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CAUSATION IN EQUITABLE COMPENSATION

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References to “Commercial Damages” are to my loose leaf service published by Thomson Reuters. I have highlighted for convenience, new additions to the text, eg extracts from an article by Tipping J, and reference to recent Federal Court decision, Hydrocool

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Overview of paper; theory and pragmatism

1. The law of remedies has tensions between competing values: full compensation and some limit on full compensation. The principle that a wronged plaintiff is entitled to compensation, phrased differently depending on the case of action eg to be put in the position as if the contract had been performed; or as if the wrong had not been committed. These principles militate in favour of full compensation.

2. The rules of causation also, in themselves, are infused with policy considerations as to the extent of liability the wrongdoer ought shoulder: should the wrongdoer underwrite falls in the market that the victim was exposed to, due to the wrong?

What about the “two shooter” example, where even had one shooter not fired, death would have eventuated in any event due to the other shooter's bullet? This is a colourful analogue of cases which reoccur, where the a trustee or fiduciary defaults, and loss eventuates which the defendant pleads would have occurred in any event.

3. The policies underpinning the rules as to causation, differ yet again depending on whether one is considering causation in the context of breach of contract, tort, or equity.

4. On the other hand, there are principles which make inroads into the principles of full compensation eg causation, remoteness, contributory negligence and
proportionate liability.

The above principles reflect different values, such as victims should be compensated, wrongdoers should pay, that there need be predictable rules that are not too expensive to apply, that there ought not be endless inquiries into the precise personal circumstances of every litigant; that people need to take responsibility for their own conduct; and there ought be a fair allocation of risk amongst those to blame.

5. By way of juxtaposing the rules of causation at common law and in equity, I will explore the “loss of market” cases, where the causes of action were different—respectively breach of duty of care in tort, and breach of an equitable obligation. They have radically different results.

6. In so doing, I will explore the status of the “rule in Brickendon” which puts the causation test against the errant fiduciary, at its most facilitative for the plaintiff.

7. In so doing, if time permits, I may discuss the practical issues thrown up for the draftsman of the pleadings in such cases, and of course, the busy solicitor who must draft the necessary letter of demand seeking to say not too much, nor too little, in advance of knowing all the evidence.

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**Commercial Damages**

[9.10] Common sense, streams, nets, billiards and labyrinths

8. In Goodhart *Essays in Jurisprudence and the Common Law* p 131, n 8, Professor Goodhart highlights how difficult a topic causation is. Many judges can define it only in terms of metaphors and similes, he says, such as Lord Sumner’s “chain of causation” and “conduit pipe”: *Weld-Blundell v Stephens* [1920] AC 956 at 986. In *Leyland Shipping Co Ltd v Norwich Fire Insurance Society Ltd* [1918] AC 350; (1918) 118 LT 120 at 369 (AC) Lord Shaw said “causation is not a chain, but a net. At each point, influences, forces, events, preceding and simultaneous, meet, and the radiation from each point extends infinitely”.

According to Andrews J in *Palsgraf v Long Island Railway Co* 248 NY 339 (1928); 162 NE 99, proximate cause is neither a chain nor a net but a stream. HH’s dicta are abstracted in *Commercial Damages*.

Professor Goodhart questions the validity of a concept that is so imprecise and labyrinth that it can only be described in terms of a series of conflicting analogies.

cited with approval by McHugh J in *March v E & MH Stramare Pty Ltd* (1991) 171 CLR 506, modern psychological research:

“[I]llustrates how judgments of causes and responsibility [by an ordinary person] are reached by an active, constructive process which goes beyond the information given and is therefore subject to various forms of error and bias; are structured by, as well as expressed in, language; and are influenced by the motives, values, experiences, and other characteristics of the judge, the specific context, and the anticipated consequences. These various effects are interwoven and difficult to disentangle both conceptually and empirically, but in general, talking about the ordinary man, common sense, and everyday judgments appears somewhat hazardous.”

**Commercial Damages**


9. The onus of proving damages lies on the plaintiff, to be discharged on the balance of probabilities *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64 at 80 per Mason CJ and Dawson J.

To establish a causal connection between a breach of contract and the damage suffered, a plaintiff need only show that the breach was a cause of the loss. This is decided by the application of common sense principles. In general, the application of the "but for" test will be sufficient to prove the necessary causal connection. However, that test is only a guide. The ultimate test is whether as a matter of commonsense, the relevant act or omission was a cause: see *Alexander v Cambridge Credit Corp Ltd* (1987) 9 NSWLR 310 per Glass and McHugh JJA.

The satisfaction of the "but for" test may not of itself, be sufficient to prove causation if there are reasons of justice or policy against attributing causal responsibility……………. Cases dealing with direct or "billiard-ball" causation may not be good precedents in matters relating to "interpersonal" causation. Even if there is a causal connection between a breach of contract and damage, no liability arises if an independent act or event can be treated in a practical sense as the sole cause of the damage: *Alexander v Cambridge Credit Corp Ltd* (1987) 9 NSWLR 310 at 350-352 per McHugh JA; *Malleson Stephen Jacques v Trenorth Ltd* [1999] 1 VR 727; *Kenny & Good Pty Ltd v MGICA (1992) Ltd* (1999) 199 CLR 413.

It is unnecessary for the relevant breach to be the exclusive or dominant cause of the loss, it being sufficient that the breach materially caused or contributed to the harm suffered: *Chappel v Hart* (1998) 195 CLR 232 at 238, 244; *Henville v Walker* (2001) 206 CLR 459 at 493. If the loss claimed is the apparent or likely result of the breach, then the onus shifts to the defendant to prove that the damages suffered did not result from the breach.
Commercial Damages [9.1510]
Concurrent claims for professional negligence and causation

10. In claims for professional negligence brought concurrently in contract, tort and equity, the same approach to causation is taken in respect of all three: *Marriott v Dowd Thomason Strachan & Moultrie* [1993] ANZ ConvR 520 High Court of New Zealand, Tomkins J, 19 March 1993, especially at 37ff.

There are suggestions in the material below that this is a correct exposition of the position.

Commercial Damages [9.1550]
The general propositions as applied to auditors and solicitors

11. There is appellate authority in both Australia and England that a company cannot succeed against its auditors merely by showing that the accounts, which had been audited by the auditors for some years, were not appropriately qualified and that this allowed the company to continue to trade and incur losses.

Providing the opportunity for the plaintiff to trade and to expose it to all the risks of trading, is not a cause of loss that occurs in the course of such trading.

Similarly, a company cannot succeed against its solicitors merely by showing that the negligence of its solicitor afforded the opportunity for the company to suffer loss.

The underlying policy factor appears to be that companies must take responsibility for their own bad management, and that as between the company's shareholders and the auditor's insurers, the loss should lie where it falls.

12. *Alexander v Cambridge Credit Corp* (1987) 9 NSWLR 310 is the key case in this area of the law, now being good authority in both Australia and England. For this reason, it will be analysed in some depth.

By 1969, the defendant auditors (Alexander) were aware that the company had established substantial trading losses. The company had issued debentures and the debenture trust deed provided that, in certain events, the trustee might appoint a receiver if certain critical ratios were breached. The accounts for end June 1971 failed to make provision for a $9 million deficiency.

The failure of the auditors to so qualify their report with respect to the borrowing ratio was held to be a breach of contractual duty on their part. This was not in dispute on appeal. Had the appropriate qualification been made it was highly probable that a receiver would have been appointed.

Between 1971 and 1974, the company continued to trade as a land developer, but was essentially badly managed. It bought huge tracts of land at
the height of a boom and had to hold onto them during a slump. External events also affected business. For example the pre-1971 boom ended in a slump, the government activated a credit squeeze, there was an excess of supply over demand, and floods prevented the development of much land held by the company.

13. If the auditors had acted as they should have, the report would have been qualified, the trustee would have acted and a receiver would have been appointed in 1971. The company claimed for the deterioration of its net worth between 1971 and 1974 when it was finally put into receivership, that is, during the three years following the breach.

14. In proceedings claiming damages for negligence against the auditors for breach of contract, Rogers J, the primary judge, found that but for the breach of contract by the auditors, the company would have gone into receivership in 1971 and the loss would not have occurred.

Damages were assessed at $145 million, being the increase in liabilities between 1971 and 1974.

15. On appeal, the predominant issue was causation. The Court of Appeal, Glass JA dissenting, allowed the appeal on the basis that there was no causal connection between the breach of contract and the damage.

16. The two majority judges took very different paths to arrive at the same result. Both majority judges felt that Alexander could not be held responsible for the disasters that occurred simply because they allowed the company to continue trading. McHugh JA considered separately the aspects of causation, remoteness and novus actus interveniens. Essentially, his Honour's view was that so far as both contract and tort were concerned, the "but for" test must be taken to be the leading and, in all but exceptional cases, the exclusive test of causation at 350, 352:

"Thus the common law is concerned with whether on a particular occasion a particular act or omission contributed to the occurrence of a particular event (causation) and if so, whether responsibility should attach to that act or omission (remoteness)."

Once causation-in-fact is established, the only question is whether the damage is so remote from the breach that the defendant should not be held responsible for it. Any question of a novus actus interveniens is to be considered in the policy area of remoteness of damage."

What made the claim "truly remarkable" to his Honour was that Cambridge did not assert that it relied on the auditors' certificates or on the failure to qualify the accounts. Through its officers, and particularly the managing director, Cambridge was well aware of the facts that gave rise to the finding that provisions should have been made for its deficiency in assets.

17. In this respect, the judgments of Mahoney and McHugh JJA were precisely the same.

18. However, Mahoney JA assumed that the loss claimed was within the restitution principle and then considered whether such loss was caused by the
defendant's breach. His Honour noted that there are several different "formulae to determine whether a particular loss is caused by a breach", namely:

- "Physical causality/billiard ball causality" where it is in the "nature of the physical world that, when the cause occurs, the effect shall follow. Cause in the physical sense is not limited to the 'billiard ball' kind of case. That is, even a physical effect may properly be seen as having several causes and such causes may be concurrent or successive": at 331.
- Interpersonal causation, where there is a nexus between the defendant's wrong and subsequent volitional human acts and the things to which they have led: at 332 per Mahony JA:

For example, the defendant may be the cause of the breach by X of his contract with the plaintiff, if the defendant induced X to break it. The servant may be the cause of the loss of goods when, by failing to lock his employer's front door, he affords a thief an opportunity to enter and take them.

19. Why is the distinction important? As Mahoney JA pointed out in the earlier case of Nader v Urban Transit Authority (NSW) (1985) 2 NSWLR 501 at 515, cases relating to physical causation are no authority in cases relating to interpersonal causation. Therefore, one must identify precisely what is the relationship between the wrong and the loss. Mahoney JA was of the view that Cambridge's loss was, in the broadest sense, the result of the defendant's breach. He categorised the causality in question as interpersonal: (1987) 9 NSWLR 310 at 331-333. The plaintiff's loss, said his Honour, resulted from the defendant's breach in the sense that the company would have ceased trading had it not been for the breach. But to allow a company to be in existence and to expose it to all the dangers of being in existence does not cause loss.

20. Galoo Ltd (in liq) v Bright Grahame Murray (a firm) [1995] 1 All ER 16; [1994] 1 WLR 1374 (applied by the UK Court of Appeal in The "Sivand" [1998] 2 Lloyd's Rep 97 and followed in various Australian cases, for example, Ampolex Ltd v Perpetual Trustee Co (Canberra) Ltd (No 2) (1996) 20 ACSR 649; 14 ACLC 1514) was a successful strike-out motion by auditors who succeeded largely on the basis of Australian authority such as Alexander v Cambridge Credit Corp (1987) 9 NSWLR 310.

Summary: a Court must apply its common sense in deciding whether a breach of duty was the cause or merely the occasion for the loss.

Commercial Damages [9.1570]

Solicitors who advise vendors and purchasers of land and businesses

21. [A] client who alleges a loss of opportunity arising from a solicitor's negligence must establish the negligence of the solicitor on the balance of probabilities and, further, that negligence has resulted in the loss alleged. Assuming negligence is established, the client must establish on the balance of
probabilities that, if properly advised, he or she would have acted differently. When those matters are established, the damages in respect of the lost opportunity to act in that way are to be assessed by reference to degrees of probability of the success of the opportunity rather than on the balance of probabilities: Tasmanian Sandstone Quarries Pty Ltd v Tasmanian Sandstone Pty Ltd [2009] SASC 111 [286] and where White J added

“Many clients are accustomed to acting in accordance with the advice of their solicitors, and it is often only a short step to infer that, if relevant advice had been given, they would have acted in accordance with it.”

22. Where the negligence of a solicitor in a conveyancing transaction has caused the vendor to lose the chance of making a gain, then whether the negligence has caused loss is determined on the balance of probabilities; and the chance so lost is valued by reference to the possibility or probability of the chance having eventuated, even if that chance is less than 50%, but so long as it is non negligible. This is especially so where past hypotheticals are in issue, such as how the vendor would have acted if properly advised: Heenan v Di Sisto [2008] NSWCA 25; (2008) Aust Torts Reports 81-941 at [30] ff, per Giles JA with whom Mason P and Mathews AJA agreed.

23. For example, the balance of probabilities is being applied to what the plaintiff would have done if properly advised by a solicitor.

24. Heenan illustrates how the value of a lost chance is quantified when there is a combination of factors, each of which must be assigned a percentage chance of having occurred had there been non negligence, viz the chance of the purchaser agreeing to a certain clause; and then the chance of the purchaser actually completing the two contracts in issue.

25. Gove v Montague Mining Pty Ltd [2000] FCA 1214 is a cautionary tale in this regard. The plaintiff claimed against its solicitors for negligent advice in relation to a commercial agreement; but failed because it did not call evidence of what it would have done if the correct advice had been given. Another cautionary tale is Lockhart v Holden [2008] QSC 257; 221 FLR 366 where the reasoning of Heenan’s case was applied, but the loss of the chance of a past hypothetical (viz how a third party who wished to buy the plaintiff’s business would have acted if asked to purchase shares of the holding company instead) was assessed conservatively for want of any evidence from that third party nor explanation as to its absence: at [79] ff.

A partially differently constituted New South Wales Court of Appeal has endorsed Heenan’s reasoning: Hendriks v McGeoch [2008] NSWCA 53.

26. The same principles apply to quantifying damages where solicitors have breached their duties of skill and care regarding the sale of a business: Tasmanian Sandstone Quarries Pty Ltd v Tasmanian Sandstone Pty Ltd [2009] SASC 111.

27. In Trust Co of Australia v Perpetual Trustees WA Ltd (1997) 42 NSWLR 237, a trustee company retained Parker & Parker, a firm of solicitors, to advise whether the company would have a conflict of duty if it acquired a particular
property. The firm mistakenly failed to advise the company of the existence of a conflict of duty. The company acquired the property and later suffered losses by reason of the commercial consequence of the purchase. The trustee company sued Perpetual Trustees, the trust manager, which claimed contribution against Parkers to recover the losses sustained alleging that, had they given correct advice on the conflict of duty issue, it would not have acquired the property.

28. McLelland CJ accepted that if Parkers had given correct advice, then the company would not have gone ahead with the transaction, but said that this was insufficient on its own to establish causation. His honour's reasoning (citing the High Court in *Medlin v State Government Insurance Commission* (1995) 182 CLR 1 at 6 and the House of Lords in *Banque Bruxelles Lambert SA v Eagle Star Insurance Co Ltd* [1997] AC 191 at 214) emerges from the observation that Parker & Parker's duty was to provide an opinion as to whether Perpetual Trustees would be in a position of conflict "for the purpose of enabling Perpetual to decide upon a course of action (namely whether to acquire the Katherine property for the trust; and if so on what terms)"; (1997) 42 NSWLR 237 at 249.

His Honour noted that the real and effective cause was Perpetual's own negligence in making an investment on behalf of the Trust that was "commercially hazardous and … improvident". This decision was unrelated to Parker & Parker's conduct since they were not retained to consider the commercial aspects of the proposed acquisition of the property. In fact, their retainer specifically disavowed such a duty. "That loss, and Perpetual's liability, would have occurred even if Parker & Parker's mistaken opinions had been correct.": NSWLR at 250.

**Examples of causes of action in equity where issues of causation might arise**

**Misuse of confidential information**

29. Equity proscribes the use of confidential information which has ended up in the hands of a third party (ie the second defendant) where the third party knows that the information has been obtained by or communicated to it in breach of confidence: *Liquid Veneer Co v Scott* (1912) 29 RPC 639, 644. Such knowledge on the part of the third party can readily be inferred from the nature of the information, and/or the circumstances in which it was communicated: *Exchange Telegraph Co Ltd v Howard & The London & Manchester Press Agency Ltd* (1906) 22 TLR 375; *Exchange Telegraph Co Ltd v Central News Limited* [1897] 2 Ch 48; *Gilbert v Star Newspaper Co Ltd* (1894) 11 TLR 4; *National Education Advancement Programs (NEAP) Pty Ltd v Ashton* (1995) 128 FLR 334, 344.

Pricing information, including the basis on which prices are calculated, *may be*
confidential information: *Brink’s Australia Pty Ltd v Kane* [2007] NSWSC 62 at [45] –[47].

30. The fact that information has been disclosed to a limited group (in this case, the “clinicians”), does not of itself mean that it is in the public domain and has lost its confidentiality: *Protec Pacific Pty Ltd v Cherry* [2008] VSC 76 at [47]. Obligations of confidence may be imposed by contract, or in equity, and contractual obligations may extend beyond those which would otherwise be imposed by equity: *Wright v Gasweld Pty Ltd* (1991) 22 NSWLR 317, 333-4 (Kirby P), 339-40 (Samuels JA).

*Unconscionable conduct*

31. *Karam v ANZ Banking Group Limited* [2001] NSWSC 709 involved a bank loan to an incorporated family business. The borrowers had limited ability to understand English and technical legal jargon. The plaintiff’s overachieved before Santow J. The headnote in the Court of Appeal [2005] NSWCA 344 reads as follows:

“Karam Bros Footwear Pty (Ltd) (the Company), was a family owned and operated business. The Company borrowed money from Australia & New Zealand Banking Group Ltd (the Bank). The Bank obtained security over the assets of the Company and the personal assets of the directors of the Company.

The directors were initially unaware that they were personally liable for the Company’s debts. They became aware of the full extent of their exposure when they requested further financial accommodation at a time when the Company was in a perilous financial condition. Unknown to the directors, the Bank had doubts about the enforceability of the original securities. To shore up its security position, the Bank made the provision of further accommodation dependent on the directors executing additional documents including acknowledgments that they were personally liable for the company’s debts and a cross deed of covenant. Further, at the request of the Bank, the directors sold various properties to reduce the Company’s indebtedness.

The directors sought relief in relation to the securities on the basis that they were unjust for the purposes of the *Contracts Review Act 1980*, were unconscionable under the general law and should be varied or set aside. They also sought damages against the Bank in negligence, damages pursuant to s82 of the *Trade Practices Act 1974* (Cth) and an order for equitable compensation.

The trial judge held the original security transactions were unconscionable.
and that subsequent transactions should be set aside on the grounds including, inter alia, economic duress and unconscionability.

Held by the Court:

HN’s [5] provided


Santow J, the trial judge, had said this:

“425 I turn now to the Bank’s second contention, namely that equitable compensation is not applicable where no breach of fiduciary duty has been established nor conduct regarded by equity as fraudulent. The short answer to that contention is that it is now well established that equitable compensation is not limited to actions against fiduciaries for breach of fiduciary duty. Rather it extends to actions against defendants who, although not fiduciaries in respect of the breach in question, have acted in breach of an equitable obligation; see Permanent Building Society (in liq) v Wheeler (1994) 11 WAR 187(FC) (breach of equitable duty to exercise care and skill not amounting in the circumstance to a breach of fiduciary duty)…………………

428 Unconscionable conduct is thus a species of equitable fraud. It is capable of being subject to equitable compensation, as indeed Handley JA confirmed in Houghton v Immer (No. 155) Pty Limited (1997) 44 NSWLR 46 at 56, referring in terms to equitable fraud.”

Commercial Damages [38.70]

Fraud on a minority

32. The doctrine of fraud on a minority was extended by the High Court in Gambotto v WCP Ltd (1994-1995) 182 CLR 432; 69 ALJR 266; [1995] HCA 12 to the expropriation of shares. Commercial Damages [38.90] Fraud on a power.
The principle was stated in *Sugden on Powers*, 5th Ed, 1831, as follows:

“But there are some cases which a court of law cannot reach. This happens where the power is duly executed according to the terms of it; *but there is some bargain behind*, or some *ill motive*, which renders the execution fraudulent, and will enable equity to relieve.”

33. As Gzell J observed in *Lin v The Owners Strata Plan No 50276 [2004] NSWSC 88* [81] “[t]he *formal validity of the exercise of a power is a prerequisite for equitable relief against its wrongful exercise*”.

34. In *Houghton v Immer (No 155) Pty Ltd 44 NSWLR 46 ; [1997] NSWCA 4 December 1997* a unanimous New South Wales Court of Appeal extended the above principles to bodies corporate and to the powers of the proprietors exercisable at general meetings.

The parties were the proprietors of lots in a strata plan. The defendants held 80% of the unit entitlement and the plaintiff 20%. The body corporate passed a resolution to permit the defendants to construct two penthouses in their lot (lot 5) and the roof which was common property. The body corporate passed a by-law allowing the proprietors of lot 5 to "to retain the consequent improvements". Thereafter, a special resolution was passed to authorise the subdivision of lot 5 and common property on and above the former roof to create two penthouse lots. The resolution authorised the body corporate to transfer to the defendants its interests in the penthouse lots derived from common property for $1.

It was held that the special resolution was a fraud on the minority and the court awarded equitable compensation, being 20% of the value of the common property as improved (after expenses) *plus* for the loss of a chance to negotiate to obtain more than 20% of the value of the common property.

This was said to be by analogy with compensation awarded under *Lord Cairn's Act*.

A valiant attempt to seek special leave was refused.

**Commercial Damages [38.150] Quantum:**

Compensation in lieu of rescission or specific restitution
Introduction to the main policy consideration viz trustees must be held strictly to their duties

35. The nature of the case will determine the appropriate remedy which the plaintiff may elect: *Spence v Crawford* [1939] 3 All ER 271 at 288. Some circumstances may call for rescission or specific restitution.

For example in *Maguire & Tansey v Makaronis* (1997) 18 CLR 449; 71 ALJR 781. HCA 23 [1997]71 ALJR 781. HCA 23 [1997], a mortgage had been improperly granted to a parties' solicitor, as part of bridging finance.

The plaintiffs asserted naivety due to being foreign immigrants, but that was held to be misleading. Nevertheless, the solicitors were in a position of conflict and had not advised the plaintiffs to obtain independent advice. The conundrum in the case was that if the mortgage and ancillary documents were rescinded on terms, such that the loan be repaid, that would be tantamount to enforcement. Were there no such terms, that would provide the Makaronis with an undeserved windfall of $250,000.

In the event, the mortgage was held rescinded upon terms, that the principal and interest be repaid within thirty day, failing which the lenders/defendants were entitled to possession.

The plurality said this about the quantum of compensation in lieu of rescission and specific restitution:

36. Rescission and "causation"

This equity to a decree of rescission is immediately generated by the preceding breach of fiduciary duty. *Contrary to submissions by the appellants, issues of "causation", by analogy with those found with the recovery of damages in tort or contract, do not emerge in this case. The fiduciary duty forbade, in the circumstances of the case, entry by the appellants into the transaction of which the giving of the Mortgage was a central part. There was no response by the appellants which showed, in the necessary sense, a fully informed consent. Subject to the need for restitution, the Mortgage was liable to be set aside at the suit of the respondents. The breach of the duty was patent at the creation of the very thing which is to be set aside.*

Where the subject-matter of the transaction is, for example, the sale of a business, intervening changes may render more complex the decree for rescission. In some circumstances, the purchaser seeking rescission by reason of fraudulent misrepresentations by the vendor, may be entitled to an
indemnity for trading losses incurred, both before the purchaser disavowed the transaction and thereafter whilst the business was maintained for the benefit of the vendor; but the indemnity will extend only to that part of the trading losses which were "directly occasioned" by the falsity of the vendor’s misrepresentations[31]. To this extent issues of "causation" may arise in cases of rescission for fraudulent misrepresentation. But that is not this case. Different considerations arise where the plaintiff seeks one or other of the further remedies referred to by the Lord Chancellor in Nocton v Lord Ashburton [32], namely an account of profits, as a personal rather than proprietary remedy[33], or, as another personal remedy, compensation for that which the plaintiff has lost "by [the fiduciary] acting", to use the Lord Chancellor’s phrase, in breach of duty. Likewise where what is sought is a proprietary remedy in the nature of a constructive trust. In these instances, there directly arises a need to specify criteria for a sufficient connection (or "causation") between breach of duty and the profit derived, the loss sustained, or the asset held.

Where the plaintiff seeks recovery of a profit, the necessary connection has been identified in this Court by asking whether the profit was obtained "by reason of [the defendant’s] fiduciary position or by reason of his taking advantage of opportunity or knowledge derived from his fiduciary position"[34]. Particularly where a complex course of dealing is in issue, minds reasonably may differ as to the outcome of the application of these principles. The point is illustrated by the narrow division of opinion in the House of Lords in Phipps v Boardman [35], as to the liability of the appellants, advisers to certain trustees, in respect of their profits on share dealings.

However, what is clear is that the principles by which liability to account for profits is assessed against errant fiduciaries express the policy of the law in holding fiduciaries to their duty. In the joint judgment of this Court in Warman International Ltd v Dwyer [36], after making this point, their Honours continued:

Thus, it is no defence that the plaintiff was unwilling, unlikely or unable to make the profits for which an account is taken or that the fiduciary acted honestly and reasonably.

[there proceeded a brief discussion of Regal (Hastings) Ltd v Gulliver , and Phipps v Boardman ]....

Recovery is sought in respect of a loss. There, the same principle underlying Hallett should be understood as attending any exposition of the phrase used by Lord Haldane LC in Nocton v Lord Ashburton [38], "by [the fiduciary] acting". It is appropriate to begin with those fiduciaries who are trustees. The obligation of a defaulting trustee is essentially one of effecting restitution to
the trust estate. In *Target Holdings Ltd v Redfern* [39], Lord Browne-Wilkinson said:

The equitable rules of compensation for breach of trust have been largely developed in relation to such traditional trusts, where the only way in which all the beneficiaries' rights can be protected is to restore to the trust fund what ought to be there. *In such a case the basic rule is that a trustee in breach of trust must restore or pay to the trust estate either the assets which have been lost to the estate by reason of the breach or compensation for such loss. Courts of Equity did not award damages but, acting in personam, ordered the defaulting trustee to restore the trust estate*[40].

His Lordship continued[41], ……:

If specific restitution of the trust property is not possible, then the liability of the trustee is to pay sufficient compensation to the trust estate to put it back to what it would have been had the breach not been committed … *Even if the immediate cause of the loss is the dishonesty or failure of a third party, the trustee is liable to make good that loss to the trust estate if, but for the breach, such loss would not have occurred.*

*Thus, there is no translation into this field of discourse of the doctrine of novus actus interveniens* [46]

**Commercial Damages [38.170] Equitable compensation and causation**

*Conceptual discussion*: where lies the weight of Australian authority on the reception of the strict rule in *Brickenden v London Loan and Savings Co* [1934] 3 DLR 465 at 469?

**Introduction**

37. Tipping J, writing extra curially in *Causation at law and in Equity-Do we have fusion?* (2000) Canterbury Law Review 443 said this:

“Historically, a closer causal relationship between the wrong committed and the harm or loss suffered has been required at law than in equity. At law the wrongs usually in issue are breach of contract and the commission of a tort, normally the tort of negligence. In equity the courts are most frequently concerned with breaches of trust in the strict sense and with breaches of fiduciary duty. The legal wrongs of breach of contract and tort must be shown to have caused the loss or damage in issue before damages can be awarded.
This need to demonstrate a casual relationship is conceptually separate from and precedes the further controls provided by the concepts of foreseeability and remoteness. Unless a sufficient causal relationship exists between wrong and loss, issues of foreseeability (tort), or reasonable contemplation (contract) and remoteness (both) do not logically arise; for without a sufficient causal link there can in any event be no recovery.

In equity the position has never been as strict. Put shortly, all that is necessary following an equitable, as opposed to a legal wrong, is loss or harm arising from or out of the transaction constituting the wrong. Thus, the relationship between the equitable wrong and ensuing loss does not have to be as close in equity as at law."

"………….the historical approach of equity has been to accept a less stringent approach to causation . Generally equity is not concerned with questions of remoteness and foreseeability. An equitable wrong is seen as affecting the conscience of the wrongdoer, as opposed to being simply a breach of legal duty, and thus equity has taken a more expansive view of causation ……………Equity's approach to relief for conventional breach of trust has tended to permeate the whole field of causation in equity. A breach of trust followed by loss to the trust estate to which the breach was material was enough to establish liability in the trustees for that loss, without regard to questions of foreseeability, remoteness or common law concepts of causation. An example of the rigours of this approach, translated into the field of breach of fiduciary duty, can be seen the decision of the Privy Council in Brickenden v London Loan & Savings Co.[17] In that case, in a judgment delivered by Lord Thankerton, the Privy Council indicated that where there had been a breach of fiduciary duty by failure to disclose material facts, the party in breach would not be allowed to maintain that disclosure would not have altered the other party’s decision to proceed with the transaction. Once the non-disclosed facts are found to be material, speculation as to what course the other party would have taken following disclosure was not regarded as relevant."
Jones [2003] WASC 102 at [103] ff, but one must:

- have regard to an assessment of it caused by the breach on a common sense view of causation: Greater Pacific Investments Pty Ltd (in liq) v Australian National Industries Ltd (1996) 39 NSWLR 143; or
- consider whether there is "an adequate or sufficient connection between the equitable compensation claimed and the breach of fiduciary duty": Maguire v Makaronis (1997) 188 CLR 449; 71 ALJR 781.HCA.

40. A plaintiff may claim equitable compensation or an account of profits, at its election: WA Fork Truck Distributors Pty Ltd v Jones [2003] WASC 102 at [130].

41. In Commercial Damages, I examine important cases such as Beach Petroleum NL v Abbott Tout Russell Kennedy (1997) 26 ACSR 114 at 280-288, a case against a solicitor for breach of retainer, negligence and breach of fiduciary duty. There, his Honour, considered a submission, founded on Brickenden v London Loan and Savings Co [1934] 3 DLR 465 at 469 that once it is established that facts not disclosed by a fiduciary are material, analysis of causation is not required in finding fault. Unsurprisingly, this rule has been the subject of criticism and debate. His Honour concluded that equitable compensation for breach of the equitable duty of skill and care should be assessed on the same basis as common law damages, and that the same common law rules of causation, remoteness and measure of damages should apply: (1997) 26 ACSR 114 at 263.

Also considered are important UK cases such as Target Holdings Ltd v Redfemns (a firm) [1994] 2 All ER 337, the UK Court of Appeal, applied the facilitative rule of causation and found for a beneficiary who would have suffered loss in any event, even if there had been no breach of trust. The majority, Peter Gibson LJ and Hirst LJ concurring held that "where the breach consists in the wrongful paying away of trust moneys so that there is an immediate loss, no inquiry is necessary – the causal connection is obvious".

Ralph Gibson LJ, dissented referring to the dicta of Street J in Re Dawson (dec'd) [1966] 2 NSWR 211 at 215 - All ER 350

42. The decision in Target Holdings Ltd v Redfemns (a firm) [1996] 1 AC 421 was dubious, provoking academic criticism (see QC. JD Heydon, Causal Relationships Between a Fiduciary's Default and the Principal's Loss, (1994) 110 Law Quarterly Review 328) and ultimately was reversed by the House of Lords which held that that it must "be shown that, but for the breach of trust,
the transaction would have not gone through."


44. Canson Enterprises recognised that a fiduciary should not be held liable for loss that does not flow from a breach of fiduciary duty. "The better approach is to look to the policy behind compensation for breach of fiduciary duty and determine what remedies will best further that policy. In so far as the same goals are shared by tort and breach of fiduciary duty, remedies may coincide." (1991) 85 DLR (4th) 129.

45. Target and Canson were followed in Greater Pacific Investments Pty Ltd (in liq) v Australian National Industries Ltd (1996) 39 NSWLR 143 where McLelland AJA, with whom Priestley and Meagher JJA agreed, stated at 154:

"..........The assessment is of the loss to the victim caused by the breach on a common sense view of causation....."

46. Running almost concurrently with Greater Pacific was Maguire v Makaronis (1997) 188 CLR 449; 71 ALJR 781 in the High Court.

Regrettfully, no reference to Greater Pacific was made in Maguire.

In Maguire, Brennan CJ, McHugh, Gaudron and Gummow JJ stated at ALJR 792-793:

"Several matters appropriately will be taken into account when there falls for consideration, in an action against a fiduciary arising other than out of breach of trust, the criteria which supply an adequate or sufficient connection between the equitable compensation claimed and the breach of fiduciary duty."

47. Maguire and Brickendon were considered by the NSW Court of Appeal in O'Halloran v RT Thomas & Family Pty Ltd (1998) 45 NSWLR 262; 29 ACSR 148 in what was held to be contumelious disregard of the rights of the company of which he was a director, O'Halloran transferred shares held by that company to B, even though B could not pay for those shares. The motive for so doing was for O'Halloran and his clique to retain their position of power in the company. There followed what was found to be a "litany of deceit and
breach of fiduciary obligations on the part of O'Halloran”.

48. Before the company could find out what had happened, the value of the shares plummeted. The company sued O'Halloran and his clique on a number of bases including breach of the Corporations Law and also breach of duties as a director. Giles J, the primary judge, had held that O'Halloran's breach of duty had caused his company “to be deprived of registration as holder of, and effective control over, the shares, and caused the loss which it suffered by reason of that deprivation”. The company alleged that by the wrongful registration of the share transfer, it lost the opportunity to sell its shares before their fall in value and this was the crucial issue on appeal. Giles J had identified the causal link of damage to O'Halloran's improper conduct in that the company was unable to sell its shares at any time over the relevant period to any person, including third parties.

49. Spigelman CJ was of the view that the issue was whether an "adequate or sufficient connection" would be established by applying the test appropriate in the case of a breach by the trustee of a traditional trust, or by some other less stringent test.

The former CJ observed at 277:

“Policy favours a stringent test in the circumstances of this case. It is the vulnerability of a company which places its property in the power of directors, that makes it appropriate to adopt the approach to causation applicable to the trustee of a traditional trust in deciding issues of causation for the contravention by a company director of his or her duty not to exercise the power to dispose of property for an improper purpose.”

50. Meagher JA, in his very short judgment concurring with Spigelman CJ, referred to the long list of the "perfidies" of O'Halloran and said at ACSR168:

“In such a situation, no court exercising equitable jurisdiction would debate whether the loss arose from the wrongful transfer, the retention or non-retention of share certificates, the failure to record the transaction, continuing attempts to sell the shares, or anything else. The company had a valuable asset, O'Halloran neutralised it. Equity will see to it that the value of the asset is restored.”

It ought be noted that the NSWCA did not characterise Mr O'Halloran’s breach of duty as a failure to avoid a conflict of interest but characterised the breach of duty as the exercise of power to dispose of the company’s property for an improper purpose.
51. These cases were considered in detail by Rolfe in Hungry Jack’s Pty Ltd v Burger King Corp [1999] NSWSC 112; (1999) 30 ACSR 551; [2001] NSWCA 187; special leave to the High Court was granted 19 April, 2002 in S157/2002; and the High Court notation for 14 November, 2002 is that consent orders were entered into and the appeal was dismissed.

Burger King breached its franchise agreement with Hungry Jack’s and was also in flagrant breach of certain fiduciary duties. Its conduct was disgraceful. Rolfe J felt that a submission by Hungry Jack’s counsel that there was no need to establish causation to the extent required at common law, it being sufficient to prove merely a breach of fiduciary duty and loss, was too simplistic. His Honour held that foreseeability was not a criterion, but causation as a matter of common sense and hindsight, were.

Rolfe J also emphasised the criterion of the majority in O’Halloran’s case of ”an adequate or sufficient connection between the equitable compensation claimed and the breach of fiduciary duty.”

The reception of Brickendon by the Federal Court

52. The Federal Court in Hydrocool Pty Limited v Hepburn (No 4) [2011] FCA 495 enthusiastically embraced Brickendon as follows:

“463. In Youyang v Minter Ellison Morris Fletcher [2003] HCA 15; (2003) 212 CLR 484 (Youyang), the High Court distinguished the case before them (involving a claim that a solicitor had dispersed funds in breach of trust) from the Brickenden case. The High Court said that the case made by Mr Youyang was not a case of a breach by the trustee of the proscriptive fiduciary obligation not to obtain an unauthorised benefit from the relationship and not to be in a position of conflict. However, the observations of the High Court in Youyang at [38]-[42], provide no comfort for an argument that the more stringent test of causation, applied in Smith, Grasso and O’Halloran, had no application where the duty breached by the failure, is the failure to avoid a conflict of interest and duty.

464. It follows that I find that the more stringent equitable test of causation is to be applied in the circumstances of this case. The policy considerations for the application of the more stringent test referred to by Spigelman CJ in O’Halloran, apply also to the circumstances of this case. A company is as vulnerable to a director with power to dispose of its property, as it is to a self-
Conclusion on *Brickendon*

53. It remains to be seen whether the rule in *Brickenden v London Loan and Savings Co* [1934] 3 DLR 465 at 469 will hold. The rule has been applied in several cases. For example, *Farrington v Rowe McBride and Partners* [1985] 1 NZLR 83; *Commonwealth Bank of Australia v Smith* (1991) 42 FCR 390 and *Wan v McDonald* (1992) 33 FCR 491.

While the majority of the High Court in *Maguire v Makaronis* (1997) 188 CLR 449; 71 ALJR 781 decided that it was not necessary to address the issue, Kirby J considered that *Brickenden* still represents the law. However, despite this, His Honour still considered bases on which some relationship between breach and loss was to be established, deciding that "the rule in *Brickenden* can quite comfortably coexist with the exposition of principle by Street J in *Dawson*. Facts will not be 'material' if the relevant loss would have happened if there had been no breach.


55. If *Brickenden* is to be retained it may be on the basis enunciated by Kirby J in *Maguire*

56. However, the New South Wales Court of Appeal in *O'Halloran v RT Thomas & Family Pty Ltd* (1998) 45 NSWLR 262; 29 ACSR 148 specifically endorsed the rule in *Brickenden* and held, essentially, that it applies until such time as it is overruled by the High Court. Accordingly, the position in Australia is stated succinctly in the dicta in *Barton v Armstrong* [1976] AC 104 at 118 at 161 cited with approval by Spigelman CJ in *O'Halloran* namely, just as is the position with fraud and duress, "in this field the court does not allow an examination into the relative importance of contributory causes".

His Honour, in his in-depth analysis of the policy considerations underpinning
this stringent rule, reiterated that a strict standard is required of a trustee of a traditional trust in dealing with trust property. His Honour stated this is because of the vulnerability of beneficiaries and that the same policy applies equally to directors of a company who have the power to dispose of company property and who do dispose of it for an improper purpose. The shepherd should not become a wolf. See also Flanagan Sailmakers Pty Ltd v Walker [2002] NSWSC 1125.

What about the equitable obligation to use skill and care?

57. There is some authority for the proposition that the rule that equity compensates regardless of foreseeability or remoteness, applies not only to breaches of fiduciary duties, but also to equitable obligations to take care; and compensation is assessed as at the date of restoration, not the date of deprivation.

This proposition was articulated in the 2005 case, Miorada v Miorada [2005] WASC 105, Cmr McKerracher QC extending the Re Dawson (dec'd) [1966] 2 NSWR 211 principle discussed above, and affirming that: "Considerations of causation, foreseeability and remoteness do not readily enter into the matter"; and as Street J put it in Dawson's case at 215: "the inquiry in each instance would appear to be whether the loss would have happened if there had been no breach".

The court summarised the principle as follows at [185]:

[T]he cases to which I have referred demonstrate that the obligation to make restitution, which courts of equity have from very early times imposed on defaulting trustees and other fiduciaries is of a more absolute nature than the common law obligation to pay damages for tort or breach of contract. It is on this fundamental ground that I regard the principles in Tomkinson's case [1961] AC 1007 as distinguishable. Moreover the distinction between common law damages and relief against a defaulting trustee is strikingly demonstrated by reference to the actual form of relief granted in equity in respect of breaches of trust. The form of relief is couched in terms appropriate to require the defaulting trustee to restore to the estate the assets of which he deprived it. Increases in market values between the date of breach and the date of recoupment are for the trustee's account: the effect of such increases would, at common law, be excluded from the computation of damages; but in equity a defaulting trustee must make good the loss by restoring to the estate the assets of which he deprived it notwithstanding that market values may have increased in the meantime. The obligation to restore to the estate the assets of which he deprived it necessarily connotes that, where a monetary compensation is to be paid in lieu of restoring assets, that compensation is to
be assessed by reference to the value of the assets at the date of restoration and not at the date of deprivation. In this sense the obligation is a continuing one and ordinarily, if the assets are for some reason not restored in specie, it will fall for quantification at the date when recoupment is to be effected, and not before.

58. *Miorada* was a case concerning, inter alia, a breach of fiduciary duty relating to dealings in land; and where the remedy ordered was *restitutio in integrum*. It was held, by reference to expert evidence and authority, that there would be no liability for CGT, by reason of the nature of remedy; and that hence there was no reason to gross up the award with an amount for CGT. However, the court invited counsel for the plaintiff to seek an order that if CGT were levied, then the plaintiff be indemnified therefore.