Zurich Australian Insurance Ltd v Withers

Court of Appeal CA317/2015; [2016] NZCA 618
13 and 14 July, 16 December 2016
Kós P, Randerson and Harrison and JJ.

Insurance – Professional indemnity cover – Exclusion clause – Whether insured entitled to indemnity – Whether acted dishonestly – Subjective and objective inquiries required.

Commercial law – Fair Trading Act 1986 – Financing arrangement – Misrepresentations – Damages – Basis for assessing compensation – Whether agent's conduct attributable to principals – Contribution to loss – Whether equal apportionment of losses between principals and accountant unreasonable – Fair Trading Act 1986, ss 9 and 43.

Professions – Chartered accountant – Degree of trust reposed by public – Standards of honesty higher than expected of ordinary person – Whether conduct that of prudent and honest accountant.

Through Aorangi Forests Ltd, which advanced funds to Orakei Securities Ltd, the Trustees of the Swindle Family Trust loaned $1.5 million to the Vintage group of companies (Vintage) in each of 2008 and 2009. They had been loaning money to Vintage annually since 2001 without incident. The funds were advanced as annual working capital for Vintage to grow grapes and make wine.

Orakei advanced the funds to Vintage under a term loan facility agreement. Each loan was for a term of two years, the second year of which allowed time to sell the previous year's vintage and yield funds for repayment. The loan facility agreement required each advance from the Swindles to be paid into the costs account. As a condition precedent to their loans the Swindles required an undertaking to Orakei from Mr Withers, acting in his capacity as the accountant to Vintage and its owners, that he was a mandatory joint signatory for the costs account and that the account would be used solely to meet production costs specified in the schedule that was required to be attached to the undertaking. Vintage repaid a small amount of the 2008 loan before defaulting and ultimately being put into liquidation in 2011.

The Swindles claimed their net loss for 2008 and 2009 was caused by Mr Withers and they sought damages. The High Court found Mr Withers had breached his duties to the Swindles under the Fair Trading Act 1986 (FTA) by making false and misleading statements in undertakings to the Swindles' agent, Mr Turner (who operated through Orakei). Mr Withers was found liable to 50 per cent of the Swindles' claim to reflect their contributory fault, principally through Mr Turner's negligence. The High Court also found that Mr Withers' professional liability insurer (Zurich Australian Insurance Ltd) was liable to

indemnify Mr Withers against the Swindles' judgment. Zurich appealed against the indemnity judgment and Mr Withers appealed against the damages award. The Swindles cross-appealed against the reduction in the damages award for contributory fault.

Held: 1 Mr Withers was not entitled to indemnity because his conduct on or before the giving of his 2008 and 2009 annual letters of undertaking was dishonest within the exclusion to cl 2.2 of his policy with Zurich. The correct test for determining dishonesty had subjective and objective elements. The Court was required to measure the insured's actual conduct and knowledge against an objective moral standard of what constituted honest conduct by a person having that knowledge. Mr Withers had signed, on successive annual occasions, unconditional undertakings that he was appointed as a mandatory joint signatory to Vintage's costs account and that the funds would only be used to meet production costs. The letters were false in both respects. Mr Withers knew, inter alia, that: his letters were required before the Swindles' funds could be drawn down; he had not made any inquiry over the years to satisfy himself that his annual statements were true; he had never signed a cheque drawn on Vintage's cost account for funds to be applied to meet production costs; he had never fulfilled the independent function which he warranted he would perform; he had limited knowledge of the production and financing arrangements within the Vintage companies; and that contrary to its obligations under the facility agreement Vintage had been making unauthorised loans to other companies in the group (see [78], [86], [90], [93], [94], [111]).

McMillan v Joseph (1987) 4 ANZ Insurance Cases ¶60-822 (CA) applied.

Royal Brunei Airlines Sdn Bhd v Tan [1995] UKPC 4, [1995] 2 AC 378 adopted.

2 Mr Withers had acted in reckless disregard of the Swindles' interest from the beginning. His recklessness was indistinguishable from a dishonest state of mind. Mr Withers must have known or appreciated that his undertakings were false. Expert evidence that a prudent and honest accountant would have ensured his statements were correct before they were made and that he would be in a position to comply with his undertakings, was affirmed by the New Zealand Institute of Accountants (NZICA) Code of Ethics. The degree of trust which the public reposed in the conduct of a professional person was also relevant. The Swindles sought and relied on Mr Withers' undertakings because he was a chartered accountant. The standards of honesty expected of a chartered accountant were higher than those expected of an ordinary person. Mr Withers' breaches of his fundamental professional obligations established that his conduct was dishonest by the objective measure. It amounted to sustained and conscious impropriety. Mr Withers passed the test for determining dishonesty (see [95], [96], [97], [98], [99], [100], [101], [102], [103], [104], [105], [109], [110]).

3 Damages under s 43 of the FTA for loss caused by misleading and deceptive conduct under s 9 were assessed on a compensatory or restorative basis. The wronged party was entitled to reimbursement of all expenditure wasted in changing its position in reliance on the misleading or deceptive conduct. The appropriate monetary award was the amount necessary to put the wronged party in the same position as it would have been but for the wrong. Mr Withers knew that the Swindles intended to rely on his undertakings, and that the undertakings were a precondition to the Swindles' annual advances to the Vintage companies. The Swindles would not have advanced any funds but

for Mr Withers' misrepresentations. Their loss was the full amount of the 2008 and 2009 advances before Orakei deducted its fees. That was $3 million less the sum of Vintage's repayment prior to its default. As no interest would have been payable if the transactions had not proceeded, the interest received in 2009 also had to be deducted from the claim (see [20], [36], [39], [40]).

4 It was correct to attribute Mr Turner's conduct to the Swindles because Mr Turner acted as the Swindles' agent for the purposes of making and managing the advances. He was engaged to represent the Swindles' interests on all aspects of the lending arrangements with Vintage. The Swindles relied on Mr Turner entirely for advice. Mr Turner explained the legal documents to them; he monitored the state of the investments throughout; and he liaised directly with the Vintage owners. The Swindles were passive investors who left Mr Turner responsible for managing the loans and he (through Orakei) charged a fee payable by Vintage. Mr Turner acted as if he was the Swindles for all purposes relevant to managing the loans. The Swindles had to assume the risk of Mr Turner's negligence in performing his duties (see [53], [54], [55], [58], [59], [60]).

Sherwin Chan & Walshe Ltd (in liquidation) v Jones [2012] NZCA 474, [2013] 1 NZLR 166 distinguished.

5 The apportionment of the Swindles' losses between them and Mr Withers equally was also correct. Taking all the factors into account, the High Court's reduction of 50 per cent of the Swindles' loss on account of their contributory fault was not unreasonable. If Mr Turner had monitored Vintage's financial statements carefully the Swindles would have learned as early as 2005 that Vintage was misapplying the advances. They would then have inevitably taken remedial steps, either by terminating the facility or by imposing more stringent and effective controls on Vintage's use of the funds. Further, if the Swindles had been advised of Vintage's prospective default and a requirement for bridging finance in December 2008, they would not have advanced the 2009 loan. The ultimate cause of the Swindles' loss was Vintage's failure. The Swindles' loss was not attributable to Mr Withers alone. Mr Withers' participation was central to the security arrangements, but his participation was irrelevant to the Swindles' underlying decision to invest in Vintage (see [66], [67], [68], [69], [70]).

Red Eagle Corporation Ltd v Ellis [2010] NZSC 20, [2010] 2 NZLR 492 considered.

Result: Appeal allowed. Judgment entered for Mr Withers against Zurich Australian Insurance Ltd set aside. Appeal against damages award allowed in part. Cross-appeal by the Trustees of the Swindle Family Trust dismissed.

Observations: Rule 41(1) of the Court of Appeal (Civil) Rules 2005, prescribes a mandatory 30-page limit for appellate submissions. Both the first and second respondents exceeded this limit by more than twice the number of pages. This proliferation and enlargement of synopses causes a fragmented approach that is neither acceptable nor, forensically, desirable (see [119], [120]).

Other cases mentioned in judgment

Colonial Mutual Life Assurance Society Ltd v Producers and Citizens Co-operative Assurance Co of Australia Ltd (1931) 46 CLR 41.

Cox & Coxon Ltd v Leipst [1999] 2 NZLR 15 (CA).

Erceg v Balenia Ltd [2008] NZCA 535.
Goldsbro v Walker [1993] 1 NZLR 394 (CA).
Harvey Corporation Ltd v Barker [2002] 2 NZLR 213 (CA).
Hickman v Turn and Wave Ltd [2011] NZCA 100, [2011] 3 NZLR 318.
Hickman v Turn and Wave Ltd [2012] NZSC 72, [2013] 1 NZLR 741.
IAG New Zealand Ltd v Jackson [2013] NZCA 302.
McCann v Switzerland Insurance Australia Ltd (2001) 203 CLR 579.
Narayan v Arranmore Developments Ltd [2011] NZCA 681, (2012) 13 NZCPR 123.
Nathan v Dollars & Sense Ltd [2008] NZSC 20, [2008] 2 NZLR 557.
O'Hagan v Body Corporate 189855 [Byron Avenue] [2010] NZCA 65, [2010] 3 NZLR 445.
Rae v International Insurance Brokers (Nelson Marlborough) Ltd [1998] 3 NZLR 190 (CA).
Schipp v Cameron [1999] NSWSC 997.
Vero Liability Insurance Ltd v Heartland Bank Ltd (formerly Marac Finance Ltd) [2015] NZCA 288.
Waikatolink Ltd v Comvita New Zealand Ltd (2010) 12 TCLR 808 (HC).
Waller v Davies [2005] 3 NZLR 814 (HC).

Appeal

This was an appeal by Zurich Australian Insurance Ltd, appellant, against a decision of Peters J [2015] NZHC 888, finding Zurich liable to indemnify Mark Donald Withers, first respondent, against the award of damages to Burvle Edward Swindle and Carolie Ann Terpening Swindle as Trustees of the Swindle Family Trust, second respondents, for Mr Withers' breach of duties under the Fair Trading Act 1986. The Swindles cross-appealed against the reduction in the damages awarded for contributory fault. Aorangi Forests Ltd was the third respondent, and Orakei Securities Ltd (in Liq) was the fourth respondent.

AC Challis and *HK Harkness* for Zurich Australian Insurance Ltd.
J Long and *SGT Ma Ching* for Mark Donald Withers.
DJ Heaney QC and *PA Robertson* for Trustees of the Swindle Family Trust, Aorangi Forests Ltd and Orakei Securities Ltd (in Liq).

Cur adv vult

The judgment of the Court was delivered by
HARRISON J.

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[Editorial note: This judgment begins at para [2].]

Introduction

[2] Burvle and Carolie Swindle are American citizens who loaned $1.5 million to the Vintage group of companies (Vintage) in each of 2008 and 2009 to a total of $3 million. The funds were advanced as annual working capital for Vintage's wine growing and producing business but the group used them for other purposes. Vintage repaid the Swindles $380,000 before defaulting and was later wound up. The Swindles have not recovered anything further from the company or various guarantors.

[3] The Swindles claimed their net loss of $2.62 million was caused by Mark Withers, Vintage's accountant. Following a defended trial in the High Court, Peters J found that Mr Withers had breached his duties to the Swindles under the Fair Trading Act 1986 (FTA) by making false and misleading statements in undertakings to the Swindles' agent upon which they relied before advancing each annual loan.[1] But the Judge reduced Mr Withers' liability to 50 per cent of the Swindles' claim to reflect their contributory fault, principally through their agent's negligence.[2] Judgment was entered for $1.31 million plus interest.[3]

[4] Peters J found that Zurich Australian Insurance Ltd, Mr Withers' professional liability insurer, was liable to indemnify him against the Swindles' judgment.[4] Zurich appeals against the indemnity judgment. Mr Withers appeals against the damages award in the primary judgment. And the Swindles cross-appeal against the reduction in the damages award for contributory fault. Mr Withers also seeks leave to adduce fresh evidence.

[5] We shall address, first, the issues of primary liability between the Swindles and Mr Withers – damages and contributory negligence – and, second, the issue of indemnity between Mr Withers and Zurich. Within each context we shall return more fully to the facts relevant to each issue.

Background facts

[6] In broad outline,[5] the Vegar family owned the Vintage group of companies through which they conducted their wine growing and producing business at Matakana. Among the companies were Matakana Estate Ltd (Matakana) and Goldridge Estate Ltd (Goldridge) which made and sold the wine.

[7] The Vegars raised money for the purpose of funding each year's wine vintage through the brokerage of Kingsley Turner. In turn he operated through corporate entities – Boston Securities Ltd and then Orakei Securities Ltd

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1 *Swindle v Withers* [2015] NZHC 888 [HC judgment].
2 At [125].
3 At [168]–[169].
4 At [165]–[166].
5 See also [14]–[82].

(Orakei) at the relevant times. The Swindles visited New Zealand frequently where they met Mr Turner. He introduced the Swindles to the Vegars and, after conducting due diligence inquiries, they agreed to lend funds to the Vintage companies.

[8] The funding arrangements, which operated through a multiplicity of intermediaries, commenced in 2001 and continued without incident until 2009. The Swindles were never in a direct contractual relationship with Vintage. Instead, their family trust loaned monies to a related company, Aorangi Forests Ltd (Aorangi), which advanced the funds to Orakei. In turn Orakei advanced the funds to Vintage under a term loan facility agreement, charging a fee of 2.25 per cent of the principal deducted on drawdown and interest at a higher rate than was payable on the underlying loans from the Swindles. Orakei was only obliged to repay the Swindles on a no-recourse basis if and to the extent that the Vintage companies repaid funds. Each loan was for a term of two years, allowing the borrower sufficient time to sell the year's vintage and yield funds for repayment. Another advance would be made for the coming year although repayment on the preceding advance remained outstanding. Also, Orakei assigned to the Swindles its rights under the facility agreement.

[9] The term loan facility agreement between Orakei and Vintage reflected the restrictions imposed by the Swindles on Vintage's use of the funds. For example, the 2008 facility agreement required Vintage to apply the funds to pay costs incurred in producing wine on these terms:[6]

> 2.3 **Purpose:** The proceeds of each Advance shall be applied by the Borrower solely for the purposes of meeting costs detailed in the Costs Schedule and not for any other purpose or for any unlawful purpose.
>
> 2.4 **Advances:** The Borrower acknowledges and agrees that each Advance ... shall be deposited into an account with a bank acceptable to the Lender (the "Costs Account"), which account shall be established solely for the purposes of meeting the costs specified in the Costs Schedule. Mark Withers is to be designated as a mandatory signatory to the Costs Account.

[10] The costs account was the account into which each advance from the Swindles was paid. The production costs specified in the schedule were the projected costs of producing the year's wine. The schedule was detailed. Expenses were itemised for purchasing juice, bottling, freight and setup costs spread over the year of the loan. Also included were itemised forecasts of income from net sales, escalating as the year progressed. All items, both of expenditure and income, were given an exact dollar figure. Each costs schedule was incorporated in each annual facility agreement between Orakei and the Vintage companies.[7]

[11] The Vintage companies produced each year's vintage through what were designated as A and B companies. Each company produced different blends. But new companies were not incorporated annually. Instead, the names of the A and B companies were changed to reflect the year of the loan. So the wine was produced each year by a differently named company – in 2008, for example, by 08A and 08B.

[12] Mr Withers and the Vegars had a long professional relationship. He was engaged to assist with tax planning and preparation of financial statements and

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6 See also [44]–[51].
7 At [30].

income tax returns for the Vintage companies. As a condition precedent to their loans the Swindles required an undertaking addressed to Orakei or its predecessors from Mr Withers, acting in his capacity as the accountant to Vintage and the Vegar family, that (a) he was a mandatory joint signatory for what was described as Vintage's costs account; and (b) the account would be used solely to meet production costs specified in a schedule attached to the undertaking. The costs schedule was to be attached to each facility agreement in the same form as the document which was to be attached to the undertaking. And Orakei was entitled to call up an advance and exercise all its rights if, among other things, Mr Withers ceased to be a mandatory joint signatory.

[13] As noted, the first of the two outstanding loans was made in April 2008 for a total of $1.5 million following Mr Turner's receipt of Mr Withers' letter on 27 March 2008 stating that:[8]

> I confirm that I have been irrevocably appointed until at least the time of repayment of each loan to Boston Securities Limited, by Vintage 2008 (A) Limited, and Vintage 2008 (B) Limited, as a mandatory joint signatory to the costs account.
>
> Further, I confirm that the costs account will be utilised solely to meet the production costs specified in the costs schedule. ...

[14] On 11 March 2009 Mr Withers sent a letter of undertaking to Mr Turner in the same form as the preceding year following which the Swindles advanced the Vintage companies $1.5 million in two instalments – $600,000 in March and $900,000 in April.

[15] In October 2009 Vintage defaulted on repayment of outstanding advances. The Vintage companies were placed in receivership on 9 December 2010 and into liquidation on 10 August 2011.

[16] Peters J found Mr Withers liable to the Swindles for misleading or deceptive conduct.[9] It was thus unnecessary to determine their alternative claim in negligence. However, the Judge would also have upheld that claim if necessary because Mr Withers owed a duty of care to the Swindles.[10] His breach caused the Swindles' loss. But their claim under the FTA was reduced by 50 per cent to allow for their equal contribution towards their loss principally due to Mr Turner's negligence.[11] Orakei was also a plaintiff but its claim was brought only to the extent the claims by the Swindles and Aorangi did not succeed.[12]

[17] Zurich declined Mr Withers' claim for indemnity on various grounds including dishonesty and recklessness. The Judge dismissed Zurich's defences and found for Mr Withers on the third party claim.[13]

Damages

[18] Section 9 of the FTA provides that:

> **9 Misleading and deceptive conduct generally**

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8 At [26]–[28]. The letter erroneously referred to Orakei's predecessor Boston Securities Ltd but nothing turns on this mistake.
9 At [11] and [88].
10 At [12].
11 At [125].
12 At [10]. Orakei claimed against Mr Withers under the Fair Trading Act 1986 and in negligent misstatement on the grounds it would not have made the investments in the Vintage companies but for Mr Withers' undertaking. Aorangi and the Swindles made an alternative claim based on Orakei's assignment of its causes of actions.
13 At [165] and [170].

No person shall, in trade, engage in conduct that is misleading or deceptive or is likely to mislead or deceive.

[19] At the relevant time, s 43 of the FTA provided:

> **43 Other orders**
>
> (1) Where, in any proceedings under this Part of this Act, or on the application of any person, the Court finds that a person, whether or not that person is a party to the proceedings, has suffered, or is likely to suffer, loss or damage by conduct of any other person that constitutes or would constitute—
>
> (a) A contravention of any of the provisions of Parts 1 to 4 of this Act; or
>
> ...
>
> the Court may ... make all or any of the orders referred to in subsection (2) of this section.
>
> (2) For the purposes of subsection (1) of this section, the Court may make the following orders—
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> ...
>
> (d) An order directing the person who engaged in the conduct, referred to in subsection (1) of this section to pay to the person who suffered the loss or damage the amount of the loss or damage ...

[20] Mr Withers knew that the Swindles intended to rely on his undertakings; and that they were a precondition to the Swindles' annual advances to the Vintage companies. However, all his undertakings from 2001 onwards were materially false. The Judge found that (a) Mr Withers was not a signatory – let alone a mandatory signatory – to the Vintage costs account; (b) instead of applying the advances to the costs of production as they arose, each Vintage company immediately transferred the funds to Matakana and Goldridge as intercompany loans;[14] (c) Mr Withers made no enquiry of the Vegars about the accuracy of the statements made in his letters; and (d) Mr Withers did not ensure that funds deposited in the costs account were applied in accordance with his letters, despite his knowledge that the Vegars' interests were complex and bordered on the "risky".[15]

[21] Peters J accepted Mr Turner's evidence that the Swindles sought Mr Withers' undertakings because the Vintage companies were single-purpose entities whose only business was to pay Matakana to make the wine and receive sufficient sale proceeds to repay the loans from Orakei – it was always intended that Vintage would have no other assets or liabilities.[16] Mr Turner was anxious to ensure that the use of the money was controlled.[17] He was satisfied that Mr Withers' participation in supervising payments made by Vintage and as a co-signatory with a list of wine-related expenses would ensure the money was not diverted elsewhere.[18] Mr Turner explained to the Swindles each year that Mr Withers' participation remained an important part of the lending structure.

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14 At [6].
15 At [147].
16 At [40].
17 At [41].
18 At [41].

He made enquiries which confirmed Mr Withers' good standing and reputation.[19] And, importantly, the Judge found the Swindles knew of and relied upon Mr Withers' undertakings when approving and making each advance to Orakei.[20]

[22] Mr Withers does not contest Peters J findings that he was in trade and that he engaged in conduct which was misleading or deceptive.[21] Nor does he contest her findings that his letters communicated that his signature would be required on every cheque drawn on the costs account; that this requirement would subsist until repayment of the loans; and that the funds in the costs account would only be disbursed to pay the costs of production specified in the schedule. Nor does Mr Withers challenge the Judge's finding that the Swindles were in fact misled or deceived by his conduct.[22]

[23] The Swindles' case was that they would not have made the advances without Mr Withers' undertakings. On that ground they sought reimbursement from Mr Withers of their entire loss. Alternatively, the Swindles claimed that their recoverable loss was the amount which would have been in the costs accounts on receivership if Mr Withers had complied with his undertakings. Peters J was satisfied there was little difference between the two approaches because Vintage paid all the funds away as soon as they were received from Orakei.[23]

[24] In the event the Judge found that Mr Withers' conduct was an effective cause of the Swindles' loss. On appeal Mr Long for Mr Withers does not challenge the Judge's causation finding. He challenges instead her finding that the full measure of the Swindles' loss was $2.62 million. He relies on two principal and interrelated grounds.

[25] First, Mr Long says the Judge overlooked the fact that the Vintage companies produced some wine in the 2008 and 2009 years. He says that loss of $2.62 million cannot be correct because when Mr Withers initially failed to "prevent" drawdown of that amount for the two-year period some of it went into wine production and came back to the Vintage companies. Thus his conduct did not cause loss to that full extent. Also, there is no evidence that $2.62 million of fresh funds actually came back from the sales of wine to the costs account for release back to Matakana and Goldridge in breach of Mr Withers' undertakings in 2010.

[26] Mr Long says the Judge should have assessed the measure of the Swindles loss at $944,678.11. He relied on an assessment conducted by an accounting witness, Brendan Lyne, of new or fresh funds of $649,506 introduced to Vintage in the period between 26 February and 12 March 2010. Mr Lyne's premise was that a "back-end gatekeeper" – the function said to be performed by Mr Withers in ensuring that the proceeds from wine sales repaid the loans – would only ever have had proper control over these funds, being the only monies which did not involve any necessary double counting of re-circulated or recycled funds. Adding two extra receipts by 09A and 09B on 29 June 2010 totalling $295,172.11, which were not put in issue, Mr Long says the total quantum of the Swindles' loss ought not to have exceeded $944,678.11.

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19 At [43].
20 At [42].
21 At [86]–[89].
22 At [97].
23 At [100].

[27] Second, and related to the first ground, Mr Long submits that the Judge erred in accepting the evidence of Grant Graham, an accounting witness called by Zurich. The Judge found:

> [107] ... that Matakana and Goldridge would have collapsed, and quickly, had Mr Withers performed his undertaking after draw down of the advances to the 08 companies. In that case, a substantial proportion of the funds advanced to 08A and 08B would have been in the costs accounts for recovery by the Plaintiffs and in all likelihood the Plaintiffs would not have made an advance in 2009.

[28] Mr Long cross-examined Mr Graham extensively at trial. On appeal he repeated the thrust of his challenge to the reliability of Mr Graham's analysis in a catalogue of arguments. He was particularly critical of Mr Graham's inability to quantify a different measure of loss from that fixed by Mr Lyne, based on what Mr Lyne described as Mr Withers' proper performance of a "modified gatekeeper" function – that is, a global assessment of what the Swindles would have recovered if Mr Withers had complied with his undertakings and the Vintage companies had collapsed earlier, triggering intervention and determination by the Swindles.

[29] We reject Mr Long's argument, which relies on Mr Lyne's evidence. His assessment of loss was advanced in a hypothetical vacuum far removed from the uncontested facts, the Judge's key findings, and the correct measure of damages available under the FTA. Its ultimate effect was to divert the High Court away from its proper inquiry. We can explain our reasons shortly.

[30] Mr Long's starting premise is that Peters J did not find the transactions would not have gone ahead if the Swindles had known the truth when Mr Withers signed the 2008 letter. He relies on this reference in Peters J's subsequent costs judgment:[24]

> [10] The sum that Mr Withers now proposes derives from a consent memorandum that the parties submitted on 8 August 2014. On its face, the memorandum was to record the Plaintiffs' loss calculated on a "no transaction" basis, which I declined to adopt. Moreover, the sum of $2,311,394 appears to treat payments of interest that were made as if they were repayments of principal. Given these points, counsel for Mr Withers withdrew the application and it is unnecessary to say more about it.

[31] This statement may appear antithetical to the Judge's finding in her substantive judgment, albeit briefly expressed, that:[25]

> I accept the [Swindles] submission that they relied on Mr Withers' undertakings in making the advances and that, *absent those undertakings, the advances would not have been made or the Plaintiffs would have required an undertaking to similar effect from a third party satisfactory to them.* [Emphasis added.]

[32] Earlier the Judge had found that:[26]

> The trustees and Aorangi knew of Mr Withers' undertakings prior to putting Orakei in funds and they would not have advanced funds to Orakei in the absence of Mr Withers' undertakings.

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24 *Swindle v Withers* [2015] NZHC 1706.
25 HC judgment, above n 1, at [107].
26 At [93].

[33] However, we do not share Mr Long's construction of Peters J's subsequent reference to declining to adopt Mr Withers' loss calculated on a no transaction basis. We construe the reference as applying to the calculation itself, not to the Judge's earlier causation finding. In any event we must proceed according to the Judge's findings in her substantive judgment – the judgment under appeal.

[34] Mr Long does not and could not challenge the Judge's findings that (a) Mr Withers' two related untrue statements were misleading and deceptive – that he held an irrevocable appointment as a mandatory joint signatory on the Vintage costs account and the funds would be used solely to meet wine production costs; (b) Mr Withers made the statements with the intention that the Swindles would rely on them and did in fact rely on them; and (c) Mr Withers' statements were central features of the security arrangements reflected in the facility agreement between Orakei and Vintage.

[35] It is thus unsurprising that on appeal Mr Withers does not challenge the Judge's acceptance of Mrs Swindle's evidence that they would not have made the 2008 and 2009 loans if they had known his statements were materially untrue.

[36] Damages awarded under s 43 of the FTA for loss caused by a breach of s 9 are assessed on a compensatory or restorative basis. The wronged party is entitled to reimbursement of all expenditure wasted in changing its position in reliance on the misleading or deceptive conduct. This measure is analogous to the tortious measure, not to the contractual measure of a lost expectation for a failure to perform a material representation. The appropriate monetary award is the amount necessary to put the wronged party in the same position as it would have been but for the wrong. The position to be restored is that which would have existed without the misrepresentation.[27] The amounts advanced in 2008 and 2009 – which would not have been made but for Mr Withers' misrepresentations – represent the restorative measure of the Swindles' loss less any recoveries.

[37] Mr Long's argument flounders on its assumption that damages can be fixed contrary to the Judge's causation finding by focusing on what the Swindles would have recovered if Mr Withers had performed his undertakings. That is not the correct inquiry. The so-called gatekeeper theories and Mr Lyne's complex "money go round" or circulation of funds theory do not apply in a situation where there would have been no funds to recirculate. Equally, the Judge's partial reliance on Mr Graham's evidence – predicated on the hypothetical assumption of Mr Withers' proper performance of his undertaking – is not determinative. Her finding that the transactions would not have been entered into but for Mr Withers' conduct is decisive on its own.[28]

[38] Mr Long also submits that Peters J erred in failing to discount damages in three respects. First, he says Orakei's lender's fee of 2.25 per cent of the principal should have been deducted because that money was beyond Mr Withers' control. This deduction is not a loss because it was never paid to the cost accounts and is not subject to Mr Withers' undertakings.

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27 *Cox & Coxon Ltd v Leipst* [1999] 2 NZLR 15 (CA) at 23 and 26, applied in *Harvey Corporation Ltd v Barker* [2002] 2 NZLR 213 (CA) at [13] and [19]; *Narayan v Arranmore Developments Ltd* [2011] NZCA 681, (2012) 13 NZCPR 123 at [49].

28 We will henceforth refer to this as the Judge's "causative finding".

[39] However, this argument does not survive the Judge's causative finding. The Swindles were the successful plaintiffs. They would not have advanced any funds but for Mr Withers' misrepresentations. Their loss – their wasted expenditure – was the full amount of the advances before Orakei's deductions of its fees.

[40] Second, Mr Long submits the Judge erred when, while giving credit for principal repayments, she failed to take into account the Swindles' receipt of $308,606 in interest payments between 31 March 2009 and 4 August 2009. We agree with Mr Long that this sum should be credited in Mr Withers' favour. The proper measure of loss is, as we have said, fixed on the premise that the transaction would not have proceeded. But for Mr Withers' misstatements, the Swindles would not have made the loans and no interest would be due from Vintage. Accordingly, the amount of the Swindles' recoverable loss must be reduced to $2,311,394 (subtracting $308,606 from $2.62 million). A further adjustment will be necessary once the cross-appeal on contribution is determined.

[41] It follows that the Judge erred in assessing interest on this basis:[29]

> I have already set out the components of [the Swindles'] loss. To the extent that the Vintage companies defaulted in instalments of interest (as I understand it, from October 2009), interest on the outstanding principal is allowed at the rate paid from time to time on funds in the costs accounts until the date the trustees commenced proceedings. This measure is consistent with performance of the undertakings. Thereafter interest accrues at the Judicature Act 1908 rate.

[42] Given the Judge's findings that the 2008 and 2009 loans would not have been made but for Mr Withers' misconduct,[30] interest could not be awarded on the premise of proper performance of an undertaking when there would have been no performance. The Judge found Mr Withers liable on what is essentially a tortious cause of action for additional loss in the form of unpaid contractual interest. However, this approach cannot be sustained. Mr Heaney for the Swindles accepted that a flat rate of five per cent would be fair for the duration of liability. In the normal course we would apply the Judicature Act 1908 rates, but we are content to adopt Mr Heaney's suggestion. In our judgment Mr Withers' liability for interest on the amended judgment sum should commence from 9 December 2010, the date when receivers were appointed to Vintage and it became clear that losses would be sustained.

[43] Third, Mr Long submits that Peters J should have reduced the award by a further $200,000, arising in the following way. In November 2010, when Matakana was wound up and liquidators were appointed, the company had possession of unbottled wine stock from the 2009 vintage. Vintage's receivers, appointed by Aorangi, claimed ownership of the wine stock. Litigation ensued between Vintage's receiver and Matakana's liquidator about title to this stock. Following a decision by Kós J in the High Court,[31] Vintage's receivers settled their claim against Matakana's liquidators for $200,000. But all these proceeds were exhausted in legal costs. Vintage's receivers made no net recovery.[32]

[44] Peters J rejected Mr Withers' claim to a credit for $200,000 for these reasons:

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29 HC judgment, above n 1, at [126].
30 At [107].
31 *Swindle v Matakana Estate Ltd (in liq)* [2012] 1 NZLR 806 (HC).
32 HC judgment, above n 1, at [66]–[67].

> [127] I have disregarded the $200,000 recovery arising from the payment by the liquidators of Matakana. There is no evidence before me that the costs incurred in achieving that recovery were unreasonable.

[45] Mr Long submits that even if Mr Withers had performed his role properly the Swindles would still have incurred costs in realising any assets from Matakana or Goldridge, and the failure to yield a net recovery is therefore not a failure for which Mr Withers should bear responsibility.

[46] We agree with Mr Long that the reasonableness of the litigation costs in recovering the $200,000 is irrelevant. However, his argument fails by virtue of the Judge's causative finding. As with Mr Long's other submissions, it is predicated on Mr Withers' notional proper performance of his undertaking, assuming the existence of a loan which the Judge found would not have been made.

Fresh evidence

[47] It is appropriate at this juncture to address Mr Withers' application to adduce further evidence. In his affidavit sworn on 1 June 2016 Mr Withers produced documents said to support a contribution defence that Aorangi and Orakei failed to lodge a caveat against the title to a five-hectare property owned by the Vegar interests. In consequence the property was transferred on 15 July 2009 to a third party for $3,071,000. The Swindles were unable to recover against the Vegars on their liability as guarantors. This evidence is said to support the Judge's finding that the Swindles contributed to their loss.

[48] In an affidavit sworn in reply for the Swindles, Mr Turner deposed that Orakei and Vintage agreed that the right to caveat only applied in the event of default by Vintage. As a result there was no event of default subsisting when the property was sold on 15 July 2009. Orakei would have been unable to sustain a caveat and prevent the transfer.

[49] In order to be admissible on appeal, further evidence must be fresh, credible and cogent. Evidence will not be fresh if it could have been produced at trial with reasonable diligence.[33] Only in exceptional and compelling circumstances will evidence which is not fresh be admitted.[34]

[50] Mr Long accepted Mr Withers' evidence was not fresh as it relates to events in 2009 which predated trial. He submits nevertheless that it should be admitted as the evidence is credible and cogent and this aspect of the adequacy of the Swindles' available security was not the focus of the trial. We disagree. The particulars pleaded by Mr Withers of the Swindles' contribution to their losses placed in issue the adequacy of the security given by Vintage and the Vegars. Mr Withers could and should have investigated this issue further such as by obtaining, by third party discovery if necessary, specific details of the Vegars' assets and liabilities at the relevant times. Furthermore, the factual contest between both deponents could only have been resolved by cross-examination.

[51] In any event we are not satisfied that this evidence is cogent and thus admissible for three reasons. First, no evidence is available of the equity available to the Vegars in the property: it is impossible to assess the financial effect of the alleged failure to lodge a caveat as the $3,071,000 for which it was sold may have all been applied to clear a mortgage to ASB Bank Ltd. Second,

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33 *Erceg v Balenia Ltd* [2008] NZCA 535 at [15].

34 *Rae v International Insurance Brokers (Nelson Marlborough) Ltd* [1998] 3 NZLR 190 (CA) at 193.

the failure to lodge a caveat is relatively insignificant given Mr Long's acceptance that the parties may have agreed a caveat could not be lodged unless there was a subsisting default. Third, as we shall explain, we agree with the Judge's finding on contribution for other reasons without needing to take account of the Swindles' alleged failure to lodge a caveat.

[52] The application for leave to adduce further evidence is therefore declined.

Contribution to loss

[53] The Swindles challenge the Judge's finding that they should bear their loss equally with Mr Withers, principally by virtue of Orakei's negligence. Her starting premise was to attribute the conduct of Mr Turner and Orakei to the Swindles. That was because Mr Turner acted as the Swindles' agent for the purposes of making and managing the advances.[35]

[54] Based on this premise of attribution, the Judge made these three factual findings of contributory fault:

(a) First, Mr Turner was on notice prior to Vintage's default that the company was making intercompany loans to Matakana and Goldridge in breach of its obligations under the facility agreement. Mr Turner received financial statements for all companies annually. Vintage's accounts for at least 2005 onwards showed a series of improper intercompany loans, including notes referring to the advances.[36] The Judge rejected Mr Turner's plea of his reliance on Mr Withers to absolve him of responsibility. She was satisfied Mr Turner should have been on independent inquiry.[37]

(b) Second, in December 2008 a Vegar family member advised Mr Turner that a Vintage company would default on its contractual repayment obligations to Orakei later that month. This occurred about nine months before Vintage's default on the Swindles' 2009 loan.[38] Mr Turner arranged short-term bridging finance, which was repaid. But he did not advise the Swindles of the Vegars' request or of his funding. Mr Turner's explanation that this event did not cause him concern about Vintage's financial standing was not accepted.[39] The Judge found the Swindles should have been more vigilant and acted more expeditiously when Vintage defaulted.[40]

(c) Third, the Swindles did not appoint receivers until December 2010. This was some 14 months after default.[41] While a creditor faced with default may be entitled to some leeway on enforcement, the Swindles' delay was excessive.[42] Increased recoveries might have been yielded on the evidence available. In particular there was evidence the Vegars may have removed assets from creditors in this 10-month period and introduced between $500,000 and $650,000 to the costs account after Vintage's default.[43]

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35 HC judgment, above n 1, at [109].
36 At [111]–[114].
37 At [115].
38 At [116].
39 At [117].
40 At [118].
41 At [119].
42 At [120].
43 At [120] and [122].

[55] Applying a "broad-brush" approach, the Judge apportioned losses equally.[44] She did not explain the grounds for her apportionment.

[56] Mr Robertson for the Swindles challenges Peters J's threshold finding of attribution. He advances two primary submissions. First, he submits the Judge was wrong to find that Mr Turner acted as the Swindles' agent and they are thus responsible for his acts or omissions. The Swindles' relationship with Orakei and Mr Turner was of a contractual nature between two distinct legal entities: the facility agreements recited that the relationship was "solely one of contract governed by this agreement". The relationship was best likened to one between a professional – an investment adviser – and a client. There was no scope to overlay a relationship of principal and agent. It follows that the inquiry should focus on the reasonableness of the Swindles' conduct and the state of their own knowledge, and whether it was an intervening operative cause of loss.

[57] Second, Mr Robertson submits that, even if there was an agency arrangement, there was no automatic imputation of the agent's knowledge to the principal; or that the consequences of the agent's conduct must be visited on the principal. He sought to rely on this Court's decision in *Sherwin Chan & Walshe Ltd (in liq) v Jones* (*Sherwin Chan*).[45]

[58] The rule of attribution derives from the relationship of principal and agent. The threshold question is whether that relationship existed here. If so, the Swindles are responsible for Mr Turner's acts and omissions as their agent as if they were their own, provided they are within the scope of his authority.[46] The attribution inquiry will depend on the tasks the agent was engaged to perform,[47] whether the agent was acting in an independent capacity,[48] and in some cases the policy of relevant legislation.[49] Imputation of the agent's knowledge to the principal will similarly depend on the scope and nature of the agency.[50] The existence of a contractual relationship between Aorangi and Orakei does not exclude a concurrent relationship of agency between the same parties or between the Swindles and Mr Turner, as no formalities are required to create a relationship of agency.[51]

[59] In our judgment, there could not be a stronger case for findings of agency and attribution. While Mr Turner's corporate persona was in a direct contractual relationship with Vintage under the term loan facility agreement, he acted as intermediary for the Swindles as the ultimate lenders and claimants under the FTA. The Swindles engaged Mr Turner or his corporate persona to represent their interests on all aspects of the lending arrangements with Vintage. The Swindles relied entirely on Mr Turner for advice. He explained the legal documents to them; he monitored the state of the investments

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44 At [125], applying *Red Eagle Corporation Ltd v Ellis* [2010] NZSC 20, [2010] 2 NZLR 492 at [39].

45 *Sherwin Chan & Walshe Ltd (in liq) v Jones* [2012] NZCA 474, [2013] 1 NZLR 166 at [59] and [61].

46 *Nathan v Dollars & Sense Ltd* [2008] NZSC 20, [2008] 2 NZLR 557 at [39]; Peter Watts and FMB Reynolds *Bowstead and Reynolds on Agency* (20th ed, Sweet & Maxwell, London, 2014) at [8–177].

47 *Nathan v Dollars & Sense Ltd*, above n 46, at [40].

48 At [8], adopting *Colonial Mutual Life Assurance Society Ltd v Producers and Citizens Co-operative Assurance Co of Australia Ltd* (1931) 46 CLR 41 at 48–49 per Dixon J.

49 *O'Hagan v Body Corporate 189855 [Byron Avenue]* [2010] NZCA 65, [2010] 3 NZLR 445 at [99]; *Sherwin Chan & Walshe Ltd (in liq) v Jones*, above n 45, at [62]; *Hickman v Turn and Wave Ltd* [2012] NZSC 72, [2013] 1 NZLR 741 at [94]–[98].

50 Watts and Reynolds, above n 46, at [8-207]; GE Dal Pont *Law of Agency* (3rd ed, LexisNexis, Australia, 2014) at [22.49]; *Hickman v Turn and Wave Ltd* [2011] NZCA 100, [2011] 3 NZLR 318 at [192]–[197]; *Waller v Davies* [2005] 3 NZLR 814 (HC) at [109].

51 Watts and Reynolds, above n 46, at [2-030] and [2-036].

throughout, for which purpose he was provided with copies of Vintage's annual financial statements; and he liaised directly with the Vegars. The Swindles were passive investors who left Mr Turner responsible for managing the facility, and for which he (through Orakei) charged a fee payable by Vintage. Mr Turner acted as if he was the Swindles for all purposes relevant to managing the loans.

[60] We agree with Mr Long that the Swindles must assume the risk of Mr Turner's negligence in performing those duties. Within the context of the broad powers to declare liability vested by s 43 of the FTA, Mr Turner's acts or omissions are treated as those of the Swindles for the purposes of apportioning liability. It would be anomalous and contrary to the underlying statutory policy of doing justice between the parties if Mr Withers' right to an apportionment of loss was defeated simply because the contributory fault was that of the agent who was authorised to exercise, and did exercise, all the principals' rights.[52] Mr Turner's omissions, and the Swindles' failure to take adequate legal steps to protect themselves against the consequences of his negligence, cannot absolve the Swindles from a contribution finding on a claim for damages against Mr Withers.

[61] This Court's decision in *Sherwin Chan* does not assist the Swindles. The claim was by a taxpayer against his accountants for negligent advice. A defence of contributory negligence based on attribution was rejected. That was because the inquiry was into the reasonableness of the principal's conduct, not its accountant's advice.[53] This situation is obviously distinguishable for the purposes of assessing whether on a contribution defence the agent's error should be attributed to the principal.[54]

[62] Mr Robertson does not challenge the Judge's first two findings on apportionment. Instead he submits, in keeping with his attribution argument, that the contribution inquiry should be limited solely to the operative effect of the Swindles' own acts or omissions – the Judge's third finding.[55] Without possession of Mr Turner's superior knowledge, Mr Robertson says the Swindles acted reasonably in relying on Mr Turner to negotiate with the Vegars and on Mr Withers' undertakings. They took reasonable care of their own interests. The only operative factor relevant to their conduct was their failure to appoint receivers immediately; and in this respect again they relied on Mr Turner's advice.

[63] We reject this limited argument. The Swindles themselves knew of Vintage's default 14 months before they appointed receivers. While a short delay in enforcing their security rights through Orakei may be justifiable, we agree with Peters J that they acted imprudently in waiting for such a lengthy period. As careful investors, the law expects them to take prompt steps to protect their secured interests. And, significantly, there is no challenge to the Judge's finding that the Vegars introduced at least $500,000 to Vintage's costs account after the company's default.

[64] The sole question is whether Peters J's apportionment survives challenge. A trial Judge applying a broad brush to FTA damages with the ultimate objective of doing justice between the parties is nevertheless required to undertake the orthodox evaluation of causative potency and relative

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52 *Red Eagle Corporation v Ellis,* above n 44, at [30]–[31].
53 *Sherwin Chan & Walshe Ltd (in liq) v Jones*, above n 45, at [59] and [68]–[70].
54 See generally *Byron Avenue*, above n 49; and *Sherwin Chan,* above n 45, at [62].
55 See [54(c)] of this judgment.

culpability within the contribution inquiry.[56] The culpability of third parties, such as Vintage and the Vegars, may be relevant.[57] The Judge's omission to carry out that exercise is not decisive as we are able to do so afresh on the evidential record.

[65] The Supreme Court's decision in *Red Eagle Corporation Ltd v Ellis* is an instructive example of the contribution assessment.[58] Red Eagle had loaned $250,000 to Annette Black in reliance on her fraudulent statement of assets and liabilities. When Red Eagle failed to recover the loan monies it sued Ms Black's business partner, Rick Ellis, for misleading or deceptive conduct. In considering whether Red Eagle had contributed to its loss, the Supreme Court referred to the "causal potency" of Mr Ellis's misrepresentation,[59] as well as Red Eagle's blameworthiness, finding the company was "very neglectful of its own interests in handing over Red Eagle's cheque immediately after receiving [a] financial statement and without searching the titles or making any other rudimentary check on ownership or seeking security from Ms Black or [her company]".[60] The Court upheld the High Court's equal apportionment of the lost loan principal between Red Eagle and Mr Ellis.[61]

[66] We are satisfied that the Swindles would have learned as early as 2005 that Vintage was misapplying the advances if Mr Turner had carefully monitored the company's financial statements. Inevitably they would have taken remedial steps – either by terminating the facility or imposing a more stringent and effective system of controls on Vintage's use of the funds. As a consequence they would not have likely suffered all of their eventual losses. This factor has significant causative potency.

[67] Also, we accept the Swindles would have taken decisive action in December 2008 if Mr Turner had advised them of Vintage's prospective default and requirement for bridging finance. There could not have been clearer evidence of financial distress, both for the company and its shareholders. In that event, the 2009 advances would not have been made, with a consequentially improved prospect of recovering the existing 2008 loan and any other outstanding monies from earlier years. The causative potency of this factor is necessarily speculative and of less force than the first.

[68] While the causative potency of these factors, together with the Swindles' delay in appointing receivers, might not necessarily justify a 50 per cent reduction, we are satisfied that two other factors are directly relevant. The first is relative culpability. The Swindles, advised by Mr Turner, exercised a commercial judgment with its attendant risks in agreeing to lend large and recurring amounts to Vintage. Mr Withers did not participate in or influence their investment decision. The ultimate cause of the Swindles' loss was Vintage's failure. It is wrong to visit all the financial consequences on Mr Withers whose participation, while central to the security arrangements, was irrelevant to the underlying investment decision.

[69] Second, on causative or causal potency, while it is not the subject of findings by the Judge, we agree with Mr Long that the Swindles could have

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56 Stephen Todd (ed) *The Law of Torts in New Zealand* (7th ed, Thomson Reuters, Wellington, 2016) at [21.2.07]; Harvey MacGregor *MacGregor on Damages* (19th ed, Sweet & Maxwell, London, 2014) at [7-006]–[7-007].

57 *Goldsbro v Walker* [1993] 1 NZLR 394 (CA) at 404.

58 *Red Eagle Corporation Ltd v Ellis*, above n 44. See also *Waikatolink Ltd v Comvita New Zealand Ltd* (2010) 12 TCLR 808 (HC) at [161]–[170].

59 *Red Eagle Corporation Ltd v Ellis*, above n 44, at [34].

60 At [39].

61 At [39].

done more to protect their loans by monitoring Vintage's financial situation. For example, they could have required audited accounts at the end of each year with independent verification that funds had in fact been applied for their agreed purpose. They could also have required security together with annually updated statements of assets and liabilities from the Vegars as guarantors.

[70] Taking these factors into account, we are satisfied that the Judge's reduction of 50 per cent of the Swindles' loss on account of their contributory fault is not unreasonable. As a result, the damages award must be reduced to $1,155,697, being 50 per cent of the Swindles' amended damages entitlement of $2,311,394.

Indemnity

Zurich's defence

[71] On 28 June 2009 Zurich and Mr Withers entered into a contract of professional indemnity insurance for the next 12 months. It was renewed annually. On 17 December 2010 Mr Withers notified Zurich of a possible claim. The insurer cancelled the policy on 28 September 2012.

[72] The insuring clauses under section 1 of the policy provided:

> **1.1 Civil Liability**
>
> Zurich will indemnify the Insured against any civil liability for breach of a duty owed in a professional capacity in connection with the Firm's Business, if a Claim in respect of such breach is first made against an Insured:
>
> (a) during the Period of Insurance; or
>
> (b) during or after the Period of Insurance and the Claim arises from a Reported Circumstance.
>
> **1.2 Defence Costs**
>
> Zurich will also indemnify the Insured against Defence Costs:
>
> (i) for any Claim covered by this Policy; or
>
> (ii) relating to any Reported Circumstance.

[73] Under s 2, which dealt with automatic extensions, coverage was extended to include liability under the FTA as follows:

> The following extensions to the Policy are included automatically.
>
> Each extension is subject (except to the extent that they may be varied by the extension) to the terms, conditions, limitations and exclusions of this Policy (including the Insuring Clauses).
>
> The inclusion of these extensions (with the exception of Automatic extension 2.17) does not increase the Limit of Indemnity.
>
> ...
>
> **2.2 Fair Trading Act**
>
> Zurich will indemnify the Insured against any civil liability arising out of a breach of Sections 9 to 14 of the Fair Trading Act 1986 (or any similar fair trading legislation in the States or Territories of the Commonwealth of Australia), in respect of any conduct alleged to have been misleading or deceptive or likely to mislead or deceive, PROVIDED THAT *Zurich will not Indemnify the Insured where such liability arises from conduct which was dishonest, fraudulent, criminal, malicious or intended by the Insured.* [Emphasis added.]

[74] Clause 4.3, which covered disentitling conduct by an insured party, is also relevant. It provided:

> Zurich will not indemnify [Mr Withers] against any liability or Claim (or related Defence Costs) arising from:
>
> ...
>
> **4.3 Dishonesty**
>
> (a) *arising out of or connected with any actual or alleged dishonest,* fraudulent, criminal, or malicious act or omission of any Insured or their consultants, contractors, sub-contractors or agents; or
>
> (b) arising out of or connected a willful breach of any statute, contract or duty, or any act or omission committed or omitted or alleged to have been committed or omitted with a *reckless disregard for the consequences* by the Insured or their consultants, contractors, sub-contractors or agents; or
>
> ... [Emphasis added.]

[75] Before us Ms Challis for Zurich relied on both the dishonesty proviso to cl 2.2 and the dishonesty exclusion in cl 4.3. First, she submitted that the dishonesty proviso applies to Mr Withers' claim for indemnity under cl 2.2. Second, or alternatively, she submitted that the "reckless disregard" extension of dishonesty in cl 4.3(b) applied to a claim under cl 2.2. In the event it will only be necessary for us to determine the first ground.

High Court decision

[76] Zurich advanced both grounds of defence in the High Court. Peters J found that Zurich was liable to indemnify Mr Withers under cl 2.2 on the Swindles' principal claim under the FTA unless his liability arose from dishonesty; proof of recklessness was insufficient.[62] In dismissing Zurich's dishonesty defence, the Judge noted its importation of both subjective and objective elements.[63] She referred to Mr Withers' evidence of misunderstanding the contents of the letters – saying he believed he was required to be a signatory on the costs account but not that he was required to sign every cheque. She appeared, however, to accept Ms Challis' submission that Mr Withers must have understood what his letters meant.[64] The Judge then continued:

> [163] The critical matter, however, is Mr Withers' email to Jean Vegar in March 2009. The inference I draw from that email is that it was only at that time that Mr Withers understood the implications of his letters. There was no reason for Mr Withers to send the email otherwise.
>
> [164] Mr Withers' explanation for not persisting in seeking a reply to that email was that he overlooked the matter. His practice was in the course of filing numerous tax returns for many clients in advance of the 31 March deadline and that consumed his attention at the time.
>
> [165] Given my findings as to his state of knowledge, I am not satisfied that Mr Withers' conduct was dishonest within the meaning of clause 2.2 of the policy.

[77] We agree with Ms Challis that this approach is unsustainable. Mr Withers' email to Mrs Vegar has little if any relevance to Zurich's

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62 HC judgment, above n 1, at [158].
63 At [160].
64 At [161]–[162].

defence.[65] The Judge did not give any other reasons for her decision or undertake an inquiry into the two elements she had earlier identified. In normal circumstances we would remit the proceeding to the High Court for reconsideration. However, we agree with Ms Challis that the question of whether Mr Withers' acted dishonestly can be determined by inferences drawn from primary facts which are not in material dispute and where no question of credibility arises.[66] We are in as good a position as the High Court to determine whether the dishonesty exclusion applies.

Legal principles

[78] Before us, and in the High Court, counsel were largely at one about the correct test for determining dishonesty within the meaning of cl 4.3 of the policy's exclusions. It has been settled in the indemnity context by a number of decisions of this Court.[67] The inquiry incorporates both subjective and objective elements: in broad outline, the Court is required to measure the insured's actual conduct and knowledge against an objective moral standard of what constitutes honest conduct by a person having that knowledge. Proof of an intention to deceive is not necessary.

[79] However, in view of the nature of Mr Long's argument for Mr Withers, we must expand briefly on both the subjective and objective elements of dishonesty. On the first or subjective element, we agree with counsel that the Privy Council's formulation in *Royal Brunei Airlines Sdn Bhd v Tan* (*Royal Brunei*) applies:[68]

> [A]cting dishonestly, or with a lack of probity, which is synonymous, means simply not acting as a honest person would in the circumstances. This is an objective standard. At first sight this might seem surprising. Honesty has a connotation of subjectivity, as distinct from the objectivity of negligence. Honesty, indeed, does have a strong subjective element in that is a description of a type of conduct assessed in the light of what a person *actually knew at the time*, as distinct from what a reasonable person would have known or appreciated. Further, honesty and its counterpart dishonesty are mostly concerned with advertent conduct, not inadvertent conduct. Carelessness is not dishonesty. Thus for the most part dishonesty is to be equated with conscious impropriety. [Emphasis added.]

[80] On the second or objective element, the Board continued in *Royal Brunei*:[69]

> However, these subjective characteristics of honesty do not mean that individuals are free to set their own standards of honesty in particular circumstances. The standard of what constitutes honest conduct is not subjective. Honesty is not an optional scale, with higher or lower values according to the moral standards of each individual.

[81] And later the Board stated:[70]

> [H]onesty is an objective standard. The individual is expected to maintain the standard which would be observed by an honest person placed in those

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65 See [89]–[91] of this judgment.
66 *McMillan v Joseph* (1987) 4 ANZ Insurance Cases 60-822 (CA) at 75,054.
67 *McMillan v Joseph*, above n 66, applied in *IAG New Zealand Ltd v Jackson* [2013] NZCA 302 at [18] and *Vero Liability Insurance Ltd v Heartland Bank Ltd (formerly Marac Finance Ltd)* [2015] NZCA 288 at [39].
68 *Royal Brunei Airlines Sdn Bhd v Tan* [1995] UKPC 4, [1995] 2 AC 378 at 389.
69 At 389.
70 At 390.

> circumstances. ... *Acting in reckless disregard of others' rights or possible rights can be a tell-tale sign of dishonesty*. An honest person would have regard to the circumstances known to him, including the nature and importance of the proposed transaction, the nature and importance of his role, the ordinary course of business, the degree of doubt ... and the seriousness of the adverse consequences [to third parties]. The circumstances will dictate which one or more of the possible courses should be taken by an honest person. [Emphasis added.]

[82] The area of contention before us related to the objective element and Mr Long's attempt to relegate the importance of evidence of professional standards. In his submission such evidence can assist the Court, but only sometimes. He sought to rely on *McMillan v Joseph* where this Court found for an insurer which raised a dishonesty defence to exclude liability.[71] A solicitor, Jack Moulder, was the insured party. He failed to disclose to his client his interest in and control over a company in which he recommended she invest funds. Mr Moulder neither obtained a specific prior authority nor recommended the client to take independent advice. The company failed and the client lost her investment. Judgment was entered for her loss against Mr Moulder who sought indemnity from his underwriters.

[83] Mr Moulder did not give evidence himself at trial. The insurer led evidence from experienced lawyers to show that Mr Moulder knew or would have known of his professional obligation as a lawyer to advise his client properly. All three members of this Court emphasised that the solicitor's conduct was to be judged by the standard of honesty generally accepted as appropriate for members of the legal profession.[72] While acknowledging the importance of the evidence of ordinary professional practice given by two solicitors at trial, Cooke P observed that Mr Moulder's failure to take proper precautions was so elementary that the case could be decided without resorting to it.[73]

[84] Mr Long's premise was that evidence of professional standards was relevant in *McMillan v Joseph* only in enabling this Court to infer that in the absence of Mr Moulder's evidence he actually knew of his obligation to give proper advice and thus knowingly breached it. Mr Long's purpose was to limit the relevance of expert evidence to the subjective inquiry. We reject that proposition. Evidence of professional standards is of singular relevance as providing the objective or ordinary measure of dishonesty. We note that its relevance in this context is beyond question in Australia.[74]

[85] Evidence of professional standards has direct relevance to Zurich's appeal. The insurer called Andrew McKay, an experienced chartered accountant. He gave evidence of appropriate professional standards. The Judge treated his evidence as material only to Zurich's defence (not pursued in this Court) of whether the indemnifier was excused by reason of Mr Withers'

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71 *McMillan v Joseph*, above n 66.
72 At 75,054 per Cooke P, 75,055 per Somers J and 75,056 per Casey J.
73 At 75,055.
74 See *Schipp v Cameron* [1999] NSWSC 997 at [918]; and *McCann v Switzerland Insurance Australia Ltd* (2001) 203 CLR 579 at [62].

knowledge of prior circumstances likely to give rise to a claim. She dismissed this defence.[75] She did not consider Mr McKay's evidence further.[76] As will become apparent, we accept that Mr McKay's evidence is directly material to the objective element.

Analysis

(a) Mr Withers' conduct

[86] It is necessary to expand on the relevant facts before addressing the discrete issue of Mr Withers' subjective state of knowledge. Mr Withers' conduct when giving the 2008 and 2009 undertakings is our reference point. However, his actions on those particular dates cannot be seen in isolation from his recurring conduct since 2001. On at least eight successive annual occasions up until 27 March 2008 he signed unconditional undertakings that he was appointed as a mandatory joint signatory to Vintage's costs account; and that that account would be used solely to meet production costs specified in the costs schedule. Each letter was false in both respects.

[87] It is notable that in 2003 Mrs Vegar provided bank account operating authorities for Mr Withers to sign with her request for the letter. He then became a co-signatory but not a mandatory signatory to Vintage's accounts with BNZ later that year. In 2004 Mr Withers did not receive or request any bank account operating authorities when giving his letter, even though by then he believed the letter required him to be a co-signatory to the accounts. In that year Vintage's bank account numbers were deleted from the letter. Mr Withers did not request fresh bank account operating authorities when Vintage changed banks. Also, on 17 March 2004 Mrs Vegar asked Mr Withers to amend and reissue his 2004 letter to say that he had been "irrevocably appointed until at least the time of repayment of each loan to [Orakei]". In explanation at trial Mr Withers said "I did as I was bid".

[88] By mid-2008, within a few months of signing his annual undertaking, Mr Withers had decided the Vegars' affairs had become too complex and risky for his firm. The trigger was an audit by the Inland Revenue Department. He advised the Vegars to retain another firm. The transition of work commenced in November 2008.

[89] On 3 March 2009 a Vintage employee requested Mr Withers to sign his annual letter. He declined as he was no longer acting as the company's accountant. A week later Peter Vegar called Mr Withers, requesting that he continue to act as tax agent and accountant for Vintage. His tone was flattering and praising, even though it was unusual and out of character. Mr Withers agreed to comply, and to sign his annual letter.

[90] Shortly afterwards, Mr Vegar asked Mr Withers to "edit/copy/paste" an amended wording into his letter to enable the Vegars to draw down funds on 12 March. Later on 11 March he emailed Mrs Vegar. Given its centrality to the Judge's decision,[77] we repeat its relevant passages as follows:

> Can I clarify something please ...
>
> The letter I have signed for the Vintage companies confirms I am a mandatory signatory but I don't ever recall actually signing any payments on the accounts. Are we actually operating this in accordance with the confirmation I have given?

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75 HC judgment, above n 1, at [143]–[150].
76 At [141]–[142].
77 See [38]–[39].

Are they assuming I am signing all payments?

[91] Mrs Vegar did not respond. Mr Withers did not pursue the issue further. The next day Vintage requested Mr Withers to sign and backdate two summary sheets for production cost schedules to 11 March 2009. Mr Withers complied without inquiry.

(b) Mr Withers' subjective knowledge

[92] The subjective element of the dishonesty inquiry is of central importance: what was Mr Withers actual state of knowledge in 2008 and 2009? Mr Long relies on what he says was Mr Withers' state of belief that he was a co-signatory to the costs account and was not required to sign every cheque on the account; that the letters conveyed his position accurately; that his knowledge that he would able to check any cheque he was asked to sign against the cost schedule was conveyed by his letters when he stated the account would be solely to meet production costs; and that he had reasonable grounds to support the contents of his letters as he understood them.

[93] In our judgment Mr Withers' evidence that he believed he was only a co-signatory and not a mandatory signatory cannot withstand scrutiny when all the evidence and context is considered. The focus is on his state of knowledge – what he actually knew at the time.[78] In March 2008 and 2009:

(a) Mr Withers knew that his letters were required to satisfy a condition precedent in Vintage's loan agreement before the company could draw down the Swindles' funds for the next year; and that the Swindles were relying on his undertakings to be true and accurate.

(b) Mr Withers knew that he had made no inquiry at any time over the preceding seven or eight-year period to satisfy himself that his statements were true – that is, he was a mandatory joint signatory to the costs account and the funds would be used only to meet production costs set out in the attached schedule.

(c) Apart from two cheques in 2001, Mr Withers knew that he had never signed a cheque drawn on Vintage's costs account for funds to be applied to meeting production costs. He knew he had never fulfilled the independent function which he warranted he would perform in each ensuing year. He knew his role as signatory was to ensure the Swindles' funds were applied for their proper purpose but never once complied. He knew, or had to know, that the Swindles' control mechanisms, which he was responsible for overseeing, were not in place.

(d) Mr Withers knew that he had limited knowledge of the production and financing arrangements within the Vintage companies; and that he had signed financial statements showing Vintage had changed its bank but did not enquire whether this affected his undertakings.

(e) Mr Withers knew that, contrary to its obligations under the facility agreement, Vintage had been making unauthorised loans to other companies in the group, even though he knew the lending arrangements required isolation of the Swindles' funds from Matakana's operations.

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78 See [80] of this judgment, quoting *Royal Brunei Airlines Sdn Bhd v Tan*, above n 68, at 389.

[94] We emphasise Mr Withers' unequivocal representations of two facts. The first – communicated in 2001, 2002 and 2003 – was a confirmation that he had been appointed by Vintage "as a mandatory joint signatory to the costs account". This changed in 2004 and, for the duration of his undertakings to 2009, read as confirmation that:

> I have been irrevocably appointed ... [until] repayment of the loan as a mandatory joint signatory to the costs account.

[95] According to Mr Withers, this statement meant that Vintage's financing arrangements required an independent co-signatory to cheques drawn on the costs account and that his function was reduced to that of an "alternate signatory". He did not understand "mandatory joint signatory" to mean that he was required to sign every cheque.

[96] This explanation is simply not available for an experienced chartered accountant when read against the plain words used, especially in context with the second confirmatory statement in his letters that "the costs account will be utilised solely to meet the production costs specified in the costs schedule". There is no room for confusion or misbelief. Mr Withers was representing to the Swindles that he held an irrevocable appointment as a mandatory joint signatory to the costs account – that is, all cheques drawn on that account – and that he would use his power to ensure that all monies in the costs account, which he knew were advanced by the Swindles, would be used solely to meet production costs specified in the schedule. This representation was of such importance to the facility agreement that Orakei was entitled to call up the loan if Mr Withers was no longer a mandatory joint signatory.

[97] Mr Withers rationalised the second confirmatory statement, which prescribed a special purpose for application of the funds, as meaning that if he was asked to sign a cheque he was required to make sure it related to an item on the costs schedule. He would only sign if satisfied that the cheque was to meet production costs by reference to that schedule. Again, that explanation cannot be reconciled with the pattern of false statements made by Mr Withers over a number of years or the plain words of his undertakings.

[98] Mr Withers' alternative position is that he did not act dishonestly because he relied principally on the Vegars whom he trusted from a long professional association. When cross-examined about why he signed the letters stating that he was a mandatory joint signatory to the costs account, he answered that "in my mind I had been appointed by my client to that role". After agreeing to sign the undertakings, Mr Withers said he relied on Jean Vegar to "honestly and correctly, set up the account operating authorities in a way consistent with what the loan agreements required ... and I believe she was doing that" (he never took any steps for the purpose of confirming that belief). Again in cross-examination Mr Withers expressed his belief that he could give the undertakings based on his trust in and reliance on the Vegars. He did nevertheless accept that he was aware of his professional obligations, including that he should not give an undertaking without reasonable grounds for believing it would be honoured.

[99] Mr Withers cannot excuse his misconduct by resorting to reliance on the Vegars. His statements represented unequivocal assurances to the Swindles of his control of Vintage's use of the funds; in that context he cannot seek to default to a state of control by the Vegars. The undertakings were personal to him. He fell into a pattern of making successively false statements, the truth of which he never verified for himself. He cannot now advance a rationalisation which is at direct odds with his actual conduct year after year.

[100] Mr Withers also sought to excuse himself on the ground that the letters were routine. He was content to rely on the fact that loans were being repaid and "the financing structure seemed to be working". He saw nothing onerous in the request to provide an undertaking. It was, instead, "a low level commitment, a formality of the financing arrangement".

[101] By 2008 Mr Withers' conduct had long passed the stages of inadvertence and indifference. Without doubt, Mr Withers acted in reckless disregard of the Swindles' interest throughout. In this context his recklessness is indistinguishable from a dishonest state of mind as a "tell-tale sign of dishonesty".[79]

[102] In our judgment, the only inference available from the fundamental and repetitive pattern of Mr Withers' false statements, when coupled with his knowledge of Vintage's financial accounts, is that he must have known or appreciated they were false.[80]

(c) Objective standards

[103] Our answer on the objective element follows inexorably from our analysis of Mr Withers' state of mind. Applying the *Royal Brunei* approach,[81] an honest person in Mr Withers' position when giving his undertakings would have had regard to all the circumstances known to him. Included among them were the nature and importance of the proposed loan, the nature and importance of his professional role when making representations of fact to the lender, and the seriousness of the adverse consequences for the Swindles if his statements were wrong.

[104] Moreover, Mr McKay's evidence was unchallenged that a prudent and honest accountant would have ensured his statements were correct before they were made; and that all necessary arrangements were in place to ensure he would be in a position to comply with his undertakings. Without this evidence, an honest accountant would not have given the undertakings. Nor would he rely on his clients to ensure that the appropriate arrangements were in place. Such an approach would compromise the independence of an honest accountant.

[105] The New Zealand Institute of Accountants (NZICA) Code of Ethics reaffirms this evidence. It opens with a recital of the Principle of Integrity:

> Members must behave with Integrity in all professional and business relationships. Integrity implies not merely honesty but fair dealing and truthfulness.

[106] By Rule 2 of the Fundamental Principle of Integrity, which concerns the making of false or misleading statements:

> *A member must not make, prepare or certify any statement which the member* knows, believes or *ought to know to be false*, incorrect or misleading ... by reason of any misstatement ... of a material fact or otherwise. [Emphasis added.]

[107] An explanatory note to Rule 2 provides that:

> A member must not give an undertaking, or make a pledge or promise to a client or third party unless the member has reasonable grounds for believing that the undertaking, pledge or promise will be honoured.

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79 *Royal Brunei Airlines Sdn Bhd v Tan*, above n 68, at 390.
80 At 389.
81 At 389–390.

[108] The separate Fundamental Principle of Objectivity and Independence affirms an accountant's obligation to be "fair, impartial and intellectually honest". An explanatory note elaborates that members must "avoid any subordination of their judgement" and "remain Objective in the performance of all professional work" including continually reviewing and managing the risks to their objectivity.

[109] An additional factor within the objective inquiry is the degree of trust which the public reposes in the conduct of a professional person. Peters J found that the Swindles sought and relied on Mr Withers' undertakings because he was a chartered accountant.[82] The standards of honesty expected of a chartered accountant in Mr Withers' position are higher than those expected of the ordinary person. The nature and extent of Mr Withers' breaches of his fundamental professional obligations are not only evidence that he knew what was required of him. They establish also that his conduct was dishonest by the objective measure. It amounted to sustained and conscious impropriety.

[110] We add that, to the extent it is relevant, Mr Withers' conduct when signing the March 2009 undertaking and his surrounding conduct confirms his dishonesty. We refer in particular to his decision to sign and backdate two summary sheets for production costs schedules to 11 March 2009 to enable drawdown. We reject Mr Withers' rationalisation that it was a "minor formality to be corrected".

[111] It follows that Mr Withers' conduct on or before 27 March 2008 and 11 March 2009 when he gave his seventh and eighth letters of undertaking to the Swindles was dishonest within the exclusion to cl 2.2 of his policy with Zurich, and that his liability arose from or was connected with those dishonest acts or omissions. Accordingly, he is not entitled to indemnity.

Result

[112] The appeal is allowed and the judgment entered for the first respondent against the appellant is set aside. Judgment is entered for the appellant against the first respondent.

[113] The appeal by the first respondent is allowed to the extent that:

(a) The judgment sum of $1.31 million is set aside. Judgment is entered for the second respondent against the first respondents for the sum of $1,155,697.

(b) The first respondent is ordered to pay interest to the second respondents on the amended judgment sum in accordance with [42] of this judgment.

[114] The cross-appeal by the second respondents is dismissed.

[115] The application by the first respondent for leave to adduce further evidence is declined.

[116] The first respondent is ordered to pay the appellant costs for a standard appeal on a band A basis with usual disbursements.

[117] The second respondents are ordered to pay costs to the first respondent on the cross-appeal for a standard appeal on a band A basis (plus a 50 per cent uplift to reflect the first respondent's limited success on the appeal against the damages award) together with usual disbursements.

[118] Costs in the High Court are to be fixed by that Court in accordance with the result of the appeal and cross-appeal.

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82 HC judgment, above n 1, at [49].

Postscript

[119] We reinforce the need for focus in appellate submissions. The mandatory 30-page limit prescribed by r 41(1) of the Court of Appeal (Civil) Rules 2005 is intended to secure that focus. Mr Withers' synopses of submissions on the primary appeal ran to 67 pages, more than double the allowed number, together with further synopses of 18 pages and 11 pages respectively on cross-appeal and interest issues. The Swindles filed a series of synopses exceeding 60 pages.

[120] This proliferation and enlargement of synopses beyond the rules is neither acceptable nor, forensically, desirable. Despite the difficulties caused to this Court by counsels' fragmented approach, we have attempted to address all of what we have identified as the primary competing arguments on each major issue.

Appeal allowed. Judgment entered for Mr Withers against Zurich Australian Insurance Ltd set aside. Appeal against damages award allowed in part. Cross-appeal by the Trustees of the Swindle Family Trust dismissed.

Solicitors for Zurich Insurance: *McElroys* (Auckland).
Solicitors for Mr Withers: *LeeSalmonLong* (Auckland).
Solicitors for the Trustees of the Swindle Family Trust, Aorangi Forests Ltd and Orakei Securities Ltd (in Liq): *Heaney & Partners* (Auckland).

Reported by: Edith PA Shelton, *Barrister*