

## *Restitution for mistaken payments: Whither mistakes of law?*

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*The traditional rule at common law precluded restitution for payments made by mistake where the payer's mistake had been one of law. That rule was set aside in New Zealand in 1958. Other jurisdictions are likely soon to follow. This article considers the law of mistaken payments absent the traditional rule. Assuming restitution is available for mistakes of law, ought the payer's ability to recover nevertheless differ according to whether the mistake was one of law or one of fact? The thesis of this article is that an approach to mistaken payment cases that deals directly with the competing merits of the parties and the relevant policy concerns, removes any need to distinguish between the two types of mistake. A distinction between mistakes of law and mistakes of fact should be irrelevant to the payer's ability to recover.*

### I INTRODUCTION

If A was mistaken as to the true state of affairs, and the mistake induced A to pay B money, A will sometimes be able to recover the payment from B. This article considers whether the classification of the mistake as one of law or as one of fact should affect A's ability to recover.

The traditional rule at common law precluded recovery for mistakes of law.<sup>1</sup> This rule was set aside in New Zealand by the Judicature Amendment Act 1958, but the distinction between mistakes of law and mistakes of fact was maintained. Thus the question was left open whether A's ability to recover might still differ according to the classification of the mistake as one of law or as one of fact.

Recent recommendations of some Commonwealth law reform bodies have favoured the New Zealand approach.<sup>2</sup> Although it is thought that the absolute bar to recovery

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1 See generally Lord Goff and G Jones *The Law of Restitution* (4ed, Sweet & Maxwell, London, 1993) chapter 4. The rule's genesis can be traced to three decisions: *Bilbie v Lumley* (1802) 2 East 469; 102 ER 448; *Brisbane v Dacres* (1813) 5 Taunt 143; 128 ER 641; and *Kelly v Solari* (1841) 9 M&W 54; 152 ER 24. These cases have been said to provide a "dubious foundation" for the rule: *David Securities Pty Ltd & Ors v Commonwealth Bank of Australia* (1992) 175 CLR 353, 372. Nevertheless, in 1943 the rule was said to be "beyond argument at this point in our legal history": *Sawyer & Vincent v Window Brace Ltd* [1943] KB 32, 34.

2 See below part II B. Since 1981, five Commonwealth law reform bodies have considered the topic of restitution for payments made by mistake of law. All have

should be set aside, the possibility of treating mistakes of fact and mistakes of law differently (the latter being less likely to found recovery) has been applauded. Likewise some judges and commentators appear to consider the distinction still to be important.<sup>3</sup>

The thesis of this article is that dealing *directly* with the competing merits of the parties removes any need to distinguish between mistakes of law and mistakes of fact. For example, consider the following fact situation, alternatively disclosing a mistake of fact and a mistake of law. The example is discussed in more detail below in part IV B.

**Example 2<sup>4</sup>**

A building company (A) sought finance from an overseas bank (B). After negotiations, A and B entered into two foreign currency loan agreements. The agreements included a grossing-up provision intended to ensure that B received the full interest due even after deduction of withholding tax. In addition to interest payments, A was to pay an amount (the "tax equivalent") equal to the withholding tax that would be deducted from the interest due. Currency fluctuations caused financial losses for A and various currency swaps were effected to attempt to minimise further losses. The loans were rolled over. B eventually brought proceedings for the recovery of monies still owing under the loans, and was awarded judgment. A seeks to reduce the quantum of this judgment, arguing that it had paid monies to B by mistake.

Mistake of fact scenario: A had incorrectly calculated the amount owed to B under the grossing-up provision. A therefore overpaid B at each interest payment, and now seeks restitution for the overpayments.

Mistake of law scenario: Section 261 of the Tax Act, which had been passed before the loan contract was formed (to protect those in A's position) made the grossing-up provision void. Despite what the contract said, A was not liable for payment of the "tax equivalent". A seeks restitution for these payments.

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recommended that the traditional common law rule be set aside: Law Reform Commission of British Columbia *Benefits Conferred Under a Mistake of Law* (LRC 51, September 1981); Law Reform Committee of South Australia *Report Relating to the Irrecoverability of Benefits Obtained by Reason of Mistake of Law* (1984); New South Wales Law Reform Commission *Restitution of Benefits Conferred Under Mistake of Law* (Report LRC 53, July 1987); English Law Commission *Restitution of Payments Made Under a Mistake of Law*, Consultation Paper 120 (HMSO, London, 1991); Scottish Law Commission *Recovery of Benefits Conferred Under Error of Law* (Discussion Paper No 95, September 1993). Unless otherwise stated, references hereafter to the Scottish Law Commission Discussion Paper No 95 are to Volume 1 of that paper.

<sup>3</sup> See below part II B.

<sup>4</sup> The fact situation is called "Example 2" because it is the second of three examples discussed below part IV. Example 2 is adapted from the facts of *David Securities*, above n 1. The mistake in that case was one of law.

In both scenarios, A's right to recover the payment from B should depend on a number of factors related to the parties' respective:

- states of mind when A made, and B received, the payment; and
- degrees of involvement in the mistake.

Such an approach, focusing on *factors* rather than rules, is best suited to capture the subtle competing interests in mistaken payment cases, whether the mistake is one of fact or one of law. The approach makes a classification of A's mistake as one of law or as one of fact irrelevant.

To develop a "factorial approach" of the sort just described, it is necessary to return to the most fundamental question in mistaken payment cases: should the payer recover?<sup>5</sup> The answer will be gleaned from an assessment of the overall justice instructed by consideration of the competing interests of the parties. That level of analysis avoids the terminological difficulties which surround this area of the law.

The article is structured as follows:

- Part II considers the environment in which the traditional rule has been set aside. Even if recovery is no longer precluded for mistakes of law, is the distinction between mistakes of law and mistakes of fact still relevant? The statutory provision which set aside the traditional rule in New Zealand is ambiguous. Opinion in other jurisdictions is divided.
- Part III develops an approach to mistaken payment cases founded on two competing principles: the "mistaken enrichment principle" and the "finality principle". Various factors are considered which help to assess the parties' respective states of mind and degrees of involvement in the mistake.
- Part IV applies the approach developed in part III to three fact situations. A distinction between mistakes of fact and mistakes of law is seen to be irrelevant.
- Part V discusses the use in New Zealand of the approach developed in part III.

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5 That approach ought not to be decried as unprincipled. It has its roots deep in the origins of restitution. In 1760, Lord Mansfield proclaimed that the action of *indebitatus assumpsit* (which became the action for money had and received) lay "for money which, ex aequo et bono, the defendant ought to refund": *Moses v Macferlan* (1760) 2 Burr 1005, 1012; 97 ER 676, 680. See RJ Sutton "*Kelly v Solari*: The Justification of the *Ignorantia Juris* Rule" (1966) 2 NZULR 173, 177. The same theme is evident in Lord Goff's speech in *Woolwich Equitable Building Society v IRC* [1993] AC 70, 171-172 where His Lordship considers whether "common justice" requires recovery.

## II DIFFERENT TREATMENT OF MISTAKES OF FACT AND MISTAKES OF LAW ABSENT THE TRADITIONAL RULE

### A *New Zealand: Section 94A of the Judicature Act 1908*

Section 94A was inserted into the Judicature Act in 1958.<sup>6</sup> Section 94A(1) provides:

**94A. Recovery of payments made under mistake of law** - (1) Subject to the provisions of this section, where relief in respect of any payment that has been made under mistake is sought in any Court, whether in civil proceedings or by way of defence, set off, counterclaim, or otherwise, and that relief could be granted if the mistake was wholly one of fact, that relief shall not be denied by reason only that the mistake is one of law whether or not it is in any degree also one of fact.

The ambiguity in the words "... relief ... shall not be denied *by reason only that* the mistake is one of law ..." <sup>7</sup> leaves section 94A(1) open to two possible interpretations.

First, the provision may proscribe denial of relief in cases involving a mistake of law where *any* of the reasons for denying relief hinge on a distinction between mistakes of fact and mistakes of law. When comparing two fact situations (one involving a mistake of fact and the other a mistake of law) the ability to recover in one but not the other may not depend on a distinction, however expressed, which ultimately rests on classification of the mistake as one of fact or as one of law. Under this interpretation, section 94A(1) abolishes the distinction between mistakes of fact and mistakes of law.

Secondly, section 94A(1) might mean that the fact that a mistake was one of law cannot be the *only reason* for denying recovery, although it may be one reason for doing so and although the other reasons for doing so might ultimately derive from the mistake being one of law.

Under the first interpretation, the same rules and thresholds must be applied to mistakes of law as are applied to mistakes of fact, even if certain rules are more frequently applicable to one type of mistake than the other. In contrast, the second interpretation allows (but does not require) the application of different rules or thresholds to the two types of mistake.

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<sup>6</sup> Section 2 of the Judicature Amendment Act 1958 inserted s 94A into the Judicature Act 1908. Section 94A was amended by s 11 of the Judicature Amendment Act 1985 which substituted the words "civil proceedings" for "an action or other proceeding". Section 2 of the principal Act was also amended, and now defines "civil proceedings" to mean "any proceedings in the Court other than criminal proceedings". On the applicability of s 94A to actions in the District Court, see: *Technic Holdings Ltd v Stonnell* Unreported, 14 May 1993, High Court, New Plymouth Registry, AP 15/92.

<sup>7</sup> Section 94A(1) (emphasis added).

It is submitted that the correct statutory interpretation of section 94A(1) is the second of those just given.<sup>8</sup> However it will also be submitted<sup>9</sup> that the courts should not take up the opportunity to treat mistakes of fact and mistakes of law differently. The first interpretation is preferable, but section 94A(1) must be amended to make this the correct interpretation.

The second interpretation is supported by a decision of the Court of Appeals of New York. Section 94A was modelled on section 112f of the Civil Practice Act 1920 of New York<sup>10</sup> which stated:

When relief against mistake is sought in an action or proceeding or by way of defense or counterclaim, relief shall not be denied merely because the mistake is one of law rather than one of fact.

One year before section 94A was enacted in New Zealand, section 112f was interpreted by the Court of Appeals of New York in *Mercury Machine Importing Corp v City of New York*.<sup>11</sup> The plaintiffs sought recovery of taxes paid pursuant to a New York law which was later held to be unconstitutional. In denying recovery, the Court held that:<sup>12</sup>

... the language of [section 112f] does not require that mistakes of law shall be treated in all instances as though they were mistakes of fact, but merely removes a technical obstacle against granting relief for mistake of law in any kind of a case.

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8 All five of the Commonwealth law reform bodies which have considered this area, above n 2, gave s 94A(1) the second interpretation offered in the text.

9 Below part V.

10 Section 112f of the Civil Practice Act 1920 was enacted in 1942. The section was replaced by s 3005 of the Civil Practice Law and Rules 1962, which provides: "When relief against a mistake is sought in an action or by way of defense or counterclaim, relief shall not be denied merely because the mistake is one of law rather than one of fact." See *McKinney's Consolidated Laws of New York* (West Publishing Co, St Paul, 1991) book 7B. Section 94A was modelled on s 112f: BJ Cameron "Payments Made Under Mistake - Judicature Amendment Act 1958" (1959) 35 NZLJ 4. The Justice Department file on ss 94A and 94B is now held at the National Archives: J Acc W 2304 18/1/198 "Recovery of Money Under Mistake of Law", hereafter "Draftsman's file". The file contains "Notes for use by Minister in Committal Debate" which state that the approach of s 94A "... is the same as that followed in the State of New York ...".

11 3 NY 2d 418; 165 NYS 2d 517; 144 NE 2d 400 (1957). References hereafter to *Mercury Machine* are to the case as reported in NY 2d. The interpretation given to s 112f by the Court of Appeals of New York is still good law in relation to s 3005 of the Civil Practice Law and Rules: see *McKinney's*, above n 10.

12 *Mercury Machine*, above n 11, 429. The majority judgment quoted from the Explanatory Note (quoted in the text to n 15) which had been before the legislature when the section was enacted. Two judges dissented from the majority, holding that the payments were recoverable; the legislature had "... revealed, in words as plain as possible, a design to abolish and put an end to the old artificial distinction between a mistake of law and a mistake of fact" (p 431).

This decision was apparently not considered when section 94A was drafted.<sup>13</sup> However, the New York Law Revision Commission paper<sup>14</sup> which had recommended the enactment of section 112f, was used as the basis for drafting section 94A. That paper included an Explanatory Note on section 112f which made clear that the distinction between mistakes of fact and mistakes of law was not being abolished:<sup>15</sup>

[The section's] purpose is to change the existing rule which denies relief merely because the mistake is one of law. Its purpose is not to grant relief in every case of mistake of law or to make the same rules applicable as in the case of mistake of fact. It does afford to the court, however, the power to act in appropriate cases involving a mistake of law.

The different wording of section 94A does not suggest an intention to depart from the New York approach. Although the ambiguity in section 94A(1) identified above is not considered in any of the New Zealand *travaux préparatoires*,<sup>16</sup> the evidence is unequivocal that section 112f was intended to be followed. The difference between abolition of the *traditional rule*, and abolition of the *distinction* between mistakes of fact and mistakes of law was apparently not appreciated in New Zealand. Yet the distinction is crucial. The New York provision abolished the traditional rule, but was certainly not intended to (and did not) abolish the distinction between mistakes of fact and mistakes of law. It is submitted that, on balance, Parliament must have had the same intention when enacting section 94A.

## B Other Jurisdictions

Five Commonwealth law reform bodies have recommended abolition of the traditional rule precluding recovery for mistakes of law. But opinion is divided on the relevance of the distinction between mistakes of fact and mistakes of law in an

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13 The impetus for s 94A began in 1956 (one year before *Mercury Machine*, above n 11), and there is no reference to the New York Court of Appeals decision in the Draftsman's file, above n 10.

14 New York Law Revision Commission *Act, Recommendation and Study relating to Restitution of Money Paid Under Mistake of Law* (Legislative Document No 65(B), 1942).

15 New York Law Revision Commission, above n 14, 3. The paper also stated, at p 5: "Relief may not be justified in every case involving a mistake of law, and the rules which have been developed in cases of mistake of fact may not be properly applicable in their entirety. If the maxim which precludes relief, however, is abrogated, the courts will be afforded a freedom to act which is now denied, and general rules, appropriate to cases involving a mistake of law, may be developed."

16 There was very little debate in the House of Representatives during the passage of the Judicature Amendment Bill: NZPD, vol 317, 1203, 14 August 1958; NZPD, vol 318, 1967, 23 September 1958. The Attorney-General, Hon HGR Mason, MP, spoke to the Bill when it was received by Governor-General's Message on 14 August, and on 23 September when the Bill was in Committee. The only other Member to speak to the Bill was Mr Harker, MP, who spoke during the Committee stage.

environment where the traditional rule no longer exists.<sup>17</sup> Some bodies favour the New Zealand approach, which they believe allows different treatment of the two types of mistakes. Other bodies would prefer to assimilate mistakes of fact and mistakes of law, and abolish any distinction between them.<sup>18</sup>

Goff and Jones strongly criticise the traditional rule, yet appear to support different treatment of mistakes of law and mistakes of fact.<sup>19</sup> Burrows and Arrowsmith advocate assimilation of the two types of mistake.<sup>20</sup> The *Restatement* clearly contemplates more difficulty in satisfying the "unjust" requirement when the mistake is one of law.<sup>21</sup> In *David Securities v Commonwealth Bank*<sup>22</sup> the High Court of Australia

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- 17 Whether a distinction between mistakes of fact and mistakes of law is able to be preserved after the traditional rule has been set aside will depend on the statutory language used. With respect, the Scottish Law Commission, above n 2, paras 2.96-2.107 gives the most comprehensive survey of the possible drafting options: (1) a statutory right of recovery for mistaken payments; (2) simple abrogation of the mistake of law rule, without mentioning mistake of fact (New York); (3) mistakes of law may be treated differently to mistakes of fact, and recoverability of the payment had the mistake been one of fact is necessary but may not be sufficient (New Zealand, Western Australia, New South Wales); (4) mistakes of law may be treated differently to mistakes of fact, and the courts are directed to have regard to the principles governing mistake of fact cases (British Columbia); (5) a combination of (3) and (4); (6) assimilation of error of law to error of fact (South Australia, England, Scotland).
- 18 The Law Reform Commission of British Columbia and the New South Wales Law Reform Commission both expressly favoured the New Zealand approach for the reason identified in the text: it allows different treatment of mistakes of fact and mistakes of law. Although the English and Scottish Law Commissions and the Law Reform Committee of South Australia recommended the assimilation of mistakes of fact and mistakes of law (contrary to the New Zealand approach) their reports might not be entirely consistent on this point. For example the Law Reform Committee of South Australia, above n 2, 30 stated that "... some of the reasons for denying recovery may apply *almost exclusively* to mistakes hitherto characterised as mistakes of law" (emphasis added). See also English Law Commission, above n 2, para 2.36; Scottish Law Commission, above n 2, para 2.72.
- 19 Goff and Jones, above n 1, 143-144.
- 20 S Arrowsmith "Mistake and the Role of the 'Submission to an Honest Claim'" in A Burrows (ed) *Essays on the Law of Restitution* (Clarendon Press, Oxford, 1991) 17, 36-37; S Arrowsmith "Payments and Mistakes of law" (1991) 141 New LJ 1105-1106; A Burrows *The Law of Restitution* (Butterworths, London, 1993) 118. References hereafter to Burrows are to *The Law of Restitution*. Burrows states: "[I]t is unfortunate that [Goff and Jones] regard their concept of 'a submission to an honest claim' ... as a heavy qualification where a mistake of law is in issue. They accordingly seem to pay undue deference to the decision in *Bilbie v Lumley* and do not take the straight forward principled approach of equating mistakes of law and fact."
- 21 American Law Institute *Restatement of the Law of Restitution, Quasi Contracts and Constructive Trusts* (St Paul, 1937), Chapter 2 "Mistake, Including Fraud", Introductory Note, p 28: "The rules with respect to restitution because of mistake of law have a history distinct from those with respect to mistake of fact ... and this,

stated that "... the rule precluding recovery of moneys paid under a mistake of law should be held not to form part of the law in Australia". However all members of the Court exhibited greater reluctance to award restitution where the payer's mistake was one of law.<sup>23</sup>

The thesis of this article is that a distinction between the two types of mistake becomes irrelevant under an approach which deals directly with the competing merits of the parties and relevant concerns underlying the law.

### III A MORE FLEXIBLE APPROACH TO MISTAKEN PAYMENTS: SHOULD THE PAYER RECOVER?

#### A Terminology

Mistaken payment cases will often involve a dispute over whether the payee was truly enriched by the payment.<sup>24</sup> But even where there is an enrichment, not all mistaken payments will be recoverable; there must be an "unjust" enrichment.

Some restitution theorists insist that "unjust" means no more than "recoverable" and involves no moral judgment.<sup>25</sup> That will be true in the majority of cases where recovery will be allowed or denied by analogy to established precedent. But there will also be difficult or borderline cases where, despite the appearance of detached application of the law, the decision on recovery reflects what the court considers to be

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together with a stronger policy against restitution in some situations, causes the limits of recovery to be narrower ...."

22 Above n 1, 376.

23 Above n 1. The facts of *David Securities* are essentially those of the mistake of law scenario of Example 2, above part I. Mason CJ, Deane, Toohey, Gaudron and McHugh JJ delivered a joint judgment. Dawson J delivered a brief judgment concurring with the joint judgment. Brennan J dissented on a number of points. Despite these differences, the High Court was apparently unanimous in considering that mistakes of law should be treated more onerously than mistakes of fact. Brennan J was the most explicit: above n 1, 393-394, 398-399. See also p 405 per Dawson J, and p 371 n 52, 375-376 per the joint judgment.

24 For example, a payee who gave good consideration for the payment may not have been enriched. See *Rover International Ltd v Cannon Film Sales Ltd* [1989] 1 WLR 912; *David Securities*, above n 1.

25 P Birks *An Introduction to the Law of Restitution* (Revised ed, Clarendon Press, Oxford, 1989) 19; LD Smith, "The Province of the Law of Restitution" (1992) 71 *Can Bar Rev* 672, 675-677. Contrast Goff and Jones, above n 1, 13, where the learned authors approve Lord Mansfield's statement in *Moses v Macferlan*, above n 5, 1012, that "the gist of this kind of action is, that the defendant, upon the circumstances of the case, is obliged by the ties of natural justice and equity to refund the money". RJ Sutton "Unjust Enrichment" (1982) 5 *OLR* 187, 194 emphasises the difficulty in defining "unjust" and the tension between rules, principles and justice.

the "just" result. In these difficult cases, the court will construct reasoning to reach a predetermined "just" result.<sup>26</sup>

There is an abundance of overlapping terminology available to construct a predetermined result. If recovery is to be denied, the payer may be held not to have made a mistake but rather an error of judgment, or a misprediction.<sup>27</sup> If the payer was mistaken, the mistake may not have caused her to make the payment.<sup>28</sup> Even a causative mistake does not guarantee recovery.<sup>29</sup> In all cases involving a payment made by mistake (whether of fact or of law), the payer will not recover if the payment was made "voluntarily" or "in submission to an honest claim".<sup>30</sup>

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- 26 An excellent example is the dissenting judgment of Dickson J (Laskin CJC concurring) in *Hydro Electric Commission of Township of Nepean v Ontario Hydro* (1982) 132 DLR (3d) 193, 212 where His Lordship, in considering whether there were "... any equitable reasons which preclude recovery ...", began with his conclusion: "In my view, honesty and common justice require that Ontario Hydro repay Nepean the moneys paid in the mistaken belief that Ontario Hydro had the authority to exact them". Ironically, Dickson J's careful use of the phrase "absence of any juristic reason for the enrichment" in *Pettkus v Becker* (1980) 117 DLR (3d) 257, 274 is often quoted by restitution theorists trying to understate any moral judgments implicit in actions for "unjust" enrichment. In *Woolwich*, above n 5, 172 Lord Goff stated that the payee's position "... appears to me, as a matter of common justice, to be unsustainable ...". His Lordship proceeded to consider a number of possible objections to "the simple call of justice".
- 27 A Beck and RJ Sutton, "Contractual Mistakes Act 1977" in New Zealand Law Commission *Contract Statutes Review - Report No 25* (Wellington, 1993) 127, para 2.11: "It is clear, of course, that an error in expectation or judgment as to the future prospects of a project or enterprise will not qualify as a 'mistake' ...." The learned authors cite *Clement v Walker* (1983) 1 BCR 446, 455-456. RJ Sutton, "Mistake of Law - Lifting the Lid on Pandora's Box" in JF Northey (ed) *The AG Davis Essays in Law* (Butterworths, London, 1965) 218, 222, n 13: "So if a man puts money on a horse, this is not a 'payment under mistake' in the normal acceptance of the word if the wrong horse comes in."
- 28 The test for causation is discussed below part IV C, n 102.
- 29 Aside from the "limiting principles" discussed in the text, the mistake may previously have been required to be "fundamental" for it to found recovery. That requirement seems now to be subsumed within the requirement of causation: *David Securities*, above n 1, 377-378, 395; Goff and Jones, above n 1, 107, 111.
- 30 Goff and Jones, above n 1, 50-51, 143-147; *Owen v Tate & Anor* [1975] 2 All ER 129. Goff and Jones seem to use the terms "submission to an honest claim" and "voluntariness" interchangeably. Similarly, the English Law Commission, above n 2, para 3.66 acknowledge that the meanings of "submission to an honest claim", "compromise settlement" and "waiver", and the extent to which they overlap, are unclear. "Voluntariness" is as relevant to cases involving a mistake of fact as it is to cases involving a mistake of law. For example, Robert Goff J's classic formulation of the requirements for a mistake of fact in *Barclays Bank Ltd v WJ Simms Son & Cooke (Southern) Ltd* [1980] QB 677, 695 makes clear that a causative mistake will not guarantee recovery: the payer's claim will fail if she "... intends that the payee shall have the money at all events, whether the fact be true or false, or is deemed in law so to intend". See also *McClenaghan v Bank of New Zealand* [1978] 2 NZLR

How is this terminology to be untangled?

First, "submission to an honest claim" is a most unhelpful phrase. The principle might apply regardless of whether the payment was made in response to a "claim".<sup>31</sup> The term "honest" also adds nothing. Certainly, a dishonest claim will usually guarantee recovery, but that is a distraction since it takes us outside the realm of "pure" mistake into the area of fraud. Secondly, effective analysis of restitution for mistaken payments requires looking past the terminology. The focus of this article is therefore on the overall justice and competing merits of the parties which lie behind the terminology: should the payer recover?

If the overall justice favours the payee, even though the payment appears *prima facie* to have been motivated by a causative mistake, then the enrichment is not "unjust". The court should explicitly identify the factors which lead to that conclusion. Since the boundaries between "mistake", "causation" and "voluntariness" are very fluid,<sup>32</sup> compartmentalisation of the material factors under these headings is a distraction. Having identified the reasons and factors which make the payment irrecoverable, the term "voluntary" becomes redundant.<sup>33</sup>

### B Competing Principles

The framework to be developed in this article rests on two competing principles: the "mistaken enrichment principle" and the "finality principle". The "mistaken

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528, 543; *Westpac Banking Corporation v Rae* [1992] 1 NZLR 338, 343; *Wason v Wareing* (1852) 15 Beav 151; 51 ER 494. *Wason* is discussed by Arrowsmith in Burrows (ed), above n 20, 25.

31 Thus, in *Brisbane v Dacres*, above n 1, the majority held that the payment must *be taken* to have been made pursuant to a demand, even though there had been no demand *in fact*. See also Arrowsmith in Burrows (ed), above n 20, 18.

32 For example, "[i]f the payer would have made the payment even if the mistaken fact or mistaken operation of the law had been known ..." there might be said to be no causation, or the payment might be characterised as voluntary: *David Securities*, above n 1, 395-397 per Brennan J. Similarly, P Watts, "Judicature Amendment Act 1958 - Mistaken Payments" in *Contract Statutes Review* above n 27, 187, para 4.23 considers that "mistake" does not encompass "... advertence and indifference, or advertence then payment despite knowledge that a different view of the law is held by the payee". Sutton, above n 27, 222 characterises *Brisbane v Dacres*, above n 1, as not disclosing a mistake. Such cases could equally be said to disclose "voluntariness" or to lack causation. *Maskell v Horner* [1915] 3 KB 106, 117 held that a payer who paid "in doubt as to his liability to pay" had not made a mistake. But the court might equally have held that the payer "took a chance"; the payer would have paid anyway; the mistake did not cause the payment; the payment was "voluntary".

33 P Birks "Modernising the Law of Restitution" (1993) 109 LQR 164, 167.

enrichment principle" reflects the merits of the payer's case:

- The payee is enriched<sup>34</sup> at the payer's expense.
- The payer has some ground for arguing that the payee would not be so enriched if the payer had not been mistaken. It seems "unjust" to allow the payee to retain the payment.

The assumption that the payer "has some ground for arguing" that a mistake caused the payment requires some explanation. To assume a mistake *did* cause the payment would be to prejudge the enquiry into the competing merits of the parties. That enquiry might lead to the conclusion that there was no mistake. On the other hand, proof of an enrichment alone will not satisfy the thresholds required for a balancing of interests to be undertaken; something more is required on which to base an enquiry whether the enrichment was "unjust".<sup>35</sup> It is therefore assumed to be *arguable* that a mistake caused the payment to be made.<sup>36</sup>

The "mistaken enrichment principle" must be balanced against the "finality principle", which reflects the merits of the payee's case:

- Where, immediately after the payment had been made and received, both parties thought that the transaction was complete, they each have an interest in holding the other to the transaction. The expectation of finality which the parties had at the time of payment should be protected.

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34 It will be assumed that the payee was enriched by the payment and still retains the enrichment. The assumption that the payee was enriched precludes an argument, for example, that the payee gave good consideration for the payment. The assumption that the payee still retains the enrichment precludes an argument that the payee has changed her position.

35 The "thresholds" referred to in the text are crucial to the framework which is developed in *this* article. Other frameworks do not require these "thresholds". See, for example, Sutton, above n 25. The learned author's framework (which applies throughout the law of restitution) consists of three principles: the principle of transactional integrity; the principle of security of property; and the principle of enrichment. The framework developed in this article is confined to cases involving mistaken payments.

36 The discussion in the text proceeds on the assumption that there is no longer a requirement that the payer's mistake must have led her to believe that she was liable to receive the payment (the requirement of a "liability mistake"): *Thomas v Houston Corbett & Co* [1969] NZLR 151 (CA) approved in *Barclays Bank*, above n 30, 695, per Robert Goff J; Burrows, above n 20, 95-99; Goff and Jones, above n 1, 107-112; Rae, above n 30; *KJ Davies (1976) Ltd v Bank of NSW* [1981] 1 NZLR 262; *Bank of New Zealand v Westpac Banking Corporation* (1991) 3 NZBLC 102,442. Contrast Watts, above n 32, para 4.75 citing *Weld v Dillon* (1914) 33 NZLR 1221 (CA).

The policy behind the "finality principle" is often expressed by saying that the payee has an interest in "security of receipt".<sup>37</sup> This interest is protected to some extent by the defence of change of position, which ensures that the payee who is no longer enriched is not required to make restitution.<sup>38</sup> But the payee may have "counted on" having the enrichment, although not satisfying the requirements of a change of position defence.<sup>39</sup> In these cases, a payee who retains the enrichment still has an interest in security of receipt.

Which of the two principles is to prevail? The payer must first prove the thresholds on which the "mistaken enrichment principle" is based. That establishes a presumption of recovery. The payer will then emphasise factors which support the "mistaken enrichment principle" and undermine the "finality principle". The payee will do the opposite.<sup>40</sup>

It is submitted that the decision on which principle is to prevail should depend on an assessment of the overall justice instructed by consideration of the states of mind of the parties and the factors identified below. A distinction between mistakes of fact and mistakes of law becomes irrelevant under this approach.

### C *States of Mind of the Parties*

The respective states of mind of the parties when the payment was made and received are important considerations in assessing the overall justice. The parties may each have the following states of mind:

- belief that the payment is owed;
- reckless belief that the payment is owed;

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37 English Law Commission, above n 2, para 2.20, 2.30. The sentiment was expressed by Gibbs J in *Brisbane v Dacres*, above n 1.

38 The change of position defence meets the concern that "... to order repayment would leave the original recipient in a worse position than if he had never received the money at all": *MacMillan Builders Ltd v Morningside Industries Ltd* [1986] 2 NZLR 12, 17 per Somers J considering s 311A(7) of the Companies Act 1955. In New Zealand, s 94B of the Judicature Act 1908 provides for a change of position defence. It is unclear whether the wider common law change of position defence recognised in *Lipkin Gorman (A Firm) v Karpnale Ltd* [1991] 2 AC 548 is also available in New Zealand.

39 For example, expenditure in the ordinary course of business will not give rise to a change of position defence: *Baker Timber Supplies v Apollo Building Associates (Tauranga) Society Ltd* (1990) 5 NZCLC 66,791.

40 The normal rule that the plaintiff must prove her cause of action is difficult to apply to actions for money had and received. It is not clear what are the elements of the cause of action and what are the defences to the cause of action. La Forest J said in *Air Canada v British Columbia* (1989) 59 DLR (4th) 161, 192 that the payee must prove the defence of submission to an honest claim. On the other hand, has the (plaintiff) payer proved an "unjust" enrichment if she has not proved that she did not pay in submission to an honest claim?

- doubts whether the payment is owed;
- indifference whether the payment is owed;
- belief that payment is not owed.

The higher up this list is the payer, the sounder will be the "mistaken enrichment principle"; the higher up the list is the payee, the sounder will be the "finality principle". For example, the payee's belief that the payer owed the payment would lead the payee to expect to be able to retain the payment. The case for protecting the payee's expectation is strong. If, at the other extreme, the payee believed that the payment was not owed, there is no such expectation to protect. There are a range of intermediate possibilities.

Similarly, the payer may have paid with any of the states of mind listed above. The higher up the list is the payer's state of mind, the more meritorious is the payer's case for recovery. For example, if the payer had some doubts whether the payment was owed then the case for recovery will be weaker than if the payer had a positive belief that the payment was owed to the payee.<sup>41</sup>

The first two of the states of mind involve a positive belief that the payment was owed. The label "reckless belief" refers to the possibility that the subjective belief may have been careless,<sup>42</sup> unreasonable or inexcusable. For example, a party might have believed that the payment was owed only through wilful blindness to the true facts. Such a party ought not to have the full advantage of the most favourable state of mind — not all subjective beliefs that the payment was owed will be equally favourable. Use of the word "reckless" signals the legitimacy of an objective assessment in these circumstances. In contrast, if a party had doubts, or was indifferent, then the assessment is subjective; these states of mind are less favourable than a belief (reckless or not) that the payment was owed.

In any event, there is difficulty in attaching importance to the subjective states of mind of the parties: evidence on their respective states of mind must be inferred from other evidence. It is in this context that some of the factors considered below are relevant. Where a factor is used to make inferences about a party's state of mind, then it should be remembered that the state of mind, not the factor itself, is important. Thus, a demand by the payee might evidence a belief that the payment is owed, but that inference might equally be drawn from other evidence. For example, a contractual provision may have required the payment to be made, with the result that both parties believed that the payment was due, unaware that a statute rendered the provision void.<sup>43</sup>

#### *D Factors to Consider*

The two principles are sensitive to factors which both reinforce and undermine them. In general, the "mistaken enrichment principle" will assume greater importance

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41 See below part III D 5.

42 See below part III D 6.

43 These were the facts of *David Securities*, above n 1.

the clearer the evidence of a mistake and of a causation nexus linking the mistake and the enrichment. That evidence will vary from case to case but several factors will commonly be important. The following factors will reinforce the "mistaken enrichment principle":

- the payee made a demand which misled the payer into thinking the payment was due;<sup>44</sup>
- the payee had the primary responsibility for ascertaining the true state of affairs;<sup>45</sup>
- the payer's mistake was ignorance of a "protective statute" passed for the benefit of the payer.<sup>46</sup>

On the other hand, several factors may undermine the "mistaken enrichment principle":

- the payer had the primary responsibility for ascertaining the true state of affairs;
- the payer made the payment under protest;
- the payer had doubts concerning liability to make the payment;
- the payer acted carelessly in thinking the payment to be due;
- there is insufficiently clear evidence that the payer made a mistake.

The "finality principle" will be compelling where, on receipt of the payment, the payee expected to be able to retain the payment because it was owed. The more definite the payee's expectations, the more important will be the "finality principle". As before, the evidence which might go to support this principle can take many forms, and will often be fact specific. But the following factors, which support the "finality principle", will often be relevant:

- the payer paid in response to a demand by the payee, or should be taken to have done so;<sup>47</sup>
- a long time has elapsed since the payment was made and received;

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44 This is one way in which the payee may have caused the mistake. The discussion proceeds on the assumption that the payee acted bona fide. If the payee lacked bona fides then the payer will recover. But, as explained above part III A, that takes us outside the realm of "pure" mistaken payments. In any event, the payer will only rarely be able to prove that the payee lacked bona fides.

45 A party might be held to have had the primary responsibility for ascertaining the truth because the true state of affairs was peculiarly within that party's province of knowledge, or because some inequality between the parties leads the law to place the obligation on the stronger party. In *David Securities*, above n 1, 384, the payee (the Commonwealth Bank of Australia) was in the "best position" to avoid the mistake, which would have counted against it.

46 See *Kiriri Cotton Ltd v Dewani* [1960] AC 192 per Lord Denning; *Ontario Hydro*, above n 26, 209, per Dickson J; *David Securities*, above n 1, 400 per Brennan J.

47 In *Brisbane v Dacres*, above n 1, the payee had not in fact made a demand for payment, but the Court held that the payment must be taken to have been made in submission to an honest claim by the payee.

- the payment was made by way of compromise.

Again, factors may undermine the "finality principle". In particular:

- the payer made the payment under protest;
- the payee had doubts concerning her entitlement to receive the payment;
- the payee acted carelessly in thinking the payment to be due.

1 *Demand for payment from the payee*

A demand for payment from the payee might be used to support, alternatively, the "mistaken enrichment principle" or the "finality principle".<sup>48</sup> In most cases, the demand will be taken as evidence that the payee believed the payment to be owed. The payer's payment in response<sup>49</sup> to the claim evidences that the belief was mutual. On that interpretation, the "finality principle" assumes importance because the law seeks to uphold the expectations of finality which both parties had at the time of payment. It is submitted that this is the true rationale for the maxim that, faced with a demand for payment, the payer must pay or litigate.<sup>50</sup> Faced with a demand, the payer has one of the states of mind listed above.<sup>51</sup> Unless the payer believes that the payment is owed, the payer should refuse to pay; a payment made, for example, when the payer doubts that it is owed will rarely give rise to an "unjust" enrichment.<sup>52</sup> If the payer meets the demand then the usual interpretation will be to emphasise the "finality principle" on the basis that both parties had an expectation of finality. However, the alternative interpretation is that the payee's demand induced the payer's mistake.<sup>53</sup> Now the demand will go to bolster the "mistaken enrichment principle" on the basis

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48 Contrast *Kelly v Solari*, above n 1, where Park B considered that a demand by the payee would swing the equities in favour of the payer, and *Brisbane v Dacres*, above n 1, where a bona fide (albeit *implied*) demand by the payee swung the equities in *her own* favour.

49 It is more common to refer to payment by the payer in "submission" to a claim by the payee. That language has been avoided in the text because it implies less than a positive belief as to liability by the payer. Such an inference is unjustifiably harsh on the payer; it is not warranted merely by evidence of a demand and payment. However, if evidence is available to show that the payer did submit to the payee's demand, then the payer's case is weaker; she will be further down the list of states of mind given above in part III C.

50 English Law Commission, above n 2, para 2.32; Goff and Jones, above n 1, 50-51; 143: "... a simple demand for money is legitimate pressure, which does not amount in law to duress." The maxim is traditionally justified by the need to "put an end to litigation". See *Re Carnac, ex parte Simmonds* (1885) 16 QBD 308, 312 per Lord Esher MR; *Moore v Vestry of Fulham* [1895] 1 QB 399, 402 per Lord Halsbury; *R v Tower Hamlets London Borough Council, ex parte Chetnik Developments Ltd* [1988] AC 858, 876.

51 Above part III C.

52 See below part III D 5.

53 *Chatfield v Paxton* (1799) 2 East 471 n(a); 102 ER 449 n(a). However, that case did involve *fraudulent* concealment of the true state of affairs by the defendant.

that the payee misled the payer. This second interpretation will be rarer, since, if the parties are of equal strength, the payer should not believe that a payment is owed merely because a demand is made of her.

## 2 *Primary responsibility for ascertaining the truth*

A related factor is that one party may be held to be primarily responsible for ascertaining the true state of affairs. The responsibility might derive from some inequality between the parties,<sup>54</sup> or from one party being in a better position to determine the truth. Where the payee has the primary responsibility for ascertaining the true state of affairs, then this will most likely be one of the "rare" cases just identified<sup>55</sup> where a demand for payment will be interpreted as having misled the payer. In these circumstances, the "mistaken enrichment principle" will be very compelling. If the payer was responsible for ascertaining the truth, then a belief that the payment was owed will be thought less excusable; the payer will be moved down the list of states of mind given above.<sup>56</sup> Here the "mistaken enrichment principle" will be undermined.

## 3 *Ignorance of a protective statute*

Parliament sometimes passes statutes which are intended to relieve certain persons from liabilities which they would otherwise have.<sup>57</sup> Where the payer's mistake was ignorance of such a "protective statute", the "mistaken enrichment principle" will be paramount. The payer must recover the payment in order to give effect to Parliamentary intention.<sup>58</sup> Again, this factor will often be found in conjunction with the two factors previously discussed. A statute might relieve the payer of a liability and at the same time place primary responsibility for knowing the effect of the statute

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54 P Birks "Restitution from the Executive: A Tercentenary Footnote to the Bill of Rights" in PD Finn (ed) *Essays on the Law of Restitution* (Law Book Co, Sydney, 1990) 164, 176 states that transactional inequality "... may turn out to be the very basis on which claims to recover payments made in response to ultra vires governmental demands should be rested."

55 Above part III D 1.

56 Above part III C.

57 For example, s 261 of the Income Tax Assessment Act 1936 (Cth) was passed to relieve "mortgagors" of a liability to pay tax on interest payments. It provides that contractual provisions which impose such a liability "shall be absolutely void". See *David Securities*, above n 1.

58 In *David Securities*, above n 1, 400, Brennan J stated: "Where the mistake under which the payment is made consists in the payer's ignorance of a statute which, in protection of a class of which the payer is a member, absolves the payer of the obligation to pay, the mistake of the payee who receives the payment honestly claiming it to be his due does not entitle the payee to retain it. *If it were otherwise, an honest but mistaken claim by the payee would frustrate the operation of the statute*" (emphasis added). In *Ontario Hydro*, above n 26, 209, Dickson J said: "To deprive a citizen of the benefit of a statute designed precisely for his protection solely because he is unaware of its existence is an absurdity."

on the payee. If the payee makes a demand in these circumstances, then the payer will recover a payment made in ignorance of the statute.<sup>59</sup>

#### 4 *Protest by the payer*

In some cases, the payer will make the payment under protest. Often this will be so where the payee has made a demand for payment. A protest by the payer might undermine the "mistaken enrichment principle" on the basis that it demonstrates that the payer was not really mistaken, or was at least aware of the liability being in doubt.<sup>60</sup> At the same time, however, the protest will undermine the "finality principle" since the payee's expectation of finality must have been less certain if the payee was aware that the payer disputed the liability.<sup>61</sup>

#### 5 *Doubts*

A party may doubt the validity of an obligation to pay, or right to receive, on the basis of an independent assessment of the supposed liability. Doubts may also arise because the parties openly dispute the liability.<sup>62</sup> Where the dispute is not resolved by a contract of compromise,<sup>63</sup> then doubts arising from the dispute will affect the overall justice of any subsequent action for restitution. It is not unrealistic to suppose that a payment might be made despite doubts as to liability.<sup>64</sup> A payer might make a commercial decision that the cost of litigation is incommensurate with the probability of success. This is the mid-way state of mind of those listed above.<sup>65</sup>

The existence of doubts in the mind of the payer will not necessarily bar recovery.<sup>66</sup> But if the payer's only complaint is that she gambled on the payment

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59 See the dissenting judgment of Dickson J (Laskin CJC concurring) in *Ontario Hydro*, above n 26. The majority (Estey J, Martland and Lamer JJ concurring) took a different view of the facts than Dickson J.

60 *Maskell v Horner*, above n 32. There will be some cases where a protest by the payer does not support the inference (suggested in the text) that the payer knew her liability was doubtful. Rather, the protest may simply have been that the payer considered the liability to be unfair, while fully believing it to be valid. See, for example, the following cases where the payer did not recover: *Ontario Hydro*, above n 26; *South Australian Cold Stores Ltd v Electricity Trust of South Australia* (1957) 98 CLR 65.

61 A protest made the payer's case stronger in *Mercury Machine*, above n 11, 425.

62 *American International Underwriters Ltd v Farmers' Mutual Insurance Ltd* [1993] 3 NZLR 305.

63 See below part III D 9.

64 "Notes", "Mistake of Law: A Suggested Rationale" (1931) 45 Harvard LR 336, 339: "One also pays to maintain credit or standing, to avoid social pressure, because of a feeling that in conscience [the money] is owing, or because of doubt, not as to the law, but as to the possibility of proving the facts from the available evidence."

65 See above part III C.

66 Section 10(1) of the *Restatement*, above n 21, provides: "A transferor is not precluded from restitution for mistake because, at the time of the transfer, he had

being owed, and it turns out not to have been owed, then the claim for recovery is unmeritorious; the enrichment was not "unjust".<sup>67</sup> In the framework of this article, doubts in the mind of the payer will weaken the "mistaken enrichment principle". On the other hand, the payee may have doubts concerning entitlement to receive the payment. In these circumstances, the "finality principle" will lose substance; the payee did not expect the payment to be final.

## 6 Carelessness

In English common law (but not in equity), negligence on the part of the payer is said to be irrelevant.<sup>68</sup> In *Kelly v Solari*, Parke B stated:<sup>69</sup>

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some doubt as to the facts." Burrows, above n 20, 102, notes that this avoids the crucial issue: when do doubts in the mind of the payer mean that the payer cannot be said to have made a mistake? In any event, the *Restatement* accepts that, even where the level of doubts do not preclude the finding of a mistake, "[n]evertheless, the policy against permitting one to reopen a transaction into which he has entered with a consciousness of the risk involved and the desirability of protecting the interests of contracting parties may prevent rescission and the consequent restitution" (p 40). Arrowsmith in Burrows (ed), above n 20, 38 states that: "... restitution should normally be refused whenever the payer had doubts on the issue on which he claims to [have been] mistaken at the time he paid."

67 The conclusion that doubts in the mind of the payer make the payment irrecoverable may be expressed in a number of ways. See above part III A; n 32.

68 *Kelly v Solari*, above n 1, disapproving dicta in *Milnes v Duncan* (1827) 6 B&C 671; 108 ER 598. It is submitted that *Kelly v Solari* was on the borderline of recovery. Parke B stated that money paid under a mistake of fact "... may, generally speaking, be recovered back, however careless the party paying may have been ...." But Lord Abinger CB was more equivocal, opining that the payer could *not* recover where "... although he might by investigation learn the state of facts more accurately, he declines to do so, and chooses to pay the money notwithstanding ...." Those, apparently, were not the facts of *Kelly v Solari*, since the appeal by the payer was allowed. But the policy had been marked "lapsed" by the insurer; the only "investigation" required to "learn the state of facts more accurately" was to look at the policy. Sutton, above n 27, 236 states that "... equitable relief may be barred by the claimant's own negligence, although the mere failure to make use of the means of knowledge may not have this effect". In both Scotland and South Africa, the payer's error must have been excusable. See Scottish Law Commission, above n 2, vol 2, paras 2.31 and 2.35, vol 1, para 2.106; *Willis Faber Enthoven (Pty) Ltd v Receiver of Revenue* 1992 (4) SA 202; *Rahim v Minister of Justice* 1964 (4) SA 630. I England "Restitution of Benefits Conferred Without Obligation" in *International Encyclopedia of Comparative Law* volume X: *Restitution - Unjust Enrichment and Negotiorum Gestio* (JCB Mohr, Tübingen and Martinus Nijhoff Publishers, Dordrecht, Boston, Lancaster, 1991) chapter 5, s 16, p 11, states that "[i]n most countries the claimant's initial fault may influence the extent and measure of restitution". However, it appears that this is often relevant to a change of position defence.

69 *Kelly v Solari*, above n 1, 59 (emphasis added).

... but if [the money] is paid under the impression of the truth of a fact which is untrue, it may, *generally speaking*, be recovered back, however careless the party paying may have been, in omitting to use *due diligence* to inquire into the fact.

That statement cannot be authority for the proposition that negligence is irrelevant.<sup>70</sup> The learned Baron says only that "generally speaking", failure to exercise "due diligence" is not a sufficient ground for denying the payer recovery. Thus, there may be cases in which carelessness *is* relevant. It is submitted that carelessness on the part of *both parties* to a mistaken payment should be a relevant consideration.<sup>71</sup> For example, recovery should be more difficult where the payer's belief as to liability was careless, reckless or wilfully blind.

Superficial analysis, however, is dangerous. If the payer has been careless in thinking that she is liable to make the payment, has not the payee been careless in thinking that she is entitled to receive it? Carelessness on one side will usually point to carelessness on the other side. The important question is whether one party has been more careless than the other; this is more likely to have been so where one party has the primary responsibility for ascertaining the true state of affairs.<sup>72</sup> Such an approach can easily be accommodated within the framework proposed in this article. Carelessness should be considered as one of the many factors relevant in assessing the overall justice. The weight to be attached to the factor will depend on the degree of carelessness. Like all the factors discussed in this section, carelessness will rarely, if ever, be conclusive. But it should always be considered.

The discussion in this part of the article assumes that the payee remains enriched. But in many claims for recovery of money paid by mistake, the payee will assert the change of position defence. The respective degrees of carelessness of the parties are also relevant in these circumstances. Where the enrichment has been lost, the loss

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70 Contrast Goff and Jones, above n 1, 126; PD Maddaugh and JD McCamus *The Law of Restitution* (Canada Law Book Ltd, Ontario, 1990) 211.

71 Burrows, above n 20, 103, submits that: "There may also be extreme cases where the plaintiff, while mistaken, so recklessly chooses not to investigate the true facts that he should be regarded as taking the risk of his mistake." Sutton, above n 27, 236, in discussing the jurisprudence which could develop around s 94A of the Judicature Act 1908 states: "The court may therefore formulate the principle that relief sought in respect of an error of law can be refused if the error is the result of carelessness or departure from a reasonably prudent standard by the plaintiff. The standard would, of course, vary with the circumstances - where the other party has represented the law erroneously, then little if any care might be required of the plaintiff. If it is established, such negligence might effectively prevent the claim even though the other party could not show that he had suffered any detriment." Contrast P Birks "The Recovery of Carelessly Mistaken Payments" [1972] *Current Legal Problems* 179, 198: "Carelessness neither is nor ought to be a basis for resisting recovery of money paid by mistake."

72 See above part III D 2.

must be allocated between the parties. If one party was relatively more careless, that party should bear more of the loss.<sup>73</sup>

#### 7 *Insufficiently clear evidence of a mistake*

The court must be satisfied that the payer was truly mistaken at the time of the payment. If the payer does not know more now than when the payment was made, then there was no mistake; the claim for recovery is unmeritorious if the payer has simply changed her mind. Thus, a court will be hesitant where there is insufficiently clear evidence of a mistake; a payer wishing to escape from an improvident bargain might concoct a mistake by concealing the extent of her knowledge at the time of payment. That injustice must always be guarded against.

#### 8 *Long time since payment*<sup>74</sup>

The greater the length of time that has elapsed since the payment was made, the more important will be the "finality principle" and the case for denying recovery. The payee's expectation of finality will have grown stronger over time. Also, the evidence which forms the basis of the action for recovery of the payment is likely to be less reliable if the transaction was in the distant past. Evidential difficulties will not always arise. But the law should create incentives to encourage early litigation of all claims, in the recognition that evidence will usually become less reliable over time. One such incentive is to make recovery of mistaken payments more difficult the greater the length of time that has elapsed since payment. Thus, it may be irrelevant that there is clear evidence of a mistake if there has been a long time since payment. The justice of the payer's case will sometimes be subordinated to the need for incentives in future cases.

#### 9 *Compromise payment*

Suppose *B* demands \$2000 from *A*, who responds that only \$1000 is owed. If the parties agree that *A* should pay \$1500 to settle the dispute, then that money is paid under a contract between *A* and *B*.<sup>75</sup> *A* has agreed to pay more than she believes to be owed and *B* has agreed not to sue for more than the \$1500. If *A* later discovers that

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73 In New Zealand, the statutory change of position defence (s 94B of the Judicature Act 1908) provides that "Relief ... shall be denied wholly or in part if ... in the opinion of the Court ... it is inequitable to grant relief, or to grant relief in full ...." That provision was applied in *Thomas*, above n 36, 178 where two-thirds of the loss was allocated to the payer on whom "the greater responsibility" lay.

74 The limitation period for actions for recovery of money paid by mistake is six years from the time that the plaintiff has discovered the mistake, or could with reasonable diligence have discovered it: ss 4 and 28 of the Limitation Act 1950. Goff and Jones, above n 1, 766. See also HM McLean "Limitation of Actions in Restitution" [1989] CLJ 472.

75 Arrowsmith in Burrows (ed), above n 20, 29-32; NH Andrews "Mistaken Settlements of Disputable Claims" [1989] LMCLQ 431.

less than \$1500 was owed, relief cannot be sought in the law of restitution; A must seek relief in the law of contract.<sup>76</sup> The reason is that the greater expectation interest arising from contractual relations ought to be protected by more stringent tests for relief.<sup>77</sup>

Using the framework developed above, it might be said that the "finality principle" is paramount where money is paid in compromise of a disputed claim. It should be appreciated, however, that true "compromise payments" are outside the law of restitution. The "compromise payment factor" is relevant to the framework developed above only because the parties might disagree whether there was in truth a compromise; this is an issue which will be litigated at the same time as the other factors just considered. The difference with this factor is that, if present, it is conclusive against the payer. But if there is held not to have been a compromise, the evidence of a dispute may be relevant to whether the parties had doubts about the obligation being owed.

### E Which Principle Should Prevail?

The thesis of this article is that the two competing principles articulated above (and the various states of mind and other factors which affect those principles) do not operate differently according to whether the mistake is one of fact or one of law. By dealing directly with the relevant interests, the distinction becomes irrelevant.

In contrast, the judges of the nineteenth century thought that the competing merits of the parties swung so heavily in favour of the payee when the mistake was one of law that recovery should be denied in all cases. That attitude persists amongst some judges today, although the difference in treatment is no longer thought to justify a rule precluding recovery in all cases of mistake of law.<sup>78</sup> In particular, the "finality principle" is said to be more significant where the mistake is one of law.<sup>79</sup> For example, in *David Securities*, Brennan J said:<sup>80</sup>

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76 In New Zealand, mistakes in contract formation must be dealt with under the Contractual Mistakes Act 1977. For discussion of the subtle, but crucial, interplay between the Contractual Mistakes Act and the law of Restitution see: *New Zealand Commentary on Halsbury's Laws of England* (4ed, Butterworths, Wellington, 1985) binder E, Mistake, para C2; Beck and Sutton, above n 27, para 2.17-2.21; *Marac Finance Ltd v Dyer* Unreported, 20 November 1989, High Court, Christchurch Registry, CP 160/88; *NB Hunt & Sons Ltd v Maori Trustee* [1986] 2 NZLR 641; *England v G&D Ritchie Holdings Ltd* Unreported, 28 February 1989, High Court, Wellington Registry, CP 912/88; DW McLauchlan and CEF Rickett "Contractual Mistakes and the Law of Restitution" [1989] NZ Recent Law Review 277.

77 For example, unilateral mistake is not an "operative mistake" under the Contractual Mistakes Act 1977 but is in the law of restitution.

78 See, for example, *David Securities*, above n 1, discussed briefly above part II B.

79 Scottish Law Commission, above n 2, para 2.83: "the need not to re-open settled transactions unfairly is the principal justification for the error of law rule."

80 *David Securities*, above n 1, 394 per Brennan J. The joint judgment also seemed to accept that mistakes of law and mistakes of fact should not be treated identically, but

To admit mistake of law as a ground for restitution in any case in which a mistake of fact would ground such a remedy would render many payments insecure even in cases where both parties expected the payment to be final: the uncertainty of the law and the overruling of decisions by later cases or on appeal would infect many payments with a provisional quality incompatible with orderly commerce.

And then later:<sup>81</sup>

The reason for introducing any limitation on restitution of payments made under a mistake of law should be identified: it is to achieve a degree of certainty in past transactions. Unless some limiting principle is introduced, the finality of any payment would be as uncertain as the governing law.

The danger that a mistake might be concocted is said to be more significant where the mistake is one of law. As one commentator has said:<sup>82</sup>

Too often what is said to be a mistake of law is really a misjudgment as to the expediency of risking the outcome of a lawsuit. Payment made with this chance element in mind is in the nature of a compromise or voluntary payment, and established considerations of policy prevent relief.

Thus, it is said that the scope for application of the "finality principle" is greater in relation to uncertainties in the law while mistakes of law have the greatest potential to undermine compromise payments. Moreover, it is said that the revealing of a mistake of law is more likely to give rise to a larger number of claims than is the case with a mistake of fact, thus opening the floodgates of litigation and creating administrative difficulties and commercial uncertainty. Brennan J clearly thought so:<sup>83</sup>

[W]hile mistakes of fact are specific to particular relationships, the revealing of a mistake of law in one case could throw into uncertainty the finality of payments made in a great variety of cases.

On this basis, the distinction between mistakes of fact and mistakes of law is sought to be perpetuated. It is submitted, with respect, that there is no evidence on which to found the concerns just identified. In New Zealand, where a mistake of law has been a good ground of recovery for 36 years, one might have expected at least some manifestation of these concerns. There has been none. The concerns said to be more significant for mistakes of law can be relevant in all cases of mistaken payments. Rather than attempt to deal only indirectly (and imperfectly) with the concerns, by

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unlike Brennan J, their Honours did not make explicit their reasons for that approach. See above part II B.

81 *David Securities*, above n 1, 398 per Brennan J.

82 "Notes", above n 64, 340. See also: Law Reform Commission of British Columbia, above n 2, 61; New South Wales Law Reform Commission, above n 2, para 5.24.

83 *David Securities*, above n 1, 394, per Brennan J. See also English Law Commission, above n 2, para 2.34.

focusing on a distinction between mistakes of fact and mistakes of law, it would be preferable to face the concerns directly. The framework proposed above attempts to do this; its success will now be tested by application to actual fact situations.

#### IV NO DISTINCTION SHOULD BE DRAWN BETWEEN MISTAKES OF FACT AND MISTAKES OF LAW

Three examples will be considered. Each is formulated alternatively to disclose a mistake of fact and a mistake of law. We will apply the framework developed in part III and assess whether the overall justice differs between the two scenarios.

##### A *Example 1*<sup>84</sup>

Customer *A* held a credit card account with Bank *B*. *A* cancelled the card and terminated the account on the 20th of the month. *A* received a final statement from *B* at the end of the month detailing the debits to the account since the last statement, and the "total amount due" by the due date. One of the transactions listed was a \$1000 debit in favour of *C*, dated the 21st of the month. The transaction was a monthly automatic payment (a "standing transaction") which *A* had forgotten to cancel. *B* had made payments to the various third parties to the listed transactions (including *C*) and claimed the "total amount due" personally from *A*. *A* paid *B* the amount stated as the "total amount due". Since *A* was not legally liable for transactions dated after termination of the account, *A* overpaid *B* by \$1000. *A* had been mistaken (as explained below). On discovering the truth, *A* commences an action against *B* in restitution for recovery of the \$1000 overpayment. In both scenarios, *B* received the payment unaware that it was not entitled to the \$1000 portion relating to the transaction with *C*.

Mistake of fact scenario: *A* thought that she had cancelled her card and terminated her account on the 22nd of the month, but later realises that she had done so on the 20th; her mistake was one of fact. (Assume that *A* and *B* both knew, at the time of payment, that *A* was not legally liable for transactions dated after termination of the account.)

Mistake of law scenario: *A* knew that she had cancelled her card and terminated her account on the 20th of the month, but thought that the terms of her contract with *B* made her liable for the transaction dated the 21st of the month. *A* later discovers that she was not liable for the transaction dated the 21st of the month; her mistake was one of law.

Prima facie, *A* made a mistake which caused her to overpay *B* by \$1000. Assume that *A* can prove an enrichment<sup>85</sup> and has satisfied the "threshold" requirements of a

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84 This example is adapted from a case cited in the *Annual Report of the Office of the Banking Ombudsman* (Wellington, 1992-1993).

85 There are some difficulties at the "enrichment" heading. In the normal course of events, *A* owes debts to the third parties (such as *C*), and *B* pays the third parties with *A*'s authority. (If that authority is not express in the credit card contract, then it is certainly implied.) Payment by *B* with the authority of the debtor (*A*) discharges the debt. At this point, *A* is in fact enriched, and indebted to *B*. Thus *A*'s payment to *B* discharges an obligation owed to *B*, so that *B* gives good consideration for the

cause of action in restitution for money had and received. It is then necessary to undertake a closer analysis of the competing merits of the parties.

Consider first the mistake of fact scenario. *A* had known the true facts, but had forgotten them. Does this amount to carelessness which should undermine the "mistaken enrichment principle"? It is submitted that *A*'s carelessness is a relevant consideration, but was not so gross as to preclude recovery.<sup>86</sup> *B* was also careless in making an erroneous demand and not realising that it had been overpaid. There is no evidence that *B* received the payment positively believing itself to be entitled to it. Nevertheless, there is still a good foundation for the finality principle: *B* received the payment "unaware that it was not entitled to it". However this fact must be balanced against several factors which undermine the "finality principle". The inequality between *A* (an individual) and *B* (her bank) should place on *B* the primary responsibility for ascertaining the true state of affairs. That responsibility might also be placed on *B* because it was in a better position to determine the truth: *B*'s management and accounting systems should have alerted *B* to the mistake. In light of *B* being responsible for ascertaining the truth, *B*'s erroneous (if innocent) demand for payment should be held to have misled *A*.<sup>87</sup> *B*'s carelessness also assumes more significance. The overall justice in the mistake of fact scenario favours *A*, who should recover the payment.

Minor elaborations on Example 1 do however produce some difficulty for *A*. Suppose that it is proved that *A* was "fairly sure" that she had terminated the account before the 21st, but could not find a record of the termination, and therefore decided to

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payment and is not enriched by it. However, in Example 1, *B*'s payment to *C* is without authority: *A* revoked the authority for *B* to discharge *A*'s debts when *A* cancelled the card and terminated the account. The issue then arises whether *A*'s debt to *C* is discharged by *B*'s payment. On this point there is disagreement. The traditional common law position is that the debt is not discharged unless the debtor authorises or ratifies the payment: *Barclays Bank Ltd v WJ Simms Son & Cooke (Southern) Ltd*, above n 30; approved in New Zealand in *KJ Davies v Bank of New South Wales*, above n 36. However, there is New Zealand authority that equity may discharge the debt without authorisation or ratification: *Westpac Banking Corporation v Rae*, above n 30. The traditional position at equity allows *B* to be subrogated to *C*'s position: *B Liggett (Liverpool) Ltd v Barclays Bank Ltd* [1928] 1 KB 48; *Butler v Rice* [1910] 2 Ch 277. On the consistency of *Rae* with earlier authority see: SR Scott "Mistaken Payment of Another's Debt - Is there an equitable solution?" [1993] NZ Recent Law Review 232; P Watts "Restitution" [1991] NZ Recent Law Review 419, 438; P Watts "Mistaken Payment of Another's Debt - A brief defence of the orthodox view" [1993] NZ Recent Law 248. It is assumed in the text that the debt is not discharged, so that *A* can take a restitutionary action against *B*.

86 *Kelly v Solari*, above n 1, held that a careless payer ought to be able to recover. A retrial was ordered.

87 Of course, if *A* was a powerful company, then there should not be held to be any inequality between the parties. Neither party would then be primarily responsible for the mistake, and the erroneous demand would be neutral.

pay. These facts significantly undermine the "mistaken enrichment principle". A now doubted liability and was more careless. Why did A not query the liability? It is submitted that A should not recover in this hypothetical. There is, however, great difficulty in drawing the line between recovery and non-recovery. What if it is proved that A considered whether she had terminated the account before or after the 21st of the month, but was sure that she had done so on the 22nd? Should the fact that A turned her mind to the issue preclude recovery?

Turning to the mistake of law formulation of Example 1, the prima facie position is unchanged. For the reasons outlined above, there are good foundations for both of the competing principles. But again, all the relevant factors must be considered. Whereas in the mistake of fact scenario, the means of knowing that the account was cancelled on the 20th are easily attributable to A, the means of knowing the correct law are not easily attached to A. Legal fictions such as *ignorantia juris neminem excusat* ought not to cloud an assessment of the overall justice.<sup>88</sup> Rather, the means of knowing the true state of affairs (the law) is more within B's province of knowledge. On this basis, B should again be burdened with the primary responsibility for ascertaining the truth. This would weaken the "finality principle". As in the mistake of fact scenario, it is submitted that A ought to recover the overpayment in the mistake of law scenario of Example 1.

Consider the elaborations of the mistake of fact scenario where A's mistake was one of law. What if A turned her mind to the question whether she was liable for the transaction on the 21st? In the mistake of fact scenario, it was supposed that A turned her mind to whether she had terminated the account before the 21st. Is the line between recovery and non-recovery drawn differently? It is submitted that doubts in the mind of the payer, and carelessness in her conduct, operate in exactly the same way in both scenarios. The "mistaken enrichment principle" will be weakened, but A might still win. Indeed, it is submitted that A should still recover because:

- B had the primary responsibility for ascertaining the true state of affairs (which weakens the "finality principle"); and
- B made an erroneous demand (which, in light of the previous factor, strengthens the "mistaken enrichment principle").

Example 1 demonstrates that any distinction between mistakes of fact and mistakes of law becomes irrelevant when the interests of the parties and material facts are dealt with directly. The merits of A's recovery in the mistake of fact scenario are no different to the merits of A's recovery when the mistake is one of law.

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88 B Smith "Correcting Mistakes of Law in Texas" (1931) 9 Texas Law Review 309, 326: "The question is not whether it is reasonable to expect a man actually to know the law, but whether considerations of policy compel us to treat him as if he did."

## B Example 2

The facts of Example 2 were set out in part I.<sup>89</sup> In the mistake of fact scenario, A's mistake was incorrectly calculating the amount due under the contract.<sup>90</sup> In the mistake of law scenario, A's mistake was being ignorant<sup>91</sup> of a statute which rendered a provision in the contract between A and B void. As these two mistakes are not entirely "parallel", care must be taken in analysing Example 2. In both scenarios, A is able to prove facts on which to found the "mistaken enrichment principle". The competing merits of the parties must then be considered. As in Example 1, B might be held to have had the primary responsibility for ascertaining the true state of affairs. Although there are insufficient facts to determine whether there is any inequality between A and B,<sup>92</sup> B seems to have been in the best position to know the truth. B's business is the giving of loans and the receiving of interest; the bank has greater expertise in these matters than the borrower. Thus, when B received the payments, it should have known that A had made incorrect calculations. Similarly, when B entered into the contract it should have known that the grossing-up provision would be void.<sup>93</sup> In both scenarios the "finality principle" is weakened. B cannot claim the most favourable of the states of mind listed above.<sup>94</sup> If B did believe that the payment was owed, a court will consider that belief to have been reckless.

Suppose, in the mistake of law scenario, that A paid "merely because the contract provided that it should do so".<sup>95</sup> Has A been careless in neglecting to consider the possibility that it was not legally liable? Perhaps it ought to have done so. But equally, in the mistake of fact scenario, ought not A to have correctly calculated the amount due? In *Kelly v Solari*,<sup>96</sup> which involved a mistake of fact, the insurer knew that the insurance policy had lapsed; it was written on the policy. Nevertheless, the insurer could have recovered a payment made after the policy had lapsed if the insurer had paid thinking that the policy was still valid. Ought not the insurer to have looked

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89 As noted above part I, the facts of Example 2 are based on *David Securities*, above n 1.

90 A is able to seek restitution in the mistake of fact scenario because A paid more than the contract required it to pay. The position would be otherwise if, through a mistake, the contract erroneously stated that the higher amount was due. In the latter case, A's action cannot be restitutionary; the mistake relates to contract formation. In New Zealand, mistakes in contract formation must be dealt with under the Contractual Mistakes Act 1977. See above n 76.

91 Mistakes include ignorance: *David Securities*, above n 1, 369; PH Winfield "Mistake of Law" (1943) 59 LQR 327. Contrast *NZ Refining Co Ltd v Attorney-General* (1993) 15 NZTC 10,038 where the Court of Appeal upheld the decision of an arbitrator that there was no mistake for the purposes of the Contractual Mistakes Act 1977 where "the parties never even thought about the issue of GST".

92 There is not necessarily inequality between A and B just because B is a bank.

93 In *David Securities*, above n 1, B (the Commonwealth Bank of Australia) had drafted the contract and certainly had the primary responsibility for ascertaining the truth.

94 Above part III C.

95 *David Securities*, above n 1, 405 per Dawson J.

96 Above n 1.

at the policy before it paid out? If the insurer in *Kelly v Solari* could recover, then A's error in calculating the amount due, or failure to investigate the validity of the grossing-up provision, should not preclude restitution. It is submitted that payments made on the faith of a prima facie contractual obligation, but in ignorance of the true legal position should be recoverable. Payments made where there is "... simply ... an omission to consider the relevant law ..."97 are no different from payments made where there is an omission to consider the relevant facts.

In the mistake of law scenario of Example 2, A's mistake was "ignorance of a protective statute". In these circumstances, Parliamentary sovereignty requires that the "mistaken enrichment principle" be paramount, even though that may involve undermining the expectations of the parties (as captured by the "finality principle").98 The "mistaken enrichment principle" does not have such weight in the mistake of fact scenario of Example 2. But this does not mean that "parallel" mistakes of fact and mistakes of law are being treated differently. Any apparent difference in treatment arises only because there is no mistake of fact which is "parallel" to "ignorance of a protective statute"; ignorance of a statute is always, by definition, a mistake of law. It would be perverse if the non-existence of a mistake of fact which is "parallel" to "ignorance of a protective statute" was thought inconsistent with the thesis of this article. First, there is no inconsistency. The thesis of the article is that the competing interests in mistaken payment cases should be dealt with directly, and that this approach makes a distinction between mistakes of fact and mistakes of law irrelevant. A corollary of the thesis is that "parallel" mistakes of fact and mistakes of law should be treated identically. But it will always be necessary to consider what the payer's mistake was. Where the mistake was "ignorance of a protective statute", then importance *will* attach to *this fact*. That such mistakes can be classified as mistakes of law is beside the point.

Secondly, the common law has traditionally made recovery more difficult where the mistake is one of law.99 It has just been said that importance should not attach to classification of "ignorance of a protective statute" as a mistake of law. But if that classification is given importance, then the fact that the mistake was one of law would *assist* the payer's case. It would be perverse if the special features of "ignorance of a protective statute" were used to perpetuate a distinction which generally makes the payer's case *more difficult*.

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97 *David Securities*, above n 1, 398 per Brennan J. In *David Securities*, Brennan and Dawson JJ expressed views contrary to that given in the text. Dawson J frankly admitted that under his view, there would be "relatively few" cases of mistake of law which would found recovery (p 404). It is unclear whether the High Court was unanimous on this point.

98 See above n 58.

99 See above part III E.

### C Example 3

An insurer (A) made a payment to the insured (B) for repair of the insured's building. The insurance contract only covered damage to the building arising from certain causes, and both parties understood this.

Mistake of fact scenario: A did not know how the damage to the building arose. Independent experts were engaged to assess the cause of the damage. They used the most modern methods of scientific analysis known at the time of the payment, and advised that, with a probability of 90%, the cause of the damage was X. In fact, cause X was "commonly understood" to be the cause of this type of damage. A knew that it was liable if the cause was X, and so paid out. Some time later, a new method of scientific analysis is discovered. Using this new method, it is discovered that, with a probability of 90%, the cause of the damage was Y (a cause of damage for which A was not liable).

Mistake of law scenario: A knew that the cause of the damage was Z, but was unsure whether the insurance contract covered this cause. A sought legal advice, and was told that there was some precedent on the issue. (The contract was a standard form contract, and was widely used in the industry.) The legal advice was that, with a probability of 90%, Z was a cause of damage for which A was liable. In fact, cause Z was "commonly understood" to be covered by the contract. A paid out. Some time later, an appellate court overrules the precedent on which the earlier advice had been given and holds that cause Z is not covered by the contract. The appellate court states that it is not changing the law; rather, the earlier decision had been wrong.

Assuming that B still retains the enrichment,<sup>100</sup> the difficult issues in Example 3 are all on the "unjust" side of unjust enrichment. The first difficulty (in both scenarios) is whether A should be held to have made a mistake. Having been advised that there was a 90% probability that it was liable, should A be able to recover when it transpires that A is not liable?<sup>101</sup> If the answer is yes, then what level of doubt would make the payment irrecoverable? Where it transpires that A was not liable, one might argue that A should be able to recover if, at the time of the payment, A had believed, *on the balance of probabilities*, that it was liable. That implies setting the threshold at 50%.<sup>102</sup> It is submitted, however, that some higher threshold should be required. A payer who believes that she may or may not be liable with equal probability should be encouraged to dispute the liability now.

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100 If B still retains the enrichment in some form then B cannot rely on a change of position defence.

101 If it was correct, at the time of payment, that there was a 90% probability that A was liable, then there would be a 1 in 10 chance that A was not liable. The facts of Example 3 do not disclose whether the assessment of the probability of liability at the time of payment was correct. It is submitted that the issue discussed in the text turns not on the correctness of the assessment of the probability but on the information on which A decides to pay.

102 Burrows, above n 20, 102, submits that: "... the best approach is to apply a balance of probabilities test. If the payer pays believing that the facts are *probably* not what they in truth are (ie he is 51% mistaken) he can recover for mistake: otherwise his doubts preclude restitution for mistake either on the grounds that he was not mistaken or that he took the risk of his mistake."

Example 3 demonstrates that uncertainty in relation to liability operates equivalently whether the uncertainty is of fact or of law. Assertions aside,<sup>103</sup> there is no evidence that uncertainties in the law are more common. It is therefore unsound to use the distinction between mistakes of fact and mistakes of law as a proxy for dealing directly with any uncertainty in a given case.

Putting that difficulty aside, what are the implications of the "common understanding" that *A* was liable in both scenarios of Example 3. How does this factor affect the overall justice? Take a more extreme case. Suppose, in the mistake of fact scenario, that there was unanimous agreement in the building and insurance industries that the damage was caused by *X*. One might argue that if *everyone* thought that the facts were such that *A* was liable, then *A* should not be able to recover. There is a strong case for upholding the expectations of the parties as captured by the "finality principle": when *B* received the payment, *B* believed (indeed *everyone* believed) that *B* was entitled to retain it. On the other hand, *A*'s argument is that *B* received and retains an enrichment to which it has never been entitled. This state of affairs was brought about by *A*'s mistake, and it would be unjust not to allow *A* to recover. Why should *A* be any less deserving of recovery if the mistake was widely made than if it was common to only *A* and *B*?<sup>104</sup> Are unusual or even peculiar mistakes more meritorious? An affirmative answer is counter-intuitive. Assuming *A* is to recover when the mistake is only common to *A* and *B*, then *A* ought also to recover when their mistake is shared more widely.

This discussion applies directly to the mistake of law scenario, which also discloses a "common understanding". Again take a more extreme case. Suppose that there was unanimous agreement amongst the legal community that cause *Z* was covered by the standard form insurance contract. One might again argue that if *everyone* thought that the law was such as to make *A* liable, then *A* should not be able to recover. The expectations of the parties should be paramount. On the other hand, *B* has never been entitled to the payment.

Whose argument is stronger? Does the overall justice favour *A* on the basis of the "mistaken enrichment principle" or *B* on the basis of the "finality principle"? It is submitted that payers ought to be entitled to the benefit of the true state of affairs: *A* should recover the payment. When the true facts are discovered, or the correct law is revealed, it becomes clear that *B* was never entitled to the payment. The interest in holding the parties to their contract should take precedence over a focus on what the

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103 See *David Securities*, above n 1, per Brennan J. The relevant passages are quoted above part III E.

104 *Watts*, above n 32, para 4.30: "... the fact that a claimant's error of law is widely held does not of itself seem to make that claim less meritorious than that of a person who makes an idiosyncratic error." See also the Law Reform Commission of British Columbia, above n 2, 72.

parties thought their respective rights and liabilities were, unless the contract itself can be set aside.<sup>105</sup>

Whichever principle is to prevail, it is submitted that the result should be the same in both the mistake of fact and the mistake of law scenarios. Example 3 demonstrates that the difficulties created by "common understandings" can arise in relation to both types of mistake. Section 94A(2) of the Judicature Act 1908 might be inconsistent with this submission. The effect of section 94A(2)<sup>106</sup> is that section 94A(1) will not avail the payer when the law as "commonly understood" at the time of the payment required or allowed the payment to be made, but the "common understanding" is shown later to have been wrong. Section 94A(2) would prevent A recovering in the mistake of law scenario of Example 3. But the provision does not affect the mistake of fact scenario.

In part V, it will be submitted that section 94A(2) should be repealed. If the provision remains, Example 3 demonstrates that the courts should fashion their attitude towards "common understandings" of facts by reference to section 94A(2) to achieve consistent results; the overall justice does not differ depending on whether there was a "common understanding" of fact, or a "common understanding" of law. In any event, section 94A(2) was never intended to lead to different treatment of mistakes of fact and mistakes of law.<sup>107</sup>

Before leaving Example 3, we should briefly consider the merits of A's claim. The presence of advisers might result in the party who engaged the advisers (A) being primarily responsible for ascertaining the true state of affairs. This responsibility would be reinforced if A was the stronger party. These factors would undermine the "mistaken enrichment principle". Further, it is likely on the facts of Example 3 that a long time would have elapsed between payment and the revealing of the mistake. This would bolster the "finality principle". A should not recover.

## V MISTAKES OF LAW IN NEW ZEALAND

Under the approach developed in part III, a distinction between mistakes of fact and mistakes of law becomes irrelevant. Whether that approach can be used in New Zealand depends on the interpretation given to section 94A of the Judicature Act 1908. The two possible interpretations of section 94A(1) were presented in part II A. It was submitted that the provision provides an opportunity to treat mistakes of fact and mistakes of law differently. If the courts do not take up this opportunity then the provision is consistent with the thesis of this article. One obstacle to such a judicial policy must be overcome: section 94A(2) of the Judicature Act 1908.

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105 The revealing of the true state of affairs in both scenarios may reveal a mistake in contract *formation*. See above n 76.

106 See below part V.

107 See below part V.

**94A. Recovery of payments made under mistake of law - ... (2)**

Nothing in this section shall enable relief to be given in respect of any payment made at a time when the law requires or allows, or is commonly understood to require or allow, the payment to be made or enforced, by reason only that the law is subsequently changed or shown not to have been as it was commonly understood to be at the time of the payment.

The effect of section 94A(2) is that subsection (1) will not avail the payer when *the law* as "commonly understood" at the time of the payment required or allowed the payment to be made, but that common understanding is shown later to have been wrong.<sup>108</sup> But there is no equivalent legislative provision in respect of mistakes of fact. Thus, where certain *facts* are "commonly understood" to be correct, but are later proved to be incorrect, there is no legislative direction inhibiting recovery of a payment made on the faith of the "commonly understood" facts.<sup>109</sup> The discrepancy might support an argument that section 94A(2) indicates a legislative policy that mistakes of law should be treated differently to mistakes of fact.

It is necessary to consider the motivation behind section 94A(2). The provision is directed to situations where payments have been made on the faith of a judicial decision which has stood for some time (being "commonly understood" to be correct) but which is subsequently overturned by an appellate court. When section 94A was enacted, it was heretical to suggest that judges made the law. Following the declaratory theory of law, judges were thought only to apply the law: they could not change the law. Thus, any appellate decision which overruled an earlier authority was considered to have declared what the law had always been; the earlier decision had been wrong, and any payment made on the faith of the earlier decision had been made by mistake. Notwithstanding orthodox legal thinking, the drafters of section 94A recognised that appellate courts do in many cases change the law. Where an appellate court did change the law, it would be unfair to allow recovery of money paid on the faith of the overruled decision since in reality, if not in legal theory, the payer had not been mistaken at the time of payment.

While the common law precluded recovery for all payments made under a mistake of law, the fiction of the declaratory theory could not give rise to the potential unfairness just identified. But absent the traditional rule, the concern resurfaces. The paramountcy of the declaratory theory in 1958 made the concern significant. Indeed, there is evidence that section 94A(2) was intended to do no more than make clear that

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108 Section 94A(2) does not say that, in these circumstances, there is no mistake, or that the payer cannot recover. The common law applies so that the payer must find an exception to the traditional rule precluding recovery for mistakes of law. But even if the payer falls within an exception to the traditional rule, she will not recover if her mistake has been revealed by the overruling of a judicial decision on which she had relied: *Julian v Mayor of Auckland* [1927] NZLR 453; *Henderson v Folkeston Waterworks Co* (1885) 1 TLR 329. See Goff and Jones, above n 1, 146, 148 where the learned authors support the rule denying recovery. It is submitted below that Parliament should vacate the decision in *Julian*.

109 See Example 3, above part IV C.

the payer should not recover in cases where an appellate court changed the law and overruled an earlier authority on which the payer had relied.<sup>110</sup>

If that is the full scope of section 94A(2) then the provision poses no obstacle for the thesis of this article; the provision merely overcomes an undesirable consequence of the declaratory theory of law. But it is submitted that section 94A(2) in fact has a wider scope.<sup>111</sup> The provision potentially precludes recovery not only where the appellate court changes the law, but also where the appellate court declares the earlier authority to have been wrong. The touchstone is that, at the time of the payment, the law was "commonly understood" to require or allow the payment to be made or enforced. Thus, a payment made because a judicial decision was "commonly understood" to so require is not recoverable pursuant to section 94A even if the earlier decision is declared to have been wrong.

It might be argued that the wide scope of section 94A(2) (wider than necessary to overcome difficulties flowing from the declaratory theory) reflects a reluctance to grant restitution where the mistake is one of law. To allow recovery would result in "too much restitution". It is submitted, however, that a better explanation for the "wider than necessary" scope of section 94A(2) is the difficulty in determining whether an appellate court has changed the law or declared what the law has always been.<sup>112</sup> As noted above, the distinction is crucial to the payer's ability to recover. But to the parties affected by this distinction, it would most often seem arbitrary. Under section 94A(2) there is no need to distinguish the two cases: the payer is denied recovery in both.<sup>113</sup> This motivation for section 94A(2) might still be relevant today. It might

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110 See Draftsman's file, above n 10, "Notes for use by Minister in Committal Debate" and a draft Explanatory Note which stated: "*Subclause* (2) provides in effect that where the payment has been made in reliance on the judgment of any Court, the fact that the judgment has subsequently been reversed on appeal or overruled (whether by a Court or by Parliament) will not of itself give rise to a claim for relief."

111 The meaning of "commonly understood" is unclear. Sutton, above n 27, 231 asks: "... would a single decision of first instance, or the 'better view' of a series of conflicting judgments, or a long-held opinion of a text-writer, come within those words?" Watts, above n 404, para 4.38, recommends repeal of s 94A(2) on the basis that "commonly understood" is so hard to define. That recommendation is supported below but for a different reason: the policy behind the provision no longer justifies its retention.

112 The difficulty identified in the text arises not only in relation to the common law, but also in relation to legislative interpretation. Where legislation is amended, Parliament might be clarifying what the law has always been, or changing the law. In some (rare) cases it will be difficult to distinguish these two possibilities. A draft version of s 94A(2) stated that recovery would be denied when payment had been made on the basis of a common understanding "whether the ... alteration in the understanding of the law results from statutory provision or by reason of any judgment ...." See Draftsman's file, above n 10.

113 Contrast the provision recommended by the New South Wales Law Reform Commission, above n 2, para 5.28 which contained an "objective" formula: relief "... should not be available where the benefit was conferred at a time when the law required or allowed the benefit to be conferred or enforced, by reason only that the

*appear* to be an arbitrary distinction whether an overruled authority was wrong, or whether the law has been changed.

But section 94A(2) has its cost: some deserving payers (who relied on a decision which was *wrong*) are denied recovery unjustly. Further, the original motivation for section 94A(2) is now less relevant: it is no longer heretical to say that judges make law.<sup>114</sup> Thus undeserving payers (who relied on a rule which has subsequently been *changed*) will not be able to recover with the aid of the declaratory theory. For these reasons, it is submitted that section 94A(2) ought to be repealed.<sup>115</sup>

In any event, section 94A(2) does not indicate any legislative policy that mistakes of law are to be treated more harshly than mistakes of fact.<sup>116</sup> Section 94A can therefore be interpreted consistently with the thesis of this article. Although the provision allows mistakes of law and mistakes of fact to be treated differently, there is no legislative policy in favour of different treatment. It is submitted that the courts

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law is subsequently changed." This provision, unlike s 94A(2), does not attempt to avoid the difficulty of making the distinction identified in the text. The Commission's provision may also be redundant since, at common law, there can be no recovery where there was not a mistake at the time of payment. Perhaps the provision was intended to encourage judges not to rigidly follow the declaratory theory. An earlier draft of s 94A(2) stated: "... nothing in this section shall enable relief to be given in respect of any payment made ... at time when the law is or appears to be in favour of the payee, by reason only ... (c) That the law is subsequently changed ...." See Draftsman's file, above n 10.

114 See, for example, *Woolwich*, above n 5, 176-177 per Lord Goff.

115 Contrast the reason given by Watts, above n 5, para 4.38. It may also be necessary for Parliament to vacate the decision in *Julian*, above n 108.

116 On 18 August 1994, the writer interviewed BJ Cameron, the author of a report on abolition of the traditional common law rule, prepared for the Law Revision Committee. That report may be found in the Draftsman's file, above n 10. Mr Cameron also assisted in the drafting of ss 94A and 94B. He stated that it was "certain" that there was no intention to suggest that mistakes of law *should* be treated differently to mistakes of fact. That is consistent with the interpretation of s 94A(1) adopted in part II A: mistakes of law *could* be treated differently to mistakes of fact. In explaining the motivation for s 94A(2), Mr Cameron referred to limitation periods and the principle that settled transactions should not be disturbed. With respect, since that principle can be relevant whether the mistake is one of fact or one of law, there was no need to enshrine it in section 94A(2). In contrast to the view expressed in the text, the Law Reform Commission of British Columbia, above n 2, 72, stated that: "Section 94A(2) is aimed at closing the 'floodgates of litigation' which might be opened if every overruling of a case or change in jurisprudence gave rise to restitutionary claims". Since there is no similar legislative restriction for mistakes of fact, the implication is that Parliament thought that mistakes of fact and mistakes of law should not be treated identically. See also the English Law Commission, above n 2, para 2.60; Watts, above n 32, para 4.29. If the view presented in the text is incorrect, then one might still argue that Parliament has considered the issue and established the only permissible difference in treatment of the two classes of mistake.

should choose not to draw a distinction between mistakes of fact and mistakes of law. To be sure, section 94A(1) should be amended to require this approach.

## VII CONCLUSION

This article has been concerned with the law of mistaken payments after the traditional common law rule prohibiting recovery for mistakes of law has been set aside. What is the relevance of a distinction between mistakes of fact and mistakes of law in that environment? Application of the approach to mistaken payment cases developed in part III to the fact situations in part IV demonstrates that a distinction between mistakes of fact and mistakes of law is irrelevant. Dealing directly with the competing merits of the parties removes any need to draw the distinction. In the words of the English Law Commission, it is "... difficult to envisage a situation in which it would be appropriate to grant recovery for mistake of fact but not to grant recovery in parallel circumstances where there is a mistake of law."<sup>117</sup> Jurisdictions which propose to abrogate the traditional rule by statute should draft the provision so that mistakes of law and mistakes of fact are assimilated, and the distinction is abolished.<sup>118</sup> Treating "parallel" mistakes of fact and mistakes of law equivalently is consistent with the statutory framework in New Zealand.<sup>119</sup> Ideally, however, section 94A(1) should be amended to remove the present ambiguity and proscribe drawing a distinction between the two types of mistake.<sup>120</sup>

Assessing the overall justice when money has been paid by mistake is a delicate and subtle task. A flexible approach is required. The factors which influence the competing merits of the parties should be explicitly identified and dealt with *directly*. By balancing the competing merits, the court can decide whether the payer should recover. A distinction between mistakes of fact and mistakes of law is "as a matter of common justice ... unsustainable".<sup>121</sup>

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117 English Law Commission, above n 2, para 2.52.

118 The drafting options available are considered above n 17.

119 Section 94A of the Judicature Act 1908.

120 See above n 17.

121 This was how Lord Goff described the position of the revenue in *Woolwich*, above n 5, 172.