

**“Don’t say you weren’t warned”
The Aon case & ASIC v Somerville**

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A seminar presented by Counsel of Gordon & Jackson’s List

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ASIC v Somerville: a new dimension — conflict of interests

Peter Agardy OWEN DIXON CHAMBERS WEST, MELBOURNE

In *Australian Securities and Investments Commission v Somerville*,¹ Windeyer J found that a solicitor had aided and abetted a breach by directors of their duties under the Corporations Act 2001 (Cth).

There were several companies involved. There was a common theme in the transactions documented by the solicitor in each case.

The solicitor prepared the agreement and incidental documents. He acted for all parties, and this is the new dimension to which I draw attention in this casenote.

The essence of the relevant transaction was that the (old) company was insolvent or about to become insolvent. The solicitor prepared an agreement by which the assets were transferred to a new company with a similar name, to be controlled by the directors of the old company. The debts remained with the old company. Settlement took place shortly before the company was to be wound up on the application of a creditor. The consideration for the sale was illusory. The old company merely obtained shares in the new company, which carried the right to receive dividends from the new company. In the event there were no dividends actually paid. The creditors of the old company were left to look to the empty shell which remained.

Justice Windeyer found that the directors had breached their duties to the old company under ss 181, 182 and 183. For example, they breached s 182(1) because they gained an advantage for themselves by securing the use of the assets in the new company.

The solicitor had written a letter of advice in which, after referring to the conventional options (such as the appointment of an administrator), he had said that the only viable alternative was to transfer the business to a solvent entity controlled by the directors of the old company. He recommended and documented an agreement by which the old company would have the right to receive dividends, so that in time all of the creditors of the old company would be paid. This was a fanciful concept.

The solicitor declined to give evidence — a tactic which did not impress Justice Windeyer, who drew an inference that his evidence would not have assisted his defence.

One aspect which was not emphasised in the decision was that the directors had an impossible conflict of interests. In the course of considering the agreement, they were effectively negotiating with themselves. They owed duties to both the old company, the vendor of the assets, and to the new company, the purchaser. They also had their own personal interests (they wanted a business to work in) and were under a duty not to permit their personal interests to conflict with the interests of any company of which they were directors.

This conflict should have been identified by the solicitor and pointed out to the directors. Instead, the solicitor assured the directors that it would be “all right”.

At the very least, the solicitor should have urged the parties to the agreement, and for that matter the directors as well, to obtain independent advice. Yet in preparing the agreement for transfer of assets, presumably on behalf of the vendor, he guaranteed that the interests of his vendor client — and its creditors — were defeated.



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Footnotes

1. *Australian Securities and Investments Commission v Somerville* (2009) 259 ALR 574; 74 ACSR 89; [2009] NSWSC 934; BC200908184.

GORDON & JACKSON LIST BREAKFAST SEMINAR

Thursday 13 May, 2010

“Don’t say you weren’t warned!”

AON RISK SERVICES AUSTRALIA LTD v. AUSTRALIAN NATIONAL UNIVERSITY¹

George H Golvan QC

A question frequently raised in litigation is how permissive a Court should be in permitting a late amendment to pleadings, or granting a late adjournment, in the interest of ensuring that the real issues between the parties are litigated. Since the decision of the High Court in *Queensland v. JL Holdings Pty Ltd*² the prevailing view was that the Court’s ultimate aim was to obtain justice, which was to be the “*paramount consideration*”, even above principles of case management.

The *JL Holdings’ Case* involved an application for leave to amend a defence, which was likely to result in the vacation of a four month trial which had been fixed six months ahead. The Federal Court trial Judge considered that maintaining the trial date was more important than permitting a party to present a further defence, even if fairly arguable, and refused the amendment. The High Court (per Dawson, Gaudron, McHugh and Kirby JJ, concurring) reversed the decision and held that justice is the paramount consideration in considering an application to amend. Although case management was a relevant consideration it should not prevail over the injustice involved in shutting a party out from raising an arguable defence. The case was viewed as permitting a wide scope for parties to amend pleadings and seek adjournments, so long as any prejudice could be cured by an appropriate order as to costs. *JL Holdings*

¹ (2009) 239 CLR 175

² (1997) 189 CLR 146.

has been used as justification for multiple amendments, in some cases even at a late stage in a case.

As has frequently been pointed out, delayed litigation can give rise to significant prejudice, which is not adequately compensated by an order for costs. For example, loss of opportunity costs and stress and disruption to life caused by involvement in litigation, are issues which are frequently raised in litigation and mediations as a justification for reaching a commercial compromise. In addition, there has been an increasing emphasis on the importance of case management considerations which have changed considerably since *JL Holdings*, with greater reliance on 'docket systems' and specialist Judge controlled lists, such as the new Commercial Court which focus on the 'just, quick and cheap' resolution of disputes, and involve intensive case management.

The unanimous decision of the High Court in the *Aon Case*, by seven Judges who took the opportunity to overrule *JL Holdings*, now gives primacy to case management principles over principles of justice to determine whether a party should be permitted to amend its pleadings to raise a new argument at the hearing, which would result in significant delay to the trial. It is of interest that three members of the High Court in *Aon* (French CJ and Crennan and Kiefel JJ) were previously Federal Court Judges, where there is strong emphasis on case management with docket Judges being appointed to virtually every case. It should also be noted, that the High Court pointed out that the *JL Holdings Case* was factually very different from *Aon*. For example, the applicant had explained and the Court accepted that the application had been made late because a material fact had only recently been discovered, unlike *Aon* where no adequate explanation for the late amendment was offered.

The Facts

- The proceeding related to fire damage to the Mt Stromlo Observatory Complex belonging to the ANU in the Canberra bushfires in 2003;

- ANU commenced proceedings against co-insurers claiming indemnity for the bushfire damage to the observatory;
- The insurers by way of defence raised issues as to under-insurance of certain buildings, and claimed that certain buildings were excluded from cover;
- ANU subsequently joined its insurance broker Aon to the proceedings. The claims against Aon related to buildings not being covered by insurance, but relevantly did not include allegations of under-insurance, even though ANU should have been alerted to the need to reconsider its claim against Aon by the defences of the insurers;
- At the beginning of the hearing ANU settled with its insurers and sought an adjournment of the proceeding to significantly amend its claim against Aon to raise new allegations concerning breach of a duty in relation to under-insurance of property. Aon objected to the late amendment and argued that ANU should be held to its existing pleading. The amendment was allowed by the Trial Judge with costs awarded on a party/party basis, even though the explanation for the delay was not satisfactory;
- On appeal, the ACT Court of Appeal dismissed Aon's appeal in relation to the amendment and adjournment, but awarded costs to Aon on an indemnity basis;
- Aon then appealed to the High Court.

The High Court Decision

The High Court (all seven Judges comprising French CJ and Heydon J, who delivered separate judgments and Gummow, Hayne, Crennan, Kiefel and Bell JJ, delivered a joint judgment) allowed the appeal deciding:

- Although the just resolution of proceedings remained a paramount purpose, speed and efficiency, in the sense of minimal delay and expense, are also to be seen as essential to the just resolution of disputes and are key objectives;

- A just resolution does not entitle a party to raise a new arguable case at any point of the proceedings, on payment of costs. There is no such entitlement. All matters relevant to the exercise of the power to amend should be weighed before an amendment is granted;
- The past view that an order for costs occasioned by an amendment will normally overcome injustice should give way to the modern position that even an order for indemnity costs will not necessarily undo the prejudice a party suffers from delay in litigation. The Court will need to weigh:
 - the time when the application is made;
 - the extent of the delay and the explanation which is given;
 - the costs and prejudices associated with granting of the amendment;
 - against the nature and importance of the proposed amendment ;
- The fact of substantial delay and wasted costs, the explanation for the delay and issues of case management will assume great importance on any application for leave to amend;
- A party requesting an amendment is required to give a satisfactory explanation for the delay in seeking the amendment;
- The High Court took into account that the amendments were so substantial, in that case, as to require Aon to, in effect, defend the case from the beginning and file a fresh Defence. Further, the application was made during the time set down for trial and would result in abandonment of the trial if granted. Also, there were issues as to whether the award of costs, even indemnity costs, would overcome the prejudice to Aon by granting the amendment;
- Statements in *JL Holdings* suggesting only a limited application for case management were no longer applicable and should not be applied in the future by Courts. On the contrary, the Courts should take into account the effects of delay, not only upon the parties to the proceeding, but also the Court, other litigants and the public generally.

Implications

- The decision overrides the assumption previously created by the High Court in *JL Holdings* that case management considerations and questions of proper Court resources are to be given limited weight in determining an application to amend pleadings, with the emphasis being on considerations of justice, particularly the injustice of cutting a party out of arguing a fairly arguable claim or defence. The High Court recognised and accepted that case management was now an accepted aspect of the civil justice system to tackle the problems of delay and costs in civil litigation;
- The case overturns the generally accepted notion that there is an entitlement of a party to a late amendment, almost as of right, purporting to raise the “*the real issues*” between the parties, on payment of costs;
- Essentially, the case is a strong warning to litigants that amendments to pleadings and late adjournments will be not freely granted any more, even on payment of indemnity costs. The Court will need to assess:
 - the nature of the proposed amendment;
 - any reasonable explanations for the delay;
 - the prejudice which will result;
 - the fact that costs may not be sufficient to overcome prejudice;
 - the interests of Court management and the interests of the public as a whole on the efficient use of Court resources and the need to maintain confidence in the Court system.

These are relevant considerations which will now need to be addressed in any argument, and/or affidavit material in relation to a late pleading amendment application.

- Although the issue was not decided, the Court suggested that the problem caused by late amendment may not be overcome by discontinuing the proceeding and commencing a fresh proceeding, as a subsequent proceeding might be estopped under the principles in *Port of Melbourne Authority v. Anshun Pty Ltd.*³
- The decision in *Aon* places emphasis upon the need for litigants to conduct litigation in a speedy and efficient manner, without undue delay, and certainly echoes the frustrations and legitimate concerns of many litigants as to the undue delays and costs involved in modern litigation. The decision also places a duty on Courts to pursue the objective of timely and cost effective disposition of proceedings in the Court by monitoring and managing the conduct of cases before them.
- It will be of some interest to discover whether the *Aon* Case will result in any real change in the practical attitude of Courts to tardy litigation. It is likely that in the same way as *JL Holdings* has previously been used to justify a permissive approach to late amendments based on achieving justice between the parties, parties will now seek to rely upon *Aon* to justify a far stricter attitude and will endeavour to seek to persuade Courts to refuse late amendments to pleadings, which are likely to result in delay or disruption to Court lists. There will also be focus on what French CJ described as the importance of not undermining confidence in justice, by undue delay in litigation⁴.
- Ultimately, however, the reality will be that each case will be considered in its own particular context. Although a party seeking a late amendment to pleadings will have extra hurdles to jump over, Courts will still be reluctant, in my opinion, to shut a party out of arguing the real issues in the case, if there is a good explanation for a delay in seeking the amendment, if any consequential delay will not be inordinate and wasted costs can be adequately compensated. But the

³ (1981) 147 CLR 589.

⁴ (2009) 239 CLR at 195 [35].

decision in *Aon* does represent an important change in culture and mentality by the High Court concerning how modern commercial litigation should, and should not, be conducted. According to the High Court, modern litigation will need to be conducted with speed and economy, in which Courts will play a more active role in undertaking case management in pursuance of these objectives and will exercise their discretion to allow amendments to a case not merely in the interests of a just resolution between the parties (which will still remain an important factor), but also give primacy to:

- the avoidance of delay;
 - interests of other litigants in the system, whose rights might be compromised by delay and disruptions to the Court lists; and
 - the interests of the public as a whole, who are entitled to have confidence in the speedy and efficient administration of justice.
- The *Aon Case* has recently been followed by Olsson AJ in the Northern Territory Supreme Court in *Territory Sheet Metal Pty Ltd v ANZ*⁵. In that case the Court refused an application by the bank to raise for the first time, after a lengthy interlocutory process and a protracted trial with primary findings, a new defence based on the *ex turpi causa* principle (i.e. no Court will lend its aid to a person who has founded his case on an illegal act). After citing the dicta in *Aon* concerning the importance of case management considerations, His Honour stated:

*"To that I would with respect, add that it also denies the effect of a proposed fundamental amendment in terms of the wanton waste of scarce and expensive public resources. To adopt the language of the plurality, it simply cannot be said that just resolution of litigation requires that a party be permitted to raise any arguable case at any point in the proceedings on the payment of costs."*⁶

⁵ [2010] NTSC 3.

⁶ [2010] NTSC at 20 [85].

The *Territory Sheet Metal Case* confirms that a permissive approach to accepting a late amendment on the payment of costs thrown away will no longer be acceptable and that considerations of delay, costs which can never be recovered and limited Court resources will also have great if not now paramount importance.

- Finally, it should also be noted that *Aon* should not be used as a justification to defeat any application which may involve a request to extend the time for compliance with a Court direction and the possible adjournment of a trial. *Aon* was recently distinguished in the Federal Court Case of *Smart Company Pty Ltd v Clipsal Australia Pty Ltd*⁷, per Lander J. A respondent applied for a substantial proceeding, involving a claim for hundreds of millions of dollars, to be dismissed for failure of the applicant to comply with an order for the filing and service of expert witness statements, and placed reliance on *Aon* to assert that case management should be complied with. The Judge concluded that the applicant in that case was not attempting to introduce a new case but attempting to prosecute an existing case. He found that the applicant simply could not comply with a direction given by the Court because the applicant's expert has not remedied himself, as he should have, and prepared his expert's report.

Justice Lander concluded⁸ that there was nothing in the decision in *Aon* that would require the Judge to refuse to extend the time within which the applicant's expert had to provide his report, even if the effect of such an order would be to cause the trial to be adjourned.

So it should not be forgotten, that despite the new approach, each case needs to be considered on its own facts, and the mere consequence of failure to comply with court management directions and even possible delay to the trial itself will not invariably result in the refusal to grant an extension of time for compliance with a court direction, particularly if the failure to refuse an extension of time will invariably lead to draconian consequences.

⁷ [2010] FCA 4.

⁸ [2010] FCA at [66 to 71].