HARRIS v DIGITAL PULSE: THE AVAILABILITY OF EXEMPLARY DAMAGES IN EQUITY

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The question of whether equity possesses a power to make an award of exemplary damages requires a consideration of the source and purpose of remedies in equity. Stated broadly, the choice is between adherence to equity's traditional refusal to award compensation by way of damages, and a more flexible approach to shaping remedies so as to assuage the consciences of the parties. This choice raises the contentious issue of the degree, if any, to which equity has been or should be influenced by the common law. The highest courts of Canada and New Zealand have both made awards of exemplary damages against defaulting fiduciaries. However, in the recent Harris v Digital Pulse *decision, the New South Wales Court of Appeal held that it had no such power, at least in situations where the parties are subject to a contract of employment. This article analyses the detailed judgments in* Harris v Digital Pulse *and concludes that the dissenting judgment of Mason P, which favoured a flexible and incremental approach to the development of remedies in equity, should be favoured over those of the majority.*

I INTRODUCTION

The recent New South Wales Court of Appeal decision in *Harris v Digital Pulse*[1] appears on its face to do little more than answer a narrow question of remedies. More significantly, however, the case is the site of a showdown between the old-school orthodoxy of the New South Wales equity bar[2] and the more flexible approach of the 'fusion fallacy' heretics. For the moment the old school has won the battle, but the war may be far from over.

By a 2:1 majority,[3] the Court found that there is no power in the law of New South Wales to award exemplary damages for breach of fiduciary duty where the parties are also in a contractual relationship. Heydon JA, in a learned and assertive judgment, thoroughly rejected the findings of Palmer J at trial and denied that equity could ever award the hitherto common law remedy of exemplary damages. That Heydon JA should reach this conclusion is far from surprising as his Honour is one of the standard-bearers of the old school approach. He is a co-author of

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1 (2003) 56 NSWLR 298 ('*Digital Pulse*').

2 Cf ibid 306 (Spigelman CJ).

3 Spigelman CJ and Heydon JA; Mason P dissenting.

the most recent edition of *Meagher, Gummow & Lehane's Equity: Doctrines and Remedies*,[4] the undisputed bible of traditional Australian equity jurisprudence. That work had the following to say about the trial judge's decision in this case:

> Palmer J ('the poor man's Robin Cooke') has disregarded all this learning and principle, and decided that damages [can] be awarded in a claim for equitable compensation ... but one hopes that this is a decision which will never be followed.[5]

The extraordinary reference to Sir Robin Cooke, more recently Lord Cooke of Thorndon, is to a number of decisions of the New Zealand Court of Appeal (of which his Lordship was then President), and in particular to *Day v Mead*[6] and *Aquaculture Corporation v New Zealand Green Mussel Co Ltd*,[7] which essentially came to the same conclusion as Palmer J. The preface to the current edition of *Meagher, Gummow and Lehane* provides the following character assassination of Lord Cooke:

> In New Zealand, the prospect of any principled development of equitable principle seems remote short of a revolution on the Court of Appeal. The blame is largely attributable to Lord Cooke's misguided endeavours. That one man could, in a few years, cause such destruction exposes the fragility of contemporary legal systems and the need for vigilant exposure and rooting out of error.[8]

Any wonder that Mason P, the dissentient in *Digital Pulse*, described the work as containing 'reasons [which] are stated with customary trenchantness, but [which are] marred by an unscholarly descent into personal abuse'.[9] His Honour cannot have been unaware that a co-author of the work he was referring to was sitting two seats to his left on the Court of Appeal bench.[10]

Clearly this is an issue where the passions run high. Rarely, if ever, have judges spoken so bluntly of their disagreement with the conclusions of other judges.[11] There is not a 'with the greatest respect' in sight. What sort of private law dispute could provoke such acrimony and heat?

The purpose of this article is not simply to comment on the decision in *Digital Pulse*. It is also important to bear in mind that the issue central to the case has not been finally decided. Firstly, the narrow approach adopted by Spigelman CJ - to confine his findings to equitable obligations arising in the context of

4 R P Meagher, J D Heydon and M J Leeming, *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies* (4th ed, 2002). Heydon JA referred in his judgment to the third edition of this work, which was authored by Meagher and Gummow JJ and the late Lehane J. Spigelman CJ and Mason P both referred to the fourth edition.

5 Ibid 839.

6 [1987] 2 NZLR 443.

7 [1990] 3 NZLR 299 ('*Aquaculture*').

8 Meagher, Heydon and Leeming, above n 4, xi.

9 (2003) 56 NSWLR 298, 321.

10 In fairness to Mason P, he later paid tribute to '[t]he profound learning in [Heydon JA's] judgment [which] reveals why his Honour will be greatly missed when he leaves this Court to take up office as a Justice of the High Court of Australia': ibid 331.

11 Cf *Liversidge v Anderson* [1942] AC 206, 245 (Lord Atkin).

contractual relations - means that it is not possible to say for certain that exemplary damages are never available in equity. That issue will surely arise at some point in the future. Secondly, there is every chance that the issue will eventually end up with the High Court. This article is written with these possibilities in mind.

II THE FACTS AND FINDINGS AT TRIAL

In April 1998, the first defendant, Mr Harris, signed a contract of employment with the plaintiff, Digital Pulse. At the time, Digital Pulse was a small company providing information technology services. Mr Harris had several years' marketing experience in the industry. The second defendant, Mr Eden, was a web designer who also had considerable industry experience when he was hired by Digital Pulse in October 1999. The contracts of both men contained express terms forbidding them from competing with Digital Pulse during their employment. Their positions of responsibility within Digital Pulse also subjected them to fiduciary duties of loyalty to the company.[12]

By November 1999, both defendants had decided to leave Digital Pulse and to start their own business in competition with it. They called their new business Juice, and it was the third defendant. Juice was incorporated on 27 January 2000 with directors including Harris and Eden. Harris' employment was terminated by Digital Pulse on 4 February 2000; Eden resigned from Digital Pulse on 5 February 2000.[13] The claims in the case concerned their activities in the months after deciding to leave Digital Pulse but before Digital Pulse became aware of this.

From October 1999, Harris and Eden were working for their new company, Juice. Projects that they became aware of at Digital Pulse were diverted to Juice. Clients who came to Digital Pulse with work had that work done by Harris and Eden for the benefit of Juice, which received the payments. Harris and Eden also stole an advertising strategy document that was the confidential information of Digital Pulse, as well as a digital camera and a personal computer.

In all, Digital Pulse claimed in respect of 10 projects, mostly for the development of websites, and for misuse of confidential information.[14] It claimed for damages for breach of the contracts of employment; equitable compensation or an account of profits for breach of fiduciary duty; compensation for breach of statutory duties under the *Corporations Act 2001* (Cth); damages or an account of profits for breach of the misleading and deceptive conduct provisions of the *Fair Trading Act 1987* (NSW) and the *Trade Practices Act 1974* (Cth); damages or an account of profits for breach of copyright; and delivery up of certain business records and equipment. Most significantly, Digital Pulse also sought exemplary damages for breach of fiduciary duty.[15]

12 *Digital Pulse v Harris* (2002) 166 FLR 421, 423.
13 Ibid.
14 Ibid.
15 Ibid 423-4.

Palmer J assessed each of the projects where the defendants were alleged to have diverted work from Digital Pulse. He found that in six cases the defendants had engaged in conduct that was in breach of contract and in breach of fiduciary duty. It was left to Digital Pulse to elect whether it would receive equitable compensation or an account of profits. In addition to this, Palmer J awarded $11,000 for misuse of confidential information and ordered the delivery up of a digital camera and a personal computer. Finally, he awarded $10,000 against each of Harris and Eden by way of exemplary damages for breach of fiduciary duty.[16]

III BASIC PRINCIPLES

Before turning to the findings of the Court of Appeal it is worth setting out, first, some basic principles and, second, the way that this issue has been dealt with in overseas jurisdictions.

A *Exemplary Damages in Tort*

It has long been held in the law of torts that there are circumstances in which a court will consider that awarding compensatory damages to a plaintiff is insufficient to punish the outrageous behaviour of the defendant.[17] This may be particularly so where an award of compensatory damages will prove less costly to the defendant than avoiding the commission of the tort, so that in *Rookes v Barnard,*[18] Lord Devlin stated that '[w]here a defendant with a cynical disregard for a plaintiff's rights has calculated that the money to be made out of his wrongdoing will probably exceed the damages at risk, it is necessary for the law to show that it cannot be broken with impunity'.[19]

In *Uren v John Fairfax & Sons Pty Ltd*, Taylor J said that exemplary damages

> might be awarded if it appeared that, in the commission of the wrong complained of, the conduct of the defendant had been high-handed, insolent, vindictive or malicious or had in some other way exhibited a contumelious disregard of the plaintiff's rights.[20]

In the same case, Windeyer J added that 'exemplary damages must be based upon something more substantial than a jury's mere disapproval of the conduct of a defendant' and that '[t]here must be evidence on which the jury could find that there was, at least, a "conscientious wrong-doing in contumelious disregard of another's rights"',[21] that latter quote citing the speech of Lord Devlin in *Rookes v Barnard*.[22] The element of deterrence was particularly brought out by the High

16 Ibid 449-50.
17 John Fleming, *The Law of Torts* (9th ed, 1998) 271-2.
18 [1964] AC 1129.
19 Ibid 1227.
20 (1966) 117 CLR 118, 129. See also *Australian Consolidated Press Ltd v Uren* (1966) 117 CLR 185, affirmed by the Privy Council: [1969] 1 AC 590.
21 (1966) 117 CLR 118, 153-4.
22 [1964] AC 1129.

Court in *Lamb v Cotogno*[23] in which the Court unanimously found that a defendant may be liable for exemplary damages even when compulsorily insured. The Court held that the deterrence value to others in analogous situations justified an award of exemplary damages.

There are a number of preconditions to the making of an award of exemplary damages. First, the defendant's conduct must be sufficiently reprehensible to justify such an award. Second, the wrong must be of a kind for which exemplary damages can be given. Third, the plaintiff must be the victim of the defendant's reprehensible behaviour. And finally, the damages must otherwise serve the purposes of retribution and deterrence.[24] It is the second of these preconditions that was in issue in *Digital Pulse*.

B *The Nature of Fiduciary Relationships*

A fiduciary relationship is said to exist where one party (the fiduciary) 'undertakes or agrees to act for or on behalf of or in the interests of another person in the exercise of a power or discretion which will affect the interests of that other person in a legal or practical sense'.[25] The celebrated dictum of Fletcher Moulton LJ that the fiduciary principle extends from the trustee to the errand boy[26] may be true, but Australian courts have been careful to limit the categories in which a fiduciary relationship will be found to exist. So while relationships such as trustee and beneficiary, solicitor and client, director and company, agent and principal, and partner and co-partner are undisputedly fiduciary in nature, other relationships are treated with trepidation.

Fiduciaries are under two basic duties. The first is not to allow themselves to be placed in a position of a conflict of interest[27] and the second is not to make unauthorised profits from the fiduciary relationship.[28] For present purposes it is important to recognise the different conceptual foundations of fiduciary relationships on the one hand and contract and tort on the other. It is a failure to understand this basic distinction that frequently forms the basis of criticisms of judgments allowing remedies from one area (for example, tort) to be imposed on another. McLachlin J puts it this way:

> In negligence and contract the parties are taken to be independent and equal actors, concerned primarily with their own self-interest. Consequently, the law seeks a balance between enforcing obligations by awarding compensation when those obligations are breached, and preserving optimum freedom for those involved in the relationship in question. The essence of a fiduciary relationship, by contrast, is that one party exercises power on behalf of another and pledges himself or herself to act in the best interests of the other.[29]

23 (1987) 164 CLR 1.
24 Michael J Tilbury, *Civil Remedies: Volume One, Principles of Civil Remedies* (1990) 258-9.
25 *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41, 96-7 (Mason J).
26 *Re Coomber* [1911] 1 Ch 723, 728-9.
27 *Keech v Sandford* (1726) 25 ER 223.
28 *Boardman v Phipps* [1967] 2 AC 46.
29 *Norberg v Wynrib* [1992] 2 SCR 226, 272.

IV OVERSEAS JURISDICTIONS

A *New Zealand*

The leading New Zealand authority in this area is *Day v Mead*,[30] which concerned a fiduciary relationship and a remedy influenced by a common law doctrine, namely contributory negligence. The plaintiff, acting on advice from his solicitor, the defendant, invested money in a private company which later went into receivership. It turned out that the defendant had numerous conflicts of interest, most significantly in that he was a director of the company in question. The trial judge found for the plaintiff but reduced damages by 50 per cent on the ground that the plaintiff should have sought independent and competent financial advice. The Court of Appeal unanimously dismissed the plaintiff's appeal, with Cooke P saying:

> Whether or not there are reported cases in which compensation for breach of a fiduciary obligation has been assessed on the footing that the plaintiff should accept some share of the responsibility, there appears to be no solid reason for denying jurisdiction to follow that obviously just course, especially now that law and equity have mingled or are interacting. It is an opportunity for equity to show that it has not petrified and to live up to the spirit of its maxims.[31]

Day v Mead was referred to in *Aquaculture*[32] in which the New Zealand Court of Appeal allowed a claim for exemplary damages[33] where the defendant had acted in ruthless disregard of the plaintiff's interests, in a manner known to be illegal but thought to be safe. The Court also overturned the trial judge in allowing a claim for compensatory damages. President Cooke (delivering the judgment of himself and Richardson, Bisson and Hardie Boys JJ) referred to five previous Court of Appeal decisions[34] and concluded that:

> For all purposes now material, equity and common law are mingled or merged. The practicality of the matter is that in the circumstances of the dealings between the parties the law imposes a duty of confidence. For its breach a full range of remedies should be available as appropriate, no matter whether they originated in common law, equity or statute.[35]

30 [1987] 2 NZLR 443.

31 Ibid 451.

32 [1990] 3 NZLR 299.

33 See also *Cook v Evatt (No 2)* [1992] 1 NZLR 676 in which Fisher J awarded $5,000 exemplary damages against a financial adviser who failed to inform a client about a pecuniary interest in an advised investment.

34 *Coleman v Myers* [1977] 2 NZLR 225; *AB Consolidated Ltd v Europe Strength Food Co Pty Ltd* [1978] 2 NZLR 515; *Van Camp Chocolates Ltd v Aulsebrooks Ltd* [1984] 1 NZLR 354; *Day v Mead* [1987] 2 NZLR 443; *A-G(UK) v Wellington Newspapers Ltd* [1988] 1 NZLR 129.

35 *Aquaculture* [1990] 3 NZLR 299, 301. A similar view was taken, in obiter, by Liu JA in the Hong Kong Court of Appeal in *China Light & Power Co Ltd v Ford* [1996] 1 HKLR 57, 65: 'It is clear that our courts have jurisdiction to award damages including exemplary damages in equity. After all, we have fusion of common law and equity in Hong Kong.'

Although the *Aquaculture* case dealt with breach of confidence, it is clear from the President's judgment that the same reasoning would apply to a breach of fiduciary duty.

Somers J delivered a separate judgment in which he agreed with the majority that an award of compensatory damages was available. However, in the absence of previous authority and argument from counsel, his Honour refused to allow the claim for exemplary damages. He stated that '[t]he exclusion of exemplary damages in this case can be justified ... on the ground that equity and penalty are strangers'.[36]

B *Canada*

The Supreme Court of Canada has largely followed the same path as the New Zealand courts. In *Canson Enterprises Ltd v Boughton & Co,*[37] a solicitor failed to disclose to a client purchaser of land a secret profit made by an intermediate vendor. In holding that the solicitor's liability should be limited to the amount of the secret profit plus consequential losses, the Supreme Court held that, although there was no equitable principle to deal with the issue, equity could, and should in this situation, borrow from the common law. After quoting from Cooke P's judgment in *Day v Mead*, La Forest J (with whom Sopinka, Gonthier and Cory JJ concurred) commented:

> I agree with Cooke P that the maxims of equity can be flexibly adapted to serve the ends of justice as perceived in our days. They are not rules that must be rigorously applied but malleable principles intended to serve the ends of fairness and justice ...
>
> Lord Diplock's remark to the effect that the two streams of common law and equity have now mingled and interact are abundantly clear in this area. That is as it should be because in this particular area law and equity have for long been on the same course and whether one follows the way of equity through a flexible use of the relatively undeveloped remedy of compensation, or the common law's more developed approach to damages is of no great moment.[38]

This was not a case where exemplary damages were awarded. In *Norberg v Wynrib,*[39] a case in which a doctor took advantage of a patient's drug addiction to gain sexual favours, McLachlin J (with whom L'Heureux-Dubé J agreed) saw the relationship as one giving rise to a fiduciary duty.[40] Her Honour cited a number of Canadian decisions awarding exemplary damages for breach of fiduciary duty[41] and cited with approval Ellis' statement that

36 *Aquaculture* [1990] 3 NZLR 299, 302.
37 [1991] 3 SCR 534 ('*Canson*').
38 Ibid 585-6.
39 [1992] 2 SCR 226.
40 The other members of the Court held that the fiduciary principle was not applicable. La Forest J (with whom Gonthier and Cory JJ agreed) held that there had been a battery. Sopinka J held that there was a breach of duty actionable in negligence or contract.
41 *W(B) v Mellor* (1989) 16 ACWS (3d) 260; *Szarfer v Chodos* (1986) 54 OR (2d) 663.

> [w]here the actions of the fiduciary are purposefully repugnant to the beneficiary's best interests, punitive damages are a logical award to be made by the Court. This award will be particularly applicable where the impugned activity is motivated by the fiduciary's self-interest.[42]

Her Honour went on to award $25,000 exemplary damages to the plaintiff.

C *United Kingdom*

No UK case has raised the question of exemplary damages in equity. However, the issue was considered by a very influential Law Commission report on aggravated, exemplary and restitutionary damages.[43] The conclusion of the Commission was of statutory intervention to enable the awarding of exemplary damages in equity. It also recommended tightly controlling the circumstances in which any award of exemplary damages could be made. Significantly, the Commission reported that:

> despite the absence of English authorities for awarding exemplary damages for an equitable wrong, we can ultimately see no reason of principle or practicality for excluding equitable wrongs from any rational statutory expansion of the law of exemplary damages. We consider it unsatisfactory to perpetuate the historical divide between common law and equity, unless there is very good reason to do so.[44]

The Commission did not recommend awards of exemplary damages for breach of contract, but where the same conduct would give rise to both a breach of contract and an equitable wrong (such as was the case in *Digital Pulse*), exemplary damages would be available.

At least two other common law jurisdictions have produced law reform commission reports recommending that exemplary damages be available in equity.[45]

V THE COURT OF APPEAL JUDGMENTS

The leading judgment in the Court of Appeal was given by Heydon JA who allowed the appeal and found that the law of New South Wales does not recognise a power to award exemplary damages for equitable wrongs. Spigelman CJ essentially agreed with Heydon JA, although with some significant differences. Most importantly, Spigelman CJ limited the scope of the ruling and only considered contractual relationships which create fiduciary obligations between the parties. He left open the possibility of exemplary damages in other situations

42 Mark Ellis, *Fiduciary Duties in Canada* (1993) 20-32.

43 United Kingdom Law Commission, *Aggravated, Exemplary and Restitutionary Damages*, Report No 247 (1997).

44 Ibid [5.55].

45 Ontario and Ireland. See Ontario Law Reform Commission, *Report on Exemplary Damages* (1991) and Irish Law Reform Commission, *Report on Aggravated, Exemplary and Restitutionary Damages* (Report No 60) (2000) [4.13].

in equity for the reason that '[r]emedial flexibility is a characteristic of equity jurisprudence'.[46] As Mason P found that exemplary damages are available in equity, this narrower finding of Spigelman CJ is the ratio of the case.[47]

The other significant difference between the two leading judgments is more one of emphasis. Spigelman CJ was clearly heavily influenced by the argument that making an award of exemplary damages in equity was something that could not be done below the High Court. While Heydon JA did avert to the possibility of the High Court developing equity to include a remedy of exemplary damages, he gave a number of indications that were he on the High Court (which of course he now is) he would still not be in favour of such a result.

A *Equity and Penalty*

One of the principal arguments made by the defendants was that, as Somers J put it in *Aquaculture*, 'equity and penalty are strangers'.[48] The proposition was not accepted by the trial judge who found that equity's jurisdiction to punish was 'muted for many years but [was] by no means dead'.[49] In support of this view, Palmer J cited a number of sixteenth and seventeenth century cases in which defendants were punished with imprisonment and fines. Even in modern equity jurisprudence the notion of punishment of a deliberate wrongdoer was evident in a number of doctrines. One of these is the rule that the allowance made for the work and skill of a defaulting fiduciary will be more liberal where the fiduciary has not been guilty of misconduct than where they have been.[50] Another is the rule that a fiduciary can never profit without the knowledge of their principal, even if the profit could never have been made by the principal.[51]

Heydon JA refused to accept that equity has punishment as one of its aims. To begin with, there are numerous statements from courts that negate this argument. The UK Court of Appeal in *Vyse v Foster* said '[t]his Court is not a Court of penal jurisdiction. It compels restitution of property unconscientiously withheld; it gives full compensation for any loss or damage through failure of some equitable duty; but it has no power of punishing any one'.[52] Those equitable doctrines which could be classified as involving an element of punishment are in fact properly justified in other ways.

46 *Digital Pulse* (2003) 56 NSWLR 298, 304.

47 There are indications that the ratio of *Digital Pulse* may be being overstated. P W Young, 'Perhaps Equity Is Beyond Childbearing' (2003) 77 *Australian Law Journal* 224 says '[t]he principal point in [*Digital Pulse*] was whether equity could award exemplary damages. The answer, by majority, was "No"'. McClellan J in *Corsecure Pty Ltd v Kaldor* [2003] NSWSC 91, [116] stated that the trial judge had found that exemplary damages were available in equity and that the Court of Appeal had reversed this decision. It is important that necessary attempts to simplify a complex case do not lead to misunderstandings as to the breadth of its ruling.

48 [1990] 3 NZLR 299, 302.

49 *Digital Pulse* (2002) 166 FLR 421, 449.

50 *Boardman v Phipps* [1967] 2 AC 46, 104, 112; *United States Surgical Corporation v Hospital Products International Pty Ltd* [1983] 2 NSWLR 157, 242-3.

51 *Parker v McKenna* (1874) LR 10 Ch App 96, 124 (James LJ).

52 (1872) LR 8 Ch App 309, 333 (James LJ).

The sixteenth and seventeenth century cases in which parties were punished with fines, pillory and imprisonment demonstrate no more than that equity would punish when there was an assault on the nature of the equitable process, such as forgery or perjury. None of the cases punish for a mere breach of an equitable duty.[53] In addition, the clear view of commentators is that the jurisdiction is obsolete and may well have been anomalous even in its day.[54] It is not an appropriate basis on which to develop a power to award exemplary damages.

Heydon JA also found that the rule that a higher rate of interest will be charged on a defaulting fiduciary than on an innocent one is not intended to punish but rather to ensure that the defendant retains no profit from their wrongdoing and to estop the defendant from denying receiving interest at a higher rate than they ought to have received.[55]

A similar rule, that a trustee is entitled to an allowance for his or her work and skill in applying the trust funds to make profit,[56] was also claimed by the plaintiff to have a punitive element in that an innocent trustee is entitled to a more liberal allowance than a trustee who is culpable. The main authority for this proposition is *Boardman v Phipps*.[57] Heydon JA pointed out the authority of that case is lessened by the fact that the parties agreed that a liberal scale should be used and no argument appeared to have been made on the point in the House of Lords.[58] Even so, the rationale behind the provision of liberal allowances to innocent trustees is not to punish guilty trustees but rather to ensure that the plaintiff only receives the profits to which they are entitled. It is a manifestation of the rule that someone 'who seeks equity must do equity'. However, equity cannot encourage wrongdoing and so will award a smaller sum, or indeed no sum, to a trustee who is not innocent.[59]

The plaintiff's third doctrine said to have a punitive element is the account of profits. Heydon JA rejected this view, saying that the true purpose of such a remedy is to prevent the unjust enrichment of the defendant. This explains why a fiduciary must discharge profits even in a situation where those profits could not have been made by the principal.

Finally, Heydon JA pointed out two further considerations. The first is that equity relieves against penalties and the second is that equity has no power to issue an injunction to prevent the commission of a crime. Both of these rules support the view that equity does not punish.[60]

Heydon JA also examined the language that is used to describe equitable obligations. He noted that the words 'penal', 'punitive', 'punish' and 'prophylactic' are in frequent use. None of them, however, can be taken as indicating that equity

53 *Digital Pulse* (2003) 56 NSWLR 298, 412-13.
54 Ibid 411-12.
55 Ibid 365-9.
56 *Brown v Litton* (1711) 24 ER 329.
57 [1967] 2 AC 46.
58 *Digital Pulse* (2003) 56 NSWLR 298, 374.
59 See *Guinness plc v Saunders* [1990] 2 AC 663.
60 *Digital Pulse* (2003) 56 NSWLR 298, 384-5.

imposes penalties on defaulters. Rather, it would appear that the language is frequently misused and should be understood as meaning no more than that equity penalises by deterring certain behaviour.[61]

After examining the same cases as Heydon JA, Mason P, while recognising that 'the caselaw, taken as a whole, reveals that equity does not set out to punish as an end in itself',[62] nonetheless found that

> it remains true, in my opinion, that equity reveals itself readier to select a more stringent remedy if the fiduciary's default is deserving of punishment, for example, because it was deliberate and/or motivated by greed. To invoke the notion of estoppel against such a miscreant, or to withhold an 'exceptional' allowance in respect of skill, expertise or expenses may mask the punitive choice, but cannot disguise it completely. When it strips a miscreant fiduciary of profits, a fortiori when it chooses a harsher alternative remedy, equity readily trumpets its punitive/deterrent intent.[63]

B *Exemplary Damages as a Criminal Sanction*

The one substantive point on which Heydon JA was in minority concerned the classification of exemplary damages as a criminal sanction. Heydon JA relied particularly on the speeches of the members of the House of Lords in *Cassell & Co Ltd v Broome*[64] to classify exemplary damages as a criminal sanction.[65] If that is so, he argued, the plaintiffs could not succeed because it is no longer an acceptable role of the judiciary to create criminal offences.[66]

Both Spigelman CJ[67] and Mason P[68] specifically rejected the classification of exemplary damages as a criminal sanction, with Mason P making the point that the tort cases on exemplary damages have never been understood as importing elements of the criminal law.[69]

C *Fusion of Law and Equity*

Palmer J made it clear in his judgment that there is no need to appeal to any perceived fusion of law and equity in order to find a power in equity to award exemplary damages. Nonetheless, the defendants claimed in the Court of Appeal that Palmer J's finding constituted a 'fusion fallacy', that is, it relied on the incorrect assumption that the passing of the *Judicature Acts*[70] merged not only the administration but also the substantive content of the rules of law and equity.

61 Ibid 406-10.
62 Ibid 331.
63 Ibid.
64 [1972] AC 1027.
65 *Digital Pulse* (2003) 56 NSWLR 298, 386-8.
66 *R v Newland* [1954] 1 QB 158; cf *Shaw v Director of Public Prosecutions* [1962] AC 220.
67 *Digital Pulse* (2003) 56 NSWLR 298, 303.
68 Ibid 322, 341.
69 Ibid 341.
70 *Supreme Court of Judicature Act 1873* (UK); *Supreme Court Act 1970* (NSW); *Judicature Act 1876* (Qld); *Supreme Court Act 1935* (SA); *Supreme Court Civil Procedure Act 1932* (Tas); *Supreme Court Act 1958* (Vic); *Supreme Court Act 1935* (WA).

All three appeal judges were clear that the *Judicature Acts* did not fuse the doctrines of law and equity and that a reliance on such a belief would be erroneous. It was left to Mason P to rebut the defendant's contention that Palmer J's judgment involved a 'fusion fallacy'. This is a charge that has also been levelled at the *Aquaculture* case.[71] Mason P, however, did not consider that either *Aquaculture* or the present case were concerned with the fusion of law and equity. Rather, the cases raised the possibility of the separate branches of law and equity adopting and adapting concepts from each other where appropriate. As Mason P pointed out, not only has this occurred in many situations since the passing of the *Judicature Acts* but indeed happened frequently before it as well. The question then becomes whether it is appropriate for equity to borrow the common law remedy of exemplary damages and use it to remedy breaches of the obligations it imposes.

D *Consistency*

The plaintiff argued that it would be incongruous for a person who has suffered a wrong to be able to claim exemplary damages if they sue in tort but not if they sue for breach of fiduciary duty. The example given by Palmer J was of a client whose money is stolen by a solicitor. If the client sues the solicitor in deceit, he or she may be awarded exemplary damages. It would be anomalous if such an award were not also available if the plaintiff chose to sue for breach of fiduciary duty.

The problem with this argument, as Heydon JA pointed out, is that there is already an anomaly. Digital Pulse succeeded in their claim for breach of contract and for breach of the *Trade Practices Act* but were precluded from claiming exemplary damages in respect of either of those causes of action because of the High Court decisions in *Gray v Motor Accident Commission*[72] and *Marks v GIO Australia Holdings Ltd.*[73] Whether exemplary damages are available in equity or not, there will be anomalies.

In addition, there are significant differences between the doctrines of tort and fiduciary duty. Concepts of breach, causation and remoteness make succeeding in a claim in negligence very different from succeeding in a claim for breach of fiduciary duty.

For these reasons, Heydon JA rejected the utility of any argument based on the need for consistency. Spigelman CJ agreed, saying that '[i]t is not apparent to me that analogical reasoning at this level of generality is appropriate. Each [of contract, tort and equity] is a distinct body of law with its own integrity'.[74] President Mason also acknowledged the potential anomalies but because in his view a fiduciary obligation was more akin to one imposed by the law of tort than it is to a contractual one, he found the consistency argument favoured the availability of exemplary damages in equity.

71 See, eg, Meagher, Heydon and Leeming, above n 4, 79-80.
72 (1998) 196 CLR 1, 6-7.
73 (1998) 196 CLR 494.
74 *Digital Pulse* (2003) 56 NSWLR 298, 308.

E *Novelty*

The plaintiffs argued that whether or not equity previously had a power to award exemplary damages, it should now have such a power on the basis that a full range of remedies should be available to correct breaches of equitable obligations. The view is supported by the New Zealand Court of Appeal in *Aquaculture*, Finn[75] and Sir Anthony Mason.[76] It was not, however, supported by the majority. Heydon JA found that the development of a power to award a new form of remedy in equity was a change in existing law that could not be made by an intermediate court of appeal. His Honour said:

> It is not necessary on this occasion to seek to determine how far this court can change the law. It is sufficient to say that to change the law in favour of the plaintiff here is not a step which should be taken. It would be a radical step. It may affect the operation of legal regimes established by statute.[77]

His Honour went further and stated that, in cases where anything more than a 'non-radical change' in equity is concerned, no development can occur below the High Court.[78] The reason why changes in equity can no longer be made by lower courts is because in the days when such developments occurred,

> the judiciary was small, highly skilled and united. It is now large, less skilled, and far from entirely united. For courts below the High Court to act in the manner of the single judges sitting in Chancery who made modern equity is to invite the spread of a wilderness of single instances, a proliferation of discordant and idiosyncratic opinions, and ultimately an anarchic 'system' operating according to the forms, but not the realities, of law.[79]

Why equity should, in this regard, be different from every other branch of law is not elaborated upon.

President Mason on the other hand was of the view that the development of a power to award exemplary damages in equity was not inappropriate for an intermediate appellate court. There are a number of reasons for this finding. Firstly, it is open for an intermediate appellate court to recognise a novel step in legal development, provided of course that it is not precluded by High Court authority. Secondly, the development of a remedy of exemplary damages is legitimate and has already been accepted at common law. Thirdly, there are no concerns of social or economic policy that would make it undesirable to recognise such a development. Fourthly, the development has been accepted by the highest courts in two other common law countries. Fifthly, there is no conclusive evidence that the remedy was not previously available in equity as the issue had never before been tested. Finally, the issue is one of remedies and not

75 Paul Finn, 'Equitable Doctrine and Discretion and Remedies' in W R Cornish et al (eds), *Restitution, Past Present and Future: Essays in Honour of Gareth Jones* (1998) 255, 271.
76 Sir Anthony Mason, 'The Place of Equity and Equitable Remedies in the Contemporary Common Law World' (1994) 110 *Law Quarterly Review* 238, 244.
77 *Digital Pulse* (2003) 56 NSWLR 298, 415.
78 See Young, above n 47.
79 *Digital Pulse* (2003) 56 NSWLR 298, 419.

rights. The conduct in question has been recognised as a breach of duty for hundreds of years, and the only change is the way the law responds to it.

F *Fiduciary Duties Arising Out of Contractual Relationships*

Spigelman CJ specifically limited his findings to fiduciary duties arising out of contractual relationships. In his Honour's view, if it is appropriate to draw analogies between fiduciary duties and other legal relationships, such analogies should be with contract law not tort. Fiduciary relationships involve satisfying expectations, much as is the case with contracts. His Honour said:

> The fiduciary duties in the present case are derived from the existence of the contract of employment. The 'undertaking or agreement' of the employees to act in the interests of the employer, and the employer's 'entitlement to expect' that that will occur - imputed to the relationship by equity - is much closer to a contractual relationship than it is to circumstances creating obligations in tort. If argument by analogy of this kind is appropriate, I prefer the contract analogy.[80]

Therefore, while essentially agreeing with Heydon JA, Spigelman CJ decided the case on this narrower basis.

VI COMMENTARY

The purpose of this section is not only to provide commentary on the decision of the Court of Appeal but also to consider how the issue may be addressed if it arises in the High Court or in a context different from that of employment contracts. This latter point is significant because the ratio of *Digital Pulse* is narrower than a broad finding that exemplary damages are never available in equity. In a situation where there has been breach of an equitable duty but where there is no corresponding contractual relationship, a court may be understandably influenced by the decision in *Digital Pulse* but is certainly not bound by it. It is also possible that in other states where the *Judicature Acts* were passed significantly earlier than in New South Wales, courts may find that equity has developed further than in that state and may choose not to follow *Digital Pulse* for that reason.

Leaving aside those judges and commentators who would never award exemplary damages for any civil wrong, in almost none of the cases, law reform commission reports and commentaries that address the question of exemplary damages in equity is there any suggestion that such an award would be unjust. The concern of those who agree with the decision in *Digital Pulse* is not that *on those facts* exemplary damages should not be available, but rather that *for that wrong* exemplary damages should not be available. In other words, they would argue that it is beyond the power of equity to make an award of exemplary damages.

There are sound reasons why in some cases an award of exemplary damages is an appropriate remedy against a defaulting fiduciary. Insofar as the merits of the

[80] Ibid 310.

issue take us, I respectfully agree with Palmer J's comment that '[c]onsistency in the law requires that the availability of exemplary damages should be co-extensive with its rationale'.[81] The House of Lords has recently made similar remarks in *Kuddus v Chief Constable of Leicestershire*.[82] While *Kuddus* was a tort and not an equity case, the House recognised as a general proposition that the availability of exemplary damages should not depend on an accident of litigation.

To say that exemplary damages are available against a negligent defendant but not against a dishonest fiduciary, is to draw a distinction that only a lawyer could love. Nonetheless, it is a distinction that many distinguished lawyers have drawn and it is the single greatest weakness of the Canadian and New Zealand decisions that they fail to address this distinction. It is not enough simply to say that exemplary damages *should* be available in equity, a reason must be given also. To do this, it is necessary to explore the nature of compensation in equity and investigate whether it is possible to come up with a justifying principle that can explain *why* equity should be able to award exemplary damages.

A *The Rationales for Awarding Exemplary Damages*

Balkin and Davis have discerned from the case law four rationales for the making of an award of exemplary damages in tort.[83] I propose to consider each of these in turn, applying the rationale to a fiduciary relationship and concluding that there is no reason why any of them should not apply equally to the field of fiduciary obligations.

1 *Deterrence*[84]

The very term 'exemplary' suggests that a major aim of the award is to deter the defendant from acting in the way that it has. It is in the interests of the law to make it plain that it will not tolerate deliberate and high-handed breaches of the duties that it imposes. This is so in tort where 'contumelious disregard' by one party of the rights of the other may be an actionable breach of the duty of care owed by the former to the latter. In negligence, the duty is to 'take reasonable care to avoid acts or omissions which you can reasonably foresee would be likely to injure your neighbour'.[85] In the realm of fiduciaries, the duty is considerably more onerous and the breach of it is more serious. Where negligence approaches the parties as equals and punishes where one has acted unreasonably, equity acknowledges that fiduciaries are in a position of particular strength over their beneficiaries and must maintain a higher standard accordingly. If ever there was a party whose conduct the law most needed to regulate carefully, it is that of a fiduciary, which is why there is a strong deterrent element in the formulation of

[81] *Digital Pulse v Harris* (2002) 166 FLR 421, 448.
[82] [2001] 3 All ER 193 ('*Kuddus*').
[83] Rosalie Balkin and Jim Davis, *Law of Torts* (2nd ed, 1996) 777. The authors cite *XL Petroleum (NSW) Pty Ltd v Caltex Oil (Australia) Pty Ltd* (1985) 155 CLR 448, 471; *Lamb v Cotogno* (1987) 164 CLR 1, 8-9; *Taylor v Beere* [1982] 1 NZLR 81, 89 (Richardson J).
[84] Gareth Jones says that a prophylactic rather than a restitutionary principle underlies fiduciary duties: Gareth Jones, 'Unjust Enrichment and the Fiduciary's Duty of Loyalty' (1968) 84 *Law Quarterly Review* 472.
[85] *Donoghue v Stevenson* [1932] AC 562, 580 (Lord Atkin).

duties imposed on fiduciaries.[86] And where that fiduciary acts deliberately in his or her own interests and not those of the beneficiary, it would seem that there is little reason in logic why a punishment including a sum by way of exemplary damages should not be available. Indeed the argument should be stronger for fiduciaries than for tortfeasors.

2 *Punishment*

Exemplary damages are frequently referred to as 'punitive damages' and the language used to describe acts that will give rise to an award of exemplary damages make it clear that the defendant's conduct is frequently bordering on the criminal.[87] However, in many cases, such as defamation, the criminal law does not offer any effective alternative and a civil award of exemplary damages may be the only realistic way of punishing the defendant. The most important situation in which punishment is required is Lord Devlin's second category of case in *Rookes v Barnard*, that is where the defendant has made a profit from the wrongdoing that exceeds the plaintiff's injury. In this situation, an award of compensatory damages is a wholly inappropriate punishment, indeed it is what the defendant has chosen as a more economic option than avoiding the injury. This argument does not apply with equal force in equity. This is because where a defaulting trustee makes a profit as a result of their breach of an equitable obligation they will always be required to account for that profit to the beneficiary,[88] even if the profit is one the beneficiary could never have made alone and is therefore a windfall.[89] However, where the gain made by the trustee is not of money or its equivalent - for example, a litigation or reputation advantage - there will be no account of profits and an award of exemplary damages will be the only way to stop the defaulting trustee from laughing in the face of the law.

3 *Assuaging feelings of wrongdoing*

This is perhaps the least important of the rationales. It may be that courts list it only as an attempt to justify the windfall that plaintiffs receive as a result of an award of exemplary damages. Nonetheless, there is no reason in common sense why a plaintiff wronged by a negligent neighbour is in any greater need of retribution than the beneficiary wronged by the fiduciary. Indeed, given the relationship of trust that exists in the latter case, parties injured by fiduciary wrongdoing are in a stronger position for demanding retribution than those injured by tortfeasors.

4 *Marking the condemnation of the court*

The efforts of the law to ensure that it will not be used against itself are an important basis for exemplary damages, but they will be undermined if the law

[86] William Gummow, 'Compensation for Breach of Fiduciary Duty' in T G Youdan (ed), *Equity, Fiduciaries and Trusts* (1989) 57, 79-80.

[87] Note, however, that courts will not award exemplary damages where the plaintiff has had a substantial criminal punishment inflicted for substantially the same conduct: *Gray v Motor Accident Commission* (1998) 196 CLR 1. See also *Daniels v Thompson* [1998] 3 NZLR 22.

[88] *Youyang Pty Ltd v Minter Ellison Morris Fletcher* (2003) 196 ALR 482.

[89] *Boardman v Phipps* [1967] 2 AC 46.

draws a distinction, one that makes little sense to most wrongdoers, between equitable wrongs and common law wrongs. Despite their differing historical derivations, equity and common law courts share a need to have the decisions they make enforced and obeyed and if an award of exemplary damages is the only way of achieving this then it must form part of the court's jurisdiction.

John Glover draws a meaningful distinction when he says that '*gains* that fiduciaries make may sometimes have to be accounted for to beneficiaries, even though they are made honestly and not at anyone's expense. Where fiduciaries cause *losses*, the prophylactic counterpart is exemplary damages'.[90] Exemplary damages are a significant head of compensation at common law. They play an important role when a duty imposed by the law is breached high-handedly and without regard to the plaintiff's interests. This situation may also arise in equity and presents itself most starkly in the realm of fiduciary obligations. These relationships require the stronger party to behave in a manner consistent only with the other party's best interests. When a breach of a fiduciary duty occurs that is analogous with a breach of a common law duty that would give rise to an award of exemplary damages, there is no reason why the court should not make an award of exemplary damages. Indeed there are a number of reasons why not doing so may even encourage wrongdoing.

B *Purposes of Remedies in Equity*

How do the above rationales fit in with the aims of equity in fashioning remedies and in particular with the view that 'equity and penalty are strangers'?[91] Firstly, this statement, while sufficient for most purposes, fails to appreciate the complex nature of shaping remedies to do equity between the parties. The general principles of remedies in tort and contract can be easily stated: restoring the plaintiff to her or his original position in the former and putting the plaintiff in the position he or she would have been in but for the breach in the latter. Equitable principles are not so simple, for the same reason that it is beyond dispute that saying what is 'just' and 'equitable' is always more difficult than saying what is legal.

Heydon JA insists that equity never punishes. But as Mason P points out, the rhetoric is not so easily reconciled with the reality. Even leaving aside the sixteenth and seventeenth century cases cited by Palmer J, which are of questionable authority, many of the recent cases can only be analysed by admitting a degree of punishment. The comment of Somers J and its tentative approval by the Full Federal Court in *Bailey v Namol*[92] is an oversimplification of the complex process of doing equity between the parties. Recognising a power to award exemplary damages in equity may be the first explicit acknowledgement of a power to punish, but this does not mean that various equitable doctrines have not been informed by a punitive background.

90 John Glover, *Commercial Equity: Fiduciary Relationships* (1995) 271 (emphasis in original).
91 *Aquaculture* [1990] 3 NZLR 299, 302 (Somers J).
92 (Unreported, Full Court of the Federal Court of Australia, Burchett, Gummow and O'Loughlin JJ, 14 October 1994).

If there are good policy reasons for allowing exemplary damages in equity and no clear reason why they should be dismissed out of a refusal of equity to punish, the next question becomes if and how such an award can be made to fit within the framework of monetary remedies in equity.

C *The Jurisdiction of Equity to Grant Compensation*

Equity has traditionally had a role of providing a remedy to assuage the consciences of the parties.[93] This has involved granting both proprietary and personal remedies. So that in the former category, property wrongly held by the defendant may be subject to an equitable interest in favour of the plaintiff, or tracing may be used to return money to the plaintiff. Equally, there are personal remedies such as rescission and an account of profits. Both proprietary and personal remedies may effectively involve the transfer of money from one party to another. However, equity has long disclaimed any power to award the equivalent of common law damages.[94] Over time, this position was softened by the emergence of a jurisdiction to award monetary compensation in equity's ancillary jurisdiction[95] and by the passing of *Lord Cairns' Act*.[96] The traditional view remains that equity had no power to award damages in its exclusive jurisdiction[97] and that monetary compensation only became recognised as part of the inherent jurisdiction of equity with the case of *Nocton v Lord Ashburton*.[98]

It is crucial here to draw the traditional distinction between damages and equitable compensation. Damages are awarded for a common law wrong and are assessed very differently from equitable compensation which is essentially restitutionary in nature.[99] Meagher, Gummow and Lehane warn that 'it is not correct to speak of "damages" as a single concept which readily in a "reforming" spirit may now be transposed from law into equity; further explanation and analysis will always be necessary if what is intended is to bear any clear meaning'.[100]

The traditional view, therefore, is that the common law award of damages has no parallel in equity because common law damages are fundamentally different from the equitable award of compensation. There are signs that this view is losing its ascendancy.

D *Legal and Equitable Wrongs*

The fusion argument, frequently referred to as the 'fusion fallacy' by its detractors, is said to rest on a belief that the *Judicature Acts* did more than merely

93 Patrick Parkinson, 'The Conscience of Equity' in Patrick Parkinson (ed), *The Principles of Equity* (1996) 28, 28-52.

94 See generally, Ian Davidson, 'The Equitable Remedy of Compensation' (1982) 13 *Melbourne University Law Review* 349.

95 Ibid 349-50.

96 *Chancery Amendment Act 1858*, 21 and 22 Vict, c 27.

97 Meagher, Heydon and Leeming, above n 4, 831.

98 [1914] AC 932. The period directly before this decision has been wistfully referred to by Gummow J as 'the last summer of the old world': Gummow, above n 86, 57.

99 Davidson, above n 94, 350-3.

100 Meagher, Heydon and Leeming, above n 4, 831.

combine the administration of common law and equity. It asserts that as an inevitable result of the *Judicature Acts*, the two streams of equity and law may cross-pollinate. In particular, its adherents would argue that equity may borrow various remedial doctrines from the common law in shaping an equitable solution to a problem. The high-water mark for the fusion argument would have to be Lord Diplock's famous statement 'the waters of the confluent streams of law and equity have surely mingled now'.[101]

Professor Burrows notes that Meagher, Gummow and Lehane are unique, not merely in Australia but in the common law world, for the vehemence of their anti-fusion views.[102] They contend that not only did the passing of the *Judicature Acts* not fuse any substantive concepts of law and equity, but any cross-pollination between the two is highly dangerous and risks the wholesale erosion of established common law or equitable doctrines. For example, actions brought in equity are not subject to the statute of limitations and a mingling of the two streams may see a reduction of the applicability of this legislation.[103] The fusion argument also raises questions of foreseeability, causation and remoteness, issues that have been the subject of much judicial disagreement.[104]

Another significant criticism is the widening of the availability of remedies and uncertainty as to how they will be applied. Are they available as of right, or are they at the court's discretion? If the latter, does this give a court an overly-wide discretion in fashioning an equitable remedy?

Most, if not all, of these concerns can be answered, especially if one favours a gradual merging of various common law and equitable concepts. Equitable wrongs should be subject to the same requirements of foreseeability and causation as common law ones.[105] Burrows has recently set out his blueprint for a merged system of civil wrongs and remedies:

> it is but a small step to a fused, simplified, and improved system in which we stop applying, and talking about, common law and equity and the differences between them. Instead, there would be one underlying concept - a civil wrong; one monetary remedy - call it 'damages'; three measures of damages (compensatory, limited by unified rules of remoteness, causation, contributory negligence and the duty to mitigate; punitive; and restitutionary); awardable with interest including, where full relief demands it, compound, rather than

[101] *United Scientific Holdings Ltd v Burnley Borough Council* [1978] AC 904, 925.

[102] Andrew Burrows, 'We Do This at Common Law and That in Equity' (2002) 22 *Oxford Journal of Legal Studies* 1, 3.

[103] On the other hand, the inapplicability of limitation legislation to equity has been behind some of the novel applications of fiduciary law. This allows plaintiffs whose tort claims are time-barred to succeed in equity. See, eg, *M(K) v M(H)* (1992) 96 DLR (4th) 289; see also the obiter comments of McHugh J in *Bennett v Minister of Community Welfare* (1992) 176 CLR 408, 426-7.

[104] See, eg, the respective views on whether remoteness and intervening cause apply to equitable compensation of Lord Browne-Wilkinson in *Target Holdings Ltd v Redfern* [1996] AC 421 and Millett LJ in *Bristol & West Building Society v Mothew* [1998] Ch 1.

[105] The view of Millett LJ in *Bristol & West Building Society v Mothew* [1998] Ch 1 and of Burrows, above n 102, 12.

> merely simple, interest; available for anticipated as well as accrued wrongs; and subject to a unified range of defences.[106]

There is a growing recognition that civil wrongs should be treated alike. In his book on gain-based damages, Edelman addresses the 'intensely difficult question' of whether a given cause of action is correctly termed a 'wrong'.[107] If a wrong is defined as a breach of duty sounding in compensation and it is correct to speak of 'equitable wrongs' then the only true difference between damages and equitable compensation is the terminology used. Further, he argues that courts are increasingly recognising the need for a common category of wrongs, regardless of whether they derive from equity or common law. He cites *Dubai Aluminium Co Ltd v Salaam*,[108] a case in which the equitable wrong of knowing assistance was found to be a 'wrongful act' within the terms of the *Partnership Act 1890*, as an example of the trend in English decisions towards treating common law and equitable wrongs as being of the same species.[109]

The Canadian and New Zealand decisions cited above are examples of a similar trend that has emerged in those jurisdictions.[110]

E *Development of a Power to Award Exemplary Damages in Equity*

A similar but slightly different argument is that as part of its process of adopting and adapting common law concepts, equity should develop a power to award exemplary damages. Meagher, Gummow and Lehane's view is that this development would be just as dangerous as any attempt to develop a single category of remedies for all wrongs. Other commentators would disagree.

Tilbury argues that 'where piecemeal fusion does take, or has taken, place, it ought not to be rejected out of hand on the basis of a backward-looking argument that such a development would not have been possible before 1875'.[111] He argues that, while the *Judicature Acts* may not have fused law and equity, such fusion is an inevitable result of a world in which their functions are administered by the same courts.[112] Sir Anthony Mason takes a similar view:

> Equity and common law are converging and will continue to converge so that the differences in origin of particular principles should become of decreasing importance. It is inevitable that equitable relief in some of its forms will become available for the protection and enforcement of common law rights to a greater extent than was formerly the case. Likewise, compensatory damages may be granted in appropriate cases for breach of equitable duties and obligations but obviously this will not occur on the footing that there is an

[106] Andrew Burrows, *Fusing Common Law and Equity: Remedies, Restitution and Reform* (2002) 25-6.
[107] James Edelman, *Gain-Based Damages: Contract, Tort, Equity and Intellectual Property* (2002) ch 2.
[108] [1999] 1 Lloyds Rep 415.
[109] Edelman, above n 107, 30-1.
[110] See Julie Maxton, 'Intermingling of Common Law and Equity' in Malcolm Cope (ed), *Equity: Issues and Trends* (1995) 25-45 and Ellis, above n 42, 20-6.
[111] Michael Tilbury, *Civil Remedies: Volume One, Principles of Civil Remedies* (1990) 12.
[112] '[T]he proposition that the Judicature Acts do not *authorize* fusion of principles, cannot lead to the conclusion that such a fusion is *prohibited*': ibid 11 (emphasis in original).

> automatic entitlement to a common law remedy for a breach of equitable duty or obligation or vice versa. It will happen in the course of the law's evolution as it becomes established that, in given circumstances, it is appropriate to grant a particular remedy.[113]

In the course of that passage, Mason addresses one of the questions posed by those sceptical of common law remedies in equity, namely whether certain remedies would be available as of right or would be fashioned by the court to suit the need of the circumstances. On the one hand, remedies will be given in appropriate situations, but on the other, in the same article Mason is careful to limit the untrammelled scope of cross-pollination of remedies. Lord Diplock's 'mingling of the two streams' comment, he argues:

> cannot mean that relief by way of damages, awarded according to common law principles, is available in every case where there is breach or violation of a purely equitable duty or obligation. Nor can it mean that the equitable remedies of specific performance and injunction are more freely available simply because the two bodies of law have, or are thought to have, mingled.[114]

Tilbury and Mason would have no difficulty in accepting that an award of exemplary damages in equity is part of the inevitable development of equity in a world where the same courts and same judges adjudicate on questions of law and equity. Indeed, some would argue that the scope of equitable compensation has already been widened since *Lord Cairns' Act* and *Nocton v Lord Ashburton*. In his book on fiduciary obligations, Finn refers to cases such as *Seager v Copydex Ltd (No 2)*[115] in which courts have awarded monetary compensation for breach of confidence. He rejects the idea that such awards can be justified under *Lord Cairns' Act* or by the general jurisdiction of equity, but continues that:

> if justification be needed for them then, it is suggested, no great violence to principle is wrought if they are regarded as modern developments in the compensatory jurisdiction of Equity which was so forcefully reaffirmed by Viscount Haldane LC in *Nocton v Ashburton*.[116]

Certainly no Australian court would doubt that since *Nocton v Lord Ashburton* equity has possessed a compensatory jurisdiction,[117] but whether that case can be said to mark the beginning of a jurisdiction to award damages and not just compensation is questionable.[118] Sir Anthony Mason seems to suggest that this would have been the path equity would have taken had it not been for the stultifying effects of the boundless expansion of the tort of negligence.[119]

[113] Mason, above n 76, 258.
[114] Ibid 240.
[115] [1969] 1 WLR 809.
[116] Paul Finn, *Fiduciary Obligations* (1977) 167.
[117] Dixon J in *McKenzie v McDonald* [1927] VLR 134, 146 suggested that the Supreme Court of Victoria anticipated the decision in *Nocton v Lord Ashburton* in the case of *Robinson v Abbott* (1893) 20 VLR 346.
[118] Edelman, above n 107, 28-9.
[119] Mason, above n 76, 239.

F *The Inherent Power of Equity to Award Damages*

In an article written following *Aquaculture*, Michalik criticises the reasoning of the New Zealand Court of Appeal in that case.[120] In particular, he argues that the majority judgment went further than necessary in finding that law and equity had for all practical purposes merged. He prefers the judgment of Somers J which comes to the same conclusion on the availability of damages in equity (although dissents on the issue of exemplary damages because of a lack of argument from counsel) without once mentioning the fusion theory.[121]

Michalik is satisfied that there have been sufficient decisions of English courts prior to *Lord Cairns' Act* in which compensation has been awarded to justify the conclusion that such an award is inherent in equity's jurisdiction. In addition, '[i]t cannot be thought that in the old days of petitions to the Chancellor, that worthy gentleman would have stopped short of ever awarding a sum of money directly as compensation'.[122]

This is also the conclusion of Palmer J in *Digital Pulse* who relied on a series of cases allowing damages in equity to justify a finding that an award of exemplary damages is within equity's inherent jurisdiction. It is worth setting out his final conclusion on this critical question:

> There is no need to appeal to any perceived fusion between the principles of equity and those of the common law in order to invest the equity court with jurisdiction to award exemplary damages. Such jurisdiction is already inherent in the court. It is, and always has been, a court of conscience; at least until the early seventeenth century, it frequently inflicted punishments in aid of its ordinary and traditional jurisdiction. Since then the exercise of the jurisdiction to punish has been muted, manifesting itself in the manner in which dishonest fiduciaries, as distinct from honest fiduciaries, will be called to account for profits and in the higher rate of interest imposed upon dishonest defaulting trustees, as distinct from honest defaulting trustees. The jurisdiction of the equity court to punish and deter may have been muted for many years but it is by no means dead.[123]

Although this view was unanimously rejected by the Court of Appeal, it has strong academic backing. In his article, 'Jurisdiction of the Court of Chancery to Award Damages', McDermott traces the historical power of equity to award compensation from medieval times right up to the enactment of the *Judicature Acts* and concludes 'prior to the enactment of Lord Cairns' Act the Court of Chancery exercised jurisdiction to award damages in a number of isolated instances ... it was not a jurisdiction that it would generally exercise'.[124] This is

[120] Paul Michalik, 'The Availability of Compensatory and Exemplary Damages in Equity: A Note on the *Aquaculture* Decision' (1991) 21 *Victoria University of Wellington Law Review* 391.
[121] Ibid 400-1.
[122] Ibid 406.
[123] *Digital Pulse v Harris* (2002) 166 FLR 421, 449.
[124] Peter McDermott, 'Jurisdiction of the Court of Chancery to Award Damages' (1992) 108 *Law Quarterly Review* 652, 672.

also the view of Spry who, in refuting the traditional assumption, said that '[t]he better view is that courts of equity have always had it within their power to award damages but that from a very early time they considered it to be ordinarily undesirable to do so'.[125]

G *The Preferred Basis*

In the previous three sections I have set out three possible bases for justifying an award of exemplary damages in equity. Firstly, there is the view that the law is developing a single category of civil wrongs, whether they arise in equity or at common law, with remedies that apply to all of them. If an award of exemplary damages is available for breach of a common law duty then a parallel power must exist in equity, whether couched in terms of damages or compensation.

Secondly, exemplary damages may be a recent development in equity, part of the inevitable mingling of law and equity that has occurred since (and indeed prior to) the passing of the *Judicature Acts*. This view is essentially that of Mason P.

Finally, a power to award exemplary damages in equity may be an inherent one. This is the view of Palmer J at first instance in *Digital Pulse v Harris*, who found the power to be muted but not dead.

In many ways, the first basis is a broader and more highly-progressed version of the second. For this reason, it is unlikely to find favour with a court that can decide this issue on the narrower grounds of the second basis. This is an area where caution and incremental steps are needed and so advocating a single category of civil wrongs - while probably a sensible end-point[126] - does not accurately reflect the current law.

Of the second and third bases, it is tempting to say that in a legal system that favours experience over logic[127] an argument based on precedent will find more favour than one based on novelty. However, given Heydon JA's thorough and learned rejection of the case law relied on by Palmer J, it is probably unlikely that a future Australian court would be receptive to this third basis.

This leaves just the second basis, that is that the law has developed - or alternatively should develop - to the point of recognising a new (or at least never-before exercised) power to award a monetary amount equivalent to common law exemplary damages for breach of equitable duties. This is in line with various law reform commission reports and, if the development is to occur in a principled manner, causes no great harm to existing doctrines or violation of precedent. For this reason, I would conclude that the judgment of Mason P is to be preferred to those of Spigelman CJ, Heydon JA and Palmer J.

[125] I Spry, *The Principles of Equitable Remedies: Specific Performance, Injunctions, Rectification and Equitable Damages* (4th ed, 1990) 608.
[126] See Burrows, above n 102.
[127] Cf Oliver Wendell Holmes, *The Common Law* (first published 1881, 1945 ed) 1.

VII CONCLUSION

The decision in *Digital Pulse* raises an issue which is as important as it is divisive. There is every reason to expect that it will arise again. Should the issue of the availability of exemplary damages in equity arise in the High Court, the battle between the traditionalists and the fusion fallacists will undoubtedly be heated. We know that the High Court is wary of mixing various branches of law in the field of remedies. It has refused to award either exemplary damages[128] or contributory negligence[129] for breach of contract. We also know that two current High Court judges, through their various writings, have shown themselves to be antipathetic to the availability of exemplary damages in equity.[130] Nonetheless, the issue has not been fully resolved and in this article I have attempted to suggest the questions that may arise and ways in which arguments may be advanced in a future case.

The issue of awarding exemplary damages for breach of fiduciary duty is not about the fusion of law and equity. Rather, it is an admission that, as Sir Anthony Mason puts it, '[t]he traditional principles of equity are not so invincibly superior to the concepts of the common law that equity cannot occasionally profit from common law ideas'.[131] It would be completely erroneous to suggest that the principled recognition of a power to award exemplary damages in equity's inherent jurisdiction would open the floodgates to the erosion of long-standing and important common law and equity doctrines.

Moreover, there are circumstances in which an award of exemplary damages in equity will be appropriate and other remedies will not suffice. *Digital Pulse* is such a case. Messrs Harris and Eden should consider themselves fortunate that what they did happened to constitute an equitable wrong and not a tort, although one suspects that this distinction did not cross their minds when they decided to rip off their employer.

For the moment the equity traditionalists have scored a significant victory. It seems unlikely that any court below the High Court would fail to follow both the obiter dictum and the ratio of a judgment authored by such a learned equity judge as Heydon JA. But the underlying premise of the 'fusion fallacists' is that the intermingling of law and equity is a slow and gradual process. It may be that in this area Australia (or at very least New South Wales) is just a few decades behind Canada and New Zealand. Time will tell and the only certainty is that more strong words will be had.

[128] *Gray v Motor Accident Commission* (1998) 196 CLR 1.
[129] *Astley v Austrust Ltd* (1999) 197 CLR 1.
[130] Gummow J, in *Bailey v Namol* (Unreported, Full Court of the Federal Court of Australia, Burchett, Gummow and O'Loughlin JJ, 14 October 1994), above n 97 and accompanying text and as a co-author of the first three editions of *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies;* Heydon J, in *Digital Pulse* and as a co-author of the fourth edition of *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies.*
[131] Mason, above n 76, 243.