MIHALJEVIC v. EIFFEL TOWER MOTORS PTY. LTD. AND GENERAL CREDITS LTD.[1]

ACADEMY OF HEALTH AND FITNESS PTY. LTD v. POWER[2]

Two recent decisions in the Victorian Supreme Court raise interesting problems in the area of rescission of contracts for innocent misrepresentation inducing entry into the contract. In the first situation, the innocent misrepresentation, although inducing entry into the contract, did not become a term of the main contract. In the second situation, the misrepresentation not only induced entry in the contract, but was incorporated in the contract as a warranty. Gillard J. in *Mihaljevic* v. *Eiffel Tower Motors Pty. Ltd. and General Credits Pty. Ltd.*[3] also sought to lay down a clear enunciation of the law relating to collateral contracts.

The facts of *Mihaljevic's* case[4] are fairly straightforward. The defendant motor car dealer published the following advertisement in the "Situations Vacant" column of a daily newspaper: "Driver (not semi) interstate capable man with good credit and reasonable asset position required for permanent contract invest of $1100 will earn approximately £4500 p.a. including no wages earnings receivable fortnightly all calculations available for inspection and right applicant may receive financial assistance . . ."

The plaintiff responded to this advertisement and was shown calculations based on the earnings from a contract with an interstate haulier to make two trips to Sydney from Melbourne each week. The truck was not available for inspection by the plaintiff at the time of his enquiry, but the salesman told him the truck was "in good condition". Relying on this statement, the plaintiff agreed to accept $2000 for his own vehicle, which amount was to be used as a deposit on the truck, and the next day, having paid a further amount of $200 on deposit and inspected the truck, he signed an offer to the defendant credit company to enter into a hire-purchase contract for the truck.

The plaintiff commenced his operations the next day. Owing to the very defective mechanical condition of the truck, he only completed two interstate operations during the next 17 days. At the end of this period he returned the truck to the defendant dealer and informed them that he would have nothing more to do with it. The plaintiff then brought proceedings against the dealer claiming damages for deceit or breach of warranty arising from the falsity of the statement by the dealer's servant as to the condition of the truck. Also—relying on s. 6(1) of the Hire Purchase Act 1959[5]—against the credit company for the same reason claiming rescission of the hire-purchase agreement and the return of moneys either paid or credited to him under the agreement.

[1] [1973] V.R. 545.
[2] [1973] V.R. 254.
[3] [1973] V.R. 545.
[4] Ibid.
[5] S.6(1) of the Hire Purchase Act provides:
"(1) Every representation warranty or statement made to the hirer or prospective

Collateral Contract

Gillard J. although not believing the salesman's testimony reliable, could not find sufficient evidence of the intention necessary for the misrepresentation to be fraudulent. Therefore to succeed in his claim for damages against the dealer, the plaintiff had to establish that the salesman's statement that the truck was "in good condition" was not only an innocent misrepresentation which had induced him to enter into the hire-purchase contract, but was also promissory in nature. In finding that the statement was in fact promissory in nature and was supported by the consideration that the plaintiff should enter the hire-purchase contract. Gillard J. referred to his earlier judgment in *J. J. Savage and Sons Pty. Ltd.* v. *Blakney*.[6] Relying on that case, he laid down seven rules which he suggested could be used to distinguish a mere misrepresentation inducing entry into a cotnract from a promissory statement which becomes a collateral contract. He said:[7]

"First to establish that a statement made during the course of negotiations was promissory or contractual in nature, proof of a common intention of the parties to impose a contractual obligation on the person making the statement is essential. Secondly, it is unnecessary that the statement must contain an express form of words. It is sufficient if in the context the words used import the requisite meaning to impose on the person making the statement or contractual obligation by way of promise or guarantee. Thirdly, whether a statement was intended to be contractual or not must be determined objectively in the light of the whole of the circumstances. Fourthly, whether an animus contrahendi[8] exists is a question of fact and can only be determined by looking at all the circumstances attending the transaction. Fifthly, in the process of drawing such conclusion the tribunal of fact is not entitled to draw any inference contrary to the express terms of any written contract made between the parties. Sixthly, it is easier to draw an inference that a warranty was intended where the person making the statement of the

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whether orally or in writing by the owner or dealer or any person acting on behalf of the owner or dealer in connection with or in the course of negotiations leading to the entering into a hire-purchase agreement shall confer on the hirer—

(a) as against the owner—the same right to rescind the agreement as the hirer would have had if the representation warranty or statement had been made by an agent of the owner; and

(b) as against the person who made the representation warranty or statement and any person on whose behalf such person was acting in making it—the same right of action in damages as the hirer would have had against them or either of them if the hirer had purchased the goods from such first-mentioned person on whose behalf he was acting (as the case requires) as a result of the negotiations."

[6] [1973] V.R. 385. Gillard J. was the trial judge. The full Court of the Victorian Supreme Court reversed his decision on the basis that they did not draw the same inference from the facts before the Court. The High Court (1970) 44 A.L.J.R. 123 unanimously in a joint judgment upheld the decision of Gillard J. The statement of law by Gillard J. in the court of first instance was not rejected in either of the appeals.

[7] At 555 and 556.

[8] Intention to create legal relations; intention, perhaps, to contract.

> condition or quality of an article has a personal knowledge thereof and the person to whom the statement is made is to the knowledge of both parties, ignorant of the condition or quality of the article and is relying on the first party's knowledge. Finally, in order to determine whether such intention be inferred, I . . . am of the opinion that the method suggested by Lord Denning M.R. in *Oscar Chess Ltd.* v. *Williams*[9] and *Hornal* v. *Neubreger Products Ltd.*[10] is the most useful way to arrive at a decision. His Lordship said :'If an intelligent bystander would reasonably infer that a warranty was intended, that would suffice even though neither party in fact had it in mind.' "

It would seem that the only rule, as such, is the first proposition mentioned and the rest of the propositions, with the exception of the fifth, are designed to emphasise that the "common intention" is to be determined objectively, rather than subjectively. The fifth proposition is a reference to the "no inconsistency" rule which is not relevant in this particular context, i.e., the tripartite situation as distinct from the true collateral contract where the main contract is between the representor and the representee. Gillard J. treated this question as though s. 6(1)(b) of the Hire Purchase Act was not relevant. However, it could be argued that the Act in limiting the action for damages to situations where the representor would have been liable if a contract had resulted between the representor and the representee, could mean that an inconsistency would bar the plaintiff's action. In this case, however, there was no such inconsistency.

It is evident that the propositions put forward are rather wide and vague, leaving the court a considerable discretion in determining which circumstances amongst "all the circumstances" will be given weight, and exactly what an "intelligent bystander" would infer from the transaction. In some ways, this is welcome, as it is obvious that in very many cases, as in the present one, the purchaser of goods has no real understanding of the documents he signs, or the legal niceties of the transactions into which he is entering. He relies principally upon representations made to him by the salesman, and if the reasoning of Gillard J. is widely followed it may represent a substantial step away from the sometimes unpalatable principle of caveat emptor.

Rescission of Contracts

Having found for the plaintiff in the issue of his claim for damages against the defendant motor dealer, His Honour turned to the question of rescission of the Hire Purchase contract with the defendant credit company. It is in this area that the second case, *Academy of Fitness and Health* v. *Power* raises certain points of interest.

Again, the facts in *Power's* case are quite simple. Power was the defendant in an action to recover moneys owed by him under a written contract pursuant to which the complainant agreed to make available to the defendant the facilities of a health studio in the manner specified

[9] [1957] 1 All E.R. 325, 328.
[10] [1956] 3 All E.R. 970, 972.

therein, including "free use at any time of the Sauna Baths at the Academy's premises". Prior to the entering into the contract, an agent of the complainant had told the defendant that the sauna baths were available at any time, and relying on this representation, the defendant entered into the contract. Subsequently the defendant discovered that the sauna baths were only available for his use on alternate days—their use alternated between men and women. Power had paid no money pursuant to the contract, and had made no use of the Academy's facilities. Power did not notify the Academy of his election to rescind the contract prior to the first hearing of the case in a Magistrate's Court.

The Magistrate had found in favour of Power, on the ground that the misrepresentation was fraudulent. However this was clearly wrong, since fraud was at no time alleged and certainly not proved. The issues in the case were thus twofold. Given that the case had to be resolved on the basis that the misrepresentation was innocent, it first had to be decided whether the contract being wholly executory, the defence of misrepresentation was sufficient, if proved, to sustain a finding of an effective rescission of the agreement by the defendant without there having been any further plea or act of disaffirmation. Crockett J. after a thorough analysis of the relevant authorities, found that it was sufficient.[11]

The second issue was whether the defendant's right in equity to rescind the contract on the ground of innocent misrepresentation inducing entry into the contract had been lost by reasons of the incorporation of the misrepresentation into the contract as a warranty, breach of which gave rise to an action for damages.

A similar issue arose in *Mihaljevic's* case. Gillard J. held that the Hire Purchase contract was executory in nature, and that restitutio in integrum was possible. He said:[12]

> "In my opinion, the hire-purchase agreement was unquestionably a contract of an executory nature which was not executed by the bailment commencing. It did not thereupon come to an end and an estate was not created out of the contract. True, a right to possession was given but that possession was to be regulated subsequently by the terms of the contract, and the prime intention of the parties was the subsequent bailment of the vehicle, and the hire-purchase agreement was only to come to an end on the future sale of the vehicle by the owner to the hirer.
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> . . . The transaction bore no resemblance to a contract followed by a conveyance of real property in completion or execution of the contract, the operation of which thereby came to an end . . ."

Concerning restitutio in integrum Gillard J. followed *Senanayake* v. *Cheng*[13] saying:[14]

> "The relevant test is whether, if the truck were returned under an order or decree for rescission, the vehicle would be substantially of the same

[11] [1973] V.R. 254, 255, 258-263.
[12] [1973] V.R. 545 at pp. 564-5.
[13] [1965] 3 W.L.R. 715.
[14] [1973] V.R. 545, 562.

quality, condition and identity as it was when it was received by the plaintiff under the contract of bailment from the credit company. Having regard in particular to the acceptance of the hire-purchase offer on 22nd April and the return of the vehicle on 25th April the answer to this question . . . must be in favour of the plaintiff".

Since Gillard J. had found that s. 6(1) of the Hire Purchase Act put the defendant in the same position as though the misrepresentation had been made by its agent[15] the question remained whether the plaintiff's right to damages against the motor dealer barred his right to rescind as against the credit company.

To resolve this question, both Gillard J. and Crockett J. considered the English Court of Appeal decision in *Leaf* v. *International Galleries*.[16] In that case, Leaf purchased a painting which the gallery represented was by Constable. Five years later Leaf discovered the painting was not by Constable and wanted to rescind the contract of purchase for innocent misrepresentation. Denning L.J. found that the misrepresentation was also a condition of the contract, and said:[17]

"Although rescission may in some cases be a proper remedy, it is to be remembered that an innocent misrepresentation is much less potent than a breach of condition; and a claim to rescission for innocent misrepresentation must at any rate be barred when a right to reject for a breach of conditions is barred. A condition is a term of the contract of a most material character, and if a claim to reject on that account is barred, it seems to me a fortiori that a claim to rescission on the ground of innocent misrepresentation is also barred.

"So, assuming that a contract for the sale of goods may be rescinded in a proper case for innocent misrepresentation, the claim is barred in this case for the self-same reason as a right to reject is barred. The buyer has accepted the picture. He had ample opportunity for examination in the first few days after he bought it."

Gillard J. sidestepped the main thrust of this statement by Lord Denning, preferring to use it as support for his finding that an innocent misrepresentation which induces a person to enter into a contract does not cease to be an innocent misrepresentation simply because it is incorporated into the contract, whether as a warranty or as a condition. Or, as in *Mihaljevic's* case, it is the only term of a contract collateral to the main contract.[18] Thus it would seem that on the reasoning of Gillard J., the plaintiff in *Leaf's* case may have succeeded in his claim for rescission, if the representation had been a collateral warranty, or else had been incorporated in the main contract as a warranty. If *Leaf's* case and *Mihaljevic's* case are to be consistent, it seems that only when a misrepresentation is incorporated into the main contract as a condition will the representee lose his right to rescind for innocent misrepresentation inducing entry into the contract.

15 [1973] V.R. 545, 561, 562.
16 [1950] 2 K.B. 86.
17 Ibid. 90-91.
18 [1973] V.R. 545, 566-7.

Crockett J. added force to this argument when he said of Lord Denning's opinion[19] "Whatever may be said about that passage, it is in terms limited to the case where the representation becomes a term that is a condition of the contract. That is not this case. The term in the present case is no more than a mere warranty. In such circumstances the position is or may be reversed. The innocent misrepresentation is or may be . . . much more potent than a breach of warranty. There seems to be no reason either in principle or by virtue of what was said by Denning L.J. to conclude that the right to rescind is lost because of the existence of a co-incident but alternative right to claim damages for breach of warranty."

It seems, that, that although the judges in both of the present cases purported to accept the decision in *Leaf's* case, they have limited it to its particular fact situation. The effect of the Victorian approach is to undermine the strictness of the provisions of the Goods Act (1958) regarding acceptance of goods, and the subsequent loss of the right to avoid the contract. That is, if the representee has an election whether to sue for damages for breach of warranty, or for rescission for innocent misrepresentation inducing entry into the contract, he may be in a much better position than if relegated to a claim for damages. This appears to be a real advance on the English law in this regard.[20] However, the effect of these two decisions is far from clear, as both appear to be easily susceptible to being limited to their particular facts. On the other hand, since rescission is a discretionary remedy, the principles enunciated in these two cases could form part of the basis for the development of a logical and just framework of law in this rather nebulous area.

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[19] [1973] V.R. 254, 265-6.
[20] See, for example, *Long* v. *Lloyd* [1958] 1 W.L.R. 753.
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