IN THE COURT OF APPEAL OF NEW ZEALAND

CA424/2015
[2016] NZCA 326

BETWEEN	THE MINISTER OF EDUCATION First Appellant
	THE SECRETARY FOR EDUCATION Second Appellant
AND	REIDY MCKENZIE LIMITED Respondent

Hearing: 3 May 2016

Court: Winkelmann, Simon France and Woolford JJ

Counsel: P C Murray and M J Hammer for Appellants
J W Turner and T J Goulding for Respondent

Judgment: 12 July 2016 at 10.30 am

JUDGMENT OF THE COURT

A The appeal is dismissed.

B The appellants must pay the respondent costs for a standard appeal on a band A basis and usual disbursements.

REASONS OF THE COURT

(Given by Simon France J)

Introduction

[1] The Minister of Education (the Minister) has initiated liquidation proceedings in relation to the respondent company. In support of her application, the Minister wishes to rely on financial accounts of the respondent which, it is agreed, disclose

balance sheet insolvency for the periods to which they relate. The Minister acquired the financial accounts in the course of settlement negotiations with Reidy McKenzie Ltd (Reidy McKenzie) in relation to separate proceedings.

[2] Reidy McKenzie contended, and Faire J agreed, that the circumstances were such as to attract settlement negotiation privilege under s 57 of the Evidence Act 2006.[1] That aspect of the decision is not appealed.

[3] But the Minister contended, unsuccessfully, that privilege had been waived, or that the privilege did not extend to liquidation proceedings. The latter contention sought to apply, by analogy, a common law exception to the privilege that has been recognised as applying to acts of bankruptcy.[2] It is these two aspects of Faire J's decision that are in issue on the appeal.

Waiver

Background facts

[4] Reidy McKenzie is a builder which has constructed schools for the Minister. The Minister contends the work on some schools was deficient and has instituted proceedings in relation to three (the schools proceedings). Reidy McKenzie, as well as denying fault, has suggested to the Minister that it would be financially pointless to obtain a substantial judgment against it.

[5] The Minister agreed to assess this latter contention and in order to facilitate that assessment, Reidy McKenzie provided the Minister with its financial statements. The process of analysing these accounts, including obtaining independent advice, took time. Meanwhile the litigation was underway and timetable obligations were falling due.

[6] The parties to the schools proceedings filed the usual timetabling memoranda as well as a sequence of memoranda designed to keep the Court informed about discussions the parties were having. As a consequence of these memoranda, an

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1 *Minister of Education v Reidy McKenzie Ltd* [2015] NZHC 1555 at [58].
2 *Re Daintrey, ex parte Holt* [1893] 2 QB 116 (QB) at 120.

allocated trial date was vacated and the timetable was indefinitely suspended. It is the memoranda filed by Reidy McKenzie for these various purposes that are said to constitute waiver of the privilege.

[7] The first relevant memorandum concerned a proposed meeting of experts. Reidy McKenzie explained it was not appointing an expert even though it intended to defend the proceeding. Two paragraphs are of relevance:

> 4. It considers it has a good defence in respect of the claims, but has had, and continues to have, without prejudice negotiations with the Ministry with a view to reaching a settlement. Last week it made its most recent annual accounts available to the Ministry in order to provide evidence to the Ministry as to its current financial position.
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> …
>
> 7. My client is not taking these proceedings lightly. It is a company which has traded successfully for many years and its directors would like the company to continue to trade. Accordingly, the company has not been put into liquidation, and is actively negotiating with Ministry representatives. If it cannot resolve matters with the Ministry, its present intention is to defend the claims within the limits of its resources.

[8] The next memoranda of relevance are a memorandum from the Minister seeking vacation of a trial date and Reidy McKenzie's response. The Minister through counsel advised the Court:

> …
>
> 4 As recorded in the Court's minute dated 30 June 2014, Reidy McKenzie says that it has been winding down its operations and it has limited means, although it does not intend to go into liquidation.
>
> 5 Since 2012, Reidy McKenzie has been providing its annual accounts to the Ministry, including the draft financial statements for the year ending 31 March 2014. These accounts have been regularly reviewed by the Ministry's forensic accountants, Deloitte.
>
> 6 On 18 July 2014, the Ministry received a report from Deloitte which has raised concerns over the liquidity of Reidy McKenzie. As a result, the Ministry and Deloitte need to carry out further enquiries, including whether this proceeding should be continued. It is expected these enquiries will take some months.
>
> 7 As soon as the plaintiffs are in a position to update the Court following the enquiries into Reidy McKenzie's liquidity they will update the Court further. However, the Ministry is loathe to incur

> the costs of preparing evidence until these enquiries have been carried out and a decision has been made as to whether there is merit in proceeding with the claim.
>
> …

[9] Reidy McKenzie through counsel replied:

> …
>
> 2. The plaintiffs' concerns are justified. My client has been responsible in making disclosure to the Ministry in respect of its financial position. It is a defendant in respect of several active proceedings brought by the Ministry.
>
> 3. My client is at present taking advice in respect of its financial position and hopes to be in a position in about 6 to 8 weeks to make a decision as to its future.
>
> …

[10] It can be added that sometime after this, however, the Court was advised settlement had not been reached.

Law and discussion

[11] Waiver is governed by s 65 of the Evidence Act. That section identifies the various ways in which a person may be taken to have waived privilege. The Minister relies upon s 65(3)(a), the operative parts of which are:

> (3) A person who has privilege waives the privilege if the person—
>
> (a) acts so as to put the privileged … information … or document in issue in a proceeding …
>
> ...

[12] It is a nice question whether waiver in the schools proceeding, had it occurred, would extend to this quite separate proceeding involving the same parties. However, we consider the question of waiver sufficiently untenable on the facts to make other analysis unnecessary.

[13] The accounts in issue are not relevant to the merits of the schools proceedings, and were in no sense being relied upon by Reidy McKenzie in the proceedings. Rather, as part of privileged settlement negotiations they were

provided by Reidy McKenzie to assist the Minister to determine whether it was financially worth continuing her proceedings against Reidy McKenzie. This is an assessment unrelated to the merits or substance of the Minister's claims.

[14] The Court need not have been told about the accounts. Presumably the references to them were to reinforce to the Court that the settlement or discontinuance discussions were being pursued assiduously. The references to providing the Ministry with the accounts were unnecessary detail, a fact that points against the idea they were being put in issue in the proceedings.

[15] This statutory test of "put in issue" within s 65(3)(a) reflects the common law approach to waiver. *Cross on Evidence* notes,[3] citing *Mann v Carnell*,[4] that the underlying rationale is the prevention of inconsistency. A litigant cannot rely on the content of a document for aspects of the litigation whilst seeking to withhold it otherwise. This principle is often advanced under the label of unfairness, the assessment being whether it is fair to allow the privilege "to survive the use to which the holder has put it—whether deliberately or otherwise".[5] There is no suggestion of either inconsistency or unfairness here. Further, as Mr Turner notes, it was the Minister who sought disclosure of some of the accounts. Reidy McKenzie has not used the accounts in a manner which make the maintenance of privilege inconsistent or unfair.

[16] Some argument was addressed to the fact that reference to the documents occurred within the context of timetabling or procedural matters. It was suggested waiver could not occur when the document was used only for procedural purposes. We see no advantage in some absolute proposition that use in a procedural context can never amount to waiver. A blanket rule is unnecessary. The statutory test is there and should be applied to the particular circumstances. It is indeed highly probable that if the only use is in a procedural context the claim of waiver will fail — but that is simply an observation rather than a rule.

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3 Mathew Downs (ed) *Cross on Evidence* (looseleaf ed, LexisNexis) at [EVA65.5].

4 *Mann v Carnell* [1999] HCA 66, (1999) 201 CLR 1 at [29].

5 Colin Passmore *Privilege* (3rd ed, Sweet & Maxwell, London, 2013) at [7–005] (footnote omitted). See generally the discussion at [7–006]–[7–013].

An exception for acts of insolvency?

[17] There have long been a number of exceptions to the settlement negotiation privilege. One of them relates to acts of bankruptcy, an exception that was first recognised in 1893 in *Re Daintrey, ex parte Holt*.[6] The Minister submits an equivalent exception should be recognised for acts of corporate insolvency. It is said that disclosure of accounts that show balance sheet insolvency is such an act.

[18] The proposition that these facts demand recognition of a new exception faces numerous hurdles both in relation to the idea of recognising a further common law exception, and then in relation to the proposition that there is a corporate equivalent to an act of bankruptcy. Were both of those obstacles to be overcome, the Minister would then need to establish that the facts of the case come within this newly-minted common law exception. We address each of these issues.

General observations

[19] The jurisprudence concerning these common law exceptions is more settled now than it has been for a number of years. Whilst there has been general agreement as to the list of so-called exceptions, uncertainty over the jurisprudential underpinning of the privilege itself resulted in dispute over whether new exceptions were possible and, if so, what circumstances were required in order to justify a further exception.[7]

[20] A clearer position has now emerged as a result of a series of decisions: *Unilever plc v The Procter & Gamble Co*,[8] *Ofulue v Bossert*[9] and *Oceanbulk Shipping and Trading SA v TMT Asia Ltd*.[10] We make three points which derive from these decisions.

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6 *Re Daintrey, ex parte Holt*, above n 2.

7 There remains a level of debate as to whether many of the established exceptions are truly exceptions or are better analysed as situations that do not attract privilege in the first place. For a judicial exposition of this latter approach see Hoffman LJ in *Muller v Linsley and Mortimer* [1996] PNLR 74 (CA) at 79. Otherwise see generally *Cross on Evidence*, above n 3, which has consistently been a proponent of this analysis. The present New Zealand statement is stated at [EVA57.9].

8 *Unilever plc v The Procter & Gamble Co* [2000] 1 WLR 2436 (CA) at 2442D.

9 *Ofulue v Bossert* [2009] UKHL 16, [2009] AC 990 at [85].

10 *Oceanbulk Shipping and Trading SA v TMT Asia Ltd* [2010] UKSC 44, [2011] 1 AC 662 at [24]. A fuller list of influential decisions is provided by Lord Clarke at [21].

[21] First, the common law "without prejudice" (or settlement negotiation) privilege, now reflected in s 57, is based on two considerations. The first is public policy, it being seen as an important value that parties to a dispute are encouraged to settle their differences. The other is recognition of an implied contract of confidentiality between the parties to settlement negotiations. Any proposal for a new exception needs to address why these considerations are outweighed in the circumstances coming within the proposed exception.

[22] Second, the list of existing exceptions is settled. The important exceptions were set out by Robert Walker LJ as he then was in *Unilever*.[11] Interestingly for present purposes, the act of bankruptcy exception was not included amongst them, although it is accepted that Robert Walker LJ's list was not exhaustive.[12]

[23] We note at this point that in *Sheppard Industries Ltd v Specialized Bicycle Components Inc* this Court held that although s 57(3) only lists some of the common law exceptions, the rest remain part of our law by virtue of s 12 of the Evidence Act.[13] This conclusion has not been without its critics,[14] but the parties accepted it correctly stated the law.

[24] Third, the categories of exception are not closed. A reliable summary of the current position is provided by Colin Passmore:[15]

> Although the courts recognise these exceptions, and although, the House of Lords has said the categories of exceptions are not closed (see Lords Rodger and Neuberger in *Ofulue v Bossert*), it has also made clear that any new exception must be scrutinised with care and only be recognised if justice clearly demands.
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> (Footnotes omitted.)

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11 *Unilever plc v The Procter & Gamble Co*, above n 8, at 2444.

12 He said so himself at 2445H. As noted in *Oceanbulk Shipping and Trading SA v TMT Asia Ltd*, above n 10, at [33], an omitted exception is established where there is an application to rectify a settlement agreement. The *Unilever* list and other exceptions are summarised by this Court in *Sheppard Industries Ltd v Specialized Bicycle Components Inc* [2011] NZCA 346, [2011] 3 NZLR 620 at [24].

13 At [15].

14 Richard Mahoney and others *The Evidence Act 2006: Act and Analysis* (3rd ed, Thomson Reuters, Wellington, 2014) at [EV10.01].

15 Passmore, above n 5, at [10–095]. The case referred to is *Ofulue v Bossert*, above n 9, at [38]–[40], [57] and [93].

[25] *Oceanbulk Shipping* is a recent example of a new exception, namely what is termed the "interpretation" exception.[16] In disputes over the meaning of a contract, evidence of the objective factual matrix relevant to interpretation is admissible.[17] In *Oceanbulk Shipping* it was held that this remains the position in relation to a settlement contract even though otherwise "without prejudice" privilege may apply.[18] The Court reasoned that the proposed exception would promote the public policy underlying the without prejudice rule by assuring parties that objective facts which emerge during negotiation will be admitted in order to ensure a correct interpretation of the settlement agreement is achieved.[19] In this way settlement will be encouraged. The case is an illustration of the new exception being justified by reference to the policy underlying the privilege itself.

[26] Before leaving a general discussion of the exceptions, it is necessary to comment briefly on one of the recognised exceptions, namely that which exists to address "unambiguous impropriety".[20] This general exception allows a court to prevent abuse of the privilege. It is not easy to establish as the label "unambiguous" emphasises, but that difficulty simply reflects the important value attached to the privilege and the protection it affords.[21] Despite the difficulty in meeting the test, the existence of this general exception is relevant to any consideration of the need for further exceptions.

The act of bankruptcy exception

[27] Turning then to the *Re Daintrey* exception, it is necessary first to briefly comment on the rules relating to personal bankruptcy. If a creditor applies to have a person declared bankrupt, it is necessary for the creditor to establish there has been "an act of bankruptcy".[22] What amounts to an act of bankruptcy is clearly defined and there are currently 12 identified situations in the Insolvency Act 2006.[23]

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16 *Oceanbulk Shipping and Trading SA v TMT Asia Ltd*, above n 10, at [36].
17 At [38].
18 At [40].
19 At [41].
20 This is the fourth of the exceptions in the list provided in *Sheppard Industries Ltd v Specialized Bicycle Components Inc*, above n 12, at [24].
21 See Passmore, above n 5, at [10–112].
22 Insolvency Act 2006, s 16.
23 These are contained in ss 17–28.

[28] One of these acts of bankruptcy is in s 22, which says it is an act of bankruptcy if a debtor notifies a creditor that the debtor has suspended or is about to suspend payment of the debt. That is what happened in *Re Daintrey*, the case which recognised the act of bankruptcy exception at issue in these proceedings.

[29] In *Re Daintrey* the debt was not disputed; rather, the debtor was struggling to pay. The debtor wrote on a without prejudice basis to the creditor suggesting a compromise and indicated that if it was not accepted, the debtor would suspend payments. The creditor initiated bankruptcy proceedings relying on the letter as an act of bankruptcy. The debtor claimed privilege but the Court held it was not available. The Court observed:[24]

> In our opinion the rule which excludes documents marked "without prejudice" has no application unless some person is in dispute or negotiation with another, and terms are offered for the settlement of the dispute or negotiation, and it seems to us that the judge must necessarily be entitled to look at the document in order to determine whether the conditions, under which alone the rule applies, exist. The rule is a rule adopted to enable disputants without prejudice to engage in discussion for the purpose of arriving at terms of peace, and unless there is a dispute or negotiations and an offer the rule has no application. It seems to us that the judge must be entitled to look at the document to determine whether the document does contain an offer of terms. Moreover, we think that the rule has no application to a document which, in its nature, may prejudice the person to whom it is addressed.

[30] Whilst the correctness of the decision has not been doubted, there has been considerable debate as to the basis for it. Robert Walker LJ in *Unilever* observed that, but for the last sentence, it is an uncontroversial example of a situation where privilege never attached.[25] That was also the view of Hoffman LJ in *Muller*.[26] However, the last sentence led some to describe a wider exception for circumstances where the communication prejudices the recipient.[27] It is not necessary in this case to consider the broader exception since the Minister's proposition is limited to a direct analogy to the bankruptcy situation. However, it is relevant to the expansion proposition that many doubt the facts of *Re Daintrey* require recognition of an

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24 *Re Daintrey, ex parte Holt*, above n 2, at 119–120.
25 *Unilever plc v The Procter & Gamble Co*, above n 8, at 2448.
26 *Muller v Linsley and Mortimer*, above n 7, at 77–80.
27 Passmore, above n 5, at [10–128]–[10–140] describes this as the prejudice exception and discusses its current uncertain boundaries.

exception.[28] We align ourselves with that view. The debt in *Re Daintrey* was not in dispute, nor were the terms of repayment. The letter was not properly to be seen as initiating settlement discussions and was not an occasion coming within the settlement negotiation privilege.

[31] Before drawing these threads together, we turn to the next obstacle the Minister faces: there is simply no corporate equivalent to an act of bankruptcy. The Minister relies on s 4(1) of the Companies Act 1993, which defines solvency in these terms:

> **4 Meaning of solvency test**
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> (1) For the purposes of this Act, a company satisfies the solvency test if—
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> (a) the company is able to pay its debts as they become due in the normal course of business; and
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> (b) the value of the company's assets is greater than the value of its liabilities, including contingent liabilities.

[32] However, whilst s 4(1) sets out the two limbs of solvency, that is not the test for when a company may be placed into liquidation on a creditor's application. The relevant test is found in s 241(4)(a) of the Companies Act and requires proof that the company is unable to pay its debts.

[33] Balance sheet insolvency is an item of evidence that may point to this test being met, but it does not establish the test. The balance sheets have nothing of the same character as the letter in *Re Daintrey*.[29]

[34] The reality is that a reason the exception recognised as long ago as 1893 has not to date been expanded to corporate insolvency is because there is no corporate equivalent to an act of bankruptcy. In this respect personal and corporate insolvency are different.

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[28] See for example *Cross on Evidence*, above n 3, at [EVA57.9].

[29] In the present case the uncontested evidence is that the company is paying its debts as they fall due.

[35] Mr Murray relies on *Law v James,* a decision of the New South Wales Court of Appeal, as authority for his proposition that the analogy he argues for is available.[30] In that case the Court transposed a bankruptcy rule, which provided that a person could not claim the benefit of a set-off if at the time they had notice of an available act of bankruptcy, into the corporate insolvency context. The Court amended the rule so that the issue became whether the person claiming the benefit of the set-off had notice of the presentation of a winding-up petition. However, the Court was prepared to do this because the relevant Companies Act expressly imported the Bankruptcy Act's rules governing the right to assert set-off into the winding-up context.[31] And the majority of the Court declined to describe the approach they took as resting upon an analogy between set-off in a bankruptcy or liquidation context, because the differences in the regimes made the analogy inapt.[32] Without that statutory mandate to transpose the concepts, we do not consider that it is possible to do so by way of analogy. We do not therefore see the case as assisting Mr Murray with his argument.

[36] Drawing all this together, we are satisfied that there is no case to extend the act of bankruptcy common law exception. On the specific level we do not consider a legitimate parallel exists between an act of bankruptcy as required by the Insolvency Act and the provision of accounts that disclose, for the period they deal with, balance sheet insolvency. The letter in *Re Daintrey* had a specific status in itself. It fulfilled the statutory requirement of an act of bankruptcy and does not need interpretation. The accounts here do none of those things; they just amount to helpful evidence. In that regard they are no different from most privileged communications an opponent wishes to use but cannot. Nor do we consider the particular facts highlight a situation where the privilege is being abused or the other party is being prejudiced. Any unfairness here lies more with the Minister's attempted use of the documents in other proceedings.

[37] On the general level we endorse the need for there to be convincing circumstances before recognising any further exceptions to the now-statutory

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30 *Law v James* [1972] 2 NSWLR 573 (CA).
31 At 576E.
32 At 577D.

settlement negotiation privilege. The public policy rationale underpinning the privilege is one of significant weight. Care is needed before an important tool in facilitating private settlement of disputes is further limited. It is also to be recognised that there are already exceptions of general applicability such as the unambiguous impropriety exception. These exceptions sufficiently provide scope to allow courts to prevent an abuse of the privilege.[33]

[38] Finally we observe that in our view there is little about the particular exception that suggests it should be given wider application. It deals with a unique requirement arising only in the law of bankruptcy.

Conclusion

[39] The High Court finding that the disclosure of the documents occurred in a situation of privilege was not challenged. The use by Reidy McKenzie of the documents to assist timetabling decisions did not, by a considerable margin, constitute waiver. The proposition that the common law exception for acts of bankruptcy should be extended to cover disclosure by a company of accounts that show balance sheet insolvency fails both because of the lack of a corporate equivalent, and because no good policy reason exists for such an expansion.

Result

[40] The appeal is dismissed. The appellants must pay the respondent costs for a standard appeal on a band A basis and usual disbursements.

Solicitors:
Meredith Connell, Auckland for Appellants
Daniel Overton & Goulding, Auckland for Respondent

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[33] Our discussion has proceeded on the assumption that, without holding it to be so, s 12 of the Evidence Act 2006 contemplates expansion of the common law as long as not inconsistent with the Act.