Allens Contract Law Update 2012
Introduction

A little over 12 months ago, the High Court delivered its judgment in Western Export Services. It was one of the most important recent contract law judgments in Australia, as it greatly limited the circumstances in which courts will have regard to surrounding circumstances for the purpose of interpreting contracts.

This Contract Law Update summarises important contract law decisions by Australian appellate courts in the 12 months following the judgment in Western Export Services. Many of these judgments also consider when courts will have regard to evidence of surrounding circumstances, albeit usually for purposes other than interpreting contracts. There have also, however, been important judgments in many other areas of contract law, from contract formation through to the enforcement of illegal contracts and (alleged) penalties.

This update provides an overview of these recent appellate decisions, and their significance for the development of Australian contract law. The case summaries attached to this update have been prepared by the litigation department at Allens.

1 Western Export Services Inc v Jireh International Pty Ltd [2011] HCA 45
2 For more information on this decision, see our Focus article
3 See section 3 below.
4 See section 2
5 See section 4
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Chapter 1: Contract formation

Contract formation

An issue that often arises in contract disputes is whether a contract has been formed and, if so, on what terms. In Osbourne\(^6\), the appellant argued that it was not bound by a contract to purchase concrete from the respondent because the person who ordered the concrete had no authority to do so. The New South Wales Court of Appeal rejected this argument on the basis that the appellant had implicitly authorised the relevant individual to describe himself as ‘General Manager, Development & Finance’ and that it was within the implied authority of a person with this title to order concrete. The case also contains a useful discussion as to why representations in emails will often be admissible as exceptions to the hearsay rule.

In Malago\(^7\), the NSW Court of Appeal considered another common issue: whether a ‘Heads of Agreement’, which contemplated a more detailed, formal contract being executed, was nevertheless itself a binding agreement. The issue in this case was relatively easy to resolve because the parties themselves had referred to the agreement as ‘binding’. Importantly, the court was prepared to make an order compelling the parties to enter into a formal sale agreement on terms to the same effect as those in the Heads of Agreement, together with some additional terms of a ‘mechanical nature’.

\(^6\) Osbourne v Bold Resources (NSW) Pty Ltd [2012] NSW CA 155.

\(^7\) Malago Pty Ltd v AWLS Engineering Pty Ltd [2012] NSW CA 227.
Disputes as to the terms on which a contract has been entered into often centre on whether an agreement effectively incorporates terms in a different document. In *Ange* the relevant ‘General Conditions’ were not attached to the final contract. Nevertheless, the Victorian Court of Appeal held that the General Conditions were part of a final contract because a copy had previously been provided to the other party and they had been clearly and specifically incorporated by reference. The judgment also contains an interesting discussion of the law of penalties (this discussion was largely superseded by the later High Court judgment in *Andrews*) and the doctrine of frustration.

In *Hughes* the Western Australia Court of Appeal considered whether the terms of an option had been varied by a subsequent letter agreement. On the facts of that case, the letter agreement was effective to vary the terms. However, because there is continuing uncertainty as to the juristic nature of an option (in particular, whether it is a conditional contract or an irrevocable offer), there is also uncertainty as to what is required to amend an option agreement. The safest approach may be to ensure that variations to option agreements are effected by deeds.

One of the old rules in relation to the formation of a contract is known as the ‘Postal Acceptance Rule’. In *Wardle*, the NSW Court of Appeal rejected an attempt to extend this rule to the performance of obligations under a contract.

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8 *Ange v First East Auction Holdings Pty Ltd* [2011] VSCS 335.
10 *Hughes v SST Barbara Ltd* [2011] WACA 234.
12 *Velvet Glove Holdings Pty Ltd v Mt Isa Mines Ltd* [2011] QCA 312.
Osborne v Boral Resources (NSW) Pty Ltd [2012] NSWCA 155

Authority of agent to incur liability under contract
Hearsay exception
Emails as business records
Section 69 Evidence Act 1995 (Cth)

This case confirms that: (i) an individual who represents himself or herself to hold a position within a company will, if the company permits that representation to be made, be inferred to have authority to make decisions that are typically made by a person with such a position; and (ii) emails containing hearsay will often be admissible as business records under section 69 of the Evidence Act 1995 (Cth).

This decision of the NSW Court of Appeal, on 23 May 2012, dealt with a company’s failure to pay for concrete supplied to it by another company. The purchaser alleged that the concrete had never been ordered or delivered.

The facts

Mr Osborne was the sole shareholder and director of Development and Investments Australia Group Pty Ltd (DIAG). DIAG entered into a credit agreement with Boral Resources (NSW) Pty Ltd (Boral). Under that agreement, a large amount of concrete was ordered and delivered in batches to an address in St Marys, with invoices sent to a post office box. Both addresses were listed in the credit agreement.

In December 2008, Mr James, who was the General Manager, Development & Finance, at DIAG, sent a new credit application form to Boral on behalf of DIAG. On the basis of that form, Boral delivered more concrete. DIAG subsequently failed to pay for the concrete. On 5 June 2009, Boral filed a statement of claim against DIAG and the appellant, claiming $217,000 for the concrete supplied and invoiced, as well as the costs of recovery and interest. Mr Osborne claimed that:

- the goods were not delivered because the St Marys address was not occupied or connected with him or DIAG; and
- there was no evidence to suggest that the concrete had been ordered by DIAG; or
- the person who ordered the concrete (Mr James) was not authorised to do so.

The judgment

The NSW Court of Appeal swiftly rejected the appellant’s arguments and held that there was clear evidence to demonstrate that Boral had delivered the concrete.

Authority of Mr James

Chief Justice Bathurst (with whom Justice Allsop and Justice Macfarlan agreed) upheld the primary judge’s decision that Mr James was an associate of Mr Osborne and DIAG. He had authority to order the concrete as:

- he was represented to be the General Manager, Development & Finance, at DIAG;
- it is a valid inference that DIAG had authorised Mr James to make this representation; and
- it was within the implied authority of a General Manager, Development & Finance, to order concrete.
Emails as business records

The issue whether DIAG had ordered concrete from Boral turned on evidence contained in two emails. Implicit in the reasoning of Chief Justice Bathurst and Justice Allsop was the conclusion that these emails were business records and thus exceptions to the hearsay rule.

Justice Macfarlan's approach was more detailed. In relation to an email sent by Mr James on behalf of DIAG, Justice Macfarlan:

• held that the email was presumed to have been sent by DIAG by virtue of s161 of the Evidence Act 1995 (Cth) (the Act);
• inferred that a copy had been retained by DIAG as part of its business records on the basis of the power conferred by s183 of the Act; and
• concluded that the email was a copy of a business record within the meaning of s69 of the Act.

As such, Mr James' email was admitted as evidence of his representation that he held the position of General Manager, Finance and Operations, of DIAG, notwithstanding that the evidence was hearsay.

Whether emails are admissible as business records was also considered by Justice Austin in ASIC v Rich [2005] NSWSC 741, where he held that emails between the Chief Operating Officer of One.Tel Europe and a non-executive director of One.Tel Ltd were excepted from the hearsay rule, as they were business records within the definition in s69 of the Act. He made his decision on the basis that:

• they formed part of the records kept by the director of One.Tel in his capacity as director; and
• their subject matter related to the company's cash position.

The emails were considered to be business records, even though there was no evidence that they were kept by any body corporate. Justice Austin inferred that the documents formed part of the records kept by the director of One.Tel, as they were kept by him in the course of or for the purposes of One.Tel's business rather than for his personal or private use.

Aqua-Marine v Reef Fisheries (No 4) [2011] FCA 578 shows a similarly broad approach to emails as business records. Justice Collier of the Federal Court of Australia held that an email was admissible under s69, even though it was a business record of a company not actually party to the proceedings. Collectively, these authorities suggest that courts are inclined to admit emails as business records under the s69 hearsay exception.
Malago Pty Ltd v AW Ellis Engineering Pty Ltd [2012] NSWCA 227

- Heads of Agreement
- Parties intended to be legally bound
- Not void for uncertainty or incompleteness
- Negotiations between solicitors concerning formal agreement intended to give effect to Heads of Agreement
- Parties bound by Heads of Agreement even though subsequent formal agreement had not been executed

This case is significant because it is a reminder to parties that a Heads of Agreement may be legally binding. However, in ordering specific performance of a contract, the court will not enforce terms that have not been agreed between the parties. This case shows that courts can give effect to agreements reached at mediations and may order specific performance of such agreements.

The facts

The appellant (the James interests) entered into negotiations with the respondent (the Ellis interests) for the sale of a super yacht marina business at Rozelle Bay in Sydney. During negotiations, the parties fell into dispute, which was referred to mediation before Mr R J Ellicott QC. At the conclusion of the mediation, the parties entered into a Heads of Agreement for the James interests to purchase the Ellis interests in the business. The parties subsequently failed to settle a formal contract giving effect to the terms of the Heads of Agreement. The James interests then withdrew from the negotiations, and proceedings were commenced by the Ellis interests seeking specific performance of the Heads of Agreement and the sale of the business. In the initial proceedings, the court found for the Ellis interests. The James interests appealed.
The appeal judgment

The Court of Appeal upheld the trial judge’s finding that the requisite intention to contract existed between the parties, as the Heads of Agreement contained plain and unequivocal language that the parties intended to be bound. In particular, the court held that the inclusion of the words ‘Without affecting the binding nature of these Heads of Agreement’ indicated the parties’ intention to enter a legally binding contract. The court upheld the trial judge’s finding that the James interests had breached the Heads of Agreement by ceasing to instruct their solicitors to negotiate the formal contract as contemplated by clause 1(g) of the Heads of Agreement.

In respect of the appropriate remedy, the court altered the trial judge’s orders for specific performance, which were that the formal contract could be supplemented with specific clauses that either had not been settled at the end of the mediation or clauses that were ‘reasonable and consistent’ with the agreed terms.

The court found that the parties did not intend to bind themselves to an agreement containing terms agreed by their respective solicitors without the necessary instructions from their clients. The court distinguished the present case from situations where additional terms were to be determined by the parties’ solicitors, such terms being provisions of a ‘mechanical nature’ only, and not requiring agreement between the parties.

In the present case, evidence of the parties’ negotiations following the mediation showed that the solicitors continued to operate on the basis of instructions from their clients and that the solicitors were not instructed to act independently to determine the outstanding terms of the contract. In altering the trial judge’s orders for specific performance, the court also considered the construction of clause 1(g) of the Heads of Agreement, and found that this clause required that the parties enter into a formal agreement containing terms to the same effect as the Heads of Agreement. Clause 1(g) of the Heads of Agreement stated:

(g) Without affecting the binding nature of these Heads of Agreement the parties within 7 days to execute a formal document or documents as agreed between their respective solicitors to carry out and express in more formal terms and additional terms as these Heads of Agreement...

The court ordered specific performance of the Heads of Agreement by entering into a formal contract for sale containing terms to the same effect as the Heads of Agreement. The court also ordered that the James interests perform the formal contract for sale.
Ange v First East Auction Holdings Pty Ltd [2011] VSCA 335

> Contract
> Incorporation of conditions
> Frustration
> Breach of contract
> Applicability of doctrine of penalties

Parties may be bound by the general conditions referenced within a contract, even if such conditions are not attached to the main contract. Additionally, parties to a contract should be aware that their conduct will be a relevant factor in determining whether they knew of, and thus ought to be bound by, the conditions in question.

This decision of the Victorian Court of Appeal, on 8 November 2011, dealt with a number of standard form contractual issues, including: the enforceability of general conditions of a contract where they have not been attached to the final, signed contract; frustration of a contract due to extraneous circumstances; and whether a fee charged upon withdrawal from a contract constitutes a penalty.

The Victorian Court of Appeal held that the general conditions were incorporated into, and formed part of, the contract in question, despite not being attached to the final contract, as they had been provided to the party previously and were specifically referred to at the contract signing. The court also held that a term of a contract which required a party to pay a fee upon withdrawing from the contract was not a penalty, for the purposes of the doctrine of penalties, as the doctrine only applied if there had been a breach of contract.22

The facts

The appellant, Mrs Ange, and her husband were collectors of valuable and expensive art. Between November 2000 and June 2007, Mr and Mrs Ange had regular contact with the respondent, an auctioneer house commonly known as Bonhams, as they had bought and sold artwork through it. Throughout their dealings, Mr and Mrs Ange made statements to the effect that the art collection belonged to Mrs Ange and Bonhams took this to be the truth.

In December 2007, Mr and Mrs Ange separated. Mrs Ange contacted Bonhams to value the art collection, explaining to them that she may have to sell it, or some pieces, as a result of the separation. Mrs Ange also requested that Bonhams store the collection for her. Bonhams agreed to do so, at no charge. On 24 February 2009, Bonhams sent Mrs Ange a standard form consignment agreement (the 24 February agreement), which attached a document titled ‘General Conditions of Business of Bonhams As at 19 June 2008’ (the general conditions) and listed the artworks that were to be stored by Bonhams.
Between February 2009 and March 2009, Mrs Ange and Bonhams regularly corresponded about the possibility of selling some of the stored paintings in an auction being held in May 2009. As a result of her perpetual indecisiveness, Bonhams informed Mrs Ange that there would be substantial withdrawal fees if she changed her mind after consigning the paintings. On the last day that the paintings could be included in the May auction catalogue, Mrs Ange agreed to consign some of her paintings for sale. Instead of preparing a new consignment agreement, Bonhams simply amended the 24 February agreement and photocopied the four amended pages for signature. Significantly, Bonhams did not reproduce and attach the general conditions to this agreement (the agreement). Mrs Ange signed the agreement in nine separate locations.

Upon learning that Mrs Ange had agreed to auction off the art collection, Mr Ange applied to the Family Court of Australia for an injunction to stop Mrs Ange from selling the artworks on the basis that the art collection was either owned by him or by them jointly. On 5 May 2009, the court granted an injunction that required Mrs Ange to withdraw the paintings from sale. The next day, Mrs Ange gave Bonham’s written notice requesting the paintings to be withdrawn from the auction, which was being held that evening. Bonhams subsequently sent Mrs Ange a tax invoice requiring payment of $749,284, being the withdrawal fee stipulated in the General Conditions (the clause). Mrs Ange refused to pay the invoice and Bonhams issued proceedings claiming the withdrawal fee. The trial judge found in favour of Bonhams and ordered Mrs Ange to pay the withdrawal fee. Mrs Ange appealed.

### The judgment

The Victorian Court of Appeal upheld the decision of the trial judge in its entirety, stating that the withdrawal fee was payable to Bonhams as the general conditions did form part of the agreement and the terms of the agreement were in no way impacted by the doctrines of penalty, frustration or unconscionability.

In particular, the court relied on Walker v Citigroup Global Markets Australia Pty Limited (2006) 233 ALR 687 and held that:

> The General Conditions in the present case form part of the agreement between Mrs Ange and Bonhams. They were intended to form part of it. They were in the possession of Mrs Ange and were clearly and specifically incorporated by reference.

Interestingly, in order to determine whether the general conditions formed part of the main contract, the court considered the circumstances surrounding the execution of the agreement, including the prior business dealings of the parties. In doing so, the court held that, while it would be flawed to argue that Mrs Ange should not be held to the general conditions on the basis that she had not read them before signing the agreement, there was substantial evidence to establish that it was ‘more probable than not’ that Mrs Ange was aware of the general conditions as:

- the general conditions were referenced directly above the signature block and by signing the contract she acknowledged that she had read and accepted them;
- not only did Mrs Ange have a copy of the general conditions, but Bonhams had notified both Mrs Ange and her lawyers of the withdrawal fee term at the time the contract was executed; and
- in opposing Mr Ange’s application for an injunction, Mrs Ange argued that she should not be put in a position where she would be liable to have a judgment against her for more than $600,000 (which would occur if she withdrew the paintings from auction).
Upon concluding that the general conditions formed part of the agreement, the court went onto consider a range of issues that may have affected the enforceability of the clause, including whether the injunction frustrated the agreement, whether Bonhams had acted unconscionably and whether the clause was a ‘penalty’.

In agreeing with the trial judge’s finding that the clause did not stipulate that withdrawal of an item from auction constituted a breach, the court stated the following:

>[t]he current state of the law in Australia is that a term of a contract that imposes an obligation on a party to pay money on the happening of a specified event which is not a breach of contract does not constitute a penalty. Primarily this is because it is not the role of the court to relieve a party from a bad bargain.

Significantly, despite Mrs Ange’s submissions to the contrary, the court followed the conclusion of NSW Court of Appeal in *Interstar*23 that the doctrine of penalties only applied to obligations which arose on a breach of contract. The court stated that it was not for an intermediate appellate court to determine whether the doctrine of penalties extends beyond a term providing for the consequences of a breach of contract; such a position would need to be decided by the High Court of Australia.24

The court also upheld the trial judge’s reasoning on the issues of frustration and unconscionability, finding that there could be no frustration of the contract in this context, as the agreement had made express provision for the possibility of a party withdrawing from the agreement and the consequences that were to ensue should this occur. Additionally, the court agreed that Bonhams had not acted unconscionably towards Mrs Ange as she was an astute businesswoman, who had adequate legal advice throughout the consignment process.

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24 The High Court so decided in *Andrews v ANZ* [2012] HCA 30.
Chapter 1: Contract Formation

Hughes v St Barbara Ltd [2011] WASCA 234

- Contract
- Option
- Nature of option: irrevocable offer or conditional contract
- Necessity of separate contract to amend irrevocable offer

The juristic nature of an option remains controversial. It will therefore usually be safest to vary an option by deed, as this may avoid any uncertainty as to the enforceability of the variation if it is not supported by consideration.

This decision of Chief Justice Martin, Justice Pullin and Justice Murphy, on 1 November 2011, dealt with, in the context of an option agreement relating to the purchase of mining tenements by Kingstream Steel Ltd from St Barbara Ltd:

- the implication of a term in a contract that each party must do all things necessary to enable the other party to have the benefit of the contract;
- the juristic nature of an option; and
- the meaning of a ‘unilateral contract’.

The court held, relying on Butt v M’donald (1896) 7 QLJ 68, that the option agreement includes a term implied by law that each party agrees to do all such things that are necessary on their part to enable the other party to have the benefit of the contract (as do all contracts).

The court also discussed the nature of an option in the context of the parties’ variation of the agreement and held that, depending on the proper construction of the agreement, an option could either be:

- a conditional contract, in which case it could only be varied by a contract supported by consideration; or
- an irrevocable offer (which the offeror is obligated to keep open for a specified time period), which could be varied by, in this case, a letter agreement between the parties.

There was some discussion, although no clear ratio decidendi was provided, regarding the nature of the letter agreement purporting to vary the option agreement, and whether it constituted a unilateral contract or a bilateral contract. Justice Pullin was of the view that both the letter agreement and the option agreement itself constituted a unilateral contract, whereas Chief Justice Martin and Justice Murphy were of the view that, as the variation to the parties’ respective rights could have been of benefit or burden to either one of them, sufficient mutual consideration existed and a bilateral contract came into existence.

The facts

St Barbara and Kingstream executed an option deed, containing an offer by St Barbara in the form of an option grant permitting Kingstream to purchase certain mining tenements. That offer was to remain open for 12 months from the date when notice was given of ministerial consent to the transaction. The option deed was subsequently varied by a supplemental deed.

Before the expiry of the option period, St Barbara, in two letters, added extra tenements (of a St Barbara subsidiary) (the additional tenements) to its offer.

About two years after Kingstream’s exercise of the option, St Barbara’s subsidiary withdrew the additional tenements. Kingstream sued for damages for breach of the sale and purchase contract that came into existence on exercise of the option.
The issues on appeal were whether:

- the letter agreement was legally effective to vary the terms of the option agreement; and
- if there was a contract, there was a breach of contract when the St Barbara subsidiary withdrew the mining tenements and how to assess any corresponding loss to Kingstream.

The main controversial discussion in the judgment relates to the question of whether the letter agreement constituted a unilateral or a bilateral contract. Chief Justice Martin and Justice Murphy were of the view that the letter agreement provided both potential benefit to, and obligation on, each party and therefore there was sufficient mutual consideration for a bilateral contract to come into existence, effecting immediate variation to the option agreement.

Justice Pullin was of the view that the letter agreement constituted an amended offer and, accordingly, a unilateral contract. His Honour opined that, if the specified event occurred and the promisee exercised its right under the option, then a subsequent bilateral contract would have arisen, in which case the promisor discharges its obligation under the unilateral contract and accepts new obligations under the bilateral contract.

On this issue, Justice Murphy said further that, if the letter agreement was not a bilateral contract, then it was either an amended offer or a unilateral contract.

As each judge agreed that the letter agreement effected a variation to the terms of the option agreement, there was no need for the court to reach a uniform conclusion on the juristic nature of an option.
Chapter 2: Contractual interpretation

In late 2011, the High Court sent a strong message to lower courts, albeit in the context of a special leave disposition, that evidence of surrounding circumstances was inadmissible for the purpose of interpreting a contract unless the contract was, on its face, ambiguous.

See our Focus: Sending a strong message on contractual interpretation. The decision of the Queensland Court of Appeal in Velvet Glove Holdings was handed down a few days later. Although it did not refer to the High Court’s special leave disposition, the reasoning of the court was consistent with it. The judgment is also a fairly orthodox application of the principle that evidence of subjective intentions or expectations is inadmissible for the purpose of interpreting a contract.

There have, however, been other appellant cases during the past 12 months that illustrate some of the circumstances in which courts will still have regard to surrounding circumstances, even if the relevant clause of the contract is not ambiguous.

In Spiers Earth Works, the WA Court of Appeal had regard to surrounding circumstances in determining that a liquidated damages clause was a penalty.

In CSG, the NSW Court of Appeal considered a clause obliging a party ‘to assign’ contracts to another party. A contract, however, cannot be ‘assigned’: only rights can be assigned. A party wishing to transfer the rights and obligations under a contract must novate that contract (which almost invariably requires the consent of all the parties to the contract). Notwithstanding that...

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12 Velvet Glove Holdings Pty Ltd v Mt Isa Mines Ltd [2011] QCA 312.
13 Spiers Earth Works Pty Ltd v Lance Tec Project Corporation Pty Ltd [No. 2] [2012] WC CA 53.
14 Other recent developments relating to the law of penalties are discussed in the next section.
15 CSG Limited v Fuji Xerox Australia Pty Ltd [2011] NSW CA 385.
the parties separately used the word ‘novate’ in other clauses of the agreement, the NSW Court of Appeal was prepared, having regard to the contract as a whole, to interpret ‘assign’ as meaning ‘novate’ even though there is (arguably) no ambiguity as to the meaning of the word ‘assign’. As to the requirements for a valid novation, these were considered by the High Court in *ALH Group Property Holdings*.16

The decision of the Victorian Court of Appeal in *Ange*17, referred to earlier, is another example of a court having regard to surrounding circumstances where the contract was unambiguous: in this case, for the purpose of determining whether the General Conditions were incorporated into the contract.

The NSW Court of Appeal has, over the past 20 years, repeatedly held that an obligation of good faith will often be implied into contracts. In *Trans Petroleum (Australia)*18, the WA Court of Appeal confirmed that, until the High Court held otherwise, WA courts should follow the law as developed by the NSW Court of Appeal. The WA Court of Appeal further held, however, that, on the facts of the case before it, an unqualified right to terminate a contract on two months’ notice was not subject to any implied obligation of good faith.

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16 *Ange v First East Auction Holdings Pty Ltd* (2011) VSCS 335.
Velvet Glove Holdings Pty Ltd v Mount Isa Mines Ltd [2011] QCA 312

Before attempting to introduce evidence of circumstances surrounding the formation of a contract, practitioners should carefully consider the actual terms of the contract. If the contract, when read as a whole, is clear and capable of only one meaning, evidence of surrounding circumstances will not be admissible.

This decision of the Queensland Court of Appeal, on 4 November 2011, dealt with the admissibility of extrinsic evidence of the circumstances surrounding the formation of a contract.

The Queensland Court of Appeal held that evidence of pre-contractual negotiations was not admissible to prove the meaning of a contract in circumstances where the contract was not ambiguous and the evidence merely went to the subjective intentions or expectations of the parties. The judgment was consistent with, but did not refer to, the High Court’s special leave disposition a few days earlier in Western Export Services.25

The facts

On 15 August 2008, Velvet Glove Holdings Pty Ltd (Velvet Glove) and Mt Isa Mines Ltd (MIM) entered into a contract whereby Velvet Glove would supply MIM with 144 accommodation units and facilities for 12 months in return for a contract price of $5,203,440. There was provision for the contract price to be paid in instalments throughout the life of the contract. The contract gave MIM an absolute discretion to terminate the contract on 10 business days’ notice. The accommodation was to be built by Velvet Glove on its own land.

MIM exercised its termination right on 3 December 2008. The termination clause provided a mechanism for the calculation of the termination payment MIM was required to pay. MIM argued that it was only required to pay a pro rata amount of the contract price that represented the actual time the contract was in force. Velvet Glove argued that the contract was a lump sum contract and it was entitled to be paid the entire contract price that would have been paid had the contract run for 12 months.

Velvet Glove sought to introduce evidence of pre-contractual negotiations. During negotiations, MIM expressed an unwillingness to make an upfront capital payment for units that were to be built on Velvet Glove’s land. Velvet Glove had also expressed its wariness to incur capital expenditure unless it was guaranteed a return. Velvet Glove argued that these negotiations supported its interpretation of the contract as a lump sum contract with provision for periodic payments.

25 Western Export Services Inc v Jireh International Pty Ltd [2011] HCA 45
The judgment

The Queensland Court of Appeal (Justice Philippides with Justices Fraser and White agreeing) held that the contract was not a lump sum contract. Justice Philippides held that the termination payment clause, when read in light of the contract as a whole, did not require MIM to pay the entire contract price.

Justice Philippides then considered whether evidence of the pre-contractual negotiations could be introduced where the terms of the contract were not ambiguous. The trial judge had said that ‘[a]mbiguity is not a necessary precursor to the examination of surrounding circumstances’. In support of this proposition the trial judge cited cases including Lion Nathan Australia Pty Ltd v Coopers Brewery Ltd [2006] FCAFC 144 and Franklins Pty Ltd v Metcash Trading Ltd [2009] NSWCA 407. This caution was repeated more forcefully by the High Court when refusing special leave in Western Export Services v Jireh International [2011] HCA 45.26

Justice Philippides focused on Justice Mason’s statement in Codelfa Construction Pty Ltd v State Rail Authority (NSW) (1982) 49 CLR 337 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. But it is not admissible to contradict the contract where it has a plain meaning.

In Codelfa, Justice Mason also said that evidence of prior negotiations could be used to establish objective background facts that were known to both parties and the subjective matter of the contract but not be used where they are merely reflective of their actual intentions and expectations.

Justice Philippides then quoted English authority, including Investors Compensation Scheme Ltd v West Bromwich Building Society [1998] 1 WLR 896, that suggested that the scope of admissible evidence had expanded since Codelfa. Justice Philippides took heed of the warning expressed by the High Court in Royal Botanic Gardens and Domain Trust v South Sydney City Council (2002) 240 CLR 45 that, until the High Court resolves the conflict between Codelfa and the later English authority, Australian courts should continue to follow Codelfa. Justice Philippides agreed with the trial judge that the evidence of the pre-contractual negotiation was not admissible, as the language used in the contract was not ambiguous or susceptible of more than one meaning.

This case doubted statements made in the NSW Supreme Court and other courts that ambiguity is not required in order to introduce surrounding circumstances evidence. Although Justice Philippides did not expressly disapprove of these statements, her Honour did say (echoing statements made by the High Court in Byrnes v Kendle [2011] HCA 26) that they should be read in light of the High Court’s caution in Royal Botanic Gardens.
Spiers Earthworks Pty Ltd v Landtec Projects Corporation Pty Ltd [No 2] [2012] WASCA 53

- Liquidated damages clause
- A genuine pre-estimate of loss as basis of liquidated damages clause
- Prevention principle

A court will consider all the circumstances that existed when the contract was made in deciding whether a liquidated damages clause is a penalty (and therefore unenforceable). It also suggests that the prevention principle does not apply where the contractor failed to satisfy a condition precedent to its contractual right to an extension of time. This follows the rulings in Turner Corporation Ltd (Receiver & Manager Appointed) v Austotel Pty Ltd (1997) 13 BCL 378 and Peninsula Balmain Pty Ltd v Abigroup Contractors Pty Ltd [2002] NSWCA 211.

This decision of the Court of Appeal of Western Australia, on 13 March 2012, considered liquidated damages and the prevention principle in a case involving the two-stage subdivision of a parcel of land.

The facts

The respondent developer, Landtec Projects Corporation Pty Ltd, had conditional approval to subdivide a parcel of land in two stages. Spiers Earthworks Pty Ltd was engaged to carry out earth works, drainage and road works, including the construction and sealing of a section of a laneway during the first stage (the first contract). Conditional approval from the local shire included condition 25, which required the laneway to be constructed in its entirety before permission to subdivide the lots would be granted. Clause 35.2 of the general conditions also required Spiers to execute the work within 10 weeks, which was the date for practical completion.

Spiers was late in completing the work required in stage one, and Landtec attempted to claim liquidated damages of $13,486 per week. The calculation of the liquidated damages was based on the loss stemming from the late receipt of proceeds of sale from the development. Spiers argued that the liquidated damages clause imposed a penalty because clearance for the further development to take place would not be granted until the road had been sealed. At the time the parties entered into the contract, Landtec had not made arrangements for the construction of the remainder of the laneway, which was required under condition 25.
The judgment

The majority determined that Landtec had no intention of achieving compliance with condition 25 before the completion of the stage 1 works. Consequently, the liquidated damages were struck down as a penalty and not able to be claimed.

Their Honours stated that the prevention principle clearly applies to delays caused by the principal, and also applies to other acts or omissions of the principal within the scope of the contract that prevents practical completion within the fixed period. The principle has no application to delays that are not caused by the default of the principal.

Spiers was unsuccessful in its attempts to rely on the prevention principle because clause 35.5 of the contract provided that: ‘any failure by the Superintendent to grant an extension of time does not cause the date for practical completion to be set at large or prejudice the contractor’s right to damages.’

Therefore, the majority did not need to determine whether contractual parties are free to exclude the prevention principle. Otherwise, Spiers would have been entitled to damages against Landtec for its breach of contract including any damages (liquidated or otherwise) it suffered as a result of Landtec-caused delays in practical completion. The majority also queried whether anyone other than the superintendent can grant an extension of time under clause 35.5 of the general conditions, as had occurred in the Peninsula Balmain case.
CSG Limited v Fuji Xerox Australia Pty Ltd [2011] NSWCA 335

The decision is an example of a court construing a clause in the context of the contract as a whole, even where it meant departing from the ordinary or strict legal meaning of the words used in the clause.

This decision of the Court of Appeal of New South Wales, on 4 November 2011, concerned whether two commercial contracts were validly terminated and the proper construction of clauses of the contracts.

The court held that the contracts were validly terminated. In making consequential declarations, the court considered the proper construction of clauses of the contracts. This involved construing the clauses in the context of the contracts as a whole to give effect to the obvious intention of the clauses.

The facts

Fuji Xerox Australia Pty Ltd (FXA) appointed CSG Limited (CSG) as a dealer in its products under two dealership agreements (the contracts). FXA terminated the contacts, claiming that CSG had breached essential terms of the contracts relating to:

- target quotas (the target quota terms), by not meeting the quotas for the 2009 calendar year, and
- potential conflicts of interest (the potential conflict of interest terms), by entering into agreements with Canon Australia Ltd.

FXA sought declarations that:

- it had validly terminated the contracts; and
- CSG was contractually obliged to cooperate with FXA to procure the novation to FXA of existing maintenance contracts with customers.

CSG sought leave to appeal.
CHAPTER 2: CONTRACTUAL INTERPRETATION

The judgment

Justice Sackville (Chief Justice Bathurst and Justice Campbell agreeing) granted leave to appeal and held that:

• CSG had breached the target quota terms and the potential conflict of interest terms;
• FXA was entitled to terminate the contracts for breach of essential terms of the contracts; and
• CSG was required to perform all acts within its power necessary to procure the novation of the maintenance contracts to FXA.

The decision is significant in respect of the latter point. The relevant clause required the dealer ‘to assign’ contracts or contractual rights to FXA, but did not refer to an obligation ‘to novate’.

However, the court held that the ‘obvious intention’ of the clause required that the word ‘assign’ include a novation of obligations under the contracts, even though other clauses in the contract appeared to recognise the distinction between ‘novation’ and ‘assignment’.

This indicates that the court may have regard to the contract as a whole in construing a clause and interpret a word as having a different meaning to its ordinary or legal meaning where the obvious intention of the clause requires the word to have or include that other meaning.
Novation

This case clarifies the test to be applied in determining whether there has been a novation of a contract.

This decision of the High Court, on 8 March 2012, considered whether an agreement effected a novation. The High Court decided that there was a novation and, since the agreement was for the sale and transfer of dutiable property, and was later cancelled, no duty was payable by reason of section 50 of the Duties Act 1997 (NSW).

The facts

The Duties Act, s50(1), relevantly provided:

An agreement for the sale or transfer of dutiable property that is cancelled is not liable to duty under this Chapter...

Oakland Glen Pty Limited (Oakland), Permanent Trustee Company Limited (as trustee of the ALE Direct Property Trust) (the trust) and ALH Group Property Holdings Pty Ltd (ALH) entered into a deed of termination.

The deed of termination cancelled a deed of consent and assignment (the deed of consent) under which the trust agreed to assign its rights under a contract for the sale of freehold land between Oakland and the trust (the 2003 contract) to ALH.

ALH paid ad valorem duty on the deed of consent. ALH claimed that no duty was payable on the deed of consent and applied for a refund. The Chief Commissioner of State Revenue for New South Wales (the Chief Commissioner) ruled that s50(1) did not apply and declined to refund the duty paid by ALH.

The Chief Commissioner disallowed the objection. ALH appealed to the Supreme Court. Justice Gzell found the deed of consent effected a novation and set aside the Chief Commissioner’s assessment. The Chief Commissioner appealed.

The Court of Appeal found the deed of consent did not effect a novation and allowed the appeal. ALH appealed to the High Court.

The judgment

The High Court held that the deed of consent effected a novation and that s50(1) was engaged. The Chief Commissioner was therefore liable to refund the duty paid by ALH.

The decision turned on whether the deed of consent effected a novation of, or merely assigned the rights under, the 2003 contract.

In reaching its decision, the High Court considered the principles relating to the novation of contracts and clarified that the relevant enquiry in determining whether there has been a novation is:

... whether it has been agreed that a new contract is to be substituted for the old and the obligations of the parties under the old agreement are to be discharged.
A court will not imply a duty of good faith into a contractual power to terminate an agreement if that would be inconsistent with the terms of the contract. This case proceeds on the basis (though declines to decide) that the line of authority in NSW regarding the implication of a duty of good faith in contract represents the law in Australia.

The decision highlights the importance of the words of the relevant clause, considered in the context of the agreement as a whole, when determining whether the court will imply an obligation of good faith. It also serves as a reminder that it is important when drafting or entering a contract to consider whether the terms may leave it open for a court to imply a duty of good faith into the exercise of a contractual power such as a power to terminate.

This decision of the Court of Appeal of Western Australia (Justices Pullin, Buss and Murphy), on 23 August 2012, dealt with the construction of a contractual power to terminate a licence agreement and, among other things, whether there was any obligation to exercise the power to terminate in good faith. This summary focuses on the aspect of the decision dealing with the implication of a duty of good faith.

Justice Pullin and Justice Murphy agreed with the judgment of Justice Buss, in which his Honour held that there was no obligation to exercise the termination power in good faith.

The facts

The appellant and the respondent entered into a license agreement, under which the respondent granted the appellant a non-exclusive license to operate a convenience store business using the respondent’s system (the Peak system) and to sell the respondent’s petroleum products. The respondent was subsequently acquired by another party, Gull Trading Pty Ltd (Gull), which operated a number of convenience/petrol stores. A number of Gull’s stores operated under the Peak system but a majority were operated using its own system (the Gull system). Gull subsequently decided to phase out use of the Peak system and use the Gull system in all of its stores.

Gull entered into negotiations with the appellant to replace the previous agreement between the appellant and the respondent with a standard form Gull franchising agreement that would require the appellant to use the Gull system. Later in the negotiations, when fee arrangements were discussed, it became clear that the new agreement would require the appellant to pay a greater ongoing fee to Gull, which would not be capped in the way that had been provided for in the previous agreement. At this point, the appellant refused to execute the new agreement.

As a result, Gull issued a written notice terminating the agreement. The previous agreement between the appellant and the respondent contained two clauses providing a power to terminate. Clause 3 provided to both parties a general right to terminate as follows:

The Term, unless terminated as provided for in clause 14 [sic: clause 13] of this Deed, shall continue from month to month with either party entitled to terminate this Deed upon two (2) months written notice to the other.
Clause 13 conferred a right on the respondent to terminate, in certain specified circumstances, including for certain breaches by the appellant.

The appellant sought a declaration from the Supreme Court of Western Australia that the termination notice was invalid, and also sought an injunction prohibiting Gull from acting on the termination notice. At first instance, Justice Allanson declared that the termination notice was valid, that there was no obligation to exercise the termination power in good faith and, in any event, the power was exercised in good faith. The appellant appealed.

The grounds of appeal relied on by the appellant included an argument that Gull was required under clause 3 to exercise the power to terminate in good faith.

The judgment

Justice Buss dismissed the appeal. His Honour held that there was no obligation to exercise the termination power in clause 3 in good faith. His Honour proceeded on the basis that the line of authority in NSW regarding the implication of a duty of good faith in contracts represents the law in Australia, but expressly declined to decide the point. His Honour cited a number of NSW Court of Appeal decisions (including Vodafone Pacific Ltd v Mobile Innovations Ltd [2004] NSWCA 15) and highlighted that a duty of good faith should not be implied where to do so would be inconsistent with the terms of the contract. It is on this basis that His Honour held that no such duty should be implied into the termination power under clause 3.

In finding that the implication of a duty of good faith would be inconsistent with the terms of the contract, His Honour had significant regard to the fact that the termination power in clause 3, when read with the other provisions of the contract, was ‘relevantly unconfined’. His Honour explained (at paragraph [140]):

The language of cl 3, read with cl 2.1 and the other provisions of the agreement as a whole, is relevantly unconfined. Clause 3 confers on each of the appellant and the respondent a right to terminate the agreement and the non-exclusive license without cause. That is, either party is entitled, at any time, to terminate for any reason, notwithstanding that the other party is not in breach, upon two months’ written notice.

His Honour contrasted clause 3 with the power to terminate in clause 13, which was more confined and provided only the respondent with a right to terminate in specified circumstances.

His Honour’s analysis shows that the question of whether a duty of good faith will be implied into the exercise of a contractual power to terminate involves construing the relevant clause in the context of the whole contract, and that the duty may not be implied where it will be inconsistent with the clause or the contract as a whole.
This decision makes clear that, when obtaining undertakings to be bound by the outcome of test cases, parties should take care to reach clear agreement as to the common questions in respect of which those undertakings will apply.

This decision also confirms the status of the postal acceptance rule as a principle of convenience, not a rule of general application in determining contractual performance.

The decision of the New South Wales Court of Appeal (Justices Campbell and Barrett and Justice Sackville), on 26 April 2012, concerned the purpose and effect of undertakings given by parties to be bound by the outcome of test cases and the application of the ‘postal acceptance rule’ in determining contractual performance.

Their Honours held that:

- in relation to test cases, parties that give undertakings to be bound by the outcome of a test case will only be bound by those findings that turn on common questions; and
- in relation to contractual performance, the postal acceptance rule is not a general rule applicable in determining whether a contract debt has been satisfied.

The facts

The first respondent, Agricultural and Rural Finance Pty Ltd (ARF), provided finance to certain investors in a managed investment scheme (the borrowers). Under the financing agreements with ARF, the borrowers were each required to make repayments to ARF of principal and interest on specified dates.

In addition to the financing agreement with ARF, each borrower also entered into an agreement with the second respondent, Oceania Agricultural Limited (OAL). Under this agreement, OAL agreed to indemnify each borrower against his or her repayment liability to ARF in the event of the scheme being terminated, provided that the borrower had previously made repayments to ARF ‘punctually’.

The scheme was terminated in 2003, five years after it commenced. ARF pursued the borrowers for repayment of the loan amounts under the terms of its financing agreements. ARF commenced proceedings in the NSW Supreme Court against more than 200 borrowers. These borrowers sought to rely on the indemnity in their respective agreements with OAL.

The Supreme Court granted leave for the claim against one borrower, Bruce Gardiner, to proceed as a test case (the Gardiner test case). Borrowers who were engaged in the Supreme Court proceedings gave undertakings ‘to be bound on common questions by the findings of the Gardiner Test Case’. Although they were directed to agree what would be the ‘common questions’, the parties failed to do so and, at the time the undertakings were given, only Mr Gardiner had filed a defence. Given the centrality of the indemnity issue to all the borrowers’ cases, the enforceability of the OAL indemnity was a critical issue in the Gardiner test case.
The Gardiner test case was decided in ARF’s favour at first instance, which decision was successfully appealed to the Court of Appeal. On a further appeal, the High Court found that Mr Gardiner could not take the benefit of the OAL indemnity because he had not made his previous repayments to ARF ‘punctually’.

Following the High Court decision in the Gardiner test case, the Supreme Court entered judgment in favour of all borrowers who ARF did not dispute had made repayments punctually. A number of borrowers, who ARF claimed had failed to make payments punctually, (the late borrowers) resisted ARF’s attempt to have the Supreme Court enter judgment against them. ARF claimed that the late borrowers’ undertakings required them to be bound by the outcome of the Gardiner test case in the High Court. The late borrowers advanced defences that had not been pleaded in the Gardiner test case, in particular, a defence that a repayment was not ‘late’ if a cheque for the value of that repayment was posted to ARF by the date the repayment was due (the postal rule defence).

The application for judgment against the late borrowers was heard at first instance by Justice Einstein, who struck out the late borrowers’ ‘new’ defences on the ground that they ‘went behind’ the undertakings that the late borrowers had given. Justice Einstein ultimately decided the substantive issues against the late borrowers. Justice Einstein’s decision was the subject of this appeal to the Court of Appeal.

The judgment

On whether the late borrowers were permitted to advance defences not argued in the Gardiner test case, Justice Campbell (with whom Justices Barrett and Sackville agreed) found that:

• in the absence of agreement by the parties at the time the undertakings were given as to what would be a ‘common question’, the late borrowers were only bound in respect of those questions that ultimately were ‘common’ between their respective cases and the Gardiner test case;
• accordingly, the late borrowers were entitled to raise defences that had not been argued in the Gardiner test case; and
• that the postal rule defence did not, per se, relate to a ‘common question’ because it concerned the method of repayment, not the underlying question of the effect of repayments being late.

On the postal rule defence, Justice Campbell found that:

• the postal acceptance rule in the law of contract is a principle of convenience;
• even though the parties to a contract might agree that some matters may be transacted by post, such an agreement does not necessarily give all postal transactions between the parties the same legal effect; and
• that payment by cheque is a conditional payment and, in the absence of a prior agreement by the creditor and the debtor to the contrary, posting a cheque will not itself constitute payment of a debt.
Penalties and illegality

In the *Bank Fees Class Action*[^19] the High Court held that the rule against penalties was not limited to breaches of contract. Where, however, the parties are in a contractual relationship, it will be comparatively rare for the doctrine of penalties to apply if there has not been a breach of contract.

Another common, controversial issue is the consequence that flows from a party entering into an illegal contract. For example, in what circumstances can a party recover money paid (or lent) under an illegal contract? These issues were considered by the High Court in *Equuscopri*[^20]. The High Court held that, on the facts of that case, amounts lent under the loan agreements were not recoverable. Interestingly, the High Court also held that, if there had been a right to recover money paid under an illegal contract, than that right was capable of being assigned (although, on the facts of this case, such rights (had they existed) had not been assigned).

Andrews v Australia and New Zealand Banking Group Ltd [2012] HCA 30

Penalty doctrine
Whether penalty doctrine limited to circumstances where there is breach of contract

The High Court has clarified that the penalty doctrine can apply even if there has not been a breach of contract. It can therefore apply if the parties are not in a contractual relationship. However, where the parties are in a contractual relationship, the penalty doctrine will have a limited application if there has not in fact been a breach of contract.

This decision of the High Court of Australia, on 6 September 2012, considered the scope of the penalty doctrine. The court held that the penalty doctrine is an equitable doctrine that is not limited to obligations that arise upon a breach of contract.27

The facts

A representative action was brought in the Federal Court by customers of Australia and New Zealand Banking Group Limited (ANZ) which, among other things, sought a declaration that certain provisions in their customer contracts were void and unenforceable as penalties. The Federal Court found that certain fees were not penalties because they were not payable upon a breach of contract.

The customers subsequently applied for leave to appeal to the Full Court of the Federal Court. Grounds one to four of their notice of 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’ (the penalty grounds). 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 removal application was granted.

The judgment

The High Court held that the penalty doctrine was an equitable doctrine and was therefore not limited to breaches of contract. In particular, the High Court emphasised the application of the doctrine to the non-satisfaction of conditions in bonds. Although the High Court’s decision was in some respects not very surprising – not least because the equitable doctrine is many centuries older than the law of contract – it did depart from some recent authorities, including the decision of the New South Wales Court of Appeal in Interstar Wholesale Finance Pty Ltd v Integral Home Loans Pty Ltd28, which the primary judge had followed in finding that the penalty doctrine did not apply.

In describing the general application of the penalty doctrine, the High Court stated that:

In general terms, a stipulation prima facie imposes a penalty on a party (‘the first 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 upon the first party an additional detriment, the penalty, to the benefit of the second party. In that sense, the collateral or accessory stipulation is 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. The first party is relieved to that degree from liability to satisfy the collateral stipulation.
Importantly, the court confirmed the distinction between a stipulation attracting the penalty doctrine with one giving rise consensually to additional rights. The court stated:

In Metro-Goldwyn-Mayer, the contract for the hiring of films to exhibitors for public showing conferred the right to one screening only. The exhibitor was obliged to pay for each additional screening a sum equivalent to four times the original fee. The questions of construction of the contract were resolved by Jacobs JA and Holmes JA in such a fashion that the penalty doctrine had no application. Jacobs JA concluded:

There is no right in the exhibitor to use the film otherwise than on an authorized occasion. If he does so then he must be taken to have exercised an option so as to do under the agreement, if the agreement so provides. The agreement provides that he may exercise such an option in one event only, namely, that he pay a hiring fee of four times the usual hiring fee.

Although this distinction is highly relevant to these proceedings, the court emphasised that the application of the penalty doctrine (once the court had clarified that it was not limited to breaches of contract) was a matter to be determined by the trial judge.

**Implications of judgment**

Notwithstanding the publicity surrounding this decision, its practical implications for parties to commercial contracts may be quite limited. The High Court held that the penalties doctrine may apply to an obligation (usually, but not necessarily, an obligation to pay money) if:

- there is a failure of a ‘stipulation’ (this can be a contractual obligation, but may also be, for example, a stipulation in a bond);
- the obligation, which is alleged to be a penalty, is ‘collateral’ to that stipulation, in that it imposes an additional detriment on a party by reason of the failure of the stipulation (this is sometimes described as being an obligation ‘in terrorem’ of the satisfaction of the primary stipulation);
- compensation is payable as a result of the failure of that stipulation (without taking into account any compensation payable by reason of the impugned obligation); and
- the obligation cannot be characterised as the provision of consideration for additional rights.

Where the parties are in a contractual relationship, it will be unusual (but not impossible) for all of these requirements to be satisfied other than by a breach of the contract.
Money paid under an unenforceable contract may be recovered by way of an action for money had and received where the restitutionary claim is not inconsistent with statute, and such claims are assignable where the assignee has a genuine and commercial interest in the claims. Care needs to be taken in drafting assignment clauses if it is intended that restitutionary claims be assigned.

This decision of the High Court, on 8 March 2012, dealt with the restitution of money paid under loan agreements that were found to be unenforceable for illegality, and the assignment of restitutionary rights.

The facts

Rural Finance Pty Ltd assigned loan agreements with investors in connection with tax-driven investment schemes in a blueberry farming enterprise to Equuscorp Pty Ltd. Equuscorp sought to recover the monies due and owing under the loan agreements.

Equuscorp commenced proceedings in the Supreme Court of Victoria for damages for breach of contract, and, in the alternative, for money had and received.

The primary judge, Justice Byrne, held: that the schemes breached section 170 of the Companies Code (the Code) because no prospectus had been registered in respect to a prescribed interest under the schemes contrary to s170(1) of the Code; the loan agreements were an essential part of the scheme and were therefore illegal and unenforceable against the investors; and that certain of the contract claims were time barred. In respect of Equuscorp's alternative claim, his Honour held that, where restitutionary relief was available to Rural, the right to claim such relief had been assigned.

The Victorian Court of Appeal, allowing the investors' appeal, held that the right to claim for restitution was not available to Rural; therefore, the right was not available to Equuscorp and, in any event, the right had not been assigned to Equuscorp.

Equuscorp appealed.
The judgment

The High Court (Chief Justice French and Justices Crennan, Kiefel; Gummow and Bell agreeing in separate reasons; Justice Heydon dissenting), dismissing the appeal, held:

1. Rural did not have a right to claim for money had and received.
   The policy of Part IV Division 6 of the Code, coherence of the law and the avoidance of stultification of the statutory purpose required that Rural be denied a right to claim for money had and received. The loan agreements were unenforceable as being made in the furtherance of an illegal purpose, under s170 of the Code. It was inconsistent with the scheme and purpose of the statute and unjust to permit Rural to be placed in the same position as if Part IV Division 6 had not enacted, had been complied and the loan agreements were effective. Rural was not an arm’s length financier but was closely related to the group of companies involved in the promotion of the schemes and the loan agreements were an integral part of those schemes.

2. The restitutionary rights (had they existed) were assignable.
   The assignment was not open to objection on the ground that it was an assignment of bare rights of action. Equuscop, as assignee, had a genuine and commercial interest in the suit. The restitutionary rights were linked to the performance of the agreement and were assigned, along with the contractual rights.

3. The restitutionary rights (had they existed) were not assigned to Equuscop.
   Three judges of the High Court (Chief Justice French and Justices Crennan and Kiefel – regarded as a majority of the six judges who heard the matter, because of the inclusion of Chief Justice French) held that Rural’s rights to claim for money had and received, had they existed, would not have been transferred to Equuscop because the assignment was limited to contractual rights (and therefore did not extend to non-contractual restitutionary rights). Justices Gummow, Bell and Heydon took a wider view of the relevant clause and held that the assignment would have extended to restitutionary rights. The differing views on this issue reflect the importance in taking care, when drafting assignment clauses, to specify whether restitutionary rights are being assigned.
Inducing breach of contract

A person may be liable in tort for inducing or procuring conduct that they know will be a breach of contract. An issue that sometimes arises is: what constitutes ‘knowledge’ that conduct will breach a contract? In LED Technologies Pty Ltd v Road Vision Pty Ltd [2012] FCAC 3, the Full Court of the Federal Court held that a person has ‘knowledge’ of a breach if they are ‘recklessly indifferent’ as to whether the conduct would give rise to a breach of contract. However, on the facts of that case, the defendant was not recklessly indifferent, so the claim failed.
LED Technologies Pty Ltd v Roadvision Pty Ltd & Anor [2012] FCAFC 3

Tort of inducement of breach of contract

Reckless indifference or wilful blindness sufficient to establish mental element

This decision establishes that a third party may be held liable for the tort of inducing or procuring a breach of contract, even in circumstances where it does not have actual knowledge of the breach, if it is wilfully blind or recklessly indifferent to whether a breach would occur (although this may be a difficult threshold to meet).

This decision of Justices Mansfield, Besanko and Flick in the Full Federal Court, on 10 February 2012, dealt with a claim of damages for the tort of inducing or procuring breach of contract.

Their Honours held that 'reckless indifference' was a category of knowledge sufficient to establish the mental element of the tort; however, on the facts, the claim was not made out.

The facts

The appellant, LED Technologies Pty Ltd, entered into a contract with Valens Co Ltd under which Valens agreed to supply automotive lamps, based on moulds owned by LED. It was a term of the contract that Valens would not sell or manufacture for sale in Australia or New Zealand the automotive lamps created from the moulds. In breach of this term, Valens manufactured and distributed lamps using LED’s moulds to the respondents, Roadvision Pty Ltd and Baxters Pty Ltd, competitors of LED.

LED brought an action against the respondents for damages, claiming that the respondents had induced Valens to breach its contract with LED. LED also claimed that the respondents had infringed two registered designs owned by it.

One of the key questions before the court involved whether the requisite mental element of the tort was made out. Salient considerations included the following:

- LED’s solicitors had sent correspondence to Valens asserting that Valens could not sell lamps made from LED’s moulds in Australia, and there was evidence that the principals of the respondents became aware of this correspondence but did not make further inquiries;
- the trial judge, at first instance, found that, despite the respondents’ knowledge of the contractual term, the mental element of the tort was not made out, as the evidence did not establish that the principals knew that the lamps distributed to them by Valens had been manufactured using LED’s moulds and had thus breached the contractual term; and
- relevant to this decision were factual findings that the decision to use LED’s moulds was not procured by the respondents but was Valens’ decision, and that the respondents were entitled to assume that an upfront payment paid by them to Valens would be used to manufacture new moulds.
The judgment

Justice Besanko (with whom Justices Mansfield and Flick agreed) undertook an extensive examination of Australian and English authorities dealing with the mental element of the tort of inducing or procuring a breach of contract. In particular, the court considered the question of whether ‘reckless indifference’ was sufficient to establish the mental element of the tort.

The court held that a category of ‘reckless indifference’ did exist, clarifying the test for this standard of knowledge at [54] as follows:

‘[R]eckless indifference is something quite close to wilful blindness. It will be negated by an honest belief, even one exhibiting a high degree of credulity. It will be established only if the facts show affirmatively that the alleged tortfeasor, faced with knowledge of at least a substantial prospect of a breach, proceeded not caring whether or not a breach would occur.’

On the facts, the court held that, while it could well be said that the respondents did not make reasonable enquiries about whether Valens were using LED’s moulds to manufacture lights for the respondents, their knowledge did not rise to the level of wilful blindness or reckless indifference, as they had not made a conscious decision not to inquire into the existence of a fact in case they ‘discovered a disagreeable truth’. Accordingly, the court found that the trial judge was correct to reject LED’s claim based on the tort of inducing or procuring a breach of contract.
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