THE NEW ZEALAND
LAW
JOURNAL
PUBLISHED BY BUTTERWORTHS JULY 1999

MR PREBBLE AND THE LAW

Mr Richard Prebble, the leader of ACT, has made an important attack on the conduct of the judiciary in recent years and warned that it is risking demands for political oversight of appointments.

These attacks are no less important for the obvious thinness of the material in *I've been writing*. The book is clearly aimed at a wide public in an election year and it is not to be supposed that Mr Prebble has used the most sophisticated arguments available to make his case.

But if one reads what is there, and ignores the personalia, there are important arguments underlying the material and it is an indictment of our law faculties that there are so few academics putting forward the same arguments in more elevated style.

The picture that Mr Prebble paints of the way in which the Waitangi process has gone out of control would justify lengthy discussion in itself, and this editorial will restrict itself to more traditionally legal subjects.

The essence of Mr Prebble's complaints are that the judiciary has lost sight of the rule of law, that they are usurping the role of Parliament in making social policy, that Parliament itself has acted unwisely and that there is a self-sustaining politically correct clique at the heart of the Ministry of Justice which presses on to achieve its own goals regardless of the Minister or the government.

In the end, however, Mr Prebble's arguments are confused by the twentieth century failure to clarify the relationship between the rule of law, which requires set principles which bind Judges, and a majoritarian position, which requires that unelected Judges not interfere in matters which belong to Parliament.

Mr Prebble does show that he sees the potential for the conflict, however, when he points out that Parliament has passed legislation which offends against the rule of law and threatens the pillars of our civilisation such as private property rights and the enforcement of agreements.

Unfortunately, Mr Prebble claims that it is the right of the nation's law-makers, ie Parliament, to make social policy. But social policy is nothing to do with law, however commonplace it may be to believe today that all Acts of Parliament are law. If they are, then law is a meaningless concept, it has no separate existence from the concept of the enforceable commands of the sovereign. It is this sort of sterile positivism which leads to the conclusion that the Nazi Holocaust was legal: this is only the reductio ad absurdum of the idea that whatever Parliament says is law.

Most Acts of Parliament are simply commands to officials, or worse, the delegation of powers to officials to exercise discretionary power. These are not what Fuller would recognise as law. Fuller's Rex realised, on consideration, that laws had to be general, abstract and prospective rules that applied equally and were possible to obey.

Nor does the rule of law imply that all aspects of life must be ruled by law. As Mr Prebble says, we need to return to the fundamental principle that that which is not clearly forbidden is lawful, which means an end to legislation requiring us to ask permission from authorities with discretionary power before we can carry on some business or do something with our own land.

Here then, lies the confusion. Is the Judges' crime that they have lost sight of the principles of the rule of law or is it that they have usurped the role of Parliament in making social policy? Because if there are fundamental principles that the Judges ought not to breach, then it is hard to see why Parliament should be allowed to do so.

And no one does believe that the support of the majority can justify everything viz the current support for international human rights documents, the Bill of Rights Act and so forth. But these documents suffer from all the faults of legislation, being drafted by groups of bureaucrats instead of emerging from decisions made by applying abstract rules to individual cases.

So Mr Prebble first accuses the Courts of abandoning the rule of law and then complains that Lord Cooke said that there may be some common law rights so deeply entrenched that Parliament cannot interfere with them.

But Mr Prebble himself then criticises Parliament for passing legislation which breaches fundamental principles and criticises Parliament in a way which implies not just that it has been inexpedient but that it ought not to have passed such legislation.

At root Mr Prebble clearly believes in the rule of law, but has not reconciled this with the modern views that Parliament is entitled to make something called social policy and that political views are purely a matter of taste and no one's philosophy is demonstrably wrong.

There are a number of other issues of interest to lawyers touched on in this book which it is not possible to deal with here. The book is clearly of a political and polemical nature rather than academic and legal. Nonetheless Mr Prebble has asked questions that few ask and for those that do not have time to read academic tomes, he provides an opportunity to rethink some of one's comfortable assumptions.

At least Mr Prebble has addressed these important issues in the form of a short book which can be read, considered and doubtless will be attacked. In this he appears streets ahead of the current leadership of both National and Labour, none of whom give any sign of wishing to address these issues at all. ❑

LETTER

FROM THE DIRECTOR OF THE SERIOUS FRAUD OFFICE

I was pleased to see the interest taken by the *Law Journal* (in the May issue) in several recent cases involving the Serious Fraud Office and the powers given to it under the Serious Fraud Office Act 1990. I am very conscious of my obligation to ensure that the powers vested in me as Director by Parliament are exercised responsibly and for proper purposes.

It may be of interest to your readers to know a little more about the particular cases referred to by Mr Lithgow and to reflect on the issues that as the Director of the Serious Fraud Office I must consider in relation to these particular matters.

Legal privilege and s 24

The Serious Fraud Office Act gives me wide powers to obtain documentary material – but only where I have reason to suspect that an investigation might disclose serious or complex fraud, or where I believe that an offence involving serious or complex fraud may have been committed. The access to documents is an important part of our powers to investigate serious or complex fraud.

The Serious Fraud Office Act specifically recognises and protects communications that are legally privileged except where they have been made or brought into existence for the purpose of committing or furthering the commission of some illegal or unlawful act. Section 24 of the Serious Fraud Office Act provides for a District Court Judge to determine any dispute over whether or not documents are legally privileged. The Judge can consider the documents before the Serious Fraud Office has access to these documents thereby preserving the integrity of the process. It is misleading to describe the *Beecroft* case as an application "to test the powers" of the Serious Fraud Office. Rather the *Beecroft* case was a joint approach under s 24 to identify which documents properly attracted legal privilege. Mr Beecroft's counsel claimed legal privilege on 25 documents, the District Court Judge identified five of those documents as attracting legal privilege. On appeal, Laurenson J identified five further documents as being protected by legal privilege.

At all times I was prepared to defer my investigation, and my access to the documents under dispute, to allow counsel time to place the matter before the Court. One consequence of the Court proceedings including the appeal process has been to add approximately six months to the time it has taken to bring this investigation to a conclusion

Section 9 admissibility of interviews

The issues surrounding the introduction at trial of the record of a compulsory interview are many. The primary consideration I believe must be the fairness of the process to both the defendant and the Crown.

The understanding that seems to have existed both within the Office, and amongst defence counsel up until recently was that statements made at a compulsory interview would only be introduced where a defendant gives evidence to the Court which is inconsistent with statements made at the earlier interview and then only that part of the interview that proves the inconsistency. The decision in the *Ross* case and an earlier case at Palmerston North (*R v Shaw*) have changed that understanding.

The issue for the Serious Fraud Office is not so much the interpretation of the Act but rather what controls the Court will in the future place on the use of these interviews to ensure a fair hearing for both the Crown and the defendant. Those controls will in turn have a direct bearing on how this Office conducts compulsory interviews which up until these recent rulings have been regarded primarily as a part of the investigation rather than as a direct source of evidence for a later trial.

If the interview is potentially able to be used without any limitations by a defendant in lieu of giving direct evidence before the Court it would open the way for offenders to make self-serving statements at interview knowing that if later charged that interview could be used to put across their account of the matter without any cross-examination in Court.

The decision is certainly not being ignored. The issues raised by the rulings both for our investigations and for the concept of a fair trial go well beyond whether the ruling in the *Ross* case was demonstrably correct in its interpretation of the Serious Fraud Office Act.

Videotaping of interviews

The Serious Fraud Office Act does not contain any express authority for recording a s 9 interview whether by way of videotaping or otherwise, but surely no one would deny that I should be able to record such an interview. The issue in the *Jaffe* case came down to what form of recording is legally acceptable. Any form of recording is open to criticism. There are cases where handwritten notes have been criticised as being inaccurate and other cases where the interpretation of an audio recording has been brought into question. It is perhaps not surprising that someone now questions the adequacy of videotaping an interview.

I make no excuse for requiring all compulsory interviews to be recorded on videotape. Not only is this a recognised form of recording in this day and age of electronic equipment it also offers the best record of exactly what transpired at the interview. It also ensures that should there be any complaint about the interview, there will be a clear record of exactly what occurred. A separate audio recording of the interview is also made.

I personally found it rather disappointing that a significant part of the argument from counsel for Mr Jaffe was that videotaping was unfair as the demeanour of the person, rather than the actual replies to questions, would influence the final decision of the Director on whether or not to prosecute. I reject that proposition absolutely. Anyone

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JUSTICE AND MAORI WOMEN

Denese Henare, The Law Commission

discusses the Commission's recent survey of Maori women

The primary purpose of NZLC Report 53, *Justice: The Experiences of Maori Women Te Tikanga o te Ture: Te Matauranga o nga wahine Maori e pa ana ki tenei*, is to assist those involved in New Zealand's justice sector institutions, particularly those who are employed by the state and on whom the Crown depends in the performance of its Treaty obligations, to better understand and respond to the needs and values of Maori women.

Before the signing of the Treaty of Waitangi, Maori women had access to and exercised influential roles as nurturers, organisers, leaders and in their relationships with land and other resources.

The words of Shakespeare put into the mouth of Petruchio describe the English common law which arrived in 1840 to civilise Maori women:

> She is my goods, my chattels; she is my house
> My household stuff, my field, my barn
> My horse, my ox, my ass, my anything.
> (*The Taming of the Shrew* 3.3)

When this view of women as property was applied to Maori women, their status was reduced to that of their counterparts. The influence of introduced laws eventually affected Maori society. Land alienation and patriarchal law placed Maori family forms and values under great stress.

For example, marriage according to custom did not mean for a Maori woman that she was transferred like a piece of property from her father to her spouse; nor did marriage affect her status. A woman remained a part of her own whanau even if she chose to live with her spouse's whanau and allow her in-laws to take responsibility for her wellbeing and support (Mikaere 1994, 125-149).

The English Laws Act of 1858 provided and declared:

> That the laws of England as existing on the 14th day of January, 1840, shall so far as applicable to the circumstances of the colony, be deemed and taken to have been in force therein as, and after that day, and shall continue to be therein applied in the administration of justice accordingly.

Thus, Maori, to marry validly for any purpose other than succession to property, had to marry either in accordance with the full requirements of the Marriage Act 1908 or in the presence of a clergyman of the Church of England or the Roman Catholic Church: see *Rira Peti v Ngarahi te Paku* (1888) 7 NZLR 235; *Rex v Wairemu Kingi* (1909) 12 GLR 175; *In re Wi Tamahau Mahupuku (Deceased), Thompson v Mahupuku* [1932] NZLR 1397.

The combined effect of successive marriage laws was that no Maori customary marriage could be considered valid for any purpose. Legal marriage imposed a legal relationship upon couples which took priority over all other relationships, including those with parents and siblings (Durie-Hall and Metge 1992, 60).

In recent times the Courts are slowly beginning to take account of Maori values, with Judges exercising powers in a way that try to meet Maori concerns (see *B v Director-General of Social Welfare* (HC, Wellington, 27 May 1997 AP 71/96).

The examples of statutes and judicial decisions which make reference to Maori cultural values do not indicate that Maori cultural identity is now secure, or that there is consensus about the place of a Maori dimension in the New Zealand legal system.

We are not aware of any other research that has specifically focused on Maori women as clients or users of justice sector services. We accept that many of the problems identified in this report could apply equally to Maori men.

However, it is clear from the Law Commission's consultation with Maori women that disregard of Maori values and culture by the justice sector, socio-economic disadvantage and ineffective services are significant barriers to their accessing justice. These barriers are fundamental in the consequences they have of deterring women from using the justice system to protect their interests and when they do use it participating in an active way.

Many of the women whom we consulted were concerned that they did not have ready access to the legal system, and too often said it was something of which they did not feel part. They usually expressed their feelings in terms of inadequate performance of the Treaty of Waitangi.

There has been much profound discussion about the Treaty and its principles. Many agencies with whom we spoke saw Treaty principles as lawyerly notions, to be found in decisions of the Waitangi Tribunal and the Court of Appeal. What the women saw as the relevant principles were simpler, namely that the Treaty promised that:

- the values of Maori must be respected and protected;
- Maori should form part of the new society and feel as much at home in New Zealand and its institutions as other New Zealanders.

Both promises suggest that, as far as practicable, the laws, legal institutions and the legal system should take account of Maori values.

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COMPUTER MISUSE

Donald Dugdale and Jason Clapham, The New Zealand Law Commission

introduce the latest Law Commission paper

Computer misuse is a global problem. In 1995 the US General Account Office discovered that hackers using the Internet had broken into the US Defence Department's computer more than 160,000 times. The Federal Bureau of Investigation reported that in 1997 there were 206 pending computer misuse cases. By 1998 that figure had increased to 480. (Denning, *Information Warfare and Security* (1999) 56.)

Computer misuse is not just an overseas problem. In November 1998, a computer hacker erased some 4,500 "Ihug" websites

We are becoming increasingly reliant on computers. In 1997 it was estimated that as many as 40 million people around the world were using the Internet, a figure predicted rise to 200 million by 1999. As our reliance on computers increases so too does the potential for computer misuse. One area where computer misuse could be acutely felt is in commerce. As the Law Commission noted in *Electronic Commerce: Part One*, NZLC R50, October 1998 business-to-business commerce over the Internet reached an estimated US$ eight billion in 1997, ten times the 1996 total. It has been estimated that electronic commerce will be worth US$ one trillion by 2002. Massive financial losses have reportedly occurred overseas as a result of computer misuse. In 1995, the US Senate's Permanent Investigations Sub-committee reported that banks and corporations lost US$800 million from hackers in 1995 alone. Federal law enforcement agencies have estimated that thieves operating through computers steal more than US$ ten billion worth of data in the United States annually.

Today there is legislation in the United Kingdom and Australia making computer misuse a criminal offence. Legislation has also been passed in Canada and Singapore.

Computer misuse is not just an overseas problem. In November 1998, a computer hacker erased some 4,500 "Ihug" websites. Shortly after the Ihug incident, it was reported that Telecom, New Zealand's largest Internet service provider, was concerned that hackers might be gaining access to the Internet by using customers' passwords and surfing the Internet at the customers' expense.

Our report notes that there is currently no criminal legislation in New Zealand directed specifically at computer misuse. After considering the existing criminal law in relation to theft, forgery, fraud, altering a document, fraudulent destruction of a document and wilful damage we conclude that it is far from clear that the existing criminal law adequately deals with computer misuse activities. We recommend new offences dealing specifically with computer misuse in a separate statute or in a distinct part of the Crimes Act 1961. This would mean that a comprehensive code in relation to computer misuse would be readily available to legal practitioners and to the public, that computer related activities would be dealt with by legislation expressed in apt terminology and that the criminal law would be rendered more clear and certain in respect of electronic crime.

We recommend the creation of four new offences:

- unauthorised interception of computer data;
- unauthorised access to data stored in a computer;
- unauthorised use of data stored in a computer; and
- unauthorised damaging of data stored in a computer.

The first offence is committed where a person eavesdrops so as to pick up information in the course of being transmitted to, or received by, a computer or intercepts the emanations from a computer and transforms those emanations into a useable form. The prosecution would be required to show; first, that the accused obtained unauthorised interception of computer data, and secondly that the accused intentionally intercepted the computer data. Those who accidentally intercept computer data should not be subject to prosecution. The offence would include instances where the attacker physically attaches an interception device to a computer or transmission device (such as telephone wires) as well as instances where there is no physical contact but the attacker places a device in proximity to such equipment.

The second offence would be committed where a person without authority, whether through physical or electronic means, accesses data stored on a computer. It is not appropriate to punish with criminal sanctions a person who accidentally or even carelessly accesses data. For example, in some cases individuals may gain unauthorised access to data by mis-dialling or by opening a programme which they did not intend to open. Consequently, the prosecution should be required to establish; first, that the accused gained unauthorised access to data, and secondly that at the time of access the accused had an intention to cause loss or harm or gain a benefit or advantage. The requirement of such an intent would mean that those who gain access simply to achieve the prize of access would not be criminally liable for their actions. However, if a person obtained unauthorised access without such an intent but then went on to cause damage through careless conduct, that person would be liable for the offence of "damaging computer data".

The third offence, unauthorised use of data stored on a computer, would cover two distinct types of activity. The first is where a person without authority gains access to data stored in a computer and goes on to use that data in an unauthorised way (eg to commit fraud or theft). The second is where a person plays no part in gaining unauthorised access to data but, nevertheless, receives and uses the data in an unauthorised way. This second situation is akin to receiving rather than theft.

The final offence, unauthorised damaging of data stored in a computer, would cover the entire continuum from denial of data to modification through to destruction of that data. This would cover both the "direct" and the "indirect" damaging of data. By "indirect" damaging we mean, for instance, writing a harmful "virus" on to a computer disk intending that someone else will use the disk and thereby introduce the virus into a computer or entering a password or otherwise blocking legitimate users from being able to access data. It would be sufficient to prove first, that the hacker gained unauthorised access and secondly, that data was damaged as a result of the hacker's actions (whether intentional or careless).

We recommend a single maximum penalty set for all four categories of computer misuse. We suggest a maximum of ten years' imprisonment.

We also recommend that the new legislation should be without territorial limitations. The existing jurisdiction provisions in the Crimes Act are inadequate to deal with computer misuse activities. Section 7 Crimes Act provides that New Zealand Courts will have jurisdiction in respect of offences under the Crimes Act if:

> any act or omission forming part of any offence, or any event necessary to the completion of any offence occurs within New Zealand ... whether the person charged with the offence was in New Zealand or not at the time of the act, omission, or event.

This would give New Zealand Courts jurisdiction where either the hacker or the computer are situated in New Zealand. However, there are situations where the effects of computer misuse may be felt in New Zealand even though neither the hacker nor the computer were situated in this country. For instance, the hacker may be in New York, the computer in California and the owner of the computer system in New Zealand. In the "Ihug" case discussed above the computer was based in California and was owned by a New Zealand company.

The Law Commission provided an advance copy of the Computer Misuse paper to the Ministry of Justice in May of this year. Following that, the Minister of Justice released a press statement saying that the Ministry is in the process of drafting a Bill which is expected to be available in June. According to the press statement the Bill will cover:

- accessing a computer system for a dishonest purpose;
- attempting to access a computer system for a dishonest purpose; and
- damaging or interfering with a computer.

A Bill limited in that way would be less comprehensive than the reform the Commission recommends. ❑

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who is familiar with the prosecutions brought by the Serious Fraud Office would know only too well that such prosecutions are firmly founded on admissible evidence and do not rely on the demeanour of the defendant at interview. The affidavit of the television producer was interesting in revealing what television producers can do with television cameras generally but bore no resemblance to the fixed camera used within the interview room at the Serious Fraud Office.

The comparison drawn with the recent case involving the Security Intelligence Service where breaking and entering a house was not regarded as an "incidental power" under the SIS legislation is hardly in the same category as video recording a properly constituted interview.

Your readers may be interested to know that it took just over a year to get the decision from the Court that the videotaping of the interview of Mr Jaffe was a proper action by the Serious Fraud Office. The consequence of this has been that the completion of the investigation has been delayed for over a year.

The task given to the Serious Fraud Office is to expeditiously investigate and prosecute cases of serious or complex fraud. Without the special powers given to the Office, a number of the prosecutions that it has brought would not have been possible. I believe that the Serious Fraud Office Act strikes a good balance between the requirements of the Office and those of the individuals being investigated. The Court rulings discussed by Mr Lithgow stand as clear evidence of a law enforcement agency committed to carrying out its task with all due diligence, but professionally and responsibly, and at all times acting within the law, even where seeking a resolution of a legal point has significantly delayed the final outcome of an investigation.

D J Bradshaw
Director

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Some of the values which are important to Maori women are referred to in the report and will be developed further in other projects of the Law Commission.

The report shows that the justice system has failed to meet the needs of Maori women. This failure is manifest in the negative experiences Maori women have described to the Law Commission and in the perceptions that they have that the justice system accords them little or no value. The consequence is that Maori women have little or no confidence in that system. That system is intended to bring all of us under the rule of law – the principle that peace and good order result from common acceptance of Parliament's laws. The consequences for the rule of law within our community, when those at the heart of Maori families are disillusioned, angry and frustrated with the system are deeply troubling.

With this in mind the Law Commission has sought in this report to explore some of the background of how this situation has arisen, and to suggest strategies based on the Treaty of Waitangi by which state agencies may best promote justice for Maori women. ❑

THE SOCIO-ECONOMIC POSITION OF WOMEN

Stuart Birks, Massey University

comments on Christine Woods' paper "Is the law fair? The socio-economic position of women in New Zealand", presented at the New Zealand Law Conference 1999

The 1999 New Zealand Law Conference included a paper by Christine Woods on "Is the law fair? The socio-economic position of women in New Zealand". She does not really address the issue of the law, but contends that women are disadvantaged. Her paper highlights the fact that there are several ways in which information can be viewed, and this can influence the conclusions drawn.

To show disadvantage, it is necessary to select appropriate indicators and assign suitable interpretations. Woods does this. To reply to claims of discrimination/disadvantage, one can show that there are different interpretations and/or present different indicators. I shall give a few examples.

Woods suggests that economic developments since 1984 have disadvantaged women. While concentrating on income and employment, she lists several other possible indicators. No data are given for these. They include education and health, within which there are numerous measures that show women to be doing better than men.

Her chosen indicators are also open to challenge. She mentions "occupational segregation", as if an appropriate pattern would have men and women identically distributed over occupations. Differences do not necessarily mean disadvantage for women, however. Note that men are "over-represented" in the dangerous occupations and poorly paid jobs such as agricultural workers. Are women being forced into certain occupations, or are men being shut out? Dr Sarah Farquhar's study of male teachers identified sexism and biases as barriers to male involvement in early childhood education. (Farquhar S (1997) *A Few Good Men or a Few Too Many?* Dept of Educational Psychology, Massey University) At primary and secondary school level, the proportion of male teachers has declined from 36 per cent of full-time teacher equivalents in 1992 to 31 per cent in 1997. (Ministry of Women's Affairs (1998) Status of Women in New Zealand.)

Men comprised 38 per cent of full-time equivalent state primary school teachers in 1971, and 22 per cent in 1995. (Ministry of Education (1996), *New Zealand Schools 1995*, table A9.)

Woods uses individual income to show disadvantage for women. But people live in households where there are intra-family transfers. It is therefore misleading to use individual earnings as a measure of socio-economic position. For example, a woman married to a partner in a law firm may choose not to do paid work, but can benefit from her husband's income. Also, aggregate data by gender provide a poor basis for decisions in individual cases when there is variation in circumstances within genders. Some women are themselves partners in law firms.

Woods relates income to qualification to indicate a "glass ceiling". She does not mention age, experience and individual choice. It would be inaccurate to compare the earnings of males who graduated in 1967 and 1997, so allowance should be made for age and experience when comparing men and women. Should we also assume that all work the same hours? Other phenomena have been suggested, such as a "pink escalator", which refers to the more rapid promotion of women to senior positions.

Woods really stretches credibility in interpretation when she asserts that similar unemployment rates from men and women show a disproportionate burden on women on the grounds that they make up a smaller proportion of the workforce.

Woods also refers to low income households. When comparing households it is necessary to consider household composition. For example, she says that 36 per cent of the bottom 20 per cent of households are sole occupant households aged 65 or over. Larger households would need to spend more to achieve the same standard of living. Wealth is also a factor. For example owner-occupiers need less income than those who rent.

There are income measurement issues to consider also. For example, family support is based on income and number of children. A two parent family will get the same amount of Family Support as a sole parent family on the same income with the same number of children, although the sole parent family: (i) includes only one adult; (ii) might be getting child support as tax free income; and (iii) could have an "absent parent" caring for the children for much of the time.

On occasion Woods groups together "women and children". This raises the issue of "gatekeeping" by women, whereby men are expected to fulfil a provider role, with caregiving by men being reliant on women's approval. Such gatekeeping, if it occurs, could help explain the small proportions of men in teaching and nursing and the service industries, as well as women's choice of work that permits them to claim continued primary caregiver status.

Woods makes the claim on pay differences that, "The issue here centres on the concept of equal pay for equal value rather than just equal pay for identical work". This principle could be challenged. Should we disregard the workings of the market, people's skills and experience, and their own career choices? How do we determine what is "equal value" if we reject the market measures?

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WORLD TRADE BULLETIN

Gavin McFarlane of Titmuss Sainer Dechert, London

shifts the focus from beef and bananas

PROJECTED BENEFITS OF FREE TRADE

A study produced by the Australian organisation Global Trade Reform has pointed to the considerable benefits which would be realised around the world if agricultural protection is reduced. The work on which they base their calculation envisages a reduction of fifty per cent in protective trade measures for goods, services and agricultural products. The protection targeted is both tariff and non-tariff barriers, and the organisation projects a boost for the global economy of around $400 billion. This has been relayed to the OECD by Australian trade representatives, and they claim that $250 billion would be saved around the world in the agricultural sector. Surprisingly perhaps, the figure for services is much lower, at around $90 billion. Manufactured goods trail in a poor third, with economies of only $66 billion. The report is controversial in claiming that the reduction of trade barriers in this way would actually stimulate exports. The report comes on the heels of fears expressed in a recent OECD release that some states are already going back on agricultural agreements which they earlier endorsed in the Uruguay Round of GATT; in response to pressure from their home farm lobbies, they are said to be reintroducing agricultural subsidies to help their exporters sell their goods overseas.

NAFTA – CLOSER LINKS TO COME?

While the Europeans continue to debate the issue of whether or not they should move forward to closer economic ties, or ultimately some form of federalism, there are signs of movement to closer links between the two North American giants, the United States and Canada. A decade after the introduction of NAFTA, pressures are building up for further movement. Although there is no shortage of trade disputes between the two countries, of which the Canadian Periodicals case in the WTO dispute forum is a leading example, over three quarters of Canadian exports go south of the border into the USA. There are already parallels between the situation on the other side of the Atlantic, and the way in which the EU has evolved through its various stages. The single market came into operation in Europe in 1993, and major industrial players in Canada are now casting envious eyes at the relatively paper-free situation which has developed within the EU when goods move within the internal market. There is still a good deal of documentation necessary to move goods across the Canadian-American border, and a strong lobby exists for the removal of border controls. As this column stresses, issues of international trade are closely bound to political economics; closer trade links opening in North America, say a move towards a full customs union, might bring rapid consequences in their wake. The joker in the Canadian pack is Quebec, where the independence tide ebbs and flows continuously. If Montreal did opt for a francophone state on its own, the prosperous Canadian provinces to the west would push hard to develop an even closer link with the USA. The interest would then turn to the maritime eastern provinces on the Atlantic seaboard, where unemployment is relatively high, and economies heavily dependent on logging and fishing. Certainly there will be considerable changes to NAFTA in the not too distant future.

NEW WTO DISPUTE PANELS

As we go to press, news comes from WTO headquarters in Geneva that three new references to the dispute system have led to the establishment of panels to hear the resulting cases. The EU is carrying forward a reference against Canada over the latter's alleged protection of its pharmaceutical products. It is claimed by Brussels that Canada allows third parties to carry out experiments for marketing approval without the consent of the patent holder, and the manufacture of patented products before the end of their period of protection. Canada has retorted that this is part of a balanced approach it operates to allow immediate distribution of products after the expiry of the patent. The EU is involved in yet another case against the United States. This time the claim is over the US Anti-dumping Act 1916, which is said by its critics to be a violation of GATT. The United States says that the statute in question is now obsolete, and that Washington has taken no action under the law for the last 82 years! The third reference has been made by Japan. It has been brought against the Canada-US Auto Pact. Tokyo claims that this agreement is WTO inconsistent as it only permits a limited number of manufacturers to import motor vehicles duty free into Canada. The EU has also joined in, contending that Canada accords certain manufacturers a tariff exemption for importing vehicles into Canada duty free subject to conditions. These include value added requirements which are said to infringe the national treatment provision of the WTO agreements. Canada rejects these claims, and says that recent increases in its importations of cars indicates that the Canadian market is an open one.

ARGENTINIAN TEXTILES AND FOOTWEAR

Readers of this column over recent months might have been forgiven for assuming that the only parties litigating in the dispute resolution forum of the World Trade Organisation are the United States and the European Union. Although these two giants dominate the stage, there are other references working their way through the process. One dispute which has just been concluded was between Argentina and the USA, and concerned importations into that country of clothing, textiles and footwear. It was alleged that in some cases duties had been imposed in excess of an ad valorem rate of 35 per cent; also there was a statistical tax of three per cent on all importations other than those from Mercrosur states. The revenue from the statistical levy was earmarked for financing statistical services for the import and export trade, as well as the general public. The United States lodged a reference with the WTO and the first instance WTO panel heard the case in the early part of 1998. It found Argentina was in violation of art II of GATT, through having applied a system of specific minimum tariffs although it had bound ad valorem tariffs. This resulted in less favourable treatment being accorded to those states to which it was applied. It also found that a regime of minimum specific import duties which had been operated since 1993 in respect of textiles. clothing and footwear was also in breach of GATT. One of the points which had told against Argentina had been that the specific duties imposed were mandatory, and were automatically collected by Customs officials of that country. So far as the three per cent ad valorem tax was concerned, this also was a violation of GATT in so far as it resulted in charges being levied which were in excess of the approximate costs of the services said to be available, and it was also a measure designed for fiscal purposes. A point was raised that domestic procedures should have been used to challenge an allegation of a non-conforming national measure, but this did not impress the panel. The question was essentially one of the supremacy of international legal agreements such as the GATT and the WTO in the Argentine system. The panel concluded that art II of the GATT would have been infringed whether or not the national law of the Argentine contained a remedy for such a situation. On the basis of these conclusions, the panel called on Argentina to adjust its domestic provisions in these areas so that it would fall into line with its obligations under the WTO agreement. Argentina took the matter on appeal to the WTO appellate body, but that forum substantially upheld the findings which had been made at first instance. It is certainly likely to add more weight to the authority of the WTO system if there is a preponderance of agreement between the two stages of the dispute resolution system. A situation should be avoided under which there is an impression of disharmony or friction between the two levels of jurisdiction. Unfortunately the considerable heat which is being engendered by the large number of heavy disputes between the EU and America have been putting the system under strain.

FREE TRADE AND ECOLOGY

Are these two terms contradictory? Certainly that is the view which is being put forward by organisations such as the International Society for Ecology and Culture.

Its adherents point to the links between the relentless march of globalisation in the name of unrestricted free trade, and the increasing threat to the environment from industrial activity and such developments as GM crops. At the heart of the matter is the fear that some multinational companies are now in a position to exercise substantial control over governments, and therefore to write their own agendas for economic policy. Undoubtedly there are enormous problems involved, and these are likely to become crucial subjects in the early years of the new centuries. In many cases there is no immediate solution, because no one has the gift of seeing into the future sufficiently clearly to be able to predict social and economic consequences which are at present unknown. Genetically modified crops provide a striking example. On the one hand, it is said that the planting of these seeds should go ahead all over the world on an unrestricted scale, because there is as yet no firm evidence that they are in any way detrimental. But on the other hand it is argued that the fact that the situation is uncertain should in itself justify a moratorium on the development and application of these GM seeds. The justification here is that because we cannot predict the consequences of using them widely, they should not be used at all, in case they wreak devastation on the environment which would be irreversible, and eventually catastrophic. But there are many other topics besides GM crops, and of equal importance. Unemployment levels in a number of advanced industrial countries remain dangerously high, but free trade does not appear to restore well paid and available employment for the unskilled and semi-skilled in Europe; these will always make up the greater part of the population. All these subjects raise acute questions about the ability of western democratic governments to continue their present forms of society throughout the new millennium; it is right that organisations such as the Institute for Ecology and Culture should be bringing a vital debate on these issues into the open. ❑

continued from p 230

Prue Hyman says that "women's labour supply is more elastic" because women have more scope to switch effort between paid and unpaid work. (Hyman P (1994), *Women and Economics: a New Zealand Feminist Perspective*, Bridget Williams Books, p 183.) If women's choices are different from men's, then we should not be surprised to find different labour market outcomes.

Woods' mention of a "double shift" is also misleading. For example, for those in full-time paid work, on average men undertake more hours of paid work than women. Overall men may be doing as many or more hours of paid and unpaid work than women. As Heather Kirkwood suggests, rather than just say women are disadvantaged by not being available for as many hours of paid work as men, we could ask, "why do men work more hours than women?" (Kirkwood H *Exploring the Gap: An exploration of the difference in income received from wages and salaries by women and men in full-time employment*, Statistics New Zealand, November 1998.)

As a broader issue, economic circumstances may not be the only factor to consider in relation to fairness under the law. There are several areas where it could be considered that women are favoured and where men's costs of achieving a similar outcome would be much higher. These areas are not only those of custody and access. Consider the working of the Domestic Violence Act in the context of Chief Justice Sir Thomas Eichelbaum's opening address at the conference:

> In today's climate, it is not always fashionable or popular to speak of the presumption of innocence, or the right to bail or of a fair trial ... A cult seems to be developing that when people appear on some serious charge – typically involving violence – it is almost an outrage to speak of the presumption of innocence.

Woods' closing quote from Dame Sylvia Cartwright highlights the need for broader input into the debate:

> Young women face a far more difficult and subtle form of discrimination. Their ambitions aren't going to be fulfilled as easily as their male partners. You can't change centuries of this inbuilt view that women have different roles in society.

Do men not have ambitions to be parents to their children? ❑

FRANCHISE FALLOUT

LITIGATION

with

Andrew Beck

The major litigation between Dymocks and its franchisees is discussed in this issue at length. The case was fought with considerable vigour and, as a result, has generated some interesting rulings in the areas of costs and stay of execution.

There were two separate proceedings: one brought by Dymocks seeking declarations that it had lawfully terminated three franchise agreements as a result of breaches by the franchisees; and one brought by the Todds, claiming damages for misrepresentation inducing them to acquire the three major franchise outlets in New Zealand. The hearings were consolidated and took some 34 days to complete.

Hammond J dismissed the misrepresentation claim, finding no actionable misrepresentations. He held that the agreements had been lawfully terminated because there had been a breach of the obligation of confidentiality between Dymocks and the Todds. This substantial win by Dymocks produced, as might be expected, a significant claim for costs.

THE COSTS RULING

The costs issue was complicated by three specific matters: there were provisions in the franchise agreements allowing a claim for full indemnity costs; a claim was made for the cost of executive time which had been lost by virtue of the proceeding; and *Calderbank* offers had been made both ways.

Dymock's starting point was its actual costs of $1,785,561.91. Its suggestion was that the appropriate apportionment was 60 per cent for the misrepresentation and 40 per cent for the termination case; this was accepted by the Court. Included in the figure was some $100,000 for employees' time and $45,000 for employees' costs.

The misrepresentation claim

Because there were Australian parties to the litigation, Hammond J went to some lengths to outline the law as to costs, explaining that the general rule is one of "partial indemnity", normally expressed as a reasonable contribution to costs. He saw it as falling between the "no costs" approach followed in the United States, and the "full indemnity subject to taxation" approach followed in the United Kingdom. He also noted the possibility of the costs being subject to taxation by an officer of the Court.

The general principles governing costs are not in dispute, and were comprehensively reviewed by McGechan J in *Holden v Architectural Finishes Ltd* [1997] 3 NZLR 143. The current law is, however, not likely to remain for long as the Rules Committee is presently finalising a new set of costs rules, which will contain a scale with far more detailed calculations. What is of particular interest in *Dymocks* is the reference to taxation.

As Hammond J explained, taxation involves the review of costs claimed by an officer of the Court, a process originating in the English system. While it is true that RR 54-59 of the High Court Rules do make provision for the taxation of costs, *McGechan on Procedure* notes quite correctly that these rules have fallen into disuse (para HR54.04). There do not appear to be any decided cases under R 54, and it would no doubt cause much consternation should a Registrar be called upon to perform this function. The only recent judicial discussion of the rule is to be found in *Kuwait Asia Bank EC v National Mutual Life Nominees Ltd* (1991) 3 PRNZ 571, where the Court of Appeal suggested that the Privy Council had been unaware of the practice in New Zealand, and stated that there was "no known precedent for taxation of costs on any basis in the New Zealand Court of Appeal" (at 572). It was noted that the standard practice in the High Court had for many years been for costs to be fixed by the Judge on memoranda (at 574).

Hammond J's interest in taxation appears to have stemmed from his concern at the size of the bill, particularly because the Dymocks' costs were significantly higher than the Todds'. He was therefore tempted to invoke the taxation jurisdiction. At p 11 he said:

> I do think that the time may be coming where taxations may be necessary to test some of the very large claims now being made in commercial litigation, and if there had been time, I may well have followed that course.

While there may well be concern at the size of legal bills in large commercial litigation, it is doubtful if the answer is to be found in taxation. The Court retains ultimate control by setting the proportion of costs it will allow, and that can reflect any perception of inefficiency on the part of legal practitioners. As it is, the proposed costs regime will apparently involve considerably more time in calculating appropriate awards. To return to a detailed taxation regime would, however, inevitably raise costs without achieving any great benefit.

In determining the appropriate proportion of costs, Hammond J drew up a detailed chart of the varying proportions of actual costs which had been awarded in a number of recent cases involving large amounts. He then listed a number of relevant factors, and mentioned a "very respectable" *Calder-*

bank offer which had been made by Dymocks. He concluded by allowing 75 per cent of $750,000, which he considered to be a reasonable starting point.

All of this tends to make one's head spin, because it appears as though the application of some scientific formula has magically produced the result. Of course that is not in fact the case. What it comes down to in the end is no more than the Judge's assessment of a reasonable contribution to costs. It is undoubtedly useful to have some understanding of the thinking processes followed by Judges, and the openness of Hammond J's approach is welcome. Caution must be exercised, however, to avoid thinking that the calculation is simply a mechanical one.

The termination claim

As mentioned above, the termination claim was complicated by the contractual provisions relating to costs. These referred both to solicitor and client costs and to allowances for employees' time. The main argument raised by the Todds was that these matters had not been pleaded or proved in evidence. In addition, as the contract was governed by Australian law, this too should have been proved as a matter of fact.

Hammond J glossed over the foreign law point by saying that, even if there were jurisdiction to review the content of such clauses, he would not have exercised it against Dymocks (p 22). That does not deal with the fact that the law was not proved, and that a vital leg of the case was therefore missing. What the Court did was to resolve the question according to New Zealand law. While this may be appropriate where the issue of foreign law has not been addressed, that can hardly be said to be the case where, as here, the foreign law had been proved in other respects by the calling of expert witnesses. In this situation, the most appropriate course of action would probably have been to make a discretionary order under R 46. Although that may not have made much difference, it would have required the Court to start from the point of view that it was not a solicitor and client award.

As far as the claim for employee time and costs was concerned, Hammond J held that this should have been pleaded and proved on a balance of probabilities (at 19). One of his main concerns seems to have been the size of the claim – he considered it unacceptable for such a large claim to be raised at that stage of the proceedings. There is, however, a serious point of principle at stake. Employees' time does not constitute an ordinary head of costs; it is entirely a contractual matter and has to be proved in the same way as any other contractual claim, regardless of amount. It would be a matter for concern if smaller claims could be slipped into the bill of costs as a matter of course.

Although, once again, the requirement appears to have been largely ignored, a claim for solicitor and client costs pursuant to a contractual provision must also be specifically pleaded and proved. This was recently confirmed in *Jefferies v Ernst and Young Nominees* unreported, 22 February 1999, Goddard J, HC Wellington CP21/99.

Hammond J's main concern was that there should be some check on the quantum of solicitor and client costs. He considered that the Court should never order 100 per cent of such a bill without the account having been sent for revision. Although he considered the possibility of providing the option of revision, in the end he decided to fix the amount himself. This practice has previously been accepted in decisions such as *National Bank of New Zealand Ltd v Murland* [1991] 3 NZLR 86.

Perhaps the major problem was that Dymocks had succeeded not on the grounds originally alleged in their notices of termination, but on the basis of something which emerged at trial. Hammond J held that only ten per cent of the total claim as alleged had been successful, even though it resulted in judgment for Dymocks. Making allowance for the fact some of the evidence would have been required anyway, he awarded 25 per cent of the costs claimed.

The situation raises a difficult question. The Court of Appeal has accepted that contractual provisions to pay solicitor and client costs are enforceable unless they are contrary to public policy: *ANZ Banking Group (NZ) Ltd v Gibson* [1986] 1 NZLR 516. It has been recognised, however, that there must be a causal link between the breach of contract and the costs incurred. In addition, the Court may itself decide what is a reasonable solicitor and client fee: *Frater Williams & Co Ltd v Australian Guarantee Corporation (NZ) Ltd* (1994) 2 NZ ConvC 191,873.

Hammond J's assessment that allowance should be made for unsuccessful claims must be right. The contractual intention could not have been that all costs would be indemnified regardless of the merits of the claim. Once it is recognised that there is a mix of successful and unsuccessful claims, any scientific approach immediately becomes largely spurious. The exercise is once again squarely in the arena of a discretionary assessment.

STAY OF EXECUTION

The main judgment in the case was delivered on 26 February 1999. On 26 March, the Todds applied for a stay of execution pending appeal to the Court of Appeal. The effect of the judgment was that the Todds would be required to surrender the businesses they had acquired back to Dymocks. The Todds argued that they would suffer significant prejudice unless they were allowed to continue in possession pending resolution of their appeal.

The High Court decision

Hammond J accepted that what was involved was essentially a balancing exercise, and he listed a number of factors requiring consideration. He noted that the fact that a specific remedy would be lost without a stay is not conclusive, nor is the fact that some prejudice may be suffered by the party concerned. Of special relevance was that, on the Court's assessment, the appeal would take a considerable time to complete.

Although refusal of a stay would mean that the Todds would inevitably lose the businesses, success on appeal would entitle them to damages, and Dymocks would be able to pay any amount awarded. Keeping the parties together would produce an intolerable situation, given the bitterness which had developed in the relationship between them. Allowing the Todds to remain in possession could have negative results both for the specific businesses and the entire Dymocks franchising operation in New Zealand.

Ultimately, Hammond J thought that the pursuance of the appeal – although entirely genuine – was at heart a tactical measure, with no real hope of the agreements ever continuing in force. He therefore declined to stay execution and, in addition, refused even an interim stay pending an application for stay to the Court of Appeal. His aim in doing this appears to have been to precipitate an early hearing of the application.

The Court of Appeal

An application for stay was duly made to the Court of Appeal under R 9 of the Court of Appeal (Civil) Rules 1997. This was heard on 5 May.

The first point of note was that the Court of Appeal held that it was entitled to have regard to the fact findings of the Court below in a stay application. The Court also considered that it was permissible to consider the reasons given by the High Court for refusing the stay. The Court of Appeal in essence accepted the reasons provided by Hammond J and refused the application. The particular point relating to what may be considered by the Court of Appeal does not seem to have arisen before. The Court dealt with the matter very swiftly and in an essentially pragmatic fashion. In an application of an essentially practical nature, this is clearly justified.

Like Hammond J, the Court of Appeal viewed the dispute as an attempt to resolve a commercial problem rather than to preserve a particular market position: a case about "money as opposed to possession". Once seen in this light, any argument as to inadequacy of damages was clearly going to fail. Indeed, the Court of Appeal went so far as to say that damages would be the appropriate remedy.

Looking at the other side of the equation, Thomas J considered that it would indeed create an intolerable situation if the Todds were permitted to remain in possession. The prejudice to Dymocks would far outweigh any possible prejudice to the Todds.

The Court was accordingly very clear in its view that the stay was not appropriate.

One thing which stands out from the decision, as well as the other Court of Appeal cases referred to by Hammond J, is the considerable reluctance of the Court to grant a stay of a decision in commercial matters. There appears to be a very heavy onus on an applicant to establish that more than a simple investment decision is at stake; that it is not simply a question of money. If this cannot be done, then the application will be a lost cause.

MONITORING EXECUTION

The Court went on to express hearty approval of the way in which Hammond J was monitoring the enforcement of the contract by way of directions hearings to ensure the efficient and expeditious transfer of the businesses.

It is clear that Hammond J adopted an extremely hands on approach to ensuring that the orders of the Court were carried out effectively, and there were apparently a number of directions hearings which culminated in the transfer of the businesses to Dymocks in terms of the judgment.

Case management practices have a tendency to come to an end with the delivery of judgment, and Hammond J seems to have been at pains to avoid the sort of situation where execution of the orders drags on interminably. The concern of the Court to ensure the carrying out of its orders is commendable; the only downside of such a practice could be the expense which might be occasioned by over-management.

SETTING ASIDE STATUTORY DEMANDS

An application to set aside a statutory demand has to be filed and served within ten working days after service of the demand: s 290 of the Companies Act 1993.

There is therefore considerable time pressure on such applications. Because of the significant consequences of failure to set aside the demand, and because the Court has no jurisdiction to extend time, it is clearly vital to get the procedure right.

It is perhaps unfortunate, therefore, that there is a fish-hook lurking in the service requirement.

Where service is to be effected on a company, it must comply with s 387 of the Companies Act 1993, which lists the exclusive methods of service of Court documents.

As these requirements are contained in a statute rather than the Rules of Court, the Court is not able to use its R 5 jurisdiction to cure any irregularity in service. That has had adverse consequences for parties in cases such as *Livi Investments Ltd v Butler Gilpat Ltd* (1998) 11 PRNZ 680 and *Roadlife Trucks Ltd v Fruehauf Pacific Ltd* unreported, 1 September 1998, Master Thomson, HC Palmerston North M79/98.

North Shore Nurseries

There was a happier outcome for the applicant in *North Shore Nurseries Ltd v Wearmouth* (1999) 12 PRNZ 672. An application to set aside a statutory demand was served on the creditor's solicitor, who signed an acknowledgment of receipt. It was later argued that service had to be effected personally on the creditor, and that the solicitor had no authority to accept service and had never indicated that he had such authority.

Although reliance was placed on the *Livi Investments* case, the vital difference here was that the creditor was a natural person rather than a company. That meant service was governed by R 192 of the High Court Rules rather than the Companies Act. Although R 192 had not in fact been complied with, the Court was able to exercise its discretion under R 5, and did in fact do so, taking its cue from *Invercargill City Council v Hamlin* (1994) 7 PRNZ 674. In that case, the Court of Appeal emphasised the fact that the document had in fact come to the attention of the party concerned, and regularised the service.

Master Faire concluded that the application had clearly come to the creditors' attention and that there was no prejudice. The statutory demand had also given the solicitor's name as the duly authorised agent. It would therefore be a mere technicality to say that the rules had not been complied with. As the Court decided there was a genuine dispute over the debt, its conclusions were of great importance for the debtor. What is of concern is that, had the creditor been a company, the particular line of reasoning would not have been open.

Need for change

It does not seem right that something as important as the right to avoid liquidation proceedings should vary depending on whether the creditor is a company or a natural person. In the one case, an application can be defeated by a technicality; in the other the Court has the ability to examine the substance of the objection. As it is so easy to slip up on the time requirements, the R 5 jurisdiction is a particularly important one in situations like this.

The Court in *Livi Investments* recognised the potential injustice and made a plea for a statutory requirement that an address for service be provided as an integral part of every statutory demand. There is much to be said for this in the interests of clarity. More fundamentally, however, it would be better if a procedural requirement such as service were not exclusively tied to a statutory provision. There does not seem to be any reason why the Companies Act should not allow service in terms of the High Court Rules in addition to any provisions. If that were the case, it would at least enable the Court to consider any irregularity pursuant to its discretion. The Court of Appeal has shown that the concern ought to be with substance; the powers of the Court to deal justly ought not to be restricted by the way in which a procedural rule is enacted.

VOIDABLE TRANSACTIONS: PROCEDURAL ASPECTS

The procedural difficulties surrounding applications to prevent liquidators setting transactions aside have occasioned much comment. Although there has not been any legislative change, the Masters, especially in Auckland have taken practical steps to ensure a minimum of injustice. The position was documented by Master Gambrill in *Howard v Wilson & Co Ltd* (1998) 12 PRNZ 553. Some of the ongoing problems are demonstrated by *Re Fazakerley Ink Ltd (in liq)* unreported, 22 December 1998, Master Thomson, HC Wellington M259/98.

Somewhat more unusual issues arose in *Stiassny v Gleeson* (1999) 12 PRNZ 684. As a result of various delays, the Court was required to consider the application of R 426A to the voidable transactions procedures. A further question arose as to the possibility of challenging the presumption of voidability by other methods.

The Rule 426A argument

The company concerned was placed in liquidation on 14 December 1995. On 30 October 1997, the liquidators served a notice on the Gleesons setting transactions aside. On 4 December 1998, the liquidators sought an order requiring payment by the Gleesons.

It was argued on behalf of the Gleesons that R 426A applied because there had been periods of delay of more than 12 months. The first period was between the date of liquidation and the date of the notice. The second was between the service of the notice and the application for payment.

Paterson J held that there was no substance in the R 426A point. Rule 426A in its terms only applies to the conduct of proceedings. While an application to put a company into liquidation is a proceeding, that proceeding is disposed of when the company is put in liquidation. The subsequent action taken by the liquidator is not part of that proceeding, but is an independent cause of action. Furthermore, the application to prevent the setting aside is an interlocutory application to which R 426A does not apply.

As far as the second period was concerned, it could not be said that the filing of a notice by the liquidator commenced a "proceeding". The only application to Court was made by the liquidators in December 1998, and was not out of time.

It is no doubt true that R 426A was not designed with applications of this sort in mind, and cannot be made to fit them neatly. The fact that there is no "proceeding" is not determinative, because the Courts have on occasions applied rules by analogy: see for example *Colonial Mutual Life Assurance Soc Ltd v Wilson Neill Ltd* [1993] 2 NZLR 617. Anomalies could also arise in that some applications by liquidators have to be brought under R 700ZI by way of statement of claim; those applications would be subject to R 426A (assuming the R 426A applies to Part IXA proceedings, which has never been decided by the Courts). It is difficult to see why a different policy should apply to applications under R 700ZH.

The truth of the matter is that applications in respect of companies in liquidation occupy a very awkward position. The procedure for these applications has been grafted into the rules in a rather ad hoc way, which means that they do not sit comfortably. Any general application of the rules will inevitably throw up the sort of difficulty which occurred in this case. The case management practices which have been widely adopted in the High Court, and which are likely to become standard practice in the near future, are not tailored towards this sort of application. What is needed is a procedure which recognises the sui generis nature of the applications and makes provision for the necessary procedural structure, including case management measures.

It is clear that the applications in a liquidation should not be allowed to languish for long periods of time, and there is certainly a public interest in ensuring that all the consequences of a liquidation are resolved as quickly as possible. This is the sort of issue which could be addressed in a proper procedure, as suggested below.

Challenging the presumption of voidability

Because no action had been taken to prevent the transactions being set aside, the liquidator proceeded to apply under s 269 of the Companies Act 1955 for payment of the sum owing. At that stage, the Gleesons opposed the application on the grounds that the criteria of s 266 had not been met and that the transaction could not be invalidated.

Paterson J held that this could not be right. If a creditor wishes to challenge the liquidator's right to set a transaction aside, that challenge must be made in accordance with the procedures of the Act. The creditor who does not make a timely application under s 268 of the Companies Act 1955 (s 294 Companies Act 1993) forfeits the right to challenge the notice. It is not possible to raise at any later stage a question as to whether the liquidator had satisfied all the requirements of the Act.

The Court did accept, however, that it might be possible to raise an estoppel against a liquidator to prevent them from recovering the debt. If some admission had been made by the liquidator at an earlier stage, that might alter the right to claim payment, as in *Re Huberg Distributors Ltd (in vol liq) (No 2)* (1987) 3 NZCLC 100,211.

The conclusion reached by the Court appears to accord with common sense and with the policy of the Act; there is clearly an intention to assess which transactions are vulnerable at an early stage. If that is the policy, however, then it makes some regulation of dilatory proceedings all the more urgent. As suggested above, it is an area where at least some case management guidelines are required, and possibly even rules laying down timetables. ❑

FRANCHISING IN NEW ZEALAND

Stewart Germann, The Stewart Germann Law Office, Auckland

surveys the scene and comments on the Australian code

Franchising is developing in New Zealand rapidly. Quite simply, franchising is a method of marketing goods and services. It has evolved out of a number of business transactions, methods and practices which have been common and popularly known for many years and, as a legal or a marketing concept, it is not new.

The real success of a business is often not limited to the product or service that it sells. It is the package of product, presentation, trade name, trade mark, service mark, the service it provides, the image, the distinctive appearance of the premises, the promotional aspects including get up, logos, etc, and the owner-operator enthusiasm and personal attention. It is that business format which can be made available throughout New Zealand to individually owned franchised outlets and all of those elements make up what is known as "the business format franchise".

There are four basic features:

- The ownership by one person (the franchisor) of a name, an idea, a secret process or piece of equipment and the goodwill and know-how associated with it.
- The grant of a licence (franchise) by the franchisor to another person (the franchisee) permitting the exploitation of such name, idea, process or equipment and the goodwill and know-how associated with it.
- The inclusion in the licence (franchise) agreement of regulations and controls relating to the operation of the business in the conduct of which the franchisee exploits his rights.
- The payment by the franchisee of a fee or other consideration for the rights which are obtained and the services which the franchisor will continue to provide to the franchisee.

FRANCHISE ASSOCIATION OF NEW ZEALAND

Prior to July 1996 there was a New Zealand chapter of the Franchise Association of Australia and New Zealand Ltd (FAANZ). Such had been the case for about ten years during which time franchising continued to grow and become more sophisticated in New Zealand. On 2 July 1996 the Franchise Association of New Zealand Incorporated was formed and registered as an incorporated society and at that stage New Zealand "broke away" from Australia for the first time (and I might add with the blessing of Australia). When the rules of the Franchise Association of New Zealand were first promulgated, the Board decided to incorporate a mandatory Code of Practice as part of those rules. Australia had not gone down that path but had a two tier approach whereby franchisors could belong to the FAANZ which had rules but no Code of Practice. Those same franchisors could voluntarily join the Franchise Code Council Ltd (FCC) of Australia and agree to abide by the Code of Practice. So there were franchisors who would belong to both bodies, franchisors who would belong to the FAANZ only, franchisors who would belong to the FCC and franchisors who belonged to neither. It was really this mishmash which caused the Australian Government to intervene with the result that on 1 July 1998 the Trade Practices Act 1974 in Australia was amended by bringing in a mandatory Franchising Code of Conduct.

New Zealand is probably the most deregulated country in the world to practise business. From a franchising point of view, this is attractive because there is no specific franchising legislation. In the USA, Australia and many other countries there are complexities and high compliance costs which are a deterrent to future growth. Franchisors who have high standards will never find a problem in any jurisdiction and will always act in a proper way. However, legislation ossifies structures and I see no need for specific franchising legislation in New Zealand.

THE FRANCHISING CODE OF PRACTICE

The Code of Practice has four main aims:

- To encourage best practice throughout franchising.
- To provide reassurance to those entering franchising that any member displaying the logo of the Franchise Association of New Zealand is serious and has undertaken to practise in a fair and reasonable manner.
- To provide the basis of self-regulation for franchising.
- To demonstrate to everyone the positive will within franchising to regulate itself.

The Code applies to all members including franchisors, franchisees or affiliates such as accountants, lawyers and consultants. All prospective new members of the Association must agree to be bound by the Code before they can be considered for membership.

What does the code cover?

- **Compliance** – all members must certify that they will comply with the Code and members must renew their certificate of compliance on an annual basis.
- **Disclosure** – a disclosure document must be provided by a franchisor to all prospective franchisees at least 14

days prior to signing a franchise agreement. The franchisor disclosure document must be updated at least annually and it must provide information including a company profile, details of the officers of the company, an outline of the franchise, full disclosure of any payment or commission made by a franchisor to any adviser or consultant in connection with a sale, listing of all components making up the franchise purchase, references and projections of turnover and possible profitability of the business.

- **Certification** – franchisors must give franchisees a copy of the Code and the franchisee must then certify that he or she has had legal advice before signing the franchise agreement.
- **Cooling off period** – all franchise agreements must contain a minimum seven day period from the date of the agreement during which time a franchisee may change its mind and terminate the purchase. This is very important and the cooling off period does not apply to renewals of term or resales by franchisees.
- **Dispute resolution** – the Code sets out a dispute resolution procedure which can be used by both franchisor and franchisee to seek a more amiable and cost effective solution than litigation. The Code requires all members to settle disputes by mutual negotiation in the first instance and this process does not affect the legal rights of both parties to resort to litigation.
- **Advisers** – all advisers must provide clients with written details of their relevant qualifications and experience and they must respect confidentiality of all information received.
- **Code of Ethics** – all members must subscribe to the Code of Ethics which sets out the spirit in which the Code of Practice will be interpreted.

The Code of Practice is not supported by legislation, nor is it compulsory for franchisors to be members of the FANZ. However, when a purchaser buys a franchise from a member of the FANZ he or she does so in the knowledge that the member has undertaken to operate according to the standards laid down in the Code. In the event of a member failing to abide by the Code then the member can be investigated with the ultimate sanction being expulsion from the FANZ and probably litigation.

EXISTING LEGALISATION

In New Zealand there is a plethora of legalisation which assists in the franchising area regardless of the fact that there is no specific franchising statute. For example, there is the Fair Trading Act 1986, the Commerce Act 1986, the Consumer Guarantees Act 1991 and the general law of contract. A franchise agreement is, of course, a document based on contract. However, clauses in the agreement are affected by the Fair Trading Act, the Consumer Guarantees Act and especially on the intellectual property area including the Trade Marks Act 1953. Intellectual property, including the goodwill of the franchise, is often one of the most valuable aspects of a franchise and can be worth millions of dollars.

The legislation which consistently trips up careless franchisors is undoubtedly the Fair Trading Act which is very wide in its application. There is no need for franchisors to fall foul of that Act, nor to be scared of it. Franchisors must not misrepresent the position, especially when commenting upon financial projections. It is far better to undersell the potential and success of a particular business rather than oversell and pay the penalty. So while there is no specific franchising legislation in New Zealand, in my opinion there are adequate safeguards to potential and actual franchisees in the existing legislation available.

SURVEY OF FRANCHISING

In 1997 for the first time in New Zealand Countrywide Bank sponsored a Survey of Franchising and this confirmed a growth rate in franchise systems of 28 per cent per annum. In 1998 the second Survey of Franchising was published and key results from that survey are as follows:

- The growth for franchisees and outlets is increasing at 20 per cent and for systems at over 25 per cent per annum.
- 64 per cent of the operations originate in New Zealand.
- 13 per cent of the indigenous systems are being exported.
- 80 per cent of the systems franchised started this decade.
- The median total start-up cost is $138,500.
- 78 per cent franchisee survival rate for last five years.
- Spouses and partners operate 52 per cent of franchise outlets.
- 24 per cent of the franchisees are women.
- People and motivational skills are the most important personal attributes for most systems.
- Franchises in automotive services and leisure are on the increase.

A further franchising survey will be undertaken in New Zealand in 1999.

LEVEL OF DISPUTES

Franchising creates a dynamic relationship between franchisor and franchisee. Because the relationship is so important, there must be a mechanism for resolving disputes and the Code of Practice promotes Alternative Dispute Resolution (ADR) and mediation in particular. The 1997 Survey showed that the level of disputes between franchisees and franchisors came to less than one per cent of the outlets surveyed. In 1998, that figure was lower still. This is not to say that disputes do not exist – they are widely regarded as inevitable. However, of the 31 disputes reported, 15 had gone to mediation rather than litigation, with ten of those 15 being instigated by the franchisor. This is the same proportion as in 1997 which indicates a desire by both parties to resolve disputes amicably rather than ending up in Court.

Dymocks Case

If the parties have fallen out to the extent where the relationship is over then this is really the divorce and it often results in litigation. A recent example of this is the case of *Dymocks Franchise Systems (NSW) Pty Ltd v Bilgola Enterprises Ltd* (HC Auckland, 26 February 1999, CP 64/98 and CP 43/98, Hammond J), heard over a protracted period between September 1998 and February 1999.

Brief facts were that between 1994 and 1996 Dymocks entered into three franchise agreements with the Todd interest ("Todds") for the establishment of "flag ships" stores in the Atrium on Elliott retail complex in Auckand, on Broadway, Newmarket, Auckland and at Lambton Quay, Wellington. By 1997 relations between Dymocks and the Todds had deteriorated and on 9 February 1998 Dymocks issued termination notices with respect to all three agreements with the Todds. The Todds denied the lawfulness of the terminations but on 13 February 1998 the Todds accepted

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DRAFTING A FRANCHISE AGREEMENT

Win Robinson, Franchize Consultants (NZ) Ltd

says that lawyers' responsibilities go further than following the client's instructions

Of course lawyers have an obligation to do the best they can by their client. It is the same with drafting a franchise agreement. The finished agreement must please the client, in most cases the franchisor.

However, in some situations the new agreement may please the client but could well play an important part in his or her undoing. Why? You the lawyer, have accepted instructions in a normal manner and have skilfully conveyed these instructions into the franchise agreement. You probably have accepted instructions at face value and have used the information given you as corner-stones of the franchise agreement, eg the royalty at X per cent of turnover, the premium or upfront franchise fees at Y$, the term as Z years, the marketing levy at $, the margin on product or services supplied at $R etc and so on. In most cases you have not been shown the rationale for these figures or their configuration. You have accepted that your would-be franchisor client knows what he or she is doing; sometimes quite rightly, other times sadly not so.

Let's just look at some of the downstream effects that those key controls may have on the franchise system. If strategic numbers (the format) are not right, the result can be one of two outcomes.

First, the wrong format can disadvantage the franchisor. For example, our consultancy was commissioned to review a franchise system that had been in operation for about three years. It was a retail operation with a smallish number of franchisees, mainly concentrated in one mass market. It was lucky that they decided to investigate when they did because had they struggled on for much longer, they would have run out of money. The reason was that the franchisor was simply subsidising the franchisees from his own retail outlet. In the franchise agreement the obligations of both parties were precisely set out, as of course were the key format figures. The franchisor being conscientious and embracing the philosophy of a win/win situation was carrying out his obligations which were costing him more than what he was being paid by the franchisees in the way of royalties and marketing levies.

Clearly in this case, the "homework" or strategic planning had not been done properly, if at all. The franchisor was slowly but surely working himself out of business. This particular example had nothing to do with reaching critical mass in the number of franchisees that were in the system. It would exacerbate the situation with more franchisees. The secondary upshot of this dilemma would have been very bad for the franchisees as well, had the franchisor gone out of business. Most franchisees would have found it very difficult to remain in business by themselves without the support they were getting from their franchisor.

Second, the reverse can also be envisaged. In my experience it may not always be by accident or from ignorance that the reverse is encountered. There are some people who upon seeing the obvious success of some franchises, figure that they too can become rich quickly from using the franchise method. They deliberately load the figures very much in their favour, usually placing a crushing burden upon the franchisee. A tell-tale indication of this type of person is when the emphasis has been placed on large upfront fees.

The genuine long-term franchisor does not look for large upfront fees, but looks to make his or her profit over the long-term from a reasonable portion of the ongoing income.

In conducting effective strategic planning, a franchisor needs to investigate many format scenarios and financially model them until he or she has arrived at the optimum configuration for his or her particular business. There are many possible results and to do it properly requires the input of someone skilled and experienced in franchising, because of the many ramifications that are possible. There is a huge responsibility. Just think of the lives it could affect.

In most franchise agreements, reference is made to items in the Operations Manual or the set of franchise Manuals. Good Manuals will describe procedures in following the systems of the franchisor. They will explain the reason things are done a certain way and they prescribe a minimum standard to which they must be done. In a well organised franchise operation, a Manual set may be up to six or seven comprehensive volumes long. Obviously a lawyer writing the franchise agreement would not be expected to read through all the franchise Manuals. However, would you think the perusal of the List of Contents would be a good idea? A conscientious lawyer should satisfy himself or herself that the franchisees will be given access to proper information.

Another area that lawyers can sometimes be asked to contribute to is the documentation connected with franchise recruitment. Here I am referring particularly to the Disclosure Document, but also to other brochures or material written to attract people to invest their money and efforts in becoming a franchisee. To write a comprehensive recruitment programme, including an accurate

Disclosure Document, the writer needs to be very familiar with the whole operating system of the franchise and not just the obligation and rights listed in the franchise agreement.

Recruitment documents have to encourage or "sell" prospects on becoming franchisees in the franchise system and at the same time safeguard the franchisor from adverse legal exposure, now or at some time in the future.

The question is whether lawyers have a bigger responsibility than just writing the franchise agreement according to the client's instructions, without reasonably satisfying themselves that they are not going to severely disadvantage another party? Or does the lawyer's responsibility end after fulfilling the client's expressed requirements?

Is it part of the lawyer's responsibility to at least believe there is lawful intent, that the format or proposition is fair and reasonable and that the franchisor has access to reasonable resources to be able to carry out his or her part of the arrangement? If the lawyer has a certain responsibility in these matters, how best can he or she (a) inquire of these matters to be able to satisfy himself or herself of the answer and (b) if the answers show that the proposed franchise system is not up to standard, how does he or she go about remedying the situation with sound advice?

The Franchise Association of New Zealand publish a Code of Practice which its members must adhere to. This Code lays down minimal requirements for Disclosure Documents which is an excellent guide. However, what help is available in the most critical of all stages, the strategic planning and structuring of a particular franchise format? There are consultants who specialise in franchise development who do this and there are experienced people running franchise systems who may also be available to help. There are also some banks that have specialist franchise departments who will be able to advise where assistance may be obtained.

What are a lawyer's responsibilities? I believe any lawyer who is instructed by a potential franchisor has an obligation to advise that client of the need to obtain expert advice from others within the franchise industry. An overall assessment of the viability of the franchise operation, its relevance to the proposed market sector, the determination of fees, the preparation of manuals etc are all critical steps in the process of establishing a franchise operation. The franchise agreement is one of these critical steps but in reality the preparation of such a document should follow the essential homework that a franchisor needs to undertake before putting together the agreement. ❑

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those repudiations. In consequence, the Todds maintained that they were discharged from further obligations under the agreements. They said that they held their three stores, entirely unencumbered by any obligation, or tie, to Dymocks. The businesses could be rebranded by the Todds, or otherwise reconstituted. Dymocks would lose the very heart of its New Zealand "arm" and there would be consequential effects for the other franchisees. In any event, both parties accepted that the three agreements were at an end and the most significant single issue before the Court was whether those three agreements were lawfully terminated.

The litigation commenced in February 1998 with the Todds issuing the proceedings and claiming misrepresentation by Dymocks, and relief at common law, or under the relevant fair trading legislation. Dymocks maintain that there was no misrepresentation during the contract formations and that no moneys whatsoever were recoverable at common law or under the fair trading legislation. Dymocks immediately thereafter commenced the proceedings and sought declarations that it was lawfully entitled to terminate all three franchise agreements, orders enforcing certain restraint of trade provisions in the agreements and orders entitling it to exercise certain options conferred by the agreements to purchase the physical assets and take over the relevant leases (without compensation for goodwill or leasehold improvements). The broad result, if such orders were made, would be to put the Todds out of the businesses altogether and they would recover much less than their substantial investments and not be able to compete against Dymocks for a reasonable period of time.

Hammond J confirmed that Dymocks had lawfully terminated the franchise agreement with Bilgola (Todds) and that the counterclaim against Dymocks for misrepresentation was dismissed in its entirety. Although the Fair Trading Act 1986 is a powerful tool in areas of misrepresentation, *Dymocks* goes to show that every case must be decided on the facts and it is certainly not automatic that any representations made by a franchisor with subsequent failure by a franchisee will result in the franchisor being liable. Dymocks had express warnings on the financial projections that they could not be relied upon, that the franchisee had to do its own homework and that at the end of the day the success of the business would depend upon the franchisee and other external factors.

AUSTRALIA v NEW ZEALAND

Zumbo in his article at p 251 clearly shows the complexity of the recent franchising legislation in Australia. The definition of just what is "a franchise" is now so wide that it will catch almost everything from distributorships to agency arrangements to licences. In New Zealand we are blessed with no franchising legislation and no sign of it on the horizon. Indeed, when I presented the 1997 Survey of Franchising to the Honourable Max Bradford in December 1997 he asked whether there was a need for franchising legislation in New Zealand. I told him that in my opinion there was not, as I felt confident that the industry would self-regulate itself. He was delighted to hear that for he said that most people who came to see him wanted legislation of some kind or other and so to have someone who did not want legislation was both refreshing and positive.

Franchising is a positive industry and I would like to think that the key players in it will spread the word to the extent that it will become more difficult for non-members of the FANZ to conduct their business practices. It is crucial to have a Code in place in order to enhance the integrity of franchising and it is also to crucial to minimise the risk of people being "ripped off" by unscrupulous franchisors who do not have to comply with the Code of Practice.

Franchising is a positive way of doing business and I predict huge growth in the future. The key aspect is that franchising must be done properly and high standards should be displayed by everyone involved in it. Franchising is not a guarantee of success but the risks are certainly minimised from a business failure point of view when a strong system is followed with good support from a franchisor. The future outlook for franchising in New Zealand is very exciting. ❑

FRANCHISORS: PRINCIPALS IN THE WORKPLACE?

Clayton Kimpton and Penny Hargreaves, Gaze Burt, Auckland

find that statutory liability may not stop with the franchisee

Franchisors and franchisees, need to be aware of the implications of the Health and Safety legislation on their businesses. Although the issue of whether a franchisor can be liable for an injury or loss to a franchisee's employee has not yet been specifically addressed, the cases do give a clear picture of the manner in which a decision could be determined. In instances where the franchisor has provided processes and systems to franchisees, they may fall within the definitions of a principal, as set out in the relevant legislation. They may therefore be exposed in the event of an accident for breach of the legislation.

HEALTH AND SAFETY

The Health and Safety in Employment Act 1992 (the Act) aims to ensure employers operate safe businesses both for employees and all those who enter and use the workplace. The obligations imposed under the Act generally are for employers to remove, minimise or isolate possible hazards in the workplace. Franchisees, as employers, are subject to the requirements of the Act in providing a safe workplace for employees. Health and Safety legislation does not however vest responsibility for maintaining a safe workplace solely on the franchisee employer. The Act also extends the responsibility for workplace health and safety to a "principal", a category into which franchisors may be placed.

Section 18 of the Act states:

(1) Every principal shall take all practicable steps to ensure that – (a) No employee of a contractor or subcontractor; and (b) If an individual, no contractor or subcontractor, – is harmed while doing any work (other than residential work) that the contractor was engaged to do. (2) Subsection (1) of this section shall be read subject to s 2(2) of this Act.

Section 2(2)expressly contemplates overlapping duties on employers and principals.

(2) For the avoidance of doubt it is hereby declared that – (b) This Act may at one time impose the same duty on two or more persons. Whether in the same capacity or different capacities; and (c) A duty imposed by this Act on any person is not diminished or affected by the fact that it is also imposed on one or more other persons, whether in the same capacity or in different capacities.

The franchise relationship is one with mutual gain and reward as between franchisor and franchisee. Franchisors fit the category of "principal" as defined in the Act ie "a person who or that engages any person (otherwise than as an employee) to do any work for gain or reward". The franchisee could fit within the definition of "contractor" under the Act, which is "a person engaged by any person (otherwise than as an employee) to do any work for gain or reward".

Several recent Court decisions on s 18 have clarified principal liability. In *Central Cranes Ltd v Department of Labour* [1997] 3 NZLR 624. The Court of Appeal held that although the employer, for relevant purposes the franchisee, holds primary responsibility for workplace safety this does not diminish the responsibility on others on whom the statutory duty is imposed.

Central Cranes determined that the duty under s 18 on principals requires all reasonably practicable steps to be taken in the circumstances to ensure no employee of a contractor is harmed while doing work for the contractor. The requirements on a principal may therefore require positive or restraining acts, or both, depending on the type of work and the possible health and safety risks.

Some other recent decisions in respect of principal liability add weight to the possibility of a franchisor being held liable for the actions of its franchisees. In *Holdsworth Group Ltd v Department of Labour* [1996] 2 ERNZ 557 it was held that for a principal (as defined in s 2 of the Act) to be liable under s 18 there must be a contractual relationship between the principal and the contractor. Franchisors and franchisees are clearly in such a contractual relationship. That case interpreted "engage" when combined with the phrase "for gain or reward" to require a contractual relationship before a party could be considered a principal.

The real test will, however, be the extent of the involvement of the principal in the employers business and the level of knowledge that they have by virtue of that involvement. In *Dept of Labour v Carter Holt Harvey* 5 February 1998, Judge McAuslan, DC North Shore CRN7044003281, charges against the company as the principal under s 18(1)(b) were dismissed. In that instance where a roofing contractor fell from a roof, the defendant's only involvement had been to provide roofing materials with the job being allocated to an experienced roofing contractor. Franchise relationships will generally involve a much greater level of

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FRANCHISES – RELATIONAL CONTRACTS

Paul Sumpter, Kensington Swan, Auckland

reviews the Dymocks *litigation*

It is an infrequent occurrence when a row between a major, reputable franchisor and a key franchisee goes to trial, still less that the hearing should take up 37 days over eight hearing weeks, involve expert witnesses (including three senior Australian lawyers), and produce 10,000 pages of documents put in evidence. However, these were features of the recent High Court decision, *Dymocks Franchise Systems (NSW) Pty Ltd v Bilgola Enterprises Ltd* HC Auckland, 26 February 1999 CP 64/98 and CP 43/98 Hammond J.

The case touched on the usual array of franchise issues including the basis on which a franchisor can terminate, misrepresentation in pre-contract negotiations, post-termination enforceability (restraint of trade, lease assignment) and the impact of personal relationships between the representatives of the franchisor and franchisee. It also raised the notion of good faith and the application of this duty to "relational" contracts such as franchises.

The Dymocks group of companies was founded in 1879, originally in George Street, Sydney as "Dymocks Book Arcade". By the mid 1980s it began franchising the business. In 1994 it entered into three franchise agreements for New Zealand sites with Mr and Mrs Todd. By 1997 relations between Dymocks and the Todds had deteriorated. In February 1998 Dymocks issued termination notices in respect of all three agreements with the Todds who, in turn, filed proceedings claiming misrepresentation by the franchisor. Dymocks filed its own proceedings seeking declarations that its terminations were lawful and other orders concerned primarily with restraint of trade and the take-over of leases and other assets. These proceedings were necessary because the Todds remained in possession of the three stores and continued to trade (by consent order after an application by Dymocks for a mandatory injunction to eject the franchisee).

The case was in one respect an unusual one. The franchise agreement contained a provision (not uncommon in itself) that the domestic law of the franchisor was to apply. This was New South Wales law and, accordingly expert Australian witnesses were required (Sir Laurence Street, retired NSW Supreme Court Judge, Professor John Carter from Sydney University and Tom Bathhurst QC of the Sydney bar). This somewhat international flavour was also reflected in the judgment handed down by Hammond J who offered his own perspective on franchising, the development of franchise law and "good faith" in contract analysis. Of the English situation the Judge remarked:

> How far British contract law will be able to hold out against the recent European Consumer Protection Directives (which have now transplanted continental principles, of bona fides and good faith, directly into the body of British contract law), is one of the single most important issues in English commercial law today. The outcome is still uncertain. (at p 31.)

The position in England appears to be exemplified by the House of Lords decision in *Walford v Miles* [1992] 2 AC 128 which held that there is no general duty of good faith in agreements to negotiate (the duty being regarded as unworkable and therefore unenforceable). This is what might be termed the traditional or "neo-classical contract" view of the law (see, for discussion; "Contracts with the lot: Franchises, Good Faith and Contract Regulations" Taylor [1997] NZLR 459).

The Judge referred in more detail to North American academic and judicial analysis and to the evolving nature of Australian law. The United States Courts have long recognised a doctrine of good faith. (See eg: *Wigand v Bachman Bechtel Building Company* 118 NE 618 (1918).) Franchise disputes in North America are, according to Hammond J, considered by the Courts on the basis that it is in society's interest to bestow on each party to such a contract reasonable security for the protection of his or her justified expectations (at pp 28-30). Franchises are "relational" agreements and for reasons both of justice and economics are subject to implied duties of fairness and reasonableness. As far as Australia is concerned (and this was the law of relevance in the case before him) Hammond J observed that in this jurisdiction, too, the law appeared to be developing concepts of good faith in contract law. His Honour's overarching observation was that a franchise contract was a two way street:

> whether viewed from a "slice of goodwill" conception, or as a relational contract, the franchisee is seen as having a very valuable, and protectable interest. He or she has certain legitimate expectations which, increasingly, the law will not allow to be trumped by brutal contract terms. (at p 31.)

Thus predisposed, the Judge turned to the particular facts and law at hand. The first issue was the construction of, in particular, the termination provision in the franchise agreement. The critical clause read (in part) as follows:

> the Franchisor shall be entitled to terminate the Agreement forthwith upon delivery of written notice of termination to the Franchisee if the Franchisee or Guarantor commits or permits any one or more of all of the following acts:

Such a provision is not uncommon in a franchise agreement and the Judge's findings are of interest. The franchisor, unsurprisingly, argued that a breach of any one of the expressly listed "acts" was sufficiently serious as to warrant termination. The Judge disagreed. He held that as a matter of construction the terms were permissive, that is the franchisor was not given an absolute right to terminate. Support for this was found by statements in the Dymocks' operations manual along the lines that "we will give you fair notice ...". The manual was relevant because, the Judge so held, the whole of this document formed part of, together with the formal franchise agreements themselves, the contractual documents between the parties. Indeed, to the possible discomfort of the franchisor, this encompassed parts of the Australian "Franchisors Association Code of Ethics" which had been set out in the operations manual. In further support was common law to the effect that a party may be estopped because of a particular understanding of the way a given term is to be read or understood (see eg: *Adaras Developments Ltd v Marcona Corporation* [1975] 1 NZLR 324, 329). Finally, under Australian law the Judge decided that an implied term of reasonableness may apply to the exercise of the right of termination. It did here, particularly as this, a franchise contract, had in the Judge's opinion a "relational" quality.

The Judge then analysed the particular grounds of termination advanced by Dymocks. A few matters were quickly dispensed with, namely breaches of the operations manual and alleged refusals or failures to participate in group buying deals and promotional activities etc. Taking an approach likely to be of concern to franchisors, Hammond J regarded these as "de minimis, substantially historical and none, whether alone or cumulatively coming anywhere near the standard to be sufficiently serious to warrant termination" (at p 40).

The lynch pin basis for termination advanced by Dymocks was for "conduct impairing goodwill" and/or a repudiation of the franchise agreement. This occurred principally in the form of a fax sent to other franchisees in New Zealand by Mr Todd explaining the difficulties which the Todds said they were experiencing with the franchisor, inviting comment and implying that all the franchisees should "gang up". However the Judge, whilst conceding that this conduct was "strong and even provocative" (at p 56) did not regard it, given the context, of such character or quality that amounted to a breach and as justifying summary termination. Nor did it amount to a repudiation of the contracts by the Todds (on the evidence, Mr Todd's fax indicated a "suspension" of activities, not an intention not to be bound). This finding is likely to raise franchisor eyebrows. The fax letter to the other franchisees said "I will no longer participate in any Dymocks' activities until the dispute is resolved" and appeared to suggest implicitly such a course of action might be appropriate for other franchisees. Dymocks saw the fax as an "incitement ... to revolt" and as a repudiation of the franchise contract.

To this point it was all doom and gloom for the franchisor – the grounds of termination set out in its notices were insufficient. However, and unbeknown to them at the outset of the proceedings, Dymocks had an ace to play. As late as the closing address an application was made to add a third ground of termination alleging breach of express and implied obligations of confidentiality under the franchise agreements. These were based upon secret discussions (unearthed only after contested further discovery and evidence extracted early at trial from a witness called by subpoena) held by Mr Todd in September 1997 with Dymocks' main competitor, the "Blue Star" Group. It was held that confidential information had been disclosed by Mr Todd to Blue Star. A vital ingredient in his finding that this permitted summary termination was the Judge's holding, pursuant to New South Wales law, that this was also a case where a party could justify termination by reference to a ground which was not known at the time of termination.

Also crucial to the finding in favour of Dymocks was the Judge's discussion of the law of implied confidentiality obligations. The express clause in the franchise contract was in familiar terms:

> The Franchisee acknowledges that his knowledge of the operation of the Business, the Dymocks System, its products and services is derived from information disclosed to the Franchisee by the Franchisor pursuant to this Agreement during the training course and in the Confidential Operations Manual, and that such information is proprietary, confidential and a trade secret of the Franchisor. The Franchisee agrees that it will obtain the absolute confidentiality of all such information and not use any such information.

The difficulty with this clause was that it did not extend to the information Mr Todd had given to the competitor which primarily concerned Mr Todd's/the franchisee's own accounts and key business information. Citing as an example *Thomas Marshall (Exports) Ltd v Guinele* [1979] Ch 227 the Judge held that there was ample authority to the effect that he could supplement express terms which prohibited the disclosure of confidential information, by wider, implied obligations. Accordingly the franchisee's business was held to be confidential to the franchisor and therefore could not be disclosed without permission to a competitor in circumstances giving rise to obvious detriment to the franchisor. In this context the Judge pointedly referred once again to the special nature of a franchise agreement – it was a "relational" contract.

As is frequently the case in many franchisor termination disputes the franchisee had retaliated strongly in this case with allegations of misrepresentation. Under New Zealand law the Judge could have called upon the assistance of the Contractual Remedies Act but it was New South Wales law which applied and this involved the old, subtle distinctions of the English common law between "innocent" and "fraudulent" misrepresentations. None here were in the fraud category and thus for the misrepresentation to be actionable it had to be false, intended by the representor to be relied upon and inducing the representee to enter into the contracts.

The franchisee also relied upon misleading or deceptive conduct under provisions in Australian legislation (there are of course similar but subtly different ones in New Zealand law) prohibiting misleading or deceptive conduct. As can be expected in a case of this length and complexity a number of factual bases were submitted as amounting to misrepresentation or as being false or misleading conduct. The core allegation concerned financial projections produced by Dymocks. But none of these bore fruit: Dymocks had been scrupulous in presenting material to the prospective franchisee, who also had his own expertise in financial matters (he had been a senior bank economist).

The counterclaim failed. Dymocks had lawfully terminated. What were the consequences? These were not straightforward. Dymocks wished to enforce a provision in its franchise contracts to take over the business assets and leases. Despite argument to the contrary, this provision was held not to be a penalty – the clause simply provided for what was to happen to business assets in the event that the franchise relationship came to an end. Dymocks, accordingly, was entitled to enforce its option to take over the business assets and leases. (An application for stay of execution pending an appeal filed by the Todds has subsequently been dismissed by the High Court and the Court of Appeal.) Dymocks also wanted to enforce a restraint of trade clause. This provision, in familiar terms, was found to be applicable (it survived termination). Favourable reference was made to the UK franchise decisions, *Office Overload Ltd v Gunn* [1977] FSR 39, *Prontaprint v Landon Litho Ltd* [1987] FSR 315 and *Kall-Kwik Printing UK Ltd v Rush* [1996] FSR 114 in support of the finding that the franchisor had protectable interests and, further, that the restraint was reasonable.

What does the Dymocks case demonstrate for franchisees, franchisors and their lawyers? Much of the case covers familiar ground – the need for care in presenting material to would-be franchisees, the part played by personality differences, the reasonableness of restraint and termination provisions and so on. Although this was a case decided in accordance with Australian contract law, the observations of Hammond J are clearly relevant in this jurisdiction and of key significance is his opinion that franchise agreements are "relational" and subject to a duty of good faith. Recent New Zealand contract cases indicate a willingness to recognise such a duty: *Provost Developments Ltd v Collingwood Towers Ltd* [1980] 2 NZLR 205, *Allen v Southland Building and Investment Society* (1995) 6 TLCR 643 and *Livingstone v Roskilly* [1992] 3 NZLR 230 are examples. According to this view, therefore, franchisee behaviour bordering on mutiny may not necessarily permit a franchisor to terminate. The carefully crafted and detailed provisions designed to confirm the franchisor's "feudal" dominance in every situation will be subject to the second guess of the Court. Life for franchisees cannot be rendered "nasty, brutish and short" by over-bearing contracts. However, from a franchisor's viewpoint the strength of franchising as a concept is undermined to the extent that this decision makes it very difficult for a franchisor to enforce strict compliance with its procedures. The decision also leaves the franchise lawyer with some interesting dilemmas in advising franchisees and franchisors alike. ❑

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control. So, although *Harvey Roofing* shows the Courts will be sensible in applying liability to principals, the Courts are unlikely to allow franchisors (who have manuals and set policies and procedures) to avoid liability in the event of an accident arising from the existence or use by a franchisee or employee of the franchisor's policies and procedures.

From the prosecutors point of view, proceeding against a franchisor is more attractive than merely proceeding against a franchisee. Compliance across a whole network is obtained by a single prosecution. Thus, the policy of the Act is enforced to the maximum effect.

The Act also places liability on lessors where they are owners of premises. Owners are expected to have some control over the premises. Franchisors also need to be aware that the Act places responsibility on them in that situation and that where they also have a responsibility in that regard for workplace health and safety it will be even more likely that they will be prosecuted for a breach either as an owner or as a principal or in both respects. Where a franchisor leases premises to a franchisee this will therefore heighten its health and safety responsibility.

Franchisors who want their franchise to have consistency cannot avoid setting specific procedures for franchisees to follow. Where franchisors stipulate terms and procedures in the franchise agreement and/or manuals, which require particular machinery, equipment or processes in order to carry out particular jobs, they need to ensure that the proper health and safety procedures in relation to those requirements are also made available to franchisees. Franchisors should check to ensure the health and safety procedures are followed on site. Franchisors who fail to take these steps where they have a high degree of control over the product being used in the workplace, could open themselves up to prosecution for health and safety breaches. The greater the level of control the franchisor has over the behaviour of the franchisee, the more likely they are to become liable as a principal. Close monitoring and high standards in of health and safety may also have a beneficial effect on premiums under the Accident Insurance Act 1998.

HUMAN RIGHTS

Another area of liability as a principal that franchisors could fall into is under s 68(2) of the Human Rights Act 1993. In the decision *Totalisator Agency Board v Gruschow* [1998] 3 ERNZ 638 principal liability was considered. The primary consideration was held to be whether the relationship between the principal employer and the person who was alleged to have breached the Act was such that it ought to have created responsibility under the Act. Where the franchise system manuals prescribe the manner by which franchisees should hire and fire employees, the terms to include in employment contracts, and pre-employment questions to ask, then the franchisor could become responsible for any difficulties arising from those documents in respect of breaches of the Human Rights Act 1993.

Although *Gruschow* was remitted to the Tribunal for determination, the High Court considered that the appellants could be responsible for Human Rights breaches because of some necessary element of control or because of a direct relationship with the employment of staff. If franchisors assist franchisees to select managers or any other employees, or if they impose strict requirements on franchisees, it could be open for the Proceedings Commissioner to claim discrimination under the Human Rights Act against the franchisor. Again, it will be the level of control the franchisor has on the relationship that is at issue.

CONCLUSION

In view of all the above, failing to monitor everyday practice or to update policy can prove to be false economy. A decision against a franchisor as a principal is a criminal prosecution and so could not only cost the principal by way of a fine but also by loss of reputation and market share. Franchisors should closely monitor franchisees to ensure on site compliance in practice with procedures or policies. ❑

KEEPING THE DEAL TOGETHER

Brian Keene, Barrister, Auckland

adds a comment on Dymocks

The principal issues before Hammond J in this case, were whether the franchise agreement had been validly terminated by Dymocks, whether this entitled Dymocks to take over the book stores run by Todds, and whether Todds were induced to enter into the agreement by misrepresentations and/or misleading or deceptive conduct.

Hammond J rejected a number of grounds for termination. However, he held that the Todds' actions in handing over key financial information to a competitor about Todds' own business for the purpose of potentially joining forces with it, was a breach of an implied obligation of confidentiality entitling Dymocks to terminate the agreement summarily. He rejected an argument that the contractual consequences of termination (taking back the business) was a penalty because they came into play on termination for any reason not just breach.

The alleged representations related to projected turnover and profitability, and statements by Dymocks as to the number of stores that would be opened in New Zealand. Hammond J rejected Todds' misrepresentation arguments, finding inter alia that on the facts pleaded there was no misrepresentation as to present or past fact capable of constituting misrepresentation or misleading or deceptive conduct in law.

The law of New South Wales governed the agreement. Accordingly, while one expects that the same conclusions would be reached under New Zealand law, caution needs to be exercised in placing weight on the decision.

The interest in the case from a New Zealand perspective, lies in Hammond J's analysis of franchise agreements as contracts of a "relational nature" (drawing in North American authority) to which different contractual rules may apply in contrast to the simple bilateral contract. Other examples cited as relational contracts were distributorships, joint ventures and some employment contracts.

Hammond J considered that in a relational contract the parties are involved in a working, ongoing and often relatively open ended relationship set up for the parties' mutual benefit. There is a joint maximisation of economic benefits. It is in society's interests to accord each party a reasonable security for the protection of his or her justified expectations which ought not to be "trumped by brutal contract terms" (at p 31). The North American view was stated as being that what is important is keeping the deal together, from which it follows that performance is terminated in law only if a breach of a substantial nature occurs.

Notably, an approach premised on "keeping the deal together" does not sit well with the relational nature of the contract because this requires that the parties be able to work together. A minor breach may have been the last straw in a relationship that has broken down. In requiring a substantial breach, Hammond J seemed to be more concerned with protection of the franchisee from abuses inherent in the relationship than with the "relational aspect" as such.

The relational nature of the agreement led Hammond J to two implied obligations. First, there was an obligation of reasonableness in termination of the contract (importing with it requirements to give notice of termination, and time for remedy of breaches). In the event, Hammond J held that there was an express term to the same effect.

Second, Hammond J found that there was an implied obligation that a franchisee must not inappropriately disclose even that own franchisee's information to third parties. Breach of this obligation was in the circumstances so serious as to justify summary termination notwithstanding the "reasonableness in termination" obligation.

Dymocks framed the obligation as an implied obligation of confidentiality. This does not seem apt given that the material that the Todds shared with the competitor was its own business information and accounts. While accepting Dymocks' submission, it seems that Hammond J saw the duty as a subset of an overall duty of good faith of both parties to maximise the benefit of the contract, rather than as breach of confidence as such. It is submitted that this is a better foundation for such an obligation.

Hammond J noted the difficulties in determining when a party was improperly using its own information rather than normal usage of it, but considered that this could be addressed by reference to the facts of the particular case. An analogy was drawn with the line between employees permissibly using general information, and impermissibly using special information derived in the course of employment.

The "different rules" that are suggested as applying in relational type contracts appear to be grounded in notions of good faith in contract performance and reasonableness in the exercise of contractual rights. Hammond J was bolstered by the developing Australian law of good faith in contract and new Australian legislation protecting the franchisee.

New Zealand Courts have not embraced that concept, at least at a general level (although see *Livingstone v Roskilly* [1992] 3 NZLR 230 at 237 per Thomas J). However, there are clearly duties of good faith and fidelity in employment, and obligations of good faith in a joint venture context were implied at least on the facts in *Kiwi Gold No Liability v Prophecy Mining No Liability* (18 July 1991 CA 30/92).

If Hammond J's approach develops in New Zealand law, it will be important that content be given to the "good faith" obligation. Hammond J's decision begins to do just that. An appeal against the decision is pending. ❑

FRANCHISING AND THE COMMERCE ACT

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find that this method of growing your business has competition law implications

Franchising is gaining in popularity in New Zealand as a method of business expansion. One of the features of a franchise is that the franchised businesses operate and are owned independently, but their freedom of action is constrained by the franchisor's framework. This dichotomy can lead to anti-competitive behaviour.

Unlike chain stores or other retailers that are subsidiaries of a company or otherwise part of a single interconnected group, the fact that a group of franchisees are all part of a single franchise arrangement gives them no general exemption from the provisions in the Commerce Act 1986 on restrictive trade practices. This article examines the impact of the Commerce Act in some of the main areas of franchising activity.

PRICING

Price fixing

The area of franchising activity most likely to raise Commerce Act concerns is pricing. Section 30 of the Act prohibits arrangements between competitors that attempt to control prices (ie price fixing). The fact that this restricts franchisees and franchisors comes as a surprise to many of them, who see "uniformity" as one of the defining features of their franchise. There may be an expectation that this will extend to all aspects of the business, including prices. In addition, franchisees often do not regard other franchisees in the same franchising group as competitors, even though they often are.

The prohibition on price-fixing is wide-ranging and catches any arrangement which fixes or attempts to fix prices, including an agreement which specifies discounts, credits or rebates. A group of franchised car dealers was caught out a couple of years ago for agreeing (at monthly franchise meetings) on maximum discounts that would be available to purchasers of new cars. This had the effect of fixing the minimum price for car sales: *Commerce Commission v North Albany Motors Ltd* (HC, Auckland, 4 December 1996, Morris J, CP 88/94), judgment was by consent with an agreed penalty.

There is an exemption in s 32 of the Act to the prohibition on price fixing arrangements for "recommendations" promulgated by groups of 50 or more persons who supply or acquire the relevant goods or services. This is primarily considered applicable to trade associations but theoretically applies to large franchise groups. The recommendation is still subject to the general prohibition on substantially lessening competition contained in s 27 of the Act.

Resale price maintenance

Linked to price fixing is the issue of resale price maintenance. This is essentially vertical price fixing, in which a wholesaler or supplier attempts to dictate the price (or the minimum price) at which retailers can resell products purchased from the wholesaler. As franchisors often supply products to franchisees, and (perhaps more so than other wholesalers) they have a significant investment in the revenue gained through resale, the opportunity and incentive for resale price maintenance is often present.

Conduct falling short of an actual requirement to resell at a particular price is also caught, if it attempts to "induce" a minimum resale price. In effect, any pressure by the supplier or consequences that negatively affect the reseller's business, will qualify. For example, the franchisor supplying on less favourable terms to a non-complying franchisee (or threatening to do so) would breach this prohibition. In addition, preventing a reseller from advertising goods below a specified price is also prohibited.

Interestingly enough, specifying a maximum resale price is not prohibited (although in some cases it may breach the general prohibition on substantially lessening competition). Furthermore, a franchisor that supplies raw materials only is not prohibited from specifying the price of the finished product, as the prohibition catches only "resale" of the supplied goods and does not apply where the original goods have been transformed.

Price recommendations

Genuine price recommendations by suppliers are specifically exempted from the prohibition on resale price maintenance (although, again, it is potentially possible that they could still be illegal under the prohibition on substantially lessening competition). The rationale for this is that suppliers may be in the best position to provide information on what prices are appropriate – this is particularly true for franchises, where the franchisee is often relying on the franchisor's greater experience and expertise for the franchised business to succeed. However, to gain protection of the exemption, the recommendation must be genuine. The goods must either carry the tag "recommended price", or franchisees must be informed beforehand that the price is recommended only and that the franchisee is under no obligation to adopt it. If there are any repercussions on the franchisee for not following the price, the recommendation is clearly not genuine and the franchisor could not rely on the exemption. This is important, as the potential for franchisors to pressure franchisees is considerable as, unlike many other retailers, franchisees often have only one source of supply, and usually rely on the franchisor for support and other functions (such as advertising).

JOINT BUYING AND PROMOTIONS

The opportunity to purchase goods in bulk and to enter into joint promotion arrangements is an important benefit of franchises, particularly in industries where bulk buying has a major impact on price and where the franchisees are relatively small and could not otherwise compete with larger businesses.

However, a joint purchase by a group of franchisees is likely to be price fixing. The Commerce Act recognises the potentially pro-competitive impact of joint buying (particularly in enabling competition with large single purchasers) by providing an exemption to the price fixing provisions. The exemption applies to prices for goods or services to be "collectively acquired" by parties to the contract. The requirement for goods or services to be "collectively acquired, directly or indirectly" enables franchisees to use their combined power to negotiate under the franchise umbrella, either through one franchisee (or the franchisor) acting as their agent, or as joint purchasers. It is not clear whether the situation of franchisees negotiating a special price but each purchasing separately would obtain the protection of the exemption.

Joint advertising of the price for resale of collectively acquired goods is also permitted (although it should be noted that this does not apply to services). In practical terms, that means that franchisees that collectively acquire goods can agree on the advertised resale price. This is a significant benefit for franchisees, as joint advertising often plays an important role in the success of franchised businesses, and promotes the overall reputation of the group to consumers. However, the franchisees cannot agree to sell at this price as this would be a breach of the prohibition on price fixing. This distinction is a fine one.

REFUSALS TO DEAL

Franchisees and franchisors need to be aware that aggressive use of their combined power may be anti-competitive if it limits the ability of others to compete with them. Section 29 of the Act prohibits exclusionary provisions (commonly known as "collective boycotts"), which are arrangements between competitors who agree not to supply goods or services to (or acquire them from) a rival competitor. It is necessary for at least two of the parties to be in competition. The "target" (ie the affected party) must also be a competitor of at least one of the parties. As franchisees are in competition with each other (in most cases), concerted action against another competitor could well breach this provision. Such arrangements could include:

- a group of franchisees agreeing with a supplier not to purchase goods from a second supplier;
- a group of franchisees agreeing with a supplier that the supplier will not supply to a competing retailer;
- pressure from a franchise group which supplies goods to prevent a retailer buying from another supplier.

THE FRANCHISE ARRANGEMENT

This article has focused on the potential anti-competitive nature of the operating activities of franchised businesses, rather than on the nature of the franchise arrangement itself. However, franchisors in particular should be aware that terms that limit the freedom of franchisees to compete may be anti-competitive. For example, an exclusive dealing requirement that the franchisee sources product only from the franchisor could potentially substantially lessen competition (although in the seminal case on this issue, exclusive dealing arrangements between a leading whiteware manufacturer and dealers were held not to substantially lessen competition, despite the considerable market share of the supplier *Fisher & Paykel Ltd v Commerce Commission* [1990] 2 NZLR 731).

Another typical feature of franchises is an exclusive territorial arrangement. Although this is a restriction on franchisees, it is unlikely – under the current law – to be anti-competitive unless there are no similar products available to consumers in a territory (assuming the territory constitutes a market). In most cases where a competitive market exists and the franchisor is not dominant, restrictions (territorial or otherwise) in the franchise arrangement will not be anti-competitive.

However, the proposed Commerce Amendment Bill currently before Parliament broadens the range of behaviour that is deemed to substantially lessen competition to include arrangements that have the effect of allocating a market for goods or services. This would prohibit franchise agreements that provide for exclusive franchise territories (or other allocations such as allocating different types of customer to different franchises).

CONCLUSION

The basis of the Commerce Act, and particularly of the prohibitions discussed above, is to promote competitive behaviour by market participants. Authorisations for restrictive trade practices are available under the Commerce Act if the public benefit outweighs the anti-competitive detriment. However, it is unlikely that the type of arrangements discussed in this article, particularly pricing arrangements, would be granted authorisation in a normal market situation. Therefore, franchisees and franchisors need to be aware of the provisions of the Commerce Act and how these impact upon their businesses in order to maximise business opportunities while minimising legal risks. The proposed changes to the Commerce Act would, if they come into effect, make it more difficult for some of the defining characteristics of franchises to survive. ❑

FRANCHISING: PRE-CONTRACTUAL RISK

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identify the challenges

Business format franchising is probably best considered as an integrated marketing concept rather than as a distinct legal concept. It is a way of allowing an independent business to maximise its chance of survival within a global framework of growing vertical integration. (Boe, Ginalski & Henward, *The Franchise Option* (2nd ed) International Franchise Association, Washington DC (1987) at p 1) A network of motivated business people using their own capital to widely penetrate a market under a common brand is a powerful force in today's competitive environment. That is not to say that the peculiarities of this form of commercial arrangement and its legal consequences can be overlooked, but rather that the arrangement is fundamentally concerned with marketing.

One result is the focus that those involved in procuring new franchisees bring to the market. The success of the franchise is dependent on many factors including the size, and thus the strength, of the network. The larger the network, the greater market penetration it achieves. At least in the early stages of establishing the network, this can lead to an over-emphasis on "selling the franchise". The establishment of new franchisees can become the preoccupation of the franchisor particularly if early capital return to the franchisor is a priority or there is an over-zealousness to expand the market rapidly.

This focus raises a very real risk in the area of pre-contractual representation. This risk is increased when it is recognised that prospective franchisees looking to buy a franchise usually have very high expectations of the knowledge and expertise of the franchisor and rely upon the credibility of the franchisor and the franchise system. Disputes arise from unmet expectations and perceptions.

A recent New Zealand Law Society seminar (*Deception in Commercial Dealings*, T Arnold QC and D Goddard (May 1999)) identified 16 separate causes of action that can arise as a result of statements made in the course of "selling" generally, which would include "selling" a franchise to prospective franchisees. Statutory causes of action include breaches of the Fair Trading Act, the Contractual Remedies Act (particularly for misrepresentation), the Contractual Mistakes Act, and the Illegal Contracts Act. Contractual rights of action can arise as a result of pre-contractual statements being read into the terms of an agreement, and causes of action in tort include negligent misstatement, deceit, and conversion. A variety of equitable rights may also arise. A franchise relationship may be open to a claim for breach of fiduciary duty. The authors of this article disagree between themselves on this issue. There is only one reported case, *Jirna Ltd v Mister Donut of Canada Ltd* (1970) 13 DLR (3d) 645 and on appeal at (1973) 22 DLR (3d) 303, dealing with this issue. Being Canadian, it may overstate the relevant equitable principles, and the principle was rejected on appeal. However, there is a clear risk on this concept being advanced further, arising from the interdependent nature of franchise relationships. In addition, there is the prospect of equitable proprietary claims, estoppel, and knowing receipt. Claims that could be categorised as restitutionary can also arise: money had and received and possibly knowing assistance (otherwise referred to as dishonest accessory liability).

It is obviously important to a franchisor that the risk of a claim based on one or more of these available causes of action be minimised. It is also important to the network of franchisees because it only takes one claim to take the franchisor's focus away from the franchise business. A successful claim can also potentially destroy a whole network as in the high profile Cut Price Deli chain collapse in Australia: *Tomlinson v Cut Price Deli* (1995) ATPR (Digest) 46-151, Drummond J

The nature of the franchise relationship involves a particularly strong reliance factor, especially in the early stages the issue of reliance is a large feature in many of these causes of action. The established franchise system itself reinforces reliance aspects of the relationship and, notwithstanding the contractual basis of the franchisee/franchisor arrangements, there are elements which are at least analogous to fiduciary concepts. It is not uncommon to find in franchise agreements an express contractual term requiring good faith. This tends to highlight that the relationship is something closer then a commercial arm's length transaction. The strength of a mature franchise arrangement is this "interdependent" nature of the relationship.

One of the "selling points" of a franchise is the minimisation of business risk, reliance on the franchise system, and the existence of an infrastructure of support and guidance to minimise that risk. This can lead to the business risk of the independent operation that the franchisee is being asked to operate, being "under sold". The corollary is that the reliance aspect of the franchise arrangements are "over sold".

The facts in *Williams v Natural Life Health Foods Ltd* [1998] 1 WLR 830 (HL) are typical of the type of dispute that arises. A franchise opportunity was sold to a franchisee based on financial projections that were not achieved, and which the House of Lords found to have been negligently prepared. The interesting element of that particular case was the attempt to fix personal liability on a director of the franchisor company. This was promoted on the basis that the franchisee relied on the personal experience, wisdom, and expertise of that director, when deciding whether or not to engage in the venture. The reasoning of the Court has excited academic comment (Farrar, "The Personal Liability of Directors for Corporate Torts" (1997) 9 Bond LR 102) but raises, perhaps as a side issue, the question of protection against personal liability for the same causes of action identified above. In the New Zealand context, s 45 Fair Trading Act also raises that issue.

The risks to a corporate franchisor are significant. The prospect of personal liability, notwithstanding the existence of a corporate identity, is sobering.

Having identified the risks, the balance of this article is designed to provide some practical pointers in the management of that risk.

MANAGING THE RISKS

The fundamental issue in relation to risk management is the establishment and maintenance of a suitable record of representations made prior to contractual commitments. The object of this approach is to attempt to bring any analysis of the issues back within an entirely contractual framework. At the very least, it raises the credibility of the franchisor, and limits conflicts of evidence.

Disclosure documents

The prime means for achieving this result is to provide initial disclosure documents that are accurate, specific, and complete. Everyone then knows and has a record of exactly what representations the franchisee must have relied upon in entering into the franchise.

Typically the documentary trail would be as follows:

(a) A booklet that generally outlines the franchise, which is essentially an "advertising" or promotional exercise. This must nonetheless be accurate;

(b) Should a potential franchisee then wish to proceed, it is usual to require at that point a confidentiality agreement;

(c) On receipt of the confidentiality agreement, the franchisor ideally provides (following appropriate selection interviews), detailed initial disclosure documentation of the franchise operation. This may include amongst other things, such details as the financial information from a selection of outlets (which should include a balance of the good outlets and the bad outlets), details of history and business experience of the franchisor, the nature and development of the franchise system, details of intellectual property, a summary of commitments to be made, details of past litigation and any current unresolved disputes, and other relevant information that is available such as lease terms, plant and fitout costs, and all other information necessary for a franchisee to perform a "due diligence" inquiry. Where financial projections are provided (it is prudent not to venture down this path), then the basis of assumptions upon which representations are made should be clearly provided;

(d) A prudent franchisee should also seek to peruse the operations manuals relating to the franchise system before making a final commitment. These manuals usually form part of the franchisee's legal commitment and should provide a detailed picture of the franchise system. A wise franchisor will permit a franchisee to peruse this document. Provided it is complete and accurate the manual can also become a risk management tool as far as representations are concerned.

Upon receipt of documentation the franchisee should be required to take their own independent accounting and legal advice and form their own judgment of the viability of the franchise opportunity.

If the franchisee is then satisfied that this opportunity is worthwhile, the formal franchise agreement can be entered into. The franchise agreement may include a clause that the franchisor enters into the agreement on the basis of the full disclosure by the franchisee of the representations it is relying on. It may also include an acknowledgement by the franchisee that there is no reliance upon any representation made by the franchisor except those expressly stated in either the initial disclosure document or the franchise agreement itself. In other words, the contract terms reinforce the obligation of disclosure of representations by "putting the boot on the other foot". The agreement should also emphasise the franchisee's responsibility to exercise its own judgment of the commercial viability of the business.

This regime allows considerable control by the franchisor over the nature and extent of disclosure made. It can thereby manage its risk.

Verbal representations

As it is not uncommon for a variety of verbal representations to be made in the course of selling or negotiating a franchise, including by any third party, it is also prudent to identify any such further representations. This can be achieved by requiring the franchisee to record any further representation it has relied upon in a written document (sometimes called a deed of representations) and, if accepted by the franchisor, can be signed by both parties. This establishes a complete record of the basis of the agreement. It also provides the franchisor with the opportunity to reconsider any representations identified by the franchisee as having been made at that point in the transaction.

The franchisee is entitled to rely on the information provided. Obviously, it is important that the franchisor does not provide "edited versions" of the facts. For instance, failure to refer to any franchisee business failures could be regarded as misleading. Providing only financial information regarding the best performing franchisees is certainly misleading. There is a significant body of decisions already where the franchisor has attempted to only selectively disclose such information. (see *Cut Price Deli*)

It is also important for the franchisee to make clear the source of information provided. Where information is not within the actual knowledge of the franchisor, this should be disclosed and the franchisor should make an appropriate disclaimer regarding the information. Otherwise the franchisee may believe that it has been adopted and approved by the franchisor. Again, the franchisee will rely on the franchisor's knowledge expertise and ability in that particular area. (*Miba Pty Ltd v Nescor Industries Group Pty* (1996) 141 ALR 525, *Thompson v Ice Creameries of Australia Pty Ltd* (1999) ATPR 41-611(p 40,672)) Reliance on the franchisor will be significantly reduced if the franchisor has disclaimed the information and, further, has invited the franchisee to make such further or other inquiries as it deems appropriate.

Disclosure, not "selling"

The disclosure stages must involve documentation that is characterised as being cautious, and moderate. This is not a "selling" stage, although obviously is of primary importance in the franchisee's determination of whether or not to take up the business opportunity. Any attempt to "gild the lily" at this stage is likely to rebound on the franchisor and provide the basis for a subsequent claim. Carefully and thoroughly prepared disclosure documentation sends a healthy early signal to a franchisee that it is dealing with a prudent franchisor that manages risk, and that has to be good for both parties as well as the network as a whole.

For this reason, the disclosure stage should be purely historical and factual. It is recommended that "projections" be avoided. The franchisee should have been encouraged to seek its own legal and accounting advice. Leave it to the franchisee's lawyer and accountant to prepare any "projections" and develop the franchisee's own business plan. The franchisor should merely provide historical factual information regarding the performance of a full range of existing franchisees, upon which the proposed franchisee can base those projections. The prospective franchisee should also be encouraged to make direct inquiries of other franchisees in the network.

the cooperative nature of a franchise relationship means that the prospective franchisee has to be considered more as a partner, than as an employee

Similarly, any opinions that are given in the course of this process must be provided on a sound and honest basis and be suitably qualified. It is to be expected that the franchisee will seek opinions on such matters as the suitability of a new site. When providing an opinion on such a matter, the basis for the opinion and the fact that it is only an opinion should be clearly stated and recorded. It would also be prudent to disclose in detail the franchisor's policy for site selection and encourage the franchisee to make their own independent judgment. The new Australian Code of Practice for the franchise industry now requires this.

The franchisor should ensure that it keeps good records of discussions, and possibly go so far as to develop a "disclosure system". In *Ice Creameries* the franchisor was able to give good evidence, corroborated by other franchisees, that when asked particular questions, these were always dealt with in a particular way. The Court found that this practice assisted in resolving a credibility issue in favour of the franchisor. (at 40,691)

The due diligence process in effect amounts to a "cooling off" period, allowing the franchisee access to relevant material and an opportunity to consider for itself whether the business is viable. It is recommended that sufficient time be given for this process, so that no allegation of undue haste and pressure can be levelled at the franchisor. If there are commercial reasons for haste, the franchisor should deal with those in other ways, rather than putting pressure on a franchisee to commit its resources to a long-term franchise arrangement.

FRANCHISEE SELECTION

The process of franchisee selection is an important one that can be overlooked given the commercial focus of extending the franchise network. However, to commit to a long-term relationship with a franchisee who is inappropriate for reasons of personality or business acumen, can be extremely counter-productive in the short to medium-term. At the end of the day, the cooperative nature of a franchise relationship means that the prospective franchisee has to be considered more as a partner, than as an employee. The relationship is a close interdependent one which will move through various phases of growth and tension during the term of a franchise. A franchisor must be aware of this and know how to respond appropriately and manage the relationship including the inevitable conflict. This can be lost sight of in the rush to have franchisees "signed up".

Due to the significant reliance factor identified earlier in this paper, the franchise system licensed to the franchisee must in itself be comprehensive. The franchisee is entitled to rely on that system meeting all necessary relevant legal criteria and obligations. Licensing requirements, tax obligations, resource management issues, employment, human rights issues, health and safety concerns, product supply considerations, should all be dealt with adequately within the franchise system and particularly through the operations manuals and training programmes. It is not possible to move all those obligations onto the franchisee without significantly affecting the value of the franchise. The credibility of the franchise system is itself compromised if the franchisee must "discover" the legal obligations arising from the operation of the system. However it is also important to balance this with a clearly established understanding that the franchisee is ultimately responsible for running their own independent business and should take their own independent advice on legal responsibilities as they particularly apply to actual trading activities.

INSURANCE

As a final practical issue, and in addition to rather than in substitution for the foregoing suggestions, the availability of insurance for franchisor's risks should also be considered. The writers are aware of at least one insurance product in the market designed particularly to deal with the types of risk identified in this paper. Apart from the franchisor protecting its own risk by this means, it also safeguards the franchisee's interest to a degree in that such protection will assist in safeguarding the continued existence of the whole franchise network should an unfortunate or even mischievous claim arise against a franchisor.

CONCLUSION

Even with all the proactive steps identified above, there can be no guarantee that a franchisor will be protected from a claim. Even with a perfect record, but knowledge that the franchisee misunderstands the effect of the information, the franchisor can still be guilty of misleading conduct. At the end of the day, a franchise network involves a series of business opportunities and a diverse group of players. Not all will be successful. Failure could be directly related to the franchisee's own performance or simply the uncertainties of the market place. That is a business reality which a careful and diligent franchisor should not be held responsible for. A franchisor faces a considerable armoury of potential causes of action arising particularly from pre-contractual representations. Reliance factors weigh in favour of a franchisee being able to successfully mount such a claim. However, the practices set out above reduce the likelihood of claims, or of any claims being successful. This thereby secures the long-term credibility of the franchisor, the franchise system and the network. It also maximises the prospects of marketing and business success, both for the franchisor and the franchisee. ❑

A FRANCHISING CODE?

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assesses Australia's new mandatory franchising code of conduct

Following the failed experiment of a voluntary Franchising Code of Practice and the subsequent recommendation for franchising legislation made by a bipartisan Federal Parliamentary Inquiry into Fair Trading, the Australian Federal Government has prescribed a new mandatory Franchising Code of Conduct under Part IVB of the Trade Practices Act 1974. In doing so, the Federal Government has filled the regulatory vacuum left by the collapse of the previous voluntary Code without recourse to potentially rigid franchising legislation that could, over time, fail to adequately reflect changing industry circumstances.

Having chosen a mandatory Code of Conduct as the mechanism for regulating franchising relationships, the government must ensure that the Code strikes an appropriate balance between the respective interests of franchisors and franchisees. Such a task will no doubt be controversial. Indeed, while it must not be used to impose unnecessary or stifling regulatory requirements on franchisors, the Code must ensure that franchisees receive appropriate information on a franchise system and gain suitable protection from potential abuses of power by franchisors.

NEW REGULATORY REGIME

With the Code now prescribed under the Trade Practices Act, the onus has fallen on the franchising sector to implement mechanisms for complying with the new regulatory regime. Such compliance is particularly critical given that the Code is underpinned by the remedies under the TPA. Those remedies include injunctions (s 80), corrective advertising (s 80A), damages (s 82), and the possibility of other orders (s 87). Significantly, a person (such as an adviser or associate of the franchisor) who is found to be involved in a contravention of the Code may also be subject to the remedies under the Act (s 75B(1)).

Although these remedies can be pursued through private action, it is generally expected that the Australian Competition and Consumer Commission (ACCC) will take primary responsibility for enforcement. The ACCC will also be able to secure compliance with the Code through representative actions under the s 87(1A) and (1B) TPA or by seeking enforceable undertakings from franchisors under s 87B.

Mandatory code as industry best practice

While compliance with the Code is now mandatory, general industry support is crucial to the evolution of the Code. After all, the Code represents an opportunity to identify and express industry best practice in a manner that can be adopted by all industry participants. Thus, although minds will always differ on the particular wording, it is important that the Code is allowed to evolve so as to adapt to changing circumstances. This evolutionary process offers a clear alternative to both a voluntary code and franchising legislation, particularly given that a mandatory Code can be used as a vehicle for formulating industry-wide standards.

Needless to say, there should always be scope to refine or modify the present Code for the purpose of raising industry standards or providing for appropriate flexibility in the Code's application. Indeed, the focus should be on formulating the best possible Code in the circumstances, rather than introducing unnecessary complications or merely focusing on drafting nuances (other than the need to ensure that the Code is drafted in plain English).

KEY ASPECTS

The Code – given legal effect through The Trade Practices (Industry Codes – Franchising) Regulations 1998 – is made up of four parts and two annexures dealing with the content of disclosure documents required under the Code. The four parts cover preliminary issues, disclosure, conditions of the franchise agreement and dispute resolution.

Preliminary issues

This Part of the Code deals with the all-important issue of the Code's application. Having set out a definition of "franchise agreement" and having qualified that definition with an inclusion and various exclusions, Part 1 draws a distinction between pre and post 1 October 1998 franchise agreements. While the Code is fully operational in relation to franchise agreements entered into, transferred, renewed or extended on or after 1 October 1998, some provisions will not operate in relation to pre 1 October 1998 agreements. These provisions impact on the content of a franchise agreement and have been excluded to ensure that the Code does not operate retrospectively.

Disclosure

The issue of disclosure is undoubtedly central to the Code's operation. Given that the Code imposes extensive disclosure obligations on franchisors, it is not surprising to find that this is one of the more controversial aspects of the Code.

Since compliance with the Code's disclosure requirements comes at a cost, there is concern that potential franchisors will be discouraged from pursuing a franchising strategy or that existing franchisors will scale down or cease their franchising activities. While such concerns will ensure that the disclosure obligations will be carefully examined as part of the proposed review of the Code, it is important that any concerns with compliance costs are weighed against the potential benefits of improved disclosure.

Conditions of agreement

Part 3 of the Code imposes a number of additional obligations concerning the operation of the franchise agreement. The Code deals with such issues as the provision of a cooling off period, the disclosure of materially relevant facts by the franchisor, the circumstances in which a franchisor can withhold consent to a transfer or terminate an agreement. These additional obligations are wide-ranging and clearly aim to modify the manner in which a franchisor behaves towards its franchisees. While a franchisor's freedom of action will be restrained in some significant areas, this is justified on the basis that such restraint can prevent abuses of power by franchisors.

These additional obligations imposed under Part 3 of the Code aim to protect franchisees in a number of areas highlighted by the Federal Parliamentary Report into Fair Trading (*Finding a Balance: Towards Fair Trading in Australia*, Report by House of Representatives Standing Committee on Industry, Science and Technology, AGPS, May 1997, at 83-120).

As the franchising sector matures and standards of conduct rise, it will be appropriate to review the need for the additional obligations under Part 3 of the Code. Alternatively, circumstances may require the imposition of further obligations under the Code. Either way, it is important that a franchisor's control over the system is not undermined and that any restriction on a franchisor's freedom of action can be justified by proven abuses by franchisors.

Dispute resolution

The provision of a low cost, effective dispute resolution process is another key objective of the Code. With concerns that litigation is costly and not conducive to the preservation of the franchising relationship, the Federal Government has been anxious to provide franchising participants with an alternative dispute resolution framework.

In doing so, the government has not only attempted to provide a simple procedure for the parties to follow in the event of a dispute, but it has also emphasised the use of mediation for the resolution of franchising disputes. Indeed, although the parties are able to decide the method by which they will resolve a dispute, a failure to agree on such a method will mean that either party can refer the matter to a mediator. More importantly, where the parties cannot agree on a mediator, the parties can approach the government-appointed mediation adviser to select a suitable mediator.

Such emphasis on the use of mediation for the resolution of franchising disputes is undoubtedly a positive step towards keeping the channels of communications open between franchisors and franchisees. All too often, resolution of franchising disputes is stifled by the parties immediately taking an adversarial stance towards one another, rather than maintaining a dialogue.

Of course, the scope for binding resolution processes should not be overlooked, particularly given both the likelihood that mediation will not resolve all disputes and the need to pursue legal action in some circumstances.

DEFINITIONAL ISSUES

"Franchise"

Of the various controversial aspects of the new Code, it comes as no surprise to find that the definition of "franchise agreement" has been under the spotlight from the very beginning of the Code's development. Indeed, given that this definition is central to the application of the Code, considerable attention has been focused on ensuring that the definition does not stray beyond what are seen as the traditional boundaries of franchising in Australia.

Unfortunately, trying to determine the boundaries of franchising is, in many cases, easier said than done. Given that franchising is a dynamic and innovative way of doing business, it is inevitable that the boundaries of franchising will always be in a state of change or evolution. Thus, trying to identify the precise boundaries at any point of time will be a matter of conjecture and subject to controversy.

Furthermore, the concept of franchising may vary from industry to industry. While the basic aspects of franchising will always be found, it is common for unique aspects to emerge in different industries. Thus, there is an obvious danger in using a single Code to deal with what may be slightly different forms of franchising or to deal with specific problems that have emerged with franchising activities in different industries.

Would it be more appropriate to develop separate Codes to deal with problematic industries? Since the Code is generic, there may be scope for developing totally separate codes for different industries. Once a separate code has been formulated for a particular industry, the mandatory Code could cease to apply to that industry.

Similarly, while a generic code, such as the current mandatory Code, could be used to deal with such things as general franchising conduct issues, basic dispute resolution processes and minimum levels of disclosure, there may be scope for developing further codes to deal with specific industry issues or problems.

Given that the issue of definition is tied to the intended coverage of a particular code, the controversy associated with the present Code could be minimised if separate codes were developed for particular industries in which the use of franchising has raised concerns.

"Franchise agreement"

The definition of "franchise agreement" is intended to ensure that the Code covers the diverse range of relationships perceived to constitute franchising in Australia. As a generic Code, it is not surprising that a broad definition has been adopted. That definition provides the starting point for determining the application of the new Code. Importantly, the definition has been modified by a specific inclusion and a number of specific exclusions.

As with the rest of the Code, the definition of franchise agreement should evolve over time to ensure the continued relevance of the Code. Indeed, given its present width there is some scope for fine-tuning the current definition during the proposed review of the Code. This is particularly the case if a decision was made to develop separate codes to deal with franchising issues in specific industries.

Before turning to consider possible modifications to the Code's definition of "franchise agreement", it is important to assess the impact of the current definition as found in cl 4(1) of the Code. That definition provides that:

> A franchise agreement is an agreement:
>
> (a) that takes the form, in whole or part, of any of the following:
>
> (i) a written agreement;
>
> (ii) an oral agreement;
>
> (iii) an implied agreement; and
>
> (b) in which a person (the franchisor) grants to another person (the franchisee) the right to carry on the business of offering, supplying or distributing goods or services in Australia under a system or marketing plan substantially determined, controlled or suggested by the franchisor or an associate of the franchisor; and

(c) under which the operation of the business will be substantially or materially associated with a trade mark, advertising or a commercial symbol:
  (i) owned, used or licensed by the franchisor or an associate of the franchisor; or
  (ii) specified by the franchisor or an associate of the franchisor; and

(d) under which, before starting business or continuing the business, the franchisee must pay or agree to pay to the franchisor or an associate of the franchisor an amount including, for example:
  (i) an initial capital investment fee; or
  (ii) a payment for goods or services; or
  (iii) a fee based on a percentage of gross or net income whether or not called a royalty or franchise service fee; or
  (iv) a training fee or training school fee;

  but excluding:
  (v) payment for goods or services at or below their wholesale price; or
  (vi) repayment by the franchisee of a loan from the franchisor; or
  (vii) payment for the wholesale price of goods taken on consignment; or
  (viii) payment of market value for purchase or lease of real property, fixtures, equipment or supplies needed to start business or to continue business under the franchise agreement.

Although this definition focuses on the traditional features of a business format franchise, the definition raises a number of issues as to how far the definition extends. To begin with, the question arises as to when a system or marketing plan is substantially determined, controlled or suggested by the franchisor. Will a party be considered to be a franchisor simply because it provides technical advice to another person on how to market just one of the products distributed by that other person? Since franchising can involve either the commitment to a total business format or the addition of a product range that complements an existing business, it is important to identify the point at which a mere distributor agreement becomes a franchise agreement.

Another set of issues relates to the payment of an amount of money by the "franchisee". Since the payment of an amount of money is an aspect of the definition of a franchise agreement, it is again important to determine point at which the payment of a fee or an amount of money turns a mere distributor relationship into a franchise agreement. While the definition of franchise agreement will cover traditional franchising arrangements involving the payment of an initial franchise fee and/or the ongoing payment of a percentage of the franchisee's turnover or sales, the question arises as to whether the definition extends to an arrangement in which only a training fee is payable or the only amount payable relates to the purchase of goods or services.

A case by case assessment will thus need to be made of whether or not a particular arrangement comes within the scope of the Code. In doing so, it will also be necessary to consider how the application of the Code has been modified by a specific inclusion and various exclusions.

Exclusions

Motor vehicle dealerships

A specific inclusion relates to motor vehicle dealership agreements (cl 4(2)(b)). While such agreements have been specifically included because of the findings of the report into Fair Trading, it is arguably more appropriate for such agreements to be dealt with under their own Code. Where motor vehicle dealer agreements are to remain within the scope of the Franchising Code, it may be appropriate to include a definition of such agreements.

Specified excluded relationships

The following recognised legal relationships will not in themselves constitute a franchise agreement:

- an employer and employee relationship;
- a partnership relationship;
- a landlord and tenant relationship;
- a mortgagor and mortgagee relationship;
- a lender and borrower relationship;
- the relationship between the members of a cooperative that is registered, incorporated or formed under a relevant Australian State or Territory law.

While such relationships may be found within a franchising arrangement or system, it is clear that the mere existence of such relationships will not give rise to a franchise agreement for the purposes of the Code.

Non-resident franchisors

The Code does not apply to a franchise agreement in circumstances where the franchisor (i) is not a resident, domiciled or incorporated in Australia; and, (ii) decides to grant only one franchise or master franchise to be operated within Australia (cl 5(3)(a)).

Other mandatory codes

To prevent overlap between different industry codes, the Code will not apply to a franchise agreement covered by another mandatory industry code prescribed under the TPA (cl 5(3)(b)). A mandatory code dealing with petroleum franchises is expected during 1999.

Fractional franchises

The Code does not apply to a franchise agreement that:

- relates to goods or services that are substantially the same as those supplied by the franchisee for at least two years immediately prior to entering into the agreement; and
- the sales of goods or services under the proposed franchise will not provide more than 20 per cent of the franchisee's gross turnover for goods or services of that kind during the first year of the franchise agreement (cl 5(3)(c)).

The exclusion will cease to apply if the franchisor is notified by the franchisee that sales of the goods or services under the franchise have provided more than 20 per cent of the franchisee's gross turnover for goods or services of that kind for three consecutive years.

While this exclusion attempts to deal with the situation where the franchisee is in a much better position to appreciate the risks associated with the franchise agreement, the exclusion is likely to be difficult to apply in practice. Clearly, this issue may need to be revisited during the proposed review of the Code.

Scope for reform

Given that breaches of the Code constitute breaches of the TPA, it is critical that any definitional issues are clarified. This may require the inclusion of additional definitions, dealing with exemptions and re-evaluating the scope of the present Code, particularly at the margins.

Twenty per cent exemption threshold

Potential difficulties with determining whether or not there is a franchise agreement could be dealt with by providing a minimum threshold below which a franchise agreement will not be covered by the Code. That threshold could ensure that a "franchise agreement" will only cover the granting of right to distribute goods or services constituting more than twenty per cent of the franchisee's sales.

Such a general exemption would operate to exclude those agreements where the level of control by one party is relatively small when compared with the overall business activities of the other party. In doing so, the level of protection offered by the Code can be commensurate with the level of control exerted by one party over another party or the level of involvement between the parties.

Exemption power

Consideration could be given to including a general exemption power under which the relevant government minister or the ACCC could assess an application for exemption from the Code. Such an application could be required to meet stringent criteria and could be subject to a user fee aimed at providing the additional resources needed to consider such applications.

Separate codes

Since definitional issues may arise because of an attempt to cover a range of diverse franchising relationships, it may be appropriate to consider developing separate codes to cater for nuances in franchising arrangements. In particular, codes may be developed for business format franchises, petroleum franchises, service based franchises and motor vehicle dealerships. The definitions in a particular code can be tightly focused to deal with the chosen form of franchising arrangement.

Needless to say, care must be taken to ensure that the development of separate codes does not lead to an unnecessary proliferation of industry Codes. Accordingly, additional codes will need to be justified on a case by case basis.

DISCLOSURE REQUIREMENTS

Part 2 of the Code outlines the franchisor's disclosure obligations. Central to these is the requirement for the franchisor to provide a disclosure document to a prospective franchisee or a franchisee proposing to renew a franchisee (cl 6(1)). That disclosure document, which is to be updated annually within three months after the end of the franchisor's financial year (cl 9(3)), is to be in the form specified by Annexure 1 of the Code (cl 7).

Annexure 1 of the Code requires the disclosure document to include the following information:

- franchisor details;
- business experience;
- litigation details;
- payments to agents;
- details concerning existing franchises;
- intellectual property details;
- franchise territory;
- details regarding the supply of goods or services to franchisees;
- details regarding the supply of goods or services by franchisees;
- site selection policy;
- details regarding marketing and other cooperative funds;
- prepayment details;
- financing details;
- franchisor obligations;
- franchisee obligations;
- summary of other conditions of agreement;
- details regarding any obligation to sign related agreements;
- details regarding any earning information provided;
- financial details; and
- other relevant disclosure information.

The disclosure document, together with a copy of the Code, is to be provided to the prospective franchisee at least 14 days before entering into the franchise agreement or paying a non-refundable amount in connection with the proposed franchise agreement (cl 10). Similarly, a franchisor is required to give the disclosure document and a copy of the Code to a existing franchisee at least 14 days before the renewal or extension of the franchise agreement.

Importantly, the franchisor must not enter into, renew or extend a franchise agreement unless the franchisor obtains a written statement to the effect that the franchisee or prospective franchisee has received, read and had a reasonable opportunity to understand both the disclosure document and the Code (cl 11(1)).

Where a franchise agreement is being entered into, a franchisor is also required to obtain a signed statement from a prospective franchisee to the effect that advice has been received regarding the proposed franchise agreement from an independent legal adviser, business adviser and/or accountant (cl 11(2)(a)). Alternatively, if a prospective franchisee does not seek independent advice, a franchisor is to obtain a statement that while the prospective franchisee has been told to seek independent advice, the franchisee has declined to do so (cl 11(2)(b)).

A franchisor proposing to grant a master franchise will also need to provide a prospective subfranchisor with a disclosure document (cl 6(5)), with the exception already noted in relation to a non-resident franchisor who grants only one master franchise.

Where a subfranchisor proposes to grant a subfranchise, the franchisor and subfranchisor will need to either individually provide a disclosure document or give a joint disclosure document which deals with the respective obligations of the franchisor and the subfranchisor (cl 6(4)). For the sake of clarity, the Code requires the subfranchisor to comply with the franchisor's disclosure obligations (cl 6(4)(b)).

A final aspect relates to the need for a party seeking to transfer a franchised business to provide the proposed transferee with a disclosure document in the form set out in Annexure 2 of the Code (cl 6(2)).

Policy arguments

From the outset, there is a tension between providing sufficient disclosure to franchisees and ensuring that the cost of providing that disclosure does not overwhelm potential or existing franchisors. Accordingly, the cost of disclosing essential information to franchisees in a timely and uniform manner needs to be considered against the potential benefits associated with franchisees being fully aware of their rights and obligations under the franchise agreement.

Inevitably, minds will differ as to whether the cost of disclosure under the Code is justifiable. While there are concerns that the level of disclosure required under the Code comes at a significant cost to franchisors, such concerns need to be considered against the benefits associated with a uniform level of disclosure throughout the sector.

In particular, since the Code requires all franchisors to comply with the same disclosure requirements, the Code creates a level playing field that is of benefit to the franchising sector as a whole. Thus, while good franchisors have always provided an appropriate level of disclosure, the Code will now ensure that the standards of franchisor disclosure are consistent at all levels of the franchising sector.

Cost of disclosure

Given that good franchisors have always provided prospective franchisees with considerable information about the operation of the franchise system, it is readily apparent that such franchisors have viewed disclosure as a legitimate cost of operating a successful franchise system. Indeed, good franchisors see comprehensive disclosure as an excellent marketing tool. Such disclosure not only demonstrates that the system is a proven one, but it also reveals the franchisor is confident in the long-term viability of the system.

Similarly, comprehensive disclosure will ensure that a prospective franchisee will see the benefit of joining the particular franchise system as opposed to another system in which the franchisor is less forthcoming about disclosure. This is particularly the case where the franchisee is parting with life savings in order to enter the franchise system.

By attracting well informed franchisees, good franchisors can minimise the risk of disputation and promote the continued success of the franchise system. Importantly, the process of collecting information for disclosure purposes can also be used by the franchisor for planning and system development purposes and may provide an early warning system in relation to emerging concerns within the franchise system.

CONDITIONS OF AGREEMENT

The Code imposes a number of conditions which impact on the formation, operation and termination of franchise agreements.

Cooling off period

A franchisee is now given the benefit of a cooling off period of seven days from the earlier of the date on which the agreement is entered into or money is paid under the agreement (cl 13). If the agreement is terminated within the cooling off period, the franchisee is entitled to be repaid all money paid under the franchise agreement less any reasonable expenses allowed for under the agreement.

Copy of the lease

Any franchisee that leases premises from the franchisor or an associate of the franchisor is to be provided with a copy of the lease or agreement to lease within one month of it being signed by the parties (cl 14).

Freedom of association

A franchisor is not to prevent its franchisees from associating with each other for a lawful purpose (cl 15).

Prohibition on general release

A franchisor cannot, as part of a franchise agreement entered into, transferred, renewed or extended on or after 1 October 1998, seek a general release from liability towards the franchisee (cl 16). This prohibition, however, does not prevent the franchisee from settling a claim against the franchisor once they have entered into the franchise agreement.

Marketing funds

Where a franchisee is required to pay money into a marketing or other cooperative fund, the franchisor must prepare a annual financial statement for the fund and organise for the statement to be audited by a registered company auditor (cl 17). Interestingly, the auditing requirement can be waived if 75 per cent of Australian franchisees agree to such a waiver.

Materially relevant facts

The Code also imposes a limited form of continuous disclosure on franchisors. In particular, a franchisor is required to disclose a number of specified matters that may not be mentioned in the franchisor's current disclosure document (cl 18). While the various matters would ordinarily be disclosed when the franchisor updates its disclosure document, the Code obliges the franchisor to inform a franchisee or a prospective franchisee within 60 days of the occurrence of such matters as:

- a change in majority ownership or control of the franchisor;
- proceedings by a public agency, a judgment in criminal or civil proceedings or an award in an arbitration against the franchisor in Australia involving a breach of a franchise agreement, a contravention of trade practices law or Corporations Law, unconscionable conduct, misconduct or an offence of dishonesty;
- a judgment against the franchisor under specific Australian legislation dealing with unconscionable conduct;
- civil proceedings in Australia against the franchisor by ten per cent or ten of the Australian franchisees (whichever is the lower);
- any judgment against the franchisor for an amount greater than the specified amount that is not discharged within 28 days;
- the franchisor or director of the franchisor being convicted of a serious offence; and
- the franchisor becoming an externally-administered body corporate.

Disclosure document

A franchisee wishing to obtain a copy of the franchisor's current disclosure document can do so once a year by writing to the franchisor (cl 19).

Franchisor's consent for transfer

Where a franchise agreement provides that a franchisee is to obtain the franchisor's consent for a transfer of the business, the franchisor must not unreasonably withhold that consent (cl 20). The Code provides a list of circumstances in which it will be considered reasonable for a franchisor to withhold consent. These circumstances include:

- the proposed transferee is unlikely to be able to meet the financial obligations under the franchise agreement;

- the proposed transferee does not meet a reasonable requirement of the franchise agreement regarding the transfer of the franchise;
- the proposed transferee does not meet the franchisor's selection criteria;
- the transfer will have a significantly adverse effect on the franchise system;
- the transferor has not complied with its obligation under the Code to provide a disclosure document to the proposed transferee;
- the proposed transferee does not agree to comply with the obligations of the franchisee under the franchise agreement;
- the transferor has not dealt with any outstanding amounts owed to the franchisor; and
- the transferor continues to be in breach of the franchise agreement.

The franchisor has 42 days in which to consider the written request for consent. During that time the franchisor may give the franchisee a written notice that consent is being withheld and provide reasons for the withholding of consent. Where the franchisor does not give such a notice in the required time, the franchisor is taken to have consented to the transfer.

Termination

The Code provides for three scenarios in relation to the termination of a franchise agreement:

- where there is a breach of the franchise agreement:

  In the absence of special circumstances as defined in the Code, a franchisor wishing to terminate a franchise agreement for a breach of its terms must:
  - give reasonable notice of the proposed termination;
  - indicate what is required to remedy the breach; and
  - must allow a reasonable time to remedy the breach.

  If the franchisee remedies the breach, the franchisor cannot terminate the franchise agreement because of that breach. A franchisor does not have to give the franchisee more than 30 days in which to remedy the breach and any dispute can be dealt with in accordance with the Code's dispute resolution provisions.
- where there is no breach of the franchise agreement:

  In the absence of both special circumstances as defined in the Code and the consent of the franchisee, a franchisor wishing to terminate a franchise agreement before it expires must give reasonable written notice of the termination and reasons for it to the franchisee. Any dispute under this scenario can also be dealt with under the Code's dispute resolution provisions.
- a set of special circumstances in which a franchisor does not have to comply with the Code's requirements in relation to termination:
  - the franchisee no longer holding a licence that is required to carry on the franchised business;
  - the franchisee becoming bankrupt or insolvent;
  - the franchisee voluntarily abandoning the franchised business;
  - the franchisee being convicted of a serious offence;
  - the franchisee operating the franchised business in a dangerous manner; and
  - the franchisee being fraudulent in connection with the franchised business.

Scope for reform

In view of the potentially wide-ranging impact of Part 3 of the Code, it is essential that the conditions introduced by that Part are justified in dealing with recognised concerns within the franchising sector. In doing so, however, those conditions must be responsive to a franchisor's need to maintain the integrity and standards of the franchise system.

Need for a cooling-off period?

Given that there will often be a significant period of time between the first meeting between a franchisor and prospective franchisee and the signing of the franchise agreement, the question arises as to the need for or the purpose served by a seven day cooling off period. A thorough review of both the franchise agreement and the franchisor's disclosure document before the agreement is signed, together with the substantial investment required of franchisees, should ensure that the cooling off period will only be utilised in limited circumstances, if at all.

Marketing funds

While the Code requires that the annual financial statements of a marketing fund are to be audited, there is no requirement as to either the use to which the funds in a marketing fund can be put or the involvement of franchisees (or other contributors) in the management of the fund. Where such issues are not dealt with under the franchise agreement or in suitable manner within the franchise system, there may be some scope for the Code to remove any uncertainty as to use of marketing funds and the respective roles of the franchisor and franchisees in the administration of the fund.

Termination

While the termination provisions are aimed at preventing abuses of a franchisor's ability to terminate the franchise agreement, it is clear that a franchisor should be allowed to protect the integrity of the franchise system by dealing with franchisees who fail to adhere to the requirements of the system. After all, a rogue franchisee can do substantial damage to not only the system, but also to the operations of other franchisees.

Accordingly, there is scope for expanding the list of special circumstances under which a franchisor can terminate the franchise agreement without complying with the Code's requirements on the issue of termination. In particular, the list could include other circumstances in which a breach by the franchisee cannot be remedied or irreparable damage is done to the system. Such an expanded list could include the disclosure of confidential system information contrary to the terms of the franchise agreement.

DISPUTE RESOLUTION

Under the Code's dispute resolution framework, a franchise agreement entered into, transferred, renewed or extended on or after 1 October 1998 will need to include an "internal complaint handling procedure" that complies with the procedure set out in the Code (cl 26). That procedure sets out a series of steps to be followed by the disputing parties and culminates in the use of mediation. Since the parties are contractually bound to follow the internal complaint handling procedure, the Code operates to make mediation of franchising disputes mandatory for post 1 October 1998 franchise agreements.

While other franchise agreements do not need to be varied to include a complaint handling procedure that complies with the Code, a party to such an agreement can, in the event of a dispute, use the procedure set out in the Code (cl 27). Interestingly, a party in dispute is given the ability to choose to use either the internal or Code complaint handling procedure (cl 28).

Procedure under the code

The dispute resolution procedure is initiated by a party informing the other party in writing about the nature of the dispute, the desired outcome and what it may take to resolve the dispute (cl 29(1)). This written notice should assist in identifying the scope of the dispute and the action required to settle the dispute. In doing so, the attention of the parties can be focused on specific issues rather than general complaints. Indeed, the notice is important in airing specific issues and guiding the parties on how those issues can be resolved.

The written notice is only a starting point and should not be interpreted in a legalistic fashion. Once the written notice is given, the parties should attempt to reach an agreement on how to resolve the dispute (cl 29(2)). This will involve the parties to agree on the particular dispute resolution process to be followed.

Where the parties cannot agree on an appropriate dispute resolution process within three weeks, either party is able to refer the matter to a mediator (cl 29(3)). If, however, the parties cannot agree on a suitable mediator, then either party can request that the government-appointed mediation adviser choose a mediator (cl 29(3)). The mediation adviser has 14 days in which to appoint a mediator (cl 30).

The parties are required to attend the mediation and attempt to resolve the dispute (cl 29(6)). While the parties obviously cannot be compelled to come to an agreement, the mediation process is clearly aimed at getting the parties talking to one another. Nevertheless, mediation under the Code does not affect the right of the parties to take legal proceedings under the franchise agreement (cl 31(1)).

The mediator may decide the time and place for mediation (cl 29(5)). The Code also provides that the parties must pay for their own costs of attending the mediation and that, unless otherwise agreed, the parties are equally liable for the costs of mediation (cl 31). Any other procedural aspects, such as the confidentially of the mediation process, will need to be dealt with in the franchise agreement or in some other contractual manner.

Policy considerations

Given that litigation is both costly and not conducive to the preservation of long-term relationships, there is a clear justification for exploring the use of alternative dispute resolution techniques for resolving franchising disputes. Indeed, in view of the long-term nature of franchising relationships, it is critical that every opportunity is taken not only in minimising the level of disputation, but also in dealing with any disputes in a timely and mutually satisfactory manner.

Clearly, mediation and other forms of alternative dispute resolution have a key role to play in the franchising sector. Such approaches to dispute resolution promote ongoing communication between the parties, a feature that is integral to a successful long-term franchising relationship.

Of course, there will be circumstances in which alternative dispute resolution techniques fail to resolve the dispute. In such circumstances, thought will need to be given to providing binding resolution mechanisms which are user-friendly and cost effective. Such mechanisms, when used to supplement other dispute resolution processes, will ensure that fewer disputes are dealt with through the costly and, potentially, destructive litigation process.

Role of mediation adviser

The provision for the minister to appoint a mediation adviser for the purposes of the Code is a unique feature of the Code's dispute resolution framework. Since the mediation adviser is required to choose a mediator where requested by the parties under the Code, the appointment of the mediation adviser will ensure that mediation can occur despite the parties not being able to agree on a suitable mediator.

While the mediation adviser's present role is a fairly limited one, there is significant scope for expanding the adviser's role to one of also assisting the parties in identifying the most appropriate alternative dispute resolution process for the parties. In doing so, the parties could benefit from the experience of the adviser in identifying suitable dispute resolution techniques.

A Franchising Ombudsman/Tribunal?

Although the use of mediation will promote the preservation of the franchising relationship, it is apparent that the success of mediation depends upon the nature of the dispute and the goodwill of the parties involved. Clearly, the emphasis on mediation as an flexible and voluntary means of dispute resolution can be a two-edged sword.

Indeed, although the voluntary nature of the mediation process may be advantageous in producing a mutually beneficial agreement, there is no guarantee that mediation will lead to a resolution of the dispute. After all, the parties in dispute cannot be required to come to an agreement through the mediation process.

Accordingly, mediation will be of limited use where the parties simply cannot reach an agreement on the resolution of the dispute or one of the parties to a dispute simply goes through the required steps without any intention of agreeing to a resolution of the dispute. While it remains to be seen whether mediation can deal with the bulk of franchising disputes, it is important that the Code's dispute resolution procedure remains responsive to the needs of the franchising sector.

Thus, where the mediation process consistently fails or is abused, consideration may need to be given the use of binding dispute resolution processes or the involvement of an independent franchising ombudsman. Of course, concern that the government may implement a binding dispute resolution process should offer clear incentive for franchising participants to act in good faith in undertaking the Code's dispute resolution procedure.

CONCLUSION

Overall, the new Code represents an important initiative by the Federal Government. Having rejected both franchising legislation and reliance on the industry itself in developing a regulatory framework, the Federal Government has pursued a unique approach to dealing with concerns within the franchising sector. While it remains to be seen whether the Code adequately addresses those concerns, it is essential that the Code is allowed to evolve to meet changing industry circumstances. By evolving and continually representing industry best practice, the Code will minimise disputes, discourage potential franchisors and franchisees who are either unprepared for or not suited to franchising, and produce the best possible outcome for the franchising sector as a whole. ❑

STUDENT COMPANION

edited by

Richard Scragg

UPDATES TO YOUR MATERIALS

PUBLIC INTERNATIONAL LAW

Allan Bracegirdle

Kumar v Minister of Immigration (High Court, Auckland, M 184/99, 16 February and 25 March 1999, Randerson J)

P v Minister of Immigration (High Court, Auckland, CP 178/97, 30 April 1999, Randerson J)

These two cases are part of a series in recent years in which the Courts have considered the application of international treaties in proceedings for judicial review, particularly, as here, in the area of immigration. Both decisions, one of interim relief, were largely founded upon the International Covenant on Civil and Political Rights (ICCPR) and the Convention on the Rights of the Child in requiring the Minister to give full consideration to those instruments and in the judgments made about the purport and application of the treaty obligations. In *Kumar*, arts 2(3), 17, 23 and 24 of ICCPR, and arts 3(1), 8, 9 and 16 of the Child Convention, were applied. In *P's case*, art 23 of ICCPR and arts 3(1) and 9 of the Child Convention were applied (reference was also made to the Hague Convention on Child Abduction, which is implemented in a specific manner in NZ law). The two treaties were applied directly, with very little linkage, or even reference, to any statutory provisions.

It seems that NZ became party to the two treaties on the basis that they did not apply directly in NZ law. They are not to be found in NZ statute law. In NZ law there are various statutory provisions that, along with administrative processes as well as the common law, enabled NZ to give effect to ICCPR (the New Zealand Bill of Rights Act 1990 refers to ICCPR but does not incorporate it into NZ law), and a host of statutes and administrative practices relied upon for the domestic legal implementation of the Child Convention. Very few treaties, to which NZ is party, that impose prohibitions or obligations that require implementation to some extent or other in NZ law, are implemented in terms. Nothing in international law requires that as a matter of course. It is due to the fact that they are nevertheless implemented in various other ways that NZ is able to become party to them. The treaties apply between NZ and the other states at international law. In NZ law, it is the implementing legislation that applies. Perhaps NZ might have gone about implementation in quite a different way, or might have chosen not to become party to the treaties, if they were to apply directly. As it was, NZ entered reservations to both ICCPR and the Child Convention upon ratification, including a broad immigration-related reservation in the latter case. The genesis of the present cases, as with most of the recent series of cases, is *Tavita v Minister of Immigration* [1994] 2 NZLR 257 (CA). Too much may be made of that case which was an interim judgment. The case merely suggested that international obligations may found mandatory relevant considerations. On its facts, the case was a riposte to a point made by the Crown that decision makers could ignore the international instruments. The Court (and the Crown) ought to be assumed to have been aware that NZ is accountable for breaches of treaties to which it is party, but at international law (to the other states parties with whom it has contracted) and not domestic law, and that looking for the international obligations in domestic law in terms will generally be unsuccessful since NZ rarely finds it necessary to proceed in that manner but will have implemented or given effect to treaty obligations in NZ law, where required, in various other ways. *Tavita* was simply recognising that NZ law in this area could develop further. To date, no such development has taken place.

EQUITY

Charles Rickett

Fairness

O'Neill v Phillips (House of Lords, 20 May 1999)

This case concerned the application of a statutory "unfairly prejudicial" jurisdiction in a company law matrix. Lord Hoffmann, in a speech concurred in by his brethren, made comments of fundamental importance about appeals to "fairness". Although fairness was chosen by Parliament as the criterion in order "to free the Court from technical considerations of legal right and to confer a wide power to do what appeared to be just and equitable" (which some today see as the role of equity), "this does not mean that the Court can do whatever the individual Judge happens to think fair. The concept of fairness must be applied judicially and the content which it is given by the Courts must be based upon rational principles". There were "tolerably well settled" equitable principles upon which the exercise of the "unfairly prejudicial" jurisdiction could be ascertained and exercised. It was not necessary "to abandon [those principles] in favour of some wholly indefinite notion of fairness". In particular:

"19th century English law, with its division between law and equity, traditionally took the view that while literal meanings might prevail in a Court of Law, equity could give effect to what it considered to have been the true intentions of the parties by preventing or restraining the exercise of legal rights". This approach – "a product of English legal history" – survived the amalgamation of the common law and equity Courts. Another approach would be to soften the literal view and adopt a general meaning view. A third approach might be to introduce "a general requirement of good faith into contractual performance".

Lord Hoffmann preferred to apply the first approach, not because it was inherently better, but because "a new and unfamiliar approach could only cause uncertainty". Further, that approach also referred to "conscience", which reflected "the ecclesiastical origins of the long-departed Court of Chancery".

Charitable Purposes

Vancouver Society of Immigrant and Visible Minority Women v Minister of National Revenue [1999] SCR 10

This decision of the Supreme Court of Canada contains excellent discussions in both the majority and minority judgments of the steps to be taken in assessing whether a purpose falls within the concept of charitable purposes and, in particular, the fourth head of Lord Macnaghten's fourfold classification in *Commissioners for Special Purposes of the Income Tax v Pemsel* [1891] AC 531 (HL) (other purposes beneficial to the community).

Controlling the Exercise of a Trustee's Discretion

Blair v Vallely and Blair (High Court, Wanganui, CP 8/98, 23 April 1999, Wild J)

A family trust contained a provision requiring distribution of the fund to all beneficiaries in equal shares on 30 April 1999. There was a power in the trustees to pay income or capital to any one or more of the beneficiaries before the distribution date. The discretion was an "absolute and uncontrolled discretion". The trustees wished to make a capital distribution prior to the distribution date, "with the aim of treating all beneficiaries equally". Accordingly, they made assessments of direct and indirect benefits already received by the various beneficiaries. One beneficiary, whom the trustees assessed as having received sizeable indirect benefit, and to whom they were therefore going to make a reduced payment, sought an injunction to prevent the trustees proceeding to discretionary distribution. Two points are important. First, "the trustees were content to have the Court examine their reasons for the proposed distribution ...". It is not clear that the Court could have proceeded as it did without that concession. Secondly, although Wild J characterised the trust as "discretionary", the case was shrouded in the notion of "equal" distribution to the existing beneficiaries. In that respect, the discretion of the trustees was severely downplayed.

Wild J stated: "It was common ground that the Court may intervene if it considers trustees have exercised their discretion ultra vires, in bad faith, partially (ie demonstrating a lack of even-handedness between beneficiaries or classes of beneficiaries) or in conflict with their duty to act only in the interests of the beneficiaries, as opposed to their own interests."

Although the proposed distribution was prima facie within the absolute and uncontrolled discretion of the trustees, the doctrine of "ultra vires" was broadened by the introduction of a test of "reasonableness". Wild J cited Tipping J in *Craddock v Crowhen* (1995) 1 NZSC 40,331 (HC) (where the latter had appealed to the administrative law concept of *Wednesbury* unreasonableness), and stated: "[T]he unreasonable exercise of a discretionary power by trustees cannot stand". Good faith involved trustees exercising their discretions with real and genuine consideration, so as to protect and not destroy beneficiaries' rights. Trustees could not act capriciously. Wild J held that in various respects the trustees had acted unreasonably, irrationally, mistakenly and incorrectly.

The decision appears to be consistent with the approach being taken in other jurisdictions. See *Maciejewski v Testra Super Pty Ltd* (1998) 44 NSWLR 601; *Scott v National Trust for Places of Historic Interest or Natural Beauty* [1998] 2 All ER 705 (HC), where Robert Walker J suggested that trustees had to be fair because beneficiaries had legitimate expectations. Like Tipping J, Robert Walker J linked this to administrative law concepts (at p 717): "... I am inclined to think that legitimate expectation may have some part to play in trust law as well as in judicial review cases ...". Here the unreasonableness jurisdiction is largely being asserted in the context of pension fund trusts, which might reasonably be said to have a "public" element in a more obvious way than family trusts. Why then did Wild J seize upon the reasonableness criterion in *Blair*? Was the trust more like a fixed trust than a truly discretionary one, wherein the "discretion" of the trustees was not a "real" discretion, and certainly not one which might deprive a beneficiary of his entitlement? If the reasonableness approach, founded as it is on beneficiaries' entitlements, is to apply to truly discretionary private trusts, it will require a reinterpretation of the "interests" of beneficiaries of discretionary trusts.

Compensation for Breaches of Fiduciary Duty: Causation and Contributory Negligence

Nationwide Building Society v Balmer Radmore and Others (High Court (Eng), 2 February 1999)

Blackburne J was confronted by claims by the plaintiff against a number of firms of solicitors in respect of mortgage loan transactions upon which the plaintiff had suffered losses. The solicitors had acted for both the plaintiff and the borrowers in the various transactions, and the claims were, inter alia, for breaches of fiduciary duties. Since the claims included common law claims, His Lordship outlined what he believed to be the position at common law on causation, whence he drew a distinction between cases of fraud and cases of negligence. Where a defendant acted fraudulently, compensation on a "restitutionary basis" was awarded (subject, perhaps somewhat surprisingly, to limiting principles of causation, remoteness and mitigation). This was a "but for" approach, aimed to put the plaintiff into the position he was in before the defendant did him the wrong. For negligence, liability to compensate was restricted to the consequences of the breach, which depended on defining the scope of the duty broken. This was a "what if" approach, aimed to put the plaintiff in the position he would have been in if the defendant had carried out his duty. Contributory negligence could operate in negligence claims, whence a Court would have regard to "the blameworthiness and causative potency of the parties' respective errors". This analysis of the common law position operated as a backdrop for two issues of particular relevance to the breach of fiduciary duty claims.

First, Blackburne J discussed "whether, assuming causation in the sense of a causal connection between breach and loss has been shown, it is relevant to establish what course of action the [plaintiff] would have followed if the defendant firm had carried out its duty". He stated, "... I take the view that, except where the fiduciary has acted dishonestly or in bad faith (or its equivalent), the correct approach to equitable compensation for breach of fiduciary duty is to assess what actual loss, applying common sense and fairness, has resulted from the breach, having regard to the scope of the duty which was broken .... [N]othing in the authorities compels me to disregard any inference which, on the evidence, can properly be drawn as to what would have happened if the fiduciary had performed his duty. Failing any such evidence, however, the beneficiary is entitled to be placed in the position he was in before the breach occurred. This assumes that he can show that the breach was causally relevant to the course of action which has given rise to his loss in the sense that, but for the breach of duty, the beneficiary would not have acted in the way which has caused his loss".

Thus, an approach similar to that for fraud-based claims at common law is to be applied, but perhaps not quite as flexible because remoteness and mitigation seem irrelevant, save in so far as those matters might arise in effect in the "what would have happened" limitation announced by Blackburne J. An even stricter test will apply if the fiduciary's conduct, in the context of breaching his fiduciary duty of loyalty and fidelity, is dishonest or in bad faith. This is not clear. All breaches of fiduciary duty, involving as they must do disloyalty or infidelity, engage the defendant's conscience. That is one of the justifications for a stringent "but for" test. The "what would have happened" limitation actually seems to be as justified in cases of dishonesty or bad faith, as it is in standard disloyalty/infidelity cases.

Secondly, Blackburne J canvassed what he called "lender fault in equity", or the issue of contributory negligence. He analysed *Day v Mead* [1987] 2 NZLR 443 (CA) and *Canson Enterprises Ltd v Boughton & Co* [1991] 3 SCR 534 (SCC), and concluded:

> I ... take the view that where, in order to establish a breach of fiduciary duty, it is necessary to find that the fiduciary was consciously disloyal to the person to whom his duty was owed, the fiduciary is disabled from asserting that the other contributed, by his own want of care for his own interests, to the loss which he suffered flowing from the breach.

The conduct of the plaintiff might well have a role to play in mitigation or in an exercise of the discretion that accompanies all equitable remedies.

Knowing Receipt Liability

Waddell v Honeybone and Others (High Court, Tauranga, CP 28/95, 20 October 1998, Randerson J)

Dubai Aluminium Co Ltd v Salaam [1999] 1 Lloyd's Rep 415

Bank of Credit and Commerce International (Overseas) Ltd v Akindele (High Court, Chancery Division, 19 November 1998, Carnwath J)

Brown v Bennett (Court of Appeal (Eng), 1 December 1998)

Satnam Investments v Dunlop Heywood & Co Ltd (Court of Appeal (Eng), 31 December 1998)

There is still confusion about the best rationale for knowing receipt liability (see [1999] NZLJ 40). In *Waddell v Honeybone* Randerson J discussed the principles of knowing receipt and dishonest assistance liability. In particular, he stated that whether dishonesty, as defined in and required for assistance liability by *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC), was the test for knowing receipt, was not resolved. However, two recent English High Court authorities contain important dicta supporting the rehabilitation of both knowing receipt and dishonest assistance within a single form of participatory liability. In *Dubai Aluminium Co Ltd v Salaam* Rix J provided a comprehensive account of the state of English law on accessory liability. While drawing some minor distinctions between knowing receipt and dishonest assistance, his entire account was premised upon a fundamental unity between the two. At p 453: "I revert to the principle of knowing receipt. In the light of *Tan* the question arises whether the mental element of 'knowing' is to have the same content in knowing receipt as in what should now be called 'dishonest assistance'. Indeed *Cowan de Groot Properties v Eagle Trust*, which Lord Nicholls had quoted ..., was a case of knowing receipt. Mr Justice Knox's test, approved by Lord Nicholls, of 'commercially disreputable conduct in the particular context involved' comes, in fact, from the obiter part of the former's judgment, in case he was wrong to say, as he preferred, that constructive knowledge would not suffice to render a defendant liable in knowing receipt. It seems to me that in the circumstances, the test in knowing receipt and dishonest assistance is likely to be the same.

> ... In the circumstances [of the present case], very little attention was paid to any separate issues which might otherwise have arisen under the heading of knowing receipt. I have already said that in the light of *Tan* I would regard the test of the mental element involved as being dishonesty in the *Tan* sense. ..."

In *Bank of Credit and Commerce International (Overseas) Ltd v Akindele* a claim by a bank against a customer in both dishonest assistance and knowing receipt, Carnwath J made similar comments. He was not prepared to discount the help that could be gained, in analysing the mental element required for knowing receipt, from the fivefold *Baden* classification. After listing them, he stated: "There remains controversy as to which of these states of mind is sufficient for the purposes of 'knowing receipt'. Before me (counsel) accepted that the 'thrust of the authorities' requires one of the first three categories. ... On that basis, it is doubtful whether the test differs materially in practice from that for 'dishonest assistance'.

....The discussion [about the liability of the defendant, in both knowing receipt and dishonest assistance] ... has concentrated on the ... issue, whether the defendant was a dishonest participant or recipient. (It is convenient to use the single word 'dishonest', while acknowledging the possible differences mentioned in my earlier discussion of the authorities)".

In *Brown v Bennett*, Morritt LJ accepted the statement of Hoffmann LJ (as he then was) in *El Ajou v Dollar Land Holdings plc* [1994] 1 BCLC 464, 478, as "a paradigm example of [knowing receipt's] proper expression": "This is a claim to enforce a constructive trust on the basis of knowing receipt. For this purpose the plaintiff must show, first, a disposal of his assets in breach of fiduciary duty; secondly, the beneficial receipt by the defendant of assets which are traceable as representing the assets of the plaintiff; and thirdly, knowledge on the part of the defendant that he assets he received are traceable to a breach of fiduciary duty".

Morritt LJ confirmed "that the receipt must be the direct consequence of the alleged breach of trust or fiduciary duty of which the recipient is said to have notice". A third party might have notice of a breach of trust, but if his (usually later) receipt of trust property was not linked to that breach, then he could not be liable.

Satnam Investments Ltd v Dunlop Heywood & Co Ltd concerned disclosure of confidential information to a third party, and the subsequent purchase of land by that party. Nourse LJ suggested that the third party could, in theory, be a knowing recipient of information, but there would need to be a sufficient nexus between the information received and the asset over which a constructive trust was sought. Most important is the comment that "[b]efore a case can fall into either category [receipt or assistance] there must be trust property or traceable proceeds of trust property". If this is correct, a mere breach of fiduciary duty unrelated to the misuse of trust or fiduciary property will not found a dishonest assistance claim. *Satnam* is also clear appellate authority for the applicability of the *Tan* dishonesty test for dishonest assistance in English law.

TORTS

Rosemary Tobin

W v Attorney-General (Court of Appeal, CA 239/98, 6 May 1999)

The appellant sought exemplary damages from the Department of Social Welfare for failing to respond to her allegations that the foster father with whom she had been placed had sexually abused her. She applied under s 4(7) Limitation Act 1950 for leave to bring a proceeding. Her claim was based on breach of fiduciary duty and breach of statutory duty. Three questions faced the Court of Appeal:

(i) When did her cause of action accrue for the purposes of the Limitation Act?
(ii) Did she suffer a disability for the purposes of the Limitation Act?
(iii) If leave to proceed was given pursuant to s 4(7) of the Act should that leave be unqualified or without prejudice to the Attorney-General's ability to pursue limitation as an affirmative defence at trial?

The decision is notable for the judgment of Thomas J.

(i) Accrual of the cause of action

In *S v G* [1995] 3 NZLR 681, 687 the Court of Appeal confirmed that where damage was an element of a cause of action the reasonable discoverability of the link between psychological and emotional harm and past sexual abuse could be employed to determine when the cause of action accrued. It was only when psychological damage is or reasonably should have been identified and linked to the abuse that the cause of action accrues. The question was, however, reasonable discoverability by whom, the hypothetical reasonable victim or the actual victim? In the High Court the Judge had interpreted the application of this test as objective, based on the reasonable person in the position of the intended plaintiff.

All three Court of Appeal Judges rejected this approach. Both Tipping and Salmon JJ considered the correct approach was to apply the standard of reasonableness to the intended plaintiff, but in the light of such characteristics, problems and difficulties as affected her. The Judge's task was to bring an objective assessment to the question of the reasonableness of the particular plaintiff's actions. Thomas J also accepted that precedent meant this was the approach to take but he reserved some trenchant criticisms for it.

Thomas J noted that while the reasonable discoverability test worked well in the defective building cases, there were obvious difficulties in attempting to apply it to cases of sexual abuse. The focus was on the victim and to that extent it was a subjective approach, but the cause of action accrues if the link between the psychological damage and the abuse should reasonably have been identified by her. Cases had discussed the reasonable sexual abuse victim but, put simply, the notion of a reasonable sexual abuse victim was "incongruous", and eventually would be perceived as "a grotesque invention of the law". Indeed, whether the Court took the reasonable sexually abused victim in the position of the plaintiff, or took the intended plaintiff as she was, and assessed her behaviour by the yardstick of the reasonable person, was largely semantic. Either way, the test objectified the intended plaintiff's subjective condition by asking whether the intended plaintiff could reasonably have been expected to make the connection between the abuse and the subsequent psychological damage. Yet this was a question which could not be approached objectively; evidence disclosed that the impact on each victim and the reaction of each victim necessarily varied. His Honour said:

"Until such time as Judges are prepared to embrace contemporary knowledge and informed psychological and scientific instruction ahead of strict adherence to the doctrine of precedent or a mechanical application of legal methodology, the judiciary's perception of what is 'reasonable' behaviour for women who are the victims of sexual violation or sexual abuse is likely to remain divorced from reality".

(ii) Disability

As Thomas J noted, in this context the Court was prepared to adopt a more subjective approach. In *T v H* [1995] 3 NZLR 37 Hardie Boys J accepted that a person who, for clearly established psychological reasons, was disabled from instructing a solicitor and commencing proceedings, was under a disability for the purposes of the Limitation Act. He considered, however, that the only circumstances covered by "disability" were limited to infancy and unsoundness of mind. Thomas J, while agreeing that such a person was under a disability, could see no reason why these were the only circumstances covered by the word. Once it was accepted that a woman who is incapable of instructing a solicitor and commencing proceedings is under a disability, that should be enough; it should not be necessary to go further and compress her psychological condition into unsoundness of mind.

(iii) Procedure

The Court confirmed that applications under s 4(7) Limitation Act 1950 are to be determined without prejudice to issues of limitation unless the intended claim is beyond doubt on its face statute barred. It was quite inappropriate in cases of this nature to reach a conclusion on a preliminary application where witnesses had not been heard and cross-examination not taken place.

EMPLOYMENT LAW

Graham Rossiter

Robertson v IHC New Zealand Inc (Employment Court, CC 8/99, 14 April 1999, Judge Palmer)

The Employment Contracts Act 1991 (s 33(2) and cl 3 of the First Schedule) require that a personal grievance be submitted "within the period of 90 days beginning with the date in which the action alleged to amount to a personal grievance occurred or came to the notice of the employee, whichever is the later". If this requirement is not met, either the employer must consent to the personal grievance being submitted out of time (which as a practical matter will, for the obvious reasons, never happen, at least in terms of an express consent) or the Employment Tribunal must grant leave for a late submission on the basis that there are exceptional circumstances and it is "just to do so". (For the case law, see paras 33.2 et seq of *Butterworths Employment Law Guide* (4th ed).)

The Employment Court in *Robertson v IHC* has now issued what is possibly the most significant decision on the 90-day rule since the statute was enacted in 1991. At the heart of this case was the genuineness of the redundancy put forward by the former employer as justification for the applicant's dismissal. The applicant's employment was terminated on the ground of contended redundancy in July 1996. She had been told by the respondent that as a result of significant reorganisation, her position was subject to "major change". In October that year, the applicant became aware of the possibility that the respondent had misrepresented the circumstances of the termination to her. She obtained access to the position description for the newly advertised position and found the specifications for the new position were identical to the former position. A personal grievance was submitted in December 1996.

The effect of the cases to date has substantially been that, apart from the situation of a summary dismissal, the 90-day period will begin to run as from the date of expiry of the notice of termination. On this basis, Ms Robertson would have been well out of time. Judge Palmer, however, resolved the question of law referred to him by the Employment Tribunal in the applicant's favour and held that the personal grievance had been validly submitted.

The Court held that the 90-day period commences on the date on which the affected employee is dismissed in circumstances which the employee is aware comprise an unjustifiable dismissal. In the situation where circumstances later come to the notice of the employee which arguably render the termination unjustifiable, the 90-day period will commence from the date the employee reasonably concludes he or she has been unjustifiably dismissed because of the further information derived. Such an approach necessarily demands an evaluation by the Employment Tribunal of all material facts to determine whether the deferred commencement of the 90-day period has been made out. Judge Palmer was, in his consideration of this use, influenced, in part, by the interpretation that has, in recent years, been given to the Limitation Act 1950 to the effect that in, for example, bodily injury cases, a cause of action accrues when the injury of the kind complained of was discovered or was reasonably discoverable as having been caused by the acts or omissions of the defendant. ❑

PUBLIC WORKS TAKINGS AND TREATY SETTLEMENTS

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calls for a review of the Public Works Act

A number of recent Court cases and other events have drawn attention to the importance of Public Works Act issues for Maori claimants. A thorough review of the Public Works Act 1981 has been called for already in the recommendations of numerous Waitangi Tribunal reports. In this brief article I argue that a review of that Act is now a matter of urgency.

A decision by the Privy Council, *Attorney-General v Horton* (Appeal No 51 of 1998, 8 March 1999, judgment by Lord Hoffman) ([1999] BCL #441; [1999] *Maori Law Review*, March pp 5-7) has sparked the current controversy. The ruling of our highest judicial body was that, as soon as the Crown or a state-owned enterprise comes to the decision that it no longer needs land for a public work, then it must offer the land back to the original owners under s 40 of the Public Works Act. It cannot hold on to the land and later decide that it is needed for a different Crown purpose.

The difficulty for Coal Corp in this case, which concerned land at Ohinewai, was that it felt obliged to take account of the interests represented by the Waikato Tainui claim, then in negotiation with the Crown following the Court of Appeal decision in *Tainui Maori Trust Board v Attorney-General* [1989] 2 NZLR 513. Whilst Coal Corp no longer wanted the land for coal mining, the Crown did still want the land to be available as part of "land for land" settlement. The importance of "land for land" was later acknowledged in the preamble to the Waikato Raupatu Claims Settlement Act 1995 and expressed in both language texts of the preamble as "i riro whenua atu, me hoki whenua mai".

Although the Privy Council decision has been welcomed by some as likely to assist Maori claimants, the decision is certain to reduce the amount of land available for settlement of historic tribal Treaty claims. Until now many claimants have sought an inventory of Crown-owned assets remaining in their region in order to target those lands which the Crown should return to Maori ownership as part of a Treaty claims settlement. What this decision clarifies is that if any of that land was taken for public works, and if the 1981 Act applies, then it will *not* be available for a Treaty settlement unless the previous owner declines the offer back.

Then there is the decision of the Court of Appeal in *Port Gisborne Ltd v Smiler* (Court of Appeal, Richardson P, Gault and Henry JJ, CA 182/98, 26 April 1999, [1999] *Maori Law Review* April pp 5-6) This has been misreported as a "ruling that land taken under the Public Works Act does not have to be offered back to its original owners". ("Land Act ruling knock for Maori", *New Zealand Herald*, 28 April 1999)

That case turned on the facts relating to Crown ownership of the Tauwhareparae Block from 1881 (when it was bought by the Crown from individual Maori) to 1884 (when it was set aside as harbour endowment land for Port Gisborne). The High Court and the Court of Appeal arrived at different conclusions on the evidence of historians concerning the status of "waste lands" of the Crown bought for the general purposes of colonisation in 1881 but not explicitly earmarked for a public works purpose until 1884.

The Appeal Court held that Tauwhareparae was not acquired and held for a public work in 1881. This finding is a plausible interpretation of the formal written record of land transactions. It may be criticised for failing to give appropriate weight to Maori oral history and Pakeha local knowledge as to the purposes of the 1881 acquisition. However, the Court did not disagree with, and indeed it specifically followed, the Privy Council in *Attorney-General v Horton* on the previous owner's right to an offer back *if* land was held for a public work.

Rather more worrying for Maori claimants than the decision itself were the Court of Appeal's obiter dicta on the meaning of "successor" in s 40. The Court favoured the view that the 1981 offer back procedures are usually available only to the original owner and the immediate successor of the original owner. This "one generation" rule would prevent Maori descendants of owners whose land was taken long ago from benefiting from an offer back under the 1981 Act.

Another issue that has arisen for Maori, especially when the compulsory taking was relatively recent, is that the original owners or their immediate successors may still be alive but they may be unable or unwilling to pay the current market price for buying back the taken land. This may also cause problems for Treaty settlements with a tribal entity. A current dispute at Turangi between the whanau of individual owners, whose Maori freehold land was compulsorily taken in the 1960s, and the hapu with whom the Crown has settled, Ngati Turangitukua, highlights the difficult interface between settlement of public works grievances and settlement of tribal lands grievances. This was foreseen by the Waitangi Tribunal in its *Turangi Township Report 1995* (p 323) which found that the offer back provisions of the 1981 Act are inconsistent with Treaty obligations.

WAITANGI TRIBUNAL FINDINGS AND RECOMMENDATIONS

The compulsory taking of land by the Crown from Maori has long been lawful in Acts of Parliament. Yet do the powers of kawanatanga or sovereignty permit this? Does the cession of governance authority include the power to set aside the guarantee of tino rangatiratanga over land by permitting Maori land to be alienated to the Crown without the consent of its right-holders? These issues have been considered in many Tribunal reports: *Manukau Report* 1985; Orakei Report 1987; Mangonui Sewerage Report 1988; Ngati Rangiteaorere Claim Report 1990; Mohaka River Report 1992; Te Maunga Railways Land Report 1994; Ngai Tahu Ancillary Claims Report 1995; Turangi Township Report 1995; Te Whanganui-A-Orotu Remedies Report 1998. The fact that these issues have been the subject of findings and recommendations in so many reports is indicative of how important public works takings are for Maori claimants. This is also made clear in Professor Alan Ward's *National Overview* published by the Waitangi Tribunal. (Ward, *National Overview*, vol II, Wellington, GP Publications, 1997, ch 11)

the Crown does not recognise failure to offer back surplus land prior to 1981 to be a Treaty breach as there was no public works law obligation on the Crown to do so prior to the 1981 Act

The clear position arrived at by the Tribunal is that compulsory acquisition of Maori land interests must be limited to "exceptional circumstances and as a last resort in the national interest". Even then, in the Tribunal's view, the acquisition should be of a leasehold interest or a licence rather than a freehold interest so that, in the event that the public work is no longer required, the land will revert to Maori control without the problems of the offer back procedures and valuations.

CROWN SETTLEMENT POLICY

It is perhaps not well known, as it should be, that in August 1996 the Office of Treaty Settlements published "*The Crown's Policy on Treaty Claims Involving Public Works Acquisitions*". The policy identifies a number of circumstances in which the Crown acknowledges that a well-founded public works grievance may exist where there was a lack of adequate (or any) compensation for taken land or a lack of adequate consultation. These grievances may constitute a breach of the Treaty for which the Crown will offer an apology. The Crown may also offer redress if "significant damage to Maori interests" occurred as a result of such Treaty breaches. There is a list of criteria to assess "significant damage".

This is a very cautious policy. Moreover, the Crown does *not* recognise failure to offer back surplus land prior to 1981 to be a Treaty breach as there was no public works law obligation on the Crown to do so prior to the 1981 Act. A 1997 amendment to this policy did recognise the possibility of a Treaty breach if there was a failure to use a statutory discretion in other Acts (in Maori Affairs legislation, for example) to offer taken Maori land back to former owners.

The obvious point for claimants is that any redress through negotiations with the Office of Treaty Settlements would have to fit within the constraints of the overall Treaty settlement envelope. Thus public works grievances would be lumped into an overall package along with confiscation, early Crown purchases, failure to return gifted lands and the Native Land Acts in a comprehensive "full and final" settlement of historical tribal grievances. Redress under Treaty settlement policy is really about "truth and reconciliation". It does not attempt to pay reparations or full restitution. "Land for land" in Treaty settlements can only be a remedy for a tiny proportion of the area of land lost contrary to Treaty guarantees. Thus claimants will remain vitally interested in the prospect of other land being returned to them under Public Works legislation.

A REVIEW OF THE PUBLIC WORKS ACT

The final paragraph of the Office of Treaty Settlements' policy in 1996 noted that the Waitangi Tribunal had recommended a review of the Public Works Act 1981. The Crown's view of changes required to the Act would be considered, it was said, "over the next 4-5 months". It is now nearly three years later. This article has been written to draw the government's attention to the need to complete its internal review and to consult with all interested parties. Among the issues which might be considered are:

- The desirability of a general policy to protect the tiny fragments of land that are still Maori-owned by avoiding any compulsory acquisition of Maori land interests;
- Whether the Tribunal's test of "exceptional circumstances and as a last resort in the national interest" would be an appropriate test as an exception to the proposed general policy; or whether there should be no exceptions;
- If there are exceptions, whether they should be restricted to the Crown acquiring only a lease or a licence – thus leaving the underlying title in Maori ownership with resulting return of control to Maori immediately the public work purpose ceases;
- The inclusion of a requirement in the Act that it shall be interpreted so as to give effect to the Treaty of Waitangi and its principles – rather than the lesser requirement of merely "taking account of" Treaty principles;
- A review of the "one generation" rule that offers back of surplus taken land are only to original owners and their immediate successors;
- A clarification that offers back of surplus should apply to all land taken from or gifted by Maori for public works – whether under Public Works Acts, Native Land Acts, project specific legislation or other legislation;
- A review of the valuation of surplus land offered back to Maori – in particular, whether the Crown can justify being the sole beneficiary of any increase in the overall market value of land in an area since the compulsory taking was compensated. Whether allowance should be made in valuations for the special rules strictly limiting alienation of multiply-owned Maori land;
- Whether the Crown and Crown entities should be permitted to retain land for the specific purpose of a settlement of Treaty of Waitangi grievances, without an obligation to offer back to former owners, in the event that land taken for a public work is no longer required for that public work. ❑

JUDICIAL REVIEW: RECENT TRENDS

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updates his paper published at [1992] NZLJ 200, 246

The purpose of this article is to attempt an overview of the current law governing the substantive grounds of judicial review of administrative action. Facetiously put, it asks: Have the grounds shifted under us?

Thirteen years after the (now) Lord Cooke of Thorndon's memorable and characteristic address, "The Struggle for Simplicity in Administrative Law" (*Judicial Review of Administrative Action in the 1980s* (1986 OUP)), simplicity in administrative law has plainly not been achieved, despite the strenuous efforts of His Lordship and others.

As Lord Cooke accurately encapsulated, the 1980s was a period of attempts to simplify and synthesise the numerous grounds of judicial review recognised in the case law under a few basic heads. The two most celebrated of these attempts were by Lord Diplock and Lord Cooke himself.

In *Council of Civil Service Unions v Minister for the Civil Service* [1985] AC 374, 410-11, Lord Diplock proposed a three-fold (but not exhaustive) categorisation of the grounds of review under the headings of "illegality", "irrationality" and "procedural impropriety". Lord Cooke for his part asserted, in *NZ Fishing Industry Association Inc v Minister of Agriculture and Fisheries* [1988] 1 NZLR 544, 552, that an administrative authority is "bound to act in accordance with law, fairly and reasonably".

However, even at the time these attempts at synthesis were made, there were other, perhaps minor, grounds of review which plainly fell outside them. Today, the position is made still more complex, by the emergence of actual or putative grounds such as "substantive unfairness" and "legitimate expectation of a substantive result", which seem to partake of – some would say, confuse – review of merits and review of procedural adequacy.

Nonetheless, the Diplock/Cooke analysis is both helpful and traditional, and enables us to deal with the main substantive grounds of review under the following headings:

- Illegality;
- Procedural Impropriety;
- Irrationality/Unreasonableness.

An analysis under these heads does not exhaust all potential grounds of judicial review. Misrepresentation, whether innocent or otherwise, which operates to bring about an administrative decision or outcome was recognised by Fisher J in the important decision of *Martin v Ryan* [1990] 2 NZLR 209 as a conceptually separate ground of review. Although briefly considered under illegality, review for breach of the New Zealand Bill of Rights Act 1990 ("the Bill of Rights") can perhaps more properly be seen as an independent ground of its own. See eg *Shortland v Northland Health Ltd* [1998] 1 NZLR 433, below. Other possible grounds have been floated by Judges and commentators, including "proportionality" and the so-called "innominate ground". For discussion see my 1992 article, and Taylor, *Judicial Review* (1991) and 1997 supp, paras 11.04-11.06.

An important issue which cuts across the various grounds of review relates to the "reviewability" of particular categories of administrative decision or action, depending on the nature of the powers and the particular subject matter at issue. This will be separately discussed following treatment of the substantive grounds of review.

ILLEGALITY

Illegality, or failure to act in accordance with law, can take a number of different forms. Perhaps the paradigm is the case of ultra vires action (in the strict sense), where the administrative authority acts in the absence of a power to do so, or in excess of such power as it has. Putting this somewhat more fully, the typical case of illegality is one where the source of the power to act, whether legislative or otherwise, is itself contravened, exceeded or abused. In addition, cases may occur where the administrative action contravenes not the statutory or other source of the power to act itself, but some other legislative provision, such as the New Zealand Bill of Rights, the Bill of Rights of 1688 (as in *Professional Promotions and Services Ltd v Attorney-General* [1990] 1 NZLR 501), or perhaps some regulatory statute such as the Commerce Act 1986.

Although some may prefer to classify them under different headings, such grounds as (independent) error of law on the part of a decision maker; mistake of fact; taking into account irrelevant factors or failing to take into account relevant factors; pursuit of a (statutorily) improper purpose; improper fettering of a decision-maker's discretion; and acting or deciding in bad faith, all may properly be characterised as part of review for illegality.

Judicial review for illegality, indeed almost the whole of modern administrative law, is largely about statutory interpretation. This truism has long been recognised: see eg *CREEDNZ Inc v Governor-General* [1981] 1 NZLR 172, 197-8. The same approach is apparent in the administrative law damages field. See for example *Attorney-General v Prince* [1998] 1 NZLR 262; *Morrison v Lower Hutt City Council* [1998] 2 NZLR 331. What is however worthy of note is the sophisticated and wide-ranging analysis of the statutory context and subject matter, and the particular tools of interpretation brought to bear, in the argument and decision of modern-day judicial review cases. Indeed, with the post-Cooke Court of Appeal, it is not uncommon to read judgments dealing with the law which comprise almost entirely statutory analysis, with little or no citation or discussion of authority.

Thus the techniques of statutory analysis go a long way beyond merely looking at the particular empowering provision and arguing to restrict, or widen, its literal meaning. The scope of review, whether for illegality or otherwise, will be affected not only by consideration of the overall scope and purpose of the statutory scheme. It will also be influenced by such matters as the existence of alternative means of oversight (for example, Ministerial; through the Ombudsmen; or indeed through the ballot box, whether that of local or central government), and the provisions of other statutes dealing with the same subject matter. Other, more specialised principles of interpretation may be invoked in particular cases, providing traps for the unwary who seek to advance a literal statutory meaning either in support of or against an illegality argument. Two of these may be briefly mentioned here.

First, there is the New Zealand-grown "make the statute work" principle enunciated in cases such as *Northland Milk Vendors Association Inc v Northern Milk Ltd* [1988] 1 NZLR 530, 537-8. In the words of Cooke P:

> The responsibility falling on the Courts ... is to work out a practical interpretation appearing to accord best with the general intention of Parliament as embodied in the Act – that is to say the spirit of the Act ... [T]he Courts must try to make the Act work while taking care not themselves to usurp the policy-making function, which rightly belongs to Parliament. The Courts can in a sense fill gaps in an Act but only in order to make the Act work as Parliament must have intended.

As *Northland Milk* itself shows, the "make the statute work" principle is likely to operate against arguments seeking to restrict those claiming to exercise statutory power, based on a literal wording or gaps in a statute. The modern trend is to interpret grants of statutory powers broadly rather than narrowly. A recent significant illustration is *New Zealand Kiwifruit Marketing Board v Beaumont* [1997] 3 NZLR 516. The issue was whether the Board, a marketing authority established by statutory regulation under the Primary Products Marketing Act 1953, had the power to market kiwifruit grown overseas.

Under the regulations establishing the Board, the principal functions of the Board were listed. The first of these was, "To acquire and cause to be marketed kiwifruit produced in New Zealand and intended for export". None of the other principal functions dealt with the matter at issue, but reg 13B of the regulations empowered the Board to buy kiwifruit harvested outside New Zealand. Under the Primary Products Marketing Act, the Board as a market authority is expressly given certain powers, including the "rights, powers, and privileges of a natural person". Section 5A(4) provides that a marketing authority shall not exercise any of its rights, powers, or privileges other than for specified purposes, including "Performing its functions".

In the High Court, Elias J held that the conferral on the Board of the powers of a natural person involved a grant of powers that were incidental and not primary. As the Board's principal functions relevantly only included the marketing of kiwifruit produced in New Zealand and intended for export, the Board lacked the power to market kiwifruit grown overseas. The Court of Appeal disagreed. The majority (Richardson P, Thomas, Keith and Tipping JJ) distinguished between an inquiry as to the existence of a power at issue and one concerning the legitimacy of the exercise of that power. Only the first of these was presently before the Court. Rejecting the approach adopted by Elias J, the majority stated (at 524):

> The structure and purpose of [the empowering section] is to give the board all the powers of a natural person. They are not incidental or subsidiary powers. They are primary powers ... [which] clearly give ... the board the power at issue. Whether it may be exercised as contemplated depends on whether, after full and proper inquiry, the purpose of its proposed exercise is legitimate. Whether that is so will depend, among other things, upon a careful analysis of the functions of the board. That analysis will involve a consideration of the statutory functions in the context of the Act and the regulations considered as a whole.

The grant by statute to an entity of specific functions and powers, in tandem with the giving of corporate status coupled with the statement that the new entity has the rights, powers and privileges of a natural person, is reasonably commonplace in this country. Given the particular wording – not reproduced in full here – of the statutory provisions at issue in *Kiwifruit Marketing*, the conclusion reached by the Court of Appeal cannot be said to be untenable. But it is submitted that it would be a surprising thing, and potentially destructive of the doctrine of ultra vires as generally understood, if the statutory grant of the rights, powers and privileges of a natural person were generally seen as conferring unlimited power notwithstanding that the statutory powers expressly conferred on the entity in question were themselves more limited in nature. In my view that is so even if the second-level limit on power contemplated by the Court of Appeal, namely that the exercise of the power can only be for a legitimate purpose in terms of the entity's statutory functions, is then to be imposed on the power so construed.

The second specialised principle of interpretation worth noting requires that ambiguous statutory provisions be interpreted consistent with the principles of international law and in particular international covenants to which New Zealand is a party. In the human rights field, s 6 of the Bill of Rights goes further, requiring an interpretation consistent with the rights conferred to be "preferred". As well, the provisions of the Bill of Rights and of applicable international covenants may reach beyond interpretation and govern, or influence, the decision-making itself, either on illegality principles as discussed above or by way of a "relevant considerations" analysis. See *Tavita v Minister of Education* [1994] 2 NZLR 257; *Puli'uvea v Removal Review Authority* (1995-96) 14 FRNZ 322; *Rajan v Minister of Immigration* [1996] 3 NZLR 543.

An interesting recent example of successful invocation of international law to narrow statutory power is *Sellers v Maritime Safety Inspector* [1999] 2 NZLR 44. Mr Sellers had been prosecuted for departing New Zealand in his foreign-registered yacht without safety equipment stipulated by the Director of Maritime Safety, contrary to s 21(1) of the Maritime Transport Act 1994. He had refused as a matter of principle to carry on his vessel the radio and emergency locator beacon equipment specified as minimum requirements by the Director in guidelines issued by him for the exercise of his powers under s 21. After a review of both international law and conventions relating to freedom of navigation of the high seas and New Zealand statute law, the Court of Appeal (at 57) held that under international law, a port state has no general power to unilaterally impose its own requirements on foreign ships relating to their construction, their safety and other equipment and their crewing if the requirements are to have effect on the high seas.

The Court of Appeal then applied the "established principle as to the construction of a statute that it should be construed, if the words shall permit, so as to be in accordance with international law", concluding (at 62):

> Under international law all that the Director would be entitled to be satisfied about in relation to the adequacy of a foreign pleasure vessel, her equipment and her crew would be to ensure compliance with accepted international standards and rules, to the extent that they allow that judgment to be made by a coastal state. ...
>
> We consider that [this] is consistent with the wording of s 21(1)(b) and (c) when that provision is read, as it must be, in its wider context. To repeat, for centuries national law in this area has been essentially governed by and derived from international law with the consequence that national law is to be read, if at all possible, consistently with the related international law. That will sometimes mean that the day to day (or at least year to year) meaning of national law may vary without formal change.
>
> The Director in his procedures for the grant of a clearance under s 21(1) has set minimum requirements which are not permitted by international law. Those requirements are in breach of the powers conferred by s 21(1) as that provision is to be understood at present. Mr Sellers should not be held to be committing an offence for not complying with requirements set without lawful authority.

In *Sellers* the relevant statutory discretion was expressed in broad and unqualified terms. There was a prohibition on departure from New Zealand waters unless (inter alia) the Director was "satisfied that the pleasure craft and its safety equipment are adequate for the voyage". Despite that breadth, the Court of Appeal was prepared having regard to what it saw as fundamental principles of international law to read down that discretion, and to do so in a way which would curtail its operation in relation to foreign pleasure vessels. This in effect permitted the provision differing scope and effect depending on the country of origin of the particular vessel. Guidelines that were (it seems) valid for New Zealand-domiciled vessels were held invalid in the case of a foreign pleasure vessel. The case underlines the importance of the specialised principles of interpretation, and the need for counsel to be thoroughly prepared to argue such issues when they arise.

It may also be noted that *Sellers* is a case of what is commonly referred to as "collateral attack"; that is, challenge to validity of administrative action otherwise than by way of an application for judicial review. However, the Court of Appeal did not discuss any of the legal issues which might be thought to arise in relation to this aspect. Contrast the detailed analysis of "collateral attack" principles embarked on by the House of Lords in the comparable case of *Boddington v British Transport Police* [1998] 2 All ER 203.

PROCEDURAL IMPROPRIETY

Procedural fairness, in terms of either notice and a fair hearing without predetermination or as a lesser alternative, a requirement of proper consultation, remains both the workhorse, and the ground potentially most likely to succeed, of modern-day administrative law.

To the extent that a statutory regime is involved, the same techniques of detailed statutory analysis as have already been referred to need to be brought to bear in the assessment and determination of the existence and content of a duty of procedural fairness. So far as the factual elements are concerned, it needs to be stressed that a breach of fairness will only be found after a very careful consideration of the entire circumstances of the case. The modern approach is stated by Tipping J in *Isaac v Minister of Consumer Affairs* [1990] 2 NZLR 606, 626:

> ... in this field the Court should take an essentially practical rather than a legalistic approach. ... the whole of the evidence should be reviewed in making a decision as to whether [the applicant] has had practical justice in the sense of fair notice of what the Minister's concerns were, what she was proposing to do and of the grounds and material upon which she was proposing to act.

Space does not permit a broad review of this wide-ranging area, but a few current "hot issues" should be touched upon.

Consultation

There can be no doubt that, since the concept of a duty to consult as a particular aspect of procedural fairness first came to prominence in the mid 1980s, consultation with persons affected by a contemplated administrative decision or action has become a major focus of administrative law and practice in this country. The leading New Zealand case is *Wellington International Airport Ltd v Air New Zealand* [1993] 1 NZLR 671. In *Te Heu Heu v Attorney-General* [1999] 1 NZLR 98, 126, Robertson J adopted the following statement of principle by Lord Bridge of Harwich in *Re Westminster City Council* ([1986] AC 668, 692):

> ... in public law ... a duty of consultation may arise from a legitimate expectation of consultation aroused either by a promise or by an established practice of consultation.

As to legitimate expectation, His Honour noted the comments of the Privy Council in *Attorney-General of Hong Kong v Ng Yuen Shiu* [1983] 2 AC 629, 636-637:

> Their Lordships consider that the word "legitimate" in [the expression "legitimate expectation"] falls to be read as meaning "reasonable". Accordingly "legitimate expectations" in this context are capable of including expectations which go beyond enforceable legal rights, provided they have some reasonable basis: ...
>
> The expectations may be based on some statement or undertaking by, or on behalf of, the public authority which has the duty of making the decision, if the authority has, through its officers, acted in a way that would make it unfair or inconsistent with good administration for him to be denied such an inquiry.

In the New Zealand context, a further and not uncommon source of a duty to consult is an express or implied duty arising under statute, again a matter for careful statutory analysis as to both the scope and the existence of the duty.

In *Te Heu Heu*, the Maori plaintiffs (who included the Tuwharetoa Maori Trust Board) had been in detailed negotiations with the respondent District Council over a Treaty of Waitangi-based consultative relationship, the details of which had not been finalised. While discussions were ongoing, the District Council agreed to purchase from another of the defendants, a state-owned enterprise subsidiary, lands which the council knew to be the subject of Treaty claim. It did so without consulting with the plaintiffs or those they represented. The plaintiffs argued that their legitimate expectation of consultation in a matter vitally affecting their interests as Treaty claimants had been ignored. This contention was not accepted. Robertson J held (at 126-7):

> The test is whether objectively the council, by conduct or assurance, had created a situation which gave rise to a legitimate expectation as to consultation about matters affecting the mutual interests of the two groups. [Counsel for the plaintiffs] accepts that on the evidence there had not been a concluded agreement as to every last aspect of the treaty-based relationship. I accept his submission that in this area of administrative law, contractual law precision is not warranted. The crucial question is whether, viewed objectively, matters had progressed to such a point that a legitimate expectation could have arisen.
>
> ... [A]lthough the Tuwharetoa Maori Trust Board in particular was claiming a substantial role for itself as of right, nothing was said or done by the council which could reasonably have suggested that the parties agreed to all the board's claims. When a local authority in good faith tries to involve any section of the community in its consultative processes – especially when it does so with tangata whenua – that is to be encouraged and supported. But it is clear that in spite of the council's overtures there remained in its responses a clear indication that at the end of the day it would make the decision. ...
>
> I find no basis for a legitimate expectation that the plaintiffs would be consulted on the transaction at issue in this case. The plaintiffs were anxious to foster a practice of regular consultation but that is not the test for whether there is legitimate expectation. The question is whether the council by its words, actions or assurances, was offering something and failed to deliver. What the plaintiffs wanted never developed beyond a hope or expectation on their part.

A brace of recent English Court of Appeal cases concerning consultation with rest home residents and others potentially affected by planned residential home closures illustrates some of the differences between sufficient and insufficient consultation. The cases are reported under *R v Devon County Council, ex p Baker* [1995] 1 All ER 73. The decisions underline the need for advice as to the proposed action well in advance of the final decision; a reasonable time for the making of submissions and in particular the putting forward of objections; and for the consideration of any objections with an open mind and on the merits. It was also held that in the context of the proposed closure, it was not required that each affected individual be consulted personally. Proper consultation could be achieved by group meetings or expression of views by a group formed to represent residents' interests and oppose the closures. These decisions would appear to be consistent with the leading New Zealand authority, *Wellington International Airport*.

Legitimate expectation of substantive result

A legitimate expectation of an entitlement to be consulted is of course an expectation as to the procedure which a decision-maker will follow and not as to the outcome. A current vexed question is whether a decision-maker may by conduct or representation, such as the formulation of a policy for dealing with applications of a particular class, bring into existence an enforceable legitimate expectation as to the substantive result.

The current Australian law on this point appears to be as emphatically stated by Brennan J in *Attorney-General (NSW) v Quinn* (1990) 93 ALR 1, 24:

> The question can be put quite starkly: when an administrative power is conferred by the legislature on the executive and its lawful exercise is apt to disappoint the expectation of an individual, what is the jurisdiction of the Courts to protect that individual's legitimate expectations against adverse exercises of the power? I have no doubt that the answer is: none.

By contrast, English law has been for some time, and arguably still is, in a state of flux: see Wade & Forsyth, *Administrative Law* (7th ed 1994), p 418-20, 522-5; De Smith, Woolfe & Jowell, *Judicial Review of Administrative Action* (5th ed 1995), p 421-30; *R v Home Secretary, ex p Hargreaves* [1997] 1 All ER 397 (CA); *R v Home Secretary, ex p Pierson* [1998] AC 539, 575, 590-1, 603 (also as to substantive unfairness, discussed below).

The New Zealand cases reflect the uncertain current position, and the comment of Robertson J in *Te Heu Heu* (at 125) that "the boundaries of the doctrine of legitimate expectation in administrative law are not settled".

For a pair of somewhat contrasting recent cases, see *Lawson v Housing New Zealand* [1997] 2 NZLR 474, 488 and *Preston v Minister of Immigration* [1998] NZAR 539, 553-6. In the former case Williams J, applying English authority, tended to rule out the invoking of legitimate expectation as a challenge to the substance or merits of a decision. In the latter, Giles J, invoking "the doctrine of substantive unfairness", appeared to accept that New Zealand law may go further than the English authorities.

Substantive unfairness

In *Thames Valley Electric Power Board v NZFP Pulp & Paper Ltd* [1994] 2 NZLR 641, a three-Judge Court of Appeal "sort of" recognised substantive unfairness as a legitimate ground of judicial review. Cooke P described it as "shading into but not identical with unreasonableness", elaborating as follows (at 652-3):

> It is clear ... that the adequacy of the administrative consideration given to a matter and of the administrative reasoning may be reviewed. ...Inevitably this means, whatever the verbal formula of review adopted, that the quality of an administrative decision as well as the procedure is open to a degree of review, although not of course to appeal in the absence of a statutory right of appeal.
>
> ... One situation justifying intervention for unfairness might be where the procedure and the decision of an administrative body, although possibly just surviving challenge if viewed separately, were in combination so questionable as to impel the conclusion that, in the words of Lord Donaldson of Lymington MR in *R v Panel on Take-overs and Mergers, ex P Guinness plc* [1990] 1 QB 146, 160, "something had gone wrong of a nature and degree that required the intervention of the Court ...". The merit of the substantive unfairness ground is that it allows a measure of flexibility enabling redress for misuses of administrative authority which might otherwise go unchecked.

The other two Judges commented only briefly on the point at issue. McKay J stated (at 654):

> The authorities cited by the President amply demonstrate that unfairness can be a ground of judicial review, but it does not follow that anything that can be described as "unfair" will suffice. ... While it may be appropriate to group such cases under the generic description of "unfairness", there is a danger that in doing so one may convey the impression that anything that is "unfair" will

> be sufficient. That would be too vague a test, and one which appears, with respect, to have led the Judge into error. What is required is unfairness of the kind illustrated by the cases, or of a similar nature based on a proper application of the same principles.

Fisher J was even more cautious (at 654):

> But on each occasion that the expression "substantive unfairness" is applied to a case it will continue to be necessary to identify a more specific and principled administrative law basis for intervention. Otherwise, as I think this case illustrates, the distinction between judicial review and appeals on the merits will become dangerously blurred.

It can be seen that neither McKay J nor Fisher J was prepared to recognise substantive unfairness as an autonomous ground of judicial review. McKay J appeared to see it as offering a rubric under which to "group" existing cases involving improper motive, abuse of power or something analogous. Fisher J stressed the continued necessity, notwithstanding the use of the term "substantive unfairness", to identify a narrower, existing ground justifying intervention in the particular case.

One may well ask, what is the difference between "legitimate expectation of a substantive result", and "substantive unfairness"? In *Preston*, Giles J invoked authorities dealing with the latter in the context of a discussion as to the availability in law of the former. In *Northern Roller Milling Co Ltd v Commerce Commission* [1994] 2 NZLR 747, 750, Gallen J appeared to equate the two.

Whatever one thinks of the conceptual underpinning of the two doctrines and the development of each in terms of earlier precedent, it seems clear that, in principle, the scope of any doctrine of substantive fairness, particularly one along Cooke lines, must be significantly the wider. A "legitimate expectation of a substantive result" can plainly only arise in factual terms if such an expectation has been engendered, by words or conduct by or on behalf of the decision-maker, and is objectively reasonable. Any relief granted would similarly have to relate to the content of the expectation, and not to some overall assessment of the outcome in terms of fairness. "Substantive unfairness" by contrast, is by definition not dependent on the existence of any legitimate expectation, and would appear to permit the Court to have regard to a much broader assessment in terms of overall fairness. On that analysis, if a full-blown separate ground of substantive unfairness were held to exist, there would appear to be no need for any separate doctrine of "legitimate expectation of a substantive result".

Moreover, although the passage from the judgment of Cooke P in *Thames Valley* quoted above seeks to draw a distinction between the procedure followed by an administrative decision-maker and the decision itself, the distinction or at any rate the resultant classification in a particular case may not be all that clear-cut. In *Pharmac v Roussel Uclaf Australia Pty Ltd* [1998] NZAR 58, 64, a central issue was whether Pharmac was entitled to undertake a reclassification exercise progressively, thus differentiating (at least temporarily) between Roussel Uclaf's "Klacid" antibiotic and a competing product, "Rulide", when reviewing the subsidies payable in respect of the therapeutic sub-group of pharmaceuticals to which both drugs belonged. (Or, as Thomas J put it, whether Pharmac was required "to act even-handedly as between companies manufacturing and selling pharmaceutical products in the same therapeutic sub-group".) As the majority noted in relation to this issue (at 64):

> We find the answer to [the question whether the plaintiff's complaint related to process or substance] elusive as it often is when the question is one of whether an error is of fact or of law. ...
>
> [The plaintiff's case] can be viewed as an attack on the substance of the decision to establish the new classification or it can be seen as an argument that there was a precondition, in terms of procedure, to doing so.
>
> In the end we inclined to the opinion that the case is about process rather than substance but in the view we take it makes no difference to the result.

Thomas J in dissent agreed that the case was about "process rather than substance" (at 82). The Privy Council on further appeal likewise appears to have classified the complaint of lack of even-handedness and consistency on Pharmac's part as giving rise to an issue of procedural fairness. See *Roussel Uclaf v Pharmac*, PC Appeal No 34 of 1998, 30 July 1998.

Both the doctrine of substantive unfairness and that of legitimate expectation of a substantive result have been tellingly criticised; see eg Poole, "Legitimate Expectation and Substantive Fairness: Beyond the Limits of Procedural Propriety" [1995] NZ Law Rev 426. In *Pharmac*, the majority of the Court of Appeal considered that any challenge to the substance of Pharmac's decision had to be judged according to the "standard test" of *Wednesbury* unreasonableness as declared in *Woolworths*, in part two, adding:

> The concept of substantive fairness discussed in *Thames Valley* ... also requires further consideration. The law in this country applicable to situations of that kind will no doubt be developed on a case by case basis. But this is not such a case. It is entirely about money, subsidisation of the sale of pharmaceuticals. There is no call for any departure, on these facts, from the position so recently taken in *Woolworths* (at 66).

The Privy Council dealt with Roussel Uclaf's unfairness arguments in the following terms:

> Their Lordships accept that if Roussel could show that Pharmac were obliged under their [Operating Policy Procedures] to review Rulide and Klacid together, or if the failure to do so was contrary to some overriding principle of fairness, requiring equals to be treated equally, then there *might be* grounds for attacking Pharmac's decision to review one before the other. ...
>
> Their Lordships are by no means persuaded that the unfairness of which Roussel now complains is a *procedural unfairness of the kind which justifies the Court's intervention by way of judicial review*. What is attacked is the decision to review the [drugs in the sub-group] one by one, not the way of arriving at that decision. *But putting that on one side*, fairness does not require all potential candidates for a sub-group to be reviewed at the same time. ... Fairness to Roussel had to be judged at the time the decision was made, and balanced against the public interest in reducing expenditure on pharmaceuticals. (Emphasis added.)

Having regard to the emphasised portions, the Privy Council cannot be seen as going so far as to uphold substantive fairness as a separate ground of review.

Thus in the post-Cooke era, particularly given the comments and approach of the Court of Appeal in *Roussel Uclaf*, the future of "substantive unfairness" plainly cannot be said to be assured. ❑

To be continued in the next issue