

# Frustration will not provide relief from a failure to deal with contractual risk

By PETER MULLIGAN and SIMON BYRNES

The contractual doctrine of frustration is well known, but many parties do not have a full understanding of what is required to rely on it.

THE SITUATIONS IN WHICH a party will be relieved from performance under an agreement due to frustration were recently considered in the Victorian Court of Appeal in *oOh! Media Roadside v Diamond Wheels*.<sup>1</sup>

Diamond Wheels had licensed to oOh! Media a site on the side of a building in King Street, Melbourne for the purpose of oOh! Media erecting a billboard for outdoor advertising. The licence agreement was entered into in November 2005 when the site was visible from a number of vantage points including Kings Way, a busy Melbourne road.

From 2006 to 2008, an open car park located at the intersection of King Street and Flinders Street was developed into the substantial Northbank Office Tower. The new tower significantly reduced the visibility of the site, including obstructing visibility for traffic travelling towards Melbourne along Kings Way.

Clause 11(c) of the agreement permitted oOh! Media to terminate the licence if “the site becomes unsuitable for the Permitted Use for any reason outside the reasonable control of the Licensee”.<sup>2</sup>

In September 2008, oOh! Media wrote to Diamond Wheels purporting to terminate the licence under cl.11(c). oOh! Media claimed that although the site was still visible from certain positions, its obstruction was substantial and had caused a dramatic decrease in the advertising revenue it was able to generate from the billboard. The site had therefore become unsuitable for advertising purposes.



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Diamond Wheels treated oOh! Media's letter as a repudiation of the licence and accepted that repudiation, but commenced proceedings against oOh! Media seeking damages for loss of the benefit of the licence agreement.

**“The doctrine of frustration is not available where a party has simply failed to take adequate contractual steps to protect itself against a foreseeable risk.”**

oOh! Media claimed that:  under cl.11(c), it had been entitled to terminate the licence as the site was no longer suitable for advertising purposes; or  alternatively, the situation created by the construction of the Northbank Office Tower was so fundamentally and radically different to that which was contemplated when the licence was entered into that the agreement had been frustrated and automatically discharged upon the construction of the tower.

At first instance, Lewitan J

considered cl.11(c) and held that the site was still sufficiently visible to be fit for its intended purpose of displaying advertising and was consequently not unsuitable for its permitted use. In respect of the frustration claim, the construction of the Northbank Office Tower was held to not result in a radical or fundamental change in circumstances or the wholesale destruction of the site's value.<sup>3</sup> Having failed on both counts, oOh! Media appealed to the Victorian Court of Appeal.

On appeal, Nettle JA<sup>4</sup> affirmed Lewitan J's decision. In respect of cl.11(c), whether the site was unsuitable for the use of displaying advertising was a matter to be determined objectively. Although the site was not as profitable to oOh!

Media following the erection of the Northbank Office Tower, the site had been let during the period that its view was obstructed. His Honour therefore held that it was open to Lewitan J to find that the site had not become unsuitable for its permitted use.<sup>5</sup>

On the issue of frustration, Nettle JA went on to examine the current state of the law at some length.

### Requirements for frustration

The doctrine of frustration has developed over many years. Some judges and commentators have expressed the view that it is a flexible doctrine, unconstrained by arbitrary formulae. There is authority for the proposition that the doctrine is available wherever a supervening event

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would result in injustice for a party to be held to a literal reading of a contract.<sup>6</sup>

Nettle JA preferred a more structured approach. His Honour stated that a contract will not be frustrated unless a supervening event occurs which:

□ confounds a mistaken common assumption that some essential thing or situation will continue to exist or be available, neither party undertaking responsibility in that regard; and

□ in so doing has the effect that, without default of either party, a contractual obligation becomes incapable of being performed because the circumstances would render it radically different from that which was undertaken by the contract.<sup>7</sup>

**Application to the licence**

In applying the test to the current case, the construction of the Northbank Office Tower was a supervening event that occurred after the licence was entered into and neither party

had undertaken responsibility for this risk under the licence. As such, the relevant questions became:

□ did the parties enter into the licence agreement on the mistaken common assump-

**“The party seeking to rely on frustration must show that performance of the obligation will not merely cause hardship, inconvenience or material loss.”**

tion that the visibility of the site from Kings Way would be unobstructed during the term of the licence; and

□ if so, did the obstruction of the site make the parties’ continued performance of their obligations radically different from that which they undertook under the licence at the time they entered into it.

**Mistaken common assumption and foreseeability**

Whether an event was foreseeable or foreseen at the time

of entry into a contract is relevant to the determination of mistaken common assumption. For example, if an event was not only foreseeable but actually foreseen by the parties at the time of entering into

a contract, it would be difficult to argue that they had entered into the contract on the basis of a common understanding that the event would not occur. This would certainly be the case where the parties had foreseen not only the event but also its nature and extent.<sup>8</sup>

However, if an event was foreseeable but not actually foreseen by the parties, then the fact that it was foreseeable may not be of much significance unless the degree of foreseeability was particularly high.<sup>9</sup> According to Nettle JA, since

most events are foreseeable in one sense or another, parties to a contract will not ordinarily be taken to have assumed the risk of an event occurring unless the degree of foreseeability is “very substantial”.<sup>10</sup>

In examining whether it was foreseeable that the visibility of the site might at some stage be obstructed, Nettle JA analysed the nature of the environment surrounding the site and evidence submitted by the parties as to common practice in the outdoor advertising industry.

In doing so, his Honour found that, given the CBD location and its constantly changing skyline, it was foreseeable that the visibility of the site could be blocked or obstructed in any number of ways.<sup>11</sup> The evidence established that the possibility of a billboard site being built out in a CBD location was well understood in the advertising industry.<sup>12</sup> It was therefore common practice in licence agreements to address this type of risk by including a clause granting the lessee a



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right of termination for a material reduction in visibility.<sup>13</sup>

In the circumstances, it was “highly foreseeable” that the line of sight from Kings Way could be obstructed wholly or partially by the construction of a building or other structure.<sup>14</sup> oOh! Media had therefore failed to make out the requirement of mistaken common assumption.

#### Was performance radically different?

In order to assess if performance of an obligation has been rendered radically different to that which was undertaken under an agreement, the agreement must be read with regard to the circumstances existing at the time it was entered into and then compared against the circumstances existing at the time the obligation must be performed.

The degree to which the performance has been rendered different is the key issue. The party seeking to rely on frustration must show that performance of the obligation

will not merely cause hardship, inconvenience or material loss, but that there has been such a change in the significance of the obligation that the thing undertaken would, if performed, be a different thing to that contracted for. The doctrine of frustration is not lightly to be invoked and is to be kept within narrow bounds.<sup>15</sup>

oOh! Media contended that the unexpressed common assumption on which the parties entered into the licence was that there would continue to be an unobstructed view of the site from Kings Way. Nettle JA rejected oOh! Media’s contention on the basis that “there was nothing in the evidence of surrounding circumstances” which supported the conclusion that a shared understanding on this issue had been reached.

oOh! Media provided evidence of the reduction in fees earned from the site following commencement of the construction work. Nettle JA found that while the construction of the Northbank Office Tower

had caused oOh! Media financial hardship, and that “there may come a point at which hardship turns to frustration”,<sup>16</sup> that point had not been reached in the present case.

#### Lessons for contracting parties

The doctrine of frustration is not available where a party has simply failed to take adequate contractual steps to protect itself against a foreseeable risk. As Weinberg JA stated: “It seems extraordinary ... that, where unimpeded and long range visibility is critical to the financial viability of an agreement to license a billboard site for outdoor advertising and promotional display purposes, the relevant agreement would

not deal specifically, and in terms, with the consequences that should flow from a material reduction in visibility, such as that which may occur with a significant build out”.<sup>17</sup>

The time to get it right is when parties are drafting the terms of their contract. It is at this stage that parties should ensure that all key risks are appropriately addressed.

If a contract is entered into on the basis of a common assumption that a particular state of affairs will continue, then parties should consider including a right to terminate for a material change in that state of affairs. This is a much better position than being left to rely upon common law concepts such as frustration. □

#### ENDNOTES

1. *oOh! Media Roadside Pty Ltd (formerly Power Panels Pty Ltd) v Diamond Wheels Pty Ltd & Anor* [2011] VSCA 116.
2. *Ibid* at [9].
3. *Ibid* at [26].
4. Redlich and Weinberg JJA agreeing.
5. *Ibid* at [27]-[60].
6. *Ibid* at [65].

7. *Ibid* at [70].
8. *Ibid* at [72]-[73].
9. *Ibid* at [72].
10. *Ibid* at [74].
11. *Ibid* at [76].
12. *Ibid* at [77].
13. *Ibid* at [78].
14. *Ibid* at [84].
15. *Ibid* at [101].
16. *Ibid* at [109].
17. *Ibid* at [123]. □

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