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd* (1978) 139 CLR 410, see [40.25].

the party in breach of a statutory prohibition, and therefore, the ex turpi rule should apply. The court held, however, that in this case the contract should be enforced. The form of the legislation indicated it was concerned with the execution of government fiscal policy and that the fines imposed for offences under the statute were to be the only legal consequence of such offences. To relieve the defendants of their legal obligation to repay their loans would provide them with a windfall gain and jeopardise the plaintiff's ability to meet its own obligations to investors and other creditors. The ex turpi principle provides a deterrent to crime, but here Parliament had already provided a deterrent. It would be odd, in the court's view, if the offender were to be punished twice – civilly as well as criminally. Similarly, if the commission of the wrong has civil consequences, this may result in the court refusing to find that the contract is unenforceable.

Where an agreement can be legally performed, but one party claims the contract is void on the basis that the other party made the contract for an illegal purpose, the party claiming that the contract is void must demonstrate that the other party had a clear intention to pursue an illegal purpose.[17] This can be quite difficult to prove because the law assumes that parties intend to comply with the law.

Statutory prohibition of contract compared

[41.25] Logically, it is only when it is determined that the contract itself is *not* prohibited by the statute that the question of its unenforceability on the basis of public policy will arise.[18] Thus, the question of statutory construction aimed at determining whether the legislation renders the contract unenforceable must come first.[19]

When a court considers whether a contract is expressly or impliedly prohibited by statute,[20] the focus is on the expressed or imputed will of the legislature. The question is whether the legislation in question suggests that Parliament intended that contracts formed in breach of the legislation should be void and therefore unenforceable. However, when the court considers whether to refuse to enforce a contract on the basis of public policy, the court determines whether it should lend its assistance to a party that is connected with illegal conduct. Thus, questions such as the deliberateness of the conduct, knowledge of the illegality and the extent of the enforcing party's involvement in the illegality become relevant.[21] When a statutory offence has been committed by a contracting party, considerations relevant to whether the contract was expressly or impliedly prohibited by the statute are also relevant to the question of whether the contract is unenforceable on public policy grounds.[22]

McHugh J's guidelines

[41.30] In *Nelson v Nelson*, McHugh J identified four circumstances in which the court would enforce legal or equitable rights despite the presence of illegality:

17 *Hutchinson v Scott* (1905) 3 CLR 359.

18 *Fitzgerald v FJ Leonhardt Pty Ltd* (1997) 189 CLR 215, 245.

19 *Bondlake Pty Ltd v Owners – Strata Plan No 60285* [2005] NSWCA 35; (2005) 62 NSWLR 158, [28].

20 See Chapter 40.

21 *Holdcroft v Market Garden Produce Pty Ltd* [2000] QCA 396; [2000] 2 Qd R 381, [31].

22 *Elvidge Pty Ltd v BGC Construction Pty Ltd* [2006] WASCA 264, [52]. For a discussion of these factors, see Chapter 40.

1. First, the courts will not refuse relief where the claimant was ignorant or mistaken as to the factual circumstances which render an agreement or arrangement illegal.
2. Second, the courts will not refuse relief where the statutory scheme rendering a contract or arrangement illegal was enacted for the benefit of a class of which the claimant is a member.
3. Third, the courts will not refuse relief where an illegal agreement was induced by the defendant's fraud, oppression or undue influence.
4. Fourth, the courts will not refuse relief where the illegal purpose has not been carried into effect.[23]

McHugh J also noted that even where the case does not come within one of the four categories listed earlier:

> the courts should not refuse to enforce legal and equitable rights simply because they arose out of or were associated with an unlawful purpose unless:
>
> (a) the statute discloses an intention that those rights should be unenforceable in all circumstances; or
>
> (b) (i) the sanction of refusing to enforce those rights is not disproportionate to the seriousness of the unlawful conduct;
>
> (ii) the imposition of the sanction is necessary, having regard to the terms of the statute, to protect its objects or policies; and
>
> (iii) the statute does not disclose an intention that the sanctions and remedies contained in the statute are to be the only legal consequences of a breach of the statute or the frustration of its policies.[24]

These guidelines were endorsed and applied in the joint judgment of McHugh and Gummow JJ and in the judgment of Kirby J in *Fitzgerald v F J Leonhardt Pty Ltd*.[25] Fitzgerald contracted with a driller, who was the holder of a drilling licence under the *Water Act*, to drill some bore holes in Fitzgerald's land. The driller bored the holes but later had to sue Fitzgerald for money due under the contract. Fitzgerald raised the defence of illegality. Although the driller was licensed to drill, no permit had been issued under the *Water Act* for drilling the bores (it was Fitzgerald's responsibility to ensure the permits were obtained). The *Water Act* stated that "a person shall not unless authorised under the Act permit a bore to be drilled" and imposed a fine of $5000 for a first offence. The High Court disallowed the defence of illegality.

The first issue was whether the contract was, as formed or performed, expressly or impliedly prohibited by the *Water Act*. The court held that the contract was not so prohibited. Although the contract was performed in contravention of the *Water Act*, the contravention was the consequence of Fitzgerald's failure to observe requirements imposed on him. The *Water Act* penalised such conduct but did not prohibit contracts. It did not prohibit some act that was essential to carrying out the contract. Performance of the work under the contract would not have been illegal if Fitzgerald had obtained the licence.

The second issue before the court in this case was whether, as a matter of public policy, the court should decline to enforce the contract on the ground that it was associated with the

23 *Nelson v Nelson* (1995) 184 CLR 538, 604–5 (footnotes omitted).

24 *Nelson v Nelson* (1995) 184 CLR 538, 613.

25 *Fitzgerald v FJ Leonhardt Pty Ltd* (1997) 189 CLR 215, 229–30 (McHugh and Gummow JJ), 249–51 (Kirby J).

illegal activity of the owner in permitting the drilling to occur without a licence. Here, the claim by the driller was insufficiently associated with the owner's breach of the *Water Act*. To impose on the driller the sanction of denying him the contractual right to claim for the work he had done would have been disproportionate to the seriousness of the offence. Further, it would have unfairly enriched Fitzgerald by conferring a windfall on him. The object of the *Water Act*, to control the right of owners of land to take water, was sufficiently protected by the prescribed penalty.

CONTRACTS WHICH PREJUDICE THE ADMINISTRATION OF JUSTICE

[41.35] An example of a contract which prejudices the administration of justice is an agreement to stifle a prosecution in respect of an offence of a public nature. Offences of a public nature include crimes such as perjury, assault, theft or forgery. In *Callaghan v O'Sullivan*,[26] the defendants, police officers, threatened to prosecute the plaintiff on a charge of being in possession of stolen goods unless the plaintiff would agree to pay them a certain sum of money. The plaintiff paid part of this sum a few days later. The defendants did not initiate any proceedings. The plaintiff then sought recovery of the money paid. The court held that money paid to stifle a prosecution could not be recovered. The purpose of the payment was a violation of the general principles of public policy.

In *A v Hayden*,[27] the High Court considered the validity of a confidentiality clause contained in an employment contract between the Commonwealth and five secret service agents. The agents were involved in a rescue training operation at the Sheraton Hotel in Melbourne. The Victorian Chief of Police believed that offences had been committed during the training operation and asked the Commonwealth to reveal the names of those who participated. The participants sought an injunction preventing their names from being disclosed. The court found that the confidentiality clause was unenforceable as its enforcement would obstruct the due administration of the criminal law.

It should be noted, however, that if an offence is of a private nature (such as criminal defamation), an agreement to pay money in return for a promise not to proceed with prosecuting that offence would not be considered against public policy.[28]

CONTRACTS WHICH PROMOTE CORRUPTION IN PUBLIC LIFE

[41.40] A contract made by a person holding public office, which involves a conflict between the public duty and the private interests of the contractor, is contrary to public policy. In *Wilkinson v Osborne*,[29] the plaintiffs, two Members of Parliament, agreed with a land agent, for a fee, to urge the Government to approve a sale of land which required Parliamentary approval under statute. The sale was approved, and the plaintiffs sued the agent for their fee. The court held that the contract was illegal, as the plaintiffs had placed their private interests in conflict with their public duty. The plaintiffs had agreed, for personal gain, to use the weight they possessed as Members of Parliament to influence the executive to advance the agent's proposal.

26 *Callaghan v O'Sullivan* [1925] VLR 664.

27 *A v Hayden* (1984) 156 CLR 532.

28 See *Kerridge v Simmonds* (1906) 4 CLR 253.

29 *Wilkinson v Osborne* (1915) 21 CLR 89. See also *Wood v Little* (1921) 29 CLR 564.

CONTRACTS PROMOTING SEXUAL IMMORALITY AND/OR PREJUDICIAL TO THE STATUS OF MARRIAGE

[41.45] Traditionally, contracts tending to promote sexual immorality and contracts prejudicialto the status of marriage have been regarded as contrary to public policy. In *JM Allan (Merchandising) Ltd v Cloke*, Lord Denning said:

> If a landlord lets a flat to a prostitute at a rent beyond any commercial rent or if he lets her a brougham of a specially intriguing nature, it may be fairly inferred that it was their common design that it should be used for an immoral purpose. The letting is unlawful and he cannot recover the rent or hire.[30]

However, community standards relating to sexual morality change. Such change can be seen, for example, in legislation that decriminalises prostitution, as well as legislation that permits people who are not married to enter into enforceable domestic relationship agreements. It can also be seen in changing attitudes towards marriage. Despite significant changes in community standards, contracts promoting sexual immorality remain within the purview of illegality. In *Ashton v Pratt (No 2)*,[31] Brereton J found that "no case stands contrary to the proposition that it is still the law that a contract to provide meretricious sexual services is contrary to public policy and illegal".[32]

Contracts that make provision for an existing relationship, as opposed to bringing about a new relationship, are unlikely to be void for illegality. In *Andrews v Parker*,[33] a man and a married woman began to live together in the man's house. The man agreed to, and did, transfer the house to the woman on condition that if she returned to her husband, she would re-transfer the house. The woman in fact returned to her husband. The husband moved into the house, and the man moved out. The court allowed the man's claim to recover the house. It rejected the woman's defence that the transfer to her was made for an immoral consideration. The contract was not one to bring about a state of extra-marital cohabitation. It provided for what was to happen when the cohabitation *ended*. However, the court went on to say that even if the consideration was immoral, it was not so immoral according to current social standards that the contract should be rendered unenforceable. "[N]otoriously the social judgments of today upon matters of 'immorality' are as different from those of last century as is the bikini from the bustle."[34]

CONTRACTS IMPOSING SERVITUDE

[41.50] A contract which restricts a person's liberty to the extent that he or she is reduced to a state of servitude is against public policy. In *Horwood v Millar's Timber and Trading Company Ltd*,[35] a clerk on a modest salary borrowed money from a moneylender on terms that assigned his salary to the moneylender and obligated the clerk neither to change his residence

30 *JM Allan (Merchandising) Ltd v Cloke* [1963] 2 QB 340, 348.

31 *Ashton v Pratt (No 2)* [2012] NSWSC 3. On appeal, the Court of Appeal did not find it necessary to deal with the illegality argument: *Ashton v Pratt* [2015] NSWCA 12; (2015) 88 NSWLR 281.

32 *Ashton v Pratt (No 2)* [2012] NSWSC 3, [50].

33 *Andrews v Parker* [1973] Qd R 93. See also *Seidler v Schallhofer* [1982] 2 NSWLR 80.

34 *Andrews v Parker* [1973] Qd R 93, 104.

35 *Horwood v Millar's Timber and Trading Company Ltd* [1917] 1 KB 305.

or employment nor to incur any legal or moral obligation, without the moneylender's consent. The court held that the contract violated a head of public policy of the most well-established kind. The contract imposed conditions far beyond what was necessary for the protection of the moneylender's interests and practically made the clerk a slave. For example, he could have been prevented from shifting house, consulting a doctor or raising money for the support of his family.

CONTRACTS TO DEFRAUD THE REVENUE AUTHORITIES

[41.55] A person who executes a contractual document with the intention of using it to defraud the revenue authorities cannot rely on that document to enforce contractual rights conferred by it.[36] In *Alexander v Rayson*,[37] a landlord who let one of his flats to the defendant at a rental of £1200 per annum asked her to sign two documents: one showed the rent at £450 and the other (a service agreement) required her to pay £750. The tenant was unaware that the landlord's object was to defraud the rating authority by showing it the first document only. The tenant declined to pay the full rent as the services promised by the landlord were inadequate. When the landlord sued for the rent, the tenant raised the defence of illegality. The court held that the landlord could not sue the tenant for the rent as his purpose was to use the documents for an unlawful purpose.

Note, however, that an intention to defraud the revenue authorities would not deprive a document of its quality of enforceability or admissibility if, in law, the document could not have served the purpose of perpetrating a fraud.[38]

CONTRACTS INFRINGING THE LAWS OF A FOREIGN COUNTRY

[41.60] A contract entered into with the intention of infringing the laws of a foreign country is against public policy.[39] If, however, Australia is at war with the foreign country, public policy is apparently not offended. In fact, any contract entered into with a resident of a country with which Australia is at war is illegal, at least if it has the effect of hindering the war effort.[40] If a war is declared after a contract has been entered into, the contract will be discharged by frustration.[41]

CONTRACTS IN RESTRAINT OF TRADE

[41.65] One of the traditional policies of the common law is that people should be free to exercise their capacities for work and trade. The courts have always taken quite a strict attitude towards contracts imposing restrictions on a person's freedom to work, or to carry on trade or business, in such place and in such manner as the person thinks fit.

36 See, eg, *Holdcroft v Market Garden Produce Pty Ltd* [2000] QCA 396.

37 *Alexander v Rayson* [1936] 1 KB 169.

38 *Gray v Pastorelli* [1987] WAR 174.

39 *Regazzoni v KC Sethia (1944) Ltd* [1958] AC 301.

40 *Hirsch v Zinc Corp Ltd* (1917) 245 CLR 43, 58–9.

41 See Chapter 17.

Basic principle

[41.70] In *Nordenfelt v The Maxim Nordenfelt Guns and Ammunition Company Ltd*, Lord Macnaghten expounded the law as follows:

> All interferences with individual liberty of action in trading and all restraints of trades of themselves, if there is nothing more, are contrary to public policy and therefore void. That is the general rule. But there are exceptions: restraints … may be justified … and indeed it is the only justification if the restriction is reasonable; reasonable, that is, in the interests of the parties concerned and reasonable with reference to the interests of the public.[42]

The *Nordenfelt* decision was approved by the High Court in *Buckley v Tutty*.[43] The restraint of trade doctrine now operates in the following manner:

1. There must be a restraint falling within the scope of the doctrine.
2. The restraint must relate to a protectable interest. Restrictions against competition per se will always be unenforceable. Examples of protectable interests that have been recognised include goodwill, confidential information and customer and client bases.
3. The party seeking to enforce the restraint must demonstrate that the scope and duration of the restraint is reasonable as between the parties.
4. Even if the restraint is reasonable as between the parties, a person will be released from the restraint if he or she is able to show that the restraint is unreasonable having regard to the public interest.

Whether or not the clause is reasonable must be judged based on the circumstances existing at the time of the contract.[44] This principle is nicely illustrated by the outcome in *McHugh v Australian Jockey Club Ltd*.[45] Since 1947, the rules of thoroughbred racing have prohibited horses bred by artificial insemination from inclusion in the Australian Stud Book, which is published by the respondents. McHugh, a breeder of thoroughbred horses, challenged the rule as a restraint of trade. McHugh argued that whilst the rule may have been reasonably necessary in 1947 to prevent fraud or mistaken identity, the introduction of mandatory blood typing in 1986 meant that the restraint was no longer reasonably necessary. The Full Court of the Federal Court rejected this argument because "nothing was contemplated in 1947 about the future possibility of DNA testing being used to resolve identification problems".[46]

Diluted illegality

[41.75] The attitude of the common law is not based primarily on any notion of fairness as between the parties. It is based rather on the desirability of encouraging the growth of commerce and thus the strength and wealth of the nation. However, although a restraint of trade clause may be held "void" and "unenforceable", it does not mean the clause is necessarily without any legal significance at all. If a person, in return for a promised benefit, *in fact* adheres to an undertaking in unreasonable restraint of trade, the promised benefit may

42 *Nordenfelt v The Maxim Nordenfelt Guns and Ammunition Company Ltd* [1894] AC 535, 565.

43 *Buckley v Tutty* (1971) 125 CLR 353.

44 *Lindner v Murdock's Garage* (1950) 83 CLR 628, 653.

45 *McHugh v Australian Jockey Club Ltd* [2014] FCAFC 45.

46 *McHugh v Australian Jockey Club Ltd* [2014] FCAFC 45, [24].

no doubt be claimed. This is because the undertaking is not regarded as "illegal" in the strict sense; it is merely unenforceable. The act of self-restraint is therefore good consideration.[47]

On the other hand, a *promise* in unreasonable restraint of trade would not as such be good consideration for a promise in return, as an unenforceable promise cannot constitute good consideration. There may of course be *other* considerations, existing alongside the unenforceable promise, to support the promise in return.[48] But even then the promise in return might not be enforceable if the unenforceable promise in restraint of trade was so material a provision in the whole bargain that there should be inferred an intention not to make a contract which would operate without it.[49]

Burden of proof

[41.80] The burden of establishing that the restraint of trade clause is reasonable as between the parties is on the promisee, that is, the party who receives the benefit of the restraint. If the promisee's burden is discharged, the burden of establishing that the clause is contrary to the public interest is on the promisor, that is, the party who agreed to be restrained.[50]

Recognised categories

[41.85] In one sense, all commercial contracts restrain trade. If A contracts to sell a certain item to B, this restricts A's freedom to sell that item to another. In practice, certain common categories of contract are recognised by the courts as subject to the rule against restraint. These categories include employment contracts, contracts for the sale of a business, and "exclusive dealing" or "solus" contracts. For example, under an employment contract, the employee may agree not to set up a rival business on leaving the employer's service or work for a rival firm. Under a contract for the sale of a business (including goodwill), the vendor may agree not to carry on a business which will compete with the purchaser's business. Under an exclusive dealing agreement, a trader may agree to buy a certain commodity exclusively from a certain seller or to sell exclusively to a certain buyer. In these recurrent categories, the courts have to decide whether the person who drafted the restraint of trade clause has avoided imposing undue restrictions on the promisor in relation to area, time and subject matter.

We will now look at some examples of these categories. Note, however, as one judge said, that

> [t]he categories of restraint of trade are not closed. As methods of trading change, so do the areas of restraint. The law, if it is to fulfil its purpose, must keep pace with them.[51]

Employment contracts

[41.90] An employer cannot legally preclude an employee from competition per se after the termination of the employee's employment. An employee who acquires skill and technical knowledge in the course of employment may later use such expertise in competition with the employer. However, an employee cannot divulge or use trade secrets of the employer or

47 *Brooks v Burns Philp Trustee Co* (1969) 121 CLR 432, 466–7.

48 See, eg, *McFarlane v Daniell* (1938) 38 SR (NSW) 337.

49 See *Humphries v "Surfers Palms North" Group Titles Plan 1955* (1994) 179 CLR 597, 621.

50 *Lloyd's Ships Holdings Pty Ltd v Davros* (1987) 17 FCR 505, 512.

51 *Petrofina (Gt Britain) Ltd v Martin* [1966] Ch 146, 169.

entice away old customers by solicitation. Moreover, the employer may protect its business, by contractual restraint of reasonable width, from use by an employee of intimate knowledge of customers acquired by the employee in the course of employment. The employer might thus protect itself against a voluntary flow of customers to its former employee by means of a provision against serving the old customers for a limited period or a provision against carrying on a rival business at all in a certain locality.

In *Lindner v Murdock's Garage*,[52] Lindner, a mechanic, was employed by motor engineers – Murdock's Garage. His contract of employment stated that it applied to the sales territory for motor vehicles of the Garage, which covered Crystal Brook and Wirrabara. These two towns were not fewer than 10 miles apart. Lindner worked in the repairs workshop in Crystal Brook for some years. When he left this employment, Murdock's Garage sought to restrain him by injunction from working with a competing business in Crystal Brook. Murdock's Garage relied on a clause in the contract to the effect that Lindner would not within one year of termination of his employment work in the same sort of business within the same area.

The majority of the High Court held that this clause was unenforceable. It went beyond what was reasonable for the protection of Murdock's Garage's business. The Garage needed protection for its business connection against the possibility of its being affected by the personal knowledge of and influence over customers which Lindner might acquire in the course of his employment. He might acquire knowledge of customers' credit, peculiarities and so on. However, for a geographical limit to be reasonable, it must be formulated with reference to the employer's customers of whom the employee is likely to acquire special knowledge. The clause in this case covered two towns. The contract did not specify at which place Lindner would be employed and he may have been, and was in fact, employed solely in one. A person employed in one area was unlikely to come into contact with customers in the other area. Accordingly, the restraint should have been limited to the area in which the employee in fact worked within a reasonable time before termination of employment. As the clause was not so limited, it was held to be void. Whilst the courts may delete part of a clause if doing so would render the clause reasonable, the courts will not add words or change words (see further [42.45]).

The decision of the New South Wales Court of Appeal in *Miles v Genesys Wealth Advisors Ltd*[53] provides an example of a restraint that was held to be reasonable and therefore enforceable. Genesys provided services to firms offering financial planning services. Mr Miles had worked as the Chief Executive Officer and, subsequently, Managing Director of a company that merged with another financial services firm to form Genesys. Mr Miles then became the Managing Director of Genesys. Mr Miles' role was highly strategic and involved, inter alia, the management of Genesys' relationships with its clients. He was also aware of which firms were highly profitable and which firms may discontinue their relationship with Genesys. When Mr Miles left Genesys' employment on 15 September 2007, he signed a deed of release in which he promised not to engage in any business or activity substantially similar to or competitive with the business of Genesys or become an employee of a competitive business until at least 15 September 2009. The deed of release also imposed obligations that required him not to disclose confidential information. Hodgson JA held that the restraint clause went no further than necessary to protect Genesys' legitimate interests. In reaching the conclusion

52 *Lindner v Murdock's Garage* (1959) 83 CLR 628.

53 *Miles v Genesys Wealth Advisors Ltd* [2009] NSWCA 25.

that the restraint clause was valid, Hodgson JA noted that Mr Miles was a senior officer of the company who had a good reputation with Genesys' clients and an intimate knowledge of Genesys' commercial strategy.[54] Hodgson JA was also influenced by the fact that Mr Miles freely agreed to the restraint clause after having had the benefit of legal advice.[55]

Often employment contracts will include other provisions, such as non-solicitation and confidentiality clauses, designed to protect the employers' interests. In *Pearson v HRX Holdings Pty Ltd*,[56] the employee argued that the restraint clause could not be said to be reasonably necessary because of the protection offered to the employer by the other clauses. After noting Pearson's considerable position of influence over HRX Holdings' customers, the court found that the employer's interest in customer connections "went beyond HRX's interest in confidential information and would not be sufficiently protected by the confidentiality provision".[57] The protection offered by the non-solicitation clause was incomplete as breaches of such clauses can be difficult to detect and enforce. Further, the clause did not stop HRX Holdings' customers following Pearson unbidden to a new employer. In finding that the restraint clause was valid, the court was also influenced by the fact that Pearson was in a strong bargaining position, had access to legal advice and had received substantial compensation (in the form of shares and payment of salary for all but three months of the restraint period) in exchange for agreeing to the restraint.

Sale of a business

[41.95] A wider range of restraints will be valid where a person sells a business (and goodwill) than is the case where a restriction is imposed on a former employee. As Gibbs J noted in *Geraghty v Minter*[58] "[t]he courts in general take a stricter and less favourable view of covenants in restraint of trade entered into between employer and employee than of similar covenants between vendor and purchaser".[59] Restraints imposed on a party who has sold his or her business are legitimate, for example, where without such a restraint the value of the goodwill which the purchaser had purchased would be put at risk. Often a seller would not be able to obtain a good price unless obligated not to compete with the purchaser.

In *Nordenfelt v The Maxim Nordenfelt Guns and Ammunition Company Ltd*,[60] Nordenfelt established a valuable business in connection with the manufacture of guns. His trade was worldwide. He sold the business and entered into a covenant not to engage in a competing business for 25 years. It was held that this covenant was reasonable for the protection of the purchaser. Although the restraint applied worldwide, the nature of the business was worldwide. The restraint "enabled Mr Nordenfelt to obtain the full value of what he had to sell; without it the purchasers could not have been protected in possession of what they wished to buy".[61] The restraint was also reasonable in the interests of the public.

54 *Miles v Genesys Wealth Advisors Ltd* [2009] NSWCA 25, [38].

55 *Miles v Genesys Wealth Advisors Ltd* [2009] NSWCA 25, [40].

56 *Pearson v HRX Holdings Pty Ltd* [2012] FCAFC 111; (2012) 205 FCR 187.

57 *Pearson v HRX Holdings Pty Ltd* [2012] FCAFC 111; (2012) 205 FCR 187, [51].

58 *Geraghty v Minter* (1979) 142 CLR 177.

59 *Geraghty v Minter* (1979) 142 CLR 177, 185.

60 *Nordenfelt v The Maxim Nordenfelt Guns and Ammunition Company Ltd* [1894] AC 535.

61 *Nordenfelt v The Maxim Nordenfelt Guns and Ammunition Company Ltd* [1894] AC 535, 573.

Franchise agreements

[41.97] Franchise agreements have characteristics in common with both employment and sale of business contracts.[62] The franchisee may have knowledge of trade secrets and the capacity to entice customers away from the franchise business. The franchisor also has a legitimate interest in protecting the goodwill of the franchise. Thus, the principles applicable to the "employment" and "sale of business" categories of cases are relevant when assessing the validity of restraint clauses in franchise agreements. In *BB Australia Pty Ltd v Karioi Pty Ltd*,[63] the franchise agreement gave Karioi Pty Ltd, the franchisee, the right to operate its two existing video store businesses under the Blockbuster banner. When the franchise agreement expired, the franchisor sought to enforce a clause that restrained the franchisee from operating a similar business within a 30 kilometre radius of the stores that had been operated by the franchisee during the term of the franchise agreement. If enforceable, this would have prevented the franchisee from operating its business from premises that it possessed prior to its entry into the franchisee agreement. MacFarlan JA (Giles JA and Sackville AJA agreeing) held that the clause in question was unenforceable. His Honour first considered principles relevant to "sale of business" cases. As the franchisee would no longer be entitled to use the Blockbuster name or business systems, the franchisor had no goodwill to protect. His Honour then considered principles drawn from "employment" cases. The nature of the business in question meant it was unlikely that the franchisee would develop relationships with clients of a kind that would allow the franchisee to entice customers away from the franchisor. Further, other restrictions imposed upon the franchisee adequately protected the franchisor against the misuse of confidential information.

Exclusive dealing contracts

[41.100] The restraint of trade rules apply to an agreement by which a trader undertakes to buy exclusively from one supplier all the goods of a particular kind that the trader needs for purposes of trade. Equally covered is an undertaking by a producer of goods to sell the goods exclusively to one buyer. Moreover, the rules apply where the restraint extends only to the use of a particular piece of land, for example, where a farmer agrees to sell all the farm's produce to a particular buyer. However, there is support for the view that the rules do not apply where a person buys, or takes a tenancy of, land which is made subject to a tie. Such a person, having no previous right to trade on that land or be there at all, gives up no freedom.[64]

In *Amoco Australia Pty Ltd v Rocca Bros Motor Engineering Co Pty Ltd*,[65] Rocca leased its service station to Amoco for a term of 15 years and Amoco granted Rocca an underlease for the same term less one day. Rocca covenanted with Amoco to carry on the business of a petrol service station on the premises for the term of the lease and to purchase petrol, to the extent of 8000 gallons per month, exclusively from Amoco as long as Amoco could supply the same. Amoco agreed to supply petrol at usual list prices, to pay for certain works at the service station and to lend Rocca plant and equipment for its operations. After a few years,

62 *Dyno Rod Plc v Reeve* [1999] FSR 148, 153.

63 *BB Australia Pty Ltd v Karioi Pty Ltd* [2010] NSWCA 347.

64 *Esso Petroleum Co Ltd v Harper's Garage (Stourport) Ltd* [1968] AC 269; *Quadramain Pty Ltd v Sevastapol Investments Pty Ltd* (1976) 133 CLR 390; *Peters (WA) Ltd v Petersville Ltd* [2001] HCA 45; (2001) 205 CLR 126, [20].

65 *Amoco Australia Pty Ltd v Rocca Bros Motor Engineering Co Pty Ltd* (1973) 133 CLR 288.

Rocca wanted to buy petrol from an oil company other than Amoco. It argued that it was not bound by the covenants in the underlease as (1) they were in restraint of trade and (2) the restraint was unreasonable. The majority of the High Court agreed. As to (1), even if a person who takes a tenancy subject to a tie gives up no right or freedom (as noted earlier), that is not what happened here. The lease and underlease formed part of the one transaction. The effect of that transaction was that Rocca subjected itself to restrictions as to the use of the land which it was previously free to use as it pleased. As to (2), while it was reasonable for Amoco to protect its commercial interests in a stable and economical system of distribution, and in the investment of moneys outlaid for the benefit of Rocca, by means of a solus agreement, a tie for a period as long as 15 years on the terms of the underlease was not reasonably necessary to protect those interests.

Legislative intervention

[41.105] Restraint of trade is also restricted by the *Competition and Consumer Act 2010* (Cth). Part IV of that Act, which is not examined in this book, is concerned with anti-competitive conduct. It seeks to prevent, inter alia, contracts, arrangements and understandings which substantially lessen competition. There are specific provisions prohibiting misuse of market power, anti-competitive agreements, exclusive dealing contracts that substantially lessen competition, retail price maintenance and so on. However, the common law rules governing the legality of restraints on employees, partners and sellers of goodwill have not been affected by the *Competition and Consumer Act 2010*.[66] Section 4M of the *Competition and Consumer Act 2010* provides that the Act does not affect the common law doctrine of restraint of trade in so far as that law is capable of operating concurrently with the Act.

CONTRACTS EXCLUDING THE JURISDICTION OF THE COURTS

[41.110] A contractual attempt to exclude the right to sue in court is against public policy.[67] For example, in *Baker v Jones*,[68] the constitutional rules of an unincorporated association provided that the central council of the association was to be the sole interpreter of the rules and that the council's decisions in all circumstances would be final. The council decided to apply the association's funds towards defraying personal legal costs incurred by certain members of the association. Another member sought a declaration from the court that the payments were unlawful. The council members argued that their decision was final under the rules of the constitution. The court rejected this argument. It pointed out that the relationship between the members of an unincorporated association is contractual and that the contract is found in the association's rules. Such a contract is subject to the limits imposed by public policy, including the limit that parties cannot, by contract, oust the ordinary courts from their jurisdiction. The members of the association could make a council or tribunal the final arbiter on questions of fact, but not on questions of law. The interpretation of the rules was a question of law that the courts would examine. After an examination of the rules in this case, the court concluded that the payments were unlawful.

66 See s 51(2).

67 *Brooks v Burns Philp Trustee Co* (1969) 121 CLR 432. Note however that a party to an agreement may not intend to enter legal relations in the first place: see Chapter 5.

68 *Baker v Jones* [1954] 2 All ER 553. See also *Brooks v Burns Philp Trustee Co Ltd* (1969) 121 CLR 432, 552–3.

Another example under this head is the decision of the High Court in *Brooks v Burns Philp Trustee Co Pty Ltd*.[69] Mrs Brooks instituted divorce proceedings and indicated to her husband that in the event of a decree absolute being granted, she would apply to the court for an order of permanent alimony. The parties executed at this time a deed of settlement. Under cl 1(b), Mr Brooks covenanted that "as from the granting of the decree absolute", he would "during the life of the wife pay to her the sum of thirteen pounds seven shillings per week". Under cl 2, Mrs Brooks covenanted that she would "accept the terms provided by this deed in full settlement of all claims against the husband for alimony and maintenance of any description". Under cl 3, Mr Brooks covenanted that, if required to do so by Mrs Brooks, he would consent to an order being made by the court for payment of the weekly sums covenanted to be paid by him in order to secure to Mrs Brooks those weekly payments. On the day following the execution of this deed, Mrs Brooks obtained a decree nisi for dissolution of the marriage and six months later a decree absolute. Mr Brooks thereafter paid the weekly sums he had promised and Mrs Brooks never applied to the court for alimony or maintenance. When Mr Brooks died, the executors of his estate asked the court whether they were still bound to pay the weekly sums to Mrs Brooks.

Counsel for Mr Brooks' executors admitted that the position he defended was "not ideal from the point of view of fairness". Even so, the High Court held by a majority (Kitto, Taylor and Owen JJ) that the executors were *not* bound to pay the weekly sums to Mrs Brooks under the deed. Her covenant in cl 2 was held to be void as an attempt to oust the jurisdiction of the court to make an order with respect to alimony in the cause then pending. Although cl 3 contemplated a possible application to the court to secure the payments provided for in cl 1(b), cl 2 still purported to preclude Mrs Brooks from seeking any order for payments other than those set out in cl 1(b). In other words, although cl 2 could not be described as purporting to oust the jurisdiction completely, it did purport to oust the jurisdiction to award more than the agreed amounts. Further, as the covenant by Mr Brooks in cl 1(b) was *dependent* on the covenant by Mrs Brooks in cl 2, it too was void. The two covenants were intended to operate reciprocally or not at all: each in relation to the other was a quid pro quo. As a result, Mr Brooks' promise could not have been enforced during his lifetime, nor was it enforceable now against his executors.

Menzies J held in a dissenting judgment that there was no ouster of the court's jurisdiction because the effect of cl 3 was that cl 2 did not bind Mrs Brooks to accept her husband's covenant in lieu of a court order for alimony. She could in terms of the deed apply to the court.

Windeyer J, in an impressive dissenting judgment, pointed out that for a period of time, Mrs Brooks could have applied to the court for an order for maintenance, but she did not do so. She was content with Mr Brooks' promise and he faithfully kept that promise during his lifetime. "It is now said that, because in the past she might have asked the court to pay her more than he had promised, she is not now to have what he promised. And this result it is said flows from the law's regard for public policy."[70] In the present context, Windeyer J considered that the label "ousting the jurisdiction" must be read in the sense of relinquishing statutory rights that cannot be effectively relinquished because of considerations of public policy. It was indisputable, in his view, that Mr Brooks could not have kept Mrs Brooks to her promise to relinquish her rights. But it did not follow that he was entitled to repudiate his promises. So long as Mrs Brooks *in fact kept her promise*, Mr Brooks was bound by his. Her

69 *Brooks v Burns Philp Trustee Co Pty Ltd* (1969) 121 CLR 432.

70 *Brooks v Burns Philp Trustee Co Ltd* (1969) 121 CLR 432, 450.

promise was not a promise to do something illegal or immoral; it was merely an unenforceable or non-binding promise. She could lawfully keep her promise if she wished. Public policy merely prevented her *abandoning* her statutory rights – it did not require that she *assert* them. Moreover, in Windeyer J's view, Mrs Brooks' unenforceable promise did not render Mr Brooks' related and dependent promise to pay the money unenforceable. The dependency of the mutual covenants implied that each covenantor should perform or be ready to perform his or her promise, not that the promise be enforceable:

> an agreement by which money is to be paid conditionally on the actual performance of an unenforceable, but not illegal, promise is a valid contract if it is supported by some other consideration than the unenforceable promise. I see no reason why it should not be equally valid if it is under seal.[71]

A contractual clause that deters, as opposed to prohibits, a party from commencing legal proceedings may also be struck down as contrary to public policy. In *Materials Fabrication Pty Ltd v Baulderstone Pty Ltd*,[72] a clause that provided that the subcontractor be stopped from commencing proceedings until it had deposited to the trust account of the Builder's solicitor an amount equal to 10 per cent of the amount claimed by the subcontractor in the proceedings was held to be void on public policy grounds. By erecting a significant financial barrier to the commencement of legal proceedings, the clause was held to have the effect of ousting the jurisdiction of the court.

A compromise of a private action does not always offend the policy against excluding the jurisdiction of the courts. For example, contractual and tortious claims can be settled out of court.[73] Nor does an arbitration clause (ie, a clause which refers a dispute to an arbitrator), provided that the exclusive power of the arbitrator is limited to the determination of issues of fact. The common law regarded a clause that made arbitration a condition precedent to legal proceedings as valid. Such a clause is known, after the leading case,[74] as a "*Scott v Avery* clause". Until 2010, uniform commercial arbitration legislation provided that such clauses did not operate to prevent legal proceedings.[75] The uniform commercial arbitration regime has, however, been reformed in a manner that will facilitate greater use of arbitration agreements. In 2010, the States and Territories agreed to bring the uniform commercial arbitration regime into line with the *UNCITRAL Model Law on International Commercial Arbitration* (as amended in 2006). The uniform commercial arbitration legislation now provides that, subject to certain exceptions: "A court before which an action is brought in a matter which is the subject of an arbitration agreement must, if a party so requests … refer the parties to aribitration".[76]

71 *Brooks v Burns Philp Trustee Co Ltd* (1969) 121 CLR 432, 467.

72 *Materials Fabrication Pty Ltd v Baulderstone Pty Ltd* [2009] VSC 405.

73 *Felton v Mulligan* (1971) 124 CLR 367, 385–6.

74 *Scott v Avery* (1856) 5 HL Cas 811; 10 ER 1121.

75 See s 55 of the *Commercial Arbitration Act 1986* (ACT); *Commercial Arbitration Act 1984* (NSW); *Commercial Arbitration Act* (NT); *Commercial Arbitration Act 1990* (Qld); *Commercial Arbitration and Industrial Referral Agreements Act 1986* (SA); *Commercial Arbitration Act 1986* (Tas); *Commercial Arbitration Act 1984* (Vic); *Commercial Arbitration Act 1985* (WA).

76 See s 8 of the *Commercial Arbitration Act 2017* (ACT); *Commercial Arbitration Act 2010* (NSW); *Commercial Arbitration (National Uniform Legislation) Act 2011* (NT); *Commercial Arbitration Act 2013* (Qld); *Commercial Arbitration Act 2011* (SA); *Commercial Arbitration Act 2011* (Tas); *Commercial Arbitration Act 2011* (Vic); *Commercial Arbitration Act 2012* (WA).

CHAPTER **42**

The consequences of illegality

[42.05] In the introduction to this Part, and in the course of the last two chapters, we have seen that two major consequences may flow from illegality: unenforceability and non-retrieval. In this chapter, we consider when illegality will prevent one or both parties from enforcing their contractual rights. We will also consider when other actions, such as restitutionary claims or tortious actions, will be unavailable because of their association with an illegal contract.

CONTRACTUAL CONSEQUENCES: UNENFORCEABILITY

Statutory illegality

[42.10] If the contract itself (or a contractual term) is prohibited by statute, whether expressly or by implication,[1] then, subject to any provision or implication to the contrary in the statute, *neither* party can enforce the contract (or the term).[2] Even a party who is innocent of any wrongdoing will not be allowed to enforce a contract that is prohibited by statute. However, this does not mean that considerations such as one party's innocence are entirely irrelevant. Quite often such considerations lead the court to find that the contract in question is not prohibited by statute on the basis that it is unlikely that parliament intended that such consequences be visited upon an innocent party. This is an example of the process of reasoning referred to at [Pt XID.25] as reasoning backwards ("the plaintiff ought to be able to recover") to a conceptual conclusion ("therefore the contract is not prohibited"). Adopting this approach, the court might also find that only the party responsible for the illegality loses his or her right to enforce the contract.[3] Such reasoning is evident in *Yango Pastoral Co Pty Ltd v First*

1 See Chapter 40.
2 *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd* (1978) 139 CLR 410.
3 *Australian Competition and Consumer Commission v Baxter Healthcare Pty Ltd* [2007] HCA 38; (2007) 232 CLR 1, [44].

Chicago Australia Ltd.[4] Yango, contrary to s 8 of the *Banking Act 1959* (Cth), carried on the business of banking. In the process of doing so, it lent funds to First Chicago. First Chicago resisted repaying the loan, arguing that the loan contract was impliedly prohibited by s 8 of the *Banking Act 1959* (Cth). Gibbs ACJ and Mason J (in separate judgments) reflected on the practical effect of finding that the contract was impliedly prohibited. It would not only mean that the wrongdoer (Yango) lost its ability to recover monies owed to it but also that innocent depositors would be unable to recover monies deposited with Yango. As it was unlikely that parliament would intend such consequences to be inflicted on innocent depositors, the statute was held not impliedly to prohibit contracts entered into in breach of s 8.

When considering the consequences of a finding of statutory illegality, the court is involved in the task of statutory interpretation. The court must determine, in accordance with the ordinary principles that govern the construction of statutes, whether the legislature intended to render a contract void. As noted above, the general rule that neither party can enforce a contract which is prohibited by statute is subject to any implication to the contrary in the relevant statute. It is possible that a court will find that, even though legislation impliedly prohibits entry into the contract in question, the statute properly interpreted provides that the contract should nevertheless be enforceable because of the impact unenforceability would have on an innocent party and/or third parties.[5]

Common law illegality

[42.15] As discussed in Chapter 41, a contract which involves illegal conduct may be unenforceable at common law on the ground of public policy even though the contract is not expressly or impliedly prohibited by statute. This has traditionally been justified by reference to the maxim *ex turpi causa non oritur actio* – an action does not arise from a base cause – but it is doubtful whether the maxim now properly describes either the basis of the rule or its usual effect. Despite the illegality, one or both of the parties should nevertheless be able to enforce the contract. The relevant considerations are captured by the *in pari delicto potior est conditio defendentis* maxim – where there is equal fault, the defendant is in the stronger position. However, as McHugh and Gummow JJ noted in *Fitzgerald v F J Leonhardt Pty Ltd*,[6] contract cases should "not be approached by considering any general in pari delicto doctrine".[7] Rather, the court should first consider whether the case comes within one of the "exceptions" or qualifications to the ex turpi causa approach summarised by McHugh J in the following passage from *Nelson v Nelson*:[8]

> First, the courts will not refuse relief where the claimant was ignorant or mistaken as to the factual circumstances which render an agreement or arrangement illegal. Second, the courts will not refuse relief where the statutory scheme rendering a contract or arrangement illegal was enacted for the benefit of a class of which the claimant is a member. Third, the courts will not refuse relief where an illegal agreement was induced by the defendant's fraud, oppression or undue influence. Fourth, the courts will not refuse relief where the illegal purpose has not been carried into effect.

4 *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd* (1978) 139 CLR 410, 413, see [40.25].
5 See *Bondlake Pty Ltd v Owners – Strata Plan No 60285* [2005] NSWCA 35; (2005) 62 NSWLR 158, 166, discussed at [40.35].
6 *Fitzgerald v F J Leonhardt Pty Ltd* (1997) 189 CLR 215.
7 *Fitzgerald v F J Leonhardt Pty Ltd* (1997) 189 CLR 215, 229.
8 *Nelson v Nelson* (1995) 184 CLR 538, 604–5.

McHugh J went on to note that, even if the case did not come within one of the four "exceptions" listed:

> Courts should not refuse to enforce legal or equitable rights simply because they arose out of or were associated with an unlawful purpose unless: (a) the statute discloses an intention that those rights should be unenforceable in all circumstances; or (b)(i) the sanction of refusing to enforce those rights is not disproportionate to the seriousness of the unlawful conduct; (ii) the imposition of the sanction is necessary, having regard to the terms of the statute, to protect its objects and policies; and (iii) the statute does not disclose an intention that the sanctions and remedies contained in the statute are to be the only legal consequences of a breach of the statute or the frustration of its policies.

Although McHugh J's comments were made in the context of public policy concerns raised by a breach of statute, they are of relevance when considering other forms of common law illegality. The comments are indicative of a more nuanced approach to illegality that sees the court balance its desire to uphold bargains against concerns associated with aiding the enforcement of agreements associated with unlawful conduct.

The way in which the court deals with the illegal performance of a contract demonstrates the flexibility in the common law approach. It also provides an example of other policy considerations trumping the concerns encapsulated in the *ex turpi* maxim. Where a contract is not illegal, but has been performed in an illegal manner, the unenforceability rule is modified. If *both* parties to a contract intend that a wrongful mode of performance should be adopted, the general rule is that *neither* party may sue on the contract. If, however, only *one* party intends to perform it in an illegal way, the innocent party who was unaware of the illegality may have a remedy. The *in pari delicto potior est conditio defendentis* maxim does not apply because the parties are not equally at fault. *Marles v Philip Trant and Sons*[9] provides an example of such reasoning. The plaintiff was a farmer and the defendants were seed merchants. The plaintiff ordered spring wheat seed, but the defendants in breach of contract delivered winter wheat seed. When the defendants delivered the seed to the plaintiff, they failed to comply with certain statutory requirements relating to the provision of an invoice. The court held that the plaintiff could sue for breach of contract as the plaintiff was an innocent party. If the defendant had sued the plaintiff for some breach of the contract, the plaintiff may have raised the defendants' illegal performance as a defence.

CONTRACTUAL CONSEQUENCES: SEVERANCE

[42.20] Illegality will not necessarily cause the entire contract to be rendered unenforceable. In fact, it may be that only one clause raises illegality concerns. In such circumstances, the offending term may be "severed" from the contract, with the balance of the contract remaining enforceable. As Kitto J noted in *Brooks v Burns Philp Trustee Co Pty Ltd*,[10] "[q]uestions of severability are often difficult, and tests that have been formulated as useful in particular classes of cases are not always satisfactory for cases of other kinds". That said, severance will generally be available where two conditions are met. First, the common law severance test must be met. A clause will not be severed if doing so changes the nature of the bargain reached between the parties. Secondly, even if the common law severance test is met, it must

9 *Marles v Philip Trant and Sons* [1954] 1 QB 29.

10 *Brooks v Burns Philp Trustee Co Pty Ltd* (1969) 121 CLR 432, 438. See also *Humphries v "Surfers Palms North" Group Titles Plan 1955* (1994) 179 CLR 597, 618, 621.

be determined that severance is an appropriate response to the illegality in question. In the context of statutory illegality, this is a matter of statutory interpretation. In the context of common law illegality, this involves determining whether severing the offending term is an appropriate response to any public policy issues raised by the contract.

Criteria determining severability

[42.25] The courts will not sever a term if doing so inappropriately reshapes the parties' bargain. The test of severability generally adopted is the same as that applied to provisions which have been found wanting on the ground of uncertainty.[11] The court will ask whether the defective promise is so material a promise in the whole contract that there should be inferred an intention not to make a contract that would operate without it. If the promise is so material, severance will not be allowed.

Another test, which comes to much the same thing, is whether the defective promise must be treated as forming with the valid promises an indivisible whole which cannot be taken to pieces without altering its nature.[12] The question, in other words, is whether severance of the defective promise would "alter the nature of the bargain as a whole" or make it a different kind of contract.[13]

In *Electric Appliance Pty Ltd v Doug Thorley Caravans (Australia) Pty Ltd*,[14] there was an agreement between a finance company and a dealer which included a promise by the finance company to pay the dealer a commission. This was contrary to the *Hire Purchase Act 1959* (Vic). The contract was illegal both as a contract to commit a criminal offence and as one prohibited by statute. Could the promise to pay the commission be severed? The court, proceeding on the basis that the criminality of the present promise was not a bar to the question of severance, held that the promise was so material in the whole bargain that there should be inferred an intention not to make a contract which would operate without it, but to make a contract which was conditional upon the operation of that promise. Hence, severance was ruled out and the contract could not be enforced.

Finally, it should be noted that a promise given *in return for* a void promise cannot be saved by severance of the void promise. If the void promise is the sole consideration for the legal promise, the latter will be rendered unenforceable for want of consideration. Even if the promises are in a deed, so that consideration is not a prerequisite of enforceability, the promises may be interpreted as *mutually dependent*. In such a case, the unenforceability of one seals the fate of the other. In *Brooks v Burns Philp Trustee Co Pty Ltd*,[15] the promises of the husband and wife were construed as mutually dependent. The result was that, according to the majority of the judges, the voidness of the wife's promise not to apply for alimony rendered the husband's reciprocal promise of weekly payments void or unenforceable as well. However, the dissenting judgment of Windeyer J to the contrary is persuasive.[16]

11 See [6.65].

12 *Brew v Whitlock (No 2)* [1967] VR 803, 811–3.

13 *Brew v Whitlock (No 2)* [1967] VR 803, 812.

14 *Electric Appliance Pty Ltd v Doug Thorley Caravans (Australia) Pty Ltd* [1981] VR 799.

15 *Brooks v Burns Philp Trustee Co Pty Ltd* (1969) 121 CLR 432, see [41.110].

16 See [41.110].

When is severance an appropriate response to illegality?

Statutory illegality

[42.30] In the case of statutory illegality, whether severance is an available option is a matter of statutory interpretation. Sometimes the statute will explicitly deal with the matter. For example, the statute may render particular provisions, rather than the entire contract, void or unenforceable. Section 4L of the *Competition and Consumer Act 2010* (Cth) provides an example of such a provision. It provides that "[i]f the making of a contract … contravenes this Act by reason of the inclusion of a particular provision in the contract, then … nothing in this Act affects the validity or enforceability of the contract … in so far as that provision is severable".

It is also possible that only part of a clause will be rendered void by statute. In *Zurich Australia Insurance Ltd v Metals & Minerals Insurance Pte Ltd*,[17] the High Court considered the operation of s 45(1) of the *Insurance Contracts Act 1984* (Cth). Section 45(1) rendered void a provision in a contract of general insurance that excluded liability of the insurer where the insured had entered into another contract of insurance in relation to the same risk. French CJ, Gummow and Crennan JJ found that the word "provision" was not to be equated with a clause of the contract. Each "clause" may contain two or more "provisions". Where a clause in an insurance contract applies to two different circumstances, s 45(1) operated only to render void that part of the clause that had the effect stipulated in s 45(1).[18] *Thomas Brown and Sons Ltd v Fazal Deen*[19] was concerned with a contractual bailment of gold bars and gems. Regulation 14(1) of the *National Security (Exchange Control) Regulations* required every person with gold to deliver it to the Commonwealth Bank within one month of the gold coming into that person's possession. The illegality of the transaction relating to the gold bars was held not to affect the legality of the transaction relating to the gems. The test applied here was that a clause is severable if its elimination changes the extent only, but not the kind of contract. On the other hand, in *North v Marra Developments Ltd*,[20] the court refused to sever the offending part of a claimant's illegal conduct. A stockbroker advised its client regarding a scheme to establish an inflated market price for the client's shares by means of the stockbroker purchasing some of the shares itself. The aim was to assist the client in the takeover of another company. The stockbroker's later claim to be remunerated by the client for professional services failed. The performance of its services had involved contemplated illegal conduct. The court held that, because the illegal conduct became an integral element in the stockbroker's performance of the contract of services, there was no basis for treating the illegality as collateral only or as severable from the remainder of the work undertaken by the stockbroker.[21]

Common law illegality

[42.35] In cases of common law illegality, the court will consider whether the degree of obloquy attaching to the violation of public policy in any particular case justifies rendering

17 *Zurich Australia Insurance Ltd v Metals & Minerals Insurance Pte Ltd* [2009] HCA 50; (2009) 240 CLR 391.

18 *Zurich Australia Insurance Ltd v Metals & Minerals Insurance Pte Ltd* [2009] HCA 50; (2009) 240 CLR 391, [31].

19 *Thomas Brown and Sons Ltd v Fazal Deen* (1962) 108 CLR 391, see [42.20].

20 *North v Marra Developments Ltd* (1981) 148 CLR 42, see [41.10].

21 *North v Marra Developments Ltd* (1981) 148 CLR 42, 60–1.

the whole contract, as distinct from particular clause(s), against "public policy". In such circumstances, it is then necessary to consider the importance of the particular clause(s) to the overall scheme of the contract. Where the clause is of minor significance, the balance of the contract may be enforceable.

The most common example of severance in response to unenforceability at common law occurs in the case of covenants found to impose an unreasonable restraint of trade.[22] In such cases, as the offending clause is regarded as merely "void" rather than unlawful, severance appears in order. However, a restraint of trade provision may be so fundamental to the arrangement that its unenforceability renders the entire contract unenforceable. In *Amoco Australia Pty Ltd v Rocca Bros Motor Engineering Co Pty Ltd*,[23] the High Court held that the promise by Rocca Bros in the underlease to purchase all its petrol from Amoco for 15 years was an unreasonable restraint of trade. In later proceedings,[24] it was held further that the trade tie was so fundamental to the underlease that its unenforceability rendered the whole transaction, lease and underlease, unenforceable by either party.

Other clauses that are traditionally treated as void and severed from the contract are clauses that attempt to oust the jurisdiction of the courts[25] and penalty clauses.[26] In other cases, where the clause may be of a more offensive kind, severance is less likely. For example, a promise to commit a crime such as murder is hardly a candidate for severance. However, it appears that provided the relevant offence is not of a heinous character, severance is possible.[27]

In *A v Hayden*,[28] the court appears to have proceeded on the assumption that public policy concerns affected the enforceability of the offending term only, and not the entire contract. The plaintiffs allegedly committed various offences in a hotel in the course of a training exercise organised by the ASIS. They sought injunctions to prevent their identities being revealed to the police for the purpose of prosecutions. They relied on confidentiality clauses in their contracts of employment with the Commonwealth to the effect that their identities would not be revealed to anyone. The court disallowed the plaintiffs' claims on the basis that the contracts had a tendency to adversely affect the administration of justice. However, it was not argued, nor does it seem likely, that in the case of any particular plaintiff, the *whole* contract of employment was contrary to public policy. Moreover, Deane J favoured the view that the promises were unenforceable *only to the extent* that their observance would have led to seriously adverse effects on the administration of justice.[29] Mason J also favoured this view.[30]

Severance is limited to deletion

[42.40] Severance will only ever result in words being *deleted* from a contract. The deletion may be of a clause, or it may be of only part of a clause. But because of the courts' reluctance to appear to be redrawing a contract, they will not add words or change words in order to

22 See [41.65]–[41.100].

23 *Amoco Australia Pty Ltd v Rocca Bros Motor Engineering Co Pty Ltd* (1973) 133 CLR 288. See also [41.100].

24 *Amoco Australia Pty Ltd v Rocca Bros Motor Engineering Co Pty Ltd* [1975] AC 561.

25 See [41.110].

26 See Chapter 28.

27 See *Electric Appliance Pty Ltd v Doug Thorley Caravans (Australia) Pty Ltd* [1981] VR 799.

28 *A v Hayden* (1984) 156 CLR 532.

29 *A v Hayden* (1984) 156 CLR 532, 596.

30 *A v Hayden* (1984) 156 CLR 532, 557.

make sense of what is left. Certain words or phrases may be deleted provided the meaning of what is left is not altered and makes sense independently of what is severed. For example, a person who sells a business in town A may promise the purchaser not to set up a rival business in towns A, B or C. If the court finds this is an unreasonable restraint of trade, it might be prepared to sever the phrase "B or C", leaving a promise restricted to town A. The meaning of what is left is not altered and makes sense independently of what was severed.

The reluctance of the courts to be seen to be rewriting contracts stems from a belief that by deleting rather than rewriting, the court is less likely to override the parties' intentions. The Canadian Supreme Court has said, however, that an approach which only allows for deletion of words is less likely to accord with the intentions of the parties. In *Transport North American Express Inc v New Solutions Financial Corporation*,[31] the parties entered into a loan agreement which provided for a rate of interest made illegal under statute. The Supreme Court of Canada held that, at least in cases of this sort, "notional severance" of the offending provisions was available as a remedy. Notional severance would mean severing only those provisions of the loan agreement that put the effective interest rate over the 60 per cent permitted by statute. Under the deletion-only approach, the court could only save the contract by deleting the stated interest rate, effectively providing for an interest-free loan, something it would have been unlikely to do given the demonstrated intention of the parties to charge and pay a very high rate of interest.

In *Peters Ice Cream (Vic) Ltd v Todd*,[32] Todd promised not to sell ice cream other than Peters "within a reasonable distance from my present place of business" in return for Peters' promise to supply him with ice cream. The court held that Todd's promise was void. The contract did not itself express any criteria for determining what was a reasonable distance and the court was not prepared to declare from time to time a distance that was reasonable and therefore valid. Nor could severance save the clause. To sever the whole phrase "within a reasonable distance from my present place of business" was inappropriate as the parties had indicated by their language that the area was not to be unlimited. Further, to sever the words "within a reasonable distance" would mean that the prohibition was against sales "from my present place of business". The word "from" would have a different meaning in the contract as severed from what it had in the original document.

A contractual provision in restraint of trade can be drafted in a way that anticipates severance. It may, for example, set out different *variables* of:

1. the kind of conduct proscribed (eg, the manufacturing of items A, B, C or D);
2. the duration of the restraint (eg, for two, four, six or eight years); and
3. the area of the restraint (eg, within a radius of three, eight, 10 or 20 kilometres).

The contract may then provide that covenants generated by the various combinations are subject to severance. This technique will be successful in defining enforceable covenants, provided the requirements of certainty are met. For example, if the widest enforceable covenant is intended by the parties, the court must be able to say which is the widest. Does a 10-kilometre radius for one year give a wider protection than a one-kilometre protection for six years? A court would not be able to say. Further, the contract must not require the court

31 *Transport North American Express Inc v New Solutions Financial Corporation* (2004) SCC 7; [2004] 1 SCR 489.

32 *Peters Ice Cream (Vic) Ltd v Todd* [1961] VR 485.

to determine the appropriate limit of restraint from the multitude of variables. The clause must be a genuine attempt to fix the covenantee's need for protection, with the agreement as to severance acting as a precaution against the possible invalidity of some of the covenants.[33]

Reform in NSW

[42.45] In New South Wales, the law relating to severability is affected by the *Restraints of Trade Act 1976* (NSW). Under this Act, a restraint of trade may be valid to the extent that it is not against public policy, whether it is in severable terms or not. This allows the courts of New South Wales to engage in what was described in the previous paragraph as "notional severance".

INDEPENDENT ACTIONS

[42.50] A party to an illegal contract may be able obtain a remedy by relying on a non-contractual cause of action such as a claim in tort or restitution. The illegality or public policy consideration that rendered the contractual rights unenforceable *may*, however, also preclude the bringing of associated non-contractual claims.

Non-retrieval: restitutionary actions

Coherence of the law

[42.55] The second potential consequence of illegality is that a party may be prevented from recovering money or property transferred under the affected contract. In other words, a claim in restitution, like a contractual claim, may founder on the defence of illegality. The ex turpi causa principle, it should be remembered, may apply in areas other than contract law. If the policy of the law is against enforcing a contract in a particular case, one would not expect the policy to be too easily side-stepped by the relying on another cause of action based on the same facts. While the importance of coherence was recently stressed in *Equuscorp Pty Ltd v Haxton*,[34] Gummow and Bell JJ also explicitly highlighted the "fallacy of an assumption that contractual and restitutionary issues can readily be collapsed".[35] The appellants sought to enforce loan agreements against the respondents. As part of a tax minimisation scheme, the respondent borrowers purchased interests in farming businesses. The purchase was funded by loans provided by Rural (who ultimately assigned the loan agreements to the appellant). The loan agreements were held to be unenforceable for illegality because, in breach of s 170 of the *Companies Code*, no valid prospectus had been issued when members of the public were invited to invest.[36] This finding that the contract itself was unenforceable on the grounds of illegality was not challenged in the High Court. Rather, the focus was on the availability of a restitutionary remedy. French CJ, Crennan and Kiefel JJ provided guidance as to when a restitutionary claim may be made, noting:

> The outcome of a restitutionary claim for benefits received under a contract which is unenforceable for illegality, will depend upon whether it would be unjust for the recipient of

33 See *Lloyd's Ships Holdings Pty Ltd v Davros* (1987) FCR 505.

34 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498.

35 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [101].

36 *Equuscorp Pty Ltd (formerly Equus Financial Services Ltd) v Bassat* [2007] VSC 553.

> a benefit under the contract to retain that benefit. There is no one-size-fits-all answer to the question of recoverability… The central policy consideration at stake … is the coherence of the law. In that context it will be relevant that the statutory purpose is protective of a class of persons from whom the claimant seeks recovery. Also relevant will be the position of the claimant and whether it is an innocent party or involved in the illegality.[37]

The High Court held that the loan monies could not be recovered by way of a restitutionary claim. Allowing such claims would have "frustrated or defeated, or have been inconsistent with, the statutory purpose of the provisions of the Code".[38] Rural was not an "arms' length" financier; it was closely related to the promoter. The loans offered by Rural furthered the illegal purpose of inviting investment without first having issued and registered a valid prospectus. It was also relevant that the borrowers were members of a class the statute aims to protect.[39] Ultimately the restitutionary claim was refused because allowing a claim in these circumstances would harm the coherence of the law. This is because Equuscorp would have been "been able to recover by such claims what the policy of the law denied it in respect of the loan agreements".[40]

In the context of statutory illegality, coherence is promoted by considering whether the statute that raised the illegality issue expressly or implicitly prohibits a restitutionary claim. This is determined by reflecting on the policy underlying the statute as well as any penalties it may impose. In the context of common law illegality, it involves considering whether allowing a restitutionary claim would be inconsistent with the policies that saw the contract under which the goods or services were transferred rendered unenforceable.

Parties not in pari delicto

[42.60] Money paid or property passed under an illegal contract may be recoverable by a party who can show that he or she was not in pari delicto, that is, was not as guilty as the other party or not as equally at fault. Despite the emphasis in *Equuscorp Pty Ltd v Haxton*,[41] on the importance of promoting the coherence of the law and preserving the policies that underpin the statute or law that raises the illegality question, it nevertheless remains appropriate to consider whether the parties are in pari delicto.

In addition to focussing on issues of coherence, French CJ, Crennan and Kiefel JJ in *Equuscorp Pty Ltd v Haxton* also found it relevant that the investors were not involved in the illegality and that they were members of a class the legislation in question aimed to protect.[42] If a party to a contract which violates a statute is a member of a class which the statute aims to protect, such a party may be characterised as not in pari delicto with the other party to the contract and may be able to claim restitution. In *Kiriri Cotton Co Ltd v Dewani*,[43] it was a statutory offence for a person letting a dwelling to receive any sum of money other than rent. Dewani paid an unlawful premium for the grant of a lease from the company. His claim for restitution of that money succeeded. The statute was intended to protect tenants from being

37 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [34].
38 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [25].
39 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [34].
40 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [45].
41 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498.
42 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [34].
43 *Kiriri Cotton Co Ltd v Dewani* [1960] AC 192.

exploited by landlords in times of housing shortage. A penalty was imposed on landlords, not tenants. Although Dewani may have been an aider and abettor of the offence, he was not in pari delicto with the company. The duty of observing the law was placed on the shoulders of the landlord for the protection of the tenant.

This case may be compared with *South Australian Cold Stores Ltd v Electricity Trust of South Australia*.[44] In that case, the prices charged for electricity by the Trust, and voluntarily paid by the company, were excessive and illegal under the *Prices Act 1948-51* (SA). The company sought to recover the amount of its overpayments and failed. The parties were in pari delicto. The object of the *Prices Act*, it was stated, is to prevent a decline in the value of money, not to protect one class against another. Even so, the result is unattractive. It left the defendant enriched at the plaintiff's expense by virtue of a mistake and it is doubtful if the public interest would have been adversely affected by a reversal of the enrichment.

A claimant who was ignorant or mistaken as to the factual circumstances, or the law, which rendered an agreement illegal is more likely to be able to recover by way of a restitutionary action.[45] So too would a party who was persuaded to enter the illegal contract by the fraud, duress or breach of fiduciary duty of the other party. Despite the illegality, such a party is regarded as innocent or as a victim and is, accordingly, less likely to be denied the right to restitution. With respect to statutory illegality, the court may reach the conclusion that the legislature did not intend to penalise an innocent party. At common law, the court may find that allowing an innocent party to recover does not offend public policy.

In *Andrews v Parker*,[46] the judge held that the contract relating to extra-marital cohabitation was not illegal. He went on to say, however, that even if he had held the contract illegal, he would have allowed the plaintiff's claim to recover his property, as the plaintiff was not in pari delicto with the defendant. The plaintiff was a weak-willed man who was put under pressure by the defendant, a strong-willed and ruthless woman, who was determined to fleece him of his property in order to find a place to live with her husband. However, it seems that it should not be inferred that parties are not in pari delicto just because one holds the rod and the other bows to it. This at least was the view taken in *Callaghan v O'Sullivan*.[47] Money that was paid to police officers to stifle a prosecution was held to be irrecoverable. The parties were held to be in pari delicto, even though the payment by one was induced by a threat to prosecute by the other. This was because both parties were regarded as equally criminal, despite the improper pressure by the police officers.

Lastly, a plaintiff may be able to retrieve money or property transferred under an illegal contract if the plaintiff can show that he or she repented before the illegal purpose was substantially achieved. In other words, where the illegal transaction is still substantially executory, the plaintiff is given an opportunity to repent (*locus poenitentiae*). It is thought that public policy is best served by allowing this opportunity before it is too late and to prevent the completion of the illegal purpose. Due notice of repudiation must be given before relief is sought. Although this exception applies where the contract is illegal on the ground that it is contrary to public policy, the exception may not be available in respect of contracts prohibited

44 *South Australian Cold Stores Ltd v Electricity Trust of South Australia* (1965) 98 CLR 65. See also *George v Greater Adelaide Land Development Co Ltd* (1929) 43 CLR 91.

45 *David Securities Pty Ltd v Commonwealth Bank of Australia* (1992) 175 CLR 353, 376, 398, 401.

46 *Andrews v Parker* [1973] Qd R 93, see [41.45].

47 *Callaghan v O'Sullivan* [1925] VLR 664, see [41.35].

by statute.[48] There are two reasons for this. First, the outcome in statutory illegality cases is determined by a process of statutory interpretation. The in pari delicto factors may, however, make the courts less likely to attribute to parliament an intention to deprive certain parties of restitutionary rights. Secondly, where a contract is prohibited by statute, the actual making of such a contract means that the illegal purpose has been substantially achieved.

In *Clegg v Wilson*,[49] the plaintiff transferred land to the defendant in return for a promise by the defendant not to give evidence in a prosecution he had caused to be commenced against the plaintiff's son. The prosecution was withdrawn by the police after the son was committed for trial on other charges. The plaintiff's agreement with the defendant was illegal as an agreement to stifle a prosecution. Moreover, the parties were in pari delicto. Nevertheless, the plaintiff succeeded in recovering her land because she had repudiated the arrangement while the illegal purpose was wholly executory.

The conclusion in *Clegg v Wilson* may seem rather odd given that the reason for the "repentance" was the realisation that an attempt to stifle the prosecution and thereby avoid the imprisonment of the plaintiff's son was otiose. Repentance and frustration of the illegal purpose are by no means the same thing. Should a person who has prepaid a contracted killer be able to claim the money back on the basis of a total failure of consideration, simply because the killer has had second thoughts? In *Alexander v Rayson*,[50] the plaintiff argued that as he had failed in his attempted fraud, and could therefore no longer use the lease documents for an illegal purpose, he was entitled to sue on them. The court rejected this argument as the plaintiff's repentance had come too late, that is, after he had been found out. However, it appears that, provided the claimant *voluntarily* withdraws before the illegal purpose is in any way achieved, there is no additional requirement that the claimant should actually have repented of the illegality.[51]

It may be difficult to determine in some cases what degree of performance is sufficient to disqualify a plaintiff from obtaining relief. In *George v Greater Adelaide Land Development Co Ltd*,[52] the company sold some land to George in respect of which planning legislation required the seller to obtain approval for a plan. It was unlawful to offer the land for sale except in accordance with the legislation. George sought to recover the instalments of purchase money he had made under the contract. The court disallowed the claim. The contract was illegal and the parties were in pari delicto. Apparently the payment of instalments signified that an illegal purpose had in fact been carried out. The court contrasted the situation before it with the case of money deposited with a *stakeholder* to abide the event of an illegal contract. In such a case, the money can be recovered if notice is given to the stakeholder at any time before the latter has actually paid it over in pursuance of the contract.[53] Nevertheless, the result in *George v Greater Adelaide Land Development Co Ltd* is unattractive, despite the illegality in question. The burden of compliance was on the development company and, from George's point of view, there was a total failure of consideration. Surely today someone in his position could reverse what looks like a quite unjust enrichment of the development company?

48 See *Clegg v Wilson* (1932) 32 SR (NSW) 109, 120–2.

49 *Clegg v Wilson* (1932) 32 SR (NSW) 109.

50 *Alexander v Rayson* [1936] 1 KB 169, see [41.55].

51 *Tribe v Tribe* [1995] 3 WLR 913.

52 *George v Greater Adelaide Land Development Co Ltd* (1929) 43 CLR 91.

53 *George v Greater Adelaide Land Development Co Ltd* (1929) 43 CLR 91, 100–1.

False statements

[42.65] A plaintiff who is induced to enter an illegal contract by the defendant's *false statement* may be able to recover damages in an action other than one for breach of the contract. Possible actions include deceit (a tortious claim that can be made where the false statement is made knowingly or recklessly), negligent misrepresentation (a tortious claim that can be brought where the false statement is made carelessly in breach of a duty of care) or misleading conduct in contravention of s 18 of the *Australian Consumer Law* (see Chaper 33) or breach of a collateral contract.

In *Hatcher v White*,[54] the plaintiff contracted to do certain building construction work for the defendant. Under statute, the work required an official permit and the defendant dishonestly represented to the plaintiff that he had obtained such a permit. The plaintiff did some work under the contract and then discovered there was no permit. Despite the illegal act, he was able to recover damages for the actual loss he sustained (the cost of the work he did) by suing in the tort of deceit. He was an innocent person induced by a fraudulent misrepresentation to enter the contract. Today, even in the absence of fraud (eg, if the defendant honestly believed he had obtained a permit), the plaintiff might equally succeed in the tort of negligence (ie, a careless misstatement in breach of a duty of care) or under statutory provisions prohibiting misleading conduct or for breach of a promise by the defendant that the permit had been obtained (ie, a promise collateral to and given as consideration for the main construction contract). Whatever the cause of action, however, would not the plaintiff still be recovering in respect of an illegal act and indeed be "relying" on that act to recover damages?

It appears that the policy of the law is that, in appropriate cases, an *innocent* plaintiff should be able to recover despite involvement in an illegal act. Note that the illegal act in the *Hatcher v White* sort of case would have been legal if the representation or promise made by the defendant to the plaintiff had been true. The parties were certainly not equally at fault (ie, they were not in pari delicto). The defendant was the one under a duty to see to compliance with the law and was relying on its own illegality to defeat the claim.

The outcome in *Hatcher v White* is consistent with observations made by the High Court in *Miller v Miller*[55] – a negligence case in which the plaintiff's injuries were sustained while she was acting illegally – that "it is greatly doubted that the [ex turpi causa] maxim, properly understood, has any application in tort".[56] Although, as we will see, illegality is relevant to certain tort actions (those involving an interference with property rights), it seems reasonable to suggest that association with illegality is unlikely to preclude the bringing of deceit and negligence cases. Similarly, a misrepresentation does not cease to be actionable under the *Australian Consumer Law* simply because it is in some way connected to an illegal contract.[57]

Torts to goods

[42.70] A plaintiff may be able to recover goods by relying on tort law, the relevant torts being trespass to goods (unlawful interference with the possession of goods), detinue (wrongful

54 *Hatcher v White* (1953) 53 SR (NSW) 285.

55 *Miller v Miller* [2011] HCA 9; (2011) 242 CLR 446.

56 *Miller v Miller* [2011] HCA 9; (2011) 242 CLR 446, [13].

57 *Brownbill v Kenworth Truck Sales (NSW) Pty Ltd* (1982) 39 ALR 191.

retention of good following a request that the goods be returned) and conversion (dealing in goods in a manner inconsistent with another's possessory rights in the goods). In these torts, because they are concerned with the protection of property, the plaintiff must have *title to sue*. In the case of trespass, this means the plaintiff must be in *actual possession* of the goods at the time of a direct violation of that possession by the defendant. For example, it would be trespass for A to take B's goods from B's house or from B's person without B's permission. The title to sue is possessory.

In the case of conversion and detinue, the plaintiff must have a proprietary interest in the goods supporting *an immediate right to possession* of those goods at the time of an act of dominion over them by the defendant. If B lent goods to A and A sold or hired out those goods to C without B's consent, that would be a conversion of B's goods by A (and indeed by C). So too would be a refusal to return the goods to B on demand. The remedy would be damages for the loss. In the case of detinue, the act of dominion is exclusively a refusal to return the goods on demand and the remedy is either damages or (in the court's discretion) an order for the return of the goods. In both instances, B has title to sue, that is, an immediate right to possession (as distinct from possession itself) at the time of A's wrongful act.

In 1945, du Parcq LJ propounded a principle as follows:

> A man's right to possess his own chattels will as a general rule be enforced against one who, without any claim of right, is detaining them, or has converted them to his own use, even though it may appear either from the pleadings, or in the course of trial, that the chattels in question came into the defendant's possession by reason of an illegal contract between himself and the plaintiff, provided that the plaintiff does not seek, and is not forced, either to found his claim on the illegal contract or to plead its illegality in order to support his claim.[58]

This principle is sometimes referred to as the "no reliance" theory, or as the "Bowmakers rule" after the case in which it was enunciated. However, its status as part of Australian law is questionable. First, in cases where the rule has been applied, the Australian courts have given it a narrow scope of operation. In *Thomas Brown and Sons Ltd v Fazal Deen*,[59] the High Court took a narrow view of the non-reliance rule. The plaintiff, Fazal Deen, was the owner of 19 gold bars and a quantity of gems. He deposited these items with the general manager of the defendant company for safe-keeping. At that time, it was illegal under statutory regulations for gold to be kept by private persons. Gold was required to be delivered to the Commonwealth Bank. In 1959, Deen demanded the return of the gold and the gems, but the defendant refused, these items having disappeared from its custody. Deen sued in detinue. The trial judge, relying on Bowmakers, allowed the detinue claim on the basis that proof of the bailment (which would involve reliance on an illegal contract) was not an essential part of the plaintiff's case. The High Court held that Deen could recover in respect of the gems because the bailment of the gems was severable from the illegal bailment of gold. Deen's claim in detinue in respect of the gold failed because in order to establish that he had a right to possess the gold, he had to rely on the illegal contract of bailment. The claim depended on the failure of the defendant to comply with the obligation imposed by the contract to redeliver the gold upon the plaintiff's demand. *Bowmakers* was distinguished on the basis that the conversion

58 *Bowmakers Ltd v Barnet Instruments Ltd* [1945] KB 65, 71.

59 *Thomas Brown and Sons Ltd v Fazal Deen* (1962) 108 CLR 391.

in that case was admitted by the defendant, as was the fact that the goods converted were the plaintiff's property.[60]

Secondly, the "no reliance" rule is inconsistent with the emphasis in recent High Court decisions[61] on the question of coherence and whether denial of the cause of action is needed to uphold the purpose of the prohibition in question.[62] In *Nelson v Nelson*,[63] the court rejected as too inflexible and extreme the view that a claimant who must plead or rely on illegal conduct cannot obtain relief. Rather, "the question of illegality is bound up with the view taken of the underlying policy of the Act".[64] The real issue is whether public policy is better served by allowing an action to recover money or property than it is by disallowing recovery. In determining this issue, the court must look at the purpose of the relevant statute and the merits of the parties. McHugh J captured the court's reluctance to see the availability of claims resolved on technical rules such as the non-reliance rule when he said:

> A doctrine that depends upon the state of the pleadings or the need to rely on a transaction that has an unlawful purpose is neither satisfactory nor soundly based in legal policy. The results produced by such a doctrine are essentially random and produce windfall gains as well as losses, even when the parties are in pari delicto.[65]

Although these comments were made in relation to the relevance of illegality to equitable claims, the emphasis on promoting the coherence of the law in recent High Court common law decisions does not bode well for the survival of the non-reliance rule in Australia. As noted above, in *Equuscorp v Haxton*, French CJ, Crennan and Kiefel JJ expressly stated that when determining whether a restitutionary action is available, "[t]here is no one-size-fits-all answer to the question of recoverability … The central policy consideration at stake … is the coherence of the law".[66]

ESTOPPEL

[42.75] A party seeking to avoid his or her contractual obligations by raising illegality as a defence may be precluded from doing so under the doctrine of estoppel by convention. As noted at [9.200], estoppel by convention is a form of common law estoppel that operates where parties to an agreement have adopted a particular state of affairs as the basis of their agreement or relations. If established, the estoppel holds the parties to the agreed or assumed facts for the purpose of the relationship in question. In *Equuscorp Pty Ltd v Wilmoth Field Warne*,[67] Equuscorp (the client) alleged that the costs agreement it had entered into with Wilmoth Field Warne (a law firm) breached the *Legal Practice Act 1996* (Vic) and that, pursuant to s 102 of the Act, the law firm was not entitled to recover any amount in respect to the legal services provided under the prohibited costs agreement. Although it found that the agreement was not

60 *Thomas Brown and Sons Ltd v Fazal Deen* (1962) 108 CLR 391, 411–2. See also *Newcastle District Fishermen's Co-Operative Society v Neal* (1950) 50 SR (NSW) 237, 239.

61 Such as *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498 and *Miller v Miller* [2011] HCA 9; (2011) 242 CLR 446.

62 *Tinsley v Milligan* [1994] 1 AC 340, 370.

63 *Nelson v Nelson* (1995) 132 ALR 133.

64 *Nelson v Nelson* (1995) 184 CLR 538, 559.

65 *Nelson v Nelson* (1995) 132 ALR 133, 189.

66 *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [34].

67 *Equuscorp Pty Ltd v Wilmoth Field Warne* [2007] VSCA 280; (2007) 18 VR 250.

void under s 102, the Full Court of the Supreme Court of Victoria nevertheless considered the law firm's argument that, if the agreement were void, the client was estopped from relying on s 102. The doctrine of estoppel by convention was said to apply because the law firm had provided legal services to the client on the basis of the parties' common assumption that the costs agreement determined the rights and obligations of the parties. The Full Court of the Supreme Court of Victoria stated that it was necessary to consider whether the operation of the doctrine of estoppel was excluded by the social policy reflected in the *Legal Practice Act 1996*.[68] If the relevant question was whether allowing the estoppel would be inconsistent with the prohibition of costs agreements of the type under consideration, the court found that the estoppel would not operate. However, if the question was whether allowing the estoppel claim would undermine the policy of the Act, then the court would have allowed the estoppel claim. The Act aimed to offer clients protection against unfair cost agreements. As Equuscorp was an experienced litigator, and because the agreement under consideration was carefully negotiated between parties of equal bargaining power, the policy of the Act would not be threatened by allowing the law firm to recover its fees in this instance. Given the finding that the agreement was not void pursuant to s 102 of the Act, the court did not need to reach a final conclusion about the applicability of estoppel. However, the decision suggests that courts will be willing to consider an argument that a party is estopped from raising the defence of illegality.

REFORM

[42.80] Carter accurately observes that "[t]he topic of illegality is one of the least satisfactory branches of contract law"[69] and that "[i]nconsistencies are particularly in evidence where the consequences of illegality are in issue".[70] It is difficult to state the law relating to illegality in contract with confidence or to articulate coherently its underlying basic principles. A question arises as to whether dramatic reform is needed and, if so, what form that reform should take.

In the UK, a series of judicial developments in the treatment of illegality in different areas of private law were generally thought not to have brought the law into a satisfactory state.[71] Accordingly, in the unjust enrichment case *Patel v Mirza*,[72] the UK Supreme Court sat as a panel of nine judges and reconsidered the approach of the law in this area. As discussed at [10.110], a majority favoured the abandonment of the reliance-based approach (which turned on whether the plaintiff needed to rely on wrongdoing in order to establish a cause of action), in favour of the adoption of a broad, policy-based approach concerned with whether it would be contrary to the public interest (focused on the integrity of the legal system and possibly also public morality) to allow recovery. Lord Toulson said that:

> In assessing whether the public interest would be harmed in that way, it is necessary (a) to consider the underlying purpose of the prohibition which has been transgressed and whether that purpose will be enhanced by denial of the claim, (b) to consider any other relevant public policy on which the denial of the claim may have an impact and (c) to consider whether denial of the claim would be a proportionate response to the illegality, bearing in mind that

68 See also *Shah v Shah* [2002] QB 35.

69 Carter, *Contract Law in Australia* (7th ed, 2018), [25-02].

70 Carter, *Contract Law in Australia* (7th ed, 2018), [25-02].

71 Goudkamp and Zou, "The Defence of Illegality in Tort Law: Beyond Judicial Redemption?" (2015) 74 *Cambridge Law Journal* 13.

72 *Patel v Mirza* [2016] UKSC 42; [2017] AC 467.

> punishment is a matter for the criminal courts. Within that framework, various factors may be relevant, but it would be a mistake to suggest that the court is free to decide a case in an undisciplined way. The public interest is best served by a principled and transparent assessment of the considerations identified, rather by than the application of a formal approach capable of producing results which may appear arbitrary, unjust or disproportionate.[73]

An alternative way to reform the law is to introduce comprehensive legislative provisions aimed at guiding the court when it comes to balancing the complex policy issues at play. In New Zealand, statutory reform was implemented by the *Illegal Contracts Act 1970* (NZ), which has since been consolidated with other contract law reform legislation in the *Contract and Commercial Law Act 2017* (NZ).[74] Section 73 of the *Contract and Commercial Law Act 2017* declares that every illegal contract is of no effect and provides that no person shall become entitled to any property under a disposition made by or pursuant to any such contract. Section 76 gives the court power to grant relief by way of restitution, compensation, variation or validation of the contract, or any other remedy the court thinks just. The power to grant such relief is subject to the express provisions of any other enactment.

The New Zealand model gives a wide discretion to the courts in respect of illegal contracts. A question arises as to whether this is necessary or wise, especially as such a discretion is not generally available in respect of legal contracts. In s 76 of the *Contract and Commercial Law Act 2017*, restitution is placed at the head of the list of possible relief measures, followed by compensation, variation and validation, in that order. It appears that there was a rationale for this listing.[75] Restitution comes first as the primary form of relief, as it may be granted without enforcing the contract itself. However, as restitution may not be possible where goods have been consumed or services already rendered, compensation is next on the list to cover that situation. Variation and validation follow to cover illegality deriving from procedural defects.[76] The merit of the New Zealand reform is that gives the courts a broad discretion to do what is just in the circumstances of each case.[77] That flexibility, however, inevitably comes at the cost of certainty: it requires courts to make assessments of a number of difficult considerations and to weigh those incommensurable factors against one another.[78] The English judicial reform and the New Zealand legislative reform illustrate the core problem which plagues this area of the law: namely, that it is difficult to find any middle ground between a rule-based approach which produces arbitrary outcomes and a discretionary approach which produces great uncertainty.

73 *Patel v Mirza* [2016] UKSC 42; [2017] AC 467, [120]. For succinct analysis and criticism, see Goudkamp, "The End of an Era? Illegality in Private Law in the Supreme Court" (2017) 133 *Law Quarterly Review* 14. On the uncertain scope of the scope of the new approach, see Strauss, "Illegality Decisions after Patel v Mirza" (2018) 134 *Law Quarterly Review* 538.

74 For a severe critique of the reform, see Furmston, "The Illegal Contracts Act 1970 – An English View" (1972) 5 *New Zealand Universities Law Review* 151.

75 For the explanation given here, see Coote, "Security of Contract and the New Zealand Contract Statutes" (2000) 16 *Journal of Contract Law* 37, 41.

76 See Barton, "The Effect of the Contract Statutes in New Zealand" (2001) 16 *Journal of Contract Law* 233, 239.

77 See Booysen, "Contractual Illegality and Flexibility – a Rose by Any Other Name" (2015) 32 *Journal of Contract Law* 170.

78 Barton, "The Effect of the Contract Statutes in New Zealand" (2001) 16 *Journal of Contract Law* 233, 240.

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