BUDDLE FINDLAY

Legal update on litigation and dispute resolution - July 2014

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From the Law Commission

Joint and several liability

In its recently released report entitled *Liability of Multiple Defendants*, the Law Commission has recommended the retention of joint and several liability, subject to amendments to "*improve fairness for both sides, and for particular sectors where defendants may face unusual circumstances or truly excessive liability*."

The Commission considered whether the current joint and several liability regime should be abandoned in favour of an alternative regime of proportionate liability, under which each defendant in a proceeding would be liable only for the proportion of loss or damages that the Court considers is just and reasonable.

In comparing the two regimes, the Commission considered that the choice is between a risk that one defendant will bear another's liability where that other defendant does not have the means to pay their share, the plaintiff bearing that risk. Unsurprisingly, the Commission was in favour of protecting the 'innocent party' (the plaintiff), particularly in light of its finding that there was no empirical evidence to show that proportionate liability would be more economically efficient.

It is not all bad news for defendants. The Commission has recommended that:

- Courts and tribunals be granted discretion to limit the full application of joint and several liability in respect of 'minor defendants' who have limited responsibility for the plaintiff's loss and for whom it would be unduly harsh to require them to pay the full or part of an amount unpaid by another defendant
- A Court or tribunal ordering supplementary contribution should do so by ordering contributions proportionate to the shares of responsibility of each solvent party, including the applicant
- The liability of building consent authorities held liable in tort for acts and omissions relating to building consents and all related work should be capped at $300,000 for a single dwelling; $150,000 per unit in a multi-unit development; and $3m per multi-unit development, with such rates reviewed over time against appropriate indices to ensure each cap remains fair to potential plaintiffs and authorities
- The Building Act 2004 should be amended to clarify the responsibility and potential liability of building consent authorities for commercial building consents
- Auditors and audit firms conducting large or complex audits in New Zealand, should be able to participate in a capped liability scheme covering their audit work which should be based on revenue, with a $2.5m cap where income from large or complex audits is under $10m per annum, a $25m cap where income from large or complex audits is between $10m and $20m per annum and an $80m cap where income from large or complex audits is over $20m per annum. The cap will apply to all claims from contracting parties or third party investors, whether founded in contract, equity, tort, or otherwise but will not apply to liability arising from fraud, dishonesty or other intentional wrongdoing.

The next step is for the government to respond to the report.

From the Courts

How long is a piece of string - considering reasonableness in commercial contracts

Commercial contracts frequently require parties to exercise any powers conferred on them under the contract in a 'commercially reasonable manner'. The UK Court of Appeal in *Barclays Bank plc v Unicredit Bank AG* [2014] EWCA Civ 302 recently held that requiring a party to act in a commercially reasonable manner meant only that that party must act in an objectively reasonable manner, which would allow it to put its own interests ahead of those of its co-contractor.

Barclays provided Unicredit Bank credit default guarantees pursuant to which Unicredit Bank transferred certain loan credit risk to Barclays, in exchange for Barclays receiving a premium and fees. Despite a minimum term of five years, Unicredit sought Barclays' consent to terminate the guarantees under an early termination clause only two years into the arrangement. The early termination clause required Barclays' consent, which the agreement required to be determined in a commercially reasonable manner. Barclays agreed to the early termination on the basis that Unicredit Bank pay it an amount equivalent to its premium and fees for the duration of the minimum five year term of the agreement.

In holding that Barclays had acted in a commercially reasonable manner, the court considered an objective standard of reasonableness. In particular, whether the decision to grant consent on those terms was so unreasonable that no commercially reasonable person could have come to that particular decision. The court held that the decision was not commercially unreasonable, but was not prepared to provide an express test for commercial reasonableness. In the absence of such a test, the only pre-emptive remedy in commercial contracts where discretion is given to the parties is clear drafting and limited use of indistinct terminology.

Illegal provision in arbitration agreement invalidates entire agreement

The Arbitration Act 1996 (Act) provides parties to an arbitration agreement with a limited right of appeal to the High Court against an award on any *"question of law"*. The Act does not permit the inclusion in an arbitration agreement of a provision extending the right of appeal to questions of fact as well as of law. In *Carr v Galloway Cook Allan* [2014] NZSC 75, the Supreme Court recently considered whether the inclusion of such a clause in an arbitration agreement invalidated the entire agreement such that the Court could exercise its discretion under Article 34, Schedule 1 of the Act and set aside the arbitral award.

The appellants argued that the agreement lacked legal force. They considered that the Court could not sever the invalid words and that this invalidity rendered the entire agreement unenforceable.

The respondent contended that the agreement could be enforced with the invalid words severed. In the alternative, the Court's power to set aside the award is discretionary and should be exercised in the respondent's favour. The respondent also argued that as the offending provision was contained in a separate sub-clause, it did not form part of the "agreement to arbitrate".

The High Court held that the words could not be severed and therefore the whole agreement was invalid. This decision was overturned by the Court of Appeal (see our discussion of the Court of Appeal decision here), but subsequently reaffirmed by the Supreme Court.

The Supreme Court considered that the offending clause formed part of the parties' agreement to submit to arbitration. The words at issue, constituting the condition to which the agreement to arbitrate was subject, were *"so material and important a promise in the agreement to arbitrate"* that they were not severable. Accordingly, the entire arbitration agreement was invalid.

The absence of a valid arbitration agreement underpinning the award was so fundamental a defect that the High Court was correct to exercise its discretion to set aside the award.

UK Supreme Court clarifies limitation periods applicable to claims against third parties in a breach of trust

In the recent decision of *Williams v Central Bank of Nigeria* [2014] UKSC 10, the UK Supreme Court has clarified the legal definition of "constructive trustee" and when statutory time limitations will apply to third parties who have knowingly assisted a trustee in a fraudulent breach of trust.

Dr Williams claimed he was the victim of a fraud perpetrated by the Nigerian State Security Services in which he was induced to serve as a guarantor of a bogus transaction of foodstuffs into Nigeria. In connection with this transaction he paid $6.5m to Mr Gale (an English solicitor) to be held on trust. Mr Gale, in breach of that trust, paid $6m to the Central Bank of Nigeria (the Bank) and retained the remainder for himself. Dr Williams alleged that the Bank was a party to Mr Gale's fraudulent breach of trust and sought to recover the funds from the Bank as a constructive trustee.

The Bank applied to have the claim struck out under section 21(3) of the Limitation Act 1980 (UK) (Act) on the basis that it was brought outside of the six year limitation period. In response, Dr Williams argued that pursuant to section 21(1)(a) of the Act, the six year limitation period would not apply to an action by a beneficiary under a trust "in respect of" any fraud or fraudulent breach of trust to which the trustee was a party or privy.

The two issues before the Supreme Court were:

- How far dishonest assisters and knowing recipients are to be treated as trustees within the meaning of section 21(1) of the Act
- Whether section 21(1)(a) of the Act only covers actions against the trustee or also covers actions against a dishonest assister in respect of a trustee's fraud.

The Court distinguished between two categories of "constructive trustee", the first being persons who have assumed fiduciary obligations in relation to trust property without being formally appointed trustees (de facto trustees) and the second being persons who never assumed (or intended to assume) the status of trustee but have exposed themselves to equitable remedies as a result of their participation in the unlawful use of trust assets (a dishonest assister and/or knowing recipient). The Court held that de facto trustees are considered a true 'trustee' for the purposes of section 21 whereas persons in the second category are not. The Court also found that section 21(1)(a) was only concerned with actions against trustees for their own fraud (and not that of another party).

Accordingly, the Court held that the section 21(1) exclusion did not apply as the Bank fell within the second category of "constructive trustees" (and was therefore not a true 'trustee') and the fraud concerned was not that of the Bank's.

This decision will be highly persuasive in New Zealand in respect of causes of action that accrue prior to 31 December 2010 under the Limitation Act 1950 (NZ) as section 21 of the Limitation Act 1980 (UK) is effectively identical to section 21 of the Limitation Act 1950 (NZ). Accordingly, New Zealand beneficiaries seeking to bring proceedings against third parties in cases involving a breach of trust that occurred before 31 December 2010 should do so within six years of the date of breach.

Termination for material breach - beware of repudiatory breach

The recent English case of *Vivergo Fuels Ltd v Redhall Engineering Solutions Ltd* [2013] EWHC 4030 (TCC)highlights the importance of caution when seeking to terminate a contract for material breach.

The contract between Vivergo and Redhall contained a common two-stage termination process. In accordance with this process, Vivergo gave notice to Redhall that Redhall was in material breach for delaying work and failing to submit a revised programme of the project at Vivergo's request. However, Vivergo then served a termination notice before the expiration of the required rectification period and after receiving an updated programme from Redhall.

Having been banned from entering the plant, Redhall served Vivergo with a notice asserting that Vivergo was in repudiatory breach of the agreement. Redhall then purported to terminate the agreement.

The Court held that Redhall had validly rectified its material breach and it had subsequently validly terminated the agreement on the basis of Vivergo's repudiatory breach. The Court outlined two requirements when determining whether termination is lawful: the breach must be sufficiently material to justify termination and the notice of termination must be valid. Where a contract contains a two-stage termination process, care should be taken to ensure rectification of the breach has not removed the right to serve a termination notice. If such a breach no longer exists and termination is attempted anyway, the terminating party may be in repudiatory breach of contract and exposed to a claim for damages.

Promise for property made in extra-marital affair upheld by the High Court in Australia - but no presumption of reliance in equitable estoppel

In *Sidhu v Van Dyke* [2014] HCA 19 the High Court of Australia rejected the lower court's finding that, based on a line of English case law, the appellant was estopped from departing from his promise to the respondent on the basis that the respondent had the benefit of a 'presumption of reliance'.

In reliance on her partner's (the appellant's) representations that he would transfer her title to the property in which she was living, the respondent claimed that she had performed unpaid work around the property instead of pursuing full time employment and had not sought a property settlement in her divorce from her husband. The High Court held that the lower court had erred in proceeding on the presumption that the respondent had acted to her detriment in reliance on the appellant's representations, and that on the available evidence, it would be unconscionable for the appellant to resile from his previous assurances. The High Court awarded equitable compensation to the respondent in the amount to be assessed by reference to the value of the property.

The approach taken in New Zealand in regard to equitable estoppel is the same as that of the Australian High Court (and not that of the English courts). In the recent decision in *Rudyard Holdings Limited v Kiwibank Ltd* [2014] NZHC 1253, the High Court

confirmed that the onus of establishing detrimental reliance is placed on the plaintiff seeking the remedy, and not upon the defendant.

Misrepresentation in pre-contractual negotiations

The English Supreme Court has recently articulated the position on negligent misrepresentation in pre-contractual negotiations.

In *Cramaso LLP v Ogilvie-Grant* [2014] UKSC 9, an owner of land entered into negotiation with a prospective tenant. The owner sent an email containing information incorrectly estimating the size of the population of game birds on the land. The prospective tenant then set up Cramaso LLP to enter into a contract with the owner. Cramaso LLP then contracted with the owner to lease the land, for the purpose of commercial shooting of game birds.

The court held that the inaccurate estimate of the size of the game population was a negligent misrepresentation. The representation remained operative in the mind of the prospective tenant, even though the comments were made before Cramaso LLP was incorporated and formed part of pre-contractual negotiations. As an agent of Cramaso LLP, it was foreseeable that the representation would induce Cramaso LLP to enter into the contract. A positive obligation remained on the owner to ensure the accuracy of his continuing representation.

The owner could have better protected his position by:

- Drawing a line and starting afresh after Cramaso LLP was formed
- Issuing a disclaimer in case the estimate of the game bird population proved to be incorrect.

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