IAG Submission on the Law Commission's Issues Paper 32: Review of Joint and Several Liability

30 January 2013

Introduction

This submission articulates the IAG New Zealand Group's ('IAG') recommendation of a move to proportionate liability in New Zealand.

In doing do so we focus on some of the issues raised in the Issues paper and discuss generally the benefits of and reasons for supporting a change to proportionate liability, rather than answering the specific questions posed.

We are happy to discuss the points we raise in this submission with the Commission.

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About the IAG New Zealand Group Limited

IAG New Zealand Limited trading under the NZI and State brands and AMI Insurance limited. IAG New Zealand Limited also underwrites general insurance for some of the country's leading financial institutions (including ASB, BNZ and The Cooperative Bank). IAG New Zealand Limited and AMI Insurance limited have a combined 42% share of the general insurance market, managing 3.8 million policies of 1.5 million New Zealanders. IAG New Zealand Limited and AMI Insurance limited are wholly owned subsidiaries of Insurance Australia Group (IAG), Australasia's largest general insurer.

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Summary

IAG welcomes the Law Commission's review of this important issue. The apportionment of a loss between multiple defendants is a critical issue in the conduct of legal proceedings in New Zealand.

IAG is a regular participant in litigation in New Zealand and each year is involved in hundreds of litigated claims. There would be few organisations who were involved in more litigation in New Zealand.

As with most insurers, IAG is involved for both plaintiffs and defendants. It acts for plaintiffs where it has paid a claim and then brings an action in the name of its customer to recover from the party responsible for the loss. It acts for defendants where its customers have liability policies and are being sued. It therefore sees the issues relevant to this Paper from both perspectives.

That extent and depth of experience leads IAG to support strongly a move to proportionate liability in New Zealand. We believe the competing policy objectives of protecting defendants from bearing a plaintiff's total loss, being unfairly treated as between themselves, protecting the plaintiff, and encouraging settlement are best served by a change to a proportionate liability regime.

No system is perfect. Apportionment of loss is difficult in a complex society and requires a balancing of interests. Some responsibility and accountability must come with the decisions of those who engage in activities with a risk of loss.

Clearly, a change to proportionate liability shifts the risk balance back towards plaintiffs to some degree. That is not unfair. Out of all the parties to a transaction or undertaking, it is the plaintiff who has the greatest control over the process. The plaintiff can choose the parties with whom they contract. They can take the steps they consider necessary to protect themselves against default by those counter-parties through terms of contract, personal guarantees, financial bonds or insurance. They should therefore bear at least some of the consequences of the inability of those parties to meet their share of liability. For the whole of that burden to fall on solvent defendants is manifestly unfair and unjustifiable.

Background

The concepts

The law of torts is concerned with the allocation of losses arising out of human activity. It is a creature of social theory whose purpose is to make as fair an adjustment of the claims of the litigating parties as possible. Common law courts and legislatures are routinely called upon to make adjustments to common law rules and create a more equitable system as society changes.

The legal concepts of joint and several liability and proportionate liability have been discussed at length in the Paper and the principles of each regime are well understood. IAG does not propose to discuss in detail the legal concepts and of each regime.

For the purposes of this submission, IAG uses joint and several liability to refer to a regime whereby a plaintiff is able to recover the whole of their loss from any one of a number of concurrent wrongdoers responsible for the plaintiff's loss.

This has the effect of allowing a plaintiff to call upon a 'deep pocket' defendant to pay the entire amount of the plaintiff's claim even if that defendant's responsibility for the loss is minor compared to other contributing defendants.

By contrast, proportionate liability is a regime where each concurrent wrongdoer is only liable to the plaintiff for the proportionate share of the plaintiff's loss caused by them.

The arguments

Consideration of the reform of the common law position of joint and several liability is not new, and, as the Review Paper states, was considered by the Law Commission in 1998.

In Australia, proportionate liability has been in place for the building industry from 1998 and more generally in relation to torts involving economic loss and breach of contract since 2002.

The adoption of proportionate liability was considered, and rejected in the mid to late 90s in the United Kingdom. Limited adoption of this reform has been undertaken in Canada. These positions contrast markedly with the adoption of proportionate liability by the majority of states in the United States of America.

The experience of these jurisdictions tends to indicate that there is no consensus on the best way to approach this type of reform. What is clear is that an assessment needs to be undertaken in light of the specific legal, social and economic factors of the particular jurisdiction.

Consideration of the adoption of proportionate liability has created considerable debate about which regime is fairer to plaintiffs or defendants. This consideration of fairness appears to centre on arguments of who should bear the risk of there being impecunious or insolvent defendants.

In IAG's submission this fairness issue should not be limited in its focus to plaintiffs or defendants. The focus of any tort reform review should be the fairness of the system to society as a whole. It is not clear to IAG why plaintiffs should expect to be able to recover the whole of the loss from any defendant when the impact of that on particular defendants can be so uneven and unjust. Rather, there needs to be a degree of re-balancing so that plaintiffs bear a share of the risk of impecunious defendants, a share that reflects their ability to manage that risk in given transactions.

IAG firmly believes further reform, replacing joint and several liability with proportionate liability, would be beneficial and would introduce a far more equitable and responsible allocation of risk and the cost of litigated claims.

New Zealand perspectives

New Zealand's legal, economic and social framework is unique. Four things are of particular importance when considering the unique New Zealand landscape in which businesses and members of the public operate:

- The no fault Accident Compensation Scheme;
- The leaky building syndrome;

- The ease with which a company is able to be set up and wound up; and
- Litigation process issues.

Accident Compensation

The no-fault Accident Compensation Scheme removes the issue of personal injury claims when considering tort reform in New Zealand. This issue which the Australian Negligence Review Panel, chaired by the Hon Justice David Ipp, was faced with raised concerns about the adoption of proportionate liability. Ultimately personal injury claims were excluded from the proportionate liability regime in Australia. In New Zealand any move to proportionate liability would not affect a person's ability to obtain compensation under the ACC scheme. This factor weighing against a change can therefore be ignored.

Leaky buildings

The leaky building syndrome and its effect on local authorities, architects, engineers, building surveyors, builders, developers and other building industry participants has been well documented.

Delay in claims

The leaky building syndrome has highlighted the issues and exposed problems with continuing with joint and several liability in New Zealand. First, issues with a leaky home almost invariably take some time to manifest themselves. The defects are latent and it is not until water damage is seen that the underlying issue can be addressed. This manifestation can take many years to appear.

At the time the damage is discovered, and the home-owner seeks recourse, it is very often the case that the development company, builder, and a number of the parties involved in the building process have been wound up or are unable to contribute significantly.

Unfair spread of liability

The defendants left to meet the cost of rectifying the damage are usually those parties who hold insurance covering the claim, such as an architect or engineer, or the local authority. These 'deep pocket' defendants are then left to assume the liability for the mistakes of other defendants.

Disincentive to act prudently

This situation does not encourage homeowners to take reasonable steps to protect themselves. Armed with the knowledge that, as long as the relevant Council was involved in inspecting the property and issuing a Certificate of Code Compliance they will be able to recover in full, builders of homes have little incentive to ensure:

- They select appropriate contractors to undertake a building project.

- The building contracts fairly allocate risk.
- The personal liability of directors of building companies is considered.
- Other means of protecting against impecuniosity are considered, e.g., warranties from suppliers, insurance of contractors, bonds to secure performance.

It is hard to see the fairness in a system which enables plaintiffs to avoid the consequences of their failure to protect their own interests in this way.

Similar considerations apply in respect of plaintiffs who are subsequent purchasers of leaky homes. Although they might not have control of the building process, they can protect themselves by means of warranty from vendors and thorough pre-purchase inspections. The courts have endorsed the common sense of that: the failure by a purchaser after 2003 to obtain a LIM is at least contributory negligence and at most a break in the chain of causation.[1]

Builders, developers and other contractors have little incentive to ensure they hold appropriate insurance or hold assets to meet any potential claims as they know plaintiffs (and other defendants) will not pursue them if they are insolvent or impecunious.

This leads to a situation where a well-insured defendant, who may perhaps be responsible for only a minor fault in comparison with the fault of other persons, may nonetheless be made liable for the entirety of the damage suffered by the plaintiff.

Economic impacts

It was this outcome that led to the liability insurance crisis in Australia. This position has also affected the risk appetite of insurers providing liability insurance in New Zealand. Along with most New Zealand liability insurers, IAG has responded to the leaky building crisis by imposing exclusions for weathertightness claims. That has been the case since 2003. The insurance market's appetite for providing liability insurance to building industry participants under the current joint and several liability rule is limited.

The practical issue of the effect of proportionate liability on the affordability and availability of liability insurance is of considerable significance to those living and carrying on business in New Zealand. Greater affordability and availability of insurance will help ensure that the risk of insolvent or impecunious wrongdoers is minimised. A change to proportionate liability will, in IAG's view, lead to insurers offering broader cover and, in time, deletion of weathertightness exclusions in liability policies. That relaxation is not likely to occur under the present regime.

Under this heading, it is also worth bearing in mind the effect of the Canterbury earthquakes on the appetite of insurers and reinsurers to continue to carry on insurance business in New Zealand. This potential effect cannot be underestimated. The costs to insurers and their reinsurers of the property damage caused by these earthquakes has been well publicised. The effect of the associated claims on the availability and cost of both property and liability insurance in New Zealand is a work-in-progress. To date, the major impact has been a significant increase in the cost of cover.

To ensure New Zealand remains a market in which reinsurers and our multinational insurers wish to invest capital, some sort of reform is necessary. A

move to proportionate liability will allow insurers to underwrite their insured's risk safe in the knowledge that they will only bear the cost of the damage their insured causes.

Company incorporation and winding up

The ease with which a company can be incorporated and subsequently wound up contributes to the lack of viable defendants to a negligence claim. This type of risk avoidance is encouraged by current joint and several liability rule as the impact of the primary targets not being available is lessened by the fact plaintiffs can sue any party who contributed to the loss. It is manifestly unfair that the persons who have received the greatest financial gain from a project contribute nothing to a subsequent claim.

Litigation process issues

The effect of joint and several liability is exacerbated by four matters of procedure and process:

- Restrictions on the right to join third parties;
- Discontinuance rules;
- Contributory negligence; and
- Costs.

Third party joinder

The unfairness of joint and several liability is sometimes compounded by a rule which prevents defendants from joining parties who may be liable. As noted by the Review Paper, the provisions of the *Law Reform Act 1936* mean that a defendant can only join and seek contribution from parties who owe the plaintiff a tortious duty. The prospective third party has to be either a joint or concurrent tortfeasor (or owe the defendant a direct duty which is less often the case). A party that owes the plaintiff a duty only in contract, for example the provider of a warranty, is not at risk of being joined by a defendant. So defendants are doubly punished: they bear the losses of other tortfeasors and cannot spread the liability to parties who have a liability themselves.

The recommendations of the Commission to change to this rule have not been adopted by Governments since then. If piecemeal change of this type is not achievable, wholesale change is required.

Discontinuance in cases involving multiple defendants

In litigation where there are many defendants, any one defendant wishing to settle directly with a plaintiff is often unable to due to claims against it by co-defendants. Where plaintiffs have sued more than one defendant, they cannot discontinue against one defendant without the consent of all, or leave of the court[2]. That is a block on early resolution of claims which would disappear if joint and several liability was abandoned: there would be no need to have defendants

remain as parties if the liability of the remaining defendants was to be determined independently.

Contributory negligence

Contributory negligence on the part of a plaintiff is not treated in an equivalent manner to defendant liability. This point is noted somewhat tangentially in the Review Paper in chapter 3 under the Hybrids heading. In IAG's view, however, it is a potent illustration of the unfairness of joint and several liability.

The Review Paper's example 5 addresses the unfairness of the current regime and suggests an appropriate solution. All parties bear the consequence of the inability of D1 to pay. If that solution is appropriate for contributory negligence, it is hard to justify adopting a regime which is harsher where only the defendants are to blame for the plaintiff's loss.

It should be remembered that in situations where there is only one defendant and it is insolvent, the plaintiff bears the burden of the insolvency. In considering issues of overall fairness, it is not clear why this position should be reversed simply because there is more than one party who contributed to the loss.

Costs

In New Zealand costs are awarded to a successful litigant on a prescribed scale which does not reflect actual costs incurred. This has the effect that even successful litigants are left substantially out of pocket. This position is amplified by the additional costs associated with contribution claims between defendants and the associated barriers to early resolution of proceedings.

Currently, substantial shares of the awards of damages in leaky building cases are not being put towards remediating the leaky home. These awards are going towards the payment of legal and expert costs. Leaky building litigation has spawned its own industry, that of the weathertightness assessor or remediation specialist. The experts retained by each party to a leaky building proceeding, along with the associated legal representatives, end up with reportedly substantial shares of court damages awards. The plaintiff homeowner in these cases is often left with insufficient funds to complete necessary repairs.

A proportionate liability regime that eliminates contribution claims and facilitates early resolution of negligence claims will reduce the cost, complexity and length of associated legal proceedings. It will allow defendants to identify their role in the plaintiffs loss early and take steps to resolve the matter, often without the need for litigation. More of the eventual settlement funds will be available to repair the affected houses.

Insurance drivers

The impact of joint and several liability on the insurance industry should not be ignored. The Australian experience provides useful guidance for New Zealand on this issue.

Justice David Ipp AO in his report into reform of the law of negligence in Australia has said[3]:

> *"The 2002 insurance crisis demonstrated that insurance is the lifeblood, not only of commerce and industry, but of medical and other professional services, and many aspects of everyday life. The events of 2002 showed that, without the availability of reasonably priced indemnity insurance, the fabric of society is at risk."*

Justice JJ Spigelman, writing extra-curially, said that by 2002, what had always been a buyers' market in insurance had become a seller's market.[4] His Honour opined that 'a sudden explosion in insurance premiums or, in many cases, a refusal by insurance companies to offer cover on any reasonable terms or even at all, caused widespread concern.'

Justice Spigelman noted that 'insurance companies had come to be regarded as a bottomless pit or even a magic pudding.'

The current joint and several liability rule (along with the procedural aspects of joint and several liability) allows and encourages plaintiffs to join insured defendants that are only marginally liable or not liable at all in the hope that a sympathetic judge will find fault, even where there is none, to protect the plaintiff.

Justice Spigelman has said that over the course of three or four decades there had been a process of 'stretching the law'. His Honour pointed out that some judges prior and during the insurance crisis assumed that a defendant was insured and proceeded on that basis. This had led to what he termed, '*a progressive increase of the burden on those who had to pay insurance premiums*'.

Bob Carr, Premier of New South Wales (as he then was) in his second reading speech for the *Civil Liability Act 2002* (NSW), criticised judges extending liability with the benefit of hindsight saying:

> *"We need our roads and schools to operate free from unrealistic standards—standards imposed by the courts with hindsight and with no regard for the cost to the community."*

Joint and several liability encourages this deep pocket syndrome as it encourages claimants to direct their claims against respondents who have the greatest capacity to satisfy a judgment, rather than against respondents who are thought to have been primarily responsible for the loss. This is of particular concern to potential respondents such as professionals, local councils and governments.

The possibility of being found liable and being required to pay damages encourages defendants to settle for an amount in excess of the amount of their proportionate share of liability in order to avoid being forced to satisfy the entire judgment in the event that concurrent tortfeasors are insolvent. This acts to drive up the size of settlements.

That has flow-on consequences for insurers:

- It drives up premiums, as insurers have to assume their customers will end up bearing more than their actual share of blame.
- It forces insurers to set aside or reserve additional amounts in respect of claims. That is a direct cost to the insurer, which is passed on to policyholders.

The problems with providing liability insurance under a joint and several liability regime were vividly demonstrated in Australia and led to occupational groups:

- Ceasing offering services because of rising insurance costs;
- Withdrawing from offering services in areas where insurance is unavailable or unaffordable.

The best evidence of the impact of proportionate liability in Australia is what has happened in the market since its introduction:

- A number of new entrants by reason of the market being more attractive to insurers, particularly since 2005;
- Increased competition has kept a lid on premium increases as insurers have striven to retain market share;
- Reduction in average premium costs across Australia for both public liability and professional indemnity;[5]
- An increase in the number of public liability and professional indemnity risks written[6].

The risks set out above apply to New Zealand. There is no reason why the benefits of proportionate liability could not equally be experienced here.

CER considerations

The greater the simplification of doing business between New Zealand and Australia will be of benefit to New Zealand. A single liability regime, with the increased certainty of proportionate liability, should encourage Australian companies to carry on business here. A single regime means lower compliance costs and increases the ease in which new products can be introduced into the New Zealand market.

The State and Federal system of government in Australia has caused some issues with uniformity in the application of proportionate liability there. The Standing Committee of Attorneys General proposed model proportionate liability laws which should resolve this issue. A New Zealand model based on the uniform rules, once adopted, will ensure that Australian business will not be faced with decisions based on liability risk when considering entering the New Zealand market. It will also remove the incentive for 'forum shopping' between the two jurisdictions.

References

1 *Body Corporate 188529 v North Shore City Council (Sunset Terraces)*) [2010] NZSC 158 paragraphs 83, 84

2 Per High Court Rule 15.20(4)

3 D A Ipp and others *Final Report of the Review of the Law of Negligence* (Commonwealth of Australia, 2002).

4 JJ Spigelman, 'Negligence and Insurance Premiums: Recent Changes in Australian Law' (2003) 11 *Torts Law Journal* 1, 3.

5 Standing Committee of Attorneys-General Proportionate Liability regulation Impact Statement September 2011.

6 Ibid.