IN THE SUPREME COURT OF NEW ZEALAND

SC 5/2013
[2013] NZSC 147

BETWEEN	PLANET KIDS LIMITED Appellant
AND	AUCKLAND COUNCIL Respondent

Hearing:	27 June 2013
Court:	Elias CJ, McGrath, William Young, Glazebrook and Gault JJ
Counsel:	G P Blanchard and J P Nolen for the Appellant J A Farmer QC and L A O'Gorman for the Respondent
Judgment:	17 December 2013

JUDGMENT OF THE COURT

A. The appeal is allowed. A declaration is made that the settlement agreement subsists.

B. The other orders sought by the appellant in its application for summary judgment are not made but the matter is referred back to the High Court to deal with the remainder of the application.

C. The respondent is to pay to the appellant costs of $25,000 plus all reasonable disbursements to be fixed if necessary by the Registrar. We certify for two counsel.

REASONS

ELIAS CJ

[1] Planet Kids Limited operated a childcare business on land leased from the Auckland Council. The Council gave notice of intention to acquire the leasehold interest under the provisions of the Public Works Act 1981 because the land was required for roading purposes. Planet Kids objected to the proposed taking. Eventually the parties concluded a settlement agreement on 3 June 2010.

[2] Under the settlement agreement, Planet Kids (which was accepted to be unable to relocate) was to receive compensation from the Council for the loss of goodwill arising from the closure of its business. In addition, the Council agreed to forgo a disputed claim for rent said to be due under the lease. In return, the Council was to receive a surrender of lease and vacant possession, a restraint of trade covenant from Planet Kids, and the chattels and plant on the premises. A deposit of 10 per cent of the compensation was paid by the Council with the balance to be paid on settlement, which was set for 20 December 2010, or earlier should the parties agree. By cl 8 of the settlement agreement it was agreed that the "[b]usiness shall remain at the sole risk of [Planet Kids] until the settlement date". Clause 9 affirmed that the Council was not purchasing Planet Kids' business but was instead merely compensating Planet Kids for the closure of the business as if the business had been sold as a going concern and that Planet Kids remained liable for any obligations connected to the business. Finally, the settlement agreement meant that the Council could tender for the road works before settlement and gave the Council and its agents the ability to enter upon the land, on 48 hours notice, for preliminary purposes associated with the roading project.

[3] In early August, Planet Kids gave notice to its staff that the business would be closing. In September parents were advised that the business would close so that they could make other child care arrangements. A tender for the road works was awarded by the Council on 1 October 2010. On 2 October the building was destroyed by fire. It is not in dispute that the effect of cl 40.1 of

the lease was that the lease terminated with immediate effect as a result of the destruction caused by the fire.

[4] The Council took the view that the settlement agreement had been brought to an end by frustration as a result of the termination of the lease and refused to pay the balance owing under the settlement agreement. Planet Kids then issued proceedings seeking judgment for the balance and made application for summary judgment. The Council applied to strike out Planet Kids' claim and, in the alternative, itself sought summary judgment on its defence that the agreement was frustrated by the termination of the plaintiff's lease and that it was not obliged to pay the sum claimed by Planet Kids.

[5] In the High Court, Peters J accepted the Council's submission that the basis on which the settlement agreement was entered into was that Planet Kids was able to transfer a leasehold interest in the land at the date of settlement.[1] Since this was impossible following termination of the lease following the fire, she held that the agreement was frustrated.[2] Although Planet Kids' application for summary judgment was declined, Peters J did not strike out its claim or enter summary judgment for the Council, pending further submissions on the effect of the Frustrated Contracts Act 1944.[3] Planet Kids appealed to the Court of Appeal, overtaking the need for further submissions in the High Court because the additional matter of the effect of the Frustrated Contracts Act was dealt with in the judgment of the Court of Appeal.

[6] The Court of Appeal agreed with the determination in the High Court that the termination of the lease had frustrated the contract.[4] Since Planet Kids no longer possessed a leasehold interest, following termination of the lease as a result of the fire, the settlement agreement was held to be "wholly or radically different from that which the parties had agreed".[5] The Court of Appeal considered that the overlay of the Public Works Act was important background since it took the view that the

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1 *Planet Kids Ltd v Auckland Council* HC Auckland CIV-2011-404-1741, 16 December 2011.
2 At [30].
3 At [35].
4 *Planet Kids Ltd v Auckland Council* [2012] NZCA 562, [2013] 1 NZLR 485 (O'Regan P, Arnold and Ellen France JJ).
5 At [54].

Council had "entered into the contract in the exercise of its powers under the Act".[6] Any basis of settlement for the claim under the Act was removed when the lease terminated.

[7] Planet Kids appeals with leave to this Court.[7] The question for determination on the appeal is whether the Courts below were correct to hold that the settlement agreement was discharged by frustration.

Frustration

[8] Discharge by frustration turns on the construction of the contract in context.[8] It is recognised that, without such discharge, injustice can result from the enforcement of a contract following significant change of circumstances which renders performance radically different from that reasonably contemplated by the parties at the time it was entered into.[9] Frustration is a tool that is "modern and flexible and is not subject to being constricted by an arbitrary formula".[10] The need for application which is contextual and flexible has been emphasised by Rix LJ in describing an approach which is "multi-factorial":[11]

> Among the factors which have to be considered are the terms of the contract itself, its matrix or context, the parties' knowledge, expectations, assumptions and contemplations, in particular as to risk, as at the time of contract, at any rate so far as these can be ascribed mutually and objectively, and then the nature of the supervening event, and the parties' reasonable and objectively ascertainable calculations as to the possibilities of future performance in the new circumstances. Since the subject matter of the doctrine of frustration is contract, and contracts are about the allocation of risk, and since the allocation and assumption of risk is not simply a matter of express or implied provision but may also depend on less easily defined matters such as "the contemplation of the parties", the application of the doctrine can often

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6 At [56].

7 *Planet Kids Ltd v Auckland Council* [2013] NZSC 36.

8 *Davis Contractors Ltd v Fareham Urban District Council* [1956] AC 696 (HL) at 720–721. The doctrine asks "whether the contract … is, on its true construction, wide enough to apply to the new situation: if it is not, then it is at an end": at 721.

9 At 729. See also *National Carriers Ltd v Panalpina (Northern) Ltd* [1981] AC 675 (HL) at 700 and *J Lauritzen AS v Wijsmuller BV (The Super Servant Two)* [1990] 1 Lloyd's Rep 1 (CA) at 8.

10 *Cricklewood Property and Investment Trust Ltd v Leightons Investment Trust Ltd* [1945] AC 221 (HL) at 241.

11 *Edwinton Commercial Corp v Tsavliris Russ (Worldwide Salvage and Towage) Ltd (The Sea Angel)* [2007] EWCA Civ 547, [2007] 2 Lloyd's Rep 517 at [111].

> be a difficult one. In such circumstances, the test of "radically different" is important: it tells us that the doctrine is not to be lightly invoked; that mere incidence of expense or delay or onerousness is not sufficient, and that there has to be as it were a breach in identity between the contract as provided for and contemplated and its performance in the new circumstances.

[9] Since the effect of frustration is "to kill the contract and discharge the parties from further liability under it",[12] it is the common object of the contract that must be frustrated "not merely the individual advantage which one party or the other might have gained from the contract".[13] Frustration is "a common relief from this common disappointment".[14] Performance must be "radically different" such that there is "a break in identity between the contract as provided for and contemplated and its performance in the new circumstances".[15] If non-trivial achievement of part of the contractual purpose is still possible, the contract is not frustrated.[16] The need to remedy injustice to the parties is the ultimate measure in assessing frustration.[17]

Was the settlement agreement frustrated as a result of the fire?

[10] Following the destruction of the building, Planet Kids could not meet its obligations to transfer chattels to the Council and provide a formal surrender of the lease. The chattels had been destroyed and the interest of Planet Kids in the leasehold had terminated on destruction of the premises under cl 40.1 of the lease so that it was no longer in a position to tender a formal surrender of lease.

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12 *The Super Servant Two*, above n 9, at 8, adopted in New Zealand in *Karelrybflot AO v Udovenko* [2000] 2 NZLR 24 (CA) at [37]–[38]. See also *Davis Contractors Ltd v Fareham Urban District Council*, above n 8, at 727.

13 *Hirji Mulji v Cheong Yue Steamship Company Ltd* [1926] AC 497 at 507. See also *Occidental Worldwide Investment Corp v SKIBS A/S Avanti (The Siboen and the Sibotre)* [1976] 1 Lloyd's Rep 293 (QB) at 326 which held that both parties must regard the condition or event in question as the foundation of the contract in order for it to found a claim of frustration.

14 At 507.

15 *The Sea Angel*, above n 11, at [111].

16 GH Treitel *Frustration and Force Majeure* (2nd ed, Sweet & Maxwell, London, 2004) at 324. Treitel illustrates the point by reference to *Herne Bay Stream Boat Co v Hutton* [1903] 2 KB 683 (CA), where a contract to hire a steam boat to view the royal review of the naval fleet at Spithead as part of the celebrations for the coronation of Edward VII was not frustrated by cancellation of the review on the King's illness because the fleet was still at Spithead to be viewed. By contrast, in *Krell v Henry* [1903] 2 KB 740 (CA), a contract to rent rooms from which the coronation processions were to be viewed was frustrated when the processions were cancelled on the days the rooms were taken for because the contract was "a licence to use rooms for a particular purpose and no other".

17 *The Sea Angel*, above n 11, at [112].

Does the impossibility of performance by Planet Kids in these respects frustrate the settlement agreement?

[11] The settlement agreement was a compromise to resolve the dispute between the parties arising from the Public Works Act notification and subsequent objection. The formal surrender of the lease by Planet Kids was not itself important in achieving this purpose so long as the Council obtained vacant possession, certainty of outcome and access in the interim to enable it to advance the roading construction. Indeed, since the Council was itself the landlord it did not require formal surrender of the lease from Planet Kids because the freehold and the leasehold estates merged. The Council was able to compel vacant possession under the terms of the settlement agreement and was also in a position to obtain performance of the restraint of trade agreement. Entering into the settlement agreement gave the Council the certainty it needed to let the contracts for the construction of the road and it obtained pre-settlement access to the property, which it needed to enable the construction arrangements to be put in place to meet its preferred time-frame. These were matters of considerable importance to it. For its part, Planet Kids closed its business against the promise of payment of compensation. The settlement agreement also resolved the outstanding rent dispute and ended any prospects of future litigation in that respect.

[12] I agree with the suggestion made by William Young J that it may be a useful check to consider whether on the facts the Council would have been entitled to cancel the contract under s 7(4) of the Contractual Remedies Act 1979 for non-performance.[18] Cancellation would not have been available to the Council unless the terms Planet Kids is unable to perform were agreed by the parties to be essential to them or unless their non-performance substantially changed the benefit or burden of the contract to the Council. If not, the impossibility of performance of these terms can hardly be said to have been "radically different" from the bargain made and productive of injustice. The terms Planet Kids is unable to perform were clearly not of that quality. The formal surrender of the lease was irrelevant: the purpose of the Council in

[18] At [175] below.

bringing the lease to an end, securing vacant possession and resolving the Public Works Act dispute was achieved by the settlement agreement. No value was assigned in the contract to the surrender of the lease. The chattels appear to have been a matter of indifference to the Council and it is not suggested that failing to obtain them substantially altered the benefit of the contract to it or was agreed to be essential. To the extent that performance of these obligations had value, adjustment through remedy under the Contractual Remedies Act is still available to the Council.

[13] More directly, the obligations that Planet Kids is unable to perform cannot be said to make performance of the contract "radically different" from that contemplated so that it is just to kill the contract and discharge the parties from a common disappointment. All the important benefits sought by the Council – closure of the business, discharge of the lease, vacant possession, the ability to meet its own timeframes in constructing the road – were obtained by it. Planet Kids went out of business on the Council's agreement to pay it compensation in order to release the premises. It gave access to the premises while it was winding its activities down. The formal documents of surrender of the lease were unnecessary to achieve its determination. The main purposes of the settlement agreement were able to be performed. Any loss of value to the Council from the inability of Planet Kids to perform strictly in accordance with the contract was able to be compensated for if necessary.

[14] I have not found it necessary to engage with the arguments developed by the parties in relation to the role of hardship, and the achievement by other means of the contractual purpose in terminating the lease, when considering frustration. These are fully addressed by Glazebrook J whose reasons I have had the advantage of reading in draft. I consider these to be aspects of the overall assessment of frustration which need not be distinctly considered in the circumstances of the relatively straightforward application called for in the present case. In relation to the discussion contained in Glazebrook J's reasons on the irrelevance of the arguments made in reliance on the Public Works Act, I agree entirely with her analysis.

[15] It is however necessary for me to say something about the question of allocation of risk, since I take a different view to that expressed by Glazebrook J at [139]–[155]. Where the parties have unmistakeably provided for a specific risk, then I agree that the eventuation of that risk may be unlikely to frustrate the contract. The allocation of risk is, however, one only of the factors to be considered. And in some cases risk allocation may not prevent an event within the type of risk being treated as frustrating the contract, if it is of a scale that is outside the reasonable contemplation of the parties.[19]

[16] I prefer not to express any view on the effect of an allocation of risk by operation of law or the effect of contractual provisions which adjust such legally imposed allocation. Questions of the effect of a contractual allocation of risk do not arise because I am of the view that cl 8 of the settlement agreement is not an allocation of the risk of destruction of the premises but acknowledgement that, even though the agreement provides for compensation for the goodwill of the business, the business remains at the sole risk of Planet Kids until the settlement date. That is consistent with cl 9 of the settlement agreement by which Planet Kids acknowledged that the Council was not purchasing its business, "but merely compensating the Lessee for the closure of the business on the same basis as if the business had been sold as a going concern". Nor do I think it is necessary to consider whether termination of the lease by operation of cl 40.1 of the lease agreement is in itself an allocation of foreseeable risk which would preclude frustration. That is because I take the view that the agreement here was, in any event, not frustrated.

Result

[17] I would allow the appeal and remit the matter to the High Court for resolution of the outstanding matters of dispute on the basis that the contract has not been frustrated and remains on foot.

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19 *The Sea Angel*, above n 11, at [112].

McGRATH, GLAZEBROOK AND GAULT JJ

(Given by Glazebrook J)

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Introduction

[18] Planet Kids Limited operated a childcare business from premises leased from the Auckland Council.[20] The Council wished to use the land for a roading project and sought to acquire the lease under the Public Works Act 1981.

[19] On 3 June 2010, Planet Kids and the Council entered into an agreement said to be in full and final settlement of any claim for compensation under the Public Works Act (the settlement agreement).

[20] Before the settlement date of the agreement, the premises were destroyed by a deliberately lit fire. Both parties accepted that, under the terms of the lease agreement, this caused the lease to terminate. The Council's position was that this event brought the settlement agreement to an end through the doctrine of frustration.

[21] Planet Kids issued proceedings seeking a declaration that the settlement agreement subsists and is enforceable by Planet Kids and judgment for the sum of $413,679.38[21] plus interest and costs on a solicitor to client basis or in the Court's discretion. Summary judgment was sought. The Council opposed the application and in turn applied for summary judgment to be granted in its favour or the striking out of the proceedings.

[22] The only defence raised by the Council in the statement of defence and counterclaim and in its notice of interlocutory application was that the settlement agreement had been frustrated and the parties had accordingly been discharged from their obligations.

[23] In the High Court,[22] Peters J accepted the Council's submission that the settlement agreement had been frustrated. Planet Kids' application for summary judgment was dismissed. The Council's application for summary judgment or the

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20 The lease was originally with Waitakere City Council.

21 The figure was said to be the compensation amount payable under the settlement agreement, less the deposit paid, the value of vehicles retained by Planet Kids and an allowance for insurance moneys received by Planet Kids for chattels destroyed in the fire. See [35], [38] and [39] below. In its statement of defence filed in the High Court, the Council disputed Planet Kids' calculations. We make no comment on whether the calculations are correct.

22 *Planet Kids Ltd v Auckland Council* HC Auckland CIV-2011-404-1741, 16 December 2011.

striking out of Planet Kids' claim was adjourned pending submissions being received from the parties and consideration of whether there should be some relief under the Frustrated Contracts Act 1944.[23]

[24] Planet Kids appealed to the Court of Appeal against Peters J's judgment. The Court dismissed the appeal.[24] It considered that there were two possible ways of construing the settlement agreement. On the first approach, the intention of the agreement was to remove Planet Kids' business so that the Council could obtain the use of its land without the lease. If that had been the proper construction of the settlement agreement, the Court said that the agreement would not have been frustrated because that goal (and other subsidiary goals including certainty of outcome) had already been achieved.[25] On the other view of the settlement agreement, which the Court of Appeal held to be the proper approach, the agreement was designed to resolve the Public Works Act dispute and to enable the Council to acquire Planet Kids' leasehold interest. Because of the fire, there was no leasehold interest to acquire and the contract was frustrated.[26]

[25] Leave to appeal to this Court was granted on the question of whether the Court of Appeal was correct to conclude that Planet Kids was not entitled to summary judgment against the Council.[27] The main issue in the appeal is whether the settlement agreement was frustrated.

[26] In broad outline, Planet Kids submits that the fire did not result in such a fundamental or radical change to the settlement agreement so as to place this case into the small group of extreme cases in which the doctrine of frustration applies. In this regard, it submits that this Court should accept the interpretation of the contract which was rejected by the Court of Appeal. Under that approach, the Council has already achieved its main purpose in entering into the settlement agreement: certainty.

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23 At [35].

24 *Planet Kids Ltd v Auckland Council* [2012] NZCA 562, [2013] 1 NZLR 485 (O'Regan P, Arnold and Ellen France JJ).

25 At [51]–[53].

26 At [54]–[66].

27 *Planet Kids Ltd v Auckland Council* [2013] NZSC 36.

[27] By contrast, the Council supports the decision of the Court of Appeal, submitting that the fire and the resulting termination of lease destroyed the fundamental assumption on which the settlement agreement was based: that Planet Kids would have an existing estate or interest in the land that would be available at the settlement date to be acquired by the Council. The continued existence of the lease was, in its submission, a prerequisite to compensation both under the Public Works Act and under the settlement agreement. Without the lease the agreement was fundamentally different.

[28] Before addressing the parties' submissions in more detail, we give some more factual background, summarise the terms of the settlement agreement, set out the statutory framework and provide a general discussion on the law of frustration.

More background

[29] On 2 October 2009, the Council gave notice of its desire to acquire the Planet Kids lease under s 18 of the Public Works Act. Negotiations followed between the parties. The Council, in an email of 16 December 2009, outlined the discussions that had taken place that day, including that the relocation of Planet Kids' business was still a possibility. The Council advised that 1 October 2010 (or earlier if possible) was "the 'drop dead' date by which [the] council requires vacant possession of the … site".

[30] On 2 March 2010, the Council gave notice under s 23 of the Public Works Act of its intention to acquire the land compulsorily. On 29 March 2010, Planet Kids gave notice of objection to this acquisition to the Environment Court, pursuant to s 23(3) of the Public Works Act.

[31] By the end of April 2010, Planet Kids and the Council had reached substantial agreement on the terms of the settlement agreement. By letter of 31 May 2010, two copies of the "newly-drafted" agreement were sent to Planet Kids for signing. Planet Kids was advised that there was urgency "as this agreement is the sole outstanding document that will enable the Council to continue its tender process". As noted above, the settlement agreement was signed on 3 June 2010. The settlement date under the agreement was 20 December 2010.

[32] In early August 2010, Planet Kids' staff were advised of the pending closure of the business and they started to seek alternative employment. Around 7 September 2010, parents of children attending Planet Kids were advised of the pending closure of the business to enable them to seek alternative childcare facilities.

[33] In the last week of September 2010, the Council let the $20 million tender for the works affecting the subject property. The tender was awarded by the Council to the successful tenderer on 1 October 2010.

[34] On the night of 2 October 2010, the day after the tender was awarded, Planet Kids' premises were destroyed by fire. As a result, cl 40.1 of the lease between Planet Kids and the Council brought the lease to an end. The relevant part of that clause provided for termination of the lease if the premises[28] were "destroyed or so damaged by fire … so as to be rendered untenantable or unfit for business or occupation".

[35] Planet Kids has been paid the sum of $133,478.80 plus GST by its insurance company in respect of chattels that were destroyed in the fire. Planet Kids has given credit for this amount in its claim.

Terms of the settlement agreement

[36] The recitals of the settlement agreement record that Planet Kids carries on business as a childcare centre (defined as the "Lessee's Business") from land leased from the Council. They then record that the Council needs to obtain possession of and demolish the premises to enable it to extend Clark Street over the adjoining rail corridor to form a new intersection with Totara Avenue. This would necessarily require the closure of Planet Kids' business.[29]

[37] The recitals go on to say that the "parties have negotiated a basis for payment" under the Public Works Act. As Planet Kids had been unable to locate comparable premises, it had been agreed that the payment of "compensation on the

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[28] There is a similar provision if the leased premises form part of buildings or improvements that are destroyed or damaged by fire.

[29] The leased land was situated close to Clark Street.

basis of business relocation and disturbance is not considered either a fair or appropriate basis for payment of compensation". Thus Planet Kids was to be compensated "for the loss of goodwill arising from a closure of the Lessee's Business, calculated on the same basis as if the lessee had sold the Lessee's Business to the Council as a going concern".

[38] Clause 1 of the settlement agreement provides:

> 1. The Council will pay to the Lessee in full and final settlement of any claim for compensation that the Lessee may have under PWA [Public Works Act] 1981 and arising directly or indirectly out of the undertaking of the works by the Council and the closure of the Lessee's Business, and the Lessee will accept payment on that basis, the following amounts:
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>   a) For the goodwill of the business, pursuant to s68(1)(b) PWA, together with all of the Lessee's chattels and plant on the premises with the exception of those chattels or plant listed in Appendix B, the sum of $538,000.00 plus GST; and
>
>   b) A sum sufficient to reimburse the reasonable valuation, accountancy and legal fees incurred by the Lessee relating to the negotiation and settlement of this agreement, pursuant to s66(1)(a)(ii) PWA
>
> (together referred to in this agreement as "the compensation").

[39] Clause 2 requires a 10 per cent deposit to be paid on execution of the settlement agreement, with the balance to be paid on 20 December 2010 (or such earlier settlement date as agreed between the parties).

[40] Clause 3 provides that, on the settlement date, Planet Kids is required to yield up vacant possession of the premises and deliver:

> (a) a validly executed surrender of the lease; and
>
> (b) a validly executed restraint of trade covenant on the agreed terms.

[41] Other relevant clauses include cl 6 which provides that, in consideration of Planet Kids entering into the settlement agreement, the sum of $40,243.70 in rent owing is forgiven.[30] Clause 7 provides that rent is to be paid up until settlement date. Clause 8 of the agreement provides:

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[30] Clause 6 of the settlement agreement states that this amount was made up from: rate and rental

> The Lessee's Business shall remain at the sole risk of the Lessee until the settlement date.

[42] Under cl 9, Planet Kids acknowledges that the Council is not purchasing the business. It therefore remains liable for all liabilities of the business and agrees to indemnify the Council in respect of all claims that may arise in relation to such liabilities, whether incurred before or after the settlement date of the agreement.

[43] Under cl 10, the Council is entitled, after execution of the settlement agreement, to enter the land to conduct any investigations into the land or any preliminary works, provided 48 hours notice is given and the investigations and works do not, without the consent of Planet Kids, interfere with the conduct of its business.

Statutory framework

[44] Section 17(1) of the Public Works Act provides that a Minister or local authority may enter into an agreement to purchase any land for any public work for which it is responsible.

[45] Section 62(1)(b) of the Public Works Act (on which the Council seeks to rely[31]) provides that the value of land shall generally be the amount for which the land would be sold on the open market by a willing seller to a willing buyer. The date this is assessed, under s 62(2)(c), is whichever is earlier of the date the land was vested in the Crown or the local authority and the date on which the land was first entered upon for the purposes of construction.

[46] Section 68(1) of the Public Works Act (referred to in cl 1(a) of the settlement agreement) provides that the owner of any land acquired under the Act for a public work shall be entitled to compensation for:

> (a) business loss resulting from relocation of the business made necessary by the taking or acquisition which loss, unless the owner and the Minister or local authority otherwise agree, shall not be determined

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arrears, some of which arose from two rental increases during the course of the lease, and costs associated with fire alarm system repairs. It appears from the evidence that Planet Kids disputed the arrears arising from the first rental increase.

[31] See [104] below.

until the business has moved and (if the circumstances so require) until sufficient time has elapsed since the relocation of the business to enable the extent of the loss to be quantified; or

(b) loss of goodwill of any such business, if–

(i) the land is valued on the basis of its existing use; and

(ii) the owner gives such assurances and undertakings not to dispose of the goodwill and not to engage in any similar trade or business as may be required by the Minister or local authority.

The law on frustration

[47] The doctrine of frustration was developed[32] to mitigate the effects of the doctrine of absolute contracts, under which a party who had bound him or herself by contract could not escape liability for damages on the basis that performance had become impossible or futile.[33] The rationale for the doctrine of absolute contracts was that it was open to the parties to have allocated the risk by contract.[34]

[48] There are three salient features of the doctrine of frustration:[35]

(a) For fundamental policy reasons related to the sanctity of contract, the threshold for frustration is high.[36]

(b) It does not depend on application or election by the parties but occurs automatically by operation of law to discharge the contract "forthwith, without more and automatically".[37]

(c) The doctrine of frustration operates to bring the contract to an end at the time of the frustrating event. The contract is not deemed invalid

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32 Starting with the case of *Taylor v Caldwell* (1863) 3 B & S 826, 122 ER 309 (QB). For a full description of the early development of the doctrine: see GH Treitel *Frustration and Force Majeure* (2nd ed, Sweet & Maxwell, London, 2004) at [2-010]–[2-043].

33 *Paradine v Jane* (1646) Aleyn 26 at 27, 82 ER 897 (KB) at 897–898.

34 See Treitel, above n 32, at [2-029]–[2-034] for a discussion of circumstances in which the doctrine of absolute contracts survives in England and Wales.

35 As discussed by JF Burrows "Frustration of Contract" in Law Commission *Contract Statutes Review* (NZLC R25, 1993) 275 at 277.

36 Treitel, above n 32, at [2-036]; and *Dysart Timbers Ltd v Nielsen* [2009] NZSC 43, [2009] 3 NZLR 160 at [32] per Tipping and Wilson JJ and at [59] per McGrath J.

37 *Hirji Mulji v Cheong Yue Steamship Co Ltd* [1926] AC 497 (PC) at 505. See also Treitel, above n 32, at [15-002]. It is suggested by Treitel at [15-014] that this rule could be modified to allow for optional discharge. We have not, however, been asked by the parties in this case to do so and therefore make no comment on the suggestion.

from the outset and so at common law there was usually no relief for part performance occurring prior to the supervening event.[38] The Frustrated Contracts Act now allows some restitutionary relief.

[49] There have been a number of justifications and tests put forward for the doctrine. These include:

(a) that there is an "implied term" or "implied condition" in the contract that, if the frustrating event occurs, the contract would be at an end;[39]

(b) that, on the occurrence of the frustrating event, there is a failure of consideration;[40]

(c) that the doctrine is based on a special exception to the doctrine of absolute contracts as required by considerations of justice;[41] and

(d) that the frustrating event removes the "foundation" of the contract.[42]

[50] The most widely accepted view of frustration, however, was set out by the House of Lords in *Davis Contractors Ltd v Fareham Urban District Council*.[43] In that case, Lord Reid said that frustration depends in most cases on the true construction of the terms of the contract read in light of the nature of the contract and the relevant surrounding circumstances when the contract was made. The question is whether the contract is, "on its true construction, wide enough to apply to the new situation: if it is not, then it is at an end".[44]

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38 This rule was set out in *Chandler v Webster* [1904] 1 KB 493 (CA). This position was later softened in *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32 (HL). See Treitel, above n 32, at [15-011], and at [15-055]–[15-059] where it is noted that in the United States restitution is permitted in respect of benefits conferred under contracts that have been frustrated after partial performance.

39 See, for example, *FA Tamplin Steamship Co Ltd v Anglo-Mexican Petroleum Products Co Ltd* [1916] 2 AC 397 (HL) at 403–404 per Earl Loreburn.

40 This explanation is commonly used in the United States: Edwin Peel *Treitel: The Law of Contract* (13th ed, Sweet & Maxwell, London, 2011) [*Treitel: The Law of Contract*] at [19-119].

41 See for example, *Hirji Mulji v Cheong Yue Steamship Co Ltd*, above n 37, at 510.

42 See, for example, *FA Tamplin Steamship Co Ltd v Anglo-Mexican Petroleum Products Co Ltd*, above n 39, at 406 per Viscount Haldane (in a dissenting speech); and *WJ Tatem Ltd v Gamboa* [1939] 1 KB 132 (KB) at 138 per Goddard J.

43 *Davis Contractors Ltd v Fareham Urban District Council* [1956] AC 696 (HL).

44 At 720–721. Lord Somervell agreed with Lord Reid as to the basis of frustration: at 733.

[51] In the same case, Lord Radcliffe said that frustration:[45]

> … occurs wherever the law recognises that without default of either party a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract. Non haec in foedera veni. It was not this that I promised to do.

[52] This, according to Lord Radcliffe, is decided by the court on behalf of the "fair and reasonable man, who represents after all no more than the anthropomorphic conception of justice".[46] Atiyah says that this means that the solution which the court finally imposes is not in any real sense dependent on the intention of the parties, but is simply based on a rule of law.[47] Treitel, however, points out that, in construing a contract, the court does not wholly disregard the intention of the parties. It will apply an objective test but will also identify and take into consideration the circumstances in which the parties intended the contract to operate.[48] We agree with Treitel's analysis on this point.

[53] In *National Carriers Ltd v Panalpina (Northern) Ltd*, Lord Simon put the matter in similar terms to those of Lord Radcliffe. He said:[49]

> Frustration of a contract takes place when there supervenes an event (without default of either party and for which the contract makes no sufficient provision) which so significantly changes the nature (not merely the expense or onerousness) of the outstanding contractual rights and/or obligations from what the parties could reasonably have contemplated at the time of its execution that it would be unjust to hold them to the literal sense of its stipulations in the new circumstances; in such case the law declares both parties to be discharged from further performance.

Viscount Simonds agreed that the contract in question was not frustrated and emphasised the need to construe the doctrine of frustration narrowly: at 713–716. Lord Morton concurred. He stated, "It is, I think, impossible to hold that a contract has been frustrated unless it can be said: 'As and from such and such a date, at latest, the contract ceased to bind the parties'" at 717.

45 At 729. A similar test was postulated in comments by one of the judgments in *Dysart Timbers Ltd v Nielsen*, above n 36, at [58] per McGrath J.

46 At 728.

47 PS Atiyah *An Introduction to the Law of Contract* (5th ed, Clarendon Press, Oxford, 1995) at 21. A similar point is made in the most recent edition of the text: Stephen A Smith *Atiyah's Introduction to the Law of Contract* (6th ed, Clarendon Press, Oxford, 2005) at 16.

48 Treitel, above n 32, at [16-016].

49 *National Carriers Ltd v Panalpina (Northern Ltd)* [1981] AC 675 (HL) [*National Carriers*] at 700. Lord Hailsham and Lord Roskill also endorsed Lord Radcliffe's approach at 688 and 717 respectively. Lord Roskill did remark, however, that he saw little distinction between Lord Radcliffe's test and the so-called construction theory. Lord Wilberforce declined to endorse a single justification for the doctrine: at 693. Lord Russell did not express any view on the basis of the doctrine.

[54] Another way of putting the test is that frustration arises when the supervening event has destroyed a basic assumption the parties had made when they entered into the contract.[50]

[55] In *Hirji Mulji v Cheong Yue Steamship Co Ltd*, Lord Sumner expressed a similar concept in the following terms:[51]

> An event occurs, not contemplated by the parties and therefore not expressly dealt with in their contract, which, when it happens, frustrates their object. Evidently it is their common object that has to be frustrated, not merely the individual advantage which one party or the other might have gained from the contract. If so, what the law provides must be a common relief from this common disappointment and an immediate termination of the obligations as regards future performance. This is necessary, because otherwise the parties would be bound to a contract, which is one that they did not really make.

[56] Looking at the question from a different angle, Atiyah says that the doctrine of frustration is essentially a risk allocation procedure. The question is whether it is reasonable to place the risk of non-performance for the events which have happened on one party or the other or neither. If it is not reasonable to place the risk on either party then the contract is frustrated. If the risk is placed on a particular party, either by the contract or by necessary implication,[52] then the doctrine of frustration does not apply.[53]

[57] Treitel says that the principal purpose of the doctrine of frustration is to provide a satisfactory means of allocating or dividing the loss caused by supervening events.[54] In this regard he sees the discharge of the contract as a result of frustration as a form of loss allocation or loss splitting between the parties to a contract.[55] We discuss his view in more detail at [131]–[133] below.

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50 Treitel, above n 32, at [1-001], referred to with approval in comments in one of the judgments in *Dysart Timbers Ltd v Nielsen*, above n 36, at [30]–[31] per Tipping and Wilson JJ.

51 *Hirji Mulji v Cheong Yue Steamship Co Ltd*, above n 37, at 507. In *National Carriers*, above n 49, Lord Hailsham suggested that *Hirji Mulji* was really an example of the "foundation of the contract" theory of frustration (see [49](d) above). He noted that the difficulty with such a formation is identifying what, in any given case, is the foundation of the contract: at 687–688.

52 The issue of risk allocation is discussed in more detail at [139]–[146] below.

53 Atiyah, above n 47, at 2401. The most recent version of the text analyses the issue, under the heading "Frustration as a risk–allocation procedure", as one of contractual interpretation as to the allocation of risk: see Stephen A Smith *Atiyah's Introduction to the Law of Contract* (6th ed, Clarendon Press, Oxford, 2005) at 187–191.

54 Treitel, above n 32, at [13-001].

55 Treitel, above n 32, at [2-026] and [3-007] and *Treitel: The Law of Contract*, above n 40, at [19-070]. See also J Beatson, A Burrows and J Cartwright *Anson's Law of Contract* (29th ed, Oxford

[58] Most of the formulations, set out at [49] above, of the basis of the doctrine of frustration have been subject to criticism.[56] Atiyah does not, however, consider the different theories to be mutually inconsistent.[57] Treitel questions whether the theoretical basis of the distinction between the various theories has any practical importance.[58] It has been said by Lord Wilberforce that the various theories "shade into one another and that a choice between them is a choice of what is most appropriate to the particular contract under consideration".[59]

[59] In *Brisbane City Council v Group Projects Pty Ltd* Stephen J made the point that application of the doctrine of frustration invites a very broad principle being applied to "infinitely variable factual situations".[60] The test is inherently imprecise as to the degree or extent that an event affects the foundation on which the parties contracted. Application of the test calls for the exercise of judgment.[61]

[60] It is probably for this reason that, in *Edwinton Commercial Corp v Tsavliris Russ (Worldwide Salvage and Towage) Ltd (The Sea Angel)*,[62] the Court of Appeal of England and Wales said that the circumstances of the cases "can be so various as to defy rule-making".[63] Rix LJ posited a multi-factorial approach taking into account the following factors: [64]

(a) the terms of the contract;

(b) its matrix or context;

University Press, Oxford, 2010) [*Anson's Law of Contract*] at 489–493. This text also suggests that the considerable judicial attention given to identifying a theoretical basis for the doctrine may be attributed to a perceived need to explain why a finding of frustration does not constitute a reallocation of risk: at 484.

56 See for example the criticisms articulated by Lord Hailsham in *National Carriers*, above n 49, at 687–688.

57 Atiyah, above n 47, at 239. The discussion of the juridical basis of the doctrine of frustration is not included in the most recent version of the text.

58 Treitel, above n 32, at [16-013].

59 *National Carriers*, above n 49, at 693. See also the comments of Lord Simon in the same case at 702 and those in *Brisbane City Council v Group Projects Pty Ltd* (1979) 145 CLR 143 at 162–163 per Stephen J.

60 *Brisbane City Council v Group Projects Pty Ltd*, above n 59, at 163.

61 At 162–163.

62 *Edwinton Commercial Corp v Tsavliris Russ (Worldwide Salvage and Towage) Ltd (The Sea Angel)* [2007] EWCA Civ 547, [2007] 2 Lloyd's Rep 517 [*The Sea Angel*]. Rix LJ delivered the judgment, with Wall and Hooper LJJ concurring.

63 At [110].

64 At [111].

(c) the parties' knowledge, expectations, assumptions and contemplations, in particular as to risk, as at the time of the contract, at least to the extent that these can be ascribed mutually and objectively; and

(d) the nature of the supervening event, and

(e) the parties' reasonable and objectively ascertainable calculations as to the possibilities of future performance in the new circumstances.

[61] Rix LJ went on to say that the consequences of the decision whether or not to apply the doctrine must be measured against the demands of justice.[65] This does not mean that the courts have a wide absolving power to dispense justice but the rules are not expected "to lead one automatically, and without an exercise of judgment, to a determined answer without consideration of the demands of justice".[66]

[62] The multi-factorial approach has been endorsed by commentators.[67] We agree that such an approach should be applied, taking into account the comments by Stephen J in *Brisbane City Council*, the factors set out by Rix LJ in *Sea Angel* and the tests discussed at [50]–[55] above. The tests set out at [49] may also provide assistance in some cases.

Issues in the appeal

[63] From the parties' submissions and the authorities we have just discussed, the following questions arise:

(a) Did the fire render performance of the settlement agreement impossible or radically different?

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65 At [112].

66 At [113].

67 It is endorsed in Michael Furmston *Cheshire, Fifoot & Furmston's Law of Contract* (16th ed, Oxford University Press, Oxford, 2012) at 722. The multi-factorial approach is also discussed, although not expressly endorsed, in *Treitel: The Law of Contract*, above n 40, at [19–008] and HG Beale (ed) *Chitty on Contracts* (31st ed, Sweet & Maxwell, London, 2012) vol 1 [*Chitty on Contracts*] at [23-019].

(b) Did the fire defeat the main purpose of the settlement agreement?

(c) Was it a fundamental assumption of the parties that the lease would subsist at settlement date?

(d) What is the relevance of the Public Works Act?

(e) Is hardship necessary?

(f) What is the effect of the lease termination being achieved through other means?

(g) Was the risk allocated to one of the parties?

(h) Was the risk of fire and lease termination foreseeable?

[64] It is convenient to deal with each of the above questions in turn. In the end, however, they form part of an overall assessment as to whether the contract was frustrated, which we deal with under a separate heading. We then consider whether summary judgment should be entered.

[65] Before we embark on our discussion, we make some brief comments on the approach of William Young J in his judgment. He accepts that a contract that is frustrated comes immediately to an end and that there is no scope for subsequent cancellation under the Contractual Remedies Act 1979. He considers, however, that a frustration analysis should occur against a consideration of the way in which the consequences of the alleged frustrating event would be dealt with under the contract were it held not to be frustrated.[68]

[66] We agree that a consideration of the position under the Contractual Remedies Act could be a useful practical cross-check for the application of the principles applicable to frustration but we do not consider it mandatory that they be argued

[68] At [175] below.

together. Here the Council chose to argue frustration and it is necessary for us to engage with that argument.

Did the fire render performance of the settlement agreement impossible or radically different?

The parties' submissions

[67] The Council submits that, following the fire and termination of the lease, Planet Kids had no estate or interest in the land, thus making performance of the settlement agreement impossible or radically different from what the parties intended.

[68] Planet Kids submits that the settlement agreement had already delivered benefits to the Council and that some parts of the settlement agreement could still be performed. This means that the fire had not caused performance of the agreement to be impossible or radically different.

Our assessment

[69] The fire did render parts of the settlement agreement impossible to perform. Following the fire, Planet Kids was incapable of delivering a validly executed surrender of lease as required under cl 3(a) of the settlement agreement (because the lease had terminated already pursuant to the lease agreement because of the fire).[69] As the lease had terminated, the obligation under cl 7 to pay rent up to the settlement date also necessarily fell away (as there was no lease under which to pay rent). The chattels and plant referred to in cl 1(a) were lost in the fire. Planet Kids could not therefore transfer these to the Council.[70]

[70] There were, however, a number of benefits that had already been enjoyed under the contract and some that still could be performed. The Council's forgiveness of the disputed rent, under cl 6, was in consideration of Planet Kids entering into the

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69 Clause 40.1 of the lease agreement. See [34] and [37] above.

70 Planet Kids has given a credit to the Council for the value of chattels and plant in its claim: see [35] above.

settlement agreement and thus was essentially complete at that point. There was no significant change to the benefit enjoyed by the Council as a result of the right of entry onto the land before the settlement date under cl 10. This benefit would not have been available to the Council, absent the settlement agreement.

[71] If this had been the sale of a business as a going concern, goodwill of the business (cl 1(a) of the settlement agreement) would have remained in existence, although the value may well have been eroded by the business interruption caused by the fire.[71] The settlement agreement was not, however, an agreement for the sale of the business, as is made clear by cl 9. Nor was the Council's aim to remove a competitor by a purchase of goodwill and the imposition of a restraint of trade. The giving of a restraint of trade relates to the requirements of the Public Works Act[72] and the goodwill figure is a notional amount for loss of goodwill caused by the Council's intended acquisition of the Planet Kids lease because of the road works.[73]

[72] The settlement agreement does not contain an explicit obligation for Planet Kids to close its business but closure was a necessary consequence of the agreement to surrender the lease, the fact that the Council was not buying the business (despite goodwill being valued on a going concern basis[74]) and the restraint of trade.

[73] A key point is that it was recognised by the parties when they entered into the settlement agreement that one consequence would be the closure of the childcare centre and the loss of goodwill. While Planet Kids had looked at the relocation of the business, by the time it entered into the agreement the inevitability of closure was a reality. It contracted on that basis.

[74] The closure of Planet Kids' business was not rendered impossible by the fire. Nor was it caused by the fire. Indeed, it had been underway before the fire. As a matter of practicality, Planet Kids had to take steps well before the settlement date to wind up its business. Parents had to be given enough notice for them to arrange

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71 Given that Planet Kids considered relocation of the business, we assume that the goodwill was not totally dependent on the particular premises.

72 See s 68(1)(b)(ii) of the Public Works Act set out at [46] above.

73 See [36] above.

74 See [37] above.

alternative childcare and staff also had to be given notice of closure.[75] The fire merely brought forward the date of closure of the business and, by the time of the fire, the goodwill had effectively already been substantially eroded.

[75] Further, although the reason for the restraint of trade was the Public Works Act requirement, it is nonetheless an obligation under the settlement agreement that it be provided and the fire did not in any way affect Planet Kids' ability to fulfil that obligation.

[76] All this means that we accept Planet Kids' submission that there were some aspects of the settlement agreement that could still be or that had already been performed. Partial performance and a remaining ability to perform further parts of a contract in the future are relevant to frustration.

[77] Where there remain significant aspects of a contract that can still be performed (despite the supervening event), the case is one of partial impossibility only. In such cases, a contract is only frustrated if the main purpose of the contract is defeated.[76] For example in *Taylor v Caldwell*, the contract concerned the provision of a music hall and the surrounding gardens for a number of concerts. The hall burnt down in the interim. The Court held the contract was frustrated notwithstanding the continued availability of the gardens. The existence of the hall, the Court stated, was essential to the contract.[77]

[78] We accept that a contract may still be frustrated even if it has already been partially performed.[78] We nevertheless consider that partial performance, which has occurred prior to the supervening event, is a factor that may be relevant to the assessment of whether the case is one of partial impossibility. This is particularly the case where there is partial performance of contracts containing multiple independent purposes and obligations but it can also be relevant in single object contracts.[79]

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75 See [32] above.

76 Treitel, above n 32, at [5-002].

77 *Taylor v Caldwell*, above n 32, at 832.

78 As pointed out by Lord Hailsham in *National Carriers*, above n 49, at 687. This is also clear from the Frustrated Contracts Act.

79 See for example *FA Tamplin Steamship Co Ltd v Anglo-Mexican Petroleum Products Co Ltd*, above n 39; *Grimsdick v Sweetman* [1909] 2 KB 740 (KB); and *Leiston Gas Co v Leiston-cum-Sizewell Urban District Council* [1916] 1 KB 912 (KB); aff'd [1916] 2 KB 428 (CA). Also see

[79] In this case, what has already been performed and what can still be performed (despite the fire) are significant enough to render this a case of partial impossibility only. We therefore need to assess if the main purpose of the settlement agreement has been frustrated, which we do in the next section.

[80] The Council's submission that the early termination of the lease rendered the obligations radically different, as it removed the basic assumption on which the settlement agreement was based, is essentially a submission that the main purpose of the agreement was defeated. This point is covered by the next section.

Did the fire defeat the main purpose of the settlement agreement?

The parties' submissions

[81] Planet Kids submits that the settlement agreement has not been frustrated as the main purpose of the agreement was largely achieved. It submits that, despite the fire, the settlement agreement resulted in certainty of outcome for the Council which was of considerable benefit, allowing it to proceed with its tender for the works.

[82] The Council's position is that the essential purpose and foundation of the contract was the acquisition of the lease interest. The fact that Planet Kids did not have a lease to surrender was sufficient to frustrate the agreement, regardless of any other benefits that may have arisen under the agreement.

Our assessment

[83] The notion that there is a common purpose or object of the parties to a contract has been criticised. It has been said that the idea of a 'common purpose' is artificial. Contracting parties are not partners. Rather each party expects certain individual benefits from performance of the contract.[80] Treitel discusses these criticisms but ultimately concludes that it makes sense with regard to most contracts

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the United States case of *Grace v Croninger* 55 P 2d 940 (Cal Ct App 1936). The relevance of partial performance is also clear from Treitel, above n 32, at [5-002].

80 See, for example, *Scanlan's New Neon Ltd v Tooheys Ltd* (1943) 67 CLR 169 at 196 per Latham CJ.

to say that the parties have a common object and that this common object will be well understood by them.[81]

[84] In order to see if a common purpose or purposes can be discerned from the settlement agreement in this case, we first consider the purpose of each party to the settlement agreement, insofar as it can be ascertained objectively on the basis of the agreement itself and the context in which the agreement was made.

[85] The purpose of the settlement agreement, when construed from the perspective of Planet Kids, was to obtain compensation for the closure of its business and, as a secondary purpose, to settle the rental dispute. The closure (or relocation) of the business arose from the Council's need for the lease to be terminated to enable it to complete the road works.

[86] Planet Kids could have maintained its Environment Court objections,[82] although it concedes that its objection was unlikely to succeed. Entering into the settlement agreement gave Planet Kids certainty as to the basis and amount of compensation for its business closure, it having decided that relocation was not an option. It also provided the opportunity to settle the rental dispute.

[87] From the Council's perspective, it needed to have Planet Kids' lease terminated in order to undertake the road works. The Council could, however, have waited for the statutory process to be completed. As noted above, it is conceded that Planet Kids' objection to the compulsory acquisition of the lease was unlikely to succeed, but it could have caused delay.

[88] What the Council achieved from the agreement, as against the compulsory acquisition process, was total certainty as to the fact of acquisition, as well as certainty as to timing and the amount of compensation payable. The settlement agreement does not expressly provide that Planet Kids must withdraw its Environment Court objection, but it is clear that one of the consequences of the

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81 Treitel, above n 32, at [2-039]–[2-043]. Treitel also in those paragraphs discusses the responses in the United States to this issue.

82 See [30] above.

agreement was that Planet Kids would cease to have standing once it relinquished the lease.

[89] Certainty of acquisition and timing were of importance to the Council. A measure of how important the entry into the agreement was for the Council was that it was prepared to forgive some $40,000 of rent that it presumably considered to be owing in consideration of Planet Kids entering into the settlement agreement. On the face of the agreement, this particular part of the settlement agreement was not dependent on whether or not the lease remained on foot.

[90] The importance of entry into the agreement from the Council's point of view is also clear from the surrounding circumstances, given the Council's wish to let the tender for the works and its "drop dead" date.[83]

[91] It is with regard to the relative importance of the lease termination and the business closure that the perspective and purpose of the parties diverge. From Planet Kids' perspective, the focus is on the business closure (albeit triggered by the lease termination) and the compensation for that closure. From the Council's perspective, the focus is on the lease termination, with the compensation for the business closure a necessary consequence of, but dependent on, that termination.

[92] There is no doubt that the settlement agreement would not have been entered into if Planet Kids did not at that time have a leasehold interest the Council wished to have terminated. Equally, there would have been no business closure if the Council had not needed the lease to be terminated in order to proceed with the road works. It would be artificial therefore not to acknowledge the importance of the termination of the lease in deciding on the main purpose of the settlement agreement.

[93] The significance of the requirement to provide a surrender of lease and the inability to do so could be exaggerated, however. That obligation must be considered in the context of the agreement as a whole. The main focus of the settlement agreement is on the closure of the business and the compensation to be paid for the closure, rather than on the surrender of lease. There was no separate

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[83] See [29] above.

consideration identified for the lease surrender. The remaining term of the lease was thus either seen by the parties as having no value, or it was thought that any value it had was subsumed in the agreed value of the business. The formal surrender document was a technicality as the lease was not registered. As William Young J points out, the mere entry into the settlement agreement amounted in practical terms to a surrender of the lease.[84]

[94] Further, the benefit for the Council in acquiring the lease was not in obtaining its possession; the Council did not want to retain the lease. It was "acquiring" the surrender of lease so that it would have an unencumbered freehold interest, as was necessary for it to undertake the road works. The fire, far from having thwarted this, in fact brought forward the date of termination of the lease. This termination was, however, achieved outside of the settlement agreement.[85]

[95] In our view, the main purpose of the settlement agreement must be assessed against the fact that the lease termination could have been achieved by the Council in one of two ways: either by agreement or by compulsorily acquisition. This suggests that the main common purpose of both parties in entering into the settlement agreement, as against letting the compulsory acquisition take its course, was certainty of outcome, timing and amount of compensation.

[96] We consider the main common purpose of the contract was to settle the Public Works Act dispute and thus to achieve certainty that Planet Kids' lease would be terminated, to identify the timing of that termination and to set the amount of compensation payable for the consequential closure of Planet Kids' business. This purpose of certainty was not thwarted by the fire but was, for all practical purposes, fulfilled before the date of the fire. Indeed, the dispute was settled immediately upon entering into the settlement agreement.

[97] Overall, the Council has received or will receive all the benefits that it contracted for, except for the actual lease surrender document and the plant and chattels that were destroyed. As the Council was not acquiring Planet Kids'

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84 See [179] below.

85 We discuss the effect of achieving an object of an agreement through other means at [100] below.

business, it seems unlikely that the plant and chattels were in any way fundamental to the Council. Further, as noted above, the formal lease surrender document was a technicality.

Was it a fundamental assumption of the parties that a lease interest would subsist at the settlement date?

[98] In the Council's submission, a fundamental assumption made by the parties when entering into the settlement agreement was that Planet Kids would have an estate or interest in the property up to the settlement date and thus a subsisting right to compensation under the Public Works Act at that date.

[99] We accept that, had the compulsory acquisition process been underway, this would have been halted by the fire as Planet Kids would not have had any land for the Council to acquire compulsorily because the lease would have been terminated as a result of the fire. It does not, however, follow that a fundamental assumption of both parties is that the lease would subsist at settlement date. It is in this regard that the different perspectives of the parties referred to at [91] above are relevant.

[100] Particularly in light of the Public Works Act overlay, looked at objectively, the Council may have been operating under the assumption that the lease would be in place at settlement date. On the other hand, the Council, having achieved the very important purpose of certainty of acquisition and timing through the settlement agreement, may have been indifferent whether the termination of the lease occurred through the agreement or under the lease itself. Either way the road works could proceed.

[101] From Planet Kids' perspective, the mere entry into the agreement triggered its business closure, which for practical reasons had to be undertaken before the settlement date. Its focus would therefore have been on achieving compensation for that closure, whether or not the lease was still in place.

[102] Therefore, even if the Council had a fundamental assumption that the lease would be in place at settlement date, this was not shared by Planet Kids. In addition, one important part of the agreement was not dependent on whether the lease existed

at settlement date – the rental forgiveness.[86] This occurred in consideration of the entry into the agreement which also supports the view that there was no fundamental mutual assumption that the lease would remain in place until settlement date.

[103] The important point, however, is that the settlement agreement was designed to achieve settlement of the Public Works Act objection expeditiously and also, as a secondary purpose, settlement of the rental dispute. Those purposes were achieved as soon as the settlement agreement was entered into.

What is the relevance of the Public Works Act?

The parties' submissions

[104] The Council submits that it is only empowered to acquire the land under the Public Works Act and that it was a prerequisite of compensation under the Act that Planet Kids' land be taken or acquired under the Act. The Council submits further that, under s 62 of the Public Works Act, the land should be valued as at the settlement date (by which time the lease in this case had been terminated).

[105] In answer to this submission, Planet Kids says that the land was not acquired under the Public Works Act but in accordance with the settlement agreement. This means that compensation is payable under the settlement agreement at the agreed amount and not under the Public Works Act.

Our assessment

[106] The Council had the power under s 17(1) of the Public Works Act to enter into the settlement agreement to "purchase" the surrender of the lease. The Council could, however, have entered into the settlement agreement even without relying on this provision as it possesses all the powers required to perform its role as a local authority.[87]

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[86] See [89] above.
[87] Local Government Act 2002, ss 11 and 12(2).

[107] Given that the Council had the power to enter into the settlement agreement, then, absent the agreement being frustrated, it is required to fulfil its obligations under it, subject to any right it may have to cancel the agreement in terms of the Contractual Remedies Act or otherwise.[88]

[108] We therefore do not accept the Council's submission that it has no mandate to pay money other than as compensation for the receipt of property. Nor are ratepayers' funds being misapplied if the Council is required to fulfil its contractual obligations with regard to a subsisting contract validly entered into.

[109] As to the Council's submission relating to s 62 of the Public Works Act, we do not see this as having any application. That section cannot (and does not purport to) dictate the compensation to be paid where land is acquired by agreement. In those cases, the compensation will be whatever is agreed between the parties. In any event, as a practical matter, the amount of compensation in an agreement will have been agreed at the time of entering into the agreement and not at the time of settlement.

[110] The Council referred in its submission to *Te Marua Ltd v Wellington Regional Water Board*.[89] In that case, it had been agreed between the landowner and the Water Board that compensation would be assessed as at 1 January 1976 on the basis provided for under the Public Works Act 1928. The market value of the land at 1 January 1976 was less than the price under an earlier cancelled contract that had been entered into by the landowner and a third party. It was held by the Court of Appeal that the compensation should be assessed at market value as at 1 January 1976, without consideration of the price agreed in the earlier contract. On 1 January 1976, the contract between the landowner and the third party was not unconditional and subsisting. It was thus not relevant to the market value of the property on that date.[90] The price upheld by the Court was calculated in the manner and at the time agreed by the parties. This case is therefore not authority for the

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88 We make no comment on what remedies may be available to the Council with regard to the inability of Planet Kids to perform some of its obligations under the settlement agreement should the agreement be held not to be frustrated.

89 *Te Marua Ltd v Wellington Regional Water Board* [1983] NZLR 694 (CA).

90 At 698.

proposition that a price agreed under a contract can be replaced by the market value at the date of settlement.

[111] In any event, in the present case there is no sum set aside as payment for the lease itself. The compensation in the agreement was for the business closure and provided payment for the goodwill and the chattels and plant of Planet Kids' business. Section 68 relates to compensation for either business relocation or goodwill as a result of the compulsory acquisition. Section 62, which relates to compensation for land value, has no application to s 68.

[112] The same principle applies, however. Relocation expenses will either be any amount agreed between the parties or, if not agreed, then as calculated in terms of s 68(1)(a). Any compensation for loss of goodwill will likewise be the amount agreed between the parties or, in the absence of agreement, the compensation provided for under s 68(1)(b) for loss of goodwill.

[113] In this case, there was an amount agreed for goodwill, which is stated in the recitals as having been calculated as if Planet Kids had sold the business to the Council as a going concern. The value of goodwill was thus a notional figure as in fact the goodwill would have dissipated in the course of the business closure, which was already underway well before the settlement date.[91] A similar situation would often arise in cases where compensation is calculated under s 68(1)(b).

Is hardship necessary?

The parties' submissions

[114] Planet Kids' next submission is that, without there being serious hardship to one or both of the parties in the continuation of a contract, the doctrine of frustration does not arise. It submits that the Council suffered no hardship as a result of the supervening event. It received Planet Kids' leasehold interest, albeit as a result of the fire and the terms of the lease rather than through the settlement agreement. No hardship was suffered through the loss of the premises, as the Council intended to

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[91] See [71] above.

demolish them anyway. No injustice will therefore arise if the settlement agreement is enforced. Instead, Planet Kids submits that it will suffer hardship if the agreement is frustrated. It has lost its business because of the settlement agreement.

[115] By contrast, the Council argues that hardship and injustice would be caused to the Council and its ratepayers if public funds were required to be expended under the settlement agreement, when Planet Kids no longer has a leasehold interest to transfer to the Council.

[116] The Council further argues that its role as landlord and acquiring authority are distinct. The benefit of the lease being terminated was received by the Council in its capacity as landlord. This did not amount to performance by Planet Kids of its obligations under the settlement agreement. The Council proposes a hypothetical situation to demonstrate this point. If a third party and not the Council had been the owner of the freehold interest, then the position argued for by Planet Kids could lead to double exposure for the Council. On the event of the fire and resulting termination of the lease, the Council would be obliged to compensate the third party freehold owner in full for the public works acquisition. The Council would also still be bound to pay the agreed compensation to Planet Kids as the previous lease holder. In the Council's submission, it would be required to pay twice for the same interest.

What role does hardship play?

[117] Planet Kids' submission that hardship is a prerequisite for frustration is extrapolated from the remarks of Lord Radcliffe in *Davis Contractors* that substantial hardship is not sufficient in itself to amount to frustration.[92] Planet Kids did not refer to any academic commentary that supported its submission.[93] Nor did it point to any more explicit statement in the case law that hardship is a prerequisite for frustration to apply.

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92 *Davis Contractors Ltd v Fareham Urban District Council*, above n 43, at 729.

93 Professor McLauchlan in an article on this case does discuss lack of hardship but we do not interpret his remarks as amounting to the exposition of a general rule. He just viewed that factor as relevant to a multi-factorial approach and the interests of justice in this case: David McLauchlan "'Frustration' in the Court of Appeal" (2013) 44 VUWLR 593 at 606.

[118] We do not accept Planet Kids' submission with regard to hardship. It does not follow from the proposition that hardship is not sufficient to constitute frustration that it is a prerequisite to the doctrine applying. One can postulate many situations where the discharge of a contract by frustration would suit both parties. Further, where both parties' obligations are wholly executory, the only loss may be loss of expectation of profit (which could not usually be dubbed hardship).

[119] Relevant to this issue is the fact that the doctrine can be invoked by either party to the contract and not only the party who is adversely affected by the supervening event (or who would be if the contract were not discharged). This results from the doctrine of automatic discharge of both parties to the contract.[94]

[120] There are some United States authorities that could be taken to support Planet Kids' proposition that hardship is a requirement. Rather than setting out a reasoned basis for that proposition, however, these cases appear to assume its existence or base it on incorrect authority.[95] The United States cases may in fact be authority for nothing more than that the threshold for frustration is high.[96]

[121] The fact that hardship is not a prerequisite to the doctrine applying does not mean, however, that lack of hardship is irrelevant.[97] In our view, lack of hardship is a factor to be taken into account in considering the nature of the supervening event and the parties' reasonable and objectively ascertainable expectations as to future performance in those circumstances.[98] Considering lack of hardship as a relevant factor is also in line with the concept that a court's decision should reflect what is just in the circumstances.[99]

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94 Treitel, above n 32, at [15-005].

95 *Lloyd v Murphy* 153 P 2d 47 (Cal 1944); *Maryland Trust Company v Tulip Realty Company of Maryland* 153 A 2d 275 (Md Ct App 1959); and *Unihealth v US Healthcare Inc* 14 F Supp 2d 623 (D NJ 1998).

96 See [48](a) above.

97 A lack of hardship was considered relevant in finding that a lease contract was not frustrated in *Grimsdick v Sweetman*, above n 79, at 747. The English courts have also been reluctant to allow parties to profit from the application of the doctrine of frustration: Treitel, above n 32, at [15-008]–[15-009]. See also the discussion of the *Tamplin* case, above n 39, in *Metropolitan Water Board v Dick, Kerr and Co, Ltd* [1918] AC 119 (HL) at 129–130.

98 See [60](d) above. See also *Metropolitan Water Board v Dick, Kerr and Co, Ltd*, above n 97, at 139.

99 *Davis Contractors Ltd v Fareham Urban District Council*, above n 43, per Lord Radcliffe at 728. See also Rix LJ's comments regarding the demands of justice discussed at [61] above.

[122] We accept Planet Kids' submission that it would suffer hardship if the settlement agreement is frustrated. The mere entry into the settlement agreement meant that it had to close its business. It had already necessarily taken steps to implement the closure. Indeed, if the fire had occurred a day before the settlement date, it would likely already have totally closed its business. If the settlement agreement is frustrated, it would suffer significant hardship as the closure would have occurred without any compensation.

[123] We do not accept the Council's submission that it would suffer hardship should the settlement agreement not be frustrated. It is true that, had the Council waited and instituted the compulsory acquisition process, then it would not have had to pay compensation in the event that the fire had still occurred. But it decided for good commercial reasons to enter into the settlement agreement and not wait for the compulsory acquisition process to terminate. It cannot constitute hardship to the Council, or misuse of ratepayers' funds, if it is called upon to perform its obligations under a contract voluntarily entered into.[100]

[124] With the termination of the lease, the Council was in the same position as it would have been had the fire not occurred. Further, the Council had already had the benefit of certainty of outcome that entry into the settlement agreement had given it, including the ability to let the tender.

[125] In such circumstances, looked at objectively, it is highly arguable that the parties' expectations following the fire would be that the agreement would remain on foot, given the lack of hardship to the Council and the benefit it has already achieved from the settlement agreement and the significant hardship to Planet Kids should the settlement agreement be frustrated.

The Council's hypothetical example

[126] We do not consider that the Council's hypothetical example is comparable. First, if the Council had not been the landlord, a different analysis would have

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[100] Subject of course to any remedies it may have under the Contractual Remedies Act or otherwise. As noted at n 88 above, we make no comment on whether there are any such remedies or on the pleading point set out at [169] below.

applied and this different analysis may have led to a different result on the issue of frustration. Secondly, assuming the Council had entered into an agreement to purchase the freehold interest from the freehold owner, the price would have been set taking into account the lease and therefore there would be no double payment. Thirdly, even if there had been no agreement with the freehold owner and the agreement with the former leasehold owner was not frustrated, the Council would still have its contractual remedies, including under the Contractual Remedies Act.

[127] We also stress that, although the Council may have different roles (acquirer and landlord), the benefits or detriments it receives or suffers in one role are available to it in all its other roles. It is also in this case not being asked to pay any more compensation than it would have had the fire not occurred.

What is the effect of the lease termination being achieved by other means?

[128] The Council achieved a termination of the lease not through the operation of the settlement agreement but because the lease agreement provided for its termination in the event the premises became untenantable.

[129] The question of how to classify cases where the result of the contract is achieved by other means is discussed by Treitel.[101] He says that the issue does not seem to have arisen in England but such situations have been discussed by German and Austrian writers. One example discussed by such writers was a contract to free a stranded ship which, before the contractor can reach her, is refloated by natural forces.

[130] Treitel posits that it is arguable in a case where the result was achieved by the normal operation of natural forces, that the doctrine of frustration is excluded on the grounds that the allegedly frustrating event was foreseeable. He says that this argument would not be available if the result was of a wholly unexpected and unforeseeable kind such as through a tide that was entirely abnormal for the season in question. In that case, Treitel says that it is at least arguable that the contract has been frustrated. He notes that total discharge of the contract would not necessarily

[101] Treitel, above n 32, at [4-086]–[4-087].

be a totally satisfactory solution in such cases but says that the general rule that frustration leads to total discharge can sometimes lead to unsatisfactory results.[102]

[131] In our view, the proposition that frustration could apply in such situations may be inconsistent with Treitel's view of frustration as a form of loss allocation or loss splitting.[103] In setting out the reasons for the rule that frustration discharges both parties from further performance, Treitel takes that the usual situation where there is a bilateral contract under which the vendor promises to provide a thing or service and the purchaser pays for it in money. In such cases, Treitel describes the vendor as bearing the price risk (he or she will not be entitled to payment for the performance which has become impossible) and the purchaser as bearing the performance risk (he or she will neither receive the performance, nor be entitled to damages for non-performance). The effect of the doctrine of discharge because of a supervening frustrating event is that the vendor is excused from performance and the purchaser excused from payment.[104]

[132] Treitel suggests that the division of the two risks operates as a form of loss allocation. Under the doctrine of absolute contracts, both the performance and price risk would be concentrated in one party, even in a case of impossibility of performance. The modern doctrine of discharge through frustration is thought to provide a better solution than the doctrine of absolute contracts where performance is prevented by supervening events for which neither party to the contract is responsible.[105] Treitel points out that one reason for preferring this approach is that it discourages a multiplicity of claims in such situations, which could be the consequence of a vendor being entitled to the price but the purchaser being entitled to damages for non-performance.[106] Treitel also notes, however, that the doctrine of

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102 Treitel, above n 32, at [4-086] notes that the German courts sometimes argued that such cases should be dealt with not under the impossibility part of the German Civil Code but in different part of the Civil Code to avoid the total discharge of a contract that occurred through the impossibility head of the Code. Treitel says that the Code has since been amended so that damages may be given, even under the impossibility head.

103 Treitel, above n 32, at [2-026].

104 Treitel, above n 32, at [2-026]–[2-028]. Treitel uses the civil law terminology of debtor and creditor. We have substituted vendor and purchaser.

105 Treitel, above n 32, at [2-027].

106 Treitel, above n 32, at [2-027].

discharge does not provide an ideal solution, particularly with regard to wasted expenditure.[107]

[133] In a situation where the result of a contract is achieved by other means there is no loss splitting. The vendor takes the price risk but the purchaser takes no performance risk because performance has already been achieved. In our view, where one of the benefits of a contract is achieved by other means, this is a factor that should be taken into account in a multi-factorial approach as telling against the doctrine of frustration applying.

Was risk allocated to one of the parties?

[134] The issue here is whether cl 8 of the settlement agreement allocated the risk of fire and lease termination to one of the parties and, if so, whether the effect of such allocation is to exclude the doctrine of frustration.

The parties' submissions

[135] The Court asked for further submissions to be filed after the hearing on the effect of cl 8 and also on the issue of foreseeability of risk.

[136] Planet Kids in its further submissions put forward two extant possibilities:[108] either cl 8 was of no relevance to the issue of frustration, or it allocated the risk to Planet Kids with the effect that the agreement was not frustrated. It outlined the arguments in favour of cl 8 allocating the risk to Planet Kids and submitted that, even if this factor is not seen as determinative, it would be an important factor to take into account in a multi-factorial approach.

[137] In its further submissions, the Council submitted that cl 8 was of no relevance as the risk of fire and lease termination fell outside the clause and the settlement agreement on its true construction.

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107 Treitel, above n 32, at [2-208].

108 The submissions noted that the Council had abandoned the argument it appeared to be making at the hearing that cl 8 supported its argument that the agreement was frustrated because it allocated the risk of lease termination to Planet Kids.

[138] The Council also submitted that, if cl 8 of the settlement agreement did allocate to Planet Kids the risk of a fire terminating the lease before settlement, then this was tantamount to an agreement that the settlement agreement was to come to an end if the risk materialised. We make no comment on that proposition. The issue of what remedies[109] might be available to the Council if the settlement agreement remains in force, under the Contractual Remedies Act or otherwise, is outside the scope of this judgment.[110]

Risks allocated by contract

[139] Where risk is allocated to one of the parties, under a contract,[111] then the doctrine of frustration is excluded, in so far as it relates to the occurrence of one of the allocated risks. The allocation of risk can be express or by necessary implication, for example, through being reflected in the price agreed for the provision of the goods, services or facilities to be provided under the contract.[112]

[140] This does not mean that the doctrine of frustration cannot be brought into operation by other events affecting the performance of such contracts, like impossibility in the method of performance, delay or illegality.[113]

[141] Despite a clause apparently allocating risk in a contract, there have been instances, as pointed out by the Council, where the courts have held that frustration has occurred. This is because the clause in question has been interpreted as being only wide enough to apply to events of a less seriously disruptive kind.[114]

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109 Subject to the pleading point made by Planet Kids: see at [169] below.

110 See at n 88 above.

111 *Chitty on Contracts*, above n 67, at [23-058]; *Treitel: The Law of Contract*, above n 40, at [19-070]–[19-075]. See also the quotations set out at [36] and [38] above which both suggest that a contract will not be frustrated where the risk of the event in question is sufficiently covered by the contract.

112 Treitel, above n 32, at [13-001].

113 Treitel, above n 32, at [3-007].

114 See, for example, *Metropolitan Water Board v Dick, Kerr and Co, Ltd*, above n 98; and *Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd*, above n 38.

Risks allocated by operation of law

[142] Where a risk is allocated to one of the parties by operation of law, this also excludes the doctrine of frustration.[115] Treitel explains that this is because, while the doctrine of frustration divides the price and purchase risk between the parties,[116] in certain specific types of contract, the law unites the performance and price risks in one party, thus preventing the application of the doctrine.[117]

[143] In a contract for the sale of land, risk passes to a purchaser when the contract is entered into. This is because, under the trust that arises from a specifically enforceable contract, the property belongs to the purchaser in equity. The risk of damage or destruction to the property therefore also passes to the purchaser.[118] Risk passes to the purchaser even with regard to conditional contracts but passes back if the condition is not fulfilled.[119] This means that there is no room for the doctrine of frustration when buildings or structures on the land are destroyed prior to settlement (although of course contractual remedies may apply, including under the Contractual Remedies Act).[120]

[144] Treitel says that, in theory, the risk of the land itself being destroyed is also covered by the risk allocation rules. He gives the example of land being washed away by a river. However, he says that the English decisions provide no actual example of such an occurrence.[121] *Chitty on Contracts* does refer to a suggestion that frustration could apply if the frustrating event prevented the vendor from

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115 See discussion in Treitel, above n 32, at [3-007]–[3-062].

116 See discussion at [131] above.

117 Treitel, above n 32, at [3-007].

118 Charles Harpum, Stuart Bridge and Martin Dixon *Megarry & Wade The Law of Real Property* (8th ed, Sweet & Maxwell, London, 2012) [*Megarry & Wade*] at [15-057(a)], citing *Paine v Meller* (1801) 6 Ves Jr 349, 31 ER 1088 (Ch); and *Rayner v Preston* (1881) 18 Ch D 297 (CA).

119 Peter Blanchard *A Handbook on Agreements for Sale and Purchase of Land* (4th ed, Handbook Press Ltd, Auckland, 1988) at [618].

120 At [618]. Blanchard notes that the position with regard to a building contract associated with a land sale is different. See also Treitel, above n 32, for the English position at [3-057]–[3-062]; and *Anson's Law of Contract*, above n 55, at 497. The position may be different in Canada. There it has been held that contracts for the sale of land may be frustrated on the basis that they are no different from other contracts. See GHL Fridman *The Law of Contract in Canada* (6th ed, Carswell, Ontario, 2011) at 635–637; John D McCamus *The Law of Contracts* (2nd ed, Irwin Law Inc, Toronto, 2012) at 624–631; and SM Waddams *The Law of Contracts* (6th ed, Canada Law Book Inc, Toronto, 2010) at [371]–[373], although Waddams' view is that the application of the doctrine to contracts for the sale of land should be tightly constrained given the settled allocations of risk in such contracts.

121 Treitel, above n 32, at [3-027].

transferring any estate whatever to the purchaser, but says that this is probably only in the event of supervening illegality.[122] Megarry and Wade, however, refer to a Privy Council case from Hong Kong, where a contract to purchase a block of flats was held to be frustrated when the building was destroyed in a landslip.[123]

[145] The position relating to chattels or goods is more complicated but generally risk passes with property.[124] Treitel suggests that, where goods or chattels are concerned, the doctrine of frustration is more likely to be displaced by the operation of the rules as to risk if under those rules the risk passes at an early, rather than at a late stage of the performance of the contract.[125]

[146] The rules relating to risk allocation in agreements for the sale and purchase of property are commonly excluded by contract, either expressly or by necessary implication. In that case, the doctrine of frustration is also displaced (as discussed in the previous section) because there is an explicit contractual provision that allocates risk.

[147] For example, the Auckland District Law Society Inc (ADLS) and Real Estate Institute of New Zealand Inc (REINZ) standard Agreement for Sale and Purchase of Real Estate[126] cl 4.1 provides that the property and chattels that are the subject of the agreement remain at the risk of the vendor until possession is given and taken. Clause 4.1 of the ADLS and REINZ approved standard Agreement for Sale and Purchase of a Business provides that the business (which is defined as including all tangible and intangible assets of the business) remains at the sole risk of the vendor until possession.[127] Both clauses then go on to set out the remedies that apply if the property is damaged or destroyed or, in the case of a business, any of the tangible assets of the business are lost, destroyed or damaged.[128]

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122 *Chitty on Contracts*, above n 67, at [23-057].

123 *Megarry & Wade*, above n 118, at [15-057], citing *Wong Lai-ying v Chinachem Investments Co Ltd* [1980] HKLR 1 (PC).

124 In New Zealand, see ss 9 and 22 of the Sale of Goods Act 1908.

125 Treitel, above n 32, at [3-010]. We are not to be taken as making any comment on this proposition.

126 Auckland District Law Society and Real Estate Institute of New Zealand *Agreement for Sale and Purchase of Real Estate* (9th ed, 2012) [*Agreement for Sale and Purchase of Real Estate*].

127 Auckland District Law Society and Real Estate Institute of New Zealand *Agreement for Sale and Purchase of a Business* (4th ed, 2008) [*Agreement for Sale and Purchase of a Business*].

128 Pursuant to s 5 of the Contractual Remedies Act, the consequence of expressly providing for

Our assessment

[148] Clause 8 of the agreement provides that Planet Kids' "business shall remain at the sole risk of the Lessee until the settlement date". This clause is in almost identical terms to cl 4.1 of the ADLS and REINZ approved Agreement for Sale and Purchase of a Business[129] and very similar in effect to cl 4.1 in the ADLS and REINZ approved Agreement for the Sale and Purchase of Real Estate,[130] although the date risk passes under those clauses is on the possession date (which of course will often coincide with the settlement date).

[149] If this were a standard agreement for the sale and purchase of a business, one would assume (if the premises or the use of the premises were also to be transferred) that cl 4.1 would be intended to place the risk of anything happening to those premises (including lease termination) on the vendor. Indeed, cl 1.1(4) of the ADLS and REINZ approved Agreement for Sale and Purchase of a Business defines "business" as including the business' assets, which here would include the lease.

[150] The parties in this case have chosen to use very similar words to the standard clauses. Normally one would assume therefore that cl 8 was intended to have the same effect as those clauses. This would mean that the risk of lease termination would remain with the vendor (in this case, Planet Kids).[131] The fact that remedies are not included in cl 8, as they are in the standard agreements, may merely mean that the parties intended that any remedies be those arising under the Contractual Remedies Act or otherwise.

[151] On the other hand, in the context of the settlement agreement, cl 8 may merely follow on from the fact that the Council was not buying Planet Kids' business and can be seen as being limited to the risk of losses the business might suffer and intended to ensure that these remained with Planet Kids, with cl 9 providing further

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remedies in an agreement is that ss 6 to 10 of the Act would have effect subject to those contractual provisions.

129 *Agreement for Sale and Purchase of a Business*, above n 127.

130 *Agreement for Sale and Purchase of Real Estate*, above n 126.

131 The adoption of standard form provisions without amendment in commercial contracts is generally treated as an adoption of the meaning usually attributed to those provisions: JW Carter *The Construction of Commercial Contracts* (Hart Publishing Ltd, Oxford, 2013) at [13.13].

protection for the Council in that regard.[132] If that were the case, the termination of the lease under cl 40.1 may fall outside the contemplation of cl 8.[133]

[152] The difficulty with that argument from the Council's point of view may be that, if the risk of lease termination is not covered by cl 8 then, under the normal rules of risk allocation in such contracts, the risk would have passed to the Council on entry into the settlement agreement. If risk is allocated by operation of law then the doctrine of frustration is excluded, as discussed above.

[153] This assumes (without deciding) that the total destruction of land is covered by the risk allocation rules excluding frustration.[134] It also assumes that risk passes to a landlord on the entry into an agreement to surrender a lease. Strictly speaking, the settlement agreement is not an agreement to acquire land. The leasehold interest will instead merge with the freehold estate on surrender.[135]

[154] Even if the risk does not, by operation of law, pass to the Council on entry into the settlement agreement because it involved a surrender rather than a purchase of the lease and a total destruction of the interest in land, it does not necessarily follow that the risk is unallocated. We record that Planet Kids, in its submissions at the hearing, suggested that, taking the circumstances as a whole, it was reasonable to interpret the agreement as placing the risk of lease termination on the Council, given the lack of detriment to the Council if the lease was terminated through fire or through surrender of lease.

[155] We do not propose to make any definitive findings on the meaning or effect of cl 8 or on whether or not the risk of lease termination was allocated by operation of law or by necessary implication to one of the parties. This is because risk

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132 We do not rule out that there may be other interpretations of cl 8 but we deal only with the two possibilities the parties currently argue.

133 This is essentially McLauchlan's argument. McLauchlan argues that the true position is that cl 8 was a standard form provision designed, probably in an abundance of caution, to make it clear that the Council was not responsible for any losses or mishaps that Planet Kids might suffer prior to settlement. He did not accept that cl 8 was drafted with cl 40.1 of the lease in mind, thus having the effect of releasing the Council from the obligation to pay compensation should the lease be terminated prior to settlement: McLauchlan, above n 93, at 604.

134 See discussion at [126] above.

135 Peter Butt *Land Law* (5th ed, Lawbook Co, Sydney, 2006) at [15237].

allocation may be relevant to the question of remedies if the settlement agreement is not frustrated. That issue is beyond the scope of this judgment.[136]

Was the risk of fire and lease termination foreseeable?

The parties' submissions

[156] Planet Kids submits that the fact that parties have foreseen an event but not made provision for it in their contract will usually prevent the doctrine of frustration from applying. The same applies to foreseeable events. Planet Kids submits that cl 40.1 of the lease agreement (which provided for termination of the lease on destruction of the premises) demonstrated that the parties had foreseen the possibility that the lease would be terminated as a result of fire. The risk of fire making the property untenantable and triggering cl 40.1 of the lease was foreseeable. Planet Kids argues that, even if this point is not determinative, it is a factor pointing against frustration.

[157] The Council submits that frustration is not necessarily excluded by the fact the supervening event was foreseeable or foreseen. The question is whether the new situation is within or outside the contract on its true construction.

The legal position

[158] A foreseen event will generally exclude the operation of the doctrine, but the inference that a foreseen event is not a frustrating event can be excluded by evidence of contrary intention. When an event is foreseeable but not foreseen by the parties, it is less likely that the doctrine of frustration will be held to be inapplicable. The degree of foreseeability required to exclude frustration is high. The supervening event must be one which any person of ordinary intelligence would regard as likely to occur. Further, not only must the supervening event be foreseeable but its consequences or effects on the contract must also be foreseeable. The inference that an event that is foreseeable may exclude frustration can also be displaced by evidence of contrary intention.[137]

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136 As noted at [138] above.

137 *Chitty on Contracts*, above n 67, at [23-059]–[23-060]. See also the discussion in Treitel, above

[159] In addition, we consider that where a risk, while unlikely to occur, would usually be dealt with in a contract of the type at issue under normal commercial practice, then this may be a factor that could be taken into account. If the parties have decided not to follow usual commercial practice and deal with the risk explicitly in their contract, this could be taken to be a conscious choice and the parties could be taken to have decided to leave the consequences to be determined, if the risk eventuates, under normal contractual principles, including any contractual remedies under the Contractual Remedies Act or otherwise. This follows from the proposition that whether or not a contract is frustrated will turn on an objective interpretation of the contract in its context, taking into account the parties' mutual knowledge, expectations, assumptions and contemplations particularly as to risk.[138]

Our assessment

[160] The fire itself was an unexpected event, particularly because it was arson and resulted in major damage to the building rendering it unusable. It was not a risk that was likely to occur. The risk of lease termination was, however, an automatic consequence of a fire that rendered the premises untenantable. In this sense, therefore the risk of lease termination was foreseeable. The parties must be presumed to know what was in the lease agreement.

[161] Further, given that the risk of termination was obvious if a serious fire occurred, one would have expected the parties to have provided for it in their contract. If they did not, then one possibility (looked at objectively) is that this was deliberate and that they had decided to take whatever consequences or remedies that would arise under the Contractual Remedies Act or otherwise in the event the lease termination occurred.

[162] This is a plausible inference in the circumstances of this case. The manner of lease termination did not in fact affect the parties. The Council would have achieved its object of lease termination even if that was not by way of surrender of lease.

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n 32, at [13-012].

138 *The Sea Angel*, above n 62, at [111], discussed at [60](c) above. See also the discussion in Stephen A Smith, *Atiyah's Introduction to the Law of Contract* above n 52 at 188.

Equally, Planet Kids would have still have been forced to close its business, however the lease termination occurred (as it had already ruled out relocation).

[163] We therefore accept Planet Kids' submission that the foreseeability of the lease termination in the event of a serious fire (evidenced by cl 40.1 of the lease agreement) is an important factor to take into account in a multi-factorial analysis.

Was the settlement agreement frustrated?

[164] This is not a case where the settlement agreement has become impossible to perform in its entirety. Indeed, the only obligations that cannot be performed by Planet Kids are either of no moment to the Council (the transfer of the chattels) or a mere technicality (the provision of the lease surrender document).[139] Further, the main purpose of the settlement agreement, being the settlement of the Public Works Act objection, was achieved immediately on entering into the settlement agreement. Certainty of acquisition, the timing of that acquisition and the price payable for the lease and the business was also achieved at that time. Certainty was important for both parties.[140]

[165] Other factors weighing against a finding that the settlement agreement is frustrated are the hardship that would be caused to Planet Kids, and the lack of hardship that would be suffered by the Council if a finding of frustration were to be made. We accept that that the Council could have acquired the lease compulsorily under the Public Works Act but it did not do so. It cannot constitute hardship for the Council to be held to an agreement it voluntarily entered into.[141]

[166] Also weighing against a finding that the settlement agreement was frustrated is the fact that the Council (apart from the chattels which were of no moment to it) in effect achieved everything it wished to achieve from the settlement agreement, albeit by other means: lease termination rather than lease surrender.[142] That the

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139 See discussion at [69]–[79] above.
140 See discussion at [83]–[103] above.
141 See [106]–[113] above for discussion of the Public Works Act issues and [117]–[125] above for a discussion of hardship.
142 See discussion at [128]–[133] above.

termination was foreseeable by virtue of cl 40.1 of the lease agreement is also a factor weighing against a finding that the settlement agreement was frustrated.

[167] We therefore hold that the settlement agreement was not frustrated as a consequence of the fire. The agreement subsists.

Should summary judgment be entered?

[168] In its application for summary judgment, Planet Kids sought a declaration that the settlement agreement subsists and is enforceable, as well as judgment for $413,679.38 plus interest and costs. Given our conclusion on frustration, it is clear that a declaration that the settlement agreement subsists should have been made.

[169] Planet Kids argued in its further submissions filed after the hearing that, if it is held that the settlement agreement has not been frustrated, then, as well as the declaration, summary judgment should be entered for Planet Kids for the sum claimed. This submission is on the basis that the Council has based its case solely on frustration and has not sought to rely on any other matter, including the Contractual Remedies Act.

[170] We have not heard argument from the Council on this proposition. We do not therefore consider it appropriate for us to enter judgment for Planet Kids for the sum claimed. Nor do we consider it appropriate to make the declaration that the settlement agreement is enforceable by Planet Kids. Rather, we consider that we should refer the matter back to the High Court to determine those matters. Planet Kids can of course make its pleading argument to that Court.

Result and costs

[171] The appeal is allowed. A declaration is made that the settlement agreement subsists. The rest of the declaration and the other orders sought by Planet Kids in its application for summary judgment are not made. The remainder of the application is referred back to the High Court for determination.

[172] The Council is to pay to Planet Kids costs of $25,000 plus all reasonable disbursements to be fixed, if necessary, by the Registrar. We certify for two counsel.

WILLIAM YOUNG J

[173] Given the way that the settlement obligations are provided for under cls 1, 2, 3 and 8 of the settlement agreement,[143] Planet Kids is prima facie (that is, subject to the law of frustration) in breach of contract because of its inability to: (a) provide a validly executed surrender of the lease and (b) hand over the chattels and plant located on the Planet Kids premises. It follows that, from the point of view of the Auckland Council, the change in circumstances brought about by the fire is addressed by the contract. Accordingly, it is entitled to the usual remedies for breach of contract, which potentially include a right to cancel.

[174] At the heart of the case is the impossibility of performance by Planet Kids. But unusually,[144] it is not Planet Kids – the party unable to perform its obligations – but rather the Auckland Council which relies on frustration. Planet Kids engaged directly with this argument. With issue primarily joined as to frustration, there has been little focus on whether Planet Kids is precluded from insisting on contractual performance by the Council by reason of its inability to meet its own obligations.

[175] I accept that a contract which is frustrated comes immediately to an end and accordingly there is no scope for subsequent cancellation under the Contractual Remedies Act 1979. But I do not think it follows that frustration must be addressed ahead, or independently, of the position under the Contractual Remedies Act. Indeed, I think that the frustration analysis should occur against a consideration of the way in which the consequences of the alleged frustrating event would be dealt with under the contract if it is held not to have been frustrated.

[176] In the present case, the application of the Contractual Remedies Act to the consequences of the fire raises issues which are logically anterior to the application

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143 Set out at [36], [37], [38] and [39], respectively of the majority judgment.

144 I am not aware of any impossibility of performance cases where frustration has been asserted by the party who is able to perform. In this respect the present case – where it is the Auckland Council who alleges frustration despite being able to perform – is at least unusual.

of frustration. This is particularly so because resolution of those issues should preclude the practical necessity to engage with the law of frustration. I say this because:

(a) If Planet Kids cannot insist on performance of the contract, the Council does not need to rely on frustration to avoid liability. But:

(b) If Planet Kids is entitled to insist on performance of the contract, the reasons why it is entitled to do so (as I will explain) would leave no practical scope for the Council to rely on frustration.

[177] Whether Planet Kids is entitled to insist on performance of the contract depends on the application of s 7(2)–(4) of the Contractual Remedies Act:

> **7 Cancellation of contract**
>
> …
>
> (2) Subject to this Act, a party to a contract may cancel it if, by words or conduct, another party repudiates the contract by making it clear that he does not intend to perform his obligations under it or, as the case may be, to complete such performance.
>
> (3) Subject to this Act, but without prejudice to subsection (2), a party to a contract may cancel it if—
>
> …
>
> (b) A term in the contract is broken by another party to that contract; or
>
> (c) It is clear that a term in the contract will be broken by another party to that contract.
>
> (4) Where subsection (3)(a) or subsection (3)(b) or subsection (3)(c) of this section applies, a party may exercise the right to cancel if, and only if,—
>
> (a) the parties have expressly or impliedly agreed that … the performance of the term is essential to him; or
>
> (b) the effect of the … breach is, or, in the case of an anticipated breach, will be,—
>
> (i) Substantially to reduce the benefit of the contract to the cancelling party; or
>
> (ii) Substantially to increase the burden of the cancelling party under the contract; or

> (iii) In relation to the cancelling party, to make the benefit or burden of the contract substantially different from that … contracted for.
>
> …

[178] If the breaches by Planet Kids of its obligations as to chattels and plant and the surrender of the lease were not within s 7(4)(a) or (b), the Council would have no entitlement to cancel under s 7(3). And if s 7(4)(a) and (b) are not engaged, it follows that the inability of Planet Kids to perform its obligations is not a repudiation for the purposes of s 7(2). If it were otherwise, any anticipated breach of contract would be a repudiation even though s 7(4)(a) and (b) are not satisfied.

[179] At least on the evidence I have seen, the chattels and plant were a matter of indifference to the Council. Accordingly, it would be difficult to conclude that the parties had expressly or impliedly agreed that satisfaction of the requirement to deliver them was essential for the purposes of s 7(4)(a). The position seems to me to be the same in respect of the surrender of the lease. The settlement agreement was practically a surrender of the lease and the delivery of a formal surrender document might be thought to have been just a technicality.[145] As well, and for similar reasons, s 7(4)(b) does not seem to me to be obviously applicable in respect of either breach.

[180] If the arguments in favour of Planet Kids were to prevail at trial, the conclusion that it was entitled to enforce the contract, but with an allowance for the chattels and plant, would reflect findings that:

(a) The parties had not "expressly or impliedly agreed that … the performance of [the relevant obligations were] essential to [the Council]" under s 7(4)(a); and

(b) The inability of Planet Kids to perform in the relevant respects had not operated:

(i) "Substantially to reduce the benefit of the contract to the [Council]", under s 7(4)(b)(i);

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[145] Were it not for the fire, Planet Kids would have had no choice but to vacate the premises on 20 December 2010 (the settlement date); compare with *Walsh v Lonsdale* (1882) 21 Ch D 9 (CA).

(ii) "Substantially to increase the burden of the [Council]", under s 7(4)(b)(ii); or

(iii) "[T]o make the benefit or burden of the contract substantially different from that … contracted for" from the point of view of the Council, under s 7(4)(b)(iii).

[181] I can see no credible basis upon which a court that made these findings against the Council could, at the same time, accept the Council's argument that the contract was frustrated.

[182] For these reasons, I would allow the appeal in the manner proposed by Glazebrook J.

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