

“the proper measure of damages in the first instance is the difference between the true value of what was acquired at the date of purchase and the price paid.”

# Assessing damages

## under the *Trade Practices Act*

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### General Principals

Section 82 of the *Trade Practices Act* allows recovery of damages caused by, amongst other things, a contravention of section 52 which prohibits misleading and deceptive conduct by corporations and individuals in trade or commerce. Section 87 also allows for recovery of damages, but confers a more discretionary power upon the court to make other orders. Neither section 82 nor section 87 prescribes the measure of damages to be used.

The courts have been reluctant to set out hard and fast principals for the assessment of damages, emphasising that general principals must give way in particular cases to solutions best adapted to give the plaintiff an amount in damages which will most fairly compensate for the wrong suffered: *Collings Construction Co Pty Ltd v CCC* (1998) 152 ALR 510.

The general principal applied by the courts can best be summarised by reference to the decision in *Kenny & Goode Pty Ltd v MGICA* (1992) Ltd (1997) 77 FCR 307 at 330,

“...the purchaser is entitled to recover as damages, a sum representing the preju-

*dice or disadvantage s/he has suffered in consequence of altering her/his position under the inducement of the respondent's misrepresentation”*

This principal has been highlighted in a recent decision of the High Court in *Marks v GIO Australia Holdings Ltd* (1998) 73 ALJR 12 at page 21,

“...a comparison must be made between the position in which the party that allegedly has suffered loss or damage is in and the position in which that party would have been in but for the contravening conduct”.

Their Honours in that decision considered how it may be determined whether or not a loss has been suffered:

“How was value to be assessed? It is to be assessed objectively, not according to what either or both of the parties to the contract believe that it would obtain from the contract. That is, the value of what in fact was acquired is to be identified according to what price freely contracting, fully informed parties would have offered and accepted for it.”

Their Honours gave an example of a person agreeing to pay \$50,000 for goods which the vendor falsely represented were worth \$100,000 but which are in fact worth \$50,000. Their Honours posed the question as to what

loss the purchaser has suffered. Their Honours then observed that if viewed objectively, a person obtained rights having a value at least equal to what they paid for, no loss has been suffered and continued:

*"It is only if some alternative (less detrimental or more beneficial) were available, that it can be said that the contract which was made was less valuable to the party that was misled than had been represented - for it is only then that a comparison of value can be made."*

Accordingly, the prima facie measure of damage will be the difference between the true value of what was acquired at the date of purchase and the price paid.

### Heads of Loss and Damage

Having regard to the detailed discussion below, the following heads of claim which we as Forensic Accountants generally assist in quantifying, may form part of a total claim for damages in a dispute under the *Trade Practices Act*.

- Difference between price paid and true value
- Subsequent trading losses
- Borrowing costs
- Opportunity loss

### Difference between price paid and true value

It is accepted that the proper measure of damages in the first instance is the difference between the true value of what was acquired at the date of purchase and the price paid.

This proper measure of damages is described in *Munchies Management v Belperio* (1988) 84 ALR 700 at 706,

*"..where a purchaser has laid out money on the acquisition of a business, the usual course taken, in the purchaser's case, is to tender evidence of the worth of the business as a going concern and to contrast this with what was paid to the vendor"*.

In *Gould v Vaggelas* (1984) 157 CLR 215 at 220, Gibbs CJ proceeded on the footing that the first step in the assessment of damages would be a valuation. His Honour said:

*"..it is well established that the measure of damages in an action of deceit for inducement to enter into a contract of purchase was usually the difference between the real*

*value of the property at the time of purchase and what the purchaser paid for it."*

It is therefore necessary to tender evidence as to the true value of what was acquired. In determining this value, it is possible to consider events subsequent to purchase not only to prove that a representation was false but also to prove the true value of the business at the date of purchase. For instance it is appropriate to look at facts such as the subsequent sale price of the business (or that it was unable to be sold) and the takings of the business after settlement for the purpose of determining its value at the time of settlement.

In *Kizbeau v WG & B Pty Ltd* (1995) 184 CLR 281 at 291 the High Court said:

*"..Thus the takings of the business subsequent to purchase are generally admissible, not only to prove that a representation concerning the takings was false, but also to prove the true value of the business at the date of purchase, even when some difference exists under which the business was conducted before and after purchase, evidence of subsequent takings may be admissible, subject to due allowance being made for any differences in relevant conditions."*

The High Court went on to say:

*"..but if it is established that the decline in takings has been caused by business ineptitude or unexpected competition, evidence of subsequent takings is not admissible to prove the value of the business as at that date, rather, events such as ineptitude and unexpected competition being regarded as supervening events."*

Consistent with the view of the High Court in *Marks*, the purchaser cannot recover the entire price paid unless the asset purchase proves to be entirely worthless. Therefore a valuation of what was purchased, at the date of purchase (having regard to appropriate subsequent events) is the first step in the assessment of damages.

### Subsequent Trading Losses

Consistent with what was said in *Kizbeau*, additional losses incurred by the purchaser in connection with the business may be included in the damages if the court is satisfied that those trading losses flowed directly from the representation: *Gould v Vaggelas* (1984) 157 CLR 215 at 223.

This matter is put clearly in *Nataf v Bikane* (1990) 92 ALR 490 at 494:-

*"We reiterate that, where a purchase has been induced by misleading conduct, it is not enough in order to recover losses subsequent to the purchase, to prove that but for the misleading conduct or as a partial consequence of it, the agreement to purchase would not have been made; that is so in every successful application of that kind. It is not the law that in every case the party held to have been engaged in misleading conduct (who may have acted quite innocently) becomes the insurer of the others' success and prima facie liable to indemnify her/him against the consequences of the purchase."*

It is necessary therefore not only to establish that subsequent trading losses were incurred, but that such trading losses were the product of the misrepresentation.

In *Gould v Vaggelas* (1984) 157 CLR this basis for recovery was explained as follows:-

*"If the purchaser, besides paying more for the business than it was worth, has suffered additional losses which resulted directly from the fraud, s/he ought to be compensated for them. Of course, the court must be satisfied that the loss did result directly from the fraud and not from some supervening cause such as folly, error or misfortune of the purchaser her/himself..."*

One factor that does affect the recoverability of subsequent losses relates to the duty to mitigate loss. Referring to *Brown v Jam Factory Pty Ltd* (1981) 35 ALR 79; 53 FLR 340 at 351, the Full Court in *Munchies* said:

*"..it has been accepted that an applicant under s 82 has an obligation to take reasonable steps to mitigate him/her consequent upon the respondents conduct."*

The proposition is that the ordinary duty to mitigate loss applies and regard may not be had to subsequent non profitable trading of the business while owned by the plaintiff beyond the point of which, being aware or when the purchaser ought reasonably have been aware, of the causes of action to it, it should have taken appropriate action to pursue its claims: *Gould v Vaggelas* at 246.

The proper course in such a case is not to continue to trade and incur a loss: ►



*Burns v M.A.N. Automotive (Aust) Pty Ltd* (1986) 161 CLR 653.

This issue was also considered in *Corbidge v Bakery Fun Factory Fun Shop Pty Ltd* (1984) ATPR 40-493 where it was said:

"...in approaching the question of damages in a Trade Practices Act case where a purchaser has been misled as to the takings or profits of a business but has not sought to avoid the contract, the main question to be decided is whether, had the true fact been known, the purchaser would have been content to buy at a lower price or would not have bought at all. In the first case, it may well be that the only damage the purchaser will have suffered is the immediate damage of the difference between the price paid and the true value. In the second case, the purchaser will also be entitled, provided damages are mitigated where possible, to any losses consequential upon the running of an unprofitable business."

In *Gould v Vaggelas* (1984) 157 CLR 215 at 221-2 the court in considering the issue of subsequent losses and mitigation in general said:

"...there may be cases in which the purchaser continues to trade, either because s/he has no real alternative or because s/he has not become aware of the nature of the fraud and in those circumstances incurs losses which are not represented by the difference between the price and value of the business. There is no reason in principle the defrauded purchaser should not recover damages for all the loss that flowed directly from the fraudulent inducement (unless, possibly, the loss was not foreseeable)."

Whether or not the purchaser takes reasonable steps to mitigate her/his loss and that includes the seeking of a rescission of the contract, does affect the recoverability of subsequent losses and the facts of each case need careful consideration when structuring a claim under this head of damage.

It is advisable to examine in detail individual profit and loss items that contribute to subsequent trading losses and be sure that the claim contains only those items which were incurred as a direct result of the contravening act. Items such as private motor vehicle costs, excess depreciation, owners remuneration and interest (discussed

separately below) may well give rise to a need for an adjustment to reported trading losses in order to properly quantify the claim under this head.

### **Borrowing Costs**

Whether borrowing costs are recoverable depends on the facts of each particular case.

In *Munchies Management v Belperio* (1988) 84 ALR 700 at 716 the Full Court agreed with the trial Judge's decision in that a claim for interest could not be sustained. The Full Court said:

"It is apparent that the purchasers made a decision to borrow a very high proportion of the purchase price in the knowledge that even if the representations as to the turnover of the business, upon which they relied, had been made good, the prospective profits of the business would have been insufficient to service the purchaser's borrowings. The interest charges were a cost that the purchases were prepared to bear and were not an item of loss suffered by reason of or as a result of the falsity of the representations."

In *Yorke v Ross Lucas Pty Ltd* (1982) 69 FLR 116, the plaintiff was not permitted to recover the cost of financing its borrowings because the borrowing costs were not considered to be a direct consequence of the purchase of the business, but the result of the plaintiff's decision to finance the purchase in a particular way.

In the following cases however, the cost of borrowings were recovered, as it was determined that the cost was incurred as a direct consequence of the negligent or deceptive conduct. *Sanrod Pty Ltd v Dainford* (1984) 54 ALR 179 at 191; *Hungerfords v Walker* (1989) 171 CLR 125; *Di Beratino v GTF Partners* (unreported, McDonald Jeremiah, Victoria Supreme Court, 10 August 1998).

Due consideration should be given to the facts of the case as to whether borrowing costs should be included in the claim. As borrowing costs are usually included in the claim for trading losses subsequent to the acquisition, an adjustment may need to be made to trading losses to the extent that borrowing costs or a portion of them should or should not be included.

### **Opportunity Loss**

It is often argued that had the purchaser known the true facts it would not have entered into the contract and that such monies used would have been applied in a different manner resulting in profit.

This principle is clear in *Corbidge v Bakery Fun Factory Fun Shop Pty Ltd* (1984) ATPR 40-493 which said:

"...loss of earnings from an alternative profitable business which the purchaser can show would have been carried on if the deception had not occurred are also .....sufficiently direct to justify additional damages."

Similarly, in *Gates v City Mutual Life Assurance Society Ltd* (1986) 160 CLR 1, the High Court stated:

"...because the object of damages in tort is to place the plaintiff in the position in which s/he would have been in but for the commission of the tort, it is necessary to determine what the plaintiff would have done had s/he not relied upon the representation. If that reliance has deprived her/him of the opportunity of entering into a different contract for the purchase of goods on which s/he would have made a profit then s/he may recover the profit on the footing that it is part of the loss s/he has suffered in consequence of altering her/his position under the inducement of the representation. This may well be so if the plaintiff can establish that s/he could and would have entered into the different contract and that it would have yielded the benefit claimed. The lost benefit is referable to opportunities foregone by reason of reliance on the representation."

Any claim therefore under this head should be properly evidenced and carefully submitted if it is to have any chance of success.

### **Final Comment**

In any claim for damages it is essential to allow sufficient time for the proper investigation and determination of the composition of the heads of claim. Too often the issue of liability takes preference over damages resulting in an inadequate consideration of both the proper heads of damage and quantum. This often leaves the Courts in a difficult position of having to decide on quantum with limited and often inappropriate quantum claims. **PL**