Carter Newell LAWYERS

Professional and Management Liability Gazette

1st edition

Carter Newell LAWYERS

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Contents

From the CEO

Carter Newell is delighted to launch its latest publication – the *Professional and Management Liability Gazette*. Joining our extensive suite of publications compiled to assist our clients in their daily operations, this Gazette is designed to provide the insurance industry with a synopsis of practical and noteworthy cases concerning liability of professionals and includes those that would be covered under Professional Liability, Directors' & Officers' and Management Liability policies.

This Gazette contains recent decisions considered by the courts. This inaugural edition focuses on decisions in the professional sphere of financial advisors and accountants, solicitors and barristers, directors and brokers, and also considers cases relating to policy interpretation, damages and procedure. Of particular note is the recent Queensland Supreme Court decision of *Invion Limited v SGB Jones Pty Ltd & Ors* [2014] QSC 97, in which Carter Newell successfully defended a disputed claim for indemnity under a Directors' & Officers' policy.

As a 'premier' legal service provider with one of the largest insurance practices in Australia, we trust our inaugural *Professional and Management Liability Gazette* will be a useful guide for our readers.

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Case Note

Boorer v HLB Mann Judd (NSW) Pty Ltd [2014] NSWCA 100

Accountant's role in the disqualification by ASIC of company directors.

The facts

The appellant, Mr Boorer was, along with his son, the director of an unlisted public company, Techontap International Ltd (**Techontap**). Techontap engaged the respondent, HLB Mann Judd (NSW) Pty Ltd (**HLB**) to (amongst other things) prepare and lodge forms with ASIC from time to time.

Mr Boorer invited Mr Leonard King and Mr Brett King (**the Kings**) to become directors of Techontap, with Leonard King as company secretary. Mr Boorer told Ms Mariana von-Lucken of HLB that the Kings and a Mr Walter Adamson consented to their respective appointments. Ms von-Lucken subsequently prepared, and Mr Boorer signed, a Form 484 notifying ASIC of Mr Adamson's and the Kings' appointments as directors and Leonard King's appointment as secretary.

Under s 201D(1) of the *Corporations Act 2001* (Cth) (**Act**) a company must first obtain a person's signed consent prior to appointing them as director. Despite this, HLB lodged the Form 484 with ASIC notifying of the appointments having only received the signed consent of Mr Adamson. ASIC's records were subsequently updated to reflect the appointments. The Kings never provided written consents to being appointed.

Techontap was wound up in December 2005. Prior to Techontap's failure, Mr Boorer had been a director of two companies to which a liquidator had been appointed. ASIC disqualified Mr Boorer from managing corporations without the leave of ASIC for two years, partly due to the finding that the misleading Form 484 was lodged by HLB on Mr Boorer's instructions. However, there were other grounds relied upon for the disqualification order.

On review, the Administrative Appeals Tribunal (**AAT**) set aside ASIC's decision and replaced it with a decision that Mr Boorer's disqualification period be reduced to one year. The AAT found the error was on the part of HLB in the lodgement of the Form 484 and that there was no blameworthy conduct on Mr Boorer's part. The AAT's decision was made almost two years after ASIC's decision, so Mr Boorer had still effectively served his two year disqualification.

Mr Boorer claimed for breach of duty against HLB regarding the lodgement of the Form 484 and also in relation to HLB's alleged failure to warn him that he might have been trading while insolvent. In relation to the Form 484 issue, Mr Boorer alleged that the disqualification had damaged his reputation and that his income had been adversely affected. He claimed damages for that alleged loss.

Issues

- Whether there had been *'a substantial wrong or miscarriage'* under r 51.53(1) of the *Uniform Civil Procedure Rules 2005* (NSW).
- Whether HLB owed (or breached) a common law duty of care to Mr Boorer.
- Whether Mr Boorer had suffered any loss.

Decision

At first instance

The trial judge dismissed both claims against HLB, finding that there was no breach of a duty of care at common law in respect of both strands of Mr Boorer's case. Her Honour also found that if there had been a breach of duty in either respect, the breach caused no loss.

In relation to the Form 484 issue, the trial judge found that:

- there had been no breach of HLB's duty of care in the circumstances as HLB had followed Mr Boorer's instructions in lodging the Form 484;
- Mr Boorer would still have been disqualified for one year as the AAT (who found in Mr Boorer's favour on the Form 484 issue) decided this was the appropriate length of disqualification given the nature of Mr Boorer's other conduct. Mr Boorer adduced no evidence to show that he was denied income by reason of his effectively being disqualified for an additional year due to ASIC's decision; and
- ASIC's finding on the Form 484 issue would effect the plaintiff's reputation for honesty and integrity. However, Mr Boorer had not demonstrated that he had lost income as result.

On appeal

Mr Boorer appealed to the NSW Court of Appeal, who unanimously upheld the trial judge's decision. The Court of Appeal refused Mr Boorer leave to contest the trial judge's findings on the insolvent trading point for a procedural issue. Further, it unanimously upheld the trial judge's decision in relation to the Form 484 issue.

In relation to the trial judge's finding that no damages were proven to flow from HLB's alleged breach, Leeming JA found that:

- if Mr Boorer's income were dependent upon his being able to be a company director, the additional year's disqualification would matter. However, Mr Boorer provided no evidence that he was denied income by reason of his being disqualified for an additional year;
- the fact of the disqualification, rather than its length or the reasons for it, was critical to Mr Boorer's reputation and Mr Boorer would have been disqualified whether or not the Form 484 was erroneously lodged; and
- no evidence was lead by Mr Boorer to contest the trial judge's finding that his work was not affected by the disqualification.

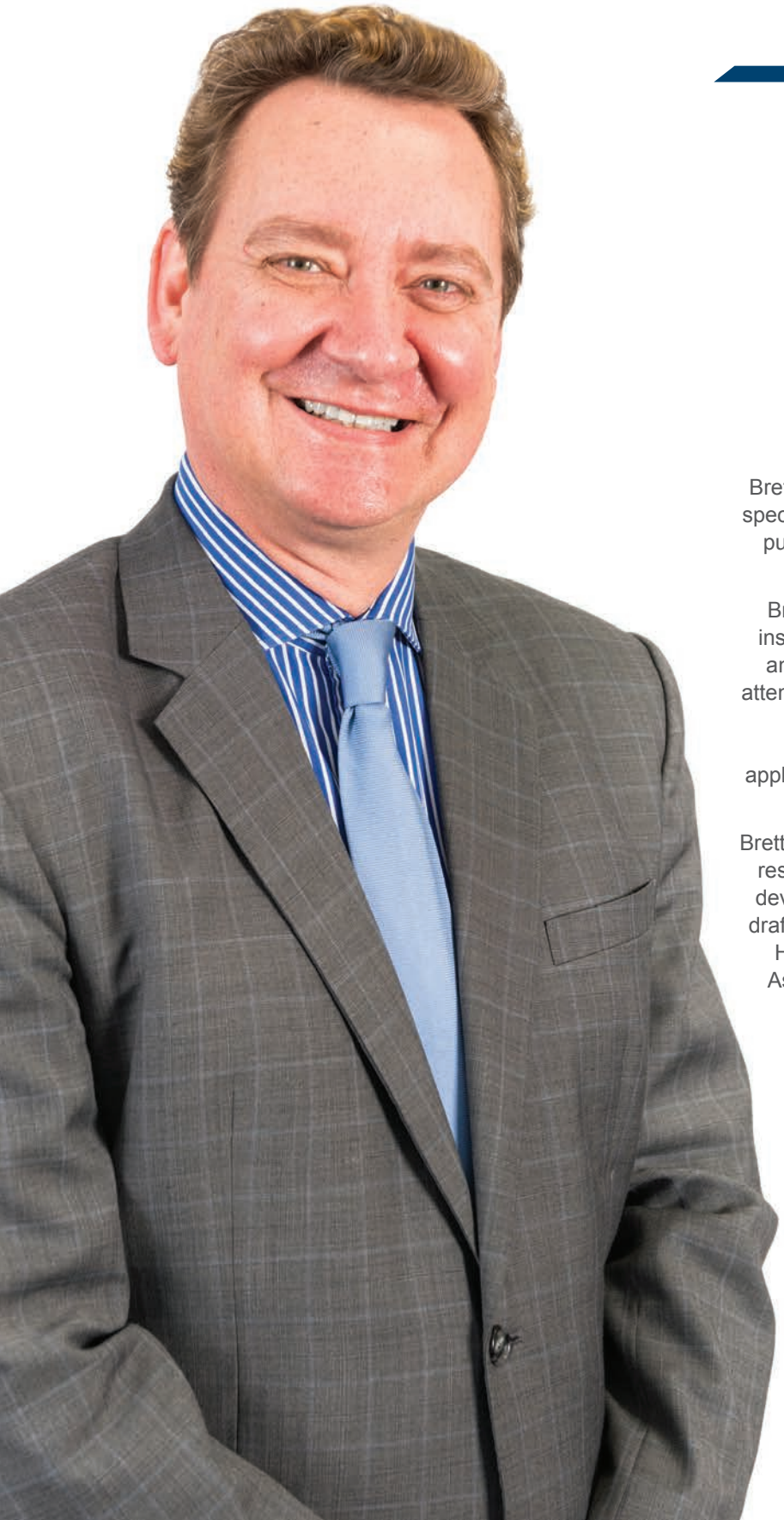
Leeming JA went on to consider a number of other matters the subject of the appeal and provided some interesting commentary in relation to the trial judge's finding that there was no breach of duty in the circumstances where Ms von-Lucken followed Mr Boorer's instructions.

In disagreeing with the trial judge's conclusion, Leeming JA observed that it was obvious that Ms von-Lucken was in breach of the Act in lodging the Form 484 knowing that written consents for two of the directors and the secretary had not been obtained.

Leeming JA stated that:

- if Ms von-Lucken believed that Mr Boorer was aware of the parts of the Act that would be breached by lodging the Form 484 and he nevertheless instructed her to do so, then while she would still be in breach of the Act, she would not be liable to him for breach of a duty at common law; and
- where, however, it was clear to Ms von-Lucken that Mr Boorer was ignorant of the obligations imposed under the Act, Leeming JA *'would not lightly accept'* that merely following Mr Boorer's instructions discharged her common law duty of care to duty him. Indeed, one of the reasons Techontap engaged HLB was to take reasonable care to ensure compliance with the Act.

Despite the above comments, it was not necessary to explore the breach of duty issue further given that no loss was found to flow from it.



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Brett Heath acts for a range of professionals, specialising in professional liability, large scale public liability and construction claims and directors' and officers' claims.

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Case Note

Razdan v Westpac Banking Corporation [2014] NSWCA 126

Misrepresentation by a bank officer about the point at which there would be a margin call, reliance, equitable remedies.

The facts

Mr Razden had margin loan with the Westpac Banking Corporation (**Bank**), secured by a share portfolio.

The Bank had a system that tracked the value of the share portfolio, and required Mr Razden to take certain action if the value of the portfolio dropped below a certain point (i.e. by repaying some of the loan or providing additional security), failing which the Bank was conferred the power to sell the shares.

In 2008, the global financial crisis significantly diminished the value of Mr Razden's portfolio, and the Bank issued a margin call. During this period, Mr Razden had numerous teleconferences with officers of the Bank, who were attempting to assist him manage his facility through the extraordinary circumstances of the global financial crisis. All of these conversations were recorded.

During one such conversation on 7 October 2008, an officer of the Bank made a statement to the effect that the Bank would sell his portfolio in the event that the gearing, being the loan balance to security value ratio, reached 95% (**95% representation**). This statement was not factually accurate. Over the next few days, Mr Razden sold a number of small share sales attempting to keep his facility afloat.

However, the market continued to fall and a short time later, the Bank sold down Mr Razden's portfolio. Mr Razden was unable to repay the outstanding amount of the loan and the Bank commenced proceedings against him. Mr Razden counterclaimed based on the 95% representation.

In essence, Mr Razden alleged that he acted in reliance upon the belief that the Bank would force sell when the gearing ratio reached 95%. By relying on the alleged representation, Mr Razden argued that he was denied the opportunity to sell more shares at an earlier juncture.

Mr Razden originally pleaded reliance upon a so-called 90% misrepresentation (as opposed to 95%). He had mistakenly pleaded the incorrect percentage of what was actually said by the Bank's officer.

Mr Razden attempted to amend his affidavit evidence during his evidence-in-chief, having reviewed the tape recordings of the conversations. This was highly prejudicial to his case, as it put in doubt whether Mr Razden could have relied upon the alleged

representation, given he could not even recall what was actually said.

At first instance, the Bank was successful in obtaining judgment. Mr Razden appealed.

Issues

- Whether an oral (and untrue) representation about the point at which there would be a margin call was a misleading representation about a future matter in contravention of s 51A of the former *Trade Practices Act 1974* (Cth) (**TPA**).
- Whether there was reliance on the misrepresentation.
- Whether other equitable remedies were available.

Decision

The Court of Appeal unanimously dismissed the appeal on all grounds.

Misrepresentation

Interestingly, the Court of Appeal came to different conclusions as to whether the 95% representation was in fact a misleading representation as to a future matter within the ambit of s 51A of the TPA.

The leading judgment of Bergin CJ concluded that the 95% representation was a representation as to a future matter, and was in the circumstances taken to be misleading. The Bank alleged that there were reasonable grounds for making the statement, as it was made within a context where Mr Razden had commonly been subject to margin calls.

Further, it was suggested that the Bank's officer was trying desperately to assist Mr Razden in holding off the intervention of another department of the Bank, who was responsible for effecting the forced sale. Bergin CJ disagreed and concluded that there were no reasonable grounds for making the statement.

Macfarlan JA and McColl JA, on the other hand, found that the statement was not calculated to induce Mr Razden's reliance, and it was accepted that there was nothing promissory or cast-iron about the statement. Indeed, it was *'a passing, spontaneous prediction made in the flow of one of many discussions.'*

'The majority found that the statement was not calculated to induce Mr Razden's reliance, and it was accepted that there was nothing promissory or cast-iron about the statement.'

In any case, the majority agreed that Mr Razden had not relied upon the statement. Aside from his incorrect recollection of the particulars of the statement, it was also significant that Mr Razden made no further mention of the statement after it was made in his dealings with the Bank. Indeed, one week later during another conversation with the same bank officer, the officer said words to the effect that if the gearing ratio gets close to 100%, the bank would force sell.

The Court of Appeal observed that if Mr Razden had relied upon the 95% representation, he would undoubtedly have raised the issue in protest during this later conversation.

Estoppel

The Court of Appeal affirmed the findings of the trial judge that the 95% representation was not the kind of assertion which could found an estoppel. Further, and consistently with the findings on misrepresentation, there was no evidence of reliance.

Breach of an implied term and unconscionable conduct

Mr Razden alleged that there was an implied term of reasonableness and good faith in the Bank's margin lending facility. On the assumption that there was an implied term of reasonableness, Bergin CJ observed that there was no evidence that the Bank acted unreasonably or not in good faith and that the events took place within the extraordinary circumstances of significant falls in global financial markets. Indeed, Her Honour observed:

> *'There was overwhelming evidence that far from acting unreasonably or conducting itself with a lack of good faith, the bank tried to assist the appellant to retain his portfolio in the hope of the market turning around.'*

Insofar as Mr Razden alleged unconscionable conduct on the part of the Bank, Bergin CJ observed that the Bank had in fact provided detailed and up to date information, often suggesting to him that he seek independent advice.

Case Note

Financial Ombudsman Services Ltd v Pioneer Credit Acquisition Services Pty Ltd [2014] VSC 172

Consideration of contract terms (implied and express) between Financial Ombudsman Services Ltd and member for external dispute resolution service.

The facts

In early April 2009, Pioneer Credit Acquisition Services Pty Ltd (**Pioneer**) purchased the right to enforce 2000 credit card debts from Barclays Bank. Shortly afterwards, it became a member of the Financial Ombudsman Services Ltd (**FOS**), an ASIC approved dispute resolution scheme, and entered into a membership contract (**membership contract**) and became subject to FOS's terms of reference (**TOR**) governing the relationship between Pioneer and FOS.

From about July to December 2009, FOS received complaints from ten complainants regarding Pioneer's attempts to recover debts from Australian residents.

Pioneer became dissatisfied with FOS and purported to terminate the membership contract based on an alleged breach of contract by FOS. FOS commenced proceedings against Pioneer seeking to recover outstanding fees of $112,419.27 together with interest and costs. Pioneer counterclaimed, arguing that the termination of the membership contract was effective.

Issues

- Is there is an implied term that FOS must correctly decide questions of law?
- Is there an implied term that FOS must restrict its concern to the resolution of consumer disputes and not act as the equivalent of a court?
- Is there an implied term that FOS must not exercise a power, or make a decision, in a manner which no reasonable tribunal could properly come to on the evidence?
- Was Pioneer entitled to terminate the membership contract, and did it do so?

Decision

The case explored a number of key aspects concerning FOS' role and obligations under the TOR with the key findings being:

- Financial Service Providers (**FSPs**) cannot extricate themselves from a matter before FOS by initiating proceedings against the complainant, even if they do so with FOS's consent;
- there is no implied contractual obligation under the TOR that requires FOS to correctly interpret questions of law and thereby making it a breach of the TOR if it fails to do so. If such a term were implied this would contradict the review process in the TOR which provides a mechanism for the correction of FOS' initial decisions by the Ombudsman;
- FOS is not required to act like a Court. Even though FOS is required to take into account relevant legal principles, it is not required to do so to the exclusion of other matters;
- FOS acknowledged that it is subject to the *'Wednesbury'* test of unreasonableness in decision-making, and its decisions may be reviewable if they fail that test; and
- early termination of the membership contract may only occur if the board of FOS agrees to the termination.

Express breach – clause 5.1(c) TOR

According to clause 5.1(c) of the TOR, FOS is not able to consider a dispute that *'is, was, or becomes, the subject of any proceedings in any court…unless the parties consent'*.

Pioneer argued that FOS breached this term of the TOR by continuing to consider two disputes which became the subject of proceeding after FOS had become involved. In each of these disputes, Pioneer had commenced proceedings to avoid the risk of the causes of action becoming time-barred (one with FOS's consent, the other without).

The court took the view that the words *'…or becomes, the subject of any proceedings'* cannot operate to allow FSPs to extricate themselves from a matter before FOS simply by initiating legal proceedings, as this would produce an absurd result and would defeat the purpose of the TOR. Accordingly, her Honour Justice Ferguson found that FOS was entitled to continue to deal with the Disputes and had not breached clause 5.1(c) of the TOR.

Implied breach – FOS to correctly decide questions of law

Pioneer argued that there was an implied term in the TOR obliging FOS to correctly decide questions of law and that it had breached the implied term by finding certain debts claimed by Pioneer were unenforceable in Australia.

The Court was not convinced, instead finding that under the TOR, FOS is expected to have regard to applicable legal principles but is not expected to apply them *'to the exclusion of all else'*.

Further, the fact that the FOS scheme contains a review process (inherently acknowledging that decisions at the early stages of a claim may be wrong and providing a mechanism for their correction) is contradictory to the term sought to be implied.

'The case explored a number of aspects concerning FOS' role and obligations under its terms of reference, making a number of key findings.'

Implied Breach – FOS not to act as a court

Relying on the observations of Cavanough J in *Wealthcare Financial Planning Pty Ltd v Financial Industry Complaints Service Ltd*[1], Pioneer submitted that there was an implied term in the TOR that FOS should not purport to act as the equivalent of a court, and that consequently it did not have the jurisdiction required to determine whether the relevant debts were enforceable in Australia.

The Court determined that Cavanough J's observations merely described the nature and role of a dispute resolution body like FOS and were not proscriptive and therefore did not create an implied term as asserted by Pioneer.

Implied Breach – unreasonable decisions

Pioneer argued that in refusing its consent to the initiation of proceedings in relation to the second dispute, when FOS had granted consent in similar circumstances in another dispute, FOS had made an unreasonable decision.

FOS conceded that its decisions could be challenged where its decision is one to which no reasonable tribunal could properly have come to on the evidence (the *Wednesbury* test of reasonableness).

In this instance however, FOS was able to satisfy Ferguson J that the decision *'was carefully taken after weighing up a number of factors, including the likelihood of the debts becoming statute barred'* and was therefore not subject to criticism under the *'Wednesbury'* test.

Membership Contract— validity of termination

Pioneer claimed that the alleged breaches of the membership contract amounted to a repudiation such that it was entitled to terminate the contract. Further, Pioneer claimed that FOS accepted the repudiation and terminated the membership contract by way of letter dated 4 January 2010.

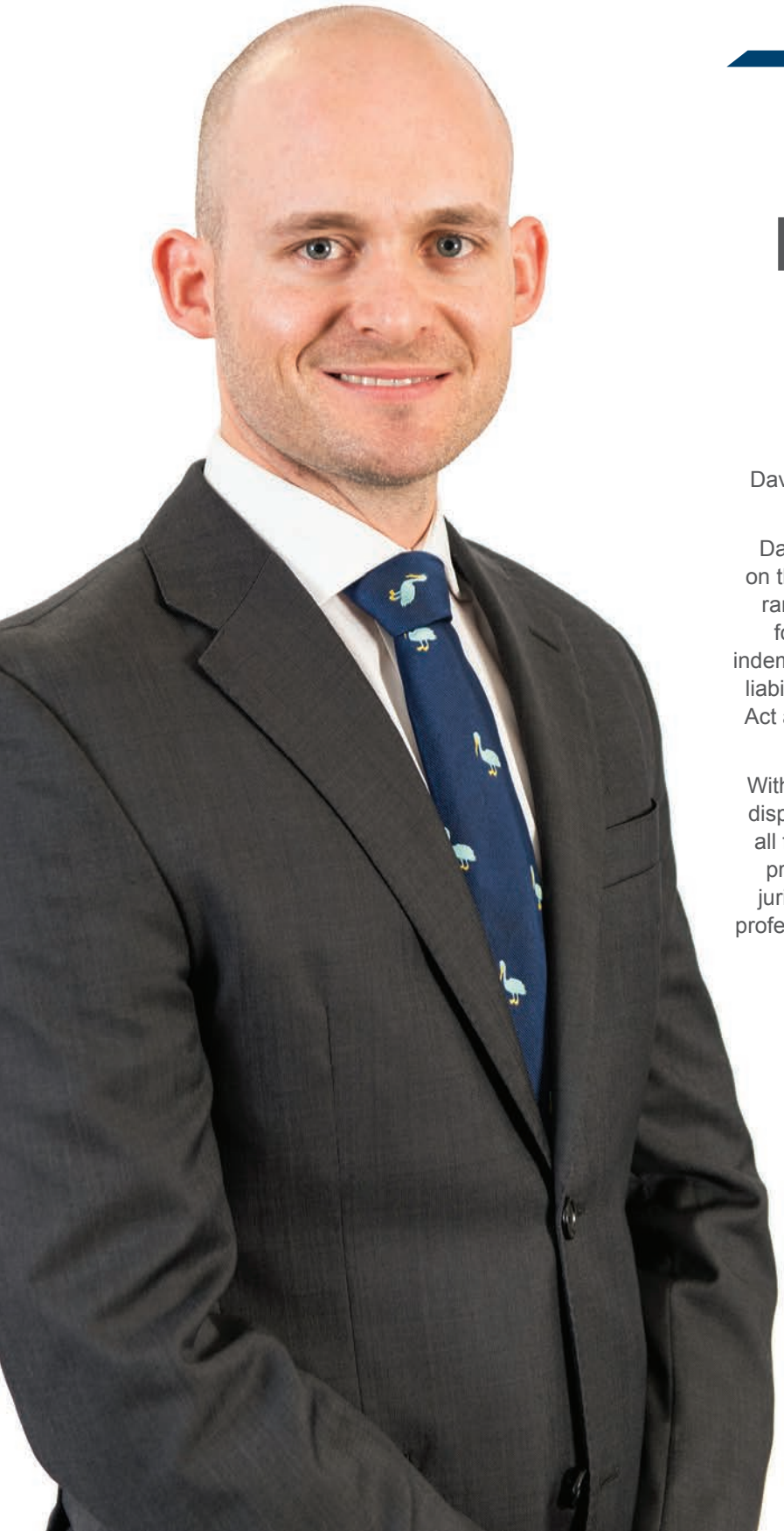
This was not accepted by Ferguson J, who found that the letter of 4 January 2010 did not have the effect of terminating the membership contract, rather it had the effect of affirming the membership contract.

In determining this, Ferguson J referred to the doctrine of election between competing and inconsistent rights which applies to defeat the right to terminate a contract after a binding election has been made between exercising that right and affirming the continued operation of the contract. The doctrine rests upon the notion that it is unfair for one party to a transaction to adopt inconsistent positions in his or her dealings with another party. Thus, Pioneer's letter acted as a mere offer to reinstate the membership contract and treat it as having been operative throughout. By continuing to deal with complaints made against Pioneer, FOS was taken to have accepted the offer.

Outcome

Since Pioneer failed to demonstrate any breaches of actual or implied terms of the TOR by FOS, and did not otherwise satisfy the Court that it had successfully terminated its contractual arrangements with FOS, Pioneer was obliged to pay to FOS the outstanding membership fees which were the subject of the debt.

[1] (2009) 69 ACSR 418.



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Case Note

Fishinthenet Investments Pty Ltd and Coastal Waters Seafood Pty Ltd [2014] NSWSC 260

Application for grant of leave by shareholder to bring derivative proceedings against former directors pursuant to section 237 of the *Corporations Act 2001* (Cth).

The facts

Fishinthenet Investments Pty Ltd (**FITN**) and its subsidiary Coastal Waters Seafood Pty Ltd (**CWS**) together operated an abalone and lobster fishing enterprise in Tasmania.

The applicant, Dennis G Pamplin Pty Ltd (**DGP**), was an equal shareholder in FITN. The other shareholder in FITN was Mr Jeff Hunt, who was also its sole director.

DGP brought an application for leave under s 237 of the *Corporations Act 2001* (Cth) (**Act**) to commence proceedings in the names of FITN and CWS against Mr Hunt, concerning the purported sale of the business enterprises. The proposed proceedings broadly alleged:

- DGP made an offer to purchase Mr Hunt's 50% shareholding in FITN for the price of $1.125 million (which ostensibly valued the business at $2.25 million) and that by an informal shareholders' resolution this offer was accepted;
- Mr Hunt, relying on a shareholders' authority to market and sell the enterprise previously given to him, instead agreed to sell the enterprise to a third party, Sun Rising Fisheries Pty Ltd (**SRF**), for the lesser sum of $2,150,125 conditional upon the purchaser withholding the sum of $150,000 for 12 months and employing Mr Hunt for a minimum term of 6 months; and
- Mr Hunt improperly deducted directors fees of $104,000 and other expenses of $80,000 from the proceeds of sale.

DGP sought declarations (on behalf of FITN) that Mr Hunt account to FITN for the difference in proceeds achieved on sale of the business, and for any money or benefit paid to him by reason of breach of fiduciary duty and contraventions of ss 181 and 182 of the Act.

Mr Hunt opposed the application for leave, contending:

- as a result of the negotiations with SRF, and following the failure of all other potential sale transactions in the previous 13 months, he formed the view that the sale price agreed with SRF was reasonable given the market conditions prevailing at the time;
- SRF was only willing to pay the agreed purchase price upon the stated conditions (regarding

deferral of payment and Mr Hunt's employment), otherwise the sale would have fallen over; and

- it was in the best interests of each company and its shareholders to accept the offer made by SRF and proceed to settlement of the sale.

Issues

In order to grant leave the Court must be satisfied of five matters outlined in s 237(2). The following four matters were most relevant in the present case:

- Whether DGP was acting in good faith in bringing the derivative proceedings.
- Whether the grant of leave is in the best interests of the companies.
- Whether the proceedings involve a serious question to be tried.
- Whether leave should be on terms that the companies be indemnified from their costs.

Decision

Justice Black refused leave to DGP, holding that only one of DGP's proposed claims was seriously arguable and could potentially be in the companies' interests, but only if they were indemnified against the costs of that claim, which His Honour considered would exceed the potential recoveries.

Good faith

The Court said that factors relevant to the good faith requirement include DGP's honest belief that a good cause of action exists and has reasonable prospects of success, and whether DGP is seeking to bring the proceedings for a collateral purpose.

Since DGP was a shareholder in FITN it would stand to benefit from any monies recovered by FITN. Consequently, the Court readily drew an inference that the proceedings were brought in good faith. There was no suggestion DGP was acting for any collateral purpose.

In the companies' best interest / serious issue to be tried

Given the overlap between these two requirements, the Court addressed them together.

The first test requires more than a *prima facie* indication that the proceedings may be, or are likely to be, in the company's interests, and the Court must be satisfied that the proposed action actually is, on the balance of probabilities, in the companies' best interests. The Court said that relevant matters include the prospects of success of the proceedings, their likely costs, the likely recovery if the proceedings are successful and the likely consequences if they are not.

The second test involves the same test that is applied by the Court in determining whether to grant an interlocutory injunction. It is a relatively low threshold to satisfy, to be assessed primarily by reference to the proposed pleadings and the evidence by which they would be supported.

The Court considered there to be fundamental difficulties with DGP's claim in respect of the sale of the business. The evidence of an informal shareholders' resolution was not sufficient to establish that there was an offer by DGP in a form capable of acceptance by FITN, comparable with the offer subsequently received from Sun Rising.

Further, the structure of the proposed transaction and the subsequent sale to SRF were not comparable, since the resolution between DGP and Mr Hunt referred to a sale of shares in FITN, whereas the sale to SRF was of the business assets. The Court therefore held there was no serious question to be tried in respect of the claim as to the terms of the sale generally, as it was unable to draw a conclusion that a sale of the shares to DGP was more favourable to FITN than a sale of the business assets to SRF.

'The Court held there was no serious question to be tried in respect of the claim as to the terms of the sale generally, as it was unable to draw a conclusion that a sale of the shares to DGP was more favourable to FITN than a sale of the business assets to SRF.'

The Court did however consider DGP's claim in respect of directors fees deducted from the proceeds of sale of a seriously arguably quality. Mr Hunt acknowledged these amounts were deducted for directors fees for the past five years, that remained outstanding. He relied on an informal agreement that he would, in effect, be paid directors fees each year if there was sufficient profits.

The Court identified a number of issues that warranted further consideration of this aspect of the claim, noting firstly it could not be determined with any certainty whether all relevant stakeholders (other shareholders at the time) had agreed to the payment of the fees. For the purpose of the suggested agreement (even if established) the Court also noted that:

- the directors fees ultimately paid to Mr Hunt included fees referable to years in which FITN was not profitable; and
- it was by no means clear that the proceeds of sale should be treated as profits, as distinct from capital.

As to the claim in respect of reimbursement of other expenses, the available evidence suggested such reimbursements were permitted by the constitution FITN, and that the allegations and evidence in this respect did not support a grant of leave.

Indemnity for costs

Of the proposed claims by DGP only that pertaining to the directors fees (quantified at $104,000), has sufficient prospects as pleaded that it could potentially be in FITN's interests to bring it. His Honour noted that the costs FITN would likely incur pursuing that claim, and the costs to which it would be exposed if the claim were unsuccessful (and in respect of any amount it may be ordered to pay by way of security for costs) would in all likelihood outweigh the potential recovery.

Moreover, DGP did not lead any evidence to establish that it or its directors had any capacity, or willingness, to given provide an indemnity for FITN's costs. This was instrumental in His Honour's decision against imposing such a requirement, and ultimately in refusing the leave application, particularly where there was a risk the costs of the proceeding may be disproportionate to the amount likely to be recovered.

Case Note

Invion Limited v SGB Jones Pty Ltd & Ors [2014] QSC 97

Consideration of dishonest conduct and breach of fiduciary duty of company directors and the application of directors and officers liability insurance.

The facts

The plaintiff, Invion Limited (**Invion**), is a research and development company in the pharmaceutical industry. It commenced proceedings against four former directors seeking recovery of termination payments, which each of the directors had received upon tendering their resignations.

The defendants included Mr Jones, the former Chairman, Mr Yeates, the former Managing Director and Chief Executive Officer, Mr Greig, the former Chief Financial Officer and Mr Graham, the former Company Secretary.

The proceedings against Mr Graham resolved before the commencement of the trial. Importantly, Mr Jones was not directly employed by the plaintiff. Rather, he had effectively entered into a consultancy agreement with the plaintiff, through a company he controlled, SGB Jones Pty Ltd. The remaining defendants were direct employees.

Prior to 2011, each of the defendant directors and SGB Jones Pty Ltd were engaged by contracts which provided for six months notice (or payment in lieu), in the event that their engagement was terminated by the plaintiff.

At the 2010 Annual General Meeting, a number of shareholders raised concerns regarding the level of remuneration of the executive directors. At this stage, the directors were concerned that the future of the executives was uncertain, in that it was possible that a major transaction with a pharmaceutical company might occur.

They considered that it was likely that if such a transaction occurred, they might be replaced. As a result, in March 2011, the Board of Invion resolved to extend the termination notice period of the contracts to 12 months.

In April 2011, Mr Jones and Mr Yeates effectively purported to modify the March 2011 resolution of the Board by amending the contracts in a manner which differed from the Board's resolution. In essence, they effected an amendment to allow for a termination payment of 12 months salary upon the resignation of each director, without the requirement that they work during the 12 months.

It was also relevant that during this period, the Board resolved to put the potential issuance of performance rights to the shareholders for approval. The original proposed resolutions included the grant of performance

rights to the directors. However, these resolutions were withdrawn on the apprehension that the shareholders would not grant performance rights to the directors.

In any case, the variations of the contracts in April 2011 were made without the Board's knowledge and authority. Indeed, it was not until October 2011, when each of the directors tendered their resignations, that the Board was informed that the termination payments, which totaled in excess of $1.1million, were payable pursuant to the amended contracts.

Invion commenced proceedings against the directors to recover the payments.

The directors made a claim for indemnity under Invion's Directors 'and Officers' insurance policy, which was denied by the insurer. The directors thereafter instituted third party proceedings against the insurer, which was represented by this firm.

The decision

Invion alleged that the directors were in breach of their duties as directors, both at common law and pursuant to sections 180 to 182 of the *Corporations Act 2001* (Cth) (**Act**), through their failure to act in good faith and in the bests in interests of Invion, that they misused their position to obtain a financial advantage, and that they did not exercise their powers for a proper purpose.

The directors argued that Invion had, at the time of its inception, effectively conferred a power upon Mr Jones, and indeed, any executive director, to modify executive employment contracts without a requirement to notify or obtain approval from the Board. After a thorough examination of Invion's records however, this argument was rejected by the Court.

The directors sought to justify the propriety of their actions by arguing that it was necessary to offer significant protection and remunerative benefits to the executive directors, including themselves, in order to dissuade the resignation of the executives. It was alleged that their resignations would have effected a catastrophic destabilisation of the company, which was already suffering from financial hardship.

The somewhat self-serving argument was promptly dispensed with by His Honour Chief Justice de Jersey, who in summary, made the following observations:

- in circumstances where concerns had been raised by shareholders about the level of executive remuneration in 2010, it was discreditable that the directors did not inform the Board of the beneficial changes they had effected to their contracts; and
- the modification of the contracts was an issue directly connected to the potential issuance of performance rights, and it was therefore discreditable to have not informed the Board of the changes to the contracts within this context.

Indeed, it might be inferred, that the fact that it was unlikely that the performance rights would be granted to the directors, was an underlying reason for the defendants' conduct, noting:

- during the Board meeting in March 2011, the directors recused themselves from voting on the proposed variations to the contracts. If the directors had been acting ethically, they surely then would have informed the Board after effectively purporting to modify the Board's resolution, which they had originally abstained from; and
- mr Jones had signed Invion's annual report which included a statement that '*Board members are fully informed on relevant issues in a timely manner.'* It is self-evident that the directors' actions in accruing a contingent liability in excess of $1.1million, at a time when they themselves alleged that the company was approaching insolvency, was a matter which should have been referred to the Board immediately.

The Court thus found that the directors were in breach of their duties both at common law and statute.

The third party claim

The third party insurer denied indemnity to the directors on the basis of the '*Conduct Exclusion'* in the policy. The '*Conduct Exclusion'* provided, in effect that:

- the insurer would not be liable for any loss arising out of any conduct or contravention in respect of which a liability is the subject of a prohibition in s 199B(1) of the Act; and
- the insurer would not be liable for any loss arising out of deliberately dishonest or deliberately fraudulent conduct.

As the Court had concluded that the defendants had occasioned breaches of fiduciary duty and contraventions of s 182 the Act, which are uninsurable, the first limb of the exclusion was triggered. Further, as the Court had concluded that the defendants had engaged in willful dishonest conduct, the second limb of the exclusion was also triggered.

The insurer also denied indemnity on the basis that the definition of '*Loss'* in the policy did not include an '*employment-related benefit'*. The insurer argued that the termination payments were property characterised as '*employment-related benefits'*, such that covering clause in the policy did not respond.

The Court accepted this argument insofar as the employed directors were concerned. The situation was different in the case of Mr Jones however, who was not an employee, but was rather an external consultant, of the plaintiff. The Court doubted whether payments to a corporate entity through a consultancy agreement could be characterised as an '*employment-related benefit'*.

In any case however, Mr Jones' claim against the insurer was unsuccessful due to the application of the '*Conduct Exclusion'*.

Case Note

Jamieson v Westpac Banking Corporation [2014] QSC 32

Consideration of the appropriate measure of loss for failed investments on a no transaction basis.

The facts

In 2007, Mr & Mrs Jamieson made investments based on a written statement of advice prepared by a financial planner employed by Westpac Bank (**Bank**).

The advice recommended two strategies, that the Jamesons:

- borrow $5 million to be invested in a managed investment scheme known as the MQ Gateway Trust; and
- borrow a further $600,000 to make undeducted contributions to their self managed superannuation fund, to in turn be invested in self-funding installment warrants.

The Jamesons proceeded with both strategies (albeit in respect of the latter borrowing and investing the greater sum of $700,000) which ultimately failed.

They commenced proceedings against the Bank alleging breaches of contract, negligence and misleading and deceptive conduct[1] in preparing and giving the advice, alleging they would not have proceeded with the investments but for the Bank's wrongdoing (a '*no transaction case*'). The Jamesons sought damages so as to restore them to the positions they would have been had no borrowings or investments been made

Decision

Justice Jackson found the Bank's advice in breach of contract, negligent and misleading, in the following respects:

- failing to properly describe the extent of the Jameson's interest obligations on the recommended loan facilities;
- erroneously stating in an unqualified way that the investments would put no more than 10% of the Jameson's overall net wealth at risk of loss; and
- failing to provide full terms and conditions, and product disclosure statements, referable to the recommended loan facilities.

His Honour was also satisfied that had the Bank not engaged in such conduct, the Jamesons would not have proceeded with the recommended investments.

Consequently, much of the decision focused on the appropriate measure of loss.

The Bank asserted that any wrongdoing on its part was not causative of any recoverable loss, advancing the following arguments:

- the applicable measure of loss should be calculated in accordance with the rule in '*Potts v Miller*'[1], as the difference between the purchase price of the investment (MQ Gateway Trust) and its true value at the time it was acquired (which the Bank contended was nil). The Bank essentially sought to exclude any ongoing losses associated with the holding the investment; and
- alternatively, the Jamesons would have entered into some other similar transaction (an '*alternative transaction case*') and given the intervention of the Global Financial Crisis would have sustained comparable losses in any event.

'The guiding principle on the applicable measure of loss was to restore the Jamesons to the position they would have been, had they not acted detrimentally on the inducement of the Bank's conduct.'

Shorty stated, the Court rejected both arguments, but in doing so His Honour made a number of important observations concerning causation and the measure of loss.

His Honour considered the guiding principle on the applicable measure of loss was to restore the Jamesons to the position they would have been, had they not acted detrimentally on the inducement of the Bank's conduct.

By purchasing the MQ Gateway Trust investment and entering into the associated loans, the Jamesons exposed themselves to the contingency and risk of loss from market movements subsequently suffered. The Bank's conduct was material to assuming that risk. It was therefore held the rule in *Potts v Miller*, while persuasive, was not appropriate in the circumstances as it excluded subsequent or continuing losses as a result of a general market decline.

His Honour instead preferred the *'net gains or losses'* approach, recognised in earlier cases such as *HTW Valuers Pty Ltd v Astonland Pty Ltd*[2] and *Kenny & Good Pty Ltd v MGICA (1992) Ltd*[3], which measured loss by looking at the net change in the Jamesons' position as at the date of trial, thereby picking up gains or losses occurring after acquisition of the investment.

On this basis His Hounour considered the Jamesons were entitled to recover consequential losses – including interest on borrowings and losses associated with market declines during the Global Financial Crisis - beyond the measure of the difference between the price paid and the true or fair value.

His Honour considered the Bank's second contention – an '*alternative transaction case*' – engaged questions of both a legal and a factual nature. The factual question was whether, on the balance of probabilities, the Jamesons would have entered into an alternative transaction. The legal question was whether the Jamesons' claim must then fail because they have failed to establish the consequences of the alternative transaction.

The Jamesons contended that if it is found they would not have entered into the recommended investment, there was no basis to inquire what similar or alternative transactions they might have entered into.

In answering these questions, characterisation of the kind of the interest and loss under consideration was necessary. For each of the alleged breaches, the interest involved the risk of loss of money paid for the investment, and the loss that might be suffered was a loss of the investment or any profit that might have been obtained. It was held that loss was suffered once it was reasonably ascertainable that the Jamesons were worse off than had they not entered into the transaction.

Ultimately therefore, His Honour considered the *'net gains or losses'* approach involved no requirement for the Jamesons to establish what alternative position they would have been in, had they acted differently. His Honour therefore rejected the Bank's argument that the Jamesons failed to prove any loss without proving what similar or alternative transaction they would have entered they he had not entered into the MQ Gateway Trust investment.

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[1] (1940) 64 CLR 282.

[2] (2004) 217 CLR 640.

[3] (1999) 199 CLR 344.

Case Note

King v Benecke [2013] NSWSC 568

Consideration of breach of duty and retainer by solicitor.

The facts

Mr George King sued his former solicitor, Ian Benekce for professional negligence arising out of the performance of work relating to a series of transactions that were intended to give Mr King effective ownership and control of the family farming and grazing business.

Mr King alleged that in breach of the retainer, Mr Benecke did not give proper effect to the transactions, allowing Mr King's father to resile from the agreement. In consequence, he alleged he was placed at a disadvantageous position at a family mediation, which vulnerability was exploited to his financial disadvantage.

Mr Benecke denied the existence of any such retainer from the plaintiff to act for him with respect to the relevant transaction, and further denied there was a casual connection between the alleged breach of duty/ retainer and any loss suffered by Mr King.

Issues

- Whether there was an implied retainer arising out of the conduct of the parties.
- Whether there was a breach of the retainer or duty of care.
- Whether any such breach of duty/retainer had caused a loss to the plaintiff.

Decision

His Honour accepted the contention that the plaintiff's case was a classic example of a *Pegrum*[1] type duty, in that there was an implied solicitor-client retainer arising out of:

- Garland Hawthorn Brahe having been the family solicitors for generations;
- Mr King having known Mr Benecke since he was a primary school aged child;
- the provision by Mr Benecke of legal services to Mr King on a variety of matters since 1997; and
- most fundamentally, since mid-1999, Mr Benecke had been acting for Mr Kingin relation to work that was inextricably linked to the relevant transfers.

In view of the above, Harrison J found that the defendant was in fact under a duty to advise the plaintiff that he could not act - and was not acting - in his interests, and that he should obtain independent legal advice. The defendant breached that duty by failing to advise the plaintiff accordingly.

Despite Harrison J observation that the breaches were extraordinary and egregious, he found they did not have a relevant causal relationship to the plaintiff's alleged loss, because:

- the plaintiff did not believe his legal position to be weak at the December 2008 mediation or at any time;
- the plaintiff was not under pressure by reason of a perception about lack of security of his legal position in December 2008;
- the plaintiff did not pay any more at the December 2008 mediation than he otherwise would have because of perceptions about lack of security of his legal position; and
- the plaintiff agreed to the December 2008 settlement because it was within the range of values he considered to be 'fair' and because it was a settlement he could comfortably afford.

The plaintiff, not having established causation, lost the case.

[1] *Pegrum v Fatharly* (1996) 14 WAR 92.

Case Note

Polon v Dorian [2014] NSWSC 571

Consideration of the existence of a duty of care and implied retainer between a solicitor and non-client, and the application of proportionate liability.

The facts

The plaintiff claimed damages with respect to losses suffered after investing $1,190,000 in a bridging finance scheme (**Scheme**).

It was alleged that the Scheme's operators, and their solicitor (the defendant), made a number of representations concerning safeguards and security over funds invested in the Scheme.

In reliance on the various representations the plaintiff made three investments in the Scheme, which ultimately failed, and it transpired there were no mechanisms in place to recover the borrowed funds.

Issues

By the time of the hearing the Scheme's operators and their entities were bankrupt and in liquidation. The claim therefore focused to a large extent on the conduct of the defendant, alleged to play a material part in influencing the plaintiff's decision to invest (above the conduct of the other impecunious parties), and involved a consideration of the following issues:

- Whether the defendant had made representations.
- The existence of a duty of care and implied retainer between the plaintiff and defendant.
- The application of the proportionate liability provisions of the *Civil Liability Act 2002* (NSW) (**CLA**).

Decision

The plaintiff's claim was based upon the premise that the defendant made a number of representations, in the nature of advice, concerning the Scheme which were false and misleading. Justice Hall was readily satisfied the representations made, they were misleading, and they were relied upon.

It was submitted on behalf of the plaintiff that the representations were made negligently, and in breach of an implied of an implied retainer, and it is here that Justice Hall made a number of important findings concerning the extent of a solicitor's obligations to non-clients.

Duty of care

According to His Honour, the question of whether the defendant owed a duty of care was to be answered by

considering whether a reasonable solicitor addressing a meeting of potential investors in relation to the soundness of investing in a particular financial product would realise that he or she was being or was likely to be trusted by those who were the recipients of the advice. If so, the statements made by the defendant may give rise to a relationship between requiring the exercise reasonable care.

The defendant argued that she was merely acting on client instructions. Importantly however, she did not make any disclaimer as to the source of her information, nor did she seek to independently verify the truth of those instructions or advise the plaintiff on obtaining independent legal advice.

Absent any disclaimer, Justice Hall considered the defendant's provided assurance to the plaintiff that her investment in the Scheme would be a safe and beneficial one. This gave rise to the existence of a duty of care. Importantly, His Honour held the duty did not to cease at the point at which the representations were made, but rather had a continuing operation during the period of the plaintiff's reliance on the representations (a period spanning approximately six months). During this period it remained the defendant's continuing duet to take reasonable steps to provide the plaintiff appropriate cautions and warnings that the initial representations had not been verified.

Implied retainer

His Honour was equally satisfied that an implied retainer existed between the plaintiff and defendant, which arose from the defendant's role in preparing and providing contracts to the plaintiff, taking and returning telephone calls from the plaintiff, preparing the relevant mortgages and caveats and undertaking administrative tasks including corresponding with the plaintiff and maintaining some form of monitoring of funds invested in the Scheme.

The Court was convinced that the defendant knew or ought to be taken as knowing that the plaintiff was looking to her and relying upon her for the relevant legal services and advice. On this basis, the Court concluded that the second defendant was, at all material times, subject to a fiduciary duty to act to protect and advance the plaintiff's interest, and her failure to do so resulted in a breach of that duty.

Proportionate liability

The plaintiff's claims were apportionable, and His Honour considered each of the defendant, the Scheme's operators, and a third individual (who was responsible for introducing the plaintiff to the Scheme's operators, but who was also bankrupt) concurrent wrongdoers in respect of the plaintiff's losses.

The Court apportioned damages between them as 60% to the Scheme's operators, 30% to the defendant and 10% to the third individual. In assessing the defendant's liability at 30%, the Court took into account the fact that her representations adopted and endorsed the promotion of the Scheme, went beyond the normal scope of her retainer with the Scheme's operators, were made without any qualification or disclaimer, or recommendation to seek independent legal advice.

Case Note

Amlin Corporate Member Ltd v Austcorp Project No 20 Pty Ltd [2014] FCAFC 78

Consideration of the definition of *'Claim'* in a professional indemnity policy of insurance.

The facts

Transactions and proceedings relating to the Ballambi Land

The proceedings arose from the 2003 acquisition by Bellpac Pty Ltd (**Bellpac**) of the Bellambi Colliery. The Bellambi Colliery included the '*Bellambi Land'* which was subject to a first mortgage in favour of The Trust Co (PTAL) Limited (**PTAL**). Austcorp Project No 20 Pty Ltd (**Austcorp**) and Compromise Creditors Management Pty Ltd (**Compromise**) held securities over the Bellambi Land ranking behind PTAL's mortgage. LM Investment Management Ltd (**LMI**) was a lender to Bellpac. Alfred Wong guaranteed that loan.

Bellpac had dealings with Gujarat NRE Coking Coal Limited (**Gujarat**) in connection with the Bellambi Colliery. Disputes arose between various parties including Bellpac and Gujarat which resulted in litigation in the Supreme Court of New South Wales (**Bellambi proceedings**).

In May 2009, LMI appointed receivers and managers to Bellpac (**Receivers**). Subsequently, Bellpac was placed into liquidation. In 2010, LMI commenced proceedings in the Supreme Court of New South Wales (**NSW proceedings**) seeking to recover from Mr Wong pursuant to his guarantee of Bellpac's obligations under the loan.

In June 2011, LMI, PTAL, the Receivers and other creditors of Bellpac (but not Austcorp and Compromise) settled the Bellambi proceedings. The settlement provided for the sale of the Bellambi Land to Gujarat for $10 million. The sale reduced, but did not extinguish, Bellpac's liability to PTAL.

In December 2011, Mr Wong filed and served a Commercial List Response (**Defence**) in the NSW proceedings which alleged that:

- PTAL owed an equitable duty to Bellpac and Mr Wong to exercise its powers of enforcement under its first mortgage in good faith, to deal fairly with Bellpac's interests in the Bellambi Land and to refrain from acting in wilful or reckless disregard of, or recklessly sacrificing Bellpac's interests in the land;
- PTAL owed a duty to Bellpac to take reasonable care to sell the Bellambi Land at market value or the best price reasonably obtainable;
- in breach of those duties, PTAL sold the Bellambi Land at gross undervalue;

- PTAL was knowingly involved in breaches by the Receivers of their duties to Bellpac in connection with the sale of the Bellambi Land;
- since it had conduct of the Bellambi proceedings and instructed the Receivers in relation to the settlement, LMI was knowingly concerned or involved in breaches of duty committed by PTAL and the Receivers in connection with the sale of the Bellambi Land; and
- in those circumstances, Mr Wong's obligations under the Guarantee were discharged or any liability under the Guarantee should be reduced.

In February 2013, Austcorp and Compromise commenced proceedings in the Federal Court of Australia against LMI and others seeking equitable compensation or damages arising from the alleged sale of the Bellambi Land at a gross undervalue and the alleged knowing involvement by LMI in breaches of duty committed by PTAL and the Receivers in connection with the sale (**Federal Court proceedings**). There was no dispute that the allegations made by Austcorp and Compromise in the Federal Court proceedings and by Mr Wong in the Defence arose from the same facts.

Insurance issues

LMI had a layered professional indemnity insurance program underwritten by several Insurers (collectively the **Insurers**). The policies incepted on 31 July 2012 (ie. after the Defence was filed and served). The relevant insuring clause provided that LMI was entitled to indemnity for:

> *'any amount up to the **Limit of Liability** stated in Item 3 of the **Schedule** in respect of **Loss** and **Defence Costs and Expenses** arising from any **Claim** for any civil liability first made against **You** during the **Period of Insurance** and arising out of or in connection with a **Wrongful Act**.'*

Claim was relevantly defined to mean:

> *'(a) any written demand or civil, regulatory or arbitration proceedings (including proceedings before the Financial Ombudsman Service Limited) or **Investigation** made against **You** for compensation or damages alleging a **Wrongful Act** and/or;*
>
> *(b) any suit, civil or third party proceedings, counter-claim or arbitration proceeding brought against **You** alleging a **Wrongful Act'**.*

Joinder of the insurers

As LMI was in liquidation, Austcorp and Compromise sought leave to proceed directly against the Insurers in the Federal Court proceedings and sought a declaration that the Insurers were liable to indemnify LMI for the breaches alleged against it. The Insurers resisted the joinder on the basis that the policies did not respond because LMI's liability (if any) arose from a claim made before their policies incepted. It was central to that argument that:

- the Defence was a counter-claim for the purposes of paragraph (b) of the Claim definition in the policies; and
- if Austcorp and Compromise succeeded against LMI, the loss would arise from the claim made against LMI in the Defence.

Leave was granted on the condition that the question of whether the claim against LMI was first made during the period of insurance be determined as a preliminary point.

Decision at first instance

At first instance[1] Jacobson J determined that:

- the Defence was not a '*Claim*' for the purpose of the policies; and
- even if that was incorrect, as the claim in the Defence was different from the claim made against LMI in the Federal Court proceedings, the latter could not be said to have been first made during the period of insurance of the policies.

The Insurers appealed.

Appeal

There were three relevant questions answered in the appeal:

- Was the Defence a '*Claim*'?
- Would any loss which LMI might suffer in the Federal Court proceedings '*arise from'* the Defence?
- Was the Defence a claim '*for any civil liability'*?

The Court of Appeal unanimously found against the Insurers on all three questions, dismissing the appeal, on the following basis.

Was the Defence a 'Claim'?

Since the Defence did not claim compensation or damages, it was accepted that paragraph (a) of the Claim definition was not satisfied.

The Insurers argued that the Defence was a counter-claim within the meaning of paragraph (b) of the Claim definition because it '*was designed to counter the demands'* by LMI against Mr Wong. The Court accepted that in certain circumstances damages claimed by way of set-off might be a counter-claim for the purpose of the policies. However, noting that the policies were designed to indemnify an insured against liabilities to third parties and not for losses suffered by the insured, the Court considered that the reference to counter-claim '*was directed to the possibility that the insured may suffer a liability to a third party by reason of the counter-claim'*.

Since the Defence only raised certain defences to LMI's action on the guarantee and did not claim any relief against, or damages from LMI, the Court held that it was not a Claim for the purpose of the policies.

If that conclusion was wrong, the Court also noted that to satisfy the definition, the Claim must be 'brought against' LMI. The Court considered that the words '*brought against*' referred to positive rather than defensive action and consequently agreed with the trial judge that a defence which asserts a set-off was not a claim brought against LMI.

Would any loss which LMI might suffer in the Federal Court proceedings 'arise from' the Defence?

In addressing this issue, the Court agreed with the trial judge that:

- the Defence did not claim damages or any order for compensation by LMI; and
- any loss asserted by Mr Wong in the Defence (being the liability under the guarantee) was not the same loss as that asserted by Austcorp and Compromise in the Federal Court proceedings (being equitable compensation arising from the breaches of duty involved in the alleged sale of Bellambi Land at undervalue).

The Court noted that the phrase '*arising from'* in the insuring clause was the causal connector between the Claim and Loss. Citing *Walton v National Employers' Insurance Association*[2] the Court accepted that '*arising from'* in this context meant originating in or springing from, concluding that:

'There is no causal linkage between the Commercial List Response and the losses claimed in these proceedings because LM could not be found liable for those losses in the proceeding in which the Commercial List Response was filed. At most, Mr Wong's guarantee could be discharged. That would involve a loss to LM but (as the Insurers acknowledged), that was not the loss claimed in these proceedings. Accordingly, the claims in these proceedings are not claims 'arising from' the Commercial List Response.'

Was the Defence a claim 'for any civil liability'?

Citing various legal authorities, the Court considered that in the context of this case a claim for civil liability must seek '*the establishment by judgment of responsibility in law*'.

The Insurers argued that the Defence included a claim for civil liability because it asserted a liability against LMI which was a civil liability – being the liability to account to Bellpac. The Court rejected that argument for various reasons including:

- the Defence did not claim that LMI was liable to account to Bellpac;
- there was no claim for relief made by Bellpac in the Defence;
- there was no express claim by Mr Wong for any relief based on LMI's alleged liability to account to Bellpac;
- when used in the Defence, '*Equitable Compensation'* referred to an amount by which Mr Wong claims to be entitled to a reduction of LMI's claim under the guarantee. It did not allege that LMI had to pay an amount by way of equitable compensation to Bellpac (or Mr Wong); and
- to the extent that the Defence asserted a liability of LMI to Bellpac, that assertion was made in support an equitable defence and did not involve or require the establishment by judgment of LMI's responsibility at law to Bellpac.

[1] *Austcorp Project No 20 Pty Ltd v LM Investment Management Ltd, in the matter of Bellpac Pty Ltd (receivers and managers appointed) (in liq) (No 2)* [2014] FCA 44.

[2] [1973] 2 NSWLR 73.

Case Note

Kyriackou v ACE Insurance Ltd [2013] VSCA 150

Whether ASIC proceedings constituted a claim for the purposes of a professional indemnity policy, and whether they involved a breach by the insured director of a *'professional'* duty.

The facts

Mr Kyriackou, a company director who was engaged in a role variously described as a '*finance originator, finance intermediary or finance consultant*', obtained a professional indemnity insurance policy with Ace Insurance.

Within the policy period, ASIC commenced proceedings seeking declaratory and injunctive relief against Kyriackou, alleging that he was involved in an unregistered managed investment scheme (**ASIC proceedings**). Some years later, the ASIC proceedings were discontinued without any determination on the merits, leaving Kyriackou with no liability but significant legal costs which he sought to recover under his professional indemnity policy with Ace.

Issues

The decision – both at first instance in the Supreme Court of Victoria and on appeal to the Victorian Court of Appeal – turned heavily on the particular wording of the insuring clauses of the Ace policy.

Particularly, the key policy definitions of '*claim*', '*Claim*' and '*Loss*' were all concerned with a stated requirement for '*civil compensation or civil damages*', and the central issue both at trial and on appeal was whether the ASIC proceedings satisfied that requirement.

A subsidiary issue was whether the ASIC proceedings were brought against Kyriackou for '*breach of a duty owed in a professional capacity*' such as to trigger coverage.

Decision

As to the first issue, the trial judge found – and the Court of Appeal agreed – that the ASIC proceedings did not satisfy the policy requirement of a claim for '*civil compensation or civil damages*', or alternatively a '*written intimation of an intention to seek*' such damages.

Kyriackou had attempted to argue that:

- whilst the originating process filed by ASIC sought (relevantly) injunctive relief pursuant to section 1324(1) of the *Corporations Act 2001* (Cth) (**Act**), ASIC also sought *'such further or other orders as the court deems fit*';
- section 1324(10) of the Act – which was not specifically referred to in the originating process

- empowers a Court to *'either in addition to or in substitution for the grant of the injunction, order* [the person to whom the injunction is directed, in this case Kyriackou] *to pay damages to any other person*'; and

- in view of the Court's ability to award damages (even if not sought by ASIC) in lieu of or in addition to the damages which ASIC had in fact sought, the ASIC proceedings should be considered a '*written intimation of an intention to seek*' relevant damages, and that such proceedings therefore constituted a '*Claim*' under the policy.

In response, Ace argued that the policy required at least a written intimation of the general nature of the claim, and that that nature must be ascertained from '*the matters actually raised and the relief in fact sought*'.

Both the trial judge and the appeal Court agreed with the insurer. The appeal held that the mere fact that s 1324(10) empowered the Court to award damages did not amount to an intimation that such a claim would be made, and consequently the claims actually made by ASIC bore '*no relationship*' to the sorts of claims covered by the policy. As a result, the policy did not respond to the claim for coverage.

As to the second and subsidiary issue of whether the ASIC proceedings constituted a claim for *'breach of a duty owed in a professional capacity'*, the Court of Appeal disagreed with the trial judge. However, in view of the first limb of the appeal having failed (above), the overall outcome of the appeal was not affected.

At first instance, the trial judge had found that the ASIC proceedings did not concern Kyriackou's breach of *'a duty owed in a professional capacity*' as required by the policy, but rather one owed in an '*entrepreneurial capacity*' in his role as an entrepreneur in the management of the group of companies.

In terms of the appropriate test to be applied, the Court of Appeal referred favourably to Buchanan JA's decision in *Suncorp Metway Insurance Pty Ltd v Landridge Pty Ltd (t/as LJ Hooker Hampton Park)*[1] and confirmed that:

> *'...whether a breach of duty answers the description of a breach of professional duty depends upon characterisation of the overall activity in the context of which the breach occurs, and is not answered by concentrating on the specific task which has not been performed or badly performed so as to give rise to liability.'*

Applying that '*overall activity*' test, the VCA held that Kyriackou had acted in a professional capacity, not because his own particular activities could be (or needed to be) characterised as '*professional*', but rather because any breach of duty took place when Kyriackou was engaged in his role as a finance originator and the activities of a finance originator satisfied the term '*professional capacity*' in the insuring clause of the policy.

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[1] *Suncorp Metway Insurance Pty Ltd v Landridge Pty Ltd (t/as LJ Hooker Hampton Park)* [2005] VSCA 223.

Case Note

Cash Converters International Ltd v Gray [2014] FCAFC 111

Consideration of the Federal Court of Australian Act rules relating to class actions against multiple respondents – whether each group member must have a claim against each respondent.

The facts

Ms Gray (as lead applicant on behalf of approximately 40,000 group members) commenced two representative proceedings under Part IVA of the *Federal Court Act 1976* (Cth) (**Act**) against various credit providers and their franchisees (collectively, **Cash Converters**). The claims against Cash Converters alleged that certain fees charged, and interest rates applied, under loan agreements were either void or unconscionable.

Section 33C(1) of the Act (which is contained within Division 2 of Part IVA) provides that:

'*where:*

7 or more persons have claims against the same person; and

the claims of all those persons are in respect of, or arise out of, the same, similar or related circumstances; and

the claims of all those persons give rise to a substantial common issue of law or fact;

a proceeding may be commenced by one or more of those persons as representing some or all of them.'

It was common ground that s 33D of the Act required Ms Gray (as representative applicant) to have a claim against each respondent (which she did). However, not every member of the class had a claim against each respondent. Cash Converters therefore argued that the proceedings were not properly constituted under s 33C(1) and should be struck out.

Cash Converters was unsuccessful at first instance. On appeal, it submitted that as a matter of statutory construction, the ordinary and natural meaning of s 33C(1)(a) is that each of the seven persons must have claims against the '*same person*' – being the respondent or respondents to the suit. As some group members did not have claims against some respondents meant, according to Cash Converters, that the representative proceedings had not been properly commenced.

Cash Converters relied upon the Full Court decision of *Philip Morris (Australia) Ltd v* Nixon[1] in which the parties had accepted that s 33C(1)(a) requires every applicant and represented party to have a claim

against the one respondent or, if there is more than one respondent, against all respondents. The Court in *Philip Morris* acknowledged that the parties' agreement on the issue was consistent with the structure of the legislation.

Ms Gray argued that section 33C(1) does not impose such a requirement and, as such, the representative proceedings had been properly commenced. Ms Gray relied upon the Full Court decision of *Bray v F Hoffman-La Roche* Ltd[2] in which the Court disagreed with the approach taken in *Philip Morris*. The first instance judge had preferred the reasoning in *Bray*.

Decision

The question before the Full Court was what does s 33C(1) require if the applicant's circumstances (and those of the group members) give rise to a claim of multiple wrongdoing against more than one respondent.

Analysing s 33C(1) of the Act, the Full Court held that:

- the section only requires a properly constituted representative proceeding to involve a group of seven or more persons, each of whom has a claim or claims against one person;
- the section does not address the situation where some group members do not have a claim against some respondents, and the court should not take it upon itself to read such a requirement into the legislation;
- to require each class member to have a claim against each respondent would impose a condition inconsistent with the words used in, and the purpose of, the legislation, and would likely require a complicated re-structure of a representative proceeding or a separate action completely – undermining many of the objectives of the legislation (for example, a reduction of legal costs, promotion of the efficient use of court resources, etc); and
- the section will be satisfied provided that the applicant and six other persons have a claim against each respondent.

As such, the Full Court concluded that the proper construction of s 33C(1) does not require every group member to have a claim against all respondents and, therefore, Ms Gray's representative proceedings had been properly commenced.

In resolving the inconsistency between the legal authorities, the Full Court noted that the parties in *Philip Morris* accepted (wrongly in the Full Court's view) that s 33C(1) required each party to have a claim against each respondent. As the issue was therefore not in dispute in those proceedings, the case was not binding and the Full Court was not obliged to follow it.

In relation to *Bray*, while the Full Court acknowledged that each of the judges addressed the issue differently, it ultimately agreed with the comments of Finkelstein J in *Bray*:

> *'… I am of the very firm view that there is nothing in the language of s33C(1), when considered in isolation or in its setting, which requires that result [that it is necessary for every applicant and every represented party to have a claim against all respondents].'*

Cash Converters' appeal was accordingly dismissed.

……..

[1] (2000) 170 ALR 487.

[2] (2003) 130 FCR 317.

Case Note

Swansson v Harrison & Ors [2014] VSC 118

Where the plaintiff sued his insurance advisor for the loss of an insurance policy that, had it not been cancelled, would have paid out upon the plaintiff's terminal cancer diagnosis.

The facts

In March 2012, the plaintiff, after consulting with the defendant, his insurance advisor, cancelled a life insurance policy he had held with AXA since 2004 and took out a policy with AIA. In May 2012, the plaintiff was diagnosed with pancreatic cancer, which by July 2013, had become terminal.

After his terminal illness diagnosis, the plaintiff made a claim under the AIA policy. That claim was declined due to non-disclosures that related to facts material to AIA's acceptance of the risk. There was no dispute of AIA's right to do so.

The cancellation of the AXA policy and the denial of the claim under the AIA policy left the plaintiff uninsured.

The plaintiff made a claim for damages against the defendant alleging that he had negligently failed to exercise the skill and care to be expected of reasonably competent insurance advisor by failing to:

- adequately explain the ongoing nature of the obligation of disclosure;
- warn the plaintiff of the risk of changing life insurance policies including the risk of non-disclosure;
- ascertain whether material events, including further medical consultations had occurred prior to the commencement of the AIA policy; and
- make further enquiries of the plaintiff in respect of his medical condition before cancelling the AXA policy.

The defendant claimed the plaintiff was contributory negligent because of the non-disclosures.

The 7 March 2012 meeting

On 7 March 2012, the plaintiff attended the offices of his insurance advisor to discuss his options with respect to life insurance. This meeting came shortly after he had received a renewal notice for his current life insurance policy (with AXA) that indicated his premium, should he wish to renew, would increase significantly.

At that meeting, it was agreed that the plaintiff would seek a new life insurer. The defendant filled out an application form on behalf of the plaintiff and with his help. In doing so, the plaintiff was required to provide the details of his most recent consultation with a doctor. That consultation was two days prior to the meeting, when the plaintiff attended his GP complaining of a *'sore stomach'*. At the plaintiff's

direction, the defendant wrote on the application form that the plaintiff was diagnosed as having giardia, was treated with antibiotics and the illness had resolved.

The reason for the inclusion of the word *'resolved'* on the application form was contended by both parties. According to the plaintiff's recollection, the word *'resolved'* was included at the defendant's suggestion (he recalled the defendant had said that, in the defendant's experience, indicating on an allocation form that a medical condition had resolved meant the application would be processed immediately). The defendant however, had a different recollection of the conversation. He recalled the plaintiff had said the illness has resolved (or used words to similar effect). Further, when the defendant suggested the application be delayed until the plaintiff was sure the condition had resolved, the plaintiff responded by saying that he wanted to proceed with finding a policy with a cheaper premium as he wanted to make a break from AXA as soon as possible. Ultimately, Justice Macaulay preferred the defendant's recollection of the conversation.

Another contentious point arising from that meeting was whether the defendant fully explained to the plaintiff the ongoing nature of his duty of disclosure. The plaintiff maintained the defendant did not at any stage during the application interview give him any advice about his duty to disclosure medical information. The defendant insisted to the contrary, recalling three separate occasions when the duty of disclosure was brought to the plaintiff's attention.

The first of those was when the defendant paraphrased passages related to disclosure that were printed on the application. He conceded that he did not read those passages to the plaintiff, but noted that, as an insurance advisor of many years experience, he had given an explanation of the duty 'hundreds of times' in his own words.

The second occasion was after the exchange referred to above where the plaintiff indicated he wanted to proceed with the application. According to the defendant, he told the plaintiff that, as the application was proceeding, he was obliged to disclose changes in his health up until the new policy was issued.

The final occasion came as the plaintiff signed the declaration at the end of the application form. By signing, the plaintiff declared that he had been informed of and understood his duty to disclose. Again, the defendant conceded that he did not read the declaration to the plaintiff verbatim but paraphrased it, and in doing so, referred to the duty of disclosure.

Again, Justice Macaulay preferred the evidence of the defendant, concluding that he sufficiently explained not only the ongoing nature of the duty of disclosure but also the consequences for its breach.

As an aside, despite preferring the evidence of the defendant, His Honour noted that he did not think the plaintiff untruthful, but that human memory is fallible and affected by the passage of time, and that self-interest may subconsciously cause a person to reconstruct a memory in the manner that best accords with his or her own cause.

Events after 7 March 2012

The application form was sent to AIA, and on 23 March 2012 AIA accepted the risk and the new policy commenced. Upon receiving confirmation that the AIA policy had commenced, the defendant, acting on behalf

of the plaintiff and in ignorance of any developments in the plaintiff's medical condition, cancelled the AXA policy on 28 March 2012.

Between the date the application form was filled out and the date the new policy commenced, the plaintiff's medical condition declined. During this time, he consulted with several doctors, underwent a series of tests and received a series of diagnoses of ever increasing seriousness. At no stage did the plaintiff contact the defendant to inform him of the progress of the medical investigations or their outcomes, nor did he volunteer this information when contacted by the defendant about other matters relevant to the application.

The defendant's negligence

The defendant's liability depended on whether he had exercised the standard of care that a reasonable and prudent insurance adviser ought to have exercised in the circumstances. In considering the defendant's negligence, his Honour noted the following facts of which the defendant was aware:

- the AXA policy, unlike the AIA policy, could not be avoided for non-disclosure (as it was more than three years old);
- the plaintiff had only been to the doctor two days before the application interview, a very short time for the plaintiff to be able to determine that his condition had resolved;
- at the time of cancelling the AXA policy, three weeks had passed without an update from the plaintiff as to any developments in his condition; and
- it was relatively easy for the defendant to *'pick up the phone'* to enquire of the plaintiff whether there had been any developments in his condition.

With those facts in mind, his Honour concluded that a reasonably prudent insurance advisor in the position of the defendant should have checked with the plaintiff for any changes in his medical condition prior to cancelling the AXA policy.

Had the defendant taken that step, His Honour thought it highly likely he would have discovered, by that date, the plaintiff had been diagnosed with pancreatitis and later with a pancreatic divisum and that further investigations were pending. With this knowledge, it was thought likely the defendant would have appreciated the AIA policy was susceptible to avoidance for non-disclosure and would therefore not have cancelled the AXA policy. Had the AXA policy not been cancelled, there was no reason to doubt the plaintiff would have made a claim under that policy and would have been paid the insured sum (being $1,477,454.79). In His Honour's view, the defendant's negligence caused the plaintiff to lose that amount.

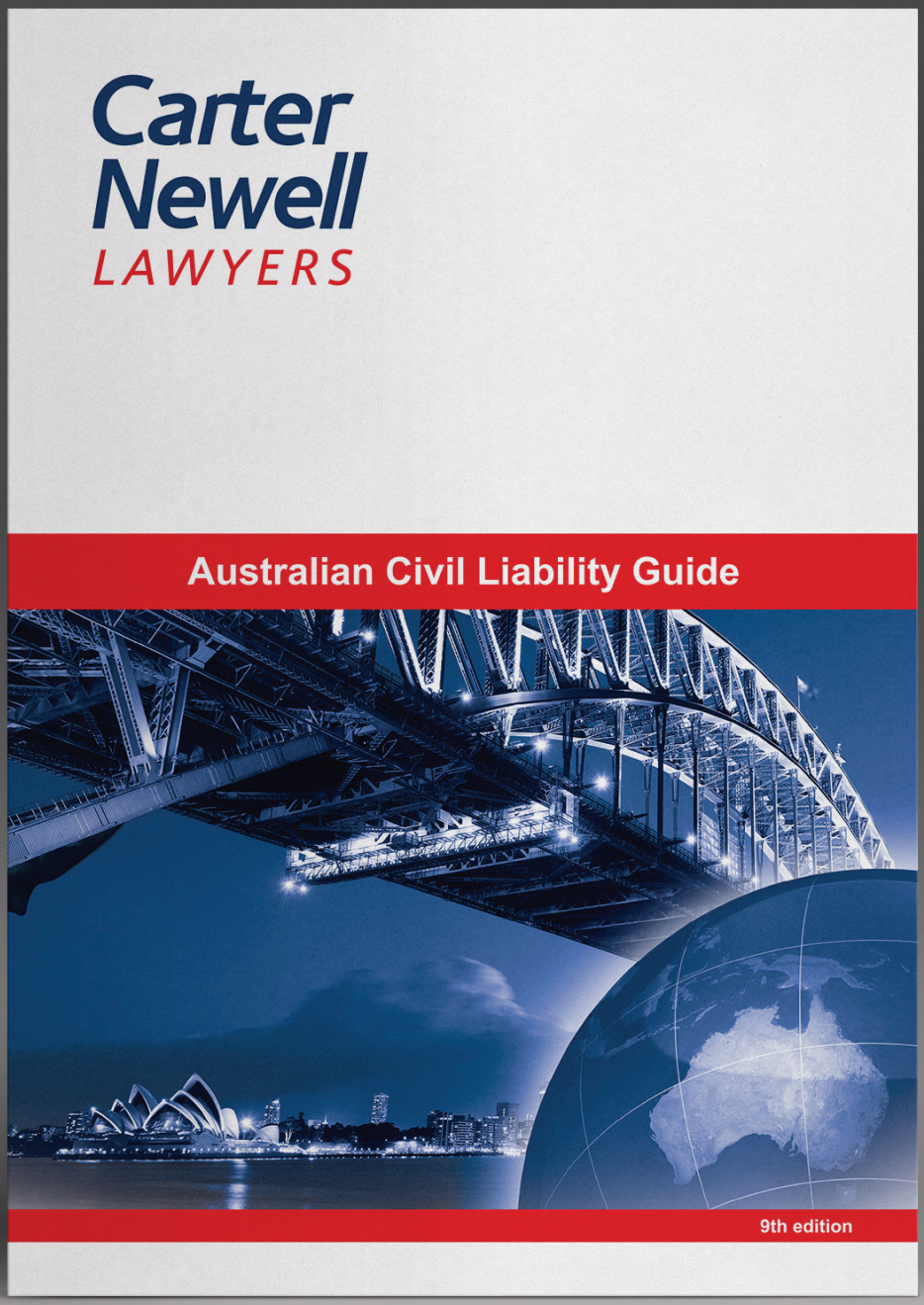
Contributory negligence

The first allegation of contributory negligence on the part of the plaintiff centred around his alleged failure to exercise reasonable care to accurately describe his medical condition during the application interview. Justice Macaulay did not accept that this was the case but rather held that, on the day of the interview, the plaintiff reasonably believed himself to be much better than when he initially consulted with his doctor and therefore, his responses were reasonable.

The second allegation of contributory negligence arose from the defendant's view that the plaintiff was careless in failing to disclose the further developments in his medical condition (being the results of medical investigations carried out after the application interview but before policy inception) on the one (or possibly two) occasions he was in touch with the defendant before inception.

Having already found that the plaintiff was aware of his ongoing duty of disclosure, His Honour had little hesitation in concluding the plaintiff failed to exercise the care a reasonable person in his situation would have taken by not telling the defendant that his stomach condition, listed on the application as being resolved, was not so and that he had in fact received a more serious diagnosis and that further investigations were pending. The plaintiff's carelessness in that regard was compounded by His Honour's conclusion the plaintiff knew or ought to have known the effect of his failure to disclose his ongoing stomach symptoms and diagnoses was that AIA could avoid the policy for non-disclosure and that he knew that he had given the defendant his authority to cancel his existing AXA policy (a policy under which he could have claimed).

After considering the role both parties had played in the cancellation of the AXA policy, Justice Macaulay concluded the plaintiff's damages should be reduced by 50%.



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