

PART I – MISREPRESENTATION

I INTRODUCTION

A Definition

A misrepresentation is a false statement of fact made prior to contract formation that induces a party to create contractual relations.

Misrepresentation is one of a number of circumstances said to vitiate assent to the terms of an agreement:

- Misrepresentation
- Misleading conduct under the *Trade Practices Act 1974* (Cth)
- Mistake
- Duress
- Undue influence
- Unconscionable dealing
- Unconscionable conduct under the *Trade Practices Act 1974* (Cth)
- Illegality

These circumstances can occur at or prior to contract formation.

Additionally, a number of circumstances can arise after contract formation that could allow a party to escape performance:

- Misleading conduct under the *Trade Practices Act 1974* (Cth)
- Unconscionable conduct under the *Trade Practices Act 1974* (Cth)
- Illegality
- Breach
- Non-fulfilment of condition
- Consent
- Frustration

B Contextualisation

Under the *Trade Practices Act 1974* (Cth) s 52, a court may order the rescission of a contract or award damages to a person to whom a misleading or deceptive representation has been made. The Act and its remedies are broader in scope than those of common law misrepresentation.

Though prohibitions on misleading and deceptive conduct today encompass most cases of misrepresentation, common law misrepresentation is still important in several circumstances:

- The *Trade Practices Act* only applies ‘in trade and commerce’
 - Thus, in domestic or other contexts, a vitiating factor at common law will be necessary
- In interpreting the *Trade Practices Act*, courts will have regard for and draw analogies with common law misrepresentation

C *Rôle*

1 *Defensive*

Misrepresentation can be asserted as an excuse by a party wishing to avoid performance. Where successful, they will be entitled to refuse performance of their obligations under the contract without incurring a penalty for its breach.

2 *Offensive*

Misrepresentation also has an offensive quality. Where coupled with a statutory cause of action, it can give rise to a right to damages or restitution.

D *Remedies*

The representee's right to rescind forms the defensive component of misrepresentation's remedial offerings. This right is premised on a finding that, where formation has been induced by misrepresentation, no valid contract was ever created.

Such retrospective invalidation means that all moneys paid under the contract – including consideration – must be refunded, and all goods returned. It also means that termination (eg, for breach), which is prospective, is not possible, since it there was never a contract to breach.

Rescission for misrepresentation takes parties back to the pre-contractual status quo. It is thus an *ab initio* remedy.

E *Primary Issues*

Three issues typically arise in the context of misrepresentation:

1 *Creation of the right to rescind*

- Something must have happened to give the right to a party

2 *Restrictions on the exercise of the right to rescind*

- Somewhat peculiarly, there may be circumstances where a right to rescind has been created but restrictions prevent it from being exercised

3 *Loss of the right to rescind*

- Something may have happened to revoke the right

II CREATION OF THE RIGHT TO RESCIND

A *At Common Law*

The creation of the right to rescind for pre-contractual misrepresentation differs in scope between equity and common law.

At common law, rescission is available only if

- The misrepresentation is fraudulent; and
- Entry into the contract was induced by the fraudulent misrepresentation

Rescission for misrepresentation is thus only actionable where:

- 1 A false statement of fact has been made; and
- 2 It is this statement that induced entry into the contract.

If no recognised misrepresentation has been made, or there is no causal connection between it and the misrepresentee's entry into the contract, then it is not actionable.

B *In Equity*

1 *Ambit of operation*

In equity, rescission is available even if the misrepresentation was innocent (ie, not fraudulent). In cases where the misrepresentation is fraudulent, equity has a concurrent jurisdiction over any right to rescind.

2 *Restrictions on the equitable right*

The ambit of the equitable right to rescind is restricted in three ways. These restrictions make it worthwhile to allege common law fraud in cases where the equitable right of rescission would otherwise be restricted.

a) *Sale of land*

Where land has been sold and a misrepresentation is discovered and acted upon only subsequent to settlement, a distinction between innocent and fraudulent misrepresentation is drawn in equity.

- Where the misrepresentation is innocent, there is no right to rescind a contract for the sale of land after settlement
- Only fraudulent misrepresentations can give rise to a right to rescind at this point

Seddon suggests that after a contract for the sale of land has been executed (ie, performed, though this is somewhat controversial – see below), a party cannot rescind for an innocent misrepresentation. The controversy pertaining to execution arises in the matter of what is to be taken as indicating performance. Does it mean signing a deed or completing the transaction? Should the rule apply to all transactions or just the sale of land?

The traditional common law rule in *Seddon's* case has since been abolished in South Australia and the Australian Capital Territory by legislation; it has also been modified for the sale of goods in Victoria and New South Wales, leading some commentators to conclude that it is a law 'in retreat' and at any rate, 'often ignored'.¹ The exception to this trend is, of course, in respect of the sale of land, where it remains a requirement that good title passes notwithstanding an innocent misrepresentation made prior to execution of the deed.

b) Contracting out of the right

It is possible to exclude the right to rescind for innocent misrepresentation by providing so in the terms of the contract.

c) Partial rescission

In some cases, it may only be possible to partially rescind the contract.

Vadasz v Pioneer Concrete (1995) HCA:

Facts

- Mr Vadasz signs a guarantee for the delivery of concrete personally assuring the supplier of his liability for payment for its delivery
- He is told it relates only to future deliveries
- In fact, it applies to all deliveries, past and present

Issue

- Is it possible to rescind the contract between Mr Vadasz and Pioneer?

Reasoning

- In signing the guarantee after being told it related to future deliveries, Mr Vadasz accepted liability for concrete already delivered
- It is only possible to allow rescission of the contract in respect of future deliveries not yet made, since Mr Vadasz was willing to accept liability for past deliveries

Decision

- Only partial rescission can occur

C *Fraud*

Fraud must be subjectively ascertained. A statement will be fraudulent where it is untrue to the knowledge of the representor; or it was made with reckless indifference as to its veracity (*John McGrath Motors*).

John McGrath Motors v Applebee (1964) HCA:

¹ NC Seddon and MP Ellinghaus, *Cheshire & Fifoot's Law of Contract* (7th ed, 1997).

Facts

- A was told that the car he was thinking of purchasing was ‘a new car’
- In fact, it was not completely new in the objective sense (it had been driven from the manufacturing warehouse to the dealer’s showroom, some 200kms because the showroom was in a rural area)
- However, nor was the car second hand

Issue

- Was the representation fraudulent?

Reasoning

- Trial judge: the car was not ‘new’ because it had been used; the dealer had knowledge of this usage, so the statement was fraudulent
- On appeal:
 - This is not the proper approach
 - It needs to be shown that the seller was conscious of the misrepresentative nature of their statement as he or she intended it to be misrepresentative
 - Determining fraud is not an objective exercise; the misrepresenter must have believed in the falsity of their misrepresentation as interpreted by them
 - A subjective test is used to determine fraud
 - However, there is an objective component: ‘recklessness’
 - A statement will be fraudulent where:
 - It is untrue to the knowledge of the representor; or
 - It was made with reckless indifference as to its veracity

Decision

- The statement that a car is ‘new’ when having been driven to the showroom is not fraudulent because it was made without knowledge of or reckless indifference towards its falsity
- Statements’ truths should be assessed against their makers’ knowledge or belief in their meanings – ‘in the sense in which he understood it’ – not a court’s construction thereof
- Because the John McGrath Motors dealer held an honest belief in the newness of the car when they made the representation, it was not fraudulent
- Subjective belief in falsity is necessary for a statement to constitute a fraudulent misrepresentation

The consequence of *John McGrath* is that a plaintiff needs to establish the subjective meaning of a representation in the eyes of the representor. This gives rise to a difficult evidential burden (see, eg, *Krakowski*).

Krakowski v Eurolynx Properties (1995) HCA:Facts

- K is in the process of buying a shop in a shopping centre owned by E
- K deals with E through an agent, B, and expresses a desire for the lease to return 10% p/a on the cost of the property, and be occupied by a reliable tenant
- B locates a tenant, Swaeder, who signs a contract for 6 years of tenancy
- The contract between K and E contains, in cl 32, a statement required by the *Sale of Land Act* (Vic), as well as a copy of the tenancy agreement between K and S and a

- merger (entire agreement) clause
- The annual fee of \$156 000 rent, negotiated by B to be paid by S, is well above the market rate, so E agrees to provide some additional enticements:
 - The first three months' rent are free
 - A cash payment of one year's rent is provided to fit out the shop premises
 - These additions are not contained in the lease itself, but within a separate letter of understanding between E and S
 - K knew nothing of these terms, which in fact violate the merger clause
 - S proceeds with the lease and becomes the K's tenant
 - However, S turns out to be an unreliable tenant: he disappears after a few months
 - K finds out about E's letter of understanding with S
 - K rescinds the contract for sale of the shop 12 months later, claiming fraudulent misrepresentation on the part of E

Issue

- Was E's misrepresentation fraudulent?

Reasoning

- In order to be voidable there needs to be fraud, because innocent misrepresentations cannot give rise to a right to rescind after settlement of a contract of sale (which there is here)
- The subject meaning of the merger clause
 - It was argued by E that collateral incentives are commonplace, and that the merger clause was not meant to exclude the possibility of such arrangements
 - This argument was rejected; the merger clause unequivocally says that there is only one contract related to the tenancy
- Corporate fraud
 - The representative drafting the letter of understanding didn't know of K's requirements or the existence of the merger clause, so how can he be guilty of fraudulent misrepresentation?
 - The Court also rejects this argument; all agents of a corporation are relevant to the question of fraud
 - The court is not interested in the state of mind of just one person, and will draw in all persons
 - The corporate mind thus extends to all actors associated with the transaction
- No evil motive or strategy need be required
 - Consciousness of the falsity of the representation is all that is needed for it to be fraudulent
 - Thus while Mallesons and E did not have ill intent in seeking to secure S as a tenant, they were collectively aware of the falsity of the merger clause, and were thus acting fraudulently in making that representation an express term
- Toohey J (dissenting):
 - The misrepresentation was not intentional because there was no knowledge of falsity and therefore no fraud

Decision

- To establish fraud, it is insufficient to prove that a representation was false
- The representor must have had no honest belief in the truth of their representation
- Here, the ancillary agreement made to induce the lessee to occupy the plaintiff's property was deliberately concealed by the developer defendant, who in their contract of sale of

- the property described the primary agreement as being complete and singular
- The third party law firm is liable to the defendants for failing to advise them of the need for disclosure of the inducement arrangement
 - Because E was aware of the falsity of cl 32 of the contract of sale, they acted fraudulently in drafting a letter of understanding containing additional incentives to secure S as tenant despite representing that the tenancy agreement was complete

D *Restitutio in Integrum*

In order to rescind a contract, it must be possible to restore both parties to their pre-contractual status quo. If no such *restitutio in integrum* is possible, the misrepresentee may not be able to rescind.

The primary difficulty is created by the elapse of a significant period of time between the execution of a contract and the time when a party seeks its rescission.

In the context of equitable rescission, it is to be noted that greater flexibility exists in determining the possibility of *restitutio*.

Alati v Kruger (1956) HCA:

Facts

- A bought a fruit shop from K
- It is stated in the contract that the shop's takings are £100/week
 - Technically, this isn't in itself a pre-contractual representation; however, the conduct of taking the contract to the offeree constitutes a representation that the terms are correct
- Within 1 week of purchase, the buyer notices that the takings are significantly less than £100
- A rescinds after 2 weeks

Issue

- Can Alati give back 'in specie' what was bought?

Reasoning

- The premises were used by A and are no longer in the same condition as when they were purchased
 - A supermarket had just opened across the road, so the business is now substantially less profitable
 - Stock had diminished from sales, and other stock is now rotting
 - Problems with the landlord have arisen in relation to the possibility of reassigning the lease
 - Therefore, at least at common law, A cannot rescind
- However, in equity, the deterioration of the business may be forgiven because it was not A's *fault*

Decision

- Where the subject of a contract is irrevocably changed by circumstances in no way the fault of the misrepresentee, where that party subsequently seeks rescission of the contract,

the agreement may be voided notwithstanding restitutio not being strictly possible

Where the subject of a contract is used or consumed in some way, it may also be possible, in equity, for the restitutio requirement to be satisfied by paying an amount equivalent to outright return of the goods to the seller (*Vadasz*).

Vadasz v Pioneer Concrete (1995) HCA:

Issue

- Can the director of a company rescind a contract for the sale of concrete due to the seller's false claim that the concrete was of a particular composition?

Reasoning

- The concrete had already been used in buildings and could not be returned
- At common law: restitutio is not possible, so no rescision
- In equity: the director can just make payment 'representing the return of the concrete' and rescision can subsequently be allowed

Decision

- The director must pay the seller an amount 'representing' the used concrete, but is then entitled to rescision of the contract of sale

E *Actionable Misrepresentation - False Statement of Fact*

1 *Statements*

Misrepresentation can be constituted by a written or verbal statement. It can also consist in the non-disclosure of salient information that misleads the other party where there is a duty to disclose that information.

A duty to disclose arises only in certain contexts:

- a) Half-truths
 - Where the statement is, without further disclosure, misleading
- b) Falsification
 - Where the statement has become false since being made
- c) Fiduciary relationships
 - Where the parties are in an fiduciary relationship (insurer/insured, lawyer/client, etc)

Thus, for example, in *Alati*, there existed no duty to disclose the opening of the supermarket. However, *Krakowski* is a case of non-disclosure (at least according to the learned trial judge). There, Eurolynx failed to disclose the other arrangements made by it in respect of securing the

tenant. The High Court of Australia also noted in that case that the merger clause itself creates an obligation to disclose all details of the transaction.

2 Facts

The law draws a distinction between facts, opinion, and predictions:

- Fact: [profitability of resort] (*Gould*) or 'very large sum of money' (*Nicholas*)
- Opinion: [this is a very good car]
- Prediction: 'I think that this land will be sewered in four months' time' (*Ritter*)

A statement containing evaluative or qualitative terms will not necessarily be an expression of opinion (*Nicholas*).

Nicholas v Thompson (1924) VR:

Facts

- The contract was for the sale of rights to a film process and a syndicate
- The buyer, N, relied upon statements made by the seller, T, that he had been offered 'a very large sum of money' for the rights

Issue

- Was the representation one as to fact or merely an opinion?

Reasoning

- The presence of evaluative or qualitative terms ('very large') do not render any statement one of opinion

Decision

- Here, the statement was not merely an expression of an opinion, but was, in fact, a statement of fact
- As such, it is capable of constituting a misrepresentation

Even where a representation does contain an element of opinion, it may still constitute a statement of fact where it is sufficiently factual (*Gould*).

Gould v Vaggelas (1985) HCA:

Facts

- Gould Holdings purchased a tourist resort from the Vaggelases on the basis of their representations that the business was very profitable and their submission of false figures as to occupancy rates and financial returns
- The Goulds' venture was unsuccessful and, two years after purchase, they damages for deceit, negligence, and breach of contract on the grounds that the statements about profitability were fraudulently misrepresented

Issue

- Were the representations statements of fact or of opinion?

Reasoning

- The statements about profitability were sufficiently factual to constitute a factual statement, even though they contained an element of opinion

Decision

- The statements were factual in nature

If the representor offers a prediction about the future couched as a representation about his state of mind, it may constitute a statement as to facts (*Ritter*).

Ritter v North Side Enterprises (1975) HCA:Facts

- North Side, the seller of property, made a statement to Ritter, the buyer, that 'I think that this land will be sewerred within 4 months' time'
- R relied on this statement in entering into the contract; later, upon discovering that the property had not yet been 'sewerred', he sought rescission of the contract of sale

Issue

- Was the representation one of fact or opinion?

Reasoning

- A statement of belief in the future connection of sewerage pipes to a property within 4 months is only a prediction, despite the buyer's assertion that the seller did not believe that statement
 - This would be a representation as to a future state of affairs
- However, the fact misrepresented was the state of mind of the representor
 - This is a representation of fact about the present which, if false, could be a basis on which to grant rescission
- Misrepresentation is fraudulent where the representor knew (or was reckless towards the possibility that) the statement was false

Decision

- If a representation is merely a predication it cannot constitute a basis for rescission
- However, where, as here, the fact misrepresented is a present state of mind (ie, a belief about the future), rescission is a possible consequence of their falsity

3 *Falsity*

The representation must, of course, be false. Whether a statement is false is an objective enquiry.

F *Actionable Misrepresentation – Inducement*

Having established that a misrepresentation existed in the form of a false statement of fact, it must be proven that the representee entered into the contract on this basis.

This causal element must be established by the representee. Direct evidence of their state of mind is difficult to adduce, so the rule of materiality operates. In the absence of direct evidence, if the statement is 'material', then the Court will infer that the inducement occurred.

Essentially, a 'material' statement is one that is objectively important (*Nicholas*). If the 'natural and probable effect of a statement will influence the mind of a normal person to enter into the contract' then an inference of causation may be drawn.

Gould v Vaggelas (1985) HCA:

Issue

- Did the representee rely on the sellers' misrepresentations in electing to enter into the contract of sale of the resort?

Reasoning

- Here, there was direct evidence of Mrs Gould's incredulity of the accounting figures provided by the Vaggelases to the Goulds
- Knowledge of the falsity of a misrepresentation normally precludes there being inducement
- Here, however, she was still found to be induced by the misrepresentation:
 - 'A knave does not escape liability because he is dealing with a fool'
 - The misstatement still had a causative influence on Mrs Gould, which is sufficient for there to be inducement

Decision

- An inference of inducement may be drawn when a party enters into a contract 'after a material representation' of fact may be rebutted
- If the representation was known by the representor to be untrue, it is still fraudulent even where the representee expresses doubt
- It is thus possible to infer that the Goulds were induced by the misrepresentations of the Vaggelases to enter into the contract

If a representor knows of a peculiar characteristic of the representee that would particularly influence them, then this becomes the relevant criterion of the inducement determination. That is, the enquiry becomes slightly objective: would a representee of this characteristic have been influenced by this misrepresentation?

Nicholas v Thompson (1924) VR:

Issue

- Did the misrepresentation induce Nicholas to enter into the contract of sale?

Reasoning

- The outcome of the sale was speculative in nature; it was a venture whose virtue was unknown and about which few concrete predictions could be made
 - Thus, the representation made by the seller that a high offer had been made becomes especially important to the buyer

- It is a material indication of the film process' quality in the absence of other material on which to base a judgment

Decision

- Though no evidence can be adduced as to the specific factors that caused Nicholas to enter into the contract, because the representation was the only material indication of quality available to him, it can be inferred that such a statement induced his assent

III EXERCISE OF THE RIGHT TO RESCIND

A *Restrictions on the Right to Rescind*

The representee induced to enter into a contract on the basis of a fraudulent or innocent misrepresentation may nevertheless be unable to exercise their equitable or common law right to rescind the contract.

1 *Contractual restrictions*

The contract may contain a provision excluding or in some way restricting rescission for innocent (but not fraudulent) misrepresentations (*Byers*).

2 *Unconscionability*

The right to rescind may not be exercised unconscionably (*Krakowski*).

The unconscionability restriction is unlikely to arise if the representation was fraudulent and the common law right exercised— equity would rarely view such a reaction as unconscionable.

However, if an innocent misrepresentation is made and an equitable right to rescind is relied upon, unconscionability may prevent rescission. For example, in *Alati*, the value of the business was decreased (though on the facts it was reasonable for the buyer to demand rescission). In *Krakowski*, the case was remitted to the Supreme Court to find out whether the buyers of the shop acted unconscionably. The Court needs to be satisfied that it would not be unconscionable to allow rescission before they will allow the right to be exercised.

3 *Partial Rescission*

It may be possible to prevent unconscionability or satisfy a requirement of the contract by allowing only partial rescission (see above Part II, s B, ss (2)(c)).

B *Loss of the Right to Rescind*

1 *Affirmation*

A misrepresentee may lose the right to rescind if they affirm the contract by engaging in conduct that suggests that they are going to continue to perform their obligations under it irrespective of the inducement.

2 *Waiver*

It may also be possible to waive the right to rescind (see, eg, the Commonwealth in *Verwayen*). This would indicate to the other party that the right is being given up voluntarily.

3 *Estoppel*

An estoppel may also operate in respect of conduct inducing an assumption in the representor to prevent the representee from departing from that position by subsequently rescinding the contract. Here, it is the party's departure or threatened departure from an assumption induced in the representor (that the contract would be affirmed) that causes the right to be lost.

V **RIGHT TO DAMAGES**

A *Innocent Misrepresentation*

Damages for misrepresentation are *sui generis*.

No damages are available for innocent, non-negligent, non-fraudulent misrepresentation, unless there is a statutory cause of action available (eg, under the *Trade Practices Act 1974* (Cth), the *Misrepresentation Act* (SA)).

B *Tortious Misrepresentation*

Where the conduct comprising the misrepresentation amounts to a tort, the misrepresentee may claim damages in tort. The quantum of damages will be according to the tort measure of reliance loss, so compensation will only be available to remedy the effect of the misrepresenter's tort (and not give the benefit of the contract as represented).

Torts for commission of which a common law action is commonly brought for damages in the context of misrepresentation include: deceit, negligence.

For example, in *Alati* (where the buyer of a fruit shop found there were fewer weekly takings than claimed by the vendor), if the buyer brought an action in tort for the vendor's misrepresentation, he would be unable to recover his loss of the claimed or expected earnings (£100 minus the actual takings), unless he can establish that he turned down a similar offer in order to accept this one. The reason such a fact would allow recovery of the difference is that in relying on the seller's misrepresentation, the loss of the benefit of entering into another, similar contract would be incurred.

If such a fact cannot be established, however, and the plaintiff wishes to rescind the contract, he would be entitled only to the reliance costs associated with running the shop for the period in

which he was its owner. If the buyer wishes nevertheless to affirm the contract, he is entitled to the difference in the value of the shop from the claimed value.

C Where the Contract is Affirmed

If the misrepresentee elects to affirm the contract, then it may be possible to sue the other party for its breach (if the representation forms a relevant term of the contract).

If, however, the misrepresentee rescinds the contract, then no such damages for breach would be available because the contract has been nullified *ab initio*. Since the contract never existed, it cannot then be breached.

D Trade Practices Act 1974 (Cth) ('TPA')

Salient characteristics:

- Actions are available to *anyone* – not just consumers
- Prohibitions on misrepresentative conduct affect more people than just corporations
- The *Fair Trading Act* (Vic) (and other equivalent state legislation) applies to 'parties', mirroring the federal legislation and making individuals also liable for breach of its provisions
- Accessories to misrepresentative conduct may also be liable: s 75B

Remedies available:

- Injunctions (though these are almost never applied for and seldom granted)
- Rescission for the act of a party
 - The TPA does not grant an automatic right
 - A party seeking rescission must apply to a court to do so
 - The right to rescind is subject to court order

Part/Section	Title	Description
I-IV	Definitions	Conduct, consumer, etc
IVA: ss 51AA, AB, AC	Unconscionable conduct	Prohibit unconscionable conduct in trade or commerce
V: 52	Consumer protection and unfair practices	Prohibits misleading conduct in trade or commerce
VI	Enforcement and Remedies	Not only available to consumers [except in QLD], and not only available against corporations
s 75B	Participants and accessories are also liable	
s 80	Injunctions	
s 82	Damages	
s 87(1A)	Other orders	Include rescission and termination