

REMEDIES

Contract Law: a practical guide

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PART A DAMAGES FOR BREACH OF CONTRACT

The general rule as to damages in contract, is that stated in *Robinson v Harman*²:

... that where a party sustains 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.

This is referred to as the compensation principle.

A plaintiff needs to prove that it suffered the loss, that the loss was caused by the breach, and that it was not too remote.

I will deal with the following topics:

1. the quantification of loss, and in particular:
 - a. prima facie rules
 - b. quantification following termination - Shevill's case

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2 (1848) 154 ER 363 at 365.

- c. "reliance" damages in contract
 - d. liquidated damages
- 2. Causation;
- 3. Remoteness;
- 4. Limiting factors
 - a. mitigation
 - b. contributory negligence; and
 - c. proportionate liability.
- 5. Limitation of actions

Quantifying the loss

Proof of loss always involves proving a hypothetical scenario: the situation the plaintiff would be in if the contract had been performed. This then needs to be compared with the plaintiff's actual situation, in consequence of the contract not having been performed.

Prima facie rules

In various situations a prima facie rule applies to the measure of damages. Such rules may be displaced by the facts of the case, or at least supplemented by further heads of proven damage.

For example:

- (a) Under the sale of goods legislation the prima facie measure of damages payable to a seller for a buyer's non-acceptance, or to the buyer for the seller's non-delivery, is the difference between the contract price and the market or current price at the time when the

goods ought to have been delivered/accepted, or if no time was fixed for delivery/acceptance, then at the time of the refusal to deliver/accept.³

- (b) A similar rule applies in the case of sale of land contracts. Where either the vendor or purchaser fails to complete, the prima facie measure of damages is the difference between price and value. As I have said, the prima facie measures may be displaced or supplemented: for example, in *Wenham v Ella*⁴ a purchaser was entitled to damages for the loss of income which would have been earned from the property up to the date of judgment.

Further, subject to the question of remoteness, it is possible for a purchaser to establish an entitlement to damages based on the expected profits from a resale.⁵

Formerly, the rule in *Bain v Fothergill*⁶ restricted damages payable for a vendor's failure to complete where the cause was a defect in title which was not the vendor's fault. Under the rule, the purchaser could only recover monies laid out. This rule has been abolished in New South Wales in respect of contracts made after 1 October 1997 by s 54B of the *Conveyancing Act 1919* (NSW), which also provides that the court may award loss of bargain damages against a vendor who cannot perform due to a defect in title.

- (c) In the case of a breach of a warranty in a building contract the prima facie measure is the cost of necessary and reasonable work required to make the building conform to the contract, together with consequential loss.⁷(Arguably, a similar measure is applicable in favour of a landlord where a tenant breaches a covenant no to alter the demised premises, although some attention must be paid to the

³ *Sale of Goods Act 1923* (NSW), ss 52(3), 53(3).

⁴ (1972) 127 CLR 454.

⁵ As discussed in *Castle Constructions Pty Ltd v Fekala Pty Ltd* (2006) 65 NSWLR 648, [2006] NSW ConvR 56-157, [2006] NSWCA 133.

⁶ (1874) LR 7 HL 158.

⁷ *Bellgrove v Eldridge* [1954] HCA 36; (1954) 90 CLR 613.

precise terms of the covenant.⁸⁾

Quantification following termination of contract - *Shevill's* case

Contract damages are concerned with vindicating a plaintiff's expectation interest, and where a contract has been terminated for the defendant's breach a plaintiff may well be entitled to measure its damages claim by reference to the whole of the profit that the plaintiff has missed out on.

But the basis of the plaintiff's right to terminate is important.

Let us first recall of the principles as to termination of contracts at law for breach. *First*, an innocent party might terminate for anticipatory breach – that is, where the promisor indicates that he or she will not perform the contract or will only perform it on terms substantially different from the agreed terms.⁹

Second, there is the case of fundamental breach – a breach which goes “so much to the root of the contract that it makes further commercial performance of the contract impossible”.¹⁰ Again, the innocent party is entitled to terminate.

Third, an innocent party might terminate for any breach of an essential term, that is:

[A] stipulation which the parties have agreed either expressly or by necessary implication or which the general law regards as a condition which goes to the root of the contract so that any breach of that term may at once and without further reference to the facts and circumstances be regarded by the innocent party as a fundamental breach ...¹¹

In any of these situations, the innocent party is given the right to terminate because they are regarded at law as having been deprived of substantially what was bargained for. It is consistent with the compensation principle that the innocent party is entitled to terminate and then recover damages for the loss of the bargain.

⁸ See *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* (2009) 236 CLR 272

⁹ *Shevill v Builders Licensing Board* (1982) 149 CLR 620 at 625-626 per Gibbs CJ.

¹⁰ *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26 at 64; *Shevill v Builders Licensing Board* (1982) 149 CLR 620 at 626 per Gibbs CJ.

¹¹ *Suisse Atlantique Societe d'Armement Maritime SA v NV Rotterdamsche Kolen Centrale*.

But many contracts make express provision for termination in defined circumstances. Where such a provision can be relied upon, a party can terminate without regard to whether any of the grounds above. But can the party have loss of bargain damages?

Shevill v Builders Licensing Board

In *Shevill v Builders Licensing Board*¹² the agreement was a lease. It provided the lessor with a right to bring an end to the lease if the tenant was 14 days late in paying rent.

The lessee had been constantly late in paying rent but the lessor accepted late, and sometimes partial, payments. In August 1977, the lessee was in arrears as to two months' rent, and the lessor terminated.

The lessor sued the lessee's guarantors, and sought damages calculated by reference to the rent under the lease for the remainder of the term less the rent which the landlord in fact received for that period. The lessor succeeded at first instance, and on appeal, but failed in the High Court. The guarantors argued that the mere fact that the clause gave the lessor the right to terminate did not entitle the lessor to damages for loss of a bargain. They said that the breach in question (non-payment of rent for two months) was not a repudiation. Any loss suffered by the lessor was occasioned by its election to terminate.

The High Court agreed with the guarantor. The clause in question was not an essential term. The fact that it provided for a right to terminate in the event of breach was not enough (the parties could have stipulated that the term was essential, but they had not done so), nor did the lessee's two month default in paying rent amount to a serious or fundamental breach – another route to termination at law.

The result was that the lessor's entitlement to terminate was generated entirely by the provisions of the lease and not by the principles whereby the law treats a party as having missed out on the substance of the bargain. As a matter of causation, the lessor's loss and damage was treated as flowing entirely from the re-entry, not the lessee's breach.

12 (1982) 149 CLR 620.

Shevill's case is accepted as standing for the proposition that:

[W]hen the lessor terminates pursuant to the contractual right given to him for breach by the lessee, the loss which he can recover for non-fundamental breach is limited to the loss which flows from the lessee's breach. The lessor cannot recover the loss which he sustains as a result of his termination because that loss is attributable to his act, not to the conduct of the lessee. It is otherwise in the case of fundamental breach, breach of an essential term or repudiation.¹³

Gumland Property Holdings Pty Ltd v Duffy Bros Fruit Market (Campbelltown) Pty Ltd

In *Shevill*, Gibbs CJ said:

It is clear that a covenant to pay rent in advance at specified times would not, without more, be a fundamental or essential term having the effect that any failure, however slight, to make payment at the specified times would entitle the lessor to terminate the lease.¹⁴

His Honour then said:

However, the parties to a contract may stipulate that a term will be treated as having a fundamental character although in itself it may seem of little importance, and effect must be given to any such agreement.¹⁵

Since the decision in *Shevill*, commercial solicitors have apparently acted on the above advice by including "anti-*Shevill*" provisions in leases and other agreements.

Do such provisions work?

In *Gumland Property Holdings Pty Ltd v Duffy Bros Fruit Market (Campbelltown) Pty Ltd*¹⁶, the High Court considered this question.

The case again concerned a lease. The tenant, by failing to pay part of the monthly rent due on a certain day, breached cl 3 of the lease. The landlord demanded that the tenant pay the shortfall in rent, and, when the shortfall was not paid, gave a notice terminating the lease.

The landlord then sued for (a) arrears of rent; (b) loss of bargain damages,

13 *AMEV-UDC Finance Ltd v Austin* (1986) 162 CLR 170 per Mason and Wilson JJ at 186.

14 (1982) 149 CLR 620 at 627.

15 (1982) 149 CLR 620 at 627.

16 (2008) 82 ALJR 576; [2008] HCA 10.

calculated as the rent and outgoings payable by the tenant under the lease after termination, less the discounted present value of rents received or to be received after that date; and (c) reinstatement damages.

One argument by the lessee, against liability for components (b) and (c), was that cl 3 (the rent payment clause) was not an essential term.

The lease had several provisions concerned with making timely payment of rent essential. They included a clause which stipulated that certain covenants – including cl 3 – were essential terms. Another clause provided (in effect) that the tenant would be liable for the full loss and damage suffered by the lessor for the term of the lease in the event that the lease was determined for default in payment of the rent.

The High Court held that as a matter of construction the covenant to pay rent was an essential term. The various provisions of the lease, including those referred to above, pointed overwhelmingly to this conclusion.

It should be noted that the High Court expressly did not decide whether the mere description of a covenant in a lease as essential, however trivial it may be thought to be, can make it essential.

Various other arguments failed. Those arguments included a causation argument, similar to the reasoning in *Shevill*. It was argued that, if the landlord decided to terminate the lease for reasons other than fundamental breach or repudiation, any damage flowing from the loss of bargain was caused by the landlord's decision to terminate rather than the tenant's breach. This argument failed because (in essence) the authorities show that the relevant distinction is between termination for non-essential breach on the one hand, and termination for fundamental breach, repudiation or *breach of a condition* on the other. It will be recalled, from earlier in this paper, that an essential term, by definition, goes to the root of the contract, so that any breach of it is a fundamental breach.

Essentially, orthodox contract law principles determined the outcome. Those principles were succinctly put in paragraph 58 of the judgment:

Save for any applicable statutory requirements or rules of law, there is no reason in law why general contractual principles do not apply to leases in this respect. Under general contractual principles, an innocent promisee can terminate the contract, and recover loss of bargain damages, where there is repudiation, or a fundamental breach, or a breach of condition – ie a breach of an essential term.

And under these principles it is possible by express provision in the contract to make a term a condition, even if it would not be so in the absence of such a provision – not only in order to support a power to terminate the contract, which the Lessee concedes, but also to support a power to recover loss of bargain damages. No convincing reason was given to explain why the former outcome was sound in law but the latter was not [citations omitted].

Quantification where expectation loss cannot be shown: “Reliance” damages in contract

In principle, damages in contract are not concerned with restoring the plaintiff to the position that it would have been in if there had been no contract, in other words, compensating the plaintiff for its losses in reliance on the contract. "Reliance" damages in this sense would treat the entry into the contract itself as the wrongful act that needs to be compensated.

Yet in a limited category of cases, damages awarded in contract can be quantified in a manner which does in fact restore the plaintiff to the position as if there had been no contract. How does this reconcile with the notion that contract damages are concerned only with remedying a breach?

McRae v Commonwealth Disposals Commission

In *McRae v Commonwealth Disposals Commission*¹⁷, the plaintiff purchased from the Commonwealth Disposals Commission (through a tender process) the following: “one (1) oil tanker including contents wrecked on Jourmaund Reef approximately 100 miles north of Samarai. Price £285”. One of the conditions of sale was that the goods “are sold as and where they lie with all faults”, and another was that no warranty was given as to “condition description quality or otherwise.” The plaintiff fitted out a salvage expedition and went to the location of the alleged tanker but it was not there.

The High Court concluded, in terms of liability, that there was, in the contract, an implied promise by the Commission that there was a tanker in the position specified. This had been breached.

17 (1951) 84 CLR 377.

The High Court considered the measure of damages. The starting point was the sale of goods legislation. As I have said, the prima facie measure of damages for non-delivery under that legislation is the difference between the contract price and the market or current price at the relevant time.

The problem in *McRae* was that there was simply no market, let alone market price, available to use as a benchmark, nor was it fair to quantify the loss by reference to the value of an average sized tanker, discounted for the fact that it was lying on a reef. The Commission had not contracted to deliver a tanker of any particular size, value or condition. There was no reason to assume that the tanker would be salvageable, let alone at a profit.

These facts would seem to present difficulties for a plaintiff, but the High Court saw things differently. Dixon and Fullagar JJ (with whom McTiernan J agreed) conceded that, if the case was simply a case of breach of contract by non-delivery, the plaintiffs could not have succeeded because they would not have been able to show that a tanker delivered in accordance with the contract would have had some value.¹⁸ But this was not a simple case of non-delivery of goods. The practical substance of the case lay, in their Honours' view, in three factors:

- (1) the Commission promised that there was a tanker at or near to the specified place;
- (2) in reliance on that promise, the plaintiffs expended considerable sums of money;
- (3) there was, in fact, no tanker at or anywhere near the specified place.

Once the promise and the breach were characterised in this way, the plaintiffs were able to make out a *prima facie* case for damages:¹⁹

"They can say: (1) this expense was incurred; (2) it was incurred because you promised us that there was a tanker; (3) the fact that there was no tanker made it certain that this expense would be wasted. The plaintiffs have in this way a starting-point. They make a prima-facie case. The fact that the expense was wasted flowed prima facie from the fact that there was no tanker; and the first fact is damage, and the second fact is breach of contract."

That would not necessarily end the matter in all cases: the plaintiffs would fail if the defendant could show that, if there had been a tanker, the expense

¹⁸ *Ibid.* at 414.

¹⁹ *Ibid.* at 414.

would equally have been wasted. But the defendant did not establish this in *McRae*.²⁰

Importantly, once the plaintiffs had shown a *prima facie* case that they had suffered loss and damages by the waste of expenditure, the burden was said to shift to the defendant to establish that the expenditure would have been wasted anyway. Their Honours went on to say that the impossibility of assessing damages in the case was caused by the defendant's breach of contract, and:

[I]n so far as the Commission's breach of contract itself reduces the possibility of an accurate assessment, it is not for the commission to complain.

The case left some unanswered questions, including whether it involved a shift in the legal onus to the defendant, and, if so, in what circumstances a plaintiff could invoke it. At one extreme, was the plaintiff simply entitled to elect between "reliance" and "expectation" damages?

Commonwealth v Amann Aviation Pty Ltd

The High Court considered these issues in *Commonwealth v Amann Aviation Pty Ltd*.²¹ This case again concerned breach by the Commonwealth of a contract which was arguably unprofitable for the plaintiff. The plaintiff (Amann) had a contract with the Commonwealth to carry out coastal surveillance for three years. The Commonwealth wrongly purported to terminate. Amann treated this as a repudiation and terminated, and sued for damages. Amann could not have made a profit in the first three years: it would need to operate for much longer in order to recoup its initial expenditure. This would have required the Commonwealth to renew the contract – which it was not obliged to do. (An important aspect of the decision was a consideration of how this possibility of renewal was to be dealt with in the assessment of damages, but I leave this aspect to one side.)

The appeal was decided by a seven-member bench of the High Court. There are six separate judgments, of which one (that of McHugh J) was in dissent. The majority decided that Amann was entitled to damages calculated by

20 *Ibid.* at 414.

21 (1991) 174 CLR 64.

reference to its wasted expenditure. In doing so they gave close consideration to the place of so-called reliance damages in contract.

I use the expression “so-called reliance damages” for a reason. Mason CJ and Dawson J pointed out²²:

[T]he expressions “expectation damages”, “damages for loss of profits”, “reliance damages” and “damages for wasted expenditure” are simply manifestations of the central principle enunciated in *Robinson v Harman* rather than discrete and truly alternative measures of damages which a party not in breach may elect to claim.

So is there any room for two alternative measures of damages in contract cases – expectation damages (if lost profits can be proven) and reliance damages (if they cannot)? In principle, the answer is no – there is just one measure of damages, and it is the measure in *Robinson v Harman*.

Wasted expenditure as damage

But this does not preclude recovery of wasted expenditure. Mason CJ and Dawson J said that damages for lost profits have two constituents:

- expenses justifiably incurred by a plaintiff in the discharge of contractual obligations; and
- any amount by which gross receipts would have exceeded those expenses.²³

The latter constituent is net profit, but both components are recoverable consistently with *Robinson v Harman*. Full performance of a contract may have been expected to lead to recoupment of expenditure. Even if no profit would have resulted, damages for expenditure that would have been recouped by full performance of the contract would be justified under *Robinson v Harman*. This is “contract damages” – damages flowing from breach – and not some alternative measure based on restoring the plaintiff to its prior position.

Essentially, the other judges were agreed that wasted expenditure might be the subject of a damages award on this basis.

Damages only to the extent of recoupment

Because damages for wasted expenditure are based on the proposition that

22 *Ibid.* at 82.

23 *Ibid.* at 81.

the plaintiff would have recouped the expenditure if the defendant had performed the contract, it follows that, if the plaintiff would not have recouped the expenditure in full, the plaintiff will only be entitled to damages in the amount that would have been recouped.²⁴ If the plaintiff would have lost a greater sum rather than recouping his expenditure, the plaintiff is not entitled to any damages.²⁵

Is there an election?

It had been held in England²⁶ that where a plaintiff had not suffered any loss of profits or could not prove what its profits would have been, the plaintiff had the right to elect between a claim for loss of profits or for wasted expenditure. This proposition does not sit well with the proposition that there is but one measure of damages, and it was rejected in *Amann Aviation*.²⁷

Is there a reversal of onus

It will be recalled that, in *McRae*, it was said that there was a shift – of some sort – in the burden of proof once the plaintiff showed that it had incurred expenditure under the contract which was wasted. The High Court considered this again in *Amann*.

Mason CJ and Dawson J were of the view that, where it is not possible to predict what position a plaintiff would have been in had the contract been fully performed, the law *assumes* that the plaintiff would at least have recovered his or her expenditure had the contract been fully performed. It is open to the defendant to show that the plaintiff's expenditure would not have been recovered if the defendant had performed the contract in full.²⁸

Deane J also thought that there was a shift of legal onus²⁹, as did Brennan J³⁰.

24 Per Mason CJ and Dawson J at 84; Brennan J at 99; Deane J at 127; Toohey J at 135; Gaudron J at 155.

25 Per McHugh J at 163.

26 *Anglia Television Ltd v Reed* [1972] 1 QB 60; *C.C.C. Films Ltd v Impact Quadrant Films Ltd* [1985] QB 16.

27 *Ibid.*, per Mason CJ and Dawson J at 84-85; Brennan J at 108; Toohey J at 136-137; Gaudron J at 155; McHugh J at 162.

28 *Ibid.* at 86.

29 *Ibid.* at 126.

30 *Ibid.* at 105.

Those judges acknowledged limits to the availability of the shift in onus, or in other words, the legal presumption which may be raised in favour of plaintiffs. First, the presumption appears only to arise where quantification of the plaintiff's expected profit is difficult or impossible (although Deane J did not rule out a broader application of the principle).³¹ Second, in the view of Brennan J, the presumption only arises where it is the defendant's repudiation or breach which denies, prevents, or precludes the existence of circumstances which would have determined the value of the plaintiff's contractual benefits.³² Third, the presumption would not, as Mason and Dawson CJ pointed out, apply to aleatory contracts – contracts for a chance – because inherent in such contracts is the possibility that not even the slightest expenditure will be recovered. Fourth, Deane J pointed out that his Honour's general statements – which included statements about the onus – may be inadequate to deal with some problems not present on the facts of *Amann Aviation*.

Toohy J and Gaudron J were also in the majority, but disagreed on this issue. In their Honours' views, the onus of proving loss and damage remains with the plaintiff: there is no reversal of the legal onus.³³ However, the circumstances of the case may (as they did in *Amann Aviation* and in *McRae*) cast an evidentiary onus on the defendant. Both judges recognised that the plaintiff may be assisted by an assumption that a plaintiff would have recovered its cost had the contract been performed.

There is likely to be little difference between these views in terms of the practical consequences in most cases.

Quantification by reference to liquidated damages clauses

An effective liquidated damages clause will govern damages for breach of contract in lieu of the common law principles. However, under the equitable doctrine of penalties, a liquidated damages clause will not be enforced if it does not represent a genuine pre-estimate of damages. The decision of the High Court in *Ringrow Pty Ltd v BP Australia Pty Ltd*³⁴ shows that the parties have considerable latitude in framing liquidated damages clauses. The Court

31 *Ibid.* at 126.

32 *Ibid.* at 106-107.

33 *Ibid.*, per Toohy J at 137-143; per Gaudron J at 155-157.

34 (2005) 224 CLR 656.

in that case emphasised that it is not enough that there be some difference between the amount to be paid under the contract for the breach and the amount which would represent a genuine pre-estimate of loss: there must be something “extravagant or unconscionable” in the comparison.³⁵

Causation

At common law, causation is a question which "must be determined by applying common sense to the facts of each particular case", and it is a question that is informed by value judgments and policy considerations.³⁶

In claims for damages for harm resulting from negligence, including negligent breach of contract,³⁷ the test for causation is stipulated in s 5D of the *Civil Liability Act 2002* (NSW). It states:

"(1) A determination that negligence caused particular harm comprises the following elements:

(a) that the negligence was a necessary condition of the occurrence of the harm ("factual causation"), and

(b) that it is appropriate for the scope of the negligent person's liability to extend to the harm so caused ("scope of liability").

(2) In determining in an exceptional case, in accordance with established principles, whether negligence that cannot be established as a necessary condition of the occurrence of harm should be accepted as establishing factual causation, the court is to consider (amongst other relevant things) whether or not and why responsibility for the harm should be imposed on the negligent party.

(3) If it is relevant to the determination of factual causation to determine what the person who suffered harm would have done if the negligent person had not been negligent:

(a) the matter is to be determined subjectively in the light of all relevant circumstances, subject to paragraph (b), and

(b) any statement made by the person after suffering the harm about what he or she would have done is inadmissible except to the extent (if any) that the statement is against his or her interest.

(4) For the purpose of determining the scope of liability, the court is to

³⁵ *Ibid.* at 666.

³⁶ *March v Stramare* (1991) 171 CLR 506[PDF], 65 ALJR 335, 99 ALR 423.

³⁷ *Civil Liability Act 2002* (NSW), s 5A.

consider (amongst other relevant things) whether or not and why responsibility for the harm should be imposed on the negligent party."

This year, in *Wallace v Kam*³⁸ the High Court of Australia had occasion to consider the effect of this section.

The case concerned a doctor's negligent failure to warn a patient of the risks of a procedure. There were two risks involved, both of which should have been drawn to the plaintiff's attention but were not. The less serious risk (neuropaxia) materialised, but it was found that the plaintiff would have undergone the treatment even if warned of this risk. The plaintiff failed in his appeal to the High Court, and the assumption that he would not have proceeded with the operation if warned of the more serious risk (paralysis) did not assist him.

In coming to its conclusion the High Court considered s 5D of the Civil Liability Act, which deals with causation in negligence cases.

Key points were:

1. The requirement in s 5D(1)(a), "that the negligence was a necessary condition of the occurrence of the harm" involves nothing more nor less than the "but for" test for causation.
2. As regards the requirement in s 5D(1)(b), "that it is appropriate for the scope of the negligent person's liability to extend to the harm so caused", this is to be answered, in established cases, through the application of precedent.
3. However, in a novel case, s 5D(4) requires the court, when applying s 5D(1)(b), "explicitly to consider and to explain in terms of legal policy whether or not, and if so why, responsibility for the harm should be imposed on the negligent party." The court must identify and articulate an evaluative judgment by reference to "the purposes and policy of the relevant part of the law".

Remoteness

The well-known rule as to remoteness of damage in the contract context is that stated by Alderson B in *Hadley v Baxendale*:³⁹

³⁸ (2013) 87 ALJR 648; [2013] HCA 19.

³⁹ (1854) 9 Ex. 341 [156 E.R. 145].

"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, ie, 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."

It is normal to talk about two limbs of the rule in *Hadley v Baxendale*, and in practice it is often important for parties to litigation to be in a position to address why a particular head of damages does or does not come within one or other limb. But it has also been said that *Hadley v Baxendale* is a single principle, rather than two separate rules or standards. In *Satef-Huttenes Albertus SpA v Paloma Tercera Shipping Co SA (The Pegase)*⁴⁰, Robert Goff J stated,

"Although the principle stated in *Hadley v Baxendale* remains the *fons et origo* of the modern law, the principle itself has been analysed and developed, and its application broadened, in the 20th century... The general result of the two cases is that the principle in *Hadley v Baxendale* is now no longer stated in terms of two rules, but rather in terms of a single principle—though it is recognised that the application of the principle may depend on the degree of relevant knowledge held by the defendant at the time of the contract in the particular case. This approach accords very much to what actually happens in practice; the courts have not been over-ready to pigeon-hole the cases under one or other of the so-called rules in *Hadley v Baxendale*, but rather to decide each case on the basis of the relevant knowledge of the defendant."

In *Commonwealth v Amann Aviation Pty Ltd*⁴¹ Mason CJ and Dawson J said:"

"It is now accepted that this is the statement of a single principle and that its application may depend on the degree of relevant knowledge possessed by the defendant in the particular case."

How likely must some eventuality be, in order to be seen as arising "according to the usual course of things"? Formulations have varied between "on the cards", "serious possibility", "grave risk", "not unlikely", "liable to result" and

⁴⁰ [1981] 1 Lloyd's Rep 175, at p 181.

⁴¹ (1991) 174 CLR 64.

"real danger".⁴² Whatever the most appropriate verbal formulation for the first limb, it is narrower than the remoteness test in tort. However, the second limb supplies the possibility of the extension of compensable loss to that which was in the reasonable contemplation of the parties.

Limiting factors

Mitigation

The principle of mitigation applies to contract claims. The defendant bears the onus to prove failure to mitigate,⁴³ and of course it is for the defendant also to plead it. In some cases there is an express term in a contract requiring a party, or all parties, to mitigate their loss following breach. But even without such a term there is a "duty" on the part of a party claiming damages to mitigate its loss, failing which its damages will be reduced.

It is not enough to point to some hypothetical scenario in which the plaintiff's loss would have been reduced if the plaintiff had acted in a certain way. The issue is whether the plaintiff has acted unreasonably. In *Sherson & Associates Pty Ltd v Bailey*⁴⁴ Heydon JA said:

A plaintiff "cannot be said to have really incurred any loss which might have been avoided by his taking such steps as a reasonably prudent man in his position would have taken to avoid further loss to himself": Driver v Wat Services Homes Commissioner (1923) 44 ALJ 130 at 134 per Irvine CJ (emphasis added). A plaintiff cannot recover damages for losses "which he would not have incurred had he acted reasonably in the ordinary course of his business": TCN Channel 9 Pty Ltd v Hayden Enterprises Pty Ltd (1989) 16 NSWLR 130 at 162 per Priestley JA (emphasis added). Subject to the criterion of reasonableness, the plaintiff "is completely free to act as he judges to be in his best interest": The Soholt [1983] 1 Lloyd's Rep 605 at 608 per Sir John Donaldson MR (emphasis added). "The word 'reasonable' has in law the prima facie meaning of reasonable in regard to those existing circumstances of which the actor, called on to act reasonably,

⁴² See Carter, Peden and Tolhurst, Contract Law in Australia (5th Edition), 2007, pp. 821-2 and the cases mentioned therein.

⁴³ *TC Industrial Plant Pty Ltd v Robert's Queensland Pty Ltd* (1963) 180 CLR 130 at 138.

⁴⁴ [2000] NSWCA 275 at [77].

knows or ought to know": *In re a Solicitor* [1945] KB 368 at 371 per Scott, *Lawrence and Morton LJJ*; see also *Adams v Eta Foods Ltd* (1987) 78 ALR 611 at 621 per Gummow J.

The mitigation principle may lead to a reduction in the plaintiff's damages for failure to mitigate.

It may also affect the quantification of damages where the plaintiff has taken reasonable steps to mitigate. The taking of such steps may actually mitigate the loss, thus reducing the amount of damages. Further, the taking of reasonable steps to mitigate may actually increase the plaintiff's loss, and the additional amounts will be allowed as part of damages if the plaintiff's actions were reasonable.

Contributory negligence

Contributory negligence at common law is a defence to negligence claims. Under legislation it is not a complete defence, but may lead to a reduction of damages.⁴⁵ Apart from statute, contributory negligence had no effect on contract claims, even where a defendant was liable concurrently in tort and contract.⁴⁶ However, the *Law Reform (Miscellaneous Provisions) Act 1965* (NSW) was amended in 2000, so as to apply apportionment for contributory negligence to contract claims involving negligence. Subsection 9(1) provides:

"(1) If a person (the "claimant") suffers damage as the result partly of the claimant's failure to take reasonable care ("contributory negligence") and partly of the wrong of any other person:

(a) a claim in respect of the damage is not defeated by reason of the contributory negligence of the claimant, and

(b) the damages recoverable in respect of the wrong are to be reduced to such extent as the court thinks just and equitable having regard to the claimant's share in the responsibility for the damage."

⁴⁵ *Law Reform (Miscellaneous Provisions) Act 1965* (NSW), s 9.

⁴⁶ *Astley v Austrust Ltd* warns that the case has some negative history, but has not been reversed or overruled (1999) 197 CLR 1

The provision applies to contract claims - where there is concurrent liability in negligence - via the definition of "wrong" in s 8, as follows:

"wrong" means an act or omission that:

- (a) gives rise to a liability in tort in respect of which a defence of contributory negligence is available at common law, or
- (b) amounts to a breach of a contractual duty of care that is concurrent and co-extensive with a duty of care in tort.

Proportionate liability

In New South Wales, the concept of proportionate liability was introduced by the *Civil Liability Act 2002*, Pt 4.

The central provision is s 35, which provides:

(1) In any proceedings involving an apportionable claim:

- (a) the liability of a defendant who is a [concurrent wrongdoer](#) in relation to that claim 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](#) responsibility for the damage or loss, and
- (b) the court may give judgment against [the defendant](#) for not more than that amount.

(2) If the proceedings involve both an apportionable claim and a claim that is not an apportionable claim:

- (a) liability for the apportionable claim is to be determined in accordance with the provisions of this Part, and
- (b) liability for the other claim is to be determined in accordance with the legal rules, if any, that (apart from this Part) are relevant.

(3) In apportioning responsibility between defendants in the proceedings:

- (a) the court is to exclude that proportion of the damage or loss in relation to which [the plaintiff](#) is contributorily negligent under any relevant law, and
- (b) the court may have regard to the comparative responsibility of any [concurrent wrongdoer](#) who is not a party to the proceedings.

(4) This section applies in proceedings involving an apportionable

claim whether or not all [concurrent wrongdoers](#) are parties to the proceedings.

(5) A reference in this Part to a defendant in proceedings includes any person joined as a defendant or other party in the proceedings (except as a plaintiff) whether joined under this Part, under rules of court or otherwise.

The application of s 35 does not depend on the concurrent wrongdoer being joined in the proceedings – either as defendant or as a cross-defendant.⁴⁷ Where there are concurrent wrongdoers that have been identified by a defendant, it falls on the plaintiff to sue them or risk obtaining partial compensation only. A plaintiff may, of course, be given leave to join the non-party concurrent wrongdoer⁴⁸, or the plaintiff may wait for the outcome and bring a fresh action against the non-party if need be.⁴⁹ But if a concurrent wrongdoer is insolvent, it is the plaintiff who loses, rather than the solvent defendants. This is in contrast to the position under the legislation for contribution between and several tortfeasors.⁵⁰

There are two key concepts in s 35. First, the provisions apply only to “apportionable claims” – which are claims for economic loss or property damage arising from failure to take reasonable care – whether in tort, under contract, or otherwise, except in personal injury cases, and to claims for economic loss or property damage for contravention of s 42 of the *Fair Trading Act 1987* (NSW).⁵¹

Clearly, not all claims for breach of contract are “apportionable claims”, but professional negligence claims (other than personal injury claims) – which in most cases have a contractual element - fall within the concept.

The other key concept is that of a “concurrent wrongdoer”. This refers to:

... a person who is one of 2 or more persons whose acts or omissions (or act or omission) caused, independently of each other or jointly, the damage or loss that is the subject of the claim.⁵²

Within the above definition, the phrase “the damage or loss that is the subject

47 *Ibid.* s 87CD(4).

48 *Ibid.* s 87CH.

49 *Ibid.* s 87CG.

⁵⁰ See Law Reform (Miscellaneous Provisions) Act 1946, s 5.

51 *Civil Liability Act 1987* (NSW) s 34(1).

52 *Ibid.* s 87CB(3).

of the claim” caused sufficient difficulties in the cases for the High Court to look at it in *Hunt & Hunt v Mitchell Morgan Lawyers v Mitchell Morgan Nominees Pty Ltd.*⁵³

In this case, the High Court overturned a decision of the New South Wales Court of Appeal. The plaintiff was a lender, which lost money due to mortgage fraud. The fraudster (with the assistance of a dishonest solicitor) had obtained possession of the certificate of title to the property of an innocent party, Mr Vella, and then he had forged Mr Vella’s signature on various documents including mortgage and loan documents, and thereby borrowed about \$1 million from the plaintiff. The plaintiff had relied on a firm of solicitors (Hunt & Hunt) to prepare appropriate security documents. In due course the fraud came to light. The fraudsters were ultimately bankrupted.

It turned out that, although the plaintiff had obtained and registered a mortgage, it could not recover any part of its loan against Mr Vella’s property in reliance on indefeasibility under the RPA. The mortgage gained indefeasibility through registration, but not the associated loan agreement did not. The mortgage itself did not contain a covenant to repay a stated amount. Rather, it relied on an “all monies” provision, with the debt obligations set forth in a separate loan agreement. Because the loan agreement was void, there were no monies owing under the “all monies” clause. The trial judge held that the plaintiff’s solicitor was negligent in preparing a mortgage without a covenant to repay a stated amount, and this was not under challenge in the High Court.

The question for the High Court was whether the fraudster and his associate were concurrent wrongdoers with Hunt & Hunt.

In the New South Wales Court of Appeal, this question had been answered in the negative, but the High Court (by majority) disagreed.

The issue came down to the proper identification of the “damage of loss that is the subject of the claim”. In both the Court of Appeal and the High Court it was accepted that loss or damage, in a claim relating to economic loss, is harm suffered to the plaintiff’s economic interest.

It was necessary to identify what the harm suffered to the plaintiff’s economic interest was in the immediate case. The Court of Appeal was of the view that two distinct losses could be identified, the one caused by Hunt & Hunt, and

⁵³ [2013] HCA 10.

the other caused by the fraudsters. Giles JA (the other members agreeing) said.⁵⁴

"The loss, or the harm to an economic interest, is in the one case paying out money when it would not otherwise have done so, and in the other case not having the benefit of security for the money paid out. The losses the subject of the claims for economic loss against [the fraudsters] and the loss the subject of the claim for economic loss against Hunt & Hunt are different."

In the High Court, the majority (French CJ, Hayne and Kieffel JJ) were of the view that the Court of Appeal had incorrectly identified the loss or harm to the plaintiff's economic interest, as

- paying money out when it would otherwise not have done so (in the case of the claim against the fraudsters); and
- not having the benefit of security for the money paid out (in the case of the claim against Hunt & Hunt).

In the view of the majority in the High Court, those statements did not describe the plaintiff's loss and damage. Rather, they described the immediate effects of the fraud in the one case, and the negligence in the other. Those effects were important in establishing how the loss and damage ultimately came to be suffered, but they were not to be equated with the loss and damage.

Essentially, neither the paying out of monies due to fraud, nor entry into a negligently drafted mortgage, will necessarily be productive of loss. So it is wrong to equate these steps with loss and damage.

Rather, in the majority's view, the "damage or loss that is the subject of the claim" was the plaintiff's inability to recover the sums advanced.

Having identified the damage or loss, there was a further and distinct step, which involved the question of causation. It was clear that Hunt & Hunt had caused the plaintiff to suffer the damage or loss, being the plaintiff's inability to recover the sums advanced.

But had the fraudsters caused this loss?

In the majority's view they had. The mortgage was ineffective, but this resulted from the concurrence of two conditions:

⁵⁴ *Mitchell Morgan Nominees Pty Ltd v Vella* (2011) 16 BPR 30,189 at 30,198-30,199 [41].

- (a) that the loan agreement was void; and
- (b) that the mortgage document did not contain a debt covenant but relied on the loan agreement.

The fraudsters' conduct caused (a), whilst Hunt & Hunt's conduct caused (b).

Therefore, the fraudsters were concurrent wrongdoers in relation to the claim.

The consequence was that the trial judge's decision was restored, so that Hunt & Hunt was liable for only 12.5% of the plaintiff's loss and damage.

At least in cases where the defendant and the putative concurrent wrongdoer have contributed independently of each other to the plaintiff's claimed loss, the case of *Mitchell Morgan* shows that some very careful analysis will often be needed in working out who should be identified as concurrent wrongdoers.

Limitation of Actions

The limitation period for a cause of action founded on a simple contract is 6 years from the accrual of the cause of action,⁵⁵ and where the cause of action is founded on a deed, the period is 12 years.⁵⁶

The general rule is that, in a breach of contract claim, the cause of action accrues at the the time of breach.⁵⁷ Thus, if the breach is a failure to do something, then it is necessary to determine when that thing fell due for performance, be it the occurrence of some event, or the expiry of a particular time period.

There is case law relating to identifying the time of accrual of causes of action in various contractual contexts.

For this seminar I shall just draw attention to one particular situation which is a little anomalous, namely loans repayable on demand. Because there is no breach of contract until a demand has been made, one would think the limitation period runs from the time of the demand, or even a reasonable time thereafter.

⁵⁵ *Limitation Act 1969* (NSW), s 14(1).

⁵⁶ *Limitation Act 1969* (NSW), s 16.

⁵⁷ *Gould v Johnson* (1702) 2 Salk 422; 91 ER 367.

However, in *Young v Queensland Trustees Ltd*⁵⁸ the High Court said that the cause of action accrues when the money is received by the borrower, and that this position had been settled since at least the end of the seventeenth century (*Collins v Benning* (1700) 12 Mod. 444, 88 ER 1440). The explanation for this lies in the old form of action known as *indebitatus assumpsit*. This form of action was based on a fictional promise to pay a debt arising out of a contract. It was a distinct cause of action from a claim for damages. Still today, there is a distinction between a claim for a contractual debt and a claim for damages for breach of contract. Because the debt is payable at any time it is demanded, it is accepted that the cause of action on the debt arose when it was first advanced.

The New South Wales Law Reform Commission published a report on this topic in 2004.⁵⁹ The Commission expressed the view that the current law should be changed so that the limitation period runs from the time of the first demand, but so far the reform has not been enacted.

PART B EQUITABLE REMEDIES

A range of equitable remedies can arise in the commercial litigation context. In today's seminar I shall discuss two of the remedies which are apt to arise in contract disputes, that is specific performance and rescission. I believe that rectification has been addressed in an earlier seminar in this series.

Specific Performance

Executed and Executory Contracts

Sometimes it is necessary to distinguish between specific performance proper and specific performance in the broader sense. Specific performance proper relates only to executory contracts. In contrast, when we talk about specific performance in the broader sense, we are talking about equitable relief in aid

⁵⁸ (1956) 99 CLR 560.

⁵⁹ The Law Reform Commission of NSW, Report 105, "Time limits on loans payable on demand", 2004.

of requiring parties to comply with the terms of their contract, whether executed or executory.

Executory contracts are contracts which require some further act of the parties, after entry into contractual relations, in order to put them into the legal relationship or the legal position which the contract contemplates. For example:

- contract for the sale of land (ie, requiring an executed transfer);
- agreement to enter into lease (ie, requiring entry into a lease);
- agreement to enter into a partnership (ie, requiring entry into a partnership deed).

When the further act required by an executory contract has been carried out, the contract is an **executed contract**. So, when the lease has actually been entered into, the contract is executed. The parties now stand as landlord and tenant. Their ongoing rights and liabilities are governed by the lease, which is an executed contract. If we seek specific performance of the agreement for lease, so as to require one party or the other to precede with entering into the lease, we are seeking specific performance proper. If, following the entry into the lease, we seek an injunction to restrain a breach, or a mandatory injunction to require a party to comply with the lease, we are seeking specific performance in the broader sense.

In many respects, the distinction is not important, but sometimes it does arise. For example, it is said that when the court decrees specific performance it does so in relation to the whole contract and not specific obligations under it. That proposition is true of specific performance proper, but within the broader concept of specific performance, the court may well grant an injunction in respect of a specific obligation which is being breached.

Requirements for Specific Performance

The first requirement (or two requirements) for specific performance is that there be a **valid contract for consideration**. Because of the doctrine of part performance, it is not always necessary that the valid contract also be enforceable. But there must be consideration: the seal on a deed is not

enough.

The second requirement is that damages is not an adequate remedy.

It is long established that damages will not be an adequate remedy in the case of contracts for the sale of land.⁶⁰ This proposition is so well entrenched that it is unlikely that a defendant will be able to persuade the court otherwise.

Apart from contracts concerning land, there are many other types of contract where specific performance may be granted. There is a lot of case law in this area and some of the older cases seem to lay down rules about particular types of contract. As a practical point, you should always look at whether contracts of the type in issue have been dealt with in the cases. But the cases can be misleading, because the modern approach is look at the circumstances of the particular case to work out whether damages is an adequate remedy. According to Spry:⁶¹

[T]he adequacy of damages must be considered from a practical and not a theoretical point of view. Damages must put the plaintiff in the same position in all material respects for specific performance to be refused on this ground, as opposed to discretionary grounds.

The third requirement relates to the issue of breach. If the defendant has failed to perform then the plaintiff can bring proceedings. But the plaintiff does not need to wait for an actual breach of the relevant obligation: it is enough that the defendant has threatened breach.⁶²

The fourth requirement is that the plaintiff, at the time of commencement of the action, has performed, or is ready, willing and able to perform the contract. But this does not mean that any breach by the plaintiff, however trivial, will result in the plaintiff failing. The plaintiff must perform or be ready and willing to perform the substance of the contract.⁶³

⁶⁰ See, for example, *Adderley v Dixon* (1824) Sim & st 607 at 610; *Re Scott and Alvarez's Contract: Scott v Alvarez* [1895] 2 Ch 603; *Dougan v Ley* (1946) 71 CLR 142 and the dissent of Sir Garfield Barwick in *Loan Investment Corp of Australasia v Bonner* [1970] NZLR 724

⁶¹ Spry, *Equitable Remedies*, 2001 LBC Information Services, Australia at p 66

⁶² *Turner v Bladin* (1951) 82 CLR 463

⁶³ *Green v Sommerville* (1979) 141 CLR 594 per Mason J at 610

This requirement is often characterised as a discretionary factor rather than as a basic prerequisite of relief. Arguably, readiness, willingness and ability need not be specifically pleaded, because it is implied in the pleading under the rules.⁶⁴ But one should bear in mind, notwithstanding this rule of pleading, that a plaintiff seeking equitable relief needs to offer to do equity – and in this context, that would include an offer to do all that is required of the plaintiff under the contract.

Whatever may be the position as to a requirement to plead readiness, willingness and ability, it is the plaintiff who bears the onus of proof once it is in issue.⁶⁵

Defences

There are several discretionary defences which can be raised in a suit for specific performance:

- (a) the decree would require continual supervision by the court;
- (b) contracts for personal service or involving a personal relationship;
- (c) want of mutuality;
- (d) impossibility of performance;
- (e) futility;
- (f) hardship;
- (g) unenforceability for want of writing – although this is subject to the equity raised by part performance;
- (g) disentitling conduct of the plaintiff: misrepresentation; mistake contributed to by plaintiff; lack of clean hands, unconscionable conduct; laches, acquiescence.

Form of relief

⁶⁴ *Uniform Civil Procedure Rules 2005* (NSW) r 14.11(d)

⁶⁵ As discussed by Mason CJ and Dawson J in *Bahr v Nicolay [No. 2]* 164 CLR 604 at 619 to 621.

There are two general forms of relief. An order for specific performance may be made, together with an order reserving liberty to apply, so that if necessary a detailed regime of orders can be sought at a later date.

The alternative is for the court to make a detailed set of orders for implementation, at the same time as making the order for specific performance. This approach may be appropriate where, for example, there are likely to be ongoing difficulties with performance.

Effect of an order for specific performance

A decree of specific performance does not supersede the contractual rights and obligations of the parties, but it does bring the future exercise of rights and performance of obligations under the contract under the control of the court.⁶⁶

An order for specific performance can be enforced using the court's various powers, but usually it will be necessary to have in place precise implementation orders first.

But what if the defendant, after the decree, has engaged in further conduct which, under the general law of contract, would justify termination? That is to say, the defendant is guilty of breach of an essential term, or a fundamental breach amounting to repudiation, or an anticipatory breach which the plaintiff would be entitled to accept and so terminate.

In such a situation, the plaintiff may prefer to terminate. Can he or she do so?

The answer is that it is possible to terminate in this situation, but a court order is necessary: a party is not entitled simply to terminate the contract as at general law.⁶⁷ The requirement for a court order in this situation has been

⁶⁶ *Singh v Nazeer* [1979] Ch 474 at 481-2; *Buckman v Rose* (1980) 1 BPR 9558; *Sunbird Plaza Pty Ltd v Maloney* (1988) 166 CLR 245 at 259-260; *Zorbas v Titan Properties (Aust)* [2005] NSWSC 440 at [12].

⁶⁷ *JAG Investment Pty Ltd v Strati* [1981] 2 NSWLR 600; *Sunbird Plaza Pty Ltd v Maloney* (1988) 166 CLR 245.

criticised on the basis of principle, but not authority.⁶⁸

Where a party seeks an order for rescission, the court does not merely adjudicate on whether the right to rescind has arisen; rather, it exercises a discretion.⁶⁹ That discretion is to be exercised on equitable principles according to the requirements of justice between the parties.⁷⁰

There are differing views as to the form in which relief is given in this situation.⁷¹ The differences hinge on whether it is the court which brings an end to the contract or whether the court discharges its earlier decree, leaving it to one or other of the parties to terminate. It is submitted that the better view that relief ought to be framed in terms of the relevant order for specific performance (and ancillary orders) being discharged and the court giving leave (so far as necessary) to the relevant party to terminate the contract.

Rescission - at Law and in Equity

The term rescission is used in various senses, but in its narrow sense the term is concerned with the avoidance *ab initio* of agreements or other dispositions.

Common Law vs Equity

There is a common law remedy of rescission and an equitable remedy of rescission.

The common law remedy of rescission is “self help”. A person entitled to rescind – for example, on the ground of fraud or duress – communicates his or her election to the other party and the agreement is thereby avoided.

The equitable remedy of rescission is not self help: it requires a court order, and the court has a discretion whether to grant it.

⁶⁸ Meagher RP, Heydon JD and Leeming MJ, *Meagher, Gummow and Lehane's Equity Doctrines and Remedies* (4th ed, Butterworths, 2002) at p 699-700.

⁶⁹ *Facey v Rawsthorne* (1925) 35 CLR 566; *JAG Investment Pty Ltd v Strati* [1981] 2 NSWLR 600.

⁷⁰ *JAG Investment Pty Ltd v Strati* [1981] 2 NSWLR 600, quoting McLelland J in *Buckman v Rose* (1980) 1 BPR 9558.

⁷¹ As discussed in Finnane E, Newton H and Wood C, *Equity Practice and Precedents* at 117-119.

To rescind at common law, it is not enough that a party has a recognized common law ground to do so – such as duress. In addition, that party needs to be in a position to restore the parties to their original state before the contract. Money must be repaid and property returned. If that cannot be done precisely, the contract cannot be rescinded at common law. This requirement is referred to as *restitutio in integrum*, and is applied quite strictly at common law.

Rescission in equity

Where precise *restitutio in integrum* is not possible, a party may still be able to rescind in equity. Rescission in equity is available on grounds that justify common law rescission - fraud and duress - as well as purely equitable grounds, such as undue influence, *Amadio* unconscionability and misrepresentation. (I believe that some or all of these grounds have been covered in earlier seminars in this series, and so I will not go into the elements of them.)

Whilst equity does not insist on precise *restitutio in integrum*, it is said that equity requires “substantial *restitutio in integrum*”,⁷² or that, by the exercise of its powers, it can do what is “practically just between the parties, and by so doing restore them substantially to the status quo.”⁷³

Equity has a broader array of remedies available to it than the common law, which it can use to achieve substantive restitution, in conjunction with a decree for rescission. For example, relief can be granted on conditions, or accounts and inquiries can be ordered so as to work out what adjustments need to be made between the parties.

⁷² D Wright, *Fiduciaries, Rescission and the Recent Changes to the High Court’s Equity Jurisprudence* (1998) 13 JCL 166.

⁷³ *Alati v Kruger* (1955) 94 CLR 216 at 224.

Working out the appropriate remedy

Alati v Kruger

Alati v Kruger,⁷⁴ was a case of rescission on the ground of common law fraud. The transaction was a sale of a business, which the purchaser was entitled to rescind because of fraudulent misrepresentations about takings. The purchaser had completed the purchase and gone into possession, before realising the fraud and taking proceedings for rescission. The purchaser succeeded but by the time of final orders, there was no prospect of the business being returned to the vendor as it had been closed down and the premises vacated. The court still permitted rescission. The substantive orders, after variation by the High Court, were to the following effect:

1. A declaration that the contract was lawfully rescinded by the respondent.
2. An order that all executed copies of it be cancelled.
3. An order (described as a declaration) requiring the plaintiff to deliver up to the defendant such chattels which were the subject of the contract as the plaintiff retained.
4. An order that an inquiry be held to ascertain the value of chattels not in the plaintiff's possession or control, the value of stock in trade received by the plaintiff from the defendant, and whether any amount should be allowed in favour of the defendant for use by the plaintiff of the defendant's property.
5. An order requiring the defendant to repay the purchase price, adjusted by reference to the value of the chattels not returned and certain other amounts, plus interest.

It is useful, with the above example in mind, to explore the basis on which such equitable relief is shaped.

I have said that the court needs to do what is "practically just". It should be noted that in the above example the court considered this requirement met

⁷⁴ (1955) 94 CLR 216.

even in circumstances where

- the lease was at an end and therefore the vendor could not be restored to his pre-contract position; yet
- the vendor was not to be given any compensation for this as part of the court's relief.

So, how could rescission be allowed in such circumstances without any requirement of compensation?

At common law the purchaser's entry into possession, alone, was enough to preclude rescission⁷⁵ - let alone the fact that there was no longer a lease to be retransferred. (It should be pointed out that it was recognised in *Alati v Kruger* that there are exceptions at common law to the requirement of precise restitutio in integrum, but they would not have assisted the purchaser.)

But equitable remedies are discretionary and flexible, and appropriate relief can be moulded so as to do practical justice. The court could decide on whether to grant relief, but also, on what terms, in the light of the fact that the business had closed down and the circumstances in which that had occurred.

This was discussed in the joint judgment of Dixon CJ, Webb, Kitto and Taylor JJ, as well as in the judgment of Fullagar J (where his Honour agreed with the orders proposed).

One possibility would be for the court to conclude that the purchaser had acted unconscientiously during the dispute by abandoning the premises, and on that basis, decline relief.

Another possibility, referred to by Fullagar J, was for the court to require the purchaser to compensate the vendor as a condition of relief.

But in the present case it could not be said that the purchaser acted unconscientiously. The purchaser had continued in the business for a considerable period (indeed, up to the end of the trial, when the trial judge had announced his findings and had reserved on the question of restitutio in integrum). The purchaser could not be expected to go on indefinitely,

⁷⁵ *Blackburn v Smith* (1848) 2 Ex. 783 at 792.

incurring losses. On the view of Dixon CJ, Webb, Kitto and Taylor JJ, the vendor was able to protect his interest, whether by appointing a receiver or by offering to take the property back or by proposing an interim arrangement.

Fullagar J considered that the purchaser should give reasonable notice before parting with possession, although the absence of reasonable notice in the immediate case did not matter because the defendant failed to show that he suffered loss by the closure of the business.

If one considers the effect of the orders in *Alati v Kruger* it is clear that the vendor was not restored to his prior position, even in a substantive sense. The vendor did not get his business back, nor any compensation for the loss of the lease or the goodwill. It might be said that the expression “substantive restitutio in integrum”, used in the joint judgment, did not describe the result of the case. The answer to such a charge is that, in the way the High Court viewed the matter, any such losses were attributable entirely to the vendor’s failure to take care of his own interests.

What the court must do in exercising its discretion, both as to whether to grant or permit rescission, and as to the terms on which relief is granted, is determine what is required by way of “practical justice”. This requirement of practical justice is informed by the maxim that “he who seeks equity must do equity”, and more generally, it is informed by equitable principles and discretionary factors.⁷⁶

The precise orders which should be made will always be driven by the circumstances of the case, which circumstances include, not merely the nature of the transaction and the position of the respective parties following the transaction, but also a consideration of what was the wrong which gave rise to the right to rescission and what was its consequence.

Maguire v Makaronis

⁷⁶ See for example *Vadasz v Pioneer Concrete (SA) Pty Ltd* (1995) 184 CLR 102 at 110 to 116.

*Maguire v Makaronis*⁷⁷ was a case of rescission on equitable grounds. A husband and wife, who were clients of solicitors, executed a mortgage in favour of the solicitors to secure bridging finance for the purchase of a poultry farm. The solicitors did not draw the clients' attention to the fact that the solicitors were to be the mortgagees, and nor did they tell them that they should obtain independent legal advice. The clients defaulted on the loan secured by the mortgage and the solicitors claimed possession of the mortgaged property. The clients were held to be entitled to rescission on the ground of breach of fiduciary duty. However, relief was conditional on payment of principal and interest. Failing such payment judgment for possession was to be entered in favour of the mortgagee.

Vadasz v Pioneer Concrete (SA) Pty Ltd

Maguire v Makaronis concerned rescission by borrowers who had use of the money advanced under a voidable transaction. What about guarantors?

An interesting contrast can be made the contrast between two guarantee cases - *Commercial Bank of Australia v Amadio*⁷⁸ and *Vadasz v Pioneer Concrete (SA) Pty Ltd*⁷⁹, as discussed in the latter case at p 115. In *Amadio*, the *Amadios* were led to believe that they were guaranteeing their son's overdraft to a limit of \$50,000. In granting relief the court relieved them from the whole of their liability on the ground that they would not have entered into the transaction at all had they known the true position.

In *Vadasz*, in contrast, the plaintiff was prepared to guarantee the future debts of the company, but did not know (as he was misled) that the guarantee he signed also extended to past debts. In those circumstances, the High Court considered that the trial judge was correct to decide that the guarantee could not be enforced in respect of the past indebtedness but could still be enforced in respect of the future indebtedness.

⁷⁷ (1997) 188 CLR 449

⁷⁸ (1983) 151 CLR 447.

⁷⁹ (1995) 184 CLR 102.

This decision has excited some controversy on the basis that it “invents a doctrine of partial rescission”.⁸⁰

The distinction between common law and equitable fraud in shaping the remedy

A further point to be aware of is the distinction between rescission for common law fraud and rescission in equity. There are two important consequences for the framing of remedies. First, common law fraud (unlike innocent misrepresentation in equity) gives rise to an entitlement to damages for deceit. When cases of common law fraud are dealt with in equity the process of restitutio in integrum can include an indemnity in lieu of damages.⁸¹ Secondly, in cases of common law fraud, the courts are traditionally far more prepared to leave a defendant uncompensated than in cases not involving conscious fraud.⁸²

Statutory Alternatives

It is a little artificial to mention rescission, and the various grounds on which it is available, without at least noticing that the facts giving rise to rescission will often also justify relief, including relief analogous to rescission, under statutory provisions. In particular, in general commercial litigation, one needs to keep in mind the relevant provisions of the Australian Consumer Law and the Contracts Review Act 1980 (NSW).

PART C RESTITUTION

Restitution can arise in a contractual setting in various situations. I will limit

⁸⁰ See Meagher RP, Heydon JD and Leeming MJ, *Meagher, Gummow and Lehane's Equity Doctrines and Remedies* (4th ed, Butterworths, 2002) at [24-050].

⁸¹ As discussed in *Belperio v Munchies Management* (1989) ATPR 40-926 at p 50,034 to 50,036.

⁸² *Berridge v Public Trustee* (1914) 33 NZLR 865 at 872; See Meagher RP, Heydon JD and Leeming MJ, *Meagher, Gummow and Lehane's Equity Doctrines and Remedies* (4th ed, Butterworths, 2002) at [24-080].

the treatment of this topic to restitution of monies paid, following the termination of a contract. I will deal with this topic briefly and at a level of general principle.

Recovery of monies paid, following termination of a contract, was historically the subject of the common money count for monies had and received by the defendant to the use of the plaintiff, on a total failure of consideration. Notwithstanding developments in recent decades affecting the law of restitution, the concept of total failure of consideration continues to be the basis of recovery of payments in this area. In terms of the modern principle of unjust enrichment, total failure of consideration is an “unjust factor”.⁸³

The failure of consideration must be “total”, not partial. In *Baltic Shipping Co v Dillon (the Mikhail Lermontov)* (1993) 176 CLR 344, the plaintiff bought a ticket on a cruise ship, and it sunk during the voyage. The plaintiff was not entitled to recover the fare, because the plaintiff had received part of the bargained-for benefit.

Where a payment has been made under a contract, and the recipient has not performed its side of the contract at all, it may be relatively easy to say, when the contract is terminated, that there has been a total failure of consideration. In this way, instalments under a purchase contract will be repayable. (Deposits are in a different category. They are part of the price, but they are also an earnest of performance. The purchaser may forfeit a deposit, and thus have no entitlement to restitution following termination. Usually, this is provided for expressly in the contract, but if it is not, a right of forfeiture will normally be implied.⁸⁴)

The situation is more complicated where there has been partial performance under the contract.

It is often the case that termination following partial performance of a contract leads to questions, not of restitution, but whether a party is entitled to recover

⁸³ See Mason, Carter, Tolhurst, *Mason & Carter's Restitution Law in Australia, 2nd Ed*, 2008, p 414.

⁸⁴ *Howe v Smith* (1884) 27 Ch D 89; Carter, Peden, Tolhurst, *Contract Law in Australia, 5th Edition*, 2007, p 892.

a debt for something done prior to termination, or in respect of an amount that fell due prior to termination. Such debt claims are in fact the other side of the coin to restitution claims. Indeed, a defendant to such a debt claim may raise total failure of consideration as a defence – ie, if the payment were to be made, it would be immediately recoverable on the ground of total failure of consideration.⁸⁵

In *McDonald v Dennys Lascelles Ltd*⁸⁶ Dixon J said:

"When a party to a simple contract, upon a breach by the other contracting party of a condition of the contract, elects to treat the contract as no longer binding upon him, the contract is not rescinded as from the beginning. Both parties are discharged from the further performance of the contract, but rights are not divested or discharged which have already been unconditionally acquired. Rights and obligations which arise from the partial execution of the contract and causes of action which have accrued from its breach alike continue unaffected. When a contract is rescinded because of matters which affect its formation, as in the case of fraud, the parties are to be rehabilitated and restored, so far as may be, to the position they occupied before the contract was made. But when a contract, which is not void or voidable at law, or liable to be set aside in equity, is dissolved at the election of one party because the other has not observed an essential condition or has committed a breach going to its root, the contract is determined so far as it is executory only and the party in default is liable for damages for its breach."

Whether one is considering a debt claim for monies not paid, or a restitution claim to recover monies that have been paid, it will be necessary to determine whether the right to payment has accrued.

This can in practice be very difficult to determine. The question is not simply whether the time for payment has arrived, because, for example, a party may have been required to pay the entire contract sum up front, with no performance being rendered at all at that stage.

This is a complex area of law and the outcome in particular cases can be difficult to work out.

⁸⁵ See *McDonald v Dennys Lascelles Ltd* (1933) 48 CLR 457; Mason, Carter, Tolhurst, *Mason & Carter's Restitution Law in Australia, 2nd Ed.*, 2008, p 426.

⁸⁶ (1933) 48 CLR 457 at 476-7.

Dixon and Evatt JJ said in *Westralian Farmers Limited -v- Commonwealth Agricultural Service Engineers Limited* (1935) 54 CLR 361 (at 379-80) said:

“When a contract comes to an end by reason of the occurrence of an event upon which the parties have by an express provision made it terminate, the question whether an inchoate liability arising thereunder does or does not become enforceable must in the end be governed by the intention of the parties. It is a rule of law that when a simple contract is discharged by the election of one party to treat himself as no longer bound after the other has committed a breach of the contract, rights and obligations which have already arisen from the partial execution of the contract shall remain unaffected (see McDonald v. Dennys Lascelles Ltd (1933) 48 C.L.R., at pp. 476, 477). No doubt it is open to the parties to provide in advance for such an event and by a stipulation to the contrary to produce some other effect. When the parties themselves have provided for the determination of the contract on a given contingency, the consequences flow altogether from their contractual stipulation and are governed by their intention, either actual or imputed. In the present case, however, all the agreement expressly says is that in any of the specified events it shall immediately terminate and be at an end. In applying such a compendious provision to a continuing relationship of the complicated character which the agreement establishes some guidance may be found in the nature of the agreement and of the obligations to which it gives rise. But primarily it remits the inquiry to a general consideration of what is involved in the sudden termination of an executory agreement under which liabilities are accruing from day to day. We are concerned only with a liability to pay a liquidated demand. In general the termination of an executory agreement out of the performance of which pecuniary demands may arise imports that, just as on the one side no further acts of performance can be required, so, on the other side, no liability can be brought into existence if it depends upon a further act of performance. If the title to rights consists of vestitive facts which would result from the further execution of the contract but which have not been brought about before the agreement terminates, the rights cannot arise. But if all the facts have occurred which entitle one party to such a right as a debt, a distinct chose in action which for many purposes is conceived as possessing proprietary characteristics, the fact that the right to payment is future or is contingent upon some event, not involving further performance of the contract, does not prevent it maturing into an immediately enforceable obligation.”

(Emphasis added.)

If anything, the above passage shows how difficult this area is at a conceptual level. More recently, McColl JA, in the NSW Court of Appeal endorsed an approach involving consideration of three factors:

- the terms of the contract;
- the performance rendered by the party claiming the accrued right; and
- the relations between the obligations sought to be enforced and the obligations discharged by termination.⁸⁷

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Neale v Ancher Mortlock and Woolley Pty Ltd [2013] NSWCA 209 at [20], citing *J W Carter, Breach of Contract, 2nd ed (1991) The Law Book Company Limited* (at [1235]); and also referring to *J W Carter and J C Phillips "The Liability of Debtors and Guarantors Under Contracts Discharged for Breach" (1992) 22 University of Western Australia Law Review 338* (at 343).