3

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'Surrounding circumstances' in contractual interpretation: where are we now?

Assessment for damages for breach of contract

PPSA models: easy as ABCD?

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Contents

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References and Citations. Cases: The full citation of a case should always be used when a case is first mentioned, eg, *Peden v Little* (1915) 20 CLR 555 or *Tolhurst v Associated Portland Cement Manufacturers* (1900) Ltd [1903] AC414. Note that full points should not be used. The citation should be repeated when subsequently referred to, unless it is repeated in the immediately following footnote in which case 'Ibid' or 'Id at xx' should be used. Books: Initial references to books should be as follows: J W Carter, Elisabeth Peden and G J Tolhurst, *Contract Law in Australia,* 5th ed, LexisNexis, Sydney, 2007, p2. Subsequent references should appear as 'Carter, Peden and Tolhurst, above, n2, p3' unless it is repeated in the immediately following footnote in which case 'Ibid' or 'id, pxx' should be used. Chapters within books should be cited as follows: P Birks, 'Mixtures' in *Interests in Goods*, 2nd ed, N Palmer and E McEndrick (eds), Lloyds of London Press, London, 1998. Journal articles should be cited as follows: B Coote, 'Consideration and Benefit in Fact and in Law' (1990) 3 JCL 23. Subsequent references should be presented as 'Coote, above, n5 at 26' unless it is repeated in the immediately following footnote in which case 'Ibid' or 'Id at xx' should be used. Legislation references to statutes should be as follows: Sale of Goods Act 1923 (NSW).

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President's message

Dear Members,

I feel sure that you're going to find this issue of CLQ full of interesting information about some of the thornier topics of commercial law.

John Eldridge's recent seminar on '"Surrounding circumstances" in contractual interpretation: where are we now?' was enjoyed by all who attended. We also received a lot of requests for the paper from those who couldn't make it on the day. We are delighted to be able to bring it to you in this issue. Here John offers an assessment of the present state of the law and a view as to its likely future development.

We also bring you the final part of Jeffrey Goldberger's comprehensive review of contract law. In this article he's covering 'Assessment of damages for breach of contract'.

Professor Sheelagh McCracken, Diccon Loxton and Andrew Boxall's in-depth, compelling and slightly controversial series on the PPSA also draws to a close this issue with 'PPSA models: As easy as ABCD?' The three-part series was prompted by the Final Report on the Review of the Personal Property Securities Act 2009 known as the Whittaker Report. They deserve congratulation on the amount of effort they have put into bringing clarity to this difficult subject.

As the end of the year draws near, the CLA's thoughts inevitably turn towards membership.

Newly introduced this year is the possibility of two-year memberships for both renewing and joining members of the CLA at a discounted rate. Spicers Retreat have once again offered a mid-week, two-night stay for two to the lucky person who wins our membership draw. This time it's at their new Hunter Valley Spicers Guesthouse that only opened on 1 November (some of you may remember it as Peppers).

I'd also suggest you take a look at our Commuter CLE podcasts and videos. We've recently added a selection of new possibilities including this year's June Judges series.

I look forward to seeing you at a seminar soon.

Norman Donato

Do you have a paper you'd like to publish?

Send submissions to:

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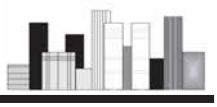

'Surrounding circumstances' in contractual interpretation: where are we now?

John Eldridge*

For several decades, the High Court's pronouncements on the subject of contractual interpretation have generated confusion in intermediate appellate courts and caused considerable academic debate. The key difficulty relates to the question of when recourse may be had to evidence of 'surrounding circumstances' as an aid to construction. In particular, a controversy has emerged in recent years as to whether it is necessary to point to textual 'ambiguity' as a precondition for the use of such evidence as an aid to construction. Though this question is fundamental and of some considerable importance, the task of answering it is far from straightforward. The object of this short article is to explain the nature of the difficulty in respect of this question, and to consider a number of recent developments both in the High Court and in intermediate appellate courts. In doing so, it is sought to offer an assessment of the present state of the law and a view as to its likely future development.

I. Introduction

Given the regularity with which disputes as to the proper construction of contracts present themselves in legal practice, it might well be thought that the basic principles in this sphere should be well-settled.[1] Though it may be accepted that academic debate in respect of construction will inevitably be characterised by disagreement,[2] and that some technicality might necessarily attend the rules which apply to the construction of special categories of contractual term,[3] it should nonetheless be possible to state simply and with some confidence the core principles of contractual interpretation.[4]

This is far from true in Australian law today. For several decades, the High Court's pronouncements on this subject have generated confusion in intermediate appellate courts and attracted astringent academic commentary.[5] The key difficulty relates to the question of when recourse may be had to evidence of 'surrounding circumstances' as an aid to construction. In particular, a controversy has emerged in recent years as to whether it is necessary to point to 'ambiguity' as a precondition for the use of such evidence as an aid to construction. Though this question is fundamental and of some considerable importance, the task of answering it is far from straightforward.

The object of this short article is to explain the nature of the difficulty in respect of this question, and to consider a number of recent developments both in the High Court and in intermediate appellate courts. In doing so, it is sought to offer an assessment of the present state of the law and a view as to its likely future development.

Before taking up this task, it is important to note that there are a number of matters which, while undoubtedly of great importance and interest, are not dealt with here. First, this article does not seek to grapple in detail with the question of what can properly be said to form part of the 'surrounding circumstances' admissible as an aid to construction. It is often necessary, for instance, to ask whether particular evidence of which direct use cannot be made can nonetheless be used indirectly to prove objective background facts known to both the parties to a contract.[6] Though the questions which arise in connection with this point are of great practical significance, they can be put to one side for present purposes.

Second, this article engages only obliquely with the many normative questions which arise in this setting. In particular, this article does not seek to enter the debate as to the limits which ought to be placed upon the evidence to which courts may have recourse when construing contracts. Though this debate is of considerable interest and of equally considerable practical importance, and must be engaged with in passing in order to offer an adequate account of the likely development of the law, it too can largely be put to one side at present.[7]

II. 'Surrounding circumstances' in contractual interpretation: an overview of the controversy

In explaining the controversy in this area, it is best to proceed by giving a roughly chronological account of the key developments. Before turning to the Australian position, however, it is necessary to give some brief consideration to the approach taken to contractual interpretation in English law. Though it would be

quite misleading to suggest that the English position is wholly settled,[8] it remains the case that the interpretation of contracts in English courts is governed by reference to the following principles, first enunciated by Lord Hoffmann in *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896 (hereafter 'the ICS principles'):

'(1) Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.

'(2) The background was famously referred to by Lord Wilberforce as the "matrix of fact", but this phrase is, if anything, an understated description of what the background may include. Subject to the requirement that it should have been reasonably available to the parties and to the exception to be mentioned next, it includes absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man.

'(3) The law excludes from the admissible background the previous negotiations of the parties and their declarations of subjective intent. They are admissible only in an action for rectification. The law makes this distinction for reasons of practical policy and, in this respect only, legal interpretation differs from the way we would interpret utterances in ordinary life. The boundaries of this exception are in some respects unclear. But this is not the occasion on which to explore them.

'(4) The meaning which a document (or any other utterance) would convey to a reasonable man is not the same thing as the meaning of its words. The meaning of words is a matter of dictionaries and grammars; the meaning of the document is what the parties using those words against the relevant background would reasonably have been understood to mean. The background may not merely enable the reasonable man to choose between the possible meanings of words which are ambiguous but even (as occasionally happens in ordinary life) to conclude that the parties must, for whatever reason, have used the wrong words or syntax. (see *Mannai Investments Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] 2 WLR 945.

'(5) The "rule" that words should be given their "natural and ordinary meaning" reflects the common sense proposition that we do not easily accept that people have made linguistic mistakes, particularly in formal documents. On the other hand, if one would nevertheless conclude from the background that something must have gone wrong with the language, the law does not require judges to attribute to the parties an intention which they plainly could not have had.'[9]

Most important for present purposes is the fact that, under these principles, a court may have recourse to evidence of relevant 'background' as a matter of course, without it being necessary first to demonstrate 'ambiguity'.[10] Of course, care must be taken not to overstate the significance these principles accord to extrinsic evidence: as principle (5) makes clear, a court will be slow to conclude that the 'background' against which a contract was concluded mandates a construction which is at odds with the language in which it is expressed.[11]

The position in Australia is far more vexed. It is necessary to begin with the authority which has been the source of much of the difficulty. In *Codelfa Construction Pty Ltd v State Rail Authority of NSW* ('*Codelfa*'),[12] Mason J (as his Honour then was) set out the following 'rule' in respect of the admissibility of surrounding circumstances when construing a contract:

'The true rule is that evidence of surrounding circumstances is admissible to assist in the interpretation of the contract if the language is ambiguous or susceptible of more than one meaning. But it is not admissible to contradict the language of the contract when it has a plain meaning.'[13]

At least on one view, this statement can be taken to mean that, when construing a contract, it is necessary to point to textual 'ambiguity' before recourse can be had to evidence of 'surrounding circumstances' as an aid to interpretation.[14] Whatever may be said against such an approach — and it is indeed open to criticism on a number of bases, some of which are discussed below — it might, but for later developments, have come to enjoy a secure place in the Australian law of contract.[15]

Difficulties began to emerge however, when, in a series of decisions over a considerable period, the High Court began to proffer statements of the law which seemed to be at odds with that set out in *Codelfa.* As there already exist a number of detailed surveys of these authorities, it is best simply to draw attention to the nature of the remarks which began to recur in the High Court's decisions.[16] In *Maggbury Pty Ltd Hafele Australia Pty Ltd,* for instance, the majority stated that:

'Interpretation of a written contract involves, as Lord Hoffmann has put it: "the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract".'[17]

The statement of Lord Hoffmann which the High Court has quoted in this passage is no doubt recognisable as the first of the ICS principles set out above. This explicit endorsement of Lord Hoffmann's principles sits uneasily alongside the approach apparently required by *Codelfa.*

In a similar vein, the High Court unanimously stated in *Pacific Carriers Ltd v BNP Paribas*:

'The construction of the letters of indemnity is to be determined by what a reasonable person in the position of Pacific would have understood them to mean. That requires consideration, not only of the text of the documents, but also the surrounding circumstances known to Pacific and BNP, and the purpose and object of the transaction.'[18]

And yet again, in *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd,* the Court stated:

'The meaning of the terms of a contractual document is to be determined by what a reasonable person would have understood them to mean. That, normally, requires consideration not only of the text, but also of the surrounding circumstances known to the parties, and the purpose and object of the transaction.'[19]

Each of these statements appears to amount to an endorsement of the ICS principles by the High Court, at least insofar as the use of 'surrounding circumstances' in construction is concerned. They suggest, put simply, a departure from the approach apparently mandated by *Codelfa,* and the abandonment of any requirement of 'ambiguity' as a precondition to the use of evidence of 'surrounding circumstances' as an aid to construction.

Such conclusions might have been arrived at without difficulty by intermediate appellate courts, were it not for the difficulties posed by the High Court's own statement as to the status of *Codelfa.* In *Royal Botanic Gardens and Domain Trust v South Sydney City Council* ('*Royal Botanic*'), the majority explained:

'[R]eference was made in argument to several decisions of the House of Lords, delivered since *Codelfa* but without reference to it ... It is unnecessary to determine whether their Lordships there took a broader view of the admissible "background" than was taken in *Codelfa* or, if so, whether those views should be preferred to those of this Court. Until that determination is made by this Court, other Australian courts, if they discern any inconsistency with *Codelfa,* should continue to follow *Codelfa*.'[20]

As is no doubt plain, lower courts were placed in an invidious position. Though the decisions in *Pacific Carriers Ltd v BNP Paribas* and *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* were delivered after *Royal Botanic*,[21] the High Court offered no explicit explanation for how they were each to be reconciled. In the wake of these decisions, a number of intermediate appellate courts surveyed the relevant authorities and concluded that it was no longer necessary to point to 'ambiguity' as a precondition to the use of evidence of 'surrounding circumstances'.[22]

Matters were soon to be complicated further, chiefly by the reasons given in the disposition of a special leave application in *Western Export Services Inc v Jireh International Pty Ltd* ('*Jireh*').[23] In the course of those reasons, Gummow, Heydon and Bell JJ stated:

'The primary judge had referred to what he described as "the summary of principles" in *Franklins Pty Ltd v Metcash Trading Ltd.* The applicant in this Court refers to that decision and to *MBF Investments Pty Ltd v Nolan* as authority rejecting the requirement that it is essential to identify ambiguity in the language of the contract before the court may have regard to the surrounding circumstances and object of the transaction. The applicant also refers to statements in England said to be to the same effect, including that by Lord Steyn in *R (Westminster City Council) v National Asylum Support Service.* Acceptance of the applicant's submission, clearly would require reconsideration by this Court of what was said in *Codelfa Construction Pty Ltd v State Rail Authority of NSW* by Mason J, with the concurrence of Stephen J and Wilson J, to be the "true rule" as to the admission of evidence of surrounding circumstances. Until this Court embarks upon that exercise and disapproves or revises what was said in *Codelfa,* intermediate appellate courts are bound to follow that precedent. The same is true of primary judges, notwithstanding what may appear to have been said by intermediate appellate courts. The position of *Codelfa,* as a binding authority, was made clear in the joint reasons of five Justices in *Royal Botanic Gardens and Domain Trust v South Sydney City Council* and it should not have been necessary to reiterate the point here. We do not read anything said in this Court in *Pacific Carriers Ltd v BNP Paribas*; *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd*; *Wilkie v Gordian Runoff Ltd* and *International Air Transport Association v Ansett Australia Holdings Ltd* as operating inconsistently with what was said by Mason J in the passage in *Codelfa* to which we have referred.'[24]

Though these remarks emphasise the necessity of demonstrating 'ambiguity' before having recourse to evidence of 'surrounding circumstances', their utility for lower courts is limited for two reasons. First, as was later observed by the High Court in *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* ('*Wright Prospecting*')[25] the reasons given upon the disposition of a special leave application do not amount to a binding precedent.[26] It is thus unclear how *Jireh* ought to be reconciled with the apparently inconsistent passages quoted above.

Second, the High Court, in the wake of *Jireh*, quickly resumed its practice of setting out general statements of the law respecting contractual interpretation which appear to be at odds with the notion that it is necessary to point to 'ambiguity' before recourse can be had to 'surrounding circumstances'. In *Electricity Generation Corporation v Woodside Energy Ltd*, for instance, the Court stated:

'The meaning of the terms of a commercial contract is to be determined by what a reasonable businessperson would have understood those terms to mean. That approach is not unfamiliar. As reaffirmed, it will require consideration of the language used by the parties, the surrounding circumstances known to them and the commercial purpose or objects to be secured by the contract.'[27]

Similarly, in the very recent decision in *Ecosse Property Holdings Pty Ltd v Gee Dee Nominees Pty Ltd,* the majority explained:

'It is well established that the terms of a commercial contract are to be understood objectively, by what a reasonable businessperson would have understood them to mean, rather than by reference to the subjectively stated intentions of the parties to the contract. In a practical sense, this requires that the reasonable businessperson be placed in the position of the parties. It is from that perspective that the court considers the circumstances surrounding the contract and the commercial purpose and objects to be achieved by it.'[28]

The High Court authorities are, in sum, in a state of disarray.[29] Faced with the unenviable task of negotiating a path

through the conflicting passages set out above, intermediate appellate courts have diverged in their conclusions as to what the law now is. Though it is not necessary here to canvass these divergent views in detail, it is worth noting some of the key differences which have emerged.

In New South Wales, there is now a well-established line of authority which holds that it is not necessary to point to 'ambiguity' before having recourse to evidence of 'surrounding circumstances'.[30] Perhaps the most important authority in this connection is *Mainteck Services Pty Ltd v Stein Heurtey SA* ('*Mainteck*'), in which Leeming JA stated, in the course of a careful consideration of the difficulties discussed above:

'To the extent that what was said in *Jireh* supports a proposition that "ambiguity" can be evaluated without regard to surrounding circumstances and commercial purpose or objects, it is clear that it is inconsistent with what was said in *Woodside* at [35]. The judgment confirms that not only will the language used "require consideration" but so too will the surrounding circumstances and the commercial purpose or objects. Although the High Court in *Woodside* did not expressly identify a divergence of approach, Jireh was notoriously controversial in precisely this respect ... It cannot be that the mandatory words "will require consideration" used by four Justices of the High Court were chosen lightly, or should be "understood as being some incautious or inaccurate use of language": cf *Fejo v Northern Territory* [1998] HCA 58; 195 CLR 96 at [45].'[31]

This conclusion has been endorsed by the Full Court of the Federal Court of Australia.[32] It has also been reiterated on a number of occasions in the courts of New South Wales, often bolstered by reference to further High Court judgments delivered since *Mainteck,* in particular *Victoria v Tatts Group Limited*[33] and *Simic v New South Wales Land and Housing Corporation*.[34] In *WIN Corporation Pty Ltd v Nine Network Australia Pty Ltd,* for instance, Barrett AJA stated:

'[T]he notion that it may first be necessary to consider context when construing a contract is not inconsistent with Mason J's "true rule". On this footing, it does not follow that the task of assessing whether a phrase or expression is ambiguous or susceptible of more than one meaning must be undertaken without regard to evidence of surrounding circumstances. This position corresponds with the approach of the High Court in *Victoria v Tatts Group Ltd* where the relevant contract was construed by reference to its text, context and purpose without any anterior finding of ambiguity as a precondition to a consideration of surrounding circumstances as an aid to discovering or elucidating context and purpose.'[35]

Similarly, in the recent decision in *Cherry v Steele-Park*,[36] Leeming JA (with whom Gleeson and White JJA agreed on this point) reviewed the relevant authorities and concluded that '[t]here is now a deal of authority for the proposition that whether there is in truth a constructional choice available to a written contract cannot be determined without first at least considering evidence of surrounding circumstances'.[37]

Different approaches can be seen elsewhere. In Victoria, the matter was considered recently in *Apple and Pear Australia Ltd v Pink Lady America LLC*.[38] The most extensive treatment of the point is found in the judgment of Tate JA, who, after careful consideration of the reasons in *Wright Prospecting,* was sceptical of the conclusion arrived at in *Mainteck*:

'In my view, it follows from what was said in [*Wright Prospecting*] that it would be wrong to conclude that the High Court has endorsed an approach to the construction of commercial contracts, whereby the surrounding circumstances, including, relevantly, pre-contractual negotiations, can invariably be relied upon to assist construction. This is not to deny that the objective approach to contractual interpretation requires, as confirmed by French CJ, Nettle and Gordon JJ in [*Wright Prospecting*], reference to the "text, context (the entire text of the contract as well as any contract, document or statutory provision referred to in the text of the contract) and purpose" ... [T]here has been controversy, reflected in the judgments of many intermediate appellate courts, about when, and in what manner, surrounding circumstances can be relied upon in the construction of commercial contracts, the questions surrounding the extent to which surrounding circumstances can be relied upon in the construction of commercial contracts raise large issues and their fate remains to be resolved by the High Court on another day. It is not in dispute that this Court must follow the precepts of the High Court. While this Court may, as a matter of judicial comity, extend deference to the observations made by other intermediate appellate courts with respect to their understanding of principles enunciated by the High Court, it is "bound directly" by what the High Court has said and "is not bound indirectly by another court's interpretation of what the High Court said".'[39]

Ferguson and McLeish JJA dealt with the point more briefly, concluding:

'Consistently with the foregoing, at least where the contractual language is ambiguous or susceptible of more than one meaning, evidence of events, circumstances and things external to the contract is permissible. The requirement of ambiguity was stated by Mason J in *Codelfa Construction Pty Ltd v State Rail Authority (NSW),* and this Court is bound to apply that decision unless and until the High Court says otherwise. As Tate JA has explained, that is this Court's primary obligation, and it is not bound to adopt the interpretations of the High Court's reasons propounded by other intermediate appellate judges or courts in preference to its own interpretation of those reasons. In our opinion, it is not necessary in this appeal to address the controversy that exists as to whether or not evidence of matters external to the contract may be called in aid to establish the ambiguity to which Mason J referred.'[40]

The courts of Western Australia have now repeatedly stated that they will continue to subscribe to the requirement of an

'ambiguity gateway' until the High Court expressly indicates that a different approach is to be preferred. In *Technomin Australia Pty Ltd v Xstrata Nickel Australasia Operations Pty Ltd*,[41] for instance, McLure P (with whom Newnes JA agreed) explained:

'After careful consideration of multiple High Court decisions on the subject, a number of intermediate appellate courts in this country came to the view that evidence of surrounding circumstances was always admissible to assist in the construction of a contract, whether or not the contractual language was ambiguous or susceptible of more than one meaning. However, in dismissing the special leave application in *Western Export Services Inc v Jireh International Pty Ltd* [2011] HCA 45; (2011) 282 ALR 604, three members of the High Court (Gummow, Heydon & Bell JJ) said that conclusion was inconsistent with binding authority. ... This court has taken the view that the guidance in *Western Export Services* should be followed until further direction from the High Court ... The controversy has raised its head again. The appellant contends that the "true rule" in *Codelfa* is the law and, as the meaning of the language of the GPR Deed is unambiguously clear, evidence of surrounding circumstances is (subject to limited exceptions) inadmissible for construction purposes. The respondents contend that the recent High Court decision in *Electricity Generation Corporation t/as Verve Energy v Woodside Energy Ltd* [2014] HCA 7 (EGC), has vindicated the pre-*Western Export Services* position adopted by those intermediate appellate courts that had abandoned the gateway requirement that the language of a contract had to be ambiguous or susceptible of more than one meaning before regard could be had to evidence of surrounding circumstances to assist in the construction of a contract. The construction issue was not raised by the *EGC* parties in this court. Gummow and Heydon JJ had retired before the hearing of *EGC* and Bell J did not sit. *Western Export Services* and the response of intermediate appellate courts thereto were not directly addressed by the High Court in *EGC*. However, the respondent points to the approach taken in the majority judgment. There can be no doubt that the majority in *EGC* took into account surrounding circumstances known to both parties in the construction of the gas supply agreement: [35], [48]. However, there is no express consideration by the majority of whether, or finding that, the language of the gas supply agreement was ambiguous or susceptible of more than one meaning. The respondent also drew this court's attention to the reliance by the majority in *EGC* on [14] of the English decision in *Rainy Sky SA v Kookmin Bank* [2011] UKSC 50; [2011] 1 WLR 2900, 2906-2907. That paragraph cites with approval Lord Hoffman's first principle in *Investors Compensation Scheme Ltd v West Bromwich Building Society (No 1)* [1997] UKHL 28; [1998] 1 WLR 896 ... Lord Hoffman's first principle is not consistent with the gateway requirement in Mason J's "true rule" in *Codelfa*. However, the appellant contends that the High Court would not impliedly repudiate the express repudiation in *Western Export Services* of the abandonment of the gateway requirement by some intermediate appellate courts. The aridity of this debate at the intermediate appellate court level is manifest. Until the High Court expressly states its position on the subject, I propose to continue to apply the "true rule" as explained in *Hancock Prospecting* at [9], [74]-[81]. In that case this court concluded that the true rule permits regard to be had to some surrounding circumstances for construction purposes without having to satisfy the gateway requirement [81].'[42]

It is not necessary to belabour the point. It is plain that until the High Court explicitly addresses and resolves the difficulty in this area, intermediate appellate courts will continue to offer divergent views. It is thus worth considering what view the High Court is likely to endorse when the occasion arises for it to decide the matter explicitly.

III. What will the High Court decide?

Offering a firm view as to the High Court's likely conclusion in respect of this question is not entirely straightforward. As was seen above in respect of *Royal Botanic* and *Byrnes v Kendle,* where the Court has adverted explicitly to the controversy in this area, it has expressly declined to offer a view as to its resolution. Even so, it is suggested that there are, on balance, good reasons to favour the view that the High Court will, when the question arises, endorse an approach to construction in which recourse may be had to 'surrounding circumstances' without it first being necessary to point to 'ambiguity'. There are, broadly speaking, two key bases for such a view.

The first is found in the statements of Kiefel and Keane JJ in *Wright Prospecting.* Though their Honours were cautious not to offer any view as to how the controversy ought ultimately to be resolved, their judgment is nonetheless noteworthy for its expression of the view that Mason J's 'true rule' is silent as to how an ambiguity might be identified. As their Honours explained:

'The "ambiguity" which Mason J said may need to be resolved arises when the words are "susceptible of more than one meaning". His Honour did not say how such an ambiguity might be identified. His Honour's reasons in *Codelfa* are directed to how an ambiguity might be resolved. In reasons for the refusal of special leave to appeal given in *Western Export Services Inc v Jireh International Pty Ltd,* reference was made to a requirement that it is essential to identify ambiguity in the language of the contract before the court may have regard to the surrounding circumstances and the object of the transaction. There may be differences of views about whether this requirement arises from what was said in *Codelfa.* This is not the occasion to resolve that question. It should, however, be observed that statements made in the course of reasons for refusing an application for special leave create no precedent and are binding on no one. An application for special leave is merely an application to commence proceedings in the Court. Until the grant of special leave there are no proceedings inter partes before the Court. The question

whether an ambiguity in the meaning of terms in a commercial contract may be identified by reference to matters external to the contract does not arise in this case and the issue identified in Jireh has not been the subject of submissions before this Court. To the extent that there is any possible ambiguity as to the meaning of the words "deriving title through or under", it arises from the terms of cl 24(iii) itself.'[43]

Insofar as this passage leaves the way open to an approach akin to that in *Mainteck* — that is, adopting a reading of *Codelfa* that dispenses with the 'ambiguity gateway' — it offers some clue as to the High Court's likely approach. Of course, whether Mason J's remarks are readily susceptible of such a reading is another question: indeed, Thomas Prince has strongly criticised *Mainteck* on precisely this point.[44]

The second basis for the view proffered here is the general lack of enthusiasm on the part of commentators and courts for the notion of an 'ambiguity gateway'. As has already been noted, it is no object of this paper to enter at length into the normative debate as to what evidence a court ought to consider when construing a contract (or the debate as to the relative importance which ought to be accorded to language and context).[45] Even so, it is important to note that though there are many commentators who contend that the modern law of contractual interpretation has accorded too much weight to extrinsic material at the expense of language,[46] such views are very rarely accompanied by a suggestion that an 'ambiguity gateway', or any similar such rule, is normatively desirable.[47] Indeed, the lack of support for the notion of an 'ambiguity gateway' is well-illustrated by considering the line of recent English cases which has been held up as evidence of a retreat from the importance formerly accorded to extrinsic material.[48] The statements as to the nature of construction in these cases is distinctly at odds with any notion of an 'ambiguity gateway'. As Lord Hodge (with whom Lord Neuberger, Lord Mance, Lord Clarke and Lord Sumption agreed) explained in *Wood v Capita Insurance Services Limited*:

'Interpretation is, as Lord Clarke stated in *Rainy Sky* (para 21), a unitary exercise; where there are rival meanings, the court can give weight to the implications of rival constructions by reaching a view as to which construction is more consistent with business common sense. But, in striking a balance between the indications given by the language and the implications of the competing constructions the court must consider the quality of drafting of the clause ... and it must also be alive to the possibility that one side may have agreed to something which with hindsight did not serve his interest ... Similarly, the court must not lose sight of the possibility that a provision may be a negotiated compromise or that the negotiators were not able to agree more precise terms. This unitary exercise involves an iterative process by which each suggested interpretation is checked against the provisions of the contract and its commercial consequences are investigated ... To my mind once one has read the language in dispute and the relevant parts of the contract that provide its context, it does not matter whether the more detailed analysis commences with the factual background and the implications of rival constructions or a close examination of the relevant language in the contract, so long as the court balances the indications given by each.'[49]

The lack of enthusiasm for the notion of an 'ambiguity' is unsurprising. Even if an approach is sought which seeks to emphasise the primacy of contractual language, the imposition of an 'ambiguity gateway' is an unnecessarily complex and fraught means of achieving such an end. It is far preferable to seek to promote the primacy of language without taking up a test which necessarily involves the answering such questions as what it is for a contractual term to be 'ambiguous'.[50]

For these reasons, then, it is submitted that the High Court is likely, when the occasion presents itself, to endorse an approach to construction in which recourse may be had to 'surrounding circumstances' as an aid to construction without it first being necessary to point to 'ambiguity'.

IV. Conclusion

It is worth, in closing, reflecting upon why the confusion in this area has proven to be so persistent. Of course, in light of the discussion above, the immediate answer to this question may seem obvious: it is the apparent (if not actual) vacillation of the High Court which has led to confusion and divergence in lower courts. To put the point in this way, however, simply masks the important question of why the High Court has opted, in cases such as *Wright Prospecting,* to decline to dispel the uncertainty which has been productive of so much difficulty.

Such a course was, at least in principle, open to the High Court on a number of occasions. The High Court has stated clearly that lower courts are to follow the 'seriously considered dicta' of a majority of the High Court,[51] and it has been seen that lower courts do indeed abide by this injunction.[52] Even if the High Court had offered guidance in this sphere which was wholly obiter, it would almost certainly have been followed by lower courts.

The High Court's reticence is likely a function of it adhering to the principle that a court ought not to determine a question where it is not necessary to do so in resolving the matter before it. As Dyson Heydon has forcefully observed:

'A discursive analysis of the law can be appropriate if it is necessary to decide the matter. An intermediate appellate court may be confronted with a conflict of authorities in different trial courts throughout Australia, and may have to choose. The possibilities are wider still in the High Court. But even in these courts it is wrong to deal with issues which, even though they have been raised, are not issues which it is necessary for the specific outcome of the case to deal with. It is even worse to deal with unnecessary issues which have not been raised. A badge of suspicion must attach to a judgment which, after setting out various issues and arguments, says "Though it is not necessary to decide this point, in deference to the careful submissions of the

parties, the court will deal with it". Courts are not supposed to decide questions which are merely moot, theoretical, abstract or hypothetical. They are not supposed to offer opinions which are merely advisory, having no foreseeable consequences for the particular parties. Their determinations are supposed to be conclusive or final decisions on concrete controversies, not inconclusive and tentative speculations on controversies which have not yet arisen. Excessive and self-indulgent surveys of the law and debates about the background to and future of particular rules contravene these prohibitions, which are based on good sense.'[53]

Few would cavil with the contention that a court should be slow to offer a view on points which are wholly academic or hypothetical. Even so, reasonable views may differ as to the degree of circumspection owed by the High Court when presented with an opportunity to provide guidance on a point which has been productive of confusion and difficulty in lower courts. The proper approach in such cases might be thought to depend upon the importance of the question and the degree to which the Court has had the opportunity to explore the competing arguments.

If considered in this way, it is difficult to find the approach adopted by the Court in this sphere wholly satisfactory. It is profoundly concerning that the law is in a state of such confusion in respect of a matter so fundamental to the law of contract. Indeed, there is considerable evidence that the difficulties in this area are the cause of much vexation for courts at first instance: a recent study of the most frequently-cited judgments in Australian contract law, for instance, found that *Jireh,* notwithstanding its lack of precedential force, is the 75th most cited 'authority' in the Australian law of contract.[54] If the High Court forbears from offering guidance on this point until its hand is forced, there is every reason to believe this confusion and difficulty will continue for some considerable time: after all, in order for it to become necessary to decide this point, the Court will have to be presented with an a matter which turns on the construction of apparently unambiguous language. There are, in short, good reasons to conclude that the High Court ought to abandon its reticence on this point and take the opportunity to offer explicit guidance as to the proper approach.

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1 On the regularity with which questions of construction arise in practice, see: David McLauchlan 'Contract Interpretation: What is it About?' (2009) 31 *Sydney Law Review* 5, 5.

2 In recent years, for instance, the question of whether the implication of terms forms part of the exercise of construction has generated considerable controversy and disagreement. The debate owes its genesis to the advice of the Privy Council in Attorney General of *Belize v Belize Telecom Ltd* [2009] 1 WLR 1988, a decision which has recently been revisited by the UK Supreme Court in *Marks and Spencer plc v BNP Paribas Securities Services Trust Company (Jersey) Limited* [2015] 3 WLR 1843. See, on this point: Wayne Courtney and J W Carter, 'Implied Terms: What is the Role of Construction?' (2014) 31 *Journal of Contract Law* 151; Joanna McCunn, '*Belize* it or Not: Implied Contract Terms in *Marks and Spencer v BNP Paribas*' (2016) 79 *Modern Law Review* 1090; J W Carter and Wayne Courtney, 'Unexpressed Intention and Contract Construction' (2017) 37 *Oxford Journal of Legal Studies* 326.

3 Special rules apply, for instance, to the construction of exclusion clauses. See: *Darlington Futures Ltd v Delco Australia Pty Ltd* (1986) 161 CLR 500. For an unusually candid discussion of the history of judicial attitudes towards the construction exclusion clauses, see: *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd* [1983] QB 284, 297 (Lord Denning).

4 The terms 'construction' and 'interpretation' are used interchangeably in this paper.

5 For particularly strong criticism, see: J W Carter, 'Context and Literalism in Construction' (2014) 31 *Journal of Contract Law* 100 and Andrew Stewart, 'What's Wrong with the Australian Law of Contract?' (2012) 29 *Journal of Contract Law* 74, where it is said (at 84) that '[i]t is almost as if the High Court regards this as a private joke that need not be shared'.

6 See: Ryan Catterwell 'The Indirect Use of Evidence of Prior Negotiations and Subjective Intention: Part of the Surrounding Circumstances' (2012) 29 *Journal of Contract Law* 183; *Codelfa Construction Pty Ltd v State Rail Authority of NSW* (1982) 149 CLR 337, 352; *WIN Corporation Pty Ltd v Nine Network Australia Pty Ltd* [2016] NSWCA 297, [57]; *Angas Securities Ltd v Small Business Consortium Lloyds Consortium No 9056* [2016] NSWCA 182, [112]; *Cherry v Steele-Park* [2017] NSWCA 295, [57]–[67].

7 The practical importance of the debate is seen in the concern, expressed on a number of occasions, that the expansion of the field of material to which courts may have recourse when construing contracts will operate to increase the cost and complexity of litigation. See, eg: Sir Christopher Staughton, 'How do the Courts Interpret Commercial Contracts' (1999) 58 *Cambridge Law Journal* 303, 307; J J Spigelman, 'From Text to Context: Contemporary Contractual Interpretation' (2007) 81 *Australian Law Journal* 322, 334.

8 For criticism of the approach which has obtained in England in recent years, and a suggestion that change is afoot, see: Lord Sumption, 'A Question of Taste: The Supreme Court and the Interpretation of Contracts', (2017) 17 *Oxford University Commonwealth Law Journal* 301.

9 *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896, 912–913. It should be noted that it is somewhat misleading to treat the ICS principles as amounting to a

radical break with all that had gone before. In addition to Lord Hoffmann's explicit reliance upon the speeches of Lord Wilberforce in *Prenn v Simmonds* [1971] 1 WLR 1381 and *Reardon Smith Line Ltd v Yngvar Hansen-Tangen* [1976] 1 WLR 989, it should also be noted that Joanna McCunn has shown that the shift towards contextual construction is in truth something of a return to an approach which prevailed in the early modern period. See: Joanna McCunn 'Revolutions in Contractual Interpretation: A Historical Perspective' in Sarah Worthington, Andrew Robertson and Graham Virgo (eds), *Revolution and Evolution in Private Law* (Hart Publishing, 2018). For an example of an authoritative endorsement of a contextual approach to interpretation as late as 1877, see *River Wear Commissioners v Adamson* (1877) 2 App Cas 743, 763 (Lord Blackburn). Though his Lordship's comments were made in the immediate context of the construction of a statute, the principles are said to be relevant to the construction of any 'instrument in writing'. See further: Lord Bingham of Cornhill, 'A New Thing Under the Sun? The Interpretation of Contract and the ICS Decision' (2008) 12 *Edinburgh Law Review* 374.

10 The terminological differences in this sphere — as between, for instance, 'context', 'background', and 'surrounding circumstances' — are not wholly insignificant, but they can be put to one side for present purposes.

11 For further discussion, see: J W Carter, *The Construction of Commercial Contracts* (Hart Publishing, 2013) chs 6 and 7.

12 (1982) 149 CLR 337.

13 Ibid 352.

14 It is worth noting that Sir Anthony Mason, writing extracurially, has expressed regret at the manner in which he expressed his view on this point. See: Sir Anthony Mason, 'Opening Address' (2009) 25 *Journal of Contract Law* 1, 3. As was observed by Allsop P (as his Honour then was) in *Masterton Homes Pty Ltd v Palm Assets Pty Ltd* [2009] NSWCA 234 (at [1]), the statement of the 'true rule' in *Codelfa* might also be contrasted with later statements of Mason J as to the proper approach to the interpretation of legal instruments. See, eg: *K & S Lake City Freighters Pty Ltd v Gordon & Gotch Ltd* (1985) 157 CLR 309, 315 (though here the context was statutory interpretation).

15 For an example of this approach being endorsed in an intermediate appellate court, see: *Brambles Holdings Ltd v Bathurst City Council* (2001) 53 NSWLR 153, 163 (Heydon JA).

16 For a detailed survey of the relevant authorities, see, eg: David McLauchlan, 'Plain Meaning and Commercial Construction: Has Australia Adopted the ICS Principles?' (2009) 25 *Journal of Contract Law* 7.

17 (2001) 210 CLR 181, 188 (footnotes omitted).

18 (2004) 218 CLR 451, 461–462 (footnotes omitted).

19 (2004) 219 CLR 165, 179 (footnotes omitted).

20 (2002) 240 CLR 45, 53 (footnotes omitted).

21 And see also, for example: *Wilkie v Gordian Runoff Ltd* (2005) 221 CLR 522, 529 (Gleeson CJ, McHugh, Gummow and Kirby JJ); *International Air Transport Association v Ansett Australia Holdings Ltd* (2008) 234 CLR 151, 160 (Gleeson CJ), 174 (Gummow, Hayne, Heydon, Crennan and Kiefel JJ).

22 See, eg: *Lion Nathan Australia Pty Ltd v Coopers Brewery Ltd* (2006) 156 FCR 1; *Franklins Pty Ltd v Metcash Trading Ltd* (2009) 76 NSWLR 603; *Masterton Homes Pty Ltd v Palm Assets Pty Ltd* [2009] NSWCA 234, [1]–[3].

23 (2011) 282 ALR 604. Though they have had a more muted impact than the special reasons in Jireh, it is worth noting also the remarks in the joint judgment of Heydon and Crennan JJ in *Byrnes v Kendle* (2011) 243 CLR 253, 285 (fn 155):

'This Court said in *Royal Botanic Gardens and Domain Trust v South Sydney City Council* (2002) 240 CLR 45 at 62-63 [39] that until this Court had decided on whether there were differences between *Investors Compensation Scheme Ltd v West Bromwich Building Society [No 1]* [1998] 1 WLR 896; [1998] 1 All ER 98 and *Codelfa Construction Pty Ltd v State Rail Authority (NSW)* (1982) 149 CLR 337, and if so which should be preferred, the latter case should be followed in Australia. The question has not been argued or decided in this Court. The opinions stated in *Masterton Homes Pty Ltd v Palm Assets Pty Ltd* (2009) 261 ALR 382 at 384-385 [1]-[4], 406-407 [112]-[113] and *Franklins Pty Ltd v Metcash Trading Ltd* (2009) 76 NSWLR 603 at 616-618 [14]-[18], 621-622 [42], 626 [63], 663-678 [239]-[305] must be read in this light.'

24 *Jireh,* 605 (footnotes omitted).

25 (2015) 256 CLR 104. Every member of the Court was in agreement on this point. See: *Wright Prospecting,* 117 (French CJ, Nettle and Gordon JJ), 133 (Kiefel and Keane JJ), 134 (Bell and Gageler JJ).

26 The same point has been made by the High Court on a number of other occasions. See, eg: *North Ganalanja Aboriginal Corporation v Queensland* (1996) 185 CLR 595, 643; *Attorney-General (Cth) v Finch* (No 2) (1984) 155 CLR 107, 114–115.

27 (2014) 251 CLR 640, 656 (footnotes omitted).

28 *Ecosse Property Holdings Pty Ltd v Gee Dee Nominees Pty Ltd* [2017] HCA 12, [16] (footnotes omitted).

29 For some of the many discussions of these difficulties, see, in addition to the works cited above: M Walton, 'Where now ambiguity?' (2011) 35 *Australian Bar Review* 176; Derek Wong and Brent Michael, '*Western Export Services v Jireh International*: Ambiguity as the gateway to surrounding circumstances?' (2012) 86 *Australian Law Journal* 57; David McLauchlan and Matthew Lees, 'Construction Controversy' (2011) 28 *Journal of Contract Law* 101; David McLauchlan and Matthew Lees, 'More Construction Controversy' (2012) 29 *Journal of Contract Law* 97; The Hon Justice Kenneth Martin, 'Contractual Construction: Surrounding Circumstances and the Ambiguity Gateway' (2013) 37 *Australian Bar Review* 118; The Hon Kevin Lindgren, 'The Ambiguity of Ambiguity in the Construction of Contracts' (2014) 37 *Australian Bar Review* 153; Thomas Prince, 'Defending Orthodoxy: *Codelfa* and Ambiguity' (2015) 89 *Australian Law Journal* 491; Daniel Reynolds, 'Construction of Contracts After *Mount Bruce Mining v Wright Prospecting*' (2016) 90 *Australian Law Journal* 190.

30 In addition to the authorities considered below, see, eg:

Righi v Kissane Family Pty Ltd [2015] NSWCA 238, [44]; *Calvo v Ellimark Pty Ltd* [2016] NSWCA 136, [55]; *Zhang v ROC Services (NSW) Pty Ltd*; *National Transport Insurance by its manager NTI Ltd v Zhang* [2016] NSWCA 370, [79].

31 (2014) 89 NSWLR 633, 653 (footnotes omitted).

32 *Stratton Finance Pty Ltd v Webb* [2014] FCAFC 110, [36]–[40] (Allsop CJ, Siopis and Flick JJ).

33 [2016] HCA 5.

34 [2016] HCA 47.

35 [2016] NSWCA 297,[59] (footnotes omitted).

36 [2017] NSWCA 295.

37 Ibid 76.

38 [2016] VSCA 280.

39 Ibid [137]–[138] (footnotes omitted).

40 Ibid [231]–[232] (footnotes omitted).

41 [2014] WASCA 164.

42 Ibid [35]–[45] (footnotes omitted). See also: *McCourt v Cranston* [2012] WASCA 60; *MacKinlay v Derry Dew Pty Ltd* [2014] WASCA 24; *Hancock Prospecting Pty Ltd v Wright Prospecting Pty Ltd* (2012) 45 WAR 29.

43 *Wright Prospecting,* 132–133 (footnotes omitted).

44 Prince, above n29, 494–495. The manner in which Mason J's 'true rule' is expressed has been subjected to some considerable textual analysis. See, further: Reynolds, above n29, 191–192.

45 It is also no object of this paper to weigh in on the question as to the proper intersection of construction and rectification. For a discussion of this point, see: Paul S Davies, 'Interpretation and Rectification in Australia' (2017) 76 *Cambridge Law Journal* 483.

46 For a recent example, see: Sumption, above n8.

47 Of course, exceptions do exist. See, eg: Prince, above n29.

48 See, eg: *Re Sigma Finance Corporation* [2010] 1 All ER 571; *Marley v Rawlings* [2014] 2 WLR 213; *Arnold v Britton* [2015] AC 1619; *Wood v Capita Insurance Services Limited* [2017] 2 WLR 1095, and generally the discussion in: Rohan Havelock, 'The 'Unitary Exercise' of Contractual Interpretation' (2017) 76 *Cambridge Law Journal* 486.

49 [2017] 2 WLR 1095, [11]–[12] (footnotes omitted).

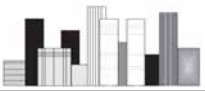
50 *Mainteck,* 655; *B & B Constructions (Aust) Pty Ltd v Brian A Cheeseman & Associates Pty Ltd* (1994) 35 NSWLR 227, 234.

51 *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* (2007) 230 CLR 89, 151.

52 See the discussion in: Matthew Harding and Ian Malkin, 'The High Court of Australia's Obiter Dicta and Decision-Making in the Lower Courts' (2012) 34 *Sydney Law Review* 12.

53 J D Heydon, 'Judicial Activism and the Death of the Rule of Law' (2003) 23 *Australian Bar Review* 110, 120–121.

54 See: Daniel Reynolds and Lyndon Goddard *Leading Cases in Contract Law: A Guide to the 100 Most Frequently Cited Cases in Contract and Related Subjects* (Federation Press, 2017).



Seminar paper

Assessment of damages for breach of contract

Jeffrey Goldberger*

This is the third part of the paper presented at Jeffrey Goldberger's annual Contract Law Master Class for the CLA in February, 2018. The first two parts of the paper were published in Vol32 No 1 and No 2 of CLQ respectively.

1 INTRODUCTION

1.1 Basic principles

- every breach generates a right to damages;
- the complainant must establish a loss flowing from the breach at the civil standard;
- the claimed loss must be caused by the breach complained of; and
- the claimed loss must not be too remote.

1.2 Purpose of an award of damages for breach of contract

The governing purpose of an award of damages for breach of contract is encapsulated in the classic statement of Parke B in *Robinson v Harman:*[179]

'The rule of the common law is, that where a party sustains a loss by reason of a breach of contract, he is, so far as money can do it, to be placed in the same situation, with respect to damages, as if the contract had been performed.'

In *Haines v Bendall*[180] the High Court restated the principle at 63:

'The settled principle governing the assessment of compensatory damages, whether in actions of tort or contract, is that the injured party should receive compensation in a sum which, so far as money can do, will put that party in the same position as he or she would have been in if the contract had been performed or the tort had not been committed: *Butler v Egg and Egg Pulp Marketing Board*; *Todorovic v Waller*; *Redding v Lee*; *Johnson v Perez*; *MBP (SA) Pty Ltd v Gogic*; *Livingstone v Rawyards Coal Co*; *British Transport Commission v Gourley*. Compensation is the cardinal concept. It is the "one principle that is absolutely firm, and which must control all else": *Skelton v Collins*, per Windeyer J. Cognate with this concept is the rule, described by Lord Reid in *Parry v Cleaver*, as universal, that a plaintiff cannot recover more than he or she has lost.'

This principle has been consistently applied in the Australian appellate courts although it must now be read in light of the decision of the High Court in *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd.*[181] The facts in *Tabcorp* were conveniently summarised by Hargrave J in *Fenridge Pty Ltd v Retirement Care Australia (Preston) Pty Ltd*[182] as follows:

'[350] That case concerned the lease of commercial premises. The tenant covenanted that it would not make any substantial alteration or addition to the demised premises without the written approval of the landlord. The tenant breached that obligation early in the lease, by destroying the foyer of the building and substituting a new foyer to meet its requirements. The lease had many years to run. The trial judge described the tenant's conduct as involving "contumelious disregard" for the landlord's rights and no challenge was made to that finding.

'[351] The landlord did not terminate the lease. It sued the tenant claiming damages for breach of the lease. The trial judge awarded damages of $34,820, representing the difference between the value of the property with the old foyer and the value of the property with the new foyer. The Full Federal Court held that the landlord was entitled to recover much more: the full cost of restoring the foyer to its original condition ($580,000), and $800,000 for loss of rent while that restoration was taking place, even though the works would not be performed until the lease expired many years in the future. The tenant appealed to the High Court, seeking to restore the trial judge's decision. In a unanimous decision (French CJ, Gummow, Heydon, Crennan and Kiefel JJ) the High Court dismissed the appeal.'

Importantly, the following passage appears in the joint judgment of the High Court:

'[13] Oliver J was correct to say in *Radford v De Froberville* that the words "the same situation, with the respect to damages,

as if the contract had been performed" do not mean "as good a financial position as if the contract had been performed" (emphasis added). In some circumstances putting the innocent party into "the same situation ... as if the contract had been performed" will coincide with placing the party into the same financial situation. Thus, in the case of the supply of defective goods, the prima facie measure of damages is the difference in value between the contract goods and the goods supplied. But as Staughton LJ explained in *Ruxley Electronics Ltd v Forsyth* such a measure of damages seeks only to reflect the financial consequences of a notional transaction whereby the buyer sells the defective goods on the market and purchases the contract goods. The buyer is thus placed in the "same situation ... as if the contract had been performed", with the loss being the difference in market value. However, in cases where the contract is not for the sale of marketable commodities, selling the defective item and purchasing an item corresponding with the contract is not possible. In such cases, diminution in value damages will not restore the innocent party to the "same situation ... as if the contract had been performed".'

In *Fenridge,* Hargrave J identified the four principles emerging from the joint judgment.

'[352] The following principles which are relevant to this case may be distilled from the joint judgment of the High Court:

'(1) The "ruling principle" with respect to damages at common law for breach of contract is that a party who sustains a loss by reason of a breach of contract is, so far as money can do it, entitled to be placed in the same position, with respect to damages, as if the contract had been performed.

'(2) The entitlement to be placed in the same situation with respect to damages as if the contract had been performed means just that. It does not mean "as good a financial position as if the contract had been performed".

'(3) It is *prima facie* no answer to a claim for damages on this basis that, viewed objectively, it is not to a plaintiff's financial advantage to be placed in the same situation as if the contract had been performed. It is for the plaintiff to judge whether he wants damages on that basis "subject to the proviso, of course, that he is seeking compensation for a genuine loss and not merely using a technical breach to secure an uncovenanted profit".

'(4) There is another qualification to the ruling principle, that the work to be undertaken must be necessary to produce conformity with the contractual obligation and must also "be a reasonable course to adopt". The test of "unreasonableness" is, however, "only to be satisfied by fairly exceptional circumstances". For example, where a building contract required a house to be built with cement rendered external walls of second-hand bricks, but the builder used new bricks of first quality underneath the cement render. The cost of demolition and re-construction with second-hand bricks would not be a reasonable course to adopt.'

Tabcorp was recently applied by the Supreme Court of Victoria in *United Petroleum Pty Ltd v Bonnie View Petroleum Pty Ltd (In Liq).*[183] I turn to the facts.

In 2010 the defendant, Bonnie View (BV) operated wholesale and retail petroleum businesses in Gippsland including one in Sale. On 14 May 2010 BV sold the Sale business, together with 18 others to the plaintiff, United Petroleum. The agreement provided for United to conduct environmental and other due diligence, including testing at the premises of each of the businesses. There was also a provision which contemplated that the parties would enter into a further agreement if testing revealed contamination involving remediation costs in excess of a defined amount.

During the due diligence process contamination was discovered at the Site. As contemplated, the parties then entered into a Side Agreement under which BV agreed to remediate the Site. In case of default, United was given a right to require an assignment of the lease. BV failed to remediate and failed to take the necessary steps to assign the lease. Ultimately United negotiated a new lease of the Site directly with the landlord under which United's remediation obligations were significantly less onerous than under the Side Agreement.

Relevantly, there was expert evidence that the site at Sale was capable of use as a petrol station without being remediated to the standards of the Side Agreement.

United instituted proceedings against BV and the guarantors claiming $470,000 being the claimed cost to remediate the Site to the standards prescribed by the Side Deed. United also claimed some $448,000 for costs incurred in obtaining the new lease plus interest on delayed profits.

A key issue was whether United was entitled to the costs of remediation of the Site by way of damages for breach of contract.

Kennedy J noted the rival contentions of the parties as follows:

'[285] BV submitted that, whilst *Robinson v Harman* was the ruling principle, courts have adopted a wide variety of approaches. Further, that in this case, the relevant measure of damages was the difference between the economic value to United of the leasehold estate with the site remediated to the standards required under the Side Agreement and the value of the estate without the site being so remediated. Further, that there was no evidence to suggest that there was any difference between these values given that United only needed to operate the site as a petrol station under the terms of the lease it entered. It followed that the value of the works to the standard imposed by the Side Agreement was of no value whatsoever.

'[290] By way of contrast, United emphasised that United's remediation obligations under the new lease were irrelevant (as were BV's obligations under the former lease) relying on *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* (*Tabcorp*). The focus instead was on the consequences of breach and restoration to the position United would have been if BV had performed its obligations.'

His Honour held in favour of the plaintiff and, relevantly, said:

'[312] The principles in *Tabcorp* are applicable. It follows that United is entitled to be placed in the same situation with respect to damages as if the contract had been performed.

'[313] The principle does not mean as good a "financial" or "economic" position as if the contract had been performed. There is therefore no warrant to examine the economic value to United instead of enforcing the contractual bargain. In particular, it is not relevant to consider United's rights and obligations under the new lease.

'[314] I also do not consider that the present circumstances come within any of the recognised qualifications. The breach is not merely technical. The present situation is also not one which could be said to be "exceptional" in the same way as the examples of *Bellgrove* or *Ruxley*. United's desire to have the site remediated to the standard specified in the Side Agreement is simply not comparable to the "unreasonableness" of demolishing a new house to rebuild it with second hand bricks or demolishing a pool to make it slightly deeper.

'[315] In *Tabcorp,* the High Court also stated that "the requirement of reasonableness did not mean that any excess over the amount recoverable on a diminution in value was unreasonable". The Court stated that such submissions "rested on a loose principle of 'reasonableness' which would radically undercut the bargain which the innocent party had contracted for and make it very difficult to determine in any particular case on what basis damages would be assessed".

'[316] In any event, I consider that it is reasonable for United to seek rectification damages. The evidence of Mr Carmeli was that although the site was likely still "fit for purpose" to operate as a petrol station and convenience store, United nevertheless "has an interest in the risk associated with the contamination of the groundwater". Pursuant to s62A of the Environment Protection Act 1970 (Vic), United, as an occupier, is also liable to a receipt of clean up notices in the event of land or water being polluted.

'[317] Thus, in regard to the remediation of the site, United is entitled to (unchallenged) rectification damages pursuant to the evidence of Mr Vass at $470,000. There is also no basis for the alternative basis suggested by Mr Parmansche given his estimate was inconsistent with the obligations under the Side Agreement.

'[318] Accordingly, the amount of $470,000 is to be awarded in respect of the remediation costs.'

1.3 Interests protected by award of damages

- Expectation loss, eg, loss of net profit
- Reliance loss, eg, wasted expenditure
- Restitution, eg, pre-payments received by the contract breaker

2 KEY CONCEPTS

2.1 Causation generally

- Common sense approach
- The 'but for' test is just a starting point

— *March v E & M H Stramare Pty Ltd*[184]

— *Travel Compensation Fund v Robert Tambree (t/as R Tambree & Associates)*[185]

- In *O'Halloran v R T Thomas & Family Pty Ltd*[186] Spigelman CJ cited with approval the following approach to causation developed by Lord Hoffman in *Environment Agency (formerly National Rivers Authority) v Empress Car Co (Abertillery) Ltd:*[187]

'The first point to emphasise is that common sense answers to questions of causation will differ according to the purpose for which the question is asked. Questions of causation often arise for the purpose of attributing responsibility to someone, for example, so as to blame him for something which has happened or to make him guilty of an offence or liable in damages. In such cases, the answer will depend upon the rule by which responsibility is being attributed. Take for example, the case of the man who forgets to take the radio out of his car and during the night someone breaks the quarterlight, enters the car and steals it. What caused the damage? If the thief is on trial, so that the question is whether he is criminally responsible, then obviously the answer is that he caused the damage.'

And later:

'... one cannot give a common sense answer to a question of causation for the purpose of attributing responsibility under some rule without knowing the purpose and scope of the rule. Does the rule impose a duty which requires one to guard against, or makes one responsible for, the deliberate act of third persons? ...

'Before answering questions about causation, it is therefore first necessary to identify the scope of the relevant rule. This is not a question of common sense fact; it is a question of law.'

Also in *Barnes v Hay*[188] Mahoney JA noted at 353:

'... the determination of a causal question involves, in my opinion, a normative decision as to whether, for the purposes of the case, the precedent act for which the defendant is responsible should be seen as causal of the plaintiff's loss. And, in my opinion, that evaluation is made, not by a "test" or "guide" such as the "but for" test, but by a functional evaluation of the relationship and the purposes or policy of the relevant part of the law.'

- McHugh JA in *Alexander v Cambridge Credit Corporation Ltd*[189] said at 358:

'Accordingly, to establish a causal connection between a breach of contract and the damage which the plaintiff has suffered, he needs only to show that the breach was a cause of the loss. This is to be decided by the application of commonsense principles. In general, the application of the "but for" test will be sufficient to prove the necessary causal connection. But that test is only a guide. The ultimate question is whether, as a matter of commonsense, the relevant act or omission was a cause.'[190]

- In discussing causation in the context of the Fair Trading Act 1987 (NSW), in *Bullabidgee Pty Ltd v McCleary,*[191] Allsop P said:

'[67] The legal context and relevant rule of responsibility direct one to the relevant legal policy and purpose of the casual question, thus affecting the evaluation of the extent of the required factual

involvement of the impugned act or omission in assessing legal responsibility for the law. An example of the relevance of the content of the rule of responsibility is the duty of a doctor to warn a patient of material risk inherent in proposed treatment.'

• Causation and mitigation

In *Luxer Holding Pty Ltd v Glentham Pty Ltd,*[192] Buss JA said:

'[41] There is a clearly established conceptual difference between the measure of damages, on the one hand, and the doctrine of mitigation, on the other. The onus is on the lessor to prove, according to the applicable measure, that it has suffered damage. The onus is on the lessee to prove that that the lessor has failed to take reasonable steps to mitigate its damage, and to demonstrate the extent to which there has been a failure to mitigate.'

The conceptual distinction between mitigation and causation was recently considered by the New South Wales Court of Appeal in *Chand v Commonwealth Bank of Australia.*[193]

• A comprehensive examination of the principles of causation in contract was undertaken by Beach J in *Siegwerk Australia Pty Ltd (in liquidation) v Nuplex Industries (Aust) Pty Ltd.*[194] His Honour said:

'***(a) General principles of causation in contract law***

'[65] Siegwerk must show that the damage to the cans and the consequent loss suffered resulted from Nuplex's breach of the tolling agreement (*Reg. Glass Pty Ltd v Rivers Locking Systems Pty Ltd* (1968) 120 CLR 516 at 523 per Barwick CJ, McTiernan and Menzies JJ). It is sufficient that the breach causally contributed to the loss (*Norton Australia Pty Ltd v Streets Ice Cream Pty Ltd* (1968) 120 CLR 635 at 643 per Barwick CJ; *Monarch Steamship Co Ltd v Karlshamns Oljefabriker (A/B)* [1949] AC 196 at 232 per Lord du Parcq; *Wenham v Ella* (1972) 127 CLR 454 at 466 per Walsh J; *Alexander v Cambridge Credit Corporation Ltd* (1987) 9 NSWLR 310 at 351 per McHugh JA).

'[66] Factual causation is generally resolved through an application of the "but for" test. The "but for" test entails a determination on the balance of probabilities that the particular harm that in fact occurred would not have occurred absent the conduct of the party in breach. The question is whether a particular act or condition was one of the conditions or relations necessary to complete the set of conditions which represent the cause posited. This is the basis of the "but for" test of causation. But the "but for" test is not the exclusive test of factual causation.

'[67] Further, it is not enough to demonstrate that Nuplex's breach of the tolling agreement materially increased the risk of harm or loss. The breach must be the or a cause including a material contribution. Nevertheless, a breach causing a material increase in risk may provide, together with other circumstances, a foundation for inferring causation, including a material contribution to the loss, in the absence of any sufficient reason to the contrary.

'[68] Further, it is irrelevant to inquire whether the breach was the dominant, effective or real cause of the loss. If the evidence is suggestive of multiple causes, the inquiry to be made is whether the breach was a cause of the loss.

'[69] It has been said that the question whether a breach of contract has caused a loss is a question of fact applying common sense principles. It is said that the common law applies the ordinary man's notion of causation instead of theories espoused by philosophers and scientists. Clearly, the object of the common law theory of causation is not the same as that of a philosophical or scientific inquiry into causation. But the conceptually elusive if not inutile phrase "common sense", when discussing questions of causation in the present context, adds little to the problem solving task.

'[70] Before proceeding further, it is necessary to be clear about the following three different levels of analysis that need to be undertaken:

'(a) First, what is the context within which and why is the question of causation being posed? In the present context what is being addressed is an alleged breach of contract, and particularly whether the relevant product met the contractual standard. What is then being considered is whether that breach was a or the cause of the relevant damage or loss. So, the lens through which causation is to be assessed starts from the proper identification of the relevant perspective for why the inquiry is being undertaken. The perspective from which causation is then to be addressed is not some diffuse or decontextualised inquiry. The lens through which causation is to be assessed must identify the act, omission, state of affairs or circumstance said to constitute the breach of the relevant normative standard. That identification is not to be described in the language of "common sense". Further, questions of causation require identification of the particular harm that was suffered. Identification of the damage sustained by a claimant will assist in identifying the acts or omissions that were its cause (Hunt & Hunt Lawyers v Mitchell Morgan Nominees Pty Ltd (2013) 247 CLR 613 at [43] to [57] per French CJ, Hayne and Kiefel JJ).

'(b) Second, once that contextual lens has been identified, the question then arises as to whether factual causation has been established in terms of the usual "but for" or necessary condition test by reference to linking the act, omission, state of affairs or circumstance referred to in subparagraph (a) with the alleged damage or loss. But even here, to use the vernacular of "common sense" is conceptually unhelpful in a case involving forensic complexity. Moreover, it is otiose in a case where the facts are simple and factual causation obvious.

'(c) Third, once that factual question has been analysed, the legal question arises, if factual causation has been established, as to whether the relevant party should be held legally responsible for that loss or damage. Alternatively expressed, is the damage within the relevant scope of liability? But this is a legal question depending in part upon the nature of both the breach and the damage alleged. It is difficult to see how the vernacular of "common sense" has utility for this third level of analysis. One is not

talking of the common sense of the layman. Moreover, one is not truly talking of the "common sense" of the lawyer, but rather a conceptual and evaluative legal question upon which reasonable minds might differ. Indeed, lawyers have struggled with this conceptual question and have sought refuge in adjectives such as "direct", "natural and probable", "direct and natural", "proximate", "real effective" and so on to categorise potential cause(s) to address the legal question. And even where they have agreed on the label, differences have arisen in their application. Further, other problems have arisen with scenarios that have had to deal with concurrent sufficient causes, causes that are neither necessary nor sufficient conditions with or without other elements, and novus actus interveniens questions. *March v E & M H Stramare Pty Ltd* (1991) 171 CLR 506 at 515 per Mason CJ is authority for a common sense test or a common sense value judgment, but it was a tort case not a contract case. The value of such a test in my context may be doubted (*cf Allianz Australia Insurance Ltd v GSF Australia Pty Ltd* (2005) 221 CLR 568 at [97] to [98] per Gummow, Hayne and Heydon JJ and *Travel Compensation Fund v Tambree* (2005) 224 CLR 627 at [45] per Gummow and Hayne JJ). Nevertheless, I have applied a common sense test. Finally, on one view, this third level of analysis is not a causation question at all, but rather a legal responsibility question once factual causation has been answered (the second level of analysis) through the relevant lens (the first level of analysis). It has been suggested that the substantive meaning of causation has been inappropriately comingled with this latter question of legal responsibility or the associated phrase "scope of liability", as the observations of Edelman J writing extra-judicially in "Unnecessary Causation" (2015) 89 ALJ 20 and Professor Jane Stapleton in "Cause-in-Fact and the Scope of Liability for Consequences" (2003) 119 LQR 388 explain. Their views may be said to resonate with those of working trial judges mining facts from the coal face of forensic inquiry.

'[71] There are several other preliminary observations that should be made.

'[72] First, one can understand some jurists using the language of "common sense". If one was instructing a jury, such simplistic language has an attraction. Further, many scenarios involving causation are straightforward with the answer being intuitively clear without further factual reflection at least.

'[73] Second, some jurists are understandably keen by the use of the vernacular of "common sense" to distinguish the lawyer's use and context of causation from that of the scientist or the philosopher. But to so distinguish does not entail that the only contrast is with a "common sense" test. Moreover, although that distinction from other fields of discourse is correct when looking at the first and third levels of analysis referred to above, the line is not so brightly drawn for the second level of analysis, where concepts from one context can assist in the conceptualisation of another.

'***(b) The nature of the contract***

'[74] Where a party breaches a contract by defective or inadequate performance, the circumstances which render the performance defective or inadequate are an integral part of the breach. They form part of the starting point for the analysis of causation (*Ramsey v Annesley College* [2013] SASC 72 at [434] per Blue J).

'[75] More generally, the selection of the relevant cause will vary with the nature of the contract, the nature of the breach and the damage suffered. The scope of a defendant's legal responsibility for loss caused by a breach of contract is to be assessed by analysing what it promised to achieve (*Chand v Commonwealth Bank of Australia* [2014] NSWSC 708 at [293] per Robb J). Further, the question of causation is to be informed by the context in which the contract was made, which may reinforce rather than attenuate a conclusion of causation (*Programmed Total Marine Services Pty Ltd v Ship Hako Endeavour* (2014) 229 FCR 563 at [14] and [15] per Allsop CJ).'

Causation under the Civil Liability Act 2002

The Act, relevantly, provides:

5D General principles

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

The High Court considered these provisions in *Adeels Palace Pty Ltd v Moubarak*[195] said at 440:

'[42] Section 5D(1) of that Act divides the determination of whether negligence caused particular harm into two elements: factual causation and scope of liability.

'[43] Dividing the issue of causation in this way expresses the relevant questions in a way that may differ from what was said by Mason CJ, in *March v Stramare (E & M H) Pty Ltd,* to be the common law's approach to causation. The references in *March v Stramare* to causation being "ultimately a matter of common sense" were evidently intended to disapprove the proposition "that value judgment has, or should have, no part to play in resolving causation as an issue of fact". By contrast, s5D(1) treats factual causation and scope of liability as separate and distinct issues.

'[44] It is not necessary to examine whether or to what extent the approach to causation described in *March v Stramare* might lead to a conclusion about factual causation different from the conclusion that should be reached by applying s5D(1). It is sufficient to observe that, in cases where the Civil Liability Act or equivalent statutes are engaged, it is the applicable statutory provision that must be applied.

'[45] Next it is necessary to observe that the first of the two elements identified in s5D(1) (factual causation) is determined by the "but for" test: but for the negligent act or omission, would the harm have occurred?'

Subsequently in *Wallace v Kam*[196] the Court, in reference to the New South Wales Act, said:

'[11] The common law of negligence requires determination of causation for the purpose of attributing legal responsibility. Such a determination inevitably involves two questions: a question of historical fact as to how particular harm occurred; and a normative question as to whether legal responsibility for that particular harm occurring in that way should be attributed to a particular person. The distinct nature of those two questions has tended, by and large, to be overlooked in the articulation of the common law. In particular, the application of the first question, and the existence of the second, have been obscured by traditional expressions of causation for the purposes of the common law of negligence in the conclusory language of "directness", "reality", "effectiveness" and "proximity".

'[14] The distinction now drawn by s5D(1) between factual causation and scope of liability should not be obscured by judicial glosses. A determination in accordance with s5D(1)(a) that negligence was a necessary condition of the occurrence of harm is entirely factual, turning on proof by the plaintiff of relevant facts on the balance of probabilities in accordance with s5E. A determination in accordance with s5D(1)(b) that it is appropriate for the scope of the negligent person's liability to extend to the harm so caused is entirely normative, turning in accordance with s5D(4) on consideration by a court of (amongst other relevant things) whether or not, and if so why, responsibility for the harm should be imposed on the negligent party.

'[15] Thus, as Allsop P explained in the present case:

'"[T]he task involved in s5D(1)(a) is the elucidation of the factual connection between the negligence (the relevant breach of the relevant duty) and the occurrence of the particular harm. That task should not incorporate policy or value judgments, whether referred to as 'proximate cause' or whether dictated by a rule that the factual enquiry should be limited by the relationship between the scope of the risk and what occurred. Such considerations naturally fall within the scope of liability analysis in s5D(1)(b), If s5D(1)(a) is satisfied, or in s5D(2), if it is not."

'[16] The determination of factual causation in accordance with s5D(1)(a) involves nothing more or less than the application of a "but for" test of causation. That is to say, a determination in accordance with s5D(1)(a) that negligence was a necessary condition of the occurrence of harm is nothing more or less than a determination on the balance of probabilities that the harm that in fact occurred would not have occurred absent the negligence.'

In a comprehensive analysis of the legislation Leeming JA in *Paul v Cooke*[197] cast doubt on the proposition advanced by the High Court in *Wallace v Kam* that factual causation excluded normative and policy considerations. His Honour said:

'[110] ... True it is that there are statements that the determination of factual causation is entirely factual and the determination of scope of liability is entirely normative, notably in *Wallace v Kam* in the High Court at [14]. What precisely flows from those two elements being delineated by the Act, something emphasised by the High Court, remains to be fully worked out. There is to my mind no basis in the statute or any decision on it to support the notion that the strength of the causal connection (or any other factual matter relevant to factual causation) is irrelevant to the determination of what is "appropriate". Where as here the causal connection is weak, that is far from an irrelevant consideration in determining whether it is appropriate for a defendant to be liable for the harm so caused. To give the simplest counterexample, the actions of the driver who ignores the red light and of the speeding ambulance driver racing to the hospital who follows the green light are both necessary conditions of their collision, yet the scope of liability of each is very different. The different considerations informing the scope of liability of the ambulance driver, for example, include facts (such as speed and whether the siren was operating) as well as matters grounded in policy. As Basten JA said in *King v Western Sydney Local Health Network* at (34]:

'"... questions of factual causation and scope of liability, as separately identified in s5D, do not readily fall into separate and independent watertight compartments."'

It should be borne in mind that the Act will apply to determine causation in relation to a claim for damages for breach of a contractual duty of care in circumstances where there is a concurrent duty of care in tort.

2.2 Remoteness

The test of remoteness in Australian law is governed by the principles formulated by Alderson B in *Hadley v Baxendale.*[198]

'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 fair-

ly and reasonably be considered either arising naturally, i.e., 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.'

In *European Bank Ltd v Robb Evans of Robb Evans and Associates*[199] the High Court stated at 437-8:

'Something immediately should be said respecting the significance for the issues in this appeal of the rule in *Hadley v Baxendale*. The rule is, of course, associated with the assessment of damages in actions for breach of contract. The principle with respect to damages at common law for breach of contract recently was confirmed by this court in *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* as that stated by Parke B in *Robinson v Harman*. The plaintiff is to be placed in the same situation with respect to damages, so far as money can do it, as if the contract had been performed.

'As Toohey J remarked in *Commonwealth v Amann Aviation Pty Ltd,* the rule in *Hadley v Baxendale* does not detract from what was said in *Robinson v Harman.* The rule is concerned with the question of remoteness and marks out the limits of the heads of damage for which the plaintiff is entitled to receive compensation. In the same case, McHugh J said of *Hadley v Baxendale* that the rule is a limit on, rather than a ground of, liability, marking out the boundary of the liability for loss or damage caused by a breach of contract.'

In respect of the scope and operation of the rule in *Hadley v Baxendale* it is suggested that the authorities establish the following key principles:

(a) The two limbs (as they are frequently referred to) are a statement of a single principle. Relevantly, in *Baltic Shipping Company v Dillon*[200] Brennan J said at 368:

'Remoteness is governed by the rules in *Hadley v Baxendale* which prescribe the measure of damages in respect of breach of contract to include not only damage naturally resulting from the breach ("ie, according to the usual course of things") but also damage which might "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". Additional or special knowledge known to both parties may widen or contract the scope of liability for breach. These rules have been merged in a single principle expressed by Lord Reid in *C Czarnikow Ltd v Koufos* and adopted in this Court:

'"The crucial question is whether, on the information available to the defendant when the contract was made, he should, or the reasonable man in his position would, have realised that such loss was sufficiently likely to result from the breach of contract to make it proper to hold that the loss flowed naturally from the breach or that loss of that kind should have been within his contemplation."'

And in *European Bank Ltd v Robb Evans of Robb Evans and Associates,* the High Court noted at 438:

'In *Commonwealth v Amann Aviation Pty Ltd* Mason J and Dawson J, with reference to the speeches of Lord Reid and Lord Upjohn in *C Czarnikow Ltd v Koufos,* said that the two limbs of the rule in *Hadley v Baxendale* represent the statement of a single principle and that the application of that principle may depend on the degree of relevant knowledge possessed by the defendant in the particular case. Lord Reid had used the expression "on the cards".'

(b) The test of remoteness in tort is reasonable foreseeability as opposed to the test in contract of reasonable contemplation. The difference is real and not purely semantic. Thus in *C Czarnikow Ltd v Koufos*[201] Lord Reid said at 385-6:

'The modern rule of tort is quite different and it imposes a much wider liability. The defendant will be liable for any type of damage which is reasonably foreseeable as liable to happen even in the most unusual case, unless the risk is so small that a reasonable man would in the whole circumstances feel justified in neglecting it. And there is good reason for the difference. In contract, if one party wishes to protect himself against a risk which to the other party would appear unusual, he can direct the other party's attention to it before the contract is made, and I need not stop to consider in what circumstances the other party will then be held to have accepted responsibility in that event. But in tort there is no opportunity for the injured party to protect himself in that way, and the tortfeasor cannot reasonably complain if he has to pay for some very unusual but nevertheless foreseeable damage which results from his wrongdoing.'

And his Lordship continued at 389:

'To bring in reasonable foreseeability appears to me to be confusing measure of damages in contract with measure of damages in tort. A great many extremely unlikely results are reasonably foreseeable: it is true that Lord Asquith may have meant foreseeable as a likely result, and if that is all he meant I would not object further than to say that I think that the phrase is liable to be misunderstood.'

And in *Alexander v Cambridge Credit Corporation Ltd*[202] McHugh JA said at 365:

'In later cases (eg, *H Parsons (Livestock) Ltd v Uttley, Ingham & Co Ltd* [1978] QB 791 at 807), there has been a tendency to play down the distinction between reasonable foreseeability and reasonable contemplation as semantic only. However, I think that the difference is a real one which results in a significant narrowing of liability. The word "contemplation" seems to be used in *Koufos* in the sense of "thoughtful consideration" or perhaps "having in view in the future". It emphasises that, if the parties had thought about the matter, they would really have considered that the result had at least a "serious possibility" of occurring.

'The actual decisions in *Hadley v Baxendale* and *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd* bear out the proposition that the contemplation test limits the area of potential liability. For it was surely reasonably foreseeable as a serious

possibility that the millshaft was required for the operation of the mill and that a launderer and dyer might have special contracts with a lucrative profit margin. Yet the losses of the plaintiffs arising from those circumstances were not recoverable.

(c) The test is based on the knowledge of the contract breaker at the date of contract.

(d) The parties need not contemplate the magnitude of a loss if loss of that type or kind falls within the rule. In *Transfield Shipping Inc v Mercator Shipping Inc,*[203] Lord Hoffman said at 70:

'[21] It is generally accepted that a contracting party will be liable for damages for losses which are unforeseeably large, if loss of that type or kind fell within one or other of the rules in *Hadley v Baxendale*: see, for example, Staughton J in *Transworld Oil Ltd v North Bay Shipping Corpn* (*The Rio Claro*) [1987] 2 Lloyds Rep 173, 175 and *Jackson v Royal Bank of Scotland plc* [2005] 1 WLR 377. That is generally an inclusive principle: if losses of that type are foreseeable, damages will include compensation for those losses, however large. But the South Australia and Mulvenna cases show that it may also be an exclusive principle and that a party may not be liable for foreseeable losses because they are not of the type or kind for which he can be treated as having assumed responsibility.

'[22] What is the basis for deciding whether loss is of the same type or a different type? It is not a question of Platonist metaphysics. The distinction must rest upon some principle of the law of contract. In my opinion, the only rational basis for the distinction is that it reflects what would reasonably have been regarded by the contracting party as significant for the purposes of the risk he was undertaking. In *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd* [1949] 2 KB 528, where the plaintiffs claimed for loss of the profits from their laundry business because of late delivery of a boiler, the Court of Appeal did not regard "loss of profits from the laundry business" as a single type of loss. They distinguished, at p543, losses from "particularly lucrative dyeing contracts" as a different type of loss which would only be recoverable if the defendant had sufficient knowledge of them to make it reasonable to attribute to him acceptance of liability for such losses. The vendor of the boilers would have regarded the profits on these contracts as a different and higher form of risk than the general risk of loss of profits by the laundry.'

And in *Alexander v Cambridge Credit Corporation Ltd*[204] McHugh JA said at 365:

'An important matter in ascertaining whether the loss or damage is too remote is the extent to which the parties may be taken to have contemplated the events giving rise to that loss or damage. The parties need not contemplate the degree or extent of the loss or damage suffered: *Wroth v Tyler* [1974] Ch 30 at 61-62; *H Parsons (Livestock) Ltd v Uttley Ingham & Co Ltd* at 813 and *South Coast Basalt Pty Ltd v R W Miller and Co Pty Ltd* [1981] 1 NSWLR 356 at 364. Nor need they contemplate the precise details of the events giving rise to the loss. It is sufficient that they contemplate the kind or type of loss or damage suffered.

'The most difficult question in determining the relevant kind of damage concerns the level of classification of the damage which the parties must have contemplated. Clearly the level must not be so high that the parties are required to contemplate the very loss in question or the precise manner of its occurrence. Nor must it be so low that any loss or damage, no matter how unusual in nature or occurrence, would fall within the classification.'

(e) Various expressions have been used to describe the degree of probability of the occurrence of the loss which is to be reasonably contemplated by the contract breaker. These expressions include 'a serious possibility', 'a real danger', 'on the cards' and 'a not unlikely event'. However, Lord Reid's exposition has been treated as authoritative by the Australian courts. His Lordship said at 388:

'... but I think that Hall's case must be taken to have established that damages are not to be regarded as too remote merely because, on the knowledge available to the defendant when the contract was made, the chance of the occurrence of the event which caused the damage would have appeared to him to be rather less than an even chance. I would agree with Lord Shaw that it is generally sufficient that that event would have appeared to the defendant as not unlikely to occur. It is hardly ever possible in this matter to assess probabilities with any degree of mathematical accuracy. But I do not find in that case or in cases which preceded it any warrant for regarding as within the contemplation of the parties any event which would not have appeared to the defendant, had he thought about it, to have a very substantial degree of probability.'

His Lordship continued at 390:

'It has never been held to be sufficient in contract that the loss was foreseeable as "a serious possibility" or "a real danger" or as being "on the cards." It is on the cards that one can win £100,000 or more for a stake of a few pence — several people have done that. And anyone who backs a hundred to one chance regards a win as a serious possibility — many people have won on such a chance. And the *Wagon Mound (No. 2)* could not have been decided as it was unless the extremely unlikely fire should have been foreseen by the ship's officer as a real danger. It appears to me that in the ordinary use of language there is wide gulf between saying that some event is not unlikely or quite likely to happen and saying merely that it is a serious possibility, a real danger, or on the cards.'

In *National Australia Bank Ltd v Nemur Varity Pty Ltd,*[205] Batt J in analysing the probability component of the remoteness test said:

'[44] The House of Lords in *Koufos* made it clear that the test for remoteness in tort is more liberal than in contract, but the members of the House used slightly different formulations to express the degree of probability of the occurrence of the loss which is to be reasonably contemplated, such as not unlikely

(Lord Reid), liable to be or at least not unlikely to be (Lord Morris of Borth-y-Gest), liable to be (Lord Hodson) and a serious possibility or real danger (Lord Pearce and Lord Upjohn). The High Court has not, according to my review of its decisions, definitively chosen one of those formulations over the others, though McHugh JA, when a member of the New South Wales Court of Appeal, expressed a preference for Lord Reid's formulation. I shall for simplicity use it.'

2.3 Remoteness and assumption of risk

An important examination of the rule in *Hadley v Baxendale* was undertaken by the House of Lords in *Transfield Shipping Inc v Mercator Shipping Inc; The Achilleas.*[206] The decision highlights the underpinning rationale of the rule and its limitations.

I turn to the facts.

By a time charter dated 22 January 2003 the owners let a vessel to charterers for about five to seven months at a daily rate of US$16,150. There was a subsequent addendum under which the parties fixed the vessel for a further period of five to seven months.

The latest date for redelivery by the charterers was 2 May 2004.

By April 2004 the market rate had more than doubled.

On 21 April 2004 the owners fixed the vessel for a new hire at a daily rate of US$39,500.

The latest date for delivery under the new charter was 8 May 2004 after which the charter had a cancellation right.

In breach of contract the charter did not redeliver the vessel until 11 May 2004.

The owners renegotiated the new charter as a result of which the charter agreed to continue the charter but at a reduced charter rate. The reduction amounted to US$8,000 on the daily rate.

The owners claimed damages based on the loss of the difference between the original rate and the reduced rate over the whole period of the fixture.

The charterers argued that the owners were only entitled to claim for the difference during the overrun period, ie, the period of nine days from 2 May to 11 May 2004.

Lord Hoffmann posited the issue for consideration as follows:

'[9] ... The case therefore raises a fundamental point of principle in the law of contractual damages; is the rule that a party may recover losses which were foreseeable (not unlikely) an external rule of law, imposed upon the parties to every contract in the fault of express provision to the contrary, or is it a prima facie assumption about what the parties may be taken to have intended, no doubt applicable in the great majority of cases but capable of rebuttal in cases in which the context, surrounding circumstances or general understanding in the relevant market shows that a party would not reasonably have been regarded as assuming responsibility for such losses?'

His Lordship noted that the owners' submission that the starting point for the analysis was the rule in *Robinson v Harman* was incorrect. His Lordship said:

'[15] In other words, one must first decide whether the loss for which compensation is sought is of a "kind" or "type" for which the contract-breaker ought fairly to be taken to have accepted responsibility.'

His Lordship then explained why, in his opinion, the owners were not entitled to the damages as claimed:

'[23] If, therefore, one considers what these parties, contracting against the background of market expectations found by the arbitrators, would reasonably have considered the extent of the liability they were undertaking, I think it is clear that they would have considered losses arising from the loss of the following fixture a type or kind of loss for which the charterer was not assuming responsibility. Such a risk would be completely unquantifiable, because although the parties would regard it as likely that the owners would at some time during the currency of the charter enter into a forward fixture, they would have no idea when that would be done or what its length or other terms would be. If it was clear to the owners that the last voyage was bound to overrun and put the following fixture at risk, it was open to them to refuse to undertake it. What this shows is that the purpose of the provision for timely redelivery in the charterparty is to enable the ship to be at the full disposal of the owner from the redelivery date. If the charterers orders will defeat this right, the owner may reject them. If the orders are accepted and the last voyage overruns, the owner is entitled to be paid for the overrun at the market rate. All this will be known to both parties. It does not require any knowledge of the owners arrangements for the next charter. That is regarded by the market as being, as the saying goes, *res inter alios acta*.'

Lord Hope said:

'[31] Assumption of responsibility, which forms the basis of the law of remoteness of damage in contract, is determined by more than what at the time of the contract was reasonably foreseeable.

'[32] ...The fact that the loss was foreseeable — the kind of result that the parties would have had in mind, as the majority arbitrators put it — is not the test. Greater precision is needed than that. The question is whether the loss was a type of loss for which the party can reasonably be assumed to have assumed responsibility.'

His Lordship continued:

'[34] In this case it was within the parties' contemplation that an injury which would arise generally from late delivery would be loss of use at the market rate, as compared with the charter rate, during the relevant period. This something that everybody who deals in the market knows about and can be expected to take into account. But the charterers could not be expected to know how, if — as was not unlikely — there was a subsequent fixture, the owners would deal with any new charterers. This was something over which they had no control and, at the time of entering into the contract, was completely unpredictable. Nothing was known at that time about the terms on which any subsequent fixture might be entered into — how short or long the period would be, for example, or what was to happen should the

previous charter overrun and the owner be unable to meet the new commencement date. It is true that neither party had any control over the state of the market. But in the ordinary course of things rates in the market will fluctuate. *So it can be presumed that the party in breach has assumed responsibility for any loss caused by delay which can be measured by comparing the charter rate with the market rate during that period. There can be no such presumption where the loss claimed is not the product of the market itself, which can be contemplated, but results from arrangements entered into between the owners and the new charterers, which cannot.'* (emphasis added)

Relevantly, Lord Walker said:

'[84] The majority arbitrators referred to a number of authorities, cited by the charterers, to the effect that the normal measure of damages for late delivery is the market rate (if higher than the charter rate) for the period from the latest date for re-delivery under contract until the date of actual re-delivery. ... Ultimately they accepted and applied the owners' submission that "what mattered was that the type of loss claimed was foreseeable": para 18 of the majority reasons. That was in my opinion too crude a test, and it was an error of law to adopt it. What mattered was whether the common intention of reasonable parties to a charterparty of this sort would have been that in the event of a relatively short delay in re-delivery an extraordinary loss, measured over the whole term of renewed fixture, was, in Lord Reid's words, "sufficiently likely to result from the breach of contract to make it proper to hold that the loss flowed naturally from the breach or that loss of that kind should have been within [the defaulting party's] contemplation". Lord Mustill's dictum in *The Gregos* indicates that that would not have been the common intention of reasonable contracting parties, and I respectfully agree.'

The significance of assumption of risk in relation to the application of *Hadley v Baxendale* was considered by Beazley JA in *Stuart Pty Ltd v Condor Commercial Insulation Pty Ltd.*[207]

In that case the plaintiff was a construction company. It held a contract with the Commonwealth for the replacement of wool insulation in residential dwellings under the Sydney Airport flight path. The contract was part of the Commonwealth's Sydney Airport Noise Insulation Program (SANIP).

There were 932 properties to be insulated.

The plaintiff subcontracted the insulation work to the defendant. Relevantly, a separate contract in the form of a purchase order was entered into between the plaintiff and defendant for each property to be insulated. On 28 January 1999 the plaintiff issued a purchase order in respect of work to be carried out on a property in Marrickville. The work was commenced on 9 February 1999.

On 27 July 1999 a fire broke out in the property. It was established that the fire was caused by the negligence of an employee of the defendant who, contrary to instructions, placed insulation material over a downlight. It over heated and ignited. The property was badly damaged.

Immediately following the fire the Commonwealth suspended the assignment of further work to the plaintiff pending an audit. Upon receipt of the audit report the Commonwealth terminated its contract with the plaintiff. In a claim for damages for breach of contract the plaintiff sought recovery of loss of profit based on the termination of the SANIP Contract with the Commonwealth.

The primary judge held that the damages claimed were too remote.

Beazley JA in delivering the principal judgment in the Court of Appeal embarked upon a detailed analysis of *Hadley v Baxendale*. In relation to the so-called "second limb" her Honour having referred to the observations of Diplock LJ in *Robophone Facilities Ltd v Blank*[208] noted:

'[54] His Lordship recognised that the rationale for a defendant's liability under the "second rule" in *Hadley v Baxendale* is an implied undertaking by the defendant to the plaintiff to bear such loss. Actual knowledge of the special circumstances is relevant as one of the factors from which this undertaking can be implied. His Lordship also considered that in order to be liable under the second rule, the defendant should have acquired this knowledge from the plaintiff, or at least that he should know that the plaintiff knew that the defendant was possessed of it at the time the contract was entered into and so could reasonably foresee at that time that an enhanced loss was liable to result from a breach. His Lordship concluded that where both these factors are present, the defendant's conduct in entering into the contract without disclaiming liability for the foreseeable enhanced loss gives rise to the implication that the defendant undertakes to bear such loss.'

In relation to the appellant's submission that the primary judge should have made certain findings of fact, Beazley JA said:

'[79] The respondent pointed out that it was not aware of the terms of the contract between SANIP and the appellant. All that it knew was that the appellant had been successful in obtaining a contract for the carrying out of the insulation work. The respondent did not know what criteria SANIP used or intended to use for the purposes of allocating work, what work it proposed to allocate, what work had been allocated at the time that the contract for the insulation work at 98 Newington Road was entered into, or what was the likely future allocation of work. Indeed, even the appellant had no knowledge of these matters. The actual circumstances were that the appellant was but one of seven contractors who had been engaged to carry out the insulation work.

'[80] The respondent's submission on this is correct. The contract with SANIP was an entire contract in the sense that there was one contract for the carrying out of such work as SANIP allocated to the appellant. However, there was no contractual obligation on SANIP to allocate any work or any percentage of work to the appellant. The evidence sup-ported an inference that the appellant wished to obtain as much work as

possible under its contract with SANIP. That is quite different from saying that the respondent was aware that the appellant wished to procure an "increased allocation" of houses.'

Her Honour then proceeded to consider the basis upon which the plaintiff would have an entitlement to damages and said:

'[88] In deciding whether the appellant has established an entitlement to damages under the second limb, the following matters require determination. The first is whether it could be said that the loss was within the reasonable contemplation of the parties. In this case, that question is, for the most part, although not solely, determined by having regard to the question whether the respondent was aware of special circumstances such as to enable the court to conclude that it would have been in the reasonable contemplation of both parties that the appellant would lose the SANIP contract if the respondent breached its contract with the appellant: see *Robophone* at 1447-1448. The second relates to the event that gave rise to the loss: see *Czarnikow v Koufos* at 385.

'[92] The question as to whether damage or loss would reasonably have been in the contemplation of the parties is an evaluative process. In this case, I am of the opinion that it would reasonably have been in the contemplation of the parties that if the respondent failed to perform the work in a good and workmanlike manner as required under its contract with the appellant, the appellant would most likely have replaced the respondent with another contractor. In that case, it may have suffered loss due to a delay in being able to find a new contractor. It may also have suffered loss because a new contractor may have quoted higher prices than those agreed between the appellant and the respondent so that the appellant's profit margin on each house was thereby reduced. Such losses would likely to have been recoverable under the second limb of *Hadley v Baxendale.* In my opinion, however, the loss in fact claimed is not one the risk of which the respondent is likely to have undertaken, even if it was aware of special circumstances relating to the contract.'

Her Honour concluded:

'[94] In this case the "special circumstance" is the appellant's contract with SANIP. The respondent knew of that contract and knew that the appellant expected it to be profitable and that there were a large number of houses upon which work was to be undertaken. Apart from that however, the respondent did not know its terms. On the approach taken in *Robophone,* that may be sufficient for the Court to infer or presume that the respondent undertook the risk, unless it could be established that there were other factors upon which any such inference could be rebutted.

'[95] In this case, there are two particular considerations that are relevant to the 'rebuttal' of any such inference. First, the supervision of the works was the responsibility of the appellant in the way I have explained above. The respondent did not undertake any contractual responsibility to supervise the work on behalf of the appellant and it was not paid for the supervision of the work. The only "supervision" undertaken by Condor was that Mr Kirkness, as the respondents' project manager, was required to ensure that the work was properly performed. That was work undertaken for Condor, as I have already said.

'[96] Secondly, under its own contract with SANIP, the appellant remained responsible for the works. The loss claimed in this case is not a loss that arises directly as between the appellant and respondent. Rather, the loss relates to a contract between SANIP and the appellant allegedly caused by the breach of the contract between the appellant and the respondent. In circumstances where, under its contract with SANIP, the appellant remained responsible for all work carried out by sub-contractors, I am of the opinion that it would not have been in the reasonable contemplation of the respondent that poor workmanship on its part would result in the loss of the appellant's entire contract with SANIP. I also doubt that it would have been in the appellant's own reasonable contemplation.

'[97] Further, the contract amount for the individual contracts between the appellant and the respondent was quite small and the respondent had no contractual right to any ongoing relationship. Rather, each house was the subject of a separate contract, although at the time that this contract was entered into, the respondent did have an expectation of being the beneficiary of the work allocated to the appellant by SANIP. However, in the absence of any contractual right to such work, and where each job involved a contract price of about $10,000, I consider that the contract price was so out of proportion to the risk of being liable for damages for the loss of the appellant's contract with SANIP not to be within the reasonable contemplation of the parties.'

Assumption of responsibility as the underpinning principle informing the boundaries of recoverable loss was also referred to by Campbell JA in *Robb Evans of Robb Evans & Associates v European Bank Ltd.*[209]

His Honour having referred to the rule in *Hadley v Baxendale* continued:

'[58] One can see why it is just that principles like these should apply to the quantification of damages for breach of contract. When A promises B that some future event will occur, both parties would reasonably understand that A is undertaking the risk of that event not occurring. But the scope of the risk that A is undertaking needs to be construed in the same way as any other aspect of a contract is construed, namely objectively in light of surrounding circumstances known to both parties: ... It is also consonant with A having undertaken a risk construed in that way that, if the event does not occur, A will be liable for those consequences of the breach that arise according to the usual course of things from the breach, and also for those consequences of the breach that would reasonably be supposed to be in the contemplation of both parties at the time they made the contract. However, damages that do not meet those criteria are

beyond the scope of the risk that A undertook, and hence ought not be recoverable. That losses recoverable for breach of contract are those for which the party in breach has assumed responsibility has recently been reiterated in *Transfield Shipping Inc v Mercator Shipping Inc* [2008] UKHL48; [2009]1 AC 61 ...'

However, in *Sylvia Shipping Co Limited v Progress Bulk Carriers Limited*[210] the English courts returned to orthodoxy in their approach to *Hadley v Baxendale.* Importantly, Hamblen J observed:

'[40] In my judgment, the decision in *The Achileas* results in an amalgam of the orthodox and the broader approach. The orthodox approach remains the general test of remoteness applicable in the great majority of cases. However, there may be "unusual" cases, such as *The Achilleas,* in which the context, surrounding circumstances or general understanding in the relevant market make it necessary specifically to consider whether there has been an assumption of responsibility. This is most likely to be in those relevantly rare cases where the application of the general test leads or may lead to an unquantifiable, unpredictable, uncontrollable or disproportionate liability or where there is clear evidence that such a liability will be contrary to market understanding and expectations.'

His Honour further noted:

'[48] The orthodox approach therefore remains the "standard rule" and it is only in relatively unusual cases, such as The Achilleas itself, where a consideration of assumption of responsibility may be required.

'[49] In my judgment, it is important that it be made clear that there is no new generally applicable legal test of remoteness in damages.'

3 EXPECTATION AND RELIANCE LOSS

In their discourse on expectation loss in *The Commonwealth v Amann Aviation Pty Limited,*[211] Mason CJ and Dawson J explored the relationship between expectation and reliance loss. Their Honours noted at 81:

'The expression "damages for loss of profits" should not be understood as carrying with it the implication that no damages are recoverable either in the case of a contract in which no net profit would have been generated or in the case of a contract in which the amount of profit cannot be demonstrated. It would be an invitation to the repudiation of contractual obligations if the law were to deny to an innocent plaintiff the right to recoupment by an award of damages of expenditure justifiably incurred for the purpose of discharging contractual obligations simply on the ground that the contract breached would not have been or could not be shown to have been profitable. If the performance of a contract would have resulted in a plaintiff, while not making a profit, nevertheless recovering costs incurred in the course of performing contractual obligations, then that plaintiff is entitled to recover damages in an amount equal to those costs in accordance with *Robinson v Harman,* as those costs would have been recovered had the contract been fully performed. Similarly, where it is not possible for a plaintiff to demonstrate whether or to what extent the performance of a contract would have resulted in a profit for the plaintiff, it will be open to a plaintiff to seek to recoup expenses incurred, damages in such a case being described as reliance damages or damages for wasted expenditure.'

The expenditure referred to now falls under the general rubric of reliance loss.

The principles informing recovery of reliance loss were first authoritatively considered by the High Court in the celebrated decision of *McRae v Commonwealth Disposals Commission.*[212]

The case involved a contract between the plaintiffs and the Commonwealth for the salvage of a sunken oil tanker. It was established that no such tanker existed. Following argument, the High Court held that the Commonwealth breached an implied warranty that the tanker existed at the specified location. In an action for damages for breach of contract the plaintiffs sought recovery of wasted expenditure rather than loss of profit on the basis that it was impossible to value a non-existent tanker for the purpose of a loss of profit claim. The defendant put that there was insufficient evidence to support the conclusion that even if the tanker had existed the plaintiffs would have recouped their expenditure in performing the contract. In a critical passage Dixon and Fullagar JJ noted at 414:

'But it is really, we think, fallacious. If we regard the case as a simple and normal case of breach by non-delivery, the plaintiffs have no starting-point. The burden of proof is on them, and they cannot establish that they have suffered any damage unless they can show that a tanker delivered in performance of the contract would have had some value, and this they cannot show. But when the contract alleged is a contract that there was a tanker in a particular place, and the breach assigned is that there was no tanker there, and the damages claimed are measured by expenditure incurred on the faith of the promise that there was a tanker in that place, the plaintiffs are in a very different position. They have now a starting-point.

'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. The burden is now thrown on the Commission of establishing that, if there had been a tanker, the expense incurred would equally have been wasted. This, of course, the Commission cannot establish. The fact is that the impossibility of assessing damages on the basis of a comparison between what was promised and what was delivered arises not because what was promised was valueless but because it is impossible to value a non-existent thing.'

Turning to *Amann Aviation.*

A contract between the Commonwealth and the plaintiff required the plaintiff to provide aerial surveillance services for a term of three years. It was acknowledged that a contract for this term would be unprofitable. However, the plaintiff expected to secure a renewal for a further three year period in light of its advantageous position as the incumbent provider. Upon a wrongful repudiation by the Commonwealth the plaintiff sought recovery of wasted expenditure.

The High Court in confirming the decision of the court below applied the presumption established by McRae.

Relevantly, Mason CJ and Dawson J noted at 94:

'It follows that we consider that the Full Court was correct in taking into account the prospect of renewal of the contract as a factor relevant to the assessment of damages. The consequence of this conclusion, in view of the onus cast upon the Commonwealth as the party in breach, is that the Commonwealth must demonstrate that the value to Amann of the prospect of renewal of the contract when combined with those expenses that would have been recovered by way of gross receipts was less than the total expenses to be incurred by Amann in the performance of its contractual obligations. If the Commonwealth was able to demonstrate that this would have been the result, had the contract been fully performed, then, in conformity with Robinson v Harman, Amann would not be entitled to all of its expenditure incurred in reliance on the Commonwealth's promise to perform and wasted as a result of the Commonwealth's breach. The Commonwealth was unable, however, to demonstrate this and so discharge the onus. Accordingly, the presumption that Amann would not have entered into a contract in which it would not recover the value of its expenditure incurred remains undisturbed. We agree with the Full Court's conclusion that Amann was entitled to recover as damages an amount commensurate with what it had expended in reliance upon the Commonwealth's promise to perform its contractual obligations.'

And Deane J noted at 126:

'In a case where a plaintiff has incurred expenditure either in procuring the contract or in its performance but it is impossible or difficult to establish the value of any benefits which the plaintiff would have derived from performance by the defendant, considerations of justice dictate that the plaintiff may rely on a presumption that the value of those benefits would have been at least equal to the total detriment which has been or would have been sustained by the plaintiff in doing whatever was reasonably necessary to procure and perform the contract (see, eg, McRae, at 414; *Holt v United Security Life Ins and Trust Co* (1909) 72 Atlantic Reporter 301, at 305-306; *L Albert and Son v Armstrong Rubber Co* (1949) 178 F 2d 182, at 188-189). In my view, the rational basis of that presumption is that that total detriment represents what would reasonably have been in the contemplation of the parties themselves as the cost to the plaintiff of full performance by the defendant (sic) and constitutes some evidence, in proceedings between them, of the value of the total benefits which would have been derived by the plaintiff from such performance. It follows from it that, at least in a case where proof of value is impossible or difficult, it is presumed in the plaintiffs favour that the future net benefits (ie, excess of future benefit over future detriment) which would have been derived from performance of the contract would have been of a value sufficient to recoup the past net expenditure reasonably incurred in procuring or performing it. Where that presumption is operative, it enables the recovery by a plaintiff of what are commonly referred to as "reliance damages", that is to say, damages equivalent to the wasted expenditure which has been reasonably incurred in reliance upon the assumption that the contractual promises of the defendant would be honoured. The presumption will be rebutted if it be self-evident or established that the plaintiff would have derived no financial or other benefit from performance of the contract or that any financial or other benefit which would have been derived from future performance would not have been sufficient in value to counterbalance the past expenditure.'

4 THE RELATIONSHIP BETWEEN RESTITUTION AND DAMAGES FOR BREACH OF CONTRACT

The relationship between the remedy of restitution and compensatory damages and their combination in one action is explained by the High Court in *Baltic Shipping Company v Dillon.*[213]

I turn to the facts.

Mrs Dillon purchased a 14 day cruise on the defendant's vessel the *Mikhail Lermontov* for which she paid $2,205. On the ninth day of the cruise the ship struck a shoal on the north-east tip of the South Island of New Zealand. The ship was holed and sunk. After the shipwreck the defendant company refunded some $787 as a "full refund ... of the unused portion of the passage money".

After settlement discussions with the company, Mrs Dillon signed a deed of release and received a further $4,700 in compensation.

In subsequent proceedings by Mrs Dillon, the deed of release was declared by the primary judge to be void under the Contracts Review Act 1980 (NSW). In those proceedings, Mrs Dillon was held entitled to restitution of the balance of the fare which she paid, together with compensatory damages for personal injuries and disappointment and distress.

In an appeal to the High Court, Baltic Shipping contended that Mrs Dillon was not entitled to pursue both a claim for restitution of the consideration paid under a contract and a claim for damages for breach of that contract.

In allowing Baltic Shipping's appeal on the restitution claim the High Court addressed two issues of fundamental importance.

First, in what circumstances may a contracting party recover a pre-payment on a failure of consideration?

Secondly, whether a restitutionary claim may be combined with a claim for damages for breach of contract?

In relation to the first issue Mason CJ said at 350:

'When, however, an innocent party seeks to recover money paid in advance under a contract in expectation of the entire performance by the contractbreaker of its obligations under the contract and the contractbreaker renders an incomplete performance, in general, the innocent party cannot recover unless there has been a total failure of consideration. If the incomplete performance results in the innocent party receiving and retaining any substantial part of the benefit expected under the contract, there will not be a total failure of consideration.

'In the context of the recovery of money paid on the footing that there has been a total failure of consideration, it is the performance of the defendant's promise, not the promise itself, which is the relevant consideration. In that context, the receipt and retention by the plaintiff of any part of the bargained for benefit will preclude recovery, unless the contract otherwise provides or the circumstances give rise to a fresh contract.'

And his Honour concluded on the facts at 353:

'The consequence of the respondent's enjoyment of the benefits provided under the contract during the first eight full days of the cruise is that the failure of consideration was partial, not total. I do not understand how, viewed from the perspective of failure of consideration, the enjoyment of those benefits was "entirely negated by the catastrophe which occurred upon departure from Picton", to repeat the words of the primary judge.

'Nor is there any acceptable foundation for holding that the advance payment of the cruise fare created in the appellant no more than a right to retain the payment conditional upon its complete performance of its entire obligations under the contract. As the contract called for performance by the appellant of its contractual obligations from the very commencement of the voyage and continuously thereafter, the advance payment should be regarded as the provision of consideration for each and every substantial benefit expected under the contract. It would not be reasonable to treat the appellant's right to retain the fare as conditional upon complete performance when the appellant is under a liability to provide substantial benefits to the respondent during the course of the voyage.'

In their joint reasons, Deane and Dawson JJ said at 375:

'The present case is not, however, one in which a party who has provided part only of the promised consideration seeks to recover part of the agreed purchase price. In the present case, it is the promisee, Mrs Dillon, who seeks to recover the whole of a prepaid purchase price on the ground that the consideration for which it was paid has wholly failed. Mrs Dillon does not rely upon any provision of the contract between Baltic and herself under which Baltic was obliged to refund the whole of the fare in the events which happened. There was no such contractual provision. The basis of her claim is the obligation of restitution which the law *prima facie* imposes upon the recipient of a payment made under a contract which has become "abortive for any reason not involving fault on the part of the plaintiff" in a case "where the consideration, if entire, has entirely failed, or where, if it is severable, it has entirely failed as to the severable residue". Such a claim is not a claim on the contract. Its historical antecedent in terms of forms of action is the old indebitatus count for money had and received to the use of the plaintiff. Its modern substantive categorization is as an action in unjust enrichment. In other words, the receipt of a payment of money for a consideration which wholly fails "is one of the categories of case in which the facts give rise to a prima facie obligation to make restitution ... to the person who has sustained the countervailing detriment".'

Their Honours concluded at 379:

'In circumstances where Mrs Dillon accepted and enjoyed the major portion of the pleasure cruise, however, there was no complete failure of the consideration for which she paid the fare. The catastrophe of the shipwreck and its consequences undoubtedly outweighed the benefits of the first eight complete days. It did not, however, alter the fact that those benefits, which were of real value, had been provided, accepted and enjoyed.'

Turning to the second issue, namely, the combination of a restitutionary claim with a claim of damages for breach of contract.

Relevantly, Mason CJ said at 359:

'... the earlier cases support the view expressed by Corbin and Treitel that full damages and complete restitution will not be given for the same breach of contract. There are several reasons. First, restitution of the contractual consideration removes, at least notionally, the basis on which the plaintiff is entitled to call on the defendant to perform his or her contractual obligations. More particularly, the continued retention by the defendant is regarded, in the language of Lord Mansfield, as "against conscience" or, in the modern terminology, as an unjust enrichment of the defendant because the condition upon which it was paid, namely, performance by the defendant may not have occurred. But, equally, that performance, for deficiencies in which damages are sought, was conditional on payment by the plaintiff. Recovery of the money paid destroys performance of that condition. Secondly, the plaintiff will almost always be protected by an award of damages for breach of contract, which in appropriate cases will include an amount for substitute performance or an amount representing the plaintiff's reliance loss. It should be noted that nothing said here is inconsistent with *McRae v Commonwealth Disposals Commission*.'

And on the same point, Deane and Dawson JJ state at 379:

'There is a further reason, which would appear not to have been raised in argument in the courts below, why Mrs Dillon's action for restitution of the fare paid to Baltic must fail. It is that she has sought and obtained an order against Baltic for compensatory damages for Baltic's failure to perform its contractual promises to her. In particular, she has received a refund of a proportionate part of the fare and has obtained and will retain (see below) the benefit of an award of damages for the disappoint-

ment and distress which she sustained by reason of Baltic's failure to provide her with the full pleasure cruise which it promised to provide. In these circumstances, Mrs Dillon has indirectly enforced, and indirectly obtained the benefit of, Baltic's contractual promises.

'Ordinarily, as has been seen, "when one is considering the law of failure of consideration and of the ... right to recover money on that ground, it is ... not the promise which is referred to as the consideration, but the performance of the promise". That statement has nothing to say, however, to the situation which exists when the promisee has sought and obtained an award of full compensatory damages for the failure to perform the promise. In that situation, the damages are awarded and received as full compensation for non-performance or breach of the promise and represent the indirect fruits of the promise. That being so, it would be quite wrong to say either that the only quid pro quo which has been obtained for the payment by the promisee is the bare promise or that the promise and the recovery of compensatory damages for its breach can realistically be seen as representing no consideration at all.'

5 RECOVERY OF CONSIDERATION PAID AS WASTED EXPENDITURE

The decision of the Queensland Court of Appeal in *Zahedpur v Idameneo (No 123) Pty Ltd*[214] provides an illustration of the practical effect of the High Court decisions in *Baltic Shipping Company v Dillon*[215] and *The Commonwealth v Amann Aviation Pty Limited.*[216]

I turn to the facts.

On 18 December 2009 Dr Zahedpur and the respondent company entered into two agreements. One was described as a Sale of Practice Deed (Sale Deed) and the other a Practice Services Deed (Services Deed). Under the Sale Deed Dr Zahedpur agreed to sell his Gladstone Medical Practice to the respondent for $500,000. Under the Services Deed (as amended) Dr Zahedpur agreed to commence as a GP at the respondent's medical centre at Springfield in Brisbane. The respondent on its part agreed to provide certain services and facilities to Dr Zahedpur including, for example, space at the Centre, administrative services, equipment and telephones.

The commencement date of the Services Deed was 29 May 2010. The term was five years.

On 20 February 2012, Dr Zahedpur abandoned the respondent's Centre complaining that the respondent had not adequately provided the agreed services.

On 1 July 2013 another GP joined the Springfield Centre.

Earlier, by letter dated 15 March 2012, the respondent by notice terminated both the Sale Deed and the Services Deed.

In these proceedings the respondent initially claimed damages for breach of contract and further, alternatively, restitution of part of the $500,000 which it had paid under the Sale Deed.

However, the respondent did not persist with its restitution claim. Relevantly, Philip McMurdo JA said:

'[30] The respondent filed no notice of contention seeking to rely upon its alternative claim in restitution and did not seek to pursue that claim in its argument in this court. That is unsurprising, because there was only a partial failure of the agreed consideration for its payment of the price under the Sale Deed. The respondent did receive some of the benefits for which that payment was made, at least by the appellant practising from the respondent's centres for a time before his departure in 2012. The payment of $500,000 was not apportioned by the Sale Deed between different benefits to be received by the respondent. Nor was this a case where it could be said that the Sale Deed, upon its proper interpretation, entitled the appellant to retain the payment only conditionally upon the performance of his obligations to work at the respondent's centres for the entirety of the agreed term. The respondent's recovery of the price, in whole or in part, by a claim in restitution was precluded by its having received part of the benefit for which it bargained. However, as I will discuss, the payment was relevant in the assessment of damages for breach of contract.'

In respect of the damages claim his Honour noted:

'[53] The respondent was to be awarded damages which, so far as possible, would place it in the same position as if the contracts had been performed. That required a consideration of a hypothesis: namely the operation at the Springfield centre in the relevant period with the services not only of the doctors who did work there but also those of the appellant, working according to the contracts. In that event, would the respondent's income from the centre have been higher than its actual income, and if so by what amount?

'[54] If the respondent was to prove that its income would have been higher, it had to prove that the demand for services at the centre would have been higher than that which was met by the doctors who did work there. The respondent sought to prove this in two ways. The first was by evidence that there was an unsatisfied demand, in the sense that the doctors who did work at the centre were unable to service all of the patients who sought treatment there. The second was by evidence to the effect that an increase in the number of doctors working at any of the respondent's centres invariably results in an increase in the demand for that centre's services. The effect of this evidence was that, subject to the limitation of the number of consulting rooms and other facilities at a centre, the potential income from a centre could always be increased by engaging another doctor.'

However, his Honour having considered the evidence as to patient demand concluded that a loss of profit claim was not available to the respondent. In this context his Honour noted:

'[73] The respondent thereby proved that during the period for which it was awarded damages, it suffered some loss, in that the presence of the appellant at the centre, working according to the contracts, would have yielded some additional profit. However, without knowing the extent to which the existing demand at the centre was unsatisfied, or the extent to which an addi-

tional doctor would have increased that demand, the profits lost to the respondent could not be fairly quantified. Therefore the respondent did not prove that there would have been a sufficient level of demand for services, above that which was satisfied by the other doctors, to yield the further profits by which the respondent's award was quantified.'

The failure of the respondent to recover loss of profit did not, however, mean that the respondent recovered nothing. Applying the principles in *The Commonwealth v Amann Aviation,* the Court of Appeal held that the respondent was entitled to recover wasted expenditure. The outcome is explained by Philip McMurdo JA. His Honour said:

'[74] But it does not follow that the respondent, having suffered a loss, was not entitled to a substantial award of damages. Where the amount of profit from the performance of the contract cannot be demonstrated, the innocent party can still recover damages assessed by reference to the expenditure incurred by that party in its performance of the contract ...

'[75] Further, the law assumes that from the defendant's due performance of the contract the plaintiff would have recovered at least its expenses of its own performance unless the defendant proves otherwise, because it is presumed that "a party would not enter into a contract in which its costs were not recoverable".'

His Honour concluded:

'[76] The relevant expenditure here was the sum of $500,000 (and GST) paid to the appellant pursuant to the Sale Deed. This was a payment made, on the face of the contracts, to secure two kinds of benefits. The first was the acquisition of what was said to be the goodwill in the appellant's practice at Gladstone. But in truth, this was a payment only for the second kind of benefit, which was the appellant's services over a five year term ...

'[77] The trial judge considered that the respondent's loss was confined to the period before another doctor was engaged in July 2013. The correctness of that view need not be considered. It may or may not have been correct if damages were to be assessed, as they were by his Honour, upon the basis of a certain loss of profit. Because, in my view, the amount of lost profits could not be fairly quantified, it was and is open to assess the respondent's loss by reference to its wasted expenditure. For its expenditure of $500,000, it had the benefit of the appellant's performance from July 2010 to February 2012, a period of about 19 months. Most of the intended benefit from the payment was not received by the respondent and absent evidence to the contrary, it could be assumed that the respondent suffered a loss of the order of more than half of that payment. There was no evidence which proved otherwise, except perhaps for the evidence showing the low demand at the centre in the year to 30 June 2015. Even disregarding that year, there remained at least 28 months for which the respondent did not have the benefit of its expenditure which equated to $100,000 per year.

'[78] There was no impediment to the quantification of damages upon this basis from the fact that the respondent pleaded and argued a case for damages quantified by lost profits. A plaintiff in the respondent's position is not put to any election between the two methods of assessment. The facts relevant to an assessment upon the basis of wasted expenditure were before the court because of the related, although distinct, claim for the recovery of effectively the same proportion of the $500,000 upon a restitutionary basis.

6 DATE FOR ASSESSMENT

6.1 General principles

Damages for breach of contract are ordinarily assessed at the date of breach. This, however, is the general rule and circumstances may require assessment to be made at some other date.

In *Johnson v Perez*[217] the members of the High Court made certain observations on this issue. Mason CJ noted at 355:

'There is a general rule that damages for torts or breach of contract are assessed as at the date of breach or when the cause of action arises. But this rule is not universal; it must give way in particular cases to solutions best adapted to giving an injured plaintiff that amount in damages which will most fairly compensate him for the wrong he has suffered ...

'The general rule that damages are assessed as at the date of breach or when the cause of action arose has been applied more uniformly in contract than in tort and for good reason. But even in contract cases courts depart from the general rule whenever it is necessary to do so in the interests of justice.'

In the decision of the Western Australian Court of Appeal in *Luxer Holdings Pty Ltd v Glentham Pty Ltd (supra),* the court examined the appropriate date for assessment of loss of bargain damages on termination of a lease. Buss JA noted:

'[33] Although damages for breach of contract are ordinarily to be assessed as at the date of the breach ... the critical date for the assessment of loss of bargain damages is the date on which the innocent party terminates .... Accordingly, where a lessor terminates the lease agreement for breach of an essential term or for repudiation, loss of bargain damages are ordinarily to be assessed as at the date of termination.'

Later his Honour noted:

'[35] The rule that a lessor's loss of bargain damages are ordinarily to be assessed as at the date of termination does not mean that evidence is excluded of events occurring after that date. Evidence of subsequent events which are relevant to the assessment process may be taken into account. For example, subsequent events may be relevant to the value of the lost bargain or whether the lessor had mitigated its damage or not.'

The relevant date for the assessment of damages was also considered by the House of Lords in *Golden Strait Corporation v Nippon Yusen Kubishika Kaisha.*[218]

The case involved the assessment of damages following repudiation of a charterparty. As noted by Lord Scott at 379:

'My Lords, the answer to the question at issue must depend on principles of the law of contract. It is true that the context in

this case is a charterparty, a commercial contract. But the contractual principles of the common law relating to the assessment of damages are no different for charterparties, or for commercial contracts in general, than for contracts which do not bear that description. The fundamental principle governing the quantum of damages for breach of contract is long established and not in dispute. The damages should compensate the victim of the breach for the loss of his contractual bargain.'

In December 2001 the charterers repudiated a charterparty due to run until 2005. The charterparty contained an express provision that both the owners and the charterers should have the right to cancel the charter if war or hostilities were to break out between any two or more of a number of countries including the United States of America, the United Kingdom and Iraq.

The owners accepted the repudiation and their claim for compensation went to arbitration.

However, before the arbitrator had assessed damages the outbreak of the Second Gulf War in March 2003 had occurred. The charterers submitted that damages should be assessed by reference to the period 17 December 2001 to March 2003 when the contract would have come to an end if it had still been on foot. The owner disagreed.

Although the owners accepted that the possibility of war occurring could be taken into account the actual occurrence of an event after 17 December 2001 should not be taken into account.

The House of Lords by a majority dismissed the owner's appeal and concluded that the assessment of damages had to bring to account the occurrence of the Second Gulf War.

Lord Scott noted at 380:

'If a contract for performance over a period has come to an end by reason of a repudiatory breach but might, if it had remained on foot, have terminated early on the occurrence of a particular event, the chance of that event happening must, it is agreed, be taken into account in an assessment of the damages payable for the breach. And if it is certain that the event will happen, the damages must be assessed on that footing. In *Maredelanto Cia Naviera SA v Bergbau-Handel GmbH, The Mihalis Angelos* [1970] 3 All ER 125 at 142, [1971]1 QB 164 at 210, Megaw U referred to events "predestined to happen". He said:

'" ... if it can be shown that those events were, at the date of acceptance of the repudiation, predestined to happen, then ... the damages which [the claimant] can recover are not more than the true value, if any, of the rights which he has lost, having regard to those predestined events."

'Another way of putting the point being made by Megaw LJ is that the claimant is entitled to the benefit, expressed in money, of the contractual rights he has lost, but not to the benefit of more valuable contractual rights than those he has lost. In *Wertheim v Chicoutini Pulp Co* [1911] AC 301 at 307, [1908-10] All ER Rep 707 at 711, Lord Atkinson referred to-

'"the general intention of the law that, in giving damages for breach of contract, the party complaining should, so far as it can be done by money, be placed in the same position as he would have been in if the contract had been performed ...."

'And, in relation to a claim by a purchaser for damages for late delivery of goods where the purchaser had, after the late delivery, sold the goods for a higher price than that prevailing in the market on the date of delivery, he observed ([1911] AC 301 at 308, [1908-10] All ER Rep 707 at 711) that:

'"... the loss he sustains must be measured by that price, unless he is, against all justice, to be permitted to make a profit by the breach of contract, be compensated for a loss he never suffered, and be put, as far as money can do it, not in the same position in which he would have been if the contract had been performed, but in a much better position."

'The result contended for by the appellant in the present case is, to my mind, similar to that contemplated by Lord Atkinson in the passage last cited. If the charterparty had not been repudiated and had remained on foot, it would have been terminated by the charterers in or shortly after March 2003 when the second Gulf war triggered the cl 33 termination option. But the owners are claiming damages up to 6 December 2005 on the footing, now known to be false, that the charterparty would have continued until then. It is contended that because the charterers' repudiation and its acceptance by the owners preceded the March 2003 event, the rule requiring damages for breach of contract to be assessed at the date of breach requires that event to be ignored.

'That contention, in my opinion, attributes to the assessment of damages at the date of breach rule an inflexibility which is inconsistent both with principle and with the authorities. The underlying principle is that the victim of a breach of contract is entitled to damages representing the value of the contractual benefit to which he was entitled but of which he has been deprived. He is entitled to be put in the same position, so far as money can do it, as if the contract had been performed.'

In relation to the application of the 'date of breach rule' to sale of goods contracts Lord Scott distinguished between a one-off sale and a supply over an extended period. His Lordship went on to state at 381 and 382:

'The assessment at the date of breach rule is particularly apt to cater for cases where a contract for the sale of goods in respect of which there is a market has been repudiated. The loss caused by the breach to the seller or the buyer, as the case may be, can be measured by the difference between the contract price and the market price at the time of the breach. The seller can re-sell his goods in the market. The buyer can buy substitute goods in the market. Thereby the loss caused by the breach can be fixed. But even here some period must usually be allowed to enable the necessary arrangements for the substitute sale or purchase to be made (see, eg, *Kaines (UK) Ltd v Osterreichische Warrenhandelsgesellschaft mbH* [1993] 2 Lloyd's Rep 1). The

relevant market price for the purpose of assessing the quantum of the recoverable loss will be the market price at the expiration of that period.

'In cases, however, where the contract for sale of goods is not simply a contract for a one-off sale, but is a contract for the supply of goods over some specified period, the application of the general rule may not be in the least apt. Take the case of a three-year contract for the supply of goods and a repudiatory breach of the contract at the end of the first year. The breach is accepted and damages are claimed but before the assessment of the damages an event occurs that, if it had occurred while the contract was still on foot, would have been a frustrating event terminating the contract, eg, legislation prohibiting any sale of the goods. The contractual benefit of which the victim of the breach of contract had been deprived by the breach would not have extended beyond the date of the frustrating event. So on what principled basis could the victim claim compensation attributable to a loss of contractual benefit after that date? Any rule that required damages attributable to that period to be paid would be inconsistent with the overriding compensatory principle on which awards of contractual damages ought to be based.'

The majority view in *Golden Strait* was approved by the New South Wales Court of Appeal in *McCrohon v Harith*[219] McColl JA (Campbell and Handley JAA agreeing) observed:

'[59] Accordingly, Lord Scott rejected (at [32]) the owners' contention, describing it as attributing "to the assessment of damages at the date of breach rule an inflexibility which is inconsistent both with principle and with the authorities." While his Lordship accepted the date of breach rule usually put the victim of a breach of contract in the same position, so far as money could do it, as if the contract had been performed (the "compensatory principle"), his Lordship did not accept that that was universally so. In his view (at [38]) the owners' argument offended the compensatory principle, because they were seeking compensation exceeding the value of the contractual benefits of which they were deprived. This was because their case required "the assessor to speculate about what might happen over the period 17 December 2001 to 6 December 2005 regarding the occurrence of a cl 33 event and to shut his eyes to the actual happening of a cl 33 event in March 2003".'

In respect of the general rule her Honour noted:

'[56] Accordingly, the general rule will yield if, at the time damages are assessed, the court is aware of new and material facts relevant to the assessment because courts prefers actual facts to speculation, prophecies, conjecture and guessing: *Willis v Commonwealth* [1946] HCA 22 ; (1946) 73 CLR 105 (at 109) per Latham CJ; *Bwllfa and Merthyr Dare Steam Collieries (1891) v Pontypridd Waterworks Co [1903]* AC 426 (at 431) per Lord MacNaghten, cited with approval by Wilson, Dawson, Toohey and Gaudron JJ in *Nikolaou v Papasavas Phillips & Co* [1989] HCA 11; (1989) 166 CLR 394 (at 404); *Kizbeau Pty Ltd v WG& B Pty Ltd* [1995] HCA 4 ; (1995) 184 CLR 281 (at 293-295) (Full Court); *HTW Valuers (Central Qld) Pty Ltd v Astonland Pty Ltd* (at [38]-[40]) (Full Court).'

In *Macourt v Clark,*[220] Tobias AJA noted:

'[61] To the authorities referred to by the primary judge I would add at this point a reference to the judgment of McColl JA, with whom Campbell JA and Handley AJA agreed, in *McCrohon v Harith* [2010] NSWCA 67 at [52]-[56]. Relevantly, for the present case, her Honour observed at [53] that:

'"[a]n injured plaintiff is not entitled to make a profit in an action in ... contract; in other words, to be awarded damages for a loss never suffered or ... to be placed in a superior position to that which he or she would have been in had the contract been performed."

'[62] At [54] her Honour noted that the date of breach rule is not rigid and will yield to some other date if necessary to provide adequate compensation. After referring to *Johnson; Golden Strait* and *Gagner* she concluded at [56] that:

'"... the general rule will yield if, at the time damages are assessed, the court is aware of new and material facts relevant to the assessment because courts prefers actual facts to speculation, prophecies, conjecture and guessing."'

7 MITIGATION OF LOSS

7.1 Some fundamental principles

• The onus is on the defendant to show that some of what is being claimed could have been avoided. In the context of a damages claim on termination of a lease, Buss JA in *Luxer Holdings Pty Ltd v Glentham Pty Ltd*[221] noted:

'[41] There is a clearly established conceptual difference between the measure of damages, on the one hand, and the doctrine of mitigation, on the other. The onus is on the lessor to prove, according to the applicable measure, that it has suffered damage. But the onus is on the lessee to prove that the lessor has failed to take reasonable steps to mitigate its damage, and to demonstrate the extent to which there has been a failure to mitigate.'

• In *Castle Constructions Pty Ltd v Fekala Pty Ltd*[222] Mason P cited with approval the following passage from the judgment of Heydon JA in *Sherson & Associates Pty Ltd v Bailey:*[223]

'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 War Services Homes Commissioner* (1923) 44 ALT 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 Priestly JA (emphasis added). Subject to the criterion of reasonableness, the plaintiff' "is completely free to act as he judges to be in his best interests": *The Soholt* [1983] 1 Lloyds 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, 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.

• In discussing the nature and significance of mitigation, Giles J in *Karacominakis v Big Country Developments Pty Ltd*[224] noted:

'[187] A plaintiff who acts unreasonably in failing to minimise his loss from the defendant's breach of contract will have his damages reduced to the extent to which, had he acted reasonably, his loss would have been less. *This is often misleadingly referred to as a duty to mitigate, although the plaintiff is not under a positive duty.* The plaintiff does not have to show that he has fulfilled his so-called duty, and the onus is on the defendant to show that he has not and the extent to which he has not .... Since the defendant is a wrongdoer, in determining whether the plaintiff had acted unreasonably a high standard of conduct will not be required, and the plaintiff will not be held to have acted unreasonably simply because the defendant can suggest other and more beneficial conduct if it was reasonable for the plaintiff to do what he did.' (emphasis added)

• The scope of mitigation was considered by the New South Wales Court of Appeal in *CJD Equipment Pty Limited v A&C Constructions Pty Limited.*[225]

This was a building case. The proprietor entered into a contract with the builder to construct works including a large building to contain offices, a showroom and workshops. The works also included the design and construction of a curtain wall.

The proprietor claimed that the internal and external slabs as constructed were inadequate for the known design loads and were also inadequate because joints had not been sealed to prevent entry of moisture. This caused the slabs to heave which led to substantial damage to the curtain wall.

The builder claimed that when heave was identified in October 2005 the proprietor should have sealed the joints between the slabs and should also have taken steps to ensure that further movement in the slabs did not impose further stress on the curtain wall.

The curtain wall was replaced. The trial judge concluded that it was a reasonable inference that if the recommended works had been carried out it would have been unnecessary to replace the curtain wall.

Handley AJA in delivering the principal judgment of the Court adopted the following statement of principle by Glass JA in *Munce v Vinidex Tubemakers Pty Ltd*:[226]

'There is authority of long standing which establishes an exception to the principle that the plaintiff bears the onus of proving all matters relating to damages. The exception relates to any disputed question which is truly a matter of mitigation of damages. In relation to questions properly so classified the defendant ... must not only introduce evidence that the plaintiff has failed to minimise his loss, but also persuade the jury that the balance of testimony favours this conclusion ... In the field of personal injury litigation, an issue of this kind will normally be raised by an allegation that some action on the part of the plaintiff would have reduced his damages, and that his failure to take such action is unreasonable. If a defendant so persuades the jury, it will then be their duty to assess the plaintiff's damages on the footing that he has taken the hypothetical action and been endowed with this hypothetical benefits.'

Relying on this guidance from Glass JA, Handley AJA concluded:

'[92] Damages for the builder's breach of contract must therefore be assessed on the basis that the proprietor "has taken the hypothetical action and been endowed with its hypothetical benefits".

'[93] Glass JA did not indicate whether the hypothetical benefits should be calculated on a gross or net basis. In other words must the hypothetical cost of the reasonable steps in mitigation be allowed when calculating the hypothetical benefits?

'[94] In my judgment the plaintiff must be allowed the cost of the reasonable hypothetical steps when calculating the hypothetical benefits. If the proprietor could have saved the cost of replacing the curtain wall in 2009 by spending $12,500 in 2005 its failure to do so only caused the further loss, it did not diminish the accrued loss that required it to spend $12,500.'

• In *Knott Investments Pty Ltd v Fulcher*[227] Muir JA (Holmes and Atkinson JJA agreeing) said:

'[44] The reasonableness of the conduct of a plaintiff in response to, or as a result of, a defendant's wrongful conduct is directly relevant to the question of whether the wrongful conduct has caused the plaintiff's loss.'

His Honour then went on to cite the following passage in the reasons for judgment of Murphy J in *Metal Fabrications (Vic) Pty Ltd v Kelcey:*[228]

'The respondents were under a duty only to act reasonably to mitigate their loss. This did not require them to chance their arm further, to risk any capital they might borrow too far or to take steps which would cause their financial ruin, if they failed: see *Payzu v Saunders* [1919] 2 KB 581; *Lesters Leather & Skin Co v Home and Overseas Brokers; Clippens Oil Co Ltd v Edinburgh & District Water Trustees* [1907] AC 291, and *Banco de Portugal v Waterlow & Sons Ltd* [1932] AC452, at p506; [1932] All ER Rep. 181, at p204.

'As Lord Macmillan remarked in the last mentioned case, the measures which the sufferer from a breach of contract may be driven to adopt "ought not to be weighed in nice scales". So long as the respondents can be seen to have acted reasonably and justifiably in the circumstances, they should not be debarred from recovering the actual loss flowing to them simply because it is asserted that, by taking some other course, the loss might well have been lower.'

• Also, the costs of mitigation are recoverable. In this context Davies J in *AAP Industries Pty Ltd v Rehau Pte Ltd (No. 2)*[229] said:

'[23] There is no doubt that a plaintiff can recover money reasonably spent in mitigating or attempting to mitigate losses: *Whitehouse Hotels Pty Ltd v Lido Savoy Pty Ltd* (1975) 49 ALJR 93; *Hammond & Co v Bussey* (1887) 20 QBD 79; *Sheahan v Stockman* (1922) 22 SR (NSW) 415 at 423 and 426.

7.2 Mitigation and the avoided loss principle

A claimant may take steps to address the consequences of a breach of contract even though a failure to take such steps would not be regarded as a failure to mitigate. If the taking of such steps results in financial gain to the claimant, the contract breaker may require that such financial gain be brought to account in the assessment of damages. In *Macourt v Clark,*[230] the New South Wales Court of Appeal cited with evident approval the following statement in *McGregor on Damages* 18th ed (2009) at [7-006]:

'[W]here the claimant does take steps to mitigate the loss to him consequent upon the defendant's wrong and these steps are successful, the defendant is entitled to the benefit accruing from the claimant's action and is liable only for the loss as lessened; this is so even though the claimant would not have been debarred under the first rule from recovering the whole loss, which would have accrued in the absence of his successful mitigating steps, by reason of these steps not being ones which were required of him under the first rule. In addition, where the loss has been mitigated other than by steps taken by the claimant subsequent to the wrong, the claimant can again recover only for the loss as lessened, provided that the benefit gained is not to be regarded as collateral. Put shortly, the claimant cannot recover for avoided loss.'

As to whether a benefit is 'collateral' Giles JA in *Ruthol Pty Ltd v Tricon (Australia) Pty Ltd*[231] said:

'[48] References to indirect or collateral benefits are not helpful when faced with novel circumstances, and a test of "arising out of the act of mitigation" is itself not easy of application. In *Hussain v New Taplow Paper Mills Ltd* (1988) 1 AC 514, which was concerned with payments to an injured employee under a workplace health insurance scheme, Lord Bridge referred (at 528) to the difficulty of articulating a single guiding rule to distinguish receipts by a plaintiff which are to be taken into account in mitigation of damage from those which are not, and to the common law treating the matter "as one depending on justice, reasonableness and public policy." I venture to repeat what I said in *Tyco Australia Pty Ltd v Optus Network Pty Ltd* [2004] NSWCA433 at [253], that "collateral":

"... combines notions of causal significance and judgmental attribution of responsibility in law (positive or negative) for benefits and burdens consequent upon mitigating conduct. In *Naumann v Ford* (1985) 2 EGLR 70 at 74 it was asked 'whether any benefit to the plaintiff could be said to relate sufficiently closely to a particular head of damage as to be appropriate to be set off against it', and in *Johns v Prunell* (1960) VR 208 at 211 it was said that the law 'endeavoured to form a kind of moral judgment as to whether it is fair and reasonable that the defendant should have the advantage of something which has accrued to the plaintiff, by way of recoupment, or other benefit, as a result of the defendant's infringement of the plaintiff's rights'."'

More recently in *Harold R Finger & Co Pty Ltd v Karellas Investments Pty Ltd,*[232] the New South Wales Court of Appeal considered the scope of the avoided loss rule.

I turn to the facts.

On 21 December 2009 Karellas delivered to Finger & Co a 'binding offer to enter into Agreement for Lease with our organisation for the new supermarket premises'.

The offer letter was signed by Finger & Co in January 2010. Finger & Co asserted that its execution of the offer brought into existence a binding heads of agreement with Karellas.

However, the subsequent negotiations did not go well.

On 8 June 2010, Karellas emailed Finger & Co attaching a turnover forecast for the supermarket noting that with such a level of turnover the business was not viable on the proposed terms of the lease.

On 9 June 2010 Karellas' solicitors wrote to Fingers & Co's solicitors as follows:

'I confirm that my client will not be proceeding with the above proposed Lease on the current proposed terms. The reasons for my client's position are explained below. Having regard to the efforts of both parties to achieve an agreement, my client is willing to continue negotiations to see if a suitable outcome could be achieved for both parties.

'... The letter of 21 December clearly confirmed that the parties would negotiate final terms of an AFL and Lease. Whilst the letter outlined some of the contemplated lease conditions there have been significant changes to the terms as contemplated in the letter of 21 December. There are other aspects of the letter still to be addressed. Importantly there were also a number of important matters that had not been discussed as at December 2009.

'My client is genuinely disappointed that a final agreement has not been reached at this stage. They were certainly looking forward to a long term relationship with your client and saw the potential for development of this site in this particular suburb.'

By letter dated 11 June 2010, Finger & Co's solicitors replied as follows:

'... We note your advice that your client will not be proceeding with the lease "on the current proposed terms". The thrust of your letter appears to be that your client would proceed with the lease of the premises but on negotiated terms favourable to your client. We are instructed by our client that it is not interested in renegotiating the terms of the lease with your client. After over five months of protracted and detailed negotiations not only on the terms of the lease but on the specifications for the building works to be carried out (both by your client and by our client) final agreement was reached between our clients. It

was only after Sydney Council refused your client's Section 96 Application to use trolleys that your client sought to withdraw from the lease.

'...

'As you are no doubt aware your client's withdrawal from the lease will result in our client incurring substantial losses. Our client will endeavour to mitigate those losses. However, we are instructed to put your client on notice that our client will hold it liable for all losses incurred by our client as a result of your client's actions including but not limited to loss of future income, holding charges, consultants' fees and legal fees.

'We will communicate further with you when our client's loss has been quantified.'

On 5 July 2010 Karellas' solicitors wrote stating:

'We note from your correspondence that you do not intend to engage in any further correspondence in relation to whether or not negotiations had been completed. We take from your statement that your client does not intend to negotiate further in relation to a lease of the Premises. In short your client has ended all negotiations with our client. Our client has accepted that position but reserves all its rights in respect to your client's actions.'

Finally on 18 August 2010, Finger & Co's solicitors wrote to Karellas' solicitors as follows:

'It is clear from the above two pieces of correspondence that your client is not prepared to proceed with the proposed Lease on the terms set out in the heads of agreement dated 21 December 2009 (the "Contract").

'As such, your client has repudiated the Contract. Our client accepts your client's repudiation and hereby terminates the Contract.'

On 16 May 2011 Finger & Co executed an agreement for lease with Woolworths under which Finger & Co agreed to carry out specified works to the supermarket premises to reach practical completion by 1 June 2012.

Finger & Co brought proceedings against Karellas for loss of bargain damages.

During the course of the trial the primary judge noted that a revised build program circulated to Woolworths on 23 December 2011 contemplated the construction of the supermarket premises and a residential development as part of the one construction project. It was also noted that had the construction of any such residential development taken place while Karellas was in occupation, it would be proper to infer that there would have been constraints in the manner in which the building work was carried out, which constraints would not have arisen if the development occurred while the supermarket premises were unoccupied (as it ultimately did).

Finger & Co acknowledged that it received some $11 million from the sale of 20 residential units. It was established that the sales yielded a profit of $5 million.

In reversing the primary judge on this point, the Court of Appeal held that Karellas had not repudiated the heads of agreement by its solicitor's letter of 8 June 2010. Relevantly, Ward JA said:

'[129] In my respectful opinion, the primary judge erred in concluding that the 9 June 2010 letter conveyed to the reasonable reader that Karellas would only continue to negotiate if Finger & Co agreed to reduce the rent. I note that his Honour accepted that the issue was one that was finely balanced.

'[130] The reason that I have reached the contrary conclusion to that reached by his Honour is that the unviability of the business was stated to be "on the proposed lease terms". The proposed lease terms at that stage encompassed a range of matters, including the proposed variation to include the mezzanine level and the change to the original proposal that the lease be on a "turn-key" basis. I accept that the most obvious way of accommodating a concern as to the viability of the business, where that concern was stated to arise from a significant reduction in the forecast turnover and where rent at a lower percentage of forecast turnover had earlier been expressed to be "impossible", would be a reduction in rent. However, that would not necessarily be the case; and I accept Karellas' submission Finger & Co in effect pre-empted the exploration of that issue by refusing to depart from the then provisionally agreed lease terms.

'[132] I consider that the primary judge placed too much weight on the reference to Karellas' willingness to negotiate "to see if" Karellas' concerns could be accommodated. The letter of 9 June 2010 was inviting further negotiation. It was certainly foreshadowing that there might be a refusal by Karellas to proceed with the then presently negotiated terms for the agreement for lease and lease if some kind of renegotiated arrangement could not be reached that would satisfy its concerns as to the future viability of the business. However, I am not persuaded that the letter conveyed an intention by Karellas not to honour its obligations under the heads of agreement (i.e., to use his Honour's words, a refusal by Karellas to negotiate in good faith "towards" a proposed agreement for lease/lease that would include not only the agreed terms in the heads of agreement, with any agreed variation thereto, but also the additional terms that the heads of agreement required be included in the formal documentation). Repudiation is not lightly to be found (*Ross T Smyth & Co Ltd v T D Bailey Son & Co* [1940] 3 All ER 60 at 71; affirmed in *Shevill v Builders Licensing Board* [1982] HCA 47; (1982) 149 CLR 620 at 633).'

Although both the primary judge and the Court of Appeal ultimately found, albeit for different reasons, that Finger & Co wrongly terminated the heads of agreement, the various judgments went on to consider Finger & Co's damages claim on the assumption that the termination was valid.

One of the key issues in the damages assessment was whether the profit which Finger & Co generated on the residential development should be brought into account for the benefit of Karellas.

The primary judge concluded, subject to one qualification, that the assessment of Finger & Co's damages should be undertaken on the basis that the damages should be reduced by the

amount of its profit from the residential development. The qualification was that his Honour did not accept that the whole of the profit should be brought to account.

Finger & Co argued that the rule as to avoided loss only applied where the action from which the benefit is derived is action taken to avoid the consequences of the wrong or, in other words, to mitigate potential loss resulting from the wrong. It argued that the avoided loss rule was inapplicable in the present case because the upper level residential development was something it had proposed to undertake independently of Karellas' breach.

Ward JA (McColl JA agreeing) restated the applicable principles. Her Honour said:

'[221] It is not disputed that the fundamental principle governing assessment of damages for breach of contract is that the innocent party is entitled to be put in the position it would have been in had the contract been performed (*Robinson v Harman* (1848) 1 Ex 850 at 855; 154 ER 363 at 365; *Wenham v Ella* [1972] HCA 43; (1972) 127 CLR 454 at 471; applied as the "ruling principle" on common law damages for breach of contract in *Tabcorp Holdings Ltd v Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272 at [13] per French CJ, Gummow, Heydon, Crennan and Kiefel JJ).

'[222] The avoided loss "rule" or principle is one that arises for consideration in the context of the concept of mitigation of loss. In *British Westinghouse Electric and Manufacturing Co Ltd v Underground Electric Railways Co of London Ltd* [1912] AC 673, Viscount Haldane LC, with whom Lords Ashbourne, Macnaghten and Atkinson agreed, said (at 689) that when "in the course of business" the plaintiff has taken action arising out of the transaction, which action has diminished his loss, then the effect in actual diminution of the loss suffered may be taken into account, emphasising (at 690) that to be taken into account the subsequent transaction "must be one arising out of the consequences of the breach and in the ordinary course of business". The rule or principle has been applied in various cases (for example, *Hoad v Scone Motors Pty Ltd* [1977] 1 NSWLR 88; *Goldburg v Shell Oil Co of Australia Ltd* (1990) 95 ALR 711; *Monroe Schneider; Commonwealth v Amann Aviation Pty Ltd* [1991] HCA 54; (1991) 174 CLR 64; *Hi-Fert Pty Ltd v Kiukiang Maritime Carriers Inc* [2000] FCA 660; (2000) 173 ALR 263; *Tasman Capital Pty Ltd v Sinclair; Cardno BSD Pty Ltd v Water Corporation (No 2)* [2011] WASCA 161).

'[223] In *Ruthol,* Giles JA, with whom Santow JA and Hunt AJA agreed, stated the principle in the following terms (at [40]):

'"If the innocent party does take action to mitigate the loss to it consequent on the guilty party's wrong, even if the action goes beyond reasonable action, in general the guilty party is entitled to an allowance for the benefit to the innocent party from that action."'

In finding against Finger & Co on this issue, her Honour said:

'[233] Finger & Co argues that it was speculation for his Honour to conclude that it obtained some benefit from constructing the upper level development without Karellas being in occupation of the supermarket. It points to the evidence that it had received Council approval in May 2010 to build over the entire ground floor area of the property a first floor slab designed to enable any future upper level to be constructed without the need to disrupt the trading of the supermarket below. Nevertheless, when comparing the feasibility of carrying out construction while a tenant was in occupation below, it is hard to believe that there would not be a greater cost, as Mr Finger conceded in cross-examination (see T 92.43; 93.4), if Karellas had been in occupation during the building works; and hence a corresponding benefit from the freeing up of the capacity to build without a tenant in occupation.

'[234] The compensating advantage or benefit derived from the termination of the heads of agreement was therefore the ability to carry out a residential development above the proposed supermarket premises freed of the constraints imposed under the terms of the heads of agreement and, had the negotiation of the matters required under the heads of agreement resulted in a binding agreement for lease/lease, freed of the constraints imposed by the need to carry out building works while there was a trading supermarket on the site (subject of course to how the final lease documentation dealt with matters such as the usual covenant for quiet enjoyment and the like). That benefit was a direct consequence of the termination of the heads of agreement. It was the freeing up of a capacity to develop the upper floor without the constraints to which that development would otherwise have been subject. Whether or not this was ultimately of any value to Finger & Co such as ought be taken into account under the avoided loss principle when assessing its damages claim is in my opinion a different question.

'[235] I am thus of the view that his Honour did not err in determining that (as the question was framed in *Naumann v Ford* [1985] 2 EGLR 70 at 74, to which reference was made at [48] in *Ruthol*) the benefit was sufficiently close to the claimed head of damages as to be appropriate to set off against it. I would be of that view even though (as his Honour accepted and as is clearly the case) Finger & Co would not have been precluded from carrying out an upper floor development of some kind had the heads of agreement not been terminated and even accepting that the decision to proceed with an upper floor development was independent of the termination of the heads of agreement (in the sense that Finger & Co had already been proposing to carry out a development of some such kind above the supermarket premises).'

7.3 Mitigation and the *Robinson v Harman* principle: *Clark v Macourt* considered

The relationship between mitigation and the so called 'ruling principle' in *Robinson v Harman* was considered by the High Court in the somewhat controversial decision in *Clark v Macourt.*[233]

Dr Clark and Dr Macourt were medical practitioners. Each conducted an assisted reproductive technology practice (known as an ART practice). Dr Clark, conducted her practice under the business name 'Fertility First' and Dr Macourt conducted his practice under the business name 'St George Fertility Centre'.

By a deed entered into in 2002 St George sold to Dr Clark what were described in clause 1a as 'the Assets' which were defined to include sperm which was in turn defined to mean all frozen donor sperm. Under clause 2a the purchase price was calculated as follows:

'In respect of each of the calendar years 2002, 2003 and 2004,15% of the amount by which the purchaser's gross fee income exceeds 105%, 110% and 115% respectively of the fee income of the purchaser for the calendar year 2001.'

The application of the formula yielded a purchase price of $386,950.91.

The donor sperm for use in an ART practice is stored in thin 'straws' about 3mm to 5mm wide. One of the Assets referred to in the deed was 3,513 straws of donor sperm. In August 2005 the straws became unusable as a result of breaches of warranty by the seller. At that time Dr Clark had used 504 of the straws leaving 3,009 to be discarded. Relying on evidence adduced in the trial his Honour held that Dr Clark could have expected to use at least 2,500 of the 3,513 straws had they been warranty compliant.

In September 2005 Dr Clark began purchasing replacement sperm from Xytex Corporation in the United States. This was the sole source of contractually compliant sperm. At the time of trial in September 2011 Dr Clark had purchased 1,546 replacement straws of Xytex sperm.

In assessing damages for breach of contract the primary judge concluded that the appropriate measure to be applied was the difference between a 'hypothetical sale' of 1,996 of the unusable straws and the amount Dr Clark would have paid in a 'hypothetical purchase' of the Xytex sperm in 2002 (being the date of breach). His Honour considered that the best evidence of what that hypothetical purchase would have cost was the first purchase by Dr Clark in September 2005 of straws of Xytex sperm for a total cost of $511 per straw. His Honour then extrapolated that figure to 1,996 straws resulting in an amount of $1,020,252.

As noted by Gageler J in the High Court appeal at 20:

'Dr Macourt, for his part, points to the remarkable prospect of being saddled, if the primary judge's measure were to be upheld, with an obligation to pay Dr Clark $1,020,252.70 in damages as a consequence of the company in effect failing to deliver one asset of a business which the company ended up selling to Dr Clark for a total price of only $386,950.91. But Dr Macourt does not seek to attach any particular legal significance to the disparity between those two figures.'

The contest in the case turned on the significance of the finding that Dr Clark charged her patients the acquisition and transport costs of the Xytex sperm from the United States.

Dr Clark had not previously charged her patients for the acquisition of the St George sperm which she had utilised up to August 2005. Dr Macourt contended that Dr Clark suffered no compensable loss, having recouped her costs from her own patients.

The primary judge characterised the 2002 deed as a contract for the sale of goods. In response to Dr Macourt's submission that Dr Clark suffered no loss his Honour noted:

'[21] The simple answer to that proposition is that Dr Clark paid twice for the use of sperm and recovery of the cost of acquisition and storage of the sperm purchased from Xytex still left her out of pocket for the amount paid under the deed.' (emphasis added)

Tobias AJA delivered the principal judgment of the Court of Appeal which allowed Dr Macourt's appeal. His Honour noted Dr Clark's submission on onus as follows:

'[95] Thus, in summary, it was submitted that to discharge their onus St George and Dr Macourt had to establish that the breach conferred on Dr Clark a benefit that Dr Clark could not have gained if the Deed had been performed. In other words, they had to prove that Dr Clark would have been unable to charge her patients in respect of hypothetically compliant St George sperm, or else to prove that any such charge she could have made would have left her in an inferior position compared with that in which she was in fact in to a proved extent.'

His Honour continued:

'[127] In my view, it cannot be gainsaid that Dr Clark took steps to mitigate her loss and that those steps met with a high degree of success. St George's breach of contract made it necessary for her to acquire sperm from an alternative source. She did so at a cost to her. That cost represented the *prima facie* loss she suffered as a result of St George's breach, subject to the effects of such mitigation as she achieved or ought to have achieved. She in fact achieved mitigation to what was, in practical terms, the maximum extent allowed by the legal and ethical constraints under which she operated and which both parties necessarily had in contemplation as being operative in the particular circumstances.

'[128] The true measure of Dr Clark's damages thus consisted of two elements. The first related to the cost of the replacement sperm sourced from Xytex before the date for assessment of damages. The second concerned the residue of the "lost" 1996 St George straws over and above those in fact replaced by Xytex sperm up to the date of trial.

'[129] In respect of the loss of each straw of replacement sperm actually sourced from Xytex before that date, the sum (if any) representing that part of the overall cost of acquisition of that straw not recouped from a patient would be the chief component of Dr Clark's loss. To each such separate sum would be added appropriate interest from the date of acquisition from Xytex to the date of assessment of damages.

'[130] In respect of the residue of the "lost" 1996 straws over and above those in fact replaced by Xytex sperm up to the date of trial, the appropriate course would have been to assume that Dr Clark would continue to source straws of donor sperm from Xytex at a cost consistent with that which had prevailed since August 2005, and that she would continue to recoup from patients the same proportion of that cost as she had done in the past. Her damages would then be calculated as the aggregate of the discounted present value of the un-recouped balances (if any) of that cost as at the date of their assessment.'

The High Court allowed Dr Clark's appeal and reinstated the judgment of the primary judge.

Keane J formed part of the majority together with Hayne, Crennan and Bell JJ. Gageler J in dissent dismissed the appeal.

Dr Macourt's key contentions were summarised by Keane J at 26:

'St George and the respondent contended that the date for assessment of damages should have been the date of trial. They argued that any loss suffered by the appellant was suffered during the period between completion of the contract and trial, and during that period the purchaser recovered the cost of acquisition, transport and storage of sperm by charging those costs to patients. On that approach, the appellant had suffered no loss by the date of trial. The primary judge rejected that contention, applying "the general rule of common law ... that damages are assessed at the time of breach of contract or when the cause of action arises".'

His Honour summarised Dr Clark's principal submission at 28:

'The appellant's challenge to the decision of the Court of Appeal may be stated succinctly. St George's breach of contract meant that the value of the sperm straws as assets acquired by the appellant under the Deed was less than it would have been if St George's promises had been kept. The appellant suffered that loss of value at the date of completion of the acquisition of the assets.'

There was a sharp difference of view between Keane J and Gageler J as to the way in which Dr Clark formulated her claim. Thus, Gageler J said at 19:

'Dr Clark has at no stage suggested that her loss is to be identified as the difference between the value of the business she acquired and the value of the business for which she contracted, and at an early stage abandoned a claim that a component of her loss was consequential loss of profits in the conduct of her business. She has at every stage sought substantial, not merely nominal, damages.'

Conversely, Keane J noted at 29:

'The respondent contended that the appellant's claim was not for the value of the sperm to which she was entitled, but for the costs and expenses associated with the "procurement of replacement sperm". The respondent said that these costs and expenses were incurred subsequent to the date of breach and, accordingly, should have been assessed at the date of trial.

'The forensic advantage to the respondent of framing the appellant's claim in this way was that it opened the way for the argument, accepted by the Court of Appeal, that the appellant recouped from her dealings with her patients the costs and expenses incurred by her in procuring replacement sperm, so that she suffered no loss by reason of St George's breach of contract.

'The respondent's contention under this heading should be rejected. The appellant was entitled to frame her claim in the manner most advantageous to her, and to have that claim determined. The nature of the appellant's claim was made clear in para 13(a) of the appellant's reply in the Supreme Court. Her claim for damages was for an award which:

'"... gives her the benefit of her bargain under the Deed by giving her, so far as money is capable of doing so, something equivalent to the value of the worthless Sperm delivered to her, as opposed to damages to compensate her specifically for her outlay to Xytex (the amount actually paid and payable to Xytex being no more than evidence of an appropriate measure of damages)."'

The core question for the Court was whether Dr Clark's damages should be assessed on a difference in value basis or on a cost basis.

Keane J restated the fundamental principle governing an award of damages for breach of contract:[234]

'The principle according to which damages for breach of contract are awarded is that the damages should put the promisee in the same situation with respect to damages, so far as money can do it, as it would have been in had the broken promise been performed. The appellant was entitled to claim this measure, rather than a measure based, either on the difference between what she paid for the sperm straws and what they were worth, or on the expense "of undoing the harm which [her] reliance on the defendant's promise has caused [her]".'

His Honour then referred to the 'ruling principle' adopted by the Court in *Tabcorp Holdings*.

In respect of the assessment of damages at 'date of breach' his Honour said at 32:

'The application of the ruling principle to measure value lost at the date of breach of contract serves the important end of bringing finality and certainty to commercial dealings. It ensures that whatever might befall the purchaser after the date of breach, for good or ill, and whether by reason of the purchaser's acumen, or lack of it, in dealing with other persons who were not party to the contract, and whatever movements may occur in the market, these developments have no bearing on the entitlement of the purchaser and the liability of the seller.'

The critical passages in his Honour's judgment are set out at 36-37 as follows:

'To say that in the conduct of the appellant's practice she was able to recover the cost to her of the Xytex sperm incurred in the course of her practice after acquiring the assets is to fail to address the claim which the appellant actually made. The loss for which the appellant claimed compensation occurred at the completion of the Deed, at which time the assets which she acquired were not as valuable as they would have been had St

George's performance measured up to its warranties. One may make this point, without dwelling impermissibly on "circumstances peculiar to the plaintiff", by observing that, at the completion of the Deed, if the appellant had been minded to on-sell her business (enhanced by the acquisition of the assets from St George) the value of that business would have been substantially less because much of the stock in trade could not have been profitably deployed by the purchaser. That the appellant was not, in fact, in the market to sell her business or its assets including its stock in trade is beside the point, which point is that the appellant's post-acquisition assets were less valuable than should have been the case.

'The point that the appellant had suffered a real loss in terms of the benefit of her bargain at the date of completion of the acquisition of the assets may be made another way. The appellant may have been able to charge fees for her services in the conduct of her practice which were within the market range but returned her a greater profit because she was not obliged to incur the extra cost of replacement sperm. Whether or not she chose to realise the value of compliant St George sperm in this way was a matter for her. Whether or not she would have been disposed to take such a course was not explored in evidence at trial; but that is not a deficit in her claim. She was entitled to claim the measure of damages under the ruling principle without going into such matters. It would be an unprecedented application of the rule in *Hadley v Baxendale* to confine the measure of a purchaser's damages by reference to the likely effects of the particular decisions of the purchaser as to how she might choose commercially to exploit the assets acquired from a seller. The point is that one cannot say that the appellant's loss was confined to the expense that she had to incur (but was able to recoup from patients) in acquiring 1,996 straws of sperm from an alternative supplier as and when she needed those straws for the treatment of patients.'

Keane J derived support for his conclusion from a line of English Court of Appeal decisions dealing with sale of goods and the *prima facie* rule set out in section 53(3) of the Sale of Goods Act 1979 (corresponding to section 54(3) of the Sale of Goods Act 1923 (NSW)). Specifically, his Honour referred to the decision in *Slater v Hoyle & Smith Ltd*[235] in which Warrington LJ said at 18:

'The purchaser here has received inferior goods of smaller value than those he ought to have received. He has lost the difference in the two values, and it seems to me immaterial that by some good fortune, with which the [sellers] have nothing to do, he has been able to recoup himself what he paid for the goods.'

Relevantly, Keane J noted at 38:

The observations of Warrington LJ apply with equal force to the present case. The value of the St George sperm lay not in what it might bring in a market for sperm as a commodity, but, as the Deed contemplated, as stock of a business. And as stock of the business they were distinctly inferior.'

Hayne J said at 10:

Showing that the appellant had charged, or could charge, third parties (her patients) the amount she had paid to acquire replacement sperm from Xytex was irrelevant to deciding what was the value of what the vendor should have, but had not, supplied. If the contract had been performed according to its terms, the appellant would have had a stock of sperm having the warranted qualities which she could use as she chose. She could have stored it, given it away or used it in her practice. In particular, she could have used it in her practice and charged her patients nothing for its supply. But because the vendor breached the contract, the appellant could put herself in the position she should have been in (if the contract had been performed) only by buying replacement sperm from Xytex. Whatever transactions she then chose to make with her patients are irrelevant to determining the value of what should have been, but was not, provided under the contract.'

Gageler J in dismissing the appeal noted at 20:

To measure a buyer's damages as the difference, as at the date of delivery, between what the buyer would have obtained in a hypothetical sale of contractually non-compliant goods delivered and what the buyer would have paid in a hypothetical purchase to obtain delivery of contractually compliant goods from another seller is ordinarily appropriate in the standard category of case where a seller fails to deliver marketable goods to a buyer in compliance with a contractual warranty. That is because the measure ordinarily gives to the buyer the monetary equivalent of the value to the buyer of the performance of the contract by the seller. The value to the buyer of having ownership of, and control over, contractually compliant goods that can be bought and sold in a market as at the time of delivery ordinarily equates to the market value of those goods at that date. The market value of goods is not ordinarily dependent on circumstances peculiar to an individual seller or individual buyer. Accordingly, it ordinarily makes no difference why the buyer chose to purchase the goods or whether the buyer could be expected actually to realise the monetary equivalent of that value by re-selling or otherwise disposing of the goods.'

And his Honour concluded at 22:

The value to Dr Clark of the company delivering frozen sperm in 2002 in compliance with the contract could not, in those circumstances, be equated with the value to a buyer of having dominion over contractually compliant goods of a nature which would be available to be re-sold by the buyer in a market at the time of delivery. The value to Dr Clark of the company delivering contractually compliant frozen sperm lay rather in Dr Clark gaining control over a stock of frozen sperm which she could then use for the treatment of her patients in the normal course of her practice. That is to say, if she had been able to take possession from the company of contractually compliant frozen sperm, Dr Clark would have had the benefit of being relieved of the need thereafter to source sperm from somewhere else as and

when she needed sperm to treat her patients.'

Two issues arise in connection with the decision of the majority.[236]

First, Keane J's reference to *Slater v Hoyle & Smith Ltd* does not take account of the critical comments of the later decision of the English Court of Appeal in *Bence Graphics International Ltd v Fasson UK Ltd.*[237] Auld LJ in referring to section 53(3) of the English Sale of Goods Act said:

'As to section 53 (3) there is, in my view, a danger of giving it a primacy in the code of section 53 that it does not deserve. The starting point in a claim for breach of warranty of quality is not to determine whether one or other party has "displaced" the prima facie test in that subsection. The starting point is the *Hadley v Baxendale* principle ...

'In my view, the time has come for *Slater's* case to be reconsidered at least in the context of claims by a buyer for damages for breach of warranty where he has successfully sold on the subject matter of the contract in its original or modified form without claims from his buyers.'

It is noteworthy that Crennan and Bell JJ in their joint reasons made a footnote reference to *Bence Graphics* but did not engage in any analysis on the case.

Secondly, the plurality do not make any comment on a line of English and Australian cases which make the point that the 'date of breach' rule is not an inflexible principle.

7.4 Mitigation and causation

Although mitigation and causation have been treated as conceptually different. Robb J in *Chand v Commonwealth Bank of Australia*[238] noted:

'[283] As will be seen from the discussion of the authorities that follows, the courts have relatively readily equated the principles of causation and mitigation where a single set of circumstances calls for the application of the two principles. There may even be a basis for saying that in those circumstances the two principles fuse into one.'

In *Chand* the New South Wales Court of Appeal considered mitigation and causation in the context of the High Court decision in *Clark v Macourt.*

I turn to *Chand.*

The plaintiff invested in products issued by Colonial First State Investments Ltd. He held units in five CFS wholesale investment funds. By July 2007 the value of Chand's investment in CFS investment products was some $2.9 million financed partly by his own funds and partly by margin loan facilities amounting to some $1.8 million.

On 25 September 2007 Chand lodged a redemption request for the whole of his investment. He received no response from the Bank and based on previous dealings he would have expected a response within 10 working days which meant that he would have expected a confirmation by 9 October 2007.

On 5 November 2007 Chand rang a call centre operated by the Bank and was informed by the call centre operator that there was no record of his redemption request on the Bank's system.

Chand did not make any further enquiry of the Bank. As noted by Ward JA239 in her Court of Appeal judgment:

'[27] In other words, he made a positive decision to remain in the market (on-risk) and to select another exit date, notwithstanding that he had earlier reached the view that highly geared stock was no longer "a safe investment option". He said that was "the easiest decision to make".'

The evidence adduced in the trial showed that for the period 25 September to 7 November 2007 the value of Chand's investments exceeded their redemption value as at 25 September 2007. From 8 November 2007 to 13 December 2007 the net value of the investments exceeded $1 million. However, from 13 December 2007 as the global financial crisis deepened the redemption value of Chand's investments steadily fell. He also paid margin calls on his bank loans in April 2008 and again in July 2008.

By July 30 2008 Chand's investments had a negative value.

As determined by the Court of Appeal at 102:

'[102] ...

'With hindsight, it is clear that there were opportunities for Mr Chand to redeem at or around the September 2007 figure during the period to mid-December 2007. His Honour did not err in so finding.'

The Bank conceded that it was in breach of contract by failing to respond to Chand's redemption request on 25 September 2007.

Chand commenced proceedings for damages for breach of contract seeking recovery of the equity which he lost together with consequential losses including his marginal call payments.

Chand contended that as a result of the Bank's breach of contract he suffered an immediate loss equal to his equity although other consequential losses followed. The primary judge (Robb J) summed up Chand's contention as follows:

'[249] If the Bank had properly performed the contract, it would have redeemed all of Mr Chand's investments, paid out his margin loan, and paid the remaining $1,034,636.81 into his bank account. The amount that Mr Chand has described as his equity loss would have been safely in his bank account. Mr Chand would have been freed from the risk of subsequent movements in the market that could reduce the portfolio value of his investments. He would have been freed from his obligations under the margin loan agreement, including the risk of having to meet margin calls if falling portfolio values caused his current loan-to-security ratio to fall below the agreed ratio.'

Chand relied on *Clark v Macourt.*

In response the Bank contended as follows:

(i) That its admitted breach of contract on 25 September 2007 did not directly cause an actual loss but created a prospective of loss, ie, a risk of loss. Relevantly, following the breach there was no diminution in the redemption value of Chand's investment.

(ii) On realising that his redemption request had not been implemented Chand could readily have issued a new request.

Instead, he made a free deliberate and informed decision to stay in the market. Accordingly, his ultimate loss was caused by that decision and not the Bank's breach. Relevantly his decision constituted a novus actus interveniens and broke the chain of causation between the Bank's breach and Chand's loss.

In *Alexander v Cambridge Credit Corporation Ltd,*[240] McHugh JA said at 361:

'Notwithstanding that a defendant's act or omission has a causal connection with the damage of the person aggrieved, no liability arises if an independent intervening act or event in conjunction with the defendant's act or omission has brought about the plaintiff's damage and the intervening act or event can be treated in a practical sense as the sole cause of the damage.'

And in *Allianz Australia Insurance Ltd v Waterboork at Yowie Bay Pty Ltd,*[241] Ipp JA said at 106:

'Traditionally, it is generally accepted that the free, deliberate and informed act or omission of a human being negatives causal connection.'

(iii) Alternatively, Chand's conduct in remaining in the market was so unreasonable in the circumstances that the Court should find that the scope of the Bank's liability should not extend to the loss actually suffered.

(iv) In the further alternative, Chand failed to mitigate when he could have avoided his loss.

The primary judge found for the Bank on the causation argument, namely, that the decision by Chand to remain in the market was a novus actus interveniens and was the real and effective cause of his loss.

The Court of Appeal dismissed Chand's appeal.

As noted above Chand relied heavily on *Clark v Macourt.* He contended that *Clark v Macourt* is an example of a case where there can be 'liability without causation', ie, liability without proof of causative damage. Ward JA said:

'[150] Mr Chand's complaint is that the practical effect of his Honour's decision was that he was not in fact put back in the position in which he would have been had the Bank redeemed his investments because, though left with the value of the investments, he remained on risk and then his loss crystallised when the market fell. It is clear from his Honour's reasons that this was the outcome because of the application of the principles of causation relating to the import of a novus actus interveniens. That finding is the subject of grounds 4 and 6.'

In rejecting the relevance of *Clark v Macourt* Ward JA (with the agreement of Bathurst CJ and Beazley P) concluded:

'[151] Insofar as the complaint in grounds 1 and 2 is that his Honour should have treated this as a case where there was no need for a causal link in order for the Bank to be liable, I cannot agree. In *Clark v Macourt,* the "loss" for which compensation was claimed was identified by Hayne J at [9] as the loss of the value of what the promisee would have received if the promise had been performed. For Mr Chand to be put in the position in which he would have been had the redemption request been redeemed, it was necessary for there to be an assessment of his prospective loss. The manner in which he quantified his claim for damages made that clear — he was seeking not simply the equity loss but also compensation for the loss flowing from the fact that the investments had been retained. This was not a claim, akin to that in *Clark v Macourt,* where Mr Chand was seeking the monetary substitute or equivalent of a product that the Bank had agreed to supply to him.

'[152] I see no error in his Honour's approach to or application of the principles relating to assessment of loss for damage for breach of contract that were confirmed in *Clark v Macourt.* Grounds 1 and 2 are not made out.'

Although the issue in the appeal may have been resolved by an application of the principle of mitigation in light of the finding of the primary judge that Chand acted unreasonably in remaining in the market, the actual decision was resolved on a causation analysis.

8 EXPECTATION DAMAGES AND NET PROFIT

8.1 Background

In any commercial dealing where a claim for breach of contract arises the central component in such claim will conventionally be loss of profit. The key issue is how is 'profit' to be determined.

In *Amann Aviation* Mason CJ and Dawson J noted at 81:

'In the ordinary course of commercial dealings, a party supplying goods or rendering services will enter into a contract with a view to securing a profit, that is to say, that party will expect a certain margin of gain to be achieved in addition to the recouping of any expenses reasonably incurred by it in the discharge of its contractual obligations. It is for this reason that expectation damages are often described as damages for loss of profits. Damages recoverable as lost profits are constituted by the combination of expenses justifiably incurred by a plaintiff in the discharge of contractual obligations and any amount by which gross receipts would have exceeded those expenses. This second amount is the net profit.'

Thus, profit in relation to a breach of contract claim means net profit. If a contract yields no net profit or a profit cannot otherwise be demonstrated then the benchmark for recovery will be expenses justifiably incurred in the course of performance and which are wasted by reason of the breach.

8.2 Profit and overheads

The ascertainment of net profit in respect of a damages claim was considered by the New South Wales Court of Appeal in *North Sydney Leagues' Club Limited v Synergy Protection Agency Pty Limited.*[242]

In that case the respondent entered into a contract with the appellant to provide security services over the period November 2004 to November 2005. In 2005 the appellant wrongfully terminated the contract. There followed various excursions to the courts. The primary judge, Einstein J handed down four separate judgments. His final judgment is reported [2011] NSWSC 286.

His Honour identified the relevant issue as follows:

'[4] In reference to the assesment (sic) of damages, the primary issue for determination is: in assessing (sic) Synergy's loss, should the court deduct from its entitlement to damages a proportionate share of indirect or overhead costs?'

His Honour summarised the position of the parties:

'[56] In the present case, the difference between the parties can be summarised as follows:

'(1) Norths has allocated all overhead costs, both fixed such as rent and variable such as telephone bills, on a pro-rata basis to Synergy's costs.

'(2) Synergy has looked at each expense individually, irrespective of whether it is a direct cost or overhead, and determined what cost was saved as a result of the loss of the contract.'

His Honour earlier noted:

'[39] At the outset I wish to express my agreeance with Ward LJ's observation in *Western Web Offset Printers Ltd v Independent Media Ltd* [1996] CLC 77, at 80H-81A that:

'"... too slavish an adoption of classifications such as direct and indirect costs or net and gross profit is liable to be distracting from the general principle of ascertaining the loss of the bargain. Confusion is only avoided by going back to the basic principle of ascertaining how the breach of contract caused loss to the particular party.'

'[40] In this vein, I keep in mind that the question in this case is how to best place Synergy in the position it would have been in had Norths' not breached its contract.

'[41] The correct way to achieve this is to deduct from forecast revenue which expenses "would have increased when the contract was being performed, and would have diminished when it ended ..." while "outgoings, such as accounting fees, rent, rates and taxes, would not reduce as a result of the termination of the contract" and should therefore not be adjusted for, per Doyle CJ in *Bartonvale Management Services Pty Ltd v International Unen Services Pty Ltd* [2002] SASC 254 at [23].

'[42] Contrary to North's assertion, no apportionment of fixed costs, ie those costs which would not increase or decrease with the loss of the Norths contract, should be considered.'

The appellant's primary submission in the appeal was that 'overheads' must be brought into account in any claim for loss of profits arising from wrongful termination. The appellant relied on the judgment of McHugh J in *Dart Industries Inc v The Décor Corporation Pty Ltd.*[243] In the context of a claim for an account of profits on a patent infringement McHugh observed at 133:

'Based on the above analysis of accounting and economic principles and practice, as well as the United States cases, the absorption method of cost accounting is the appropriate method of accounting for general overheads in a case of infringement. The test to be applied was concisely stated in *Alfred Bell and Co v Catalda Fine Arts* where the Court said: "The test is not whether such an overhead item had been increased by the handling of the infringements but whether this overhead item actually assisted in the production of the infringing profits".'

As explained by the plurality, absorption costing is a costing method whereby general overheads are apportioned by some appropriate means often by sales or volume, to the manufacture or sale of each product.

The New South Wales Court of Appeal in dismissing the appeal concluded that the appellants' reliance on *Dart Industries* was misconceived. As noted by Macfarlan JA:

'[88] As Beazley JA has pointed out, the judgment of McHugh J in *Dart Industries Inc v Decor Corporation Pty Ltd* is not presently relevant. The issue in that case was what expenses were in fact incurred, looking at the position in retrospect. There was no question there, as there is in the present case, of what expenses were (or could have been) avoided following another party's breach of contract.'

Beazley JA noted:

'[81] In my opinion, the appellant's submissions also failed to engage with the essential nature and extent of the claim the respondent made. This was recorded by his Honour, at [58], but bears repeating by way of conclusion. The respondent "looked at each expense individually, irrespective of whether it [was] a direct cost or overhead and determined what cost was saved as a result of the loss of the [contracts with the appellant]". The appellant failed to demonstrate in its argument on the appeal that the respondent had not in fact undertaken that task in a sufficiently adequate way. In seeking to attack the judgment on the basis that his Honour should have, but failed to deduct overhead expenses in the post-termination period, the appellant did not have regard to what the respondent in fact claimed and what it had not. The appellant has not established any error in his Honour's acceptance of the respondent's evidence in relation to its loss arising from the appellant's breach of contract.'

The Court recognised the fundamental distinction between contract damages and the equitable remedy of account of profits, namely, in the former the focus is putting the innocent party in the position as if the contract was performed while in the latter the focus is the prevention of unjust enrichment.

The underpinning rationale of the equitable remedy of account of profit was further considered by the Full Federal Court in *V-Flow Pty Ltd v Holyoake Industries (Vic) Pty Ltd.*[244] The Court noted:

'[57] On the other hand, the purpose of an account of profit is to prevent the unjust enrichment of the fiduciary by compelling the fiduciary to surrender any profits actually made by the fiduciary that were made improperly, and nothing beyond that. It is not to punish the errant fiduciary (*Dart Industries Inc v Décor Corporation Pty Ltd* (1993) 179 CLR 101 at 111) (*Dart*). The errant fiduciary is made to account for, and is then stripped of, profits made that it would be unconscientious for that person to retain, because they are profits made by the fiduciary dishonestly. For example, in the case of infringement of

intellectual property rights, the account is limited to the profits of the wrongdoer during the period when the victim's rights were being infringed (*Colbeam Palmer Ltd v Stock Affiliates Pty Ltd* (1968) 122 CLR 25 at 34).'

9 RESTITUTIONARY AND DISGORGEMENT DAMAGES

It is unlikely at this stage in the development of Australian law that a court would make an order for an account of profits as a remedy for breach of contract. The compensatory principle appears to still command the field, namely, the criterion for assessment of damages is loss to the plaintiff and not gain by the defendant.

However, the House of Lords (as it was then styled) in *Attorney General v Blake*[245] signalled the acceptance in English law of a restitutionary approach in respect of breach derived gains even in the absence of any provable loss to the plaintiff.

In affirming the decision of the Court of Appeal granting a restitutionary remedy, Lord Nicholls having analysed the authorities noted at 397:

'My conclusion is that there seems to be no reason, in principle, why the court must in all circumstances rule out an account of profits as a remedy for breach of contract. I prefer to avoid the unhappy expression "restitutionary damages". Remedies are the law's response to a wrong (or, more precisely, to a cause of action). When, exceptionally, a just response to a breach of contract so requires, the court should be able to grant the discretionary remedy of requiring a defendant to account to the plaintiff for the benefits he has received from his breach of contract. In the same way as a plaintiff's interest in performance of a contract may render it just and equitable for the court to make an order for specific performance or grant an injunction, so the plaintiff's interest in performance may make it just and equitable that the defendant should retain no benefit from his breach of contract.

'The state of the authorities encourages me to reach this conclusion, rather than the reverse. The law recognises that damages are not always a sufficient remedy for breach of contract. This is the foundation of the court's jurisdiction to grant the remedies of specific performance and injunction. Even when awarding damages, the law does not adhere slavishly to the concept of compensation for financially measurable loss. When the circumstances require, damages are measured by reference to the benefit obtained by the wrongdoer. This applies to interference with property rights. Recently, the like approach has been adopted to breach of contract. Further, in certain circumstances an account of profits is ordered in preference to an award of damages. Sometimes the injured party is given the choice: either compensatory damages or an account of the wrongdoer's profits. Breach of confidence is an instance of this. If confidential information is wrongfully divulged in breach of a non-disclosure agreement, it would be nothing short of sophistry to say that an account of profits may be ordered in respect of the equitable wrong but not in respect of the breach of contract which governs the relationship between the parties. With the established authorities going thus far, I consider it would be only a modest step for the law to recognise openly that, exceptionally, an account of profits may be the most appropriate remedy for breach of contract. It is not as though this step would contradict some recognised principle applied consistently throughout the law to the grant or withholding of the remedy of an account of profits. No such principle is discernible.

'The main argument against the availability of an account of profits as a remedy for breach of contract is that the circumstances where this remedy may be granted will be uncertain. This will have an unsettling effect on commercial contracts where certainty is important. I do not think these fears are well founded. I see no reason why, in practice, the availability of the remedy of an account of profits need disturb settled expectations in the commercial or consumer world. An account of profits will be appropriate only in exceptional circumstances. Normally the remedies of damages, specific performance and injunction, coupled with the characterisation of some contractual obligations as fiduciary, will provide an adequate response to a breach of contract. It will be only in exceptional cases, where those remedies are inadequate, that any question of accounting for profits will arise. No fixed rules can be prescribed. The court will have regard to all the circumstances, including the subject matter of the contract, the purpose of the contractual provision which has been breached, the circumstances in which the breach occurred, the consequences of the breach and the circumstances in which relief is being sought. A useful general guide, although not exhaustive, is whether the plaintiff had a legitimate interest in preventing the defendant's profit-making activity and, hence, in depriving him of his profit.'

Lord Steyn noted at 404:

'For my part practical justice strongly militates in favour of granting an order for disgorgement of profits against Blake. The decision of the United States Supreme Court in *Snepp v US* (1980) 444 US 507 is instructive. On very similar facts the Supreme Court imposed a constructive trust on the intelligence officer's profits. Our law is also mature enough to provide a remedy in such a case but does so by the route of the exceptional recognition of a claim for disgorgement of profits against the contract breaker. In my view therefore there is a valid claim vesting in the Attorney General against Blake for disgorgement of his gain.'

In *Australian Rugby Union Ltd v Hospitality Group Pty Ltd*[246] Gyles J having considered the decision of the English Court of Appeal in Blake stated at 128:

'Mr Gleeson put an argument to suggest that the ARU is entitled to an account of profits made by THG as a result of the breach. In relation to breach of contract, he said that I should follow the lead of the *obiter dicta* of the United Kingdom Court

of Appeal in *Attorney General v Blake* [1998] 2 WLR 805 (now on appeal to the House of Lords) and referred to passages in the judgment of Deane J and Gaudron J in *Trident General Insurance Co Ltd v McNiece Bros Pty Ltd* (1988) 165 CLR 107 (145-6 and 174-7). Such a radical change in the received wisdom as to the common law of Australia is not for a single judge. Even if the House of Lords were to approve what was said on the issue in the Court of Appeal, I would have significant reservations about adopting it. In any event, I do not think it appropriate to hold up this judgment until the House of Lords decision is available.'

In an unsuccessful appeal by Hospitality Group the Full Federal Court (Hill, Emmett and Finkelstein JJ) said:

'[159] Whether or not the law of contract is "seriously defective" (*Attorney-General v Blake* [1998] Ch 439 at 457 per Lord Woolf MR), if the court is unable to award disgorgement damages (the terminology proposed by L Smith in "Disgorgement of the Profits of Breach of Contract: Property, Contract and .'Efficient Breach'" (1994) 24 *Canadian Business Law Journal* 121), the position in Australia is that the loss recoverable for breach of contract is limited to that laid down in *Robinson v Harman (supra).* That is, the aggrieved party is entitled only to compensation. If he has suffered no loss, he is not entitled to be compensated in an appropriate case, the aggrieved party may be able to recover (by a claim in restitution) benefits that he has made available to the wrongdoer; for example, he may be able to recover the price paid under an incomplete contract or recover possession of goods sold but not paid for. Presently, however, it would be inconsistent with the current principles laid down by the High Court to confer a windfall on a plaintiff under the guise of damages for breach of contract.

'[160] Turning to the remedies available to the victim of a tort, those remedies may conveniently (if somewhat inaccurately) be divided into two groups (a) damages; and (b) other remedies. Here, we are not concerned with non-pecuniary remedies, the principal ones being injunction and restitution. So far as pecuniary remedies are concerned, it should be noted that damages may be either compensatory or noncompensatory. In the latter category are contemptuous damages, nominal damages, exemplary damages and restitutionary damages. Restitutionary damages may be limited to cases involving the misuse of a plaintiff's property: *Surrey County Council v Bredero Homes Ltd* [1993] 1 WLR 1361.

'[161] Speaking generally, an award of damages is made in order to compensate the plaintiff for his injury. The rule is that the plaintiff is to be placed in the same position as he was before the tort was committed: *Livingstone v Rawyards Coal Co* (1880) 5 App Cas 25 at 35. This is sometimes referred to as the rule of restitution in integrum. The rule is more easily applied to losses which are capable of calculation in money terms. In areas where the losses are not readily quantifiable, for example where damages are claimed for pain and suffering or in an action for defamation, the court attempts to award "fair compensation": *Clerk & Lindsell on Torts* (17th ed, 1995) para 27-09.

'[162] However described, it is not possible to slot an account of profits into the general framework of remedies that are available in tort, when the account is not awarded to compensate the plaintiff for his actual or presumed loss. That is to say, under presently accepted principles, an injured plaintiff cannot claim a windfall to prevent a wrongdoer profiting from his wrong, except in those cases where exemplary damages are available and it is proper that illicit profits are taken into account in assessing the quantum of the award, as happened in *McMillan v Singh* (1984) 17 HLR 120, 125 and *John v MGN Ltd* [1997] QB 586, 619.'

The Western Australia Court of Appeal considered the issue in *Dalecoast Pty Ltd v Guardian International Pty Ltd.*[247] The Court did not decide whether *Blake* was good law in Australia.

The authorities were considered by Blue J in *Testel Australia Pty Ltd v KRG Electrics Pty Ltd.*[248] His Honour, in following the approach in Hospitality Group, noted:

'[109] As a judge at first instance, I should follow a decision of an intermediate court of appeal concerning the common law of Australia unless I am persuaded that it is plainly wrong. Applying that approach, I should follow the decision of the Full Court of the Federal Court in *Hospitality Group Pty Ltd v Australian Rugby Union Ltd.* Testel concedes that the decision of the Full Court that an account of profits is not a remedy available at common law in tort was part of the ratio decidendi of that case, but contends that the decision that the remedy is not available for breach of contract was obiter dicta because the Full Court rejected ARU's breach of contract case. This is an artificial distinction, given the approach of Hill and Finkelstein JJ in that case. The tort in question was the tort of inducing breach of contract, and the Full Court addressed the availability of the remedy in contract first before addressing its availability in tort. Their conclusion on contract was fully reasoned as if it were the ratio decidendi of the case. I am not persuaded that the decision of the Full Court was plainly wrong. If the common law is to be revised so as to include a discretionary remedy of an account of profits as a remedy for breach of contract, given the traditional state of the law, such revision should only be made at appellate court level. The revision would need to decide the nature and extent of the availability of the remedy for breach of contract as well as whether the law as to exemplary damages should be revised instead.'

10 DAMAGES FOR LOSS OF A CHANCE

10.1 Background and broad principles

The scope and basis for recovery of damages for loss of a chance has been considered on numerous occasions by the appellate courts in both Australia and England. In tort the question has frequently arisen in personal injury claims and in both contract and tort the question has arisen in relation to the provision of negligent advice by professional advisers. In these types of claim,

assessing future possibilities and past hypothetical events becomes relevant to the quantification of damages.

The facts in *Malec v J C Hutton Pty Ltd*[249] provide an important illustration of the issue. The plaintiff contracted acute brucellosis as a result of the defendant's negligence. This in turn caused the plaintiff to develop a neurotic condition. However on the evidence there was a chance that the plaintiff could have developed the neurotic condition in any event. It was found that on a balance of probabilities the defendant's negligence caused the relevant pain and suffering. However, as noted by the High Court when quantifying the plaintiff's loss it would be relevant to take account of the chance that factors, unconnected with the defendant's negligence, might have brought about the onset of a neurotic condition in any event. Brennan and Dawson JJ wrote at 639 - 640:

'The fact that the plaintiff did not work is a matter of history, and facts of that kind are ascertained for the purposes of civil litigation on the balance of probabilities: if the court attains the required degree of satisfaction as to the occurrence of an historical fact, that fact is accepted as having occurred. By contrast, earning capacity can be assessed only upon the hypothesis that the plaintiff had not been tortiously injured: what would he have been able to earn if he had not been tortiously injured? To answer that question, the court must speculate to some extent. As the hypothesis is false — for the plaintiff has been injured — the ascertainment of earning capacity involves an evaluation of possibilities, not establishing a fact as a matter of history. Hypothetical situations of the past are analogous to future possibilities: in one case the court must form an estimate of the likelihood that the hypothetical situation would have occurred, in the other the court must form an estimate of the likelihood that the possibility will occur. Both are to be distinguished from events which are alleged to have actually occurred in the past.'

10.2 Causation and quantification

Where a plaintiff suffers loss as a result of negligent advice there is a hypothetical question relevant to the quantification of damages, namely, what would the plaintiff have done if the advice had been provided without negligence. In this context both the English and Australian cases have highlighted the important distinction to be drawn between causation and quantification. The central question raised in some of the English cases is when does the issue of causation end and the process of quantification begin.

In considering the proper approach to the assessment of damages for future or potential events the starting point is the following passage in the joint reasons in *Malec* at 642:

'When liability has been established and a common law court has to assess damages, its approach to events that allegedly would have occurred, but cannot now occur, or that allegedly might occur, is different from its approach to events which allegedly have occurred. A common law court determines on the balance of probabilities whether an event has occurred. If the probability of the event having occurred is greater than it not having occurred, the occurrence of the event is treated as certain; if the probability of it having occurred is less than it not having occurred, it is treated as not having occurred. Hence, in respect of events which have or have not occurred, damages are assessed on an all or nothing approach. But in the case of an event which it is alleged would or would not have occurred, or might or might not yet occur, the approach of the court is different. The future may be predicted and the hypothetical may be conjectured. But questions as to the future or hypothetical effect of physical injury or degeneration are not commonly susceptible of scientific demonstration or proof. If the law is to take account of future or hypothetical events in assessing damages, it can only do so in terms of the degree of probability of those events occurring. The probability may be very high — 99.9 per cent — or very low — 0.1 per cent. But unless the chance is so low as to be regarded as speculative — say less than 1 per cent — or so high as to be practically certain — say over 99 per cent — the court will take that chance into account in assessing the damages. Where proof is necessarily unattainable, it would be unfair to treat as certain a prediction which has a 51 per cent probability of occurring, but to ignore altogether a prediction which has a 49 per cent probability of occurring. Thus, the court assesses the degree of probability that an event would have occurred, or might occur, and adjusts its award of damages to reflect the degree of probability. The adjustment may increase or decrease the amount of damages otherwise to be awarded.'

Although *Malec* involved a tort claim the principles noted in the joint reasons have been applied by the High Court in the context of a commercial transaction. In *Sellars v Adelaide Petroleum NL*[250], Mason CJ, Dawson, Toohey and Gaudron JJ in their joint judgment said at 355:

'..., we consider that acceptance of the principle enunciated in Malec requires that damages for deprivation of a commercial opportunity, whether the deprivation occurred by reason of breach of contract, tort or contravention of s52(1), should be ascertained by reference to the court's assessment of the prospects of success of that opportunity had it been pursued. The principle recognised in *Malec* was based on a consideration of the peculiar difficulties associated with the proof and evaluation of future possibilities and past hypothetical fact situations, as contrasted with proof of historical facts. Once that is accepted, there is no secure foundation for confining the principle to cases of any particular kind.

'On the other hand, the general standard of proof in civil actions will ordinarily govern the issue of causation and the issue whether the applicant has sustained loss or damage. Hence the applicant must prove on the balance of probabilities that he or she has sustained some loss or damage. However, in a case such as the present, the applicant shows some loss or damage was sustained by demonstrating that the contravening conduct caused

the loss of a commercial opportunity which had some value (not being a negligible value), the value being ascertained by reference to the degree of probabilities or possibilities. It is no answer to that way of viewing an applicant's case to say that the commercial opportunity was valueless on the balance of probabilities because to say that is to value the commercial opportunity by reference to a standard of proof which is inapplicable.

'The conclusion which we have reached on this question finds support in other considerations. The approach results in fair compensation whereas the all or nothing outcome produced by the civil standard of proof would result in the vast majority of cases in over-compensation or under-compensation to an applicant who has been deprived of a commercial opportunity. Furthermore, it is an approach which conforms to the long-standing practice of taking into account contingencies in the assessment of damages.'

Brennan J in a separate judgment said at 362:

'*Gates v City Mutual Life Assurance Society Ltd* shows that, for the purposes of s82(1) of the Act, the loss of a mere opportunity to acquire a benefit is not in itself a loss, but the loss of the benefit will be such a loss if the plaintiff proves that he could and would have taken the opportunity and that the benefit would then have been yielded. That is tantamount to saying that the benefit is a loss in respect of which an amount may be recovered if the links in the chain of causation up to the loss of the benefit are proved. In this respect the law under s82(1) is no different from the law of torts.'

His Honour also noted at 364:

'As a matter of common experience, opportunities to acquire commercial benefits are frequently valuable in themselves, not only when they will probably fructify in a financial return but also when they offer a substantial prospect of a financial return. The volatility of the market for speculative shares testifies to both the valuable character of commercial opportunities and the difficulty of assessing the value of opportunities which are subject to serious contingencies. Provided an opportunity offers a substantial, and not merely speculative, prospect of acquiring a benefit that the plaintiff sought to acquire or of avoiding a detriment that the plaintiff sought to avoid, the opportunity can be held to be valuable. And, if an opportunity is valuable, the loss of that opportunity is truly "loss" or "damage" for the purposes of s82(1) of the Act and for the purposes of the law of torts. In a statute which is intended to govern commercial transactions, it would be pedantically inappropriate to exclude the loss of a valuable commercial opportunity from the categories of "loss" and "damage" in s82(1) of the Act.

'However, a causal relationship between the loss of such an opportunity and the defendant's contravening or tortious conduct must be proved before any issue of assessment of the amount of the loss arises...

To prove the substantiality of a prospect of acquiring a benefit or of avoiding a detriment and what would have been the plaintiff's actions if the opportunity had been offered, it will usually be necessary to tender evidence to establish the plaintiff's objectives and the contingencies in the way of their achievement. Evidence of that kind will bear upon both the existence and the value of the lost opportunity.'

And finally his Honour observed at 368:

'Although the issue of a loss caused by the defendant's conduct must be established on the balance of probabilities, hypotheses and possibilities the fulfilment of which cannot be proved must be evaluated to determine the amount or value of the loss suffered. Proof on the balance of probabilities has no part to play in the evaluation of such hypotheses or possibilities: evaluation is a matter of informed estimation. However, where the amount of a loss depends upon the happening or non-happening of some event, it is unnecessary to speculate on the possibility that it might have happened and it is impermissible to do so. A plaintiff seeking to prove the amount of a loss does not obtain the right to argue for a possibility by refraining from adducing evidence of the fact. Nor, in my opinion, is it necessary or permissible to speculate on the prospects that a court might have awarded a pecuniary sum to a plaintiff who has lost a cause of action. The court will determine what, if anything, it would have awarded in an action to enforce that cause of action and that determination determines whether anything of value was lost and what its value was. Neither of these situations is relevant to the present case'.

In *Origin Energy LPG Ltd (formerly Boral Gas (NSW) Pty Ltd) v BestCare Foods Ltd,*[251] Lord JA succinctly stated the approach:

'[84] Where a claim is made for loss of a chance or opportunity caused by negligence (or breach of contract), the loss of that chance or opportunity must be proved on the balance of probabilities. Once the loss of a chance or opportunity has been so proved, then it is for the Court to value the possibility or prospect of that chance or opportunity (and this is not an exercise to be carried out on the balance of probabilities) (see *Malec v JC Hutton Ltd* [1990] HCA 20; (1990) 169 CLR 638; *Commonwealth v Amann Aviation Pty Ltd* [1991] HCA54; (1992) 174 CLR 64; *Sellars v Adelaide Petroleum NL* [1994] HCA 4; (1994) 179 CLR332 and, more recently, *Tabet v Gett* [2010] HCA12; (2010) 240 CLR537).

10.3 Contemporary application of the *Sellars v Adelaide Petroleum NL* methodology

The principles stated by the High Court in *Sellars* were considered in some detail and applied by the New South Wales Court of Appeal in *Prosperity Advisers Pty Ltd v Secure Enterprises Pty Ltd t/a Strathearn Insurance Brokers.*[252]

I turn to the facts.

Prosperity provided financial and planning services to its clients. Strathearn was an insurance broker based in Western Australia.

In early 2005 Prosperity approached Strathearn with a view to Strathearn placing professional indemnity insurance on its behalf. At that time Prosperity carried professional indemnity insurance with Allianz under a policy due to expire in February 2005. On 23 February 2005 Prosperity's then current broker provided quotations from a number of insurers in respect of the 2005/2006 year. Many of these insurers declined to cover financial planning activities including the provision of investment advice.

However, Strathearn was able to provide Prosperity with various options offered by QBE Insurance and in this regard recommended an option which covered Prosperity's accounting and financial services with a limit of indemnity for financial planning services of $2,000,000 for any one claim and $6,000,000 in aggregate. The proposed policy provided for an excess or deductible of $40,000 for each and every claim.

Importantly, the proposed policy included an aggregation clause so that multiple claims arising from causally connected acts, errors or omissions were treated as one claim for the purpose of applying the deductible. Prosperity took up this option and obtained the relevant professional indemnity policy from QBE Insurance.

Prosperity provided advice to some of its clients in respect of investment in mezzanine debt products promoted by the Westpoint Group.

Subsequently, the Westpoint Group failed as did the investments. The investors made claims against Prosperity for losses arising out of an alleged breach of a duty of care in the provision of investment advice. In turn Prosperity made a claim on QBE under its professional indemnity policy.

QBE's solicitors notified Prosperity that the policy conditions did not apply to aggregate the vast majority of the investor claims made against Prosperity with the consequence that the deductible applied to each claim.

Ultimately, Prosperity reached a settlement with QBE under which Prosperity contributed some $800,000 to a pool to be divided among Prosperity's clients.

Prosperity had earlier relied upon advice from Strathearn that its maximum deductible would be $120,000 and in the current proceedings sought to recover $680,000 from Strathearn for damages for breach of contract. The breach consisted in negligent advice as to the proper interpretation and application of the aggregation clause in the policy.

The substance of Prosperity's complaint was lucidly explained by Tobias JA:

'[25] In effect Prosperity's complaint was that Mr Stephen Hughes had failed to inform Mr Michael Hughes in their conversation of 24 February 2005 that depending on the circumstances, the claims of the 100 hypothetical clients referred to in the conversation might arise out of different acts, errors or omissions which would not be aggregated into one claim with the payment of only one, or at the most, three deductibles. It therefore alleged that if it had received accurate advice in relation to the operation of the aggregation clause (cl 6.7) of the Policy, it would have obtained or negotiated to obtain different policy wording either with QBE or some other professional indemnity insurer, with the result that the claims it faced would have been aggregated so that only one, or at the most three, deductibles were payable. In these circumstances, it would only have been required to pay a maximum of $120,000 into the pool and not $800,000.'

Tobias JA in delivering the judgment of the Court of Appeal sought to apply the principles formulated in Sellars.

Importantly, his Honour, noted:

'[73] In my opinion, the following propositions may be deduced from the above passages from Sellars as relevant to the present case:

'(a) Prosperity must prove on the balance of probabilities that it has sustained some loss or damage although in a case such as the present, it may do so by demonstrating that, on the evidence, Strathearn's conduct caused the loss of a commercial opportunity which had some value which was not negligible;

'(b) Thus there must be evidence as to what Prosperity would have done had it known that the QBE policy did not offer cover on the terms it wanted and, further, that cover was or at least may have been available on those terms elsewhere;

'(c) Upon the assumption that Prosperity proved that had it known that the QBE policy would not provide it with the cover it sought, it would have proceeded through its broker into the market to seek such cover, it must still prove as a matter of probability or possibility that such cover would have been available and provided to it at a price and on terms which it was prepared to pay and accept; in other words, it must elicit evidence as to the value of the chance which it alleges it lost as a result of Strathearn's conduct;

'(d) It is thus impermissible, in the absence of evidence, to speculate on the possibility that such cover would have been obtainable; rather, the evidence must establish that there was a substantial, and not merely a speculative, prospect of its availability. Prosperity cannot merely argue for a possibility by refraining from adducing evidence to support the probability or possibility that the cover sought was not only available but could be obtained on acceptable terms.'

Turning to the joint reasons in *Malec,* Tobias JA noted:

'[87] Prosperity placed considerable reliance upon the passage from the joint judgment of Deane, Gaudron and McHugh JJ in *Malec* which I have recorded at [64] above to support the proposition that a chance is so low as to be regarded as speculative only if it is less than one per cent. However, in my opinion this would be a misunderstanding of what their Honours were saying. Certainly they regarded a chance as being speculative if it was less than one per cent but they were not in my view laying down some form of standard (one per cent) or benchmark above which a lost chance would not be speculative. Prosperity accepted that this was so.'

In dismissing Prosperity's appeal Tobias JA said:

'[85] It is true that Prosperity advanced its case at trial upon the basis that as a consequence of Strathearn's breaches, it lost the opportunity to seek the policy it required from the relevant market. However, I do not accept the submission that the primary judge failed to identify the lost chance as being the lost opportunity to actually obtain the policy of the requisite type. His Honour made it clear (at [29] and [32]) first, that Prosperity's primary case was that it would have been able to negotiate an amendment or endorsement to the standard terms of an insurer's existing policy to incorporate an aggregation clause of the type that it sought and, secondly, that it was probable or possible that such negotiations may have been successful. His Honour was conscious of the relevant principles and of the requirement for Prosperity to establish that it would have had "a substantial prospect of acquiring" a policy of the requisite type: Sellars at 368. In my opinion, the first error of the primary judge asserted by Prosperity cannot be sustained.'

The critical point was that, on the evidence, Prosperity had failed to establish that having regard to the state of the insurance market at the time it had any realistic prospect of obtaining a policy with the relevant aggregation clause. Thus, had Strathearn provided appropriate advice it would have made little economic difference to the ultimate outcome.

10.4 The position in England

The principles governing an award of damages for loss of a chance were also recently analysed by the Queen's Bench Division of the High Court in *The Trustees of Ampleforth Abbey Trust v Turner & Townsend Project Management Limited.*[253] The court in considering the position relied upon the earlier Court of Appeal decision in *Allied Maples Group Ltd v Simmons & Simmons.*[254]

I turn first to Allied Maples. The plaintiff entered into a corporate takeover agreement with the vendor. The defendant solicitors in breach of their retainer failed to give the plaintiff proper advice as to the incorporation of provisions appropriate to protect the plaintiff against the risk of certain third party liabilities.

As found by the trial judge, had the defendant been given appropriate advice the plaintiffs would have sought to negotiate with the vendor with a view to obtaining contractual protection against the liabilities. The defendant contended that it could not be shown on a balance of probabilities that the vendor would have agreed to give the contractual protection.

Stuart-Smith LJ noted at 1609:

'In these circumstances, where the plaintiff's loss depends upon the actions of an independent third party, it is necessary to consider as a matter of law what it is necessary to establish as a matter of causation, where causation ends and quantification of damage begins.'

His Lordship noted at 1614:

'But, in my judgment, the plaintiff must prove as a matter of causation that he has a real or substantial chance as opposed to a speculative one. If he succeeds in doing so, the evaluation of the chance is part of the assessment of the quantum of damage, the range lying somewhere between something that just qualifies as real or substantial on the one hand and near certainty on the other. I do not think that it is helpful to seek to lay down in percentage terms what the law at upper ends of the bracket should be.

All that the plaintiffs had to show in causation on this aspect of the case is that there was a substantial chance that they would have been successful in negotiating total or partial (by means of a cap liability) protection.'

The Court of Appeal concluded that the plaintiff had satisfied the causation requirement and it was a matter for the judge to consider the degree of probability of the negotiations having a successful outcome in the light of the evidence.

In *Ampleforth Abbey Trust* the defendants were engaged by the trustees as project manager in respect of a major redevelopment of school premises. In breach of a contractual duty the defendants failed to ensure that an executed construction contract was brought into existence between the trustees and the builder. The whole of the works were carried out under a series of letters of intent issued by the trustees although prepared by the defendants. The proposed building contract under negotiation with the builders contained a liquidated damages clause in respect of late completion by the builder. No such clause was incorporated in any of the letters of intent.

Subsequently, a dispute arose between the trustees and the builder concerning late completion. The dispute was ultimately settled when the trustees agreed to pay certain sums to the builder. Due to the absence of a liquidated damages clause in the letters of intent no allowance in favour of the trustees was made in respect of late completion by the builder.

The trustees then commenced proceedings against the defendants contending that they had suffered economic loss arising out of the disadvantageous settlement brought about by the failure of the defendants to ensure the execution of a building contract. In substance the trustees were claiming the loss of a benefit or chance for a better outcome in their settlement negotiations with the builder.

The court in analysing the case considered that there were two steps.

First, establishing a causal link on a balance of probabilities between the loss complained of and the breach.

Secondly, the quantification of damages.

In respect of the first issue the Court having noted the principles set out by the Court of Appeal in *Allied Maples* observed:

'[134] In my judgment, the correct approach in the present case is accordingly as follows.

'(1) In order to establish causation of loss, the Trust must prove on the balance of probabilities:

'(a) that, if it had received appropriate advice, it would have acted in accordance with that advice;

'(b) that, if it had done so, there would have been a real or substantial chance, as opposed to a speculative chance, that Kier would have signed the contract including the liquidated damages provision; but it does not have to prove that Kier would have signed the contract;

'(c)'that the signed contract would materially have improved the Trust's position as against Kier;

'(d)'that the Trust would have availed itself of its improved position.

'(2)'If the Trust discharges the burden of proving that it has suffered loss, the court must assess the amount of that loss. The process of quantification of damages will require both (a) a valuation of the benefit that the Trust would have obtained if it had a contract and (b) an assessment of the size of the chance that Kier would have signed the contract.'

In respect of the causation point the court noted:

'[135] On the balance of probabilities, I find that, if it had received non-negligent advice, the Trust would have acted in accordance with advice and done what was necessary, for its part, to procure a signed contract.'

On the quantification point the court noted:

'[150] I find that, if TTPM had discharged its duty, there was a two-thirds chance that Kier would have signed the contract (including the liquidated damages provision) and a one-third chance that matters would have turned out much as they did, viz. with works proceeding throughout without a contract. Although it cannot be said that there was literally no chance that Kier would have walked off site and the Trust would have had to find a new contractor, I regard the chance of that having happened as minimal; to the extent that such a chance might have existed, I do not regard it as substantial enough to warrant a specific allowance, having regard to the necessarily broad approach involved in the assessment of the chances of having or failing to have a contract. There is no good reason to suppose that any of the matters identified by Kier and TTPM as standing in the way of a contract were intractable. As explained below, I reject the contention that Kier had unexpressed reasons of its own for being unwilling to sign the contract. It remains possible that, when concentrated efforts were made to finalise the contract, some previously unidentified problem would have been identified and would have prevented the parties concluding the contract within a short timescale. In such circumstances, the strong probability is that the matter would have proceeded in much the way it did, with continuing efforts to resolve the outstanding issues. Only an unrealistic caricature of the appropriate stance for TTPM to have taken, coupled with a failure to appreciate that the parties would necessarily have remained responsive to changing circumstances, would militate against that conclusion.'

11 DAMAGES FOR DISAPPOINTMENT

11.1 The general principle

As observed by Mason CJ in *Baltic Shipping Co v Dillon,*[255] pain and suffering is a well-known head of damage recoverable in actions for personal injury. And, in some circumstances at least, a plaintiff can recover damages for injury to his or her feelings caused by tortious conduct; assault, false imprisonment, malicious prosecution and defamation are causes in action for which a plaintiff may recover damages on that score.

However, the general rule accepted ever since *Hamlin v Great Northern Railways Co*[256] is that damages for anxiety, disappointment and stress are not recoverable in actions for breach of contract.

In an analysis of the exclusionary rule Mason CJ referred sympathetically to the dissenting view in the Supreme Court of Canada that the principle in *Hadley v Baxendale* is the test to be applied in determining an award of damages for disappointment or distress.

However Mason CJ concluded at 365:

'On the other hand, as a matter of ordinary experience, it is evident that, while the innocent party to a contract will generally be disappointed if the defendant does not perform the contract, the innocent party's disappointment and distress are seldom so significant as to attract an award of damages on that score. For that reason, if for no other, it is preferable to adopt the rule that damages for disappointment and distress are not recoverable unless they proceed from physical inconvenience caused by the breach or unless the contract is one the object of which is to provide enjoyment, relaxation or freedom from molestation. In cases falling within the last mentioned category, the damages flow directly from the breach of contract, the promise being to provide enjoyment, relaxation or freedom from molestation. In these situations the court is not driven to invoke notions such as "reasonably foreseeable" or "within the reasonable contemplation of the parties" because the breach results in a failure to provide the promised benefits. In my view, this approach to the problem is to be preferred to the artificial expedient of saying that damages of the kind under consideration will be awarded for breaches of non-commercial contracts but not for breaches of commercial contracts. That expedient requires a distinction to be drawn between commercial and non-commercial contracts; that distinction is by no means easy to draw and, in any event, it is not a distinction which should necessarily be decisive in determining whether such damages are available or not.'

Brennan J who focused on an approach based on *Hadley v Baxendale* noted at 368 and 369:

'In one sense, a promisee's disappointment of mind flows naturally whenever a contractual promise is not fulfilled. This is the point made by Lord Atkinson in *Addis v Gramophone Company Ltd.* But where disappointment of mind is no more than a mental reaction to a breach of contract and damage flowing therefrom, the law has treated such a mental reaction as too remote. Thus, in *Fink v Fink,* Dixon and McTiernan JJ held that, in assessing the amount to be awarded for breach of contract, "[r]esentment, disappointment and the loss of esteem of friends are not proper elements". In my opinion, there is a sound policy underlying this rule.

'The institution of contract, by which parties are empowered to create a charter of their rights and obligations inter se, can operate effectively only if the parties, at the time when they create their charter, can form some estimate of liability in the event of default in performance. But no approximate estimate of liability could be formed if the subjective mental reaction of an innocent party to a breach and resultant damage were added on as further damage without proof of pecuniary loss by the innocent party. If the mental reaction to breach and resultant damage were itself a head of damage, the liability of a party in breach would be at large and liable to fluctuation according to the personal situation of the innocent party. If a promisor were exposed to such an indefinite liability in the event of breach, the making of commercial contracts would be inhibited, the assignment of a contractual right would carry new risks for the party subject to the reciprocal obligation, and trade and commerce would be seriously impeded.'

11.2 Wrongful dismissal and *Addis v Gramophone Co Ltd*[257]

A specific principle relating to damages for distress has developed in the context of employment law. In *Addis* the House of Lords held that an employee who has been wrongfully dismissed cannot recover damages for injured feelings based on the manner in which the wrongful dismissal took place nor can such employee recover for any loss he may sustain from the fact that his having been dismissed of itself makes it more difficult for him to obtain fresh employment. As noted by Lord Nicholls in *Malik v Bank of Credit & Commerce International SA*[258] at 38:

'In particular, *Addis's* case is generally understood to have decided that any loss suffered by the adverse impact on the employee's chances of obtaining alternative employment is to be excluded from an assessment of damages for wrongful dismissal.'

The correctness of *Addis* was accepted by the High Court in *Baltic Shipping.* However, as noted by Barrett JA in *Shaw v State of New South Wales:*[259]

'[96] In *Baltic Shipping,* the members of the High Court quoted Lord Loreburn's observation in *Addis* that damages awarded to a dismissed employee for breach of contract "cannot include compensation either for the injured feelings of the servant, or for the loss he may sustain from the fact that his having been dismissed of itself makes it more difficult for him to obtain fresh employment". But *Baltic Shipping* itself was concerned with only compensation for injured feelings. There was no occasion to deal directly with the compensability of "the loss he may sustain from the fact that his having been dismissed of itself makes it more difficult for him to obtain fresh employment".'

Barrett JA also noted developments in English law which indicated that the *Addis* principle should be confined to wrongful dismissal cases and that it had no application to breaches of the subsequently recognised implied "trust and confidence" term.

On a more general level his Honour noted:

'[117] At large in both *Baltic Shipping* and *Russell* was the question whether, if a dismissed employee establishes breach of contract on the part of the employer and shows that he or she, despite reasonable efforts, did not find new employment for a particular period, the financial loss actually sustained through unemployment for that period is compensable (assuming that a causal link is proved). It is arguable that loss of that kind is, in the words of Alderson B in *Hadley* (at 355), loss which "may fairly and reasonably be considered" as arising "according to the usual course of things" or "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 therefore appears that the correctness of the second element of the *Addis* principle remains an open question in Australian law.

12 INTEREST AS DAMAGES

12.1 The position at common law

Historically the common law did not allow the recovery of interest for the late payment of a debt or damages.

As noted by Mason P in *Palasty v Parlby:*[260]

'[50] The nineteenth century rules for calculating damages generally ignored losses stemming from delay in receipt of contract damages. The decision in *London Chatham and Dover Railway Co v South Eastern Railway Co* [1893] AC 429 confirmed these cases and required common law courts to refuse damages to compensate a plaintiff for losses stemming from delay in recoupment having been wrongfully kept out of money due under a contract, even where such losses were direct and foreseeable.'

The strictness of the common law position was ameliorated by statute both in England and in Australia. For example, in New South Wales the power of the Supreme Court to award interest up to judgment is established by section 100 of the Civil Procedure Act 2005. Relevantly, section 100 provides:

(1) In proceedings for the recovery of money (including any debt or damages or the value of any goods), the court may include interest in the amount for which judgment is given, the interest to be calculated at such rate as the court thinks fit:

(a) on the whole or any part of the money, and

(b) for the whole or any part of the period from the time the cause of action arose until the time the judgment takes effect.

Brereton J in *Hexiva Pty Ltd v Lederer (No.2)*[261] said:

'[7] The effect of the statutory provision is that pre-judgment interest can be awarded on a claim for damages, whereas at common law interest could not be claimed on damages since there was no entitlement to the sum until judgment.'

Although there has been some relaxation in the common law position in England the Australian High Court in *Hungerfords v Walker*[262] comprehensively swept aside the historical restraint of the common law and proceeded to reformulate the

basis upon which interest could be recovered as an element of a damages claim.

12.2 Interest as damages for breach of contract — *Hungerfords v Walker*

In *Hungerfords,* Mason CJ and Wilson J in their joint reasons noted the key question at 132:

'This appeal raises the important question whether, at common law, a court, when awarding damages for breach of contract or negligence, can include in its award damages, assessed by reference to appropriate interest rates, for the loss of the use of money which the plaintiff paid away and lost as a direct consequence of the defendant's breach of contract or negligence.'

In dealing with this question their Honours noted the development in English law which sought to ameliorate the historical common law by allowing recovery of interest in a breach of contract action but only where the loss claimed could be characterised as special damages falling within the second limb of *Hadley v Baxendale*. In rejecting this piecemeal approach their Honours noted at 142:

'If a plaintiff sustains loss or damage in relation to money which he has paid out or forgone, why is he not entitled to recover damages for loss of the use of money when the loss or damage sustained was reasonably foreseeable as liable to result from the relevant breach of contract or tort? After all, that is the fundamental rule governing the recovery of damages, according to the first limb in *Hadley v Baxendale Ltd* ... The object of the second limb in *Hadley v Baxendale* was to include loss arising from special circumstances of which the defendant had actual knowledge when that loss does not fall within the first limb because it does not arise from "the ordinary course of things" of which the defendant has imputed knowledge ... To allow a plaintiff to recover special, but not general, damages, is illogical, subverts the second limb in *Hadley v Baxendale* from its intended purpose and introduces a new element into the general measure of damages for negligence.'

Their Honours noted at 149:

'But we see no reason for allowing the reluctance of the common law to extend to cases where the defendant's breach of contract or negligence has caused the plaintiff to pay away or the defendant to withhold money and, as a result, the plaintiff has been deprived of the use of the money so paid away or withheld. The recovery of compensation for the loss may be ascribed to the operation of the second limb in *Hadley v Baxendale*. However, we would prefer to put it on the footing that it is a foreseeable loss, necessarily within the contemplation of the parties, which is directly related to the defendant's breach of contract or tort.'

Additionally, Mason CJ and Wilson J identified the two possible bases upon which interest as damages could be calculated as either:

(a) expense incurred; or

(b) opportunity cost.

Expense incurred relates to the cost of borrowing to make up for the money which would otherwise have been available to the plaintiff but for the defendant's breach of contract or negligence.

Alternatively, opportunity cost becomes appropriate where a plaintiff is not compelled to borrow. It represents the lost opportunity to invest. As their Honours noted at 144:

'Incurred expense and opportunity cost arising from paying money away or the withholding of moneys due to the defendant's wrong are something more than the late payment of damages. They are pecuniary losses suffered by the plaintiff as a result of the defendant's wrong and therefore constitute an integral element of the loss for which he is entitled to be compensated by an award of damages.'

In their joint judgment Brennan and Deane JJ noted at 152:

'There is, in our view, a critical distinction between an order that interest be paid upon an award of damages and an actual award of damages which represents compensation for a wrongfully caused loss of the use of money and which is assessed wholly or partly by reference to the interest which would have been earned by safe investment of the money or which was in fact paid upon borrowings which otherwise would have been unnecessary or retired.'

It is manifestly clear that to attract the Hungerfords principle the breach of contract relied upon must have caused or resulted in the plaintiff paying money away or the defendant withholding money properly due.

12.3 Establishing a claim

In *Hexiva Pty Ltd v Lederer (No.2)*[263] Brereton J compared the approach of the courts to claims for statutory interest with the approach to claims for interest as damages.

His Honour noted:

'[9] However, courts have apparently adopted a far more stringent approach to what is required to prove a claim for interest as damages, than to claims for statutory pre-judgment interest. Whereas the cases on statutory pre-judgment interest suggest that loss from late payment will be assumed, the cases in which interest is claimed as damages for deprivation of money suggest that the plaintiff bears the onus of establishing the loss, which is not presumed to arise from the mere withholding of money ...'

In this context Brereton J made specific reference to the observations of Giles J in *Hobartville Stud Pty Ltd v Union Insurance Co Ltd.*[264] Giles J noted at 363-4:

'In my view the plaintiff's submission misconceives the nature of damages for loss of use of money. The references to general damages do not invoke an assessment analogous to the award of damages for pain and suffering: they distinguish damages within the first limb of *Hadley v Baxendale* ... from damages within the second limb. It still remains necessary to undertake a factual investigation into the loss suffered through being held out of the money. At the end of the day it may be deter-

mined that market rates of interest are the appropriate measure of the loss, but that is not necessarily so. Whether the plaintiff would have made a profit from the use of the money withheld from it, and the amount of the profit, must be determined on the evidence, and there is not an automatic allowance of interest upon the money withheld.

'Accordingly, to recover interest as damages the plaintiff will need to bring forward specific evidence of its loss which, as noted by Giles J, will require a detailed investigation of all the relevant facts.'

12.4 The basis for computation

In *Sempra Metals Ltd v Inland Revenue Commissioners,*[265] the House of Lords although in the context of a restitutionary claim held that interest was to be calculated on a compound basis. However the appropriate rate is more problematic.

In *Heydon v NRMA Ltd (No 2),*[266] Mason J noted:

'[30] It would be intolerably burdensome if a court required evidence and argument in every case as to what rate or rates of interest would do justice to the principles which I have endeavoured to summarise. The interests of the parties and of the court, including the interest of consistency as a component of justice, are served by taking a broad, standard approach whereby interest is calculated according to pre-determined rates that the parties can take into account in their dealings during the litigation and in their endeavour to avoid wasteful disputation concerning its outcome.'

Some further guidance on computation is provided by the decision of Owen J in *The Bell Group Ltd (in liq) v Westpac Banking Corporation [No. 9].*[267] Although his Honour was concerned with interest as part of a claim for equitable compensation rather than as a restitutionary claim, the difference does not impact on the relevance of his Honour's comments.

Importantly his Honour noted:

'[9718] I have looked at the rates applied to judgment debts from time to time under section 32 of the Supreme Court Act 1935 (WA) and section 8(1) of the Civil Judgments Enforcement Act 2004 (WA). I have compared those rates with the Westpac business indicator rate. Interest at 1% below the business indicator rate would be approximately the mid-point between the judgment debt rate and the business indicator rate. *I do not pretend that there is much science in that line of reasoning. My task is to do practical justice. For want of any better measure .., I think the business indicator rate less 1% is fair. It does practical justice*.' (emphasis added)

His Honour also noted that interest was to be calculated on monthly rests.

13 Equitable compensation and account of profits

In section 5 above reference was made to the basis of the equitable remedy of account of profits by way of contrast with a common law claim for damages for breach of contract.

There is a further dichotomy to be addressed, namely, equitable compensation and account of profits.

The nature of the relationship between these remedies and their differing objectives was lucidly explained by the Full Federal Court in *V-Flow Pty Limited v Holyoake Industries (Vic) Pty Limited:*[268]

'[55] The object of the equitable remedy of compensation or damages is restitution of what the victim has lost. The question is whether the loss would have occurred but for the breach. While the monetary sum awarded to the victim is normally computed by reference to the detriment actually suffered by the victim, it may occasionally be computed by reference to the profit that has been made by the errant fiduciary. Nevertheless, the primary purpose of equitable compensation or damages is compensatory (*Nocton v Lord Ashburton* (1914) AC 932; *Re Dawson* (1966) 84 WN (pt 1) (NSW) 399). No element of penalty is involved. (Meagher, Gummow and Lehane, *Equity: Doctrines & Remedies* (4th ed) at [23-02]).

'[56] The obligation imposed by equity to pay damages or compensation is not fettered by the usual notions that serve to diminish the quantum of an award of damages at common law. The obligation imposed by equity upon an errant fiduciary is of a more absolute nature than the common law obligation to pay damages for tort or breach of contract. Thus, the obligation is not limited or influenced by common law principles governing remoteness of damage, foreseeability or causation (*Hill v Rose* (1990) VR 129 at 144). However, while foreseeability is not a concern in assessing equitable compensation or damages, the only losses that are made good are those that, on a common sense view of causation, are caused by the breach of duty (*Canson Enterprises Ltd v Boughton and Co* (1991) 3 SCR534 at 556).

'[57] On the other hand, the purpose of an account of profit is to prevent the unjust enrichment of the fiduciary by compelling the fiduciary to surrender any profits actually made by the fiduciary that were made improperly, and nothing beyond that. It is not to punish the errant fiduciary (*Dart Industries Inc v Décor Corporation Pty Ltd* (1993) 179 CLR 101 at 111) (*Dart*). The errant fiduciary is made to account for, and is then stripped of, profits made that it would be unconscientious for that person to retain, because they are profits made by the fiduciary dishonestly. For example, in the case of infringement of intellectual property rights, the account is limited to the profits of the wrongdoer during the period when the victim's rights were being infringed (*Colbeam Palmer Ltd v Stock Affiliates Pty Ltd* (1968) 122 CLR 25 at 34).'

In the earlier decision in *GM & AM Pearce & Co Pty Ltd v Australian Tallow Producers*[269] the Victorian Court of Appeal addressed the distinction between equitable compensation and account of profits. The court noted that a plaintiff entitled to recovery for breach of a fiduciary duty was bound to make an

election. Warren CJ (Chernof JA and Dodds-Streeton AJA, agreeing) noted:

'[56] A plaintiff, where faced with a choice between an account of profits or equitable compensation, must make a decision as to which one it will pursue. For instance, in *Tang Man Sit v Capacious Investments* the plaintiff was awarded an account of profits and compensation in the same suit and sought to enforce both remedies. However, in that case the Privy Council reiterated, as did the High Court in *Warman International Ltd v Dwyer* that an account for profits and an award of damages are alternative and not cumulative remedies. Normally, where both remedies are available, a plaintiff must elect between them. Ordinarily, the election need not be made before the trial starts and may be delayed until determination of the cause of action. There is therefore no difficulty where the plaintiff claims both equitable compensation and an account of profits in the prayer for relief, however, election must be made when (but not before) judgment is given. Where the plaintiff does not know which remedy is more favourable at the time of judgment on liability, the court may order discovery or other orders designed to give the plaintiff the information it requires to make the election.'

The Full Federal Court in *V-Flow* also noted the additional compensation remedy contained in s1317H of the Corporations Act. In a critical assessment of the provision the Court noted:

'[54] The language of s1317H is singularly inelegant. Section 1317H(1) provides that the court may order a person to compensate a corporation for damage suffered by the corporation, if the damage resulted from a contravention of relevant provisions of the Corporations Act by that person. Section 1317H(2) then appears to direct the court determining the damage suffered by the corporation to include, as damage, profits made by any person resulting from the contravention. That appears to refer to profits made, irrespective of whether there was countervailing damage suffered by the corporation. That is to say, the effect of s1317H(2) is definitional, in the sense that it brings into the compensatory scheme of s1317H the capacity for the court to order that the compensation include profits, even though there was no corresponding loss on the part of the corporation (*Grimaldi v Chameleon Mining (No 2)* 200 FCR296 at [630]-[631]). That scheme involves a conflation of the concepts of equitable compensation or damages, on the one hand, and account of profits, on the other.

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179 (1848) 154 ER 363
180 (1991) 172 CLR 60
181 (2009) 236 CLR 272
182 [2013] VSC 464
183 [2017] VSC 185
184 (1991) 171 CLR 506
185 [2005] HCA Trans 23
186 (1998) 45 NSWLR 262
187 [1999] 2 AC 22
188 (1988) 12 NSWLR 337
189 (1987) 9 NSWLR 310
190 Edelman J writing extra judicially was critical of the common sense approach and suggested that what is meant by causation is necessity commonly known as the "but for" test. His Honour noted:
'Although the test of necessity, as a sole test for causation, is not currently fashionable in Australia and England there are some signs that judicial opinion is shifting.
'One sign is the growing criticism of the dominant Australian approach which uses the language of "common sense causation". As Dixon J of the Victorian Supreme Court recently observed with great cogency, the "common sense" approach is not a legal test. In difficult cases, the "sense" of an answer is rarely "common" among judges.'
His Honour also noted that there are situations in which liability may be established in the absence of a causal link of which *Clark v Macourt* (2013) 253CLR 1 is an example: Edelman: *Unnecessary Causation* (2015) 89 ALJ 20.
191 [2011] NSWCA 259
192 (2007) 35 WAR 254
193 [2015] NSWCA 181
194 [2016] FCA 158
195 (2009) 239 CLR 420
196 [2013] HCA 19
197 [2013] NSWCA 311
198 (1854) 9 Exch 341
199 (2010) 240 CLR 432
200 (1992) 176 CLR 344
201 [1969] 1 AC 350
202 (1987) 9 NSWLR 310
203 [2009] 1AC 61
204 (1987) 9 NSWLR 310
205 (2002) 4 VR 252
206 [2009] 1 AC 61
207 [2006] NSWCA 334
208 [1966] 3 All ER 128
209 [2009] NSWCA 67
210 (2010) 2 Lloyds Rep 81
211 (1991) 174 CLR 64
212 (1951) 84 CLR 377
213 (1992) 176 CLR 344
214 [2016] QCA 134
215 (1992) 176 CLR 344
216 (1991) 174 CLR 64
217 (1988) 166 CLR 351
218 [2007] 2 AC 353
219 [2010] NSWCA 67
220 [2012] NSWCA 367
221 (2007) 35 WAR 254

222 [2006] NSWCA 133 at paragraph 57
223 [2000] NSWCA 275
224 [2000] NSWCA 313
225 [2011] NSWCA 188
226 (1974) 2 NSWLR 235 at 239
227 [2013] QCA 67
228 1986 VR 507 at 513
229 [2017] NSWSC 1136
230 [2012] NSWCA 367
231 [2005] NSWCA 443
232 [2016] NSWCA 123
233 (2013) 253 CLR 1
234 at 30
235 [1920] 2 KB 11
236 The decision of the majority in favour of Dr Clark was trenchantly criticised by Carter, Courtney and Tolhurst in their article: 'Issues of Principle in Assessing Contract Damages' (2014) *Journal of Contract Law* 171. The authors sought to identify five bases on which *Clark v Macourt* was wrongly decided. One of their key criticisms was expressed at 204:

'Second, consistently with its own prior decisions, in order to identify whether a prima facie measure was relevant, and to apply that measure, the court was required to characterise the transaction. Since the choice of prima facie measure depends on the nature of the contract and the obligation breached by the defendant, the appropriate prima facie measure was the sale of goods measure as applied to the business as a whole. The contract was a sale of business, not an agreement to transfer particular assets purchased severally. The nature of the stock of sperm as an asset, including the fact that it was not "sold" to the purchaser, pointed strongly against a selective approach. So also did the way the price was arrived at. The breach of warranty measure in *Clark v Macourt* was therefore the difference between the warranted value of the business and the value of the business transferred to the Purchaser. Since there was no evidence of either, the purchaser's claim should have failed.'

237 [1998] QB 87
238 [2014] NSWSC 708
239 [2015] NSWCA 181 at 27.
240 (1987) 9 NSWLR 310
241 (2009) NSWCA 224
242 [2012] 83 NSWLR 710
243 (1993) 179 CLR 101
244 (2013) 296 ALR 418
245 [2000] 4 All ER 385
246 (2000) 173 ALR 702
247 [2003] WASCA 142
248 [2013] SASC 91
249 (1990) 169 CLR 638
250 (1994) 179 CLR 332
251 [2013] NSWCA 90
252 [2012] NSWCA 192
253 [2012] EWHC 2137
254 [1995] 4 All ER 907
255 (1993) 176 CLR 344 at 359
256 (1856) LJ Ex 20
257 [1909] AC 488
258 [1998] AC 20
259 [2012] NSWCA 102
260 [2007] NSWCA 345
261 [2007] NSWSC 49
262 (1989) 171 CLR 125
263 [2007] NSWSC 49
264 (1991) 25 NSWLR 358
265 [2008] 1 AC 561
266 (2001) 53 NSWLR 600
267 (2008) 39 WAR 1
268 (2013) 296 ALR 418
269 [2005] VSCA 113

PPSA models: easy as ABCD?

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1 INTRODUCTION

This paper is the final in a series of three papers, the first paper being 'PPSA models: a minimalist approach'[1] and the second, 'Chains of leases: aligning PPSA models with commercial expectations'.[2]

These papers have been prompted by the Final Report on the Review of the Personal Property Securities Act 2009 ('Whittaker Report'). In 2015 it put forward[3] a model for explaining how the Personal Property Securities Act 2009 (Cth) ('PPSA') applies to transactions in which under general law the secured party has or obtains ownership and, in the case of goods, possession of those goods lies with the grantor. Examples include a sale under a retention of title arrangement and certain types of leases and bailments. That model — described by the Whittaker Report as the unitary model — treats the grantor as (or as if it were) the owner for the purposes of the PPSA and, in the case of goods, characterises the transaction as a 'transfer' of the goods to the grantor by the secured party.[4]

In 'PPSA models: a minimalist approach' we contend that the unitary model is more aptly described as the 'recharacterisation model' and develop our arguments in favour of a different model. This model is described in the Whittaker Report as the 'possession model'.[5] However, we use instead the title 'minimalist model' to emphasise that while it too embraces the new statutory regime, it eschews any assumption that the grantor is (or is treated as) owner. Rather, in the case of goods, the minimalist model confirms the grantor's interest as that of legal possession and the transaction as a delivery of possession of the goods. While under both models the interest of the person who is the owner under general law is acknowledged as a security interest under the PPSA and dealt with accordingly by the PPSA, the minimalist model in our view more fully reflects the express wording of the statute and more readily achieves PPSA objectives of clarity, certainty and transparency.

In this paper, we analyse in Part 2 the practical consequences of the models in various scenarios and identify the major points of difference. These scenarios are often colloquially referred to as 'ABCD priority problems'. They envisage situations where, for example, A, the grantor of a security interest over goods in favour of a secured party, B, sells, leases or otherwise bails the goods to a third party, C, who either grants (or has previously granted) a security interest to D or sells, leases or otherwise bails the goods to D.[6] In our second paper, 'Chains of leases: aligning PPSA models with commercial expectations' we explore these issues in the very specific and technical context of 'lease chains' — a difficult and controversial area that in Australia is currently proving problematic. As the title foreshadows, we raise there the important question of how the different models align with reasonable commercial expectations.

The practical value in investigating these two models is becoming increasingly evident as Australian courts provide varying explanations as to how the PPSA operates. A recent decision handed down by the South Australian Full Court in *Samwise Holdings Pty Ltd v Allied Distribution Finance Pty Ltd* ('*Samwise Holdings*')[7] on 14 September 2018 discloses some of the complexities involved in grappling with concepts such as 'possession' and 'collateral' under the PPSA.[8] These are examined in Part 3. Part 4 concludes.

Discussion in this paper draws generally on a table, which we have set out as an Appendix. This table is based on that put forward in Annexure C to the Whittaker Report which sets out consequences in various ABCD scenarios of applying the recharacterisation model. It shows in mark-up the changes that would be made to the original table under the minimalist model and demonstrates the effect of that model on the various scenarios covered. In doing so, it responds directly to Recommendation 51 of the Whittaker Report, which proposed[9] that the Commonwealth Government not only 'provide stakeholders with an opportunity to present further arguments in support of the competing models' but also, more specifically, 'allow ... proponents of the 'possession' model to complete a corresponding version of the table that is attached to this report as Annexure C'.

Our Appendix substitutes the term 'goods' for that of 'collateral' which is used by the Report's Annexure C. The analysis in

Annexure C is confined to tangible property and hence is more restricted in scope than the use of the broader term 'collateral' implies. Furthermore, 'collateral' is inherently ambiguous and its use in Annexure C risks begging the question of whether the relevant secured property is the thing itself or a right in it.[10]

2 RECHARACTERISATION OR MINIMALIST MODEL FOR THE PPSA? THE PRACTICAL CONSEQUENCES

In this section, we focus on those transactions in the Appendix where substantive differences arise between the two models. As fact patterns numbered 2-3 in the Appendix show, the choice of model does not influence the outcome in situations where there is a transfer of ownership and possession under general law. Those fact patterns deal with transactions involving 'an outright sale for cash' and 'an outright sale, with security back for the unpaid purchase price'. The choice, however, becomes critical under arrangements where ownership and possession are divided: as happens under sales of goods on retention of title terms and leases of goods under finance leases and/or PPS leases. Most of these common examples are detailed in the Appendix as fact patterns 4-6 and are discussed here in [2.1]. Short-term operating leases detailed in fact pattern 1 are examined in [2.2], while [2.3] and [2.4] analyse the operation of the models in two other situations which are not expressly covered by Annexure C but which flow from the analysis adopted in the Annexure and the text of the Whittaker Report.

The most disturbing scenario for secured parties is likely to be the first scenario in [2.1], particularly in so far as it relates to leases amounting to security interests.[11]

2.1 Goods: grantor of a security interest becomes a secured party (eg, by leasing the goods to a third party)

Where A has granted a perfected security interest[12] to B, A reserves title and enters into a transaction with C under which A's ownership becomes a security interest granted by C (eg, a PPS lease[13] or an in substance security lease to C,[14] or a retention of title sale[15] to C).

(a) Recharacterisation model

Under the recharacterisation model, according to the Whittaker Report, B can lose (and to a degree win) as follows, even though B has protected its security interest by perfection.[16] A critical point is that B needs to take further action to maintain perfection. The position is as follows.

As C is to be treated as the owner, there is a 'transfer' from A to C for the purposes of s34 and s66, with the following consequences.

- On grant of the lease, a financing change statement or new financing statement is necessary for B's security interest, because C becomes the grantor. If it was done by financing change statement, another financing change statement would presumably be necessary on the expiry of the lease when A becomes grantor again. But in our view at all times there would still need to be a registration with respect to B's security interest over A's rights — necessitating parallel registrations of the same security interest, for each of A and C as grantor.
- If B gave its consent to the reservation of title security interest which the model treats as a transfer, B's security interest in the goods (but not their proceeds) would arguably be extinguished. This is on the basis that a transfer is a 'disposal' for the purposes of s32(1)(a)(i), as discussed in 'Chains of leases: aligning PPSA models with commercial expectations'.[17]
- Unless and until the financing statement is registered as against C, B's security interest in the goods can only be temporarily perfected. This has two consequences. Under s52 B can lose its security interest over the goods if C sells to D, even if C holds its interest subject to B's security interest. If B's security interest over the goods is not reperfected by registration within the relevant temporary perfection period, it will cease to be perfected. In practice, B may not be sufficiently aware of this issue to lodge a statement for registration, and so may become unperfected. It should be noted (though this is not mentioned in the Whittaker Report) B's security interest should still be fully effective over A's rights under its security interest.
- On the other hand, B's security interest is under s67 a transferor-granted security interest. That would generally give it priority over other security interests granted by C, even where s55 or another general priority provision might have given priority to those other security interests (for example, if they were the first to achieve registration).

The model could therefore be seen as having the advantage of ensuring this super-priority for B. But there are two limitations. First, B would need to lodge a financing change statement or financing statement to protect itself (which may often not happen in practice) . Second, B would in any event still have a valid security interest over A's security interest, which will rank ahead of those other security interests, at least if A's security interest is perfected as a PMSI in time.

- If A fails to perfect its security interest over the goods against C, then on C's insolvency that security interest vests in C. If C has taken free of B's security interest,[18] then under the recharacterisation model, as it is outlined in the Whittaker Report, B would have nothing.
- However, even in this model, it could nonetheless be argued that B still has its perfected security interest over A's rights in the goods that have now vested in C, and to that extent C takes those rights subject to it.[19]

(b) Minimalist model

For the minimalist model, B is more protected from A's actions or inactions and from C's insolvency. B does not have to take further action to respond to the security interest arising between

A and C. In priority disputes with holders of security interests granted by C, B's priority is dependent on the application of the default priority rules under s55.[20]

• Unless the transaction involving the security interest from C to A involves an actual transfer according to general law principles, there is no transfer and no need for B to file a financing change statement or a new financing statement.

• Unless it is a transfer in the usual meaning of that word, the dealing with C is free of B's security interest only if and to the extent that a specific provision of the PPSA so provides, and not on the basis that B's security interest is unperfected as a result of not taking the further action of reperfecting within the relevant time period, nor on the basis that it is a 'disposal' under s32(1)(a)(i).

• If A fails to perfect against C, but B's security interest is perfected as against A, on the insolvency of C, B's security interest is not affected by s267, and it does not vest in C. A's security interest — its ownership rights — vests in C, but the goods are still subject to B's security interest.[21]

• A priority conflict between B and the holder of a security interest granted by C as perfected secured parties is resolved under s55 and not ss66-68. B wins where it has registered its financing statement first. B is vulnerable in respect of the goods in circumstances not discussed in the table where C has in fact previously given D an All PAP Security Interest and D's registration is earlier than that of B.[22] However, where A's security interest (its ownership) has priority over D (for example, because a registration as a PMSI was made in sufficient time) in some circumstances B may be able to take advantage of that priority through its security interest over A's ownership/security interest, for example where A enforces against C and C ceases to have sufficient rights in the goods for D's security interest to attach to the goods, or where C (or D when enforcing) disposes of the goods in circumstances where the buyer does not take free of A's title.

See 'ABCD' fact patterns 4, 5 and 6 in the Appendix.

2.2 Goods: grantor of a security interest grants short-term lease of goods

Where owner A leases goods to C under a short-term lease which does not give rise to a security interest, and A is the grantor of a security interest to B, and C the grantor of a security interest to D, the differences are less stark for B. B is less at risk, but D gets a very different interest, and there is a different analysis.

(a) Recharacterisation model

In the recharacterisation model, according to the Whittaker Report:

• C could take a lease free of B's security interest (ie, it gets possession and its rights under the lease during the term of lease free of interference from B).

• Whether or not C takes free, D only gets a security interest over C's possessory rights in the goods under the lease.[23] B's interest would defeat D on lease termination.[24]

(b) Minimalist model

For the minimalist model:

• C could take the lease free of B's security interest (ie, it gets possession and its rights under the lease during the term of lease free of interference from B).

• Whether or not C takes free, D gets a security interest over the goods and not just the possessory interest, but that security interest is defeasible by, or subject to, A's rights as owner. A cannot retake possession while the lease is on foot. B retains a valid security interest over the goods, but where C does take its lease free of B's security interest, B also cannot take possession while the lease is on foot. A priority dispute between B and D is resolved by application of the default priority rules under s55, but B can take advantage of A's rights as owner in respect of the goods, to which D's interest is subject, in some circumstances.

See 'ABCD' fact pattern 1 in the Appendix.

2.3 Non-goods: grantor of a security interest becomes a secured party (eg, by sale to a purchaser under a retention of title arrangement)

This is a fact pattern similar to Whittaker Report fact pattern 4, but arising where the collateral is not goods and A retains title (eg, A sells financial collateral, like shares or a chose in action to C under a retention of title).[25] The Whittaker Report and most texts do not deal with the scenario.

The scenario assumes that C has 'rights in the collateral', sufficient to enable the security interest to attach under s19(2) to that collateral. C cannot have possession as the property is a chose in action.[26]

(a) Where C sells to D:

• In the recharacterisation model, C would presumably be treated as owner, and D as a 'buyer', B is temporarily perfected and D gets the asset free of B's security interest.

• In the minimalist model, D only gets C's rights under the ROT contract, unless s46 or another specific taking free provision applies.

(b) Where C grants a security interest to D:

(i) In a D v A priority dispute:

• in the recharacterisation model, priority is determined by PPSA priority provisions.

• in the minimalist model, the question is whether C's rights (which are not possession) are sufficient to enable D's security interest to attach to the underlying collateral (as was assumed in *Gauntlet*).[27] If they are sufficient, the result is the same as under the recharacterisation model. If not, the collateral is different, being

limited to C's rights, and so the PPSA priority rules do not apply.

(ii) In a D v B priority dispute:

• In the recharacterisation model, B's security interest will generally win (as the transferor-granted security interest) so long as it is either temporarily perfected or a financing change statement is lodged.

• In the minimalist model, s66 does not apply until title passes. If C has sufficient rights for the security interest to attach to the underlying collateral, priority will be decided under the PPSA default priority provisions.

2.4 Accounts: grantor of a deemed security interest created through an absolute transfer grants a security interest to a third party

Where A absolutely transfers an account to C, and A subsequently purports to transfer the account or grant a security interest to B, and C grants a security interest to D:

(a) In priority dispute B v C:

• Under the recharacterisation model, the result is determined by general statutory priority provisions, as A is treated as the owner and hence is regarded as having sufficient rights in the account to enable B's security interest to attach to it.

• Under the minimalist model, A is not the owner. Alternative positions would appear to be arguable. Either B's security interest can attach as a matter of statutory construction of the PPSA rather than by treating A as having ownership,[28] producing the same result as the recharacterisation model, or B's security interest cannot be attached, as A has no rights following the absolute transfer.

(b) In priority dispute B v D:

• Under the recharacterisation model, priority will be determined by general statutory priority provisions as A is treated as the owner and hence is regarded as having sufficient rights in the account to enable B's security interest to attach to it. Section 66 does not apply as B's security interest arose after the transfer to C.

• Under the minimalist model there are two alternative analyses. Either:

— B's security interest cannot attach as A has no rights following the absolute transfer, in which case D will win; or

— B's security interest attaches to the account as a matter of statutory construction, in which case there will be the same result as under the recharacterisation model.

We deal with this at a conceptual level in more detail in 'PPSA models: a minimalist approach', Part 4.6. This is not a reason for rejecting the minimalist model which addresses other issues.

3. RECENT JUDICIAL INTERPRETATION

While preferring the minimalist model for the reasons set out in 'PPSA models: a minimalist approach', we note that the recharacterisation approach was seemingly favoured in the first substantive decision in Australia on the operation of the PPSA, although it was not critical to the outcome. In *Re Maiden Civil (P&E) Pty Ltd; Albarran v Queensland Excavation Services Pty Ltd* ('*Maiden Civil*')[29] in 2013, Brereton J of the Supreme Court of New South Wales explored the priority of a lessor's unperfected security interest under a PPS lease as against a perfected security interest of a third party financier of the lessee. Following Canadian and New Zealand authority, Brereton J concluded that the lessee's rights were 'not limited to possessory rights, but include proprietary rights'.[30] Seemingly interpreting 'proprietary' as 'ownership', he thus found those rights sufficient to enable the third party financier's security interest to attach to the goods.[31]

The facts in *Maiden Civil* obviously differ from the scenarios depicted in Part 2 as ABCD priority problems. The case might rather be described as addressing an 'ACD priority problem' where A, the lessor under a PPS lease, leases goods to C who has given a security interest over its present and future property to D. Although there is no 'B' as a secured party of A, the relevant consideration for the purposes of this paper is the court's view of the legal characterisation of the interests of A and C as secured party and grantor respectively. That characterisation is equally important in an ABCD priority problem. *Maiden Civil* thus goes to the core of the debate on the competing models, even though on the facts the case is an example of a situation where the outcome would have been the same whichever model was adopted.

While subsequent courts at first instance have varied in the extent to which they expressly adopt the characterisation in *Maiden Civil*,[32] there has been little analysis at appellate level until the very recent decision of the Full Court of South Australia in *Samwise Holdings*.[33] That Court has now made some general observations highly pertinent to the debate.

Samwise Holdings also concerned an ACD priority problem. A priority dispute arose between Allied Distribution Finance Pty Ltd ('ADF'), a floor plan financier of a company trading as Bill's Motorcycles ('BM'), and Samwise Holdings Pty Ltd ('Samwise'). ADF's security interest arose through a bailment of motorcyles to BM under a PPS lease, while Samwise held a security interest over all BM's present and after-acquired property, which had been perfected by registration in June 2014. At issue on the appeal was the priority of ADF's interest as a purchase money security interest ('PMSI'). Under PPSA s62, a PMSI's ability to attract 'super-priority' when taken over goods that are inventory depends on it being perfected by registration prior to the grantor obtaining possession. ADF had made a registration on 14 April 2016; it became a bailor and hence a secured party on 18 April 2016. On the facts, however, BM had been in possession of the bailed goods prior to the registration date under arrangements with another secured party.

The Full Court held that BM's prior possession was not as grantor of the PMSI, but rather 'possession simpliciter'. Since

BM had only become a grantor under the PPS lease on 18 April 2016, registration had occurred by the prescribed time. Hence ADF's PMSI had priority over Samwise's All PAP.

The discussion relevant to this paper occurred in the context of Doyle J addressing Samwise's argument that the trial judge 'erred by proceeding according to conventional principles of derivative title and nemo dat, whereas the PPS Act has in material respects unwound these principles'.[34] Doyle J analysed the position as follows (emphasis added):[35]

'It is true that the PPS Act has unwound the principles of derivative title and nemo dat in material respects. However, that is so only in the context of contests between security interests under the PPS Act. So, in the case of a PMSI holder who *retains title* to goods in the possession of the grantor, the PPS Act nevertheless treats the grantor's *possession as sufficient* to create a security interest over *the ownership of those goods* in favour of another. Unless the PMSI holder can establish priority under the PPS Act, its interest will lose out to that of the other security interest holder *despite it retaining title* to the goods. It has thus been said that ostensible ownership – in the radical sense of bare possession or control – has effectively replaced derivative title for the purposes of determining priority disputes under the PPS Act.

'However, the principles of derivative title and nemo dat continue to exist and operate in other contexts. Thus, where the possession of assets exists independently of any security interest under the PPS Act, this will not suffice to enable the party in possession to grant a security interest in the ownership of the assets, or which results in the owner losing title to those assets. In such a case, any supervening security interest in the assets only attaches to the grantor's possessory interest in the assets.'

At first glance, the initial paragraph appears to support a minimalist approach.

• The existing interest of ownership under a reservation of title arrangement remains ownership but is a security interest under the PPSA.

• Possession is sufficient to enable a third party's security interest to attach to what is described as the ownership of the goods, bringing that third party's security interest into a priority dispute with that of the existing owner.

In ACD terms, A's interest which is ownership of the goods is a security interest. C's possession of those goods enables D to claim a security interest over those same goods, bringing D and A into a priority dispute over the goods.

The analysis is, however, not without some ambiguity. The third party's security interest is, for example, described as being created or granted over (in PPSA terms, attaching to) the 'ownership interest' in the goods. This description may be problematic for two reasons, both of which are explored in more detail in 'PPSA models: a minimalist approach':

• That usage may not reflect the language of the PPSA. Under s19(2) the security interest 'attaches to collateral'. In 'PPSA models: a minimalist approach' we note the ambiguity of the term 'collateral'.[36] It can refer to a thing (whether tangible or intangible) or to a right in the thing. We conclude that in the context of goods at least, it means the goods themselves rather than the ownership interest in the goods.

We acknowledge that this difference may not matter where the goods are owned by the grantor. To say that the security interest attaches to the ownership interest is effectively the same as saying that it attaches to the goods. We point out, however, that the difference assumes significance where the ownership of the goods and their possession are in different persons. Courts have seen a difference between saying that the security interest attaches to a possessory interest in the goods and that it attaches to the goods.[37]

In the above extract (and subject to our comments below), Doyle J appears to adopt a further approach. He makes no reference to the security interest in question attaching to the goods. Rather, he focuses on its possible attachment to interests in goods; either to an ownership interest or to a possessory interest.

• That usage is problematic if it implies that there is only one title in the goods. That would downplay the impact of legal possession. As Goode points out,[38] and as we explore in 'PPSA models: a minimalist approach', there may be said to be two independent legal titles: an indefeasible title and a possessory title.

'If O is the true owner but T has taken possession of the asset animo domini, both are considered to have title to the absolute interest in the property. O's title, being the best, is indefeasible; T's is a defeasible title, being subordinate to that of O but effective against all others not claiming under O or defending T's claim with O's authority ...

'... no more than two independent legal titles can exist in goods at any one time. Each of these is separately transferable *inter vivos* or capable of being bequeathed by will.'

By using 'collateral' to mean the thing rather than the interest in the thing, the PPSA avoids theoretical debate about which title in the goods is engaged and whether that title is obtained through a possessory interest.

In 'PPSA models: a minimalist approach' we note that it is possible to adopt a minimalist approach and yet not accept that possession arising other than under a security interest could give rise to a security interest over the goods as distinct from a possessory interest in the goods.[39] If Doyle J's subsequent reference to the security interest attaching to the possessory interest is understood as meaning a limited possessory interest in the goods falling far short of ownership, it would be consistent with that approach.

We would contend that that approach overlooks the fact that the grantor in possession has a defeasible title to the goods. Such title is good against the whole world except the true owner and enables a security interest to attach to (in PPSA concepts) the goods, but to be defeasible against the true owner. As the true owner's interest in this instance is not classified as a security interest under the PPSA and is not subject

to the PPSA priority rules, it prevails under general law.

That approach also assumes the relevance of the nemo dat doctrine to the operation of attachment under PPSA s19. While we question that assumption at some length in 'PPSA models: a minimalist approach,' we also emphasise that the worth of possessory title appears frequently to be underestimated.[40] An application of nemo dat does not preclude a person dealing with a grantor in possession from obtaining defeasible title.

If, however, Doyle J's judgement is read as merely indicating that the security interest attaches to the possessory interest as opposed to the ownership interest, without making any assumption as to the respective rights given by those two interests, or their respective worth, then it could be said to be consistent with our broader analysis.

Also problematic in *Samwise Holdings* is its citation of *Graham v Portacom New Zealand Ltd* ('*Portacom*')[41] and *Maiden Civil* in support of the proposition that ostensible ownership replaces derivative title.[42] The proposition is in itself uncontroversial. It is simply another way of describing a characteristic of a possessory interest — it gives the person in possession the appearance of ownership. As a stand-alone proposition, it appears to support the notion that possession is sufficient to enable the security interest to attach to the goods. However, *Portacom* (and in turn *Maiden Civil*) in fact cite the proposition as part of a larger passage extracted from a learned article in the *McGill Law Journal*.[43] The next sentence in that passage reads:

'Thus, by the very act of deeming a true lease to be a PPSA security interest, ownership in the leased assets is effectively vested in the lessee as against the lessee's secured creditors and trustee in bankruptcy.'

The article's authors had noted in earlier discussion in the context of a retention of title sale arrangement where the vendor is the secured party and the buyer is the grantor (or, in Canadian and New Zealand terminology, the debtor) that:[44]

'PPSA analysts are of the unanimous opinion that it is necessary to reconceptualize the arrangement so as to involve an executed sale to the buyer followed by the grant back of a security interest to the seller in order to rationalize the application of the legislation to conditional sales and analogous title reservation security transactions. Pursuant to this approach, the seller is a "secured creditor and not an owner of the collateral; the owner of the collateral is the buyer," and it is to the debtor's undivided ownership interest that the security interest attaches.'

Ostensible ownership based on the possession of the grantor appears to be transformed under a recharacterisation analysis from a possessory interest to what William Young J of the New Zealand Court of Appeal has described as 'a deemed ownership interest'.[45] Certainly, in both *Portacom* and *Maiden Civil* the courts refer to a separate proprietary interest in the form of ownership.[46] It is thus unclear to what extent (if at all) the Full Court's citation of these cases implies approval of the recharacterisation model favoured in those cases.

4. CONCLUSION

In examining the practical consequences of the application of the two models, it is important to acknowledge and accept that the major substantive differerences arise for the most part in transactions involving goods where a secured party retains ownership while the grantor has possession. In other transactions the models generally produce the same result.

Within those restricted circumstances the differences are nonetheless stark. In particular, our analysis shows that the recharacterisation model could result in an existing secured party who is perfected by registration in relation to goods being required to lodge a financing change statement or a financing statement each time its grantor becomes a secured party in respect of those goods (for example, by leasing or consigning them) and, prior to that lodgement, becoming only temporarily perfected in relation to the goods. In fact, because its security interest continues over the rights of its grantor, it will need to maintain two registrations as secured party: one in respect of those rights (with the original grantor as grantor), the other in respect of the goods (with the lessee or consignee as grantor). With 'lease chains' of successive leases, it may need to maintain more. And an analysis of 'lease chains' in 'Chains of leases: aligning PPSA models with commercial expectations' shows the perfected secured party at risk in a range of situations, particularly where it deals with a grantor that is a leasing company or that it authorises to lease the collateral.

Hence, where a difference between models does occur the recharacterisation model affects secured parties who are owners of goods in ways which are in our view inappropriate as a policy matter. The existing secured party perfected by registration with respect to goods should not be required to take further action to maintain its perfection and priority status. In a theme we develop further in 'Chains of leases: aligning PPSA models with commercial expectations', we contend that this onerous outcome under the recharacterisation model is contrary to reasonable commercial expectations in Australia.

Samwise Holdings serves as a timely reminder (if one were needed) that examining the competing models is not an exercise in theory devoid of practical consequences. The issues that they raise cannot be ignored in the hope that they will disappear. Already, an even more recent decision[47] handed down by the Western Australian Court of Appeal on 21 September 2018 risks taking the debate in a different direction by 'assuming (without deciding)' that a security interest arising under a particular general security agreement could potentially be a 'sui generis security interest with features relevantly equivalent to a fixed charge'.[48] To the extent that the Court of Appeal may be understood as envisaging the creation of an entirely new interest rather than the attribution of statutory consequences to an existing property interest, the Court adopts a very different approach to that of the Full Court in *Samwise Holdings.* It is nonetheless of note that much of the decision seems focused on

the actual characterisation of the underlying interest that is treated as the PPSA security interest.[49]

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1 Diccon Loxton, Sheelagh McCracken and Andrew Boxall, 'PPSA models: a minimalist approach' (2018) 32 (1) *Commercial Law Quarterly* 3.

2 Diccon Loxton, Sheelagh McCracken and Andrew Boxall, 'Chains of leases: aligning PPSA models with commercial expectations' (2018) 32(2) *Commercial Law Quarterly* 3.

3 Commonwealth, Review of the Personal Property Securities Act 2009, Final Report (2015) [5.1.2.1]-[5.1.2.2].

4 Whittaker Report, above n3, [5.1.2.2], Annexure C [2].

5 Ibid [5.1.2.2].

6 See Whittaker Report, above n3, Annexure C, [4]. See also Ronald Cuming, 'Double-Debtor ABCD Problems in Personal Property Security Legislation' (1992) 7 *Banking and Finance Law Review* 359 (where the original grantor is B and its secured party is A).

7 [2018] SASCFC 95 (Kourakis CJ, Parker and Doyle JJ).

8 These concepts, together with 'proprietary interest', are discussed at some length in 'PPSA models: a minimalist approach', Part 3, [3.2]-[3.4].

9 Whittaker Report, above n3, [5.1.2.3].

10 See 'PPSA models: a minimalist approach', Part 3, [3.4].

11 Particular and additional complications arise in the context of chains of leases: see generally 'Chains of leases: aligning PPSA models with commercial expectations'.

12 PPSA s21.

13 PPSA ss12, 13.

14 PPSA s12(2)(i).

15 PPSA s12(2)(d).

16 This factual scenario assumes that B has not authorised the lease and that its security interest continues under PPSA s32. For discussion of the position where B authorises the lease, see 'Chains of leases: aligning PPSA models with commercial expectations'.

17 See the discussion in 'Chains of leases: aligning PPSA models with commercial expectations' Part 4(a). That discussion relates to leases, but it is equally applicable to other reservation of title security interests. The Whittaker Report does not address this possibility, but it does suggest that the terms should be conformed, so that instead of using 'disposal' in one place and 'transfer' in another, the same term would be used: Whittaker Report, above n3, [7.1].

18 It is controversial whether C can take free where the arrangement is that of retention of title. It is not clear that C is a 'buyer' for the purpose of s46. See Appendix, marked up fact pattern 3 and further discussion in 'PPSA models: a minimalist approach' at Part 4, [4.2(b)].

19 For a contrary view, see Craig Wappett, 'Competing Interests in Leased Collateral under the PPSA' (2015) 24 *Australian Property Law Journal* 255. See also discussion in 'Chains of leases: aligning PPSA models with commercial expectations', Part 4(g).

20 PMSI priority provisions under PPSA ss62, 63 do not apply in this scenario as the competing security interests of B and D are not granted by the same grantor.

21 See 'Chains of leases: aligning PPSA models with commercial expectations' Part 4(g).

22 See 'Chains of leases: aligning PPSA models with commercial expectations' Part 4(h).

23 These may be valuable. See the discussion of the nature of possession in 'PPSA models: a minimalist approach', Part 3, [3.3].

24 If PPSA s37(1) operates and goods are repossessed by A exercising a right to enforce the lease or on expiry of the lease, then under 76(3) D has priority over B as to goods. This outcome is open to question. See 'Chains of leases: aligning PPSA models with commercial expectations', Part 6.

25 A similar transaction involving confidential information was considered in *Re Gauntlet Energy Corporation* [2003] ABQB 718 ('*Gauntlet*').

26 If, in a particular scenario, a contract of sale was specifically performable, it might be possible for example to argue that C had an equitable interest.

27 [2003] ABQB 718 (Kent J). While the Court did not specifically discuss the issue, its recharacterisation of the purchaser as the owner led to it describing (at [25]) the purchaser as having a proprietary interest.

28 See John Stumbles, 'The Impact of the Personal Property Securities Act on Assignments of Accounts' (2013) 37 *Melbourne University Law Review* 415, 447-457, who contends (at 456- 457) that an approach based on construing the attributes of the security interest as set-out in the PPSA 'avoids any language to the effect that the transferor retains a deemed interest in an unperfected transferred account.'

29 (2013) 277 FLR 337; [2013] NSWSC 852. See generally 'PPSA models: a minimalist approach', Part 3, [3.1].

30 Ibid, [26]. See 'PPSA models: a minimalist approach', Part 3, [3.1], [3.2].

31 Ibid [34], where the court refers to the third party's security interest attaching to 'the Caterpillars', being the leased construction vehicles. In 'PPSA models: a minimalist approach', Part 3, [3.2] we challenge the apparent assumption that possessory rights are not proprietary, contending that the latter term should not be restricted to 'ownership', but should rather be understood as meaning a property right.

32 'PPSA models: a minimalist approach', Part 4, [4.3] and footnotes 201 and 202.

33 [2018] SASCFC 95.

34 [2018] SASCFC 95, [97].

35 [2018] SASCFC 95, [98]-[99]. Doyle J, with whom Parker J concurred, delivered the principal judgment. Kourakis CJ delivered a short separate judgment also dismissing the appeal, stating his agree-

ment with the reasons given by Doyle J.

36 'PPSA models: a minimalist approach', Part 3, [3.4].

37 In 'PPSA models: a minimalist approach' we note (at [3.4]) that the difference 'may be reduced if full weight is given to a possessory title, but it still becomes important in priority disputes between secured parties, particularly when PPSA rules apply to security interests in the "same collateral" ...'.

38 Ewan McKendrick, *Goode on Commercial Law,* Penguin Books (5th ed: 2016) [2.21], [2.22].

39 'PPSA models: a minimalist approach', Part 2, [2.4].

40 'PPSA models: a minimalist approach', Part 4, [4.2(a)].

41 [2004] 2 NZLR 528.

42 [2018] SASCFC 95, [98] note 31.

43 Michael G Bridge, Roderick A Macdonald, Ralph L Simmonds and Catherine Walsh, 'Formalism, Functionalism, and Understanding the Law of Secured Transactions (1999) 44 *McGill Law Journal* 567, 603. See *Portacom* [2004] 2 NZLR 528, [28], *Maiden Civil* (2013) 277 FLR 337, [29].

44 Michael G Bridge, Roderick A Macdonald, Ralph L Simmonds and Catherine Walsh, 'Formalism, Functionalism, and Understanding the Law of Secured Transactions (1999) 44 *McGill Law Journal* 567, 588. See also at 598-603.

45 *Waller v New Zealand Bloodstock Ltd* [2006] 3 NZLR 629; [2005] NZCA 254, [85].

46 Interestingly, in *Portacom* [2004] 2 NZLR 528, [33] the court also refers very briefly in the alternative to Counsel's suggestion that proprietary rights may be 'characterised as having been "derived" from its leasehold interest.' In *Maiden Civil* (2013) 277 FLR 337; [2013] NSWSC 852, [78], in the context of a discussion of the role of PPSA s 112, the court refers to the PPSA treating 'ostensible ownership, through possession' as 'a sufficient right in collateral for a PPS lessee to deal with it, to the extent of creating in a third party a valid security interest which, on perfection, prevails over the lessor's unperfected interest.'

47 *Hamersley Iron Pty Ltd v Forge Group Power Pty Ltd (in liq) (recs & mgrs apptd)* [2018] WASCA 163.

48 *Hamersley Iron Pty Ltd v Forge Group Power Pty Ltd (in liq) (recs & mgrs apptd)* [2018] WASCA 163, [139].

49 Despite its reference to a *sui generis* interest the court nonetheless appears to conceptualise the interest as, or at least akin to, a charge: *Hamersley Iron Pty Ltd v Forge Group Power Pty Ltd (in liq) (recs & mgrs apptd)* [2018] WASCA 163. In its assumption, it in fact suggests in the alternative (at [139]) that the PPSA 'provides for the security interest in this case to operate as a fixed charge.' At [137], it points to what it perceives as 'at least one significant difference between a security interest and a fixed charge' under general law.

The Appendix — Marked Up Annexure C to the Whittaker Report, showing changes arising under the minimalist model — begins overleaf. The authors acknowledge the contribution of this material from the Australian Government Attorney-General's Department.

APPENDIX

Comparison with Annexure C of the Whittaker Report

Explanation of the ~~unitary~~ minimalist model's approach to the concept of 'rights in the collateral', and related matters

1. Introduction

Section 5.1.2 of the Whittaker report noted that two models had been proposed to explain the implications of the requirement in s19(2)(a) that a security interest will only attach to collateral if the grantor has 'rights in the collateral'. The report refers to the two models as the 'unitary' model and the 'possession' model. We refer to them as the 'recharacterisation' model and the 'minimalist' model respectively.

This Appendix ~~annexure seeks~~ is based on Annexure C to the report which sought to explain how the ~~unitary~~ 'recharacterisation' model works in practice, by showing the outcomes that it produces in a range of fact patterns.* This Appendix shows how the 'minimalist' model works by showing the outcomes it produces in those fact patterns.

Changes are marked against the Annexure. Some changes do not reflect differences between the models; rather they reflect where we differ from the report.

~~2.~~ Deleted

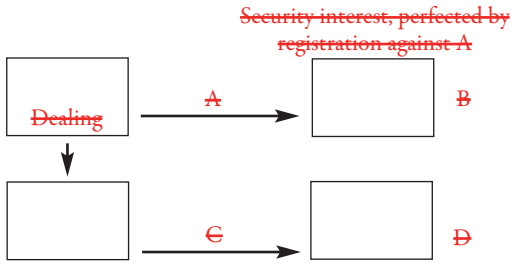
~~3.~~ Deleted

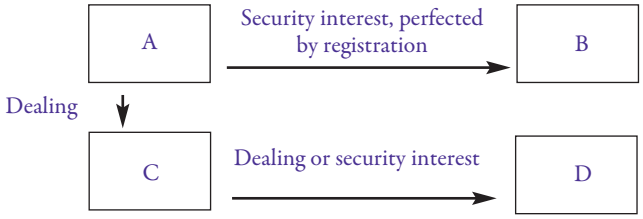
4. Testing the model against representative fact patterns

The attached table shows the results produced by the ~~unitary~~ minimalist model in a range of fact patterns based on the table contained in the report.

However, it refers to 'goods' rather than 'collateral' as the term 'collateral' in our view begs the question as to what interest is being dealt with. Further, much of the table concentrates on leases which are relevant only for goods. Nor is possession as a concept relevant to all forms of personal property, and possession in relation to goods affects title in ways which are inapplicable to many other forms of personal property. In particular, a possessor of goods who is not the owner has a possessory title, as good as absolute title against everyone but the true owner, and can pass such a defeasible title. This is relevant to both models but was not mentioned in the relevant table in the report, perhaps because it dealt with collateral generally.

In each of the fact patterns, A owns ~~collateral~~ goods, and has given a perfected security interest over the ~~collateral~~ goods to B. A then deals with the ~~collateral~~ goods in favour of C, and C then deals with the ~~collateral~~ goods in favour of D. This is what the academic literature calls an A-B-C-D problem. Diagrammatically, it looks like this:





The A-C dealings examined in the attached table are:
(1) a short-term rental (that is not a security interest);
(2) an outright sale for cash;
(3) an outright sale, with security back for the unpaid purchase price;
(4) a sale on retention–of-title terms;
(5) a finance lease or other lease that is an in-substance security interest; and
(6) a lease that is a PPS lease, but is not an in-substance security interest.

Each of dealings (3), (4), (5) and (6) results in C granting a security interest over the ~~collateral~~ goods to A. As a sub-variable of each of those dealings, the table examines what happens if that security interest is either perfected or unperfected.

As a further sub-variable for each of those fact patterns, the table also examines what happens if the dealing by A to C allows C to take the ~~collateral~~ goods free of B's security interest, or is subject to B's security interest.

The table then examines the outcomes produced by the model if C either sells the ~~collateral~~ goods to D, or if C grants D a security interest over ~~it~~ them. The table also examines what happens if C becomes insolvent.

Key to the Appendix — Black = unchanged copy • Red = deleted copy • Purple = inserted copy

How the minimalist model works in practice

	Fact Pattern			Outcome
	A ...	C takes its interest ...	C then ...	
1	rents the ~~collateral~~ goods to C under a short- term lease that is not a security interest.	subject to B's security interest.	sells to D.	D ~~only~~ gets C's possessory rights under the lease, and a defeasible title to the goods subject to A's rights and in each case subject to B's security interest.[4]
			gives D a perfected security interest.	D vs A: A wins.[5] ~~D vs B: B wins.[6]~~ D vs B: to a limited extent priority is determined by s55 and general priority provisions, otherwise B wins.[6]
			becomes insolvent.	A's interest: survives.[7] B's interest: survives.[8]
		free of B's security interest.	sells to D.	~~D only~~ D gets C's possessory rights under the lease, free of B's security interest,[9] and a defeasible title to the goods subject to A's rights.[9]
			gives D a perfected security interest.	D vs A: A wins.[10] D vs B: D wins, in a limited way.[11]
			becomes insolvent.	A's interest: survives.[12] B's interest: survives.[13]

~~1~~

~~2~~

~~3~~

4 C~~'s transaction with A does not give rise to a security interest, so C is not treated by the Act as if it were the owner of the collateral. All that C can sell to D is~~ can sell to D title to the goods defeasible by A, as true owner, and C's possessory rights under the lease, subject in each case to B's rights under its security interest.

~~5 C's ability to give a security interest over the collateral to D is bounded by C's own limited interest in the collateral (or put another way, C can only give a security interest to D over its possessory rights to the collateral), so D's rights to the collateral are no greater than C's.~~

5 C can give a security interest to D over the goods, defeasible by A's rights, ~~while D's security interest is bounded by C's own limited interest in the collateral (that is, D only has security~~ and over C's possessory rights under the lease~~)~~.

~~6 B has security over A's ownership interest in the collateral.~~

6 B and D both have security interests over the goods. Those security interests may be subject to a priority dispute to which s55 might apply to the extent they are over the same collateral. But D's interest is subject to A's rights. B's security interest continues over A's winning rights which extend to A's right to recover the goods as against C and D, at least after the lease terminates.

7 Section 267 is not relevant, because C is not the grantor of a security interest.

8 Section 267 is not relevant, because C is not the grantor of a security interest.

9 ~~C's transaction with A does not give rise to a security interest, so C is not treated by the Act as if it were the owner of the collateral.~~ C can only sell to D its possessory rights under the lease, albeit free of B's rights under its security interest, and a defeasible title to the goods subject to A's rights (A's rights being subject to B's security interest).

~~10 The analysis is the same as in 2.~~

10 The fact that C takes ~~its rights under the lease~~ free of B's security interest does not improve D's position as against A. At best D's collateral is an interest in the goods defeasible by A.

11 D can enforce its security interest ~~free of interference from B. That security interest, however, is still only~~ over C's possessory rights to the ~~collateral under the rent agreement, not over the collateral as a whole.~~ goods under the lease free of interference from B. It can also enforce over the defeasible title in the goods. B continues to have a security interest over ~~the collateral itself~~ A's reversionary rights in the goods.

12 Section 267 is not relevant, because C is not the grantor of a security interest.

13 Section 267 is not relevant, because C is not the grantor of a security interest.

	Fact Pattern			Outcome
	A ...	**C takes its interest ...**	**C then ...**	
2	sells the ~~collateral~~ goods to C for cash.	subject to B's security interest.	sells to D.	D takes the ~~collateral~~ goods, free of B's security interest.[14]
			gives D a perfected security interest.	D vs A: D wins.[15] D vs B: B wins.[16]
			becomes insolvent.	A's interest: not relevant.[17] B's interest: survives.[18]
		free of B's security interest.	sells to D.	D takes the ~~collateral~~ goods, free of B's security interest.[19]
			gives D a perfected security interest.	D vs A: D wins.[20] D vs B: D wins.[21]
			becomes insolvent.	A's interest: not relevant.[22] B's interest: not relevant.[23]

14 If ~~collateral is~~ goods are transferred subject to a security interest, then the transferee becomes the grantor of the security interest. B's security interest will cease to be perfected by the registration (unless the ~~collateral is~~ goods are serial-numbered property and both A and C hold ~~it~~ them as consumer property), because the registration no longer identifies the correct grantor (as the grantor is now C). Instead, B's security interest is temporarily perfected under s34. As B's security interest is only temporarily perfected, D takes free of it (s52).

15 A has sold the ~~collateral~~ goods to C, so A no longer has any interest in ~~it~~ them.

16 If ~~collateral is~~ goods are transferred subject to a security interest, then the transferee becomes the grantor of the security interest. B's security interest will cease to be perfected by the registration (unless the ~~collateral is~~ goods are serial-numbered property and both A and C hold ~~it~~ them as consumer property), because the registration no longer identifies the correct grantor (as the grantor is now C). Instead, B's security interest is temporarily perfected under s34 (until B becomes aware of the sale and has C's details, at which point temporary perfection ceases and B needs to perfect by registration against C — s34(1)(c)(ii)). The competition between B's perfected security interest and D's perfected security interest is regulated by ss66 to 68. As a general rule, B's security interest will prevail.

17 A has sold the ~~collateral~~ goods to C, so A no longer has any interest in ~~it~~ them.

18 B's interest is not affected by s 267, because it is perfected (temporarily, under s 34). Also, while C has become the grantor of B's security interest, it might be suggested C did not ~~grant it~~ 'grant' it as required by s267(1)(b) (A did).

19 D benefits from the fact that C took the ~~collateral~~ goods free of B's security interest, under the 'shelter' principle. C took free of B's security interest, so D does as well.

20 A has sold the ~~collateral~~ goods to C, so A no longer has any interest in ~~it~~ them.

21 D benefits from the fact that C took the ~~collateral~~ goods free of B's security interest, under the 'shelter' principle. C took free of B's security interest, so D does as well.

22 A has sold the ~~collateral~~ goods to C, so A no longer has any interest in ~~it~~ them.

23 C has taken free of B's security interest.

	Fact Pattern			
	A ...	**C takes its interest ...**	**C then ...**	**Outcome**
3(a)	sells the ~~collateral~~ goods to C on deferred payment terms (but with no retention of title clause), and takes a security interest over the ~~collateral~~ goods to secure the payment. A perfects its security interest, as a PMSI.	subject to B's security interest.	sells to D.	D takes the ~~collateral~~ goods subject to A's security interest, but free of B's security ~~interest.[24]~~ interest. Depending on the terms of the security interest, B may still have a security interest over A's rights under A's security interest and the proceeds of exercise of those rights.[24]
			gives D a perfected security interest.	D vs A: A wins.[25] D vs B: B wins.[26]
			becomes insolvent.	A's interest: survives.[27] B's interest: survives.[28]
		free of B's security interest.	sells to D.	D takes the ~~collateral~~ goods subject to A's security interest, but free of B's security interest.[29] Depending on the terms of the security interest, B may still have a security interest over A's rights under A's security interest and the proceeds of exercise of those rights.
			gives D a perfected security interest.	D vs A: A wins.[30] D vs B: ~~D wins.[31]~~ D wins, but B may still through its security interest over A's rights receive the fruits of A's victory over D.[31]
			becomes insolvent.	A's interest: survives.[32] B's interest: ~~not relevant.33~~ not relevant as against C, though B's interest may still be effective against A and its rights depending on its coverage.[33]

24 D takes the ~~collateral~~ goods subject to A's security interest, unless a taking free rule applies. However, D takes the ~~collateral~~ goods free of B's security interest, because B's security interest was only temporarily perfected (s52). But B's security interest is still effective as against A and its rights.

25 A and D both have perfected security interests. A has a PMSI, and will prevail (if it has perfected in time) under s62, even if D also has a PMSI (s63).

26 If ~~collateral is~~ goods are transferred subject to a security interest, then the transferee becomes the grantor of the security interest. B's security interest will no longer be perfected by the registration (unless the ~~collateral is~~ goods are serial-numbered property and both A and C hold ~~it~~ them as consumer property), because the registration no longer identifies the correct grantor (as the grantor is now C). Instead, B's security interest is temporarily perfected under s34 (until B becomes aware of the sale and has C's details, at which point temporary perfection ceases and B needs to perfect by registration against C —s34(1)(c)(ii)). The competition between B's perfected security interest and D's perfected security interest is regulated by ss66 to 68. As a general rule, B's security interest will prevail.

27 A's security interest is not affected by s267, because it is perfected.

28 B's security interest is not affected by s267, because it is perfected (even though only temporarily).

29 D takes the ~~collateral~~ goods subject to A's security interest, unless a taking free rule applies. D takes the ~~collateral~~ goods free of B's security interest, however, under the 'shelter' principle — C took free of B's security interest, so D does as well. B's security interest may still be effective as against A's rights depending on the terms of the security interest.

30 A and D both have perfected security interests. A has a PMSI, and will prevail (if it has perfected in time) under s62, even if D also has a PMSI (under s63).

31 D benefits from the fact that C took the ~~collateral~~ goods free of B's security interest, under the 'shelter' principle. C took free of B's security interest, so D does as well.

32 A's security interest is not affected by s267, because it is perfected.

33 C has taken free of B's security interest.

	Fact Pattern			
	A ...	**C takes its interest ...**	**C then ...**	**Outcome**
3(b)	sells the ~~collateral~~ goods to C on deferred payment terms and takes a security interest over the ~~collateral~~ goods to secure the payment. A fails to perfect its security interest.	subject to B's security interest.	sells to D.	D takes the ~~collateral~~ goods free of both A's and B's security interests.[34]
			gives D a perfected security interest.	D vs A: D wins.[35] D vs B: B wins.[36]
			becomes insolvent.	A's interest: vests in C.[37] B's interest: survives.[38]
		free of B's security interest.	sells to D.	D takes the ~~collateral~~ goods free of both A's and B's security interests.[39]
			gives D a perfected security interest.	D vs A: D wins.[40] D vs B: D wins.[41]
			becomes insolvent.	A's interest: vests in C.[42] B's interest: not relevant.[43]

34 D takes the ~~collateral~~ goods free of A's security interest, because A's security interest was unperfected (s43). D takes the ~~collateral~~ goods free of B's security interest, because B's security interest was only temporarily perfected (s52).

35 D has a perfected security interest. A also has a security interest, but A's security interest is unperfected. D's security interest prevails (s55(3)).

36 If ~~collateral is~~ goods are transferred subject to a security interest, then the transferee becomes the grantor of the security interest. B's security interest will cease to be perfected by the registration (unless the ~~collateral is~~ goods are serial-numbered property and both A and C hold ~~it~~ them as consumer property), because the registration no longer identifies the correct grantor (as the grantor is now C). Instead, B's security interest is temporarily perfected under s34 (until B becomes aware of the sale and has C's details, at which point temporary perfection ceases and B needs to perfect by registration against C — s34(1)(c)(ii). The competition between B's perfected security interest and D's perfected security interest is regulated by ss66 to 68. As a general rule, B's security interest will prevail.

37 Section 267.

38 B's security interest is not affected by s267, because it is perfected (even though only temporarily).

39 D takes the ~~collateral~~ goods free of A's security interest, because A's security interest was unperfected (s43). D takes the ~~collateral~~ goods free of B's security interest, under the 'shelter' principle — C took free of B's security interest, so D does as well.

40 D has a perfected security interest. A also has a security interest, but A's security interest is unperfected. D's security interest prevails (s55(3)).

41 D benefits from the fact that C took the ~~collateral~~ goods free of B's security interest, under the 'shelter' principle. C took free of B's security interest, so D does as well.

42 Section 267

43 C has taken free of B's security interest.

	Fact Pattern			
	A ...	**C takes its interest ...**	**C then ...**	**Outcome**
4(a)	sells the ~~collateral~~ goods to C on retention of title terms. A perfects its security interest.	subject to B's security interest.	sells to D.	~~Same as for 3(a).~~ D takes the ~~collateral~~ possessory right to the goods and a defeasible title to the goods subject to A's security interest, ~~but~~ and not free of B's security interest.[44]
			gives D a perfected security interest.	~~Same as for 3(a).~~ D vs A: A wins.[45] ~~D vs B: B wins.~~ D vs B: will to an extent be decided on general priority principles under s55 etc of the PPSA, though B will still have a security interest over A's winning rights.[46]
			becomes insolvent.	~~Same as for 3(a).~~ A's interest: survives.[47] B's interest: survives.[48]
		free of B's security interest.	sells to D.	~~Same as for 3(a): D takes the collateral subject to A's security interest, but free of B's security interest.~~ D takes the possessory right to the goods and a defeasible title to the goods subject to A's security interest, but free of B's security interest.[49] Depending on the terms of its security interest, B may still have a security interest over A's ownership/security interest in the goods (subject to D's possession and rights) and over A's rights under A's security interest and the proceeds of exercise of those rights.
			gives D a perfected security interest.	~~Same as for 3(a).~~ D vs A: A wins.[50] ~~D vs B: D wins.~~ D vs B: D wins though B's interest may still be effective against A's rights to the goods (subject to C's rights), rights and proceeds depending on its coverage.[51]
			becomes insolvent.	~~Same as for 3(a).~~ A's interest: survives.[52] B's interest: not relevant.~~[53]~~ as against C, though B's interest may still be effective against A's interest in the goods (subject to C's possessory rights), rights and proceeds depending on its coverage.[53]

44 C has possession but does not have full title to the goods. D takes the ~~collateral~~ goods subject to A's ownership rights (which are a security interest), unless a taking free rule applies. However, D ~~takes~~ does not take the ~~collateral~~ goods free of B's security interest, because B's security interest was ~~only~~ not temporarily perfected (s52) since there was no transfer between A and C (ie, s34 is not engaged).

45 A and D both have perfected security interests. A has a PMSI, and will prevail (if it has perfected in time) under s62, even if D also has a PMSI (s63).

~~**46** If collateral is transferred subject to a security interest, then the transferee becomes the grantor of the security interest. B's security interest will no longer be perfected by the registration (unless the collateral is serial-numbered property and both A and C hold it as consumer property), because the registration no longer identifies the correct grantor (as the grantor is now C). Instead, B's security interest is temporarily perfected under s34 (until B becomes aware of the sale and has C's details, at which point temporary perfection ceases and B needs to perfect by registration against C — s34(1)(c)(ii))~~

46 B and D both have security interests over the goods. Those security interests may be subject to a priority dispute to which s55 will apply to the extent they are over the same collateral. But D's interest is subject to A's rights. B's security interest continues over A's winning rights, which extend to A's right to recover the goods as against C and D. B's security interest will remain perfected by registration, because A's security interest resulting from the ROT is not a transfer and registration with respect to B's security interest still identifies the correct grantor. The competition between B's perfected security interest and D's perfected security interest is not regulated by ss66 to 68 because there is no transfer. ~~As a general rule, B's security interest will prevail.~~

47 A's security interest is not affected by s267, because it is perfected.

48 B's security interest is not affected by s267, because it is perfected. ~~(even though only temporarily).~~

49 D takes the ~~collateral~~ goods subject to A's security interest, unless a taking free rule applies. D takes the ~~collateral~~ goods free of B's security interest under the 'shelter' principle — C took free of B's security interest, so D does as well. However B may still have a security interest over A's interest, rights and proceeds.

50 A and D both have perfected security interests. A has a PMSI, and will prevail (if it has perfected in time) under s62, even if D also has a PMSI (under s63).

51 D takes the ~~collateral~~ goods free of B's security interest under the 'shelter' principle. C took free of B's security interest, so D does as well. That does not affect B's rights against A and against A's interest and rights.

52 A's security interest is not affected by s267, because it is perfected.

53 C has taken free of B's security interest. But A's interest is still subject to B's security interest.

	Fact Pattern			
	A ...	**C takes its interest ...**	**C then ...**	**Outcome**
4(b)	sells the ~~collateral~~ goods to C on retention of title terms. A fails to perfect its security interest.	subject to B's security interest.	sells to D.	~~Same as for 3(b).~~ D takes the ~~collateral~~ goods free of ~~both~~ A's ~~and~~ but not B's security ~~interests.~~" interest.[54]
			gives D a perfected security interest.	~~Same as for 3(b).~~ D vs A: D wins.[55] ~~D vs B: B wins.~~" D vs B: will be decided on general priority principles under s55 etc of the PPSA.[56]
			becomes insolvent.	~~Same as for 3(b).~~ A's interest: vests in C.[57] B's interest: survives.[58]
		free of B's security interest.	sells to D.	Same as for 3(b) but reasoning differs: D takes the ~~collateral~~ goods free of both A's and B's security interests.[59]
			gives D a perfected security interest.	Same as for 3(b): D vs A: D wins.[60] D vs B: D ~~wins.~~" wins.[61]
			becomes insolvent.	~~Same as for 3(b).~~ A's interest: vests in C.[62] B's interest: ~~not relevant.~~" Query whether B's interest is still valid over A's rights that have vested in C [63]

54 D takes the ~~collateral~~ full title to the goods free of A's security interest, because A's security interest (which is ownership) was unperfected (s43). ~~D takes the collateral free of~~ Although C only had possession and could normally only give D a defeasible title, D takes full title to the goods because the only party that could defease that title would have been A. But the goods are still subject to B's security interest, because there was no transfer from A to C and therefore B's security interest was ~~only~~ not temporarily perfected (s52).

55 D has a perfected security interest. A also has a security interest, but A's security interest is unperfected. D's security interest prevails (s55(3)).

56 ~~If collateral is transferred subject to a security interest, then the transferee becomes the grantor of the security interest. B's security interest will cease to be perfected by the registration (unless the collateral is serial-numbered property and both A and C hold it as consumer property), because the registration no longer identifies the correct grantor (as the grantor is now C). Instead, B's security interest is temporarily perfected under s34 (until B becomes aware of the sale and has C's details, at which point temporary perfection ceases and B needs to perfect by registration against C — s34(1)(c)(ii)).~~

56 B and D both have security interests over the goods. Those security interests may be subject to a priority dispute to which s55 will apply to the extent they are over the same collateral. The competition between B's perfected security interest and D's perfected security interest is not regulated by ss66 to 68 because there is no transfer from A to C. ~~As a general rule,~~ C does not become grantor. B's security interest will ~~prevail.~~ remain perfected by the registration.

57 Section 267.

58 B's security interest is not affected by s267, because it is perfected. ~~(even though only temporarily).~~

59 D takes the ~~collateral~~ goods free of A's security interest, because A's security interest was unperfected (s43) (and cannot defease what otherwise would be defeasible title). D takes the ~~collateral~~ goods free of B's security interest under the 'shelter' principle — C took free of B's security interest, so D does as well.

60 D has a perfected security interest. A also has a security interest, but A's security interest is unperfected. D's security interest prevails (s55(3)).

61 D takes the ~~collateral~~ goods free of B's security interest under the 'shelter' principle. C took free of B's security interest, so D does as well.

62 Section 267.

63 C has taken free of B's security interest but A's interest which vests in C may be subject to B's security interest.

	Fact Pattern			Outcome
	A ...	**C takes its interest ...**	**C then ...**	
5(a)	~~leases the collateral to C under a~~ leases the goods to C under a lease that is an in-substance security interest. A perfects its security interest.	subject to B's security interest.	sells to D.	Same as for ~~3(a)~~ 4(a): D takes the ~~collateral but~~ possessory right to the goods and a defeasible title to the goods subject to A's security interest, and not free of B's security interest.[64]
			gives D a perfected security interest.	Same as for ~~3(a)~~ 4(a): D vs A: A wins.[65] ~~D vs B: B wins.~~[66] D vs B: will to an extent be decided on general priority principles under s55 etc of the PPSA, though B will still have a security interest over A's winning rights.[66]
			becomes insolvent.	Same as for ~~3(a)~~ 4(a): A's interest: survives.[67] B's interest: survives.[68]
		free of B's security interest.	sells to D.	Same as for ~~3(a)~~ 4(a): D takes the ~~collateral but~~ possessory right to the goods and a defeasible title to the goods subject to A's security interest but free of B's security interest.[69] Depending on the terms of its security interest, B may still have a security interest over A's 'reversionary' rights under A's security interest (lease) and the proceeds of exercise of those rights.[69]
			gives D a perfected security interest.	Same as for ~~3(a)~~ 4(a): D vs A: A wins.[70] ~~D vs B: D wins.~~[71] D vs B: D wins though B's interest may still be effective against A's reversionary rights to the goods (subject to C's rights), rights and proceeds depending on its coverage.[71]
			becomes insolvent.	Same as for ~~3(a)~~ 4(a): A's interest: survives.[72] B's interest: not relevant.[73] as against C, though B's interest may still be effective, and enforced, against A's reversionary rights (subject to C's rights), rights and proceeds depending on its coverage.[73]

64 C has possession but does not have full title to the goods. D takes the ~~collateral~~ goods subject to A's ownership rights (which are a security interest), unless a taking free rule applies. However, D ~~takes~~ does not take the ~~collateral~~ goods free of B's security interest, because B's security interest was ~~only~~ not temporarily perfected (s52) since there was no transfer between A and C (ie, s34 is not engaged).

65 A and D both have perfected security interests. A has a PMSI, and will prevail (if it has perfected in time) under s62, even if D also has a PMSI (s63).

~~**66** If collateral is transferred subject to a security interest, then the transferee becomes the grantor of the security interest. B's security interest will no longer be perfected by the registration (unless the collateral is serial-numbered property and both A and C hold it as consumer property), because the registration no longer identifies the correct grantor (as the grantor is now C). Instead, B's security interest is temporarily perfected under s34 (until B becomes aware of the sale and has C's details, at which point temporary perfection ceases and B needs to perfect by registration against C — s34(1)(c)(ii))~~

66 B and D both have security interests over the goods. Those security interests may be subject to a priority dispute to which s55 will apply to the extent they are over the same collateral. But D's interest is subject to A's rights. B's security interest continues over A's winning rights which extend to A's reversionary right to recover the goods as against C and D. B's security interest will remain perfected by registration, because A's security interest resulting from the lease is not a transfer and registration with respect to B's security interest still identifies the correct grantor. The competition between B's perfected security interest and D's perfected security interest is not regulated by ss66 to 68 because there is no transfer. ~~As a general rule, B's security interest will prevail.~~

67 A's security interest is not affected by s267, because it is perfected.

68 B's security interest is not affected by s267, because it is perfected ~~(even though only temporarily)~~.

69 D takes the ~~collateral~~ goods subject to A's security interest unless a taking free rule applies. D takes the ~~collateral~~ goods free of B's security interest under the 'shelter' principle — C took free of B's security interest, so D does as well. However B may still have a security interest over A's interest, rights and proceeds.

70 A and D both have perfected security interests. A has a PMSI, and will prevail (if it has perfected in time) under s62, even if D also has a PMSI (under s63).

71 D takes the ~~collateral~~ goods free of B's security interest under the 'shelter' principle. C took free of B's security interest, so D does as well. That does not affect B's rights against A and against A's interest and rights.

72 A's security interest is not affected by s267, because it is perfected.

73 C has taken free of B's security interest.

	Fact Pattern			
	A ...	**C takes its interest ...**	**C then ...**	**Outcome**
5(b)	leases the ~~collateral~~ goods to C under a lease that is an in-substance security interest. A fails to perfect its security interest.	subject to B's security interest.	sells to D.	Same as for ~~3(b)~~ 4(b): D takes the ~~collateral~~ goods free of ~~both~~ A's ~~and~~ but not B's security interests.[74]
			gives D a perfected security interest.	Same as for ~~3(b)~~ 4(b): D vs A: D wins.[75] ~~D vs B: B wins.[76]~~ D vs B: will be decided on general priority principles under s55 etc of the PPSA.[76]
			becomes insolvent.	Same as for ~~3(b)~~ 4(b): A's interest: vests in C.[77] B's interest: survives.[78]
		free of B's security interest.	sells to D.	Same as for ~~3(b)~~ 4(b): D takes the ~~collateral~~ goods free of both A's and B's security interests.[79]
			gives D a perfected security interest.	Same as for ~~3(b)~~ 4(b): D vs A: D wins.[80] D vs B: ~~B~~ D wins.[81]
			becomes insolvent.	Same as for ~~3(b)~~ 4(b): A's interest: vests in C.[82] B's interest: ~~not relevant.83~~ Query whether B's interest is still valid over A's rights that have vested in C.[83]

74 D takes the ~~collateral~~ goods free of A's security interest, because A's security interest (which is ownership) was unperfected (s43). ~~D takes the collateral free of~~ Although C only had possession and could normally only give D defeasible title and possessory rights D takes full title to the goods, because A cannot assert its rights. But the goods are still subject to B's security interest, because there was no transfer from A to C, B's security interest ~~was only~~ remained perfected and not temporarily perfected ~~(s52)~~.

75 D has a perfected security interest. A also has a security interest, but A's security interest is unperfected. D's security interest prevails (s55(3)).

~~**76** If collateral is transferred subject to a security interest, then the transferee becomes the grantor of the security interest. B's security interest will cease to be perfected by the registration (unless the collateral is serial-numbered property and both A and C hold it as consumer property), because the registration no longer identifies the correct grantor (as the grantor is now C). Instead, B's security interest is temporarily perfected under s34 (until B becomes aware of the sale and has C's details, at which point temporary perfection ceases and B needs to perfect by registration against C — s34(1)(c)(ii))~~

76 B and D both have security interests over the goods. Those security interests may be subject to a priority dispute to which s55 will apply to the extent they are over the same collateral. The competition between B's perfected security interest and D's perfected security interest is not regulated by ss66 to 68 because there is no transfer from A to C. ~~As a general rule,~~ C does not become grantor. B's security interest will ~~prevail~~ remain perfected by the registration.

77 Section 267.

78 B's security interest is not affected by s 267, because it is perfected ~~(even though only temporarily)~~.

79 D takes the ~~collateral~~ goods free of A's security interest, because A's security interest was unperfected (s43) (and cannot defease what otherwise would have been defeasible). D takes the ~~collateral~~ goods free of B's security interest, under the 'shelter' principle — C took free of B's security interest, so D does as well.

80 D has a perfected security interest. A also has a security interest, but A's security interest is unperfected. D's security interest prevails (s55(3)).

~~**81** If collateral is transferred subject to a security interest, then the transferee becomes the grantor of the security interest. B's security interest will cease to be perfected by the registration (unless the collateral is serial-numbered property and both A and C hold it as consumer property), because the registration no longer identifies the correct grantor (as the grantor is now C). Instead, B's security interest is temporarily perfected under s34 (until B becomes aware of the sale and has C's details, at which point temporary perfection ceases and B needs to perfect by registration against C — s34(1)(c)(ii)). The competition between B's perfected security interest and D's perfected security interest is regulated by ss66 to 68. As a general rule, B's security interest will prevail.~~

81 D takes the goods free of B's security interest under the 'shelter' principle. C took free of B's security interest, so D does as well.

82 Section 267.

83 C has taken free of B's security interest but A's interest which vests in C may be subject to B's security interest.

	Fact Pattern			
	A ...	**C takes its interest ...**	**C then ...**	**Outcome**
6(a)	leases the ~~collateral~~ goods to C under a PPS lease that is not an in-substance security interest. A perfects its security interest.	subject to B's security interest.	sells to D.	Same as for 4(a): D takes the ~~collateral~~ possessory right to the goods and a defeasible title to the goods but subject to A's security interest and not free of B's security interest.[84]
			gives D a perfected security interest.	Same as for 4(a): D vs A: A wins.[85] ~~D vs B: B wins.~~[~~86~~] D vs B: will to an extent be decided on general priority rules under s55 etc of the PPSA though B will still have a security interest over A's winning rights.[86]
			becomes insolvent.	Same as for 4(a): A's interest: survives.[87] B's interest: survives.[88]
		free of B's security interest.	sells to D.	Same as for 4(a): D takes the ~~collateral~~ possessory right to the goods and a defeasible title to the goods, ~~but~~ subject to A's security interest but free of B's security interest.[89] Depending on the terms of its security interest, B may still have a security interest over A's 'reversionary' rights under A's security interest (lease) and the proceeds of exercise of those rights.
			gives D a perfected security interest.	Same as for 4(a): D vs A: A wins.[90] D vs B: D ~~wins.91~~ wins though B's interest may still be effective against A's rights to the goods (subject to C's rights), rights and proceeds depending on its coverage.[91]
			becomes insolvent.	Same as for 4(a): A's interest: survives.[92] B's interest: not relevant.[~~93~~] as against C, though B's interest may still be effective, and enforced, against A's reversionary rights (subject to C's rights), rights and proceeds depending on its coverage.[93]

84 D takes the ~~collateral~~ goods subject to A's security interest, unless a taking free rule applies. However, D ~~takes~~ does not take the ~~collateral~~ goods free of B's security interest, because B's security interest was ~~only~~ not temporarily perfected (s52) since there was no transfer between A and C (ie, s34 is not engaged).

85 A and D both have perfected security interests. A has a PMSI, and will prevail (if it has perfected in time) under s62, even if D also has a PMSI (s63).

~~**86** If collateral is transferred subject to a security interest, then the transferee becomes the grantor of the security interest. B's security interest will no longer be perfected by the registration (unless the collateral is serial-numbered property and both A and C hold it as consumer property), because the registration no longer identifies the correct grantor (as the grantor is now C). Instead, B's security interest is temporarily perfected under s34 (until B becomes aware of the sale and has C's details, at which point temporary perfection ceases and B needs to perfect by registration against C — s34(1)(c)(ii)). The competition between B's perfected security interest and D's perfected security interest is regulated by ss66 to 68. As a general rule, B's security interest will prevail.~~

86 B and D both have security interests over the goods. Those security interests may be subject to a priority dispute to which s55 will apply to the extent they are over the same collateral. But D's interest is subject to A's rights. B's security interest continues over A's winning rights which extend to A's reversionary right to recover the goods as against C and D. B's security interest will remain perfected by registration, because A's security interest resulting from the lease is not a transfer and registration with respect to B's security interest still identifies the correct grantor. The competition between B's perfected security interest and D's perfected security interest is not regulated by ss66 to 68 because there is no transfer.

87 A's security interest is not affected by s267, because it is perfected.

88 B's security interest is not affected by s267, because it is perfected ~~(even though only temporarily)~~.

89 D takes the ~~collateral~~ goods subject to A's security interest, unless a taking free rule applies. D takes the ~~collateral~~ goods free of B's security interest, however, under the 'shelter' principle — C took free of B's security interest, so D does as well. However, B may still have a security interest over A's interest, rights and proceeds.

90 A and D both have perfected security interests. A has a PMSI, and will prevail (if it has perfected in time) under s62, even if D also has a PMSI (under s63).

91 D takes the ~~collateral~~ goods free of B's security interest under the 'shelter' principle. C took free of B's security interest, so D does as well. That does not affect B's rights against A and against A's interest and rights.

92 A's security interest is not affected by s267, because it is perfected.

93 C has taken free of B's security interest.

	Fact Pattern			
	A ...	**C takes its interest ...**	**C then ...**	**Outcome**
6(b)	leases the ~~collateral~~ goods to C under a PPS lease that is not an in-substance security interest. A fails to perfect its security interest.	subject to B's security interest.	sells to D.	Same as for 4(b): D takes the ~~collateral~~ goods free of A's but not B's security interests.[94]
			gives D a perfected security interest.	Same as for 4(b): D vs A: D wins.[95] ~~D vs B: B wins.~~[96] D vs B: will be decided on general priority rules under s55 etc of the PPSA.[96]
			becomes insolvent.	Same as for 4(b): A's interest: vests in C.[97] B's interest: survives.[98]
		free of B's security interest.	sells to D.	Same as for 4(b): D takes the ~~collateral~~ goods free of A's and B's security interests.[99]
			gives D a perfected security interest.	Same as for 4(b): D vs A: D wins.[100] D vs B: D wins.[101]
			becomes insolvent.	Same as for 4(b): A's interest: vests in C.[102] B's interest: ~~not relevant.~~[103] Query whether B's interest is still valid over A's rights that have vested in C.

94 D takes the ~~collateral~~ goods free of A's security interest, because A's security interest was unperfected (s43). However, D does not take the goods free of B's security interest because B's security interest was ~~only~~ not temporarily perfected ~~(s52)~~ since there was no transfer between A and C.

95 D has a perfected security interest. A also has a security interest, but A's security interest is unperfected. D's security interest prevails (s55(3)).

~~**96** If collateral is transferred subject to a security interest, then the transferee becomes the grantor of the security interest. B's security interest will cease to be perfected by the registration (unless the collateral is serial-numbered property and both A and C hold it as consumer property), because the registration no longer identifies the correct grantor (as the grantor is now C). Instead, B's security interest is temporarily perfected under s34 (until B becomes aware of the sale and has C's details, at which point temporary perfection ceases and B needs to perfect by registration against C — s34(1)(c)(ii))~~

96 B and D both have security interests over the goods. Those security interests may be subject to a priority dispute to which s55 will apply to the extent they are over the same collateral. The competition between B's perfected security interest and D's perfected security interest is not regulated by ss66 to 68 because there is no transfer from A to C. ~~As a general rule,~~ C does not become grantor. B's security interest will ~~prevail~~ remain perfected by the registration.

97 Section 267.

98 B's security interest is not affected by s267, because it is perfected ~~(even though only temporarily)~~.

99 D takes the ~~collateral~~ goods free of A's security interest, because A's security interest was unperfected (s43) (and cannot defease what would otherwise be defeasible). D takes the ~~collateral~~ goods free of B's security interest, under the 'shelter' principle — C took free of B's security interest, so D does as well.

100 D has a perfected security interest. A also has a security interest, but A's security interest is unperfected. D's security interest prevails (s55(3)).

101 D takes the ~~collateral~~ goods free of B's security interest under the 'shelter' principle. C took free of B's security interest, so D does as well.

102 Section 267

103 C takes free of B's security interest but A's interest which vests in C may be subject to B's interest.