

## Legal update on litigation and dispute resolution - June 2013

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### Put it in writing: The risks of oral agreements to lease

Section 24 of the Property Law Act 2007 provides that in order to be enforceable, a lease of land must be in writing and signed by the party against whom it is to be enforced. However, an exception to this rule arises where an oral agreement to lease has been the subject of "part performance".

The High Court has recently considered the doctrine of part performance in *Dunroamin Nurseries Ltd v Zealandia Horticulture Ltd* [2013] NZHC 1074. In that case, a draft deed of lease existed but a final version was never signed. Notwithstanding this, the lessee occupied the premises and paid rent to the lessor. After three years, it sought to terminate the lease, alleging that it had never agreed to the terms of the draft deed. The lessor asked the High Court to enforce the lease.

The Court agreed to do so, on the basis that the threefold test for part performance had been met. In particular:

- There was a sufficient oral contract. An offer to lease was made by the lessor when it handed over the draft deed of lease. While there was no express acceptance, it could be inferred from the lessor's failure to put forward a counter-offer, its taking over of the premises and its payment of rent
- The taking of possession, issuing of invoices and receipt of rent were sufficient acts of part performance, consistent with the contract alleged by the lessor
- It was not unconscionable for the lessor to rely on the part performance. The relevant circumstances by which unconscionability is to be judged are those at the time of the part performance (not those existing later). The lessor had acted in good faith and had taken a number of steps in reliance on the existence of a lease, including the erection of a building and the financing of it.

The case serves as a cautionary tale for parties whose lease agreements are oral only. It confirms the real risk that, where a lease is not contained in a signed document, it may not be enforceable. Moreover, even if a Court does order its enforcement, that enforcement may be on different terms than those which a party had understood to apply.

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### Competitor's product as inspiration

In *Oraka Technologies Limited v Geostel Vision Limited* [2013] NZCA 111, the Court of Appeal has provided further guidance as to the principles applicable to claims of copyright infringement.

In its judgment, the Court confirmed the continued applicability of the well-known "*Wham-O*" test, which requires a plaintiff to establish that: (a) the defendant has reproduced the entire copyright work or a substantial part of it; (b) there is sufficient objective similarity between the infringing work and the copyright work, or a substantial part thereof; and (c) there is a causal connection between the copyright work and the infringing work.

In the present case, the Court held that there was sufficient objective similarity between the defendants' product (a cup assembly for an asparagus grading machine) and the plaintiff's copyright works to merit a consideration of the remaining two steps.

As to causal connection, in most cases, copying can be deduced by inference. However, this was an unusual case, in that there was direct evidence of copying. In particular, notes and diagrams made it clear that the defendants' design path began with the plaintiff's works and there was evidence that the defendants had suggested that problems with the design be resolved by reference to solutions found in those works.

Significantly, the Court also held that it was appropriate to draw a negative inference from the defendants' failure to call evidence from the only person who knew whether or not reference was made to certain material during the design process, particularly given the speed with which the defendants' design was produced.

As to the question of substantiality, the Court noted that it is wrong to jump to the conclusion that a substantial part has been taken just because copying has occurred. The quality of what has been taken is much more significant than the quantity, what is or is not 'substantial' is closely associated with how original the work at issue is, and functional constraints may assist in determining both originality and substantiality.

Applying these principles to the case before it, the Court found that the defendants had copied a substantial part of the copyright works. In particular, it disagreed with the defendants that many of the constraints they relied on to explain the similarities were truly functional.

The Court of Appeal's judgment highlights the risk for businesses in using competitors' products as the basis for their own designs. While doing so will not automatically result in copyright infringement, it will increase the risks of claims of this nature, particularly if the features focused on are highly original.

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## Bailment vs lease - the difference may matter

An arrangement that looks like a lease will not always amount to one. Sometimes, it may be a mere bailment. This distinction may be significant for various reasons, including the issue of how much notice must be given to terminate the arrangement.

In *Acernus Aero Limited v Vincent Aviation Limited* [2013] NZHC 595, the parties agreed that, in consideration for a monthly fee, the defendant would store the plaintiff's aircraft in a hangar it leased, and add the aircraft to its Air Operators Certificate. After a dispute the defendant purported to terminate the arrangement summarily (although it had given a seven day notice of termination a month and half earlier).

The plaintiff sued the defendant on a number of grounds, most relevantly on the basis that it had not given reasonable notice of termination. It argued that the parties had entered into a sub-lease or licence. As, under section 245 of the Property Law Act 2007, the notice period implied into leases and licences is 10 clear working days where termination is due to non-payment, insufficient notice had been given.

The Court rejected the argument that the arrangement was a lease, as it had none of the essential elements of such a contract. In particular:

- There was no certainty of premises. No precise area of the hangar could be assigned to the space that the aircraft occupied
- The plaintiff did not have exclusive possession of any part of the hangar. The defendant was free to move the aircraft as it saw fit
- There was no certainty of commencement date or term.

The Court also found that no licence was in place. Under a licence, the licensor assumes no obligation to the licensee for the care of an item that the licensee brings onto the land. By contrast, the plaintiff had asked that the aircraft be stored in the plaintiff's facility and care, which is what happened. The plaintiff took responsibility for the aircraft, and maintained insurance.

Against this background, the Court held that the arrangement was a mere bailment. As such, there was no statutory notice period necessary before termination. Rather, 'reasonable' notice was required and had been given.

The High Court's decision underlines that it is prudent to document commercial arrangements, particularly in relation to the use of land, in clear and certain written terms.

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## The devil is in the detail: Multi-tiered dispute resolution clauses must be certain and specific

It is common for major commercial contracts to contain 'staged' dispute resolution clauses, culminating in the issue of court or arbitration proceedings as a final step. The English High Court has recently provided guidance as to the extent to which parties are bound to follow the preliminary, 'conciliatory' steps in such clauses, before seeking relief from a court or arbitrator.

In *Tang v Grant Thornton International & Ors* [2012] EWHC 3198 (Ch), the contract between the parties provided for two steps to be taken before either of them was able to refer a dispute to arbitration (Preliminary Steps).

After a dispute arose, the Chief Executive recused himself from attempting to resolve it, meaning that step one of the Preliminary Steps was not fulfilled. Moreover, as no board members put themselves forward to act as the panel, the panel contemplated by step two was not constituted. After the defendants referred the dispute to arbitration, the plaintiffs claimed that the Preliminary Steps were conditions precedent to arbitration and that, as they had not been fulfilled, the arbitral tribunal had no jurisdiction to determine the dispute. The tribunal disagreed and the plaintiffs appealed to the High Court.

The Court upheld the tribunal's jurisdiction, holding that the relevant test as to whether a clause such as those setting out the Preliminary Steps ought to be given legal effect is:

- Whether the provision prescribes without the need for further agreement a sufficiently certain and unequivocal commitment to commence a process
- From which may be discerned what steps each party is required to take to put the process in place
- And which is sufficiently clearly defined to enable the court to determine objectively:
  - what under that process is the minimum required of the parties to the dispute in terms of their participation in it; and
  - when or how the process will be exhausted or properly terminable without breach.

Applying those principles to the case before it, the Court found that the Preliminary Steps were not a condition precedent to arbitration. In particular:

- The relevant clause was too nebulous in terms of the process and too equivocal in terms of content. In particular, there was no guidance as to the quality or nature of the attempts to be made to resolve a dispute or difference
- The two month 'delay' period referred to in the clause should not be interpreted as a permanent bar on commencing arbitration if no panel was established, or seized of the dispute
- It was unrealistic to contend that if no panel was constituted, no arbitration could be commenced, even long after the request for conciliation would have been required to be referred to the second stage.

While decisions of the English High Court are not binding in New Zealand, this judgment is relevant to those involved in drafting dispute resolution clauses in this country. It reinforces that if multi-tiered clauses are to have teeth, they must be expressed unequivocally and in sufficient detail to enable a Court to enforce them without having to 'fill in the gaps'. This will mean specifying not only timeframes, but also clear and detailed procedures.

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## Honesty and reasonableness may excuse breach of trust

In the recent decision of *Santander UK Plc v RA Legal Solicitors (a firm)* [2013] EWHC 1380 (QB), the Court of Appeal of England and Wales considered the liability of solicitors who had released their client's funds in respect of a fraudulent mortgage transaction, without knowledge of the fraud.

The client bank, Santander UK Plc, had agreed to lend to its borrower to purchase a house. Santander released the funds to its lawyers, RA Legal, which then paid them out to the vendor's solicitors. However, as those solicitors were fraudulent, Santander never obtained its charge over the property.

RA Legal denied the claim of breach of trust by Santander and also argued that even if a breach had occurred, they were entitled to the protection of section 61 of the Trustee Act 1925, which protects trustees who have acted "*honestly and reasonably, and ought fairly to be excused for the breach of trust*".

The Court of Appeal found that RA Legal had acted in breach of trust. However, notwithstanding the breach of trust, RA Legal were entitled to the protection of section 61. This was for the following reasons:

- There was no dispute that they had acted honestly and without knowledge of the fraud
- They had also acted reasonably. Acting reasonably does not require compliance with best practice in all respects. The standard is reasonableness and not perfection. While criticisms could be made of RA Legal's conduct, none of those criticisms were connected with Santander's loss and nor did they amount to such a departure from ordinary and proper standards so as to deny RA Legal relief
- It was fair to excuse RA Legal's breach of trust or to grant them relief from all liability for it. The law generally leans towards confining the responsibility of professional people to a duty to take reasonable care for their liability for breach of duty and does not readily impose on them responsibility for loss resulting from the fraud of others.

Section 61 is similar in nature to section 73 of New Zealand's own Trustee Act 1956 which grants the Court the power to relieve a trustee from personal liability for breach of trust where s/he has acted honestly and reasonably, and ought fairly to be excused for the breach of trust and for his/her failure to obtain directions from the Court. As such, the decision is likely to be as welcome to trustees in New Zealand as to their counterparts in England.

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## Arbitration clauses can pre-empt foreign court proceedings

The recent English Supreme Court decision of *Ust-Kamenogorsk Hydropower Plant JSC (Appellant) v AES Ust-Kamenogorsk Hydropower Plant LLP (Respondent)* [2013] UKSC 35 has confirmed that the English courts have jurisdiction to injunct foreign proceedings that are in breach of an arbitration agreement, even when no arbitration has commenced or is contemplated.

The case arose as a result of the issue of court proceedings in Kazakhstan by one of the parties to a concession agreement. The English Commercial Court granted an interim anti-suit injunction restraining those proceedings, on the basis of an arbitration clause in the agreement. Although the Kazakh proceedings were withdrawn, the applicant remained concerned that further action would be taken in the Kazakh Courts and sought and received a final injunction.

The Supreme Court upheld the injunction, holding that an arbitration agreement gives rise to a 'negative obligation', whereby both parties promise not to commence proceedings other than in the forum specified in the agreement. Independently of the English Arbitration Act 1996 the Courts have an inherent power to declare rights and enforce this 'negative obligation' by injuncting foreign proceedings brought in breach of an arbitration agreement even when arbitration is not on foot or contemplated.

In the New Zealand context, this decision has two practical implications:

- The English courts may issue anti-suit injunctions against New Zealand legal proceedings, where an English law agreement provides that the dispute which is the subject of those proceedings is to be arbitrated, even if no arbitration is contemplated or on foot by the other party.
- The New Zealand courts have the power to stay court proceedings where the parties have agreed to arbitrate their disputes. Therefore, they may look to the decision for guidance as to how to deal with foreign proceedings brought in contravention of a New Zealand law arbitration agreement. Of course if they were to grant an injunction, its effectiveness would depend on whether a foreign court and the other party would abide by the orders of the New Zealand courts.

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## Malicious prosecution applies to civil as well as criminal proceedings

In the recent case of *Crawford Adjusters & Ors v Sagikor General Insurance (Cayman) Ltd & Anor (Cayman Islands)* [2013] UKPC 17 the Privy Council has confirmed that the tort of malicious prosecution applies to civil as well as criminal proceedings.

The decision arose out of legal proceedings brought by a company against a loss-adjuster employee. The claim arose because a vice-president of the company, with a grudge against the employee, had hired an independent loss adjuster to review the employee's work but restricted the independent adjuster's access to certain information. As a result, the independent adjuster's reports were skewed against the employee. The legal proceedings caused him considerable loss.

Days before the trial, the company discontinued its action and judgment was awarded in favour of the employee, who then amended his counter-claim to include malicious prosecution and abuse of process. However, the Cayman Islands Court of Appeal held that the current state of the law was such that the tort of malicious prosecution applied only to criminal proceedings.

The majority of the Privy Council disagreed, holding that the reasoning that limited the application of the tort in respect of civil proceedings was no longer valid. In reaching this view, Lord Wilson JSC referred to the New Zealand decision of *Rawlinson v Purnell Jenkinson & Roscoe* [1999] 1 NZLR 479. In that case, the High Court had dismissed the plaintiff's claim as there was no 'malice' to the defendant's actions. However, it accepted that a malicious prosecution claim relating to civil proceedings should not be dismissed ex ante, although it noted that the issue could only be resolved by the appropriate appellate Courts.

Against this background, the *Sagikor* decision will be of interest to the New Zealand courts and may signal a new direction for malicious prosecution claims in this country.

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