

## EQUITABLE CONTRIBUTION

### Introduction

This article looks at two recent cases which consider the doctrine of equitable contribution. In *Friend v Brooker*<sup>1</sup> the High Court considered fundamental questions respecting the nature and scope of the doctrine. In *Carr and Purves v Thomas*,<sup>2</sup> the New South Wales Court of Appeal discussed the differing impact of a release from liability as opposed to a covenant not to sue on the rights of equitable contribution as between company directors.

### *Friend v Brooker*

The relevant facts were:

- in July 1977 Mr Brooker and Mr Friend incorporated a company to carry on an engineering and construction business. Each of the men were directors of the company and controlled the shareholding equally;
- to finance the operations of the company, each of Mr Friend and Mr Brooker obtained personal loans from time to time which were then on-lent to the company and reflected in the loan accounts of the directors as unsecured loans;
- in November 1986 Mr Brooker obtained a personal loan of \$350,000 (the **SMK loan**) from a company called SMK Investments Pty Limited (**SMK**). \$330,000 of the loan was used to discharge company debts;
- the company ceased trading in 1990 and was deregistered in 1996. Mr Brooker and Mr Friend disputed who was responsible for the repayment of various loans, including the SMK loan.

Mr Brooker commenced proceedings in the Supreme Court in 2000 and sought, amongst other things, a declaration that a partnership or joint venture existed between Mr Brooker and Mr Friend. Mr Brooker sought an order for the taking of a full accounting of the partnership or joint venture. Mr Brooker was unsuccessful at first instance.<sup>3</sup>

By majority of Mason P and McColl JA (Basten JA dissented) the New South Wales Court of Appeal allowed Mr Brooker's appeal.

By unanimous decision, the High Court<sup>4</sup> allowed Mr Friend's appeal and ordered that Mr Friend was not required to make equitable contribution in respect of the SMK loan. The High Court held that, based on the trial judge's findings, the basic characteristics of the doctrine of equitable contribution (summarised below) were not satisfied. The High Court went on to reject that the notion of 'common design' (favoured in particular by Mason P in the Court of Appeal) could provide a basis for equitable contribution.

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<sup>1</sup> [2009] HCA 21.

<sup>2</sup> [2009] NSWCA 208.

<sup>3</sup> *Brooker v Friend & Brooker Pty Ltd* [2005] NSWSC 395. Decision of Nicholas J.

<sup>4</sup> By joint judgment of French CJ, Gummow, Hayne and Bell JJ, with whom Heydon J agreed in a separate judgment. Heydon J provided an additional and independent ground for allowing the appeal, being in effect that there had been procedural irregularity in the proceedings before the Court of Appeal. This article does not further refer to this ground of appeal.

The High Court's key points about the principles governing the doctrine of equitable contribution include:

- the equity to seek contribution arises because the exercise of a creditor's rights ought not disadvantage some of those debtors bearing a common burden. While equity, like the common law, does not seek to direct the manner in which the creditor exercises its rights, it does make an adjustment between the debtors to ensure the sharing of the burden between those subjected to the creditor's action;<sup>5</sup>
- the doctrine requires that there be 'contribution between parties sharing co-ordinate liabilities or a common obligation to make good the one loss, where the liabilities were of the same nature and to the same extent';<sup>6</sup>
- the 'community of interest' which may be a basis for equitable contribution must be something which has its source in a common burden imposed by law. A plaintiff's entitlement to equitable contribution from a defendant 'must arise from the operation of law upon their situation, not by some looser notion of economic interest which disregards or supersedes the legal framework within which the parties chose to have their dealings';<sup>7</sup>
- the rights of contribution are not attracted 'merely because they are owed to the same party and related to the same transactions or otherwise connected in time or circumstance'<sup>8</sup> and the doctrine is not enlivened merely because one parties' payment operates to the financial benefit or relief of the other party.<sup>9</sup>

The High Court found that the absence of a 'common legal burden' presented a 'major difficulty' against the application of the doctrine of equitable contribution. It was noted that SMK had not contracted with Mr Friend and Mr Brooker had not contracted with SMK as trustee for himself and Mr Friend. Also of significance was the trial judge's rejection that the relationship between the parties was one of partnership or joint venture or 'some other relationship which gave rise to an entitlement to an accounting'.

### **'Common design'**

In the Court of Appeal decision, Mason P had found that Mr Brooker could overcome the above mentioned difficulties by relying on a purported category of contribution based upon 'common design', which was said to obviate the need for exposure to a common legal obligation.

The final formulation of the notion of common design, presented by Mr Brooker's counsel to the High Court was as follows:

'Contribution will be enforced where the party seeking it has, by reason of and reliance on a common design with the party from whom contribution is sought, undertaken a risk or expense which:

- a was undertaken with the knowledge and assent of that other party;
  - b was undertaken in order to effectuate or facilitate the common purpose or benefit which was the object of their common design;
  - c in light of the parties' relationship and the nature of their common design, could not fairly be expected to be borne as a burden alone by the party undertaking it;
- and there is no contract to the contrary.'

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<sup>5</sup> *Friend v Brooker*, [38]

<sup>6</sup> *Friend v Brooker*, [40], citing *Burke v Lfot Pty Limited* [2002] HCA 17, which is said to have identified the basic characteristics of the doctrine 'with reference to long established authority'.

<sup>7</sup> *Friend v Brooker*, [46]

<sup>8</sup> *Friend v Brooker*, [48] citing French J in *Re La Rosa; Ex Parte Norgard v Rodpat Nominees Pty Ltd* [1991] 31 FCR 83 at 91

<sup>9</sup> *Friend v Brooker*, [48]

The High Court noted that there was at least a significant evidentiary obstacle in that it was not open for the Court of Appeal or the High Court to make any finding about element 'c' of the formulation referred to above.

The Court went on to say that further and 'as an additional ground of decision' (which is presumably a pointed understatement) the suggested principle of common design is 'not the law of Australia'.<sup>10</sup> In rejecting this suggested principle the joint judgment reviews the authority<sup>11</sup> relied upon by Mason P and finds that it was an 'infirm foundation' for the existence of any such principle when properly analysed.<sup>12</sup>

### ***Carr v Thomas***

In *Carr v Thomas*, Resource Equities Limited (**REL**) commenced proceedings against its directors asserting that they had breached directors' duties owed to REL. One of the directors (the respondent) had entered into a "settlement deed" with REL which provided that the respondent and REL agreed to resolve the REL proceedings between them. It also provided that nothing in the deed was intended to affect or compromise in any way the REL proceedings as against any defendant other than the respondent.

By cross-claim in the proceedings, the other directors (the appellants) sought equitable contribution from the respondent alleging that he owed the same duties to REL as were alleged against the appellants and had breached those duties in the same manner as REL alleged against the appellants.

At first instance, McDougall J granted the respondent's motion and summarily struck out the cross claim on the basis that the settlement deed released the respondent from any liability which he might have had to REL in relation to the subject matter of the proceedings and, accordingly, he and the appellants had no coordinate liability to REL.

The Court of Appeal<sup>13</sup> granted the appeal, overturning the first instance decision. This meant that it was open to the appellants to seek equitable contribution from the respondent, subject to satisfying the requirements of the doctrine.

In coming to this inclusion the Court of Appeal noted:

- there is a general rule that where a creditor releases one or some of a number of debtors jointly and severally liable for the same debt, then all debtors are released;<sup>14</sup>
- a covenant not to sue does not act as a release of a party's obligations. It is a contract that one party will not sue the other.<sup>15</sup>

The Court of Appeal held that the "settlement deed" between the respondent and REL was clearly a covenant not to sue. It was further held that the covenant not to sue did not release or extinguish the respondent's liability to REL. Therefore, if it could be established that the respondent's liability was a coordinate liability then the appellants were still entitled to claim contribution from the respondent.

### **Conclusion**

In *Friend v Brooker* the High Court confirms that the doctrine of equitable contribution requires that there be contribution between parties who share co-ordinate liabilities to make good the one loss, where the liabilities are of the same nature and to the same extent. For equitable contribution to apply the parties must first be under a common burden. The Court of

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<sup>10</sup> *Friend v Brooker*, [66]

<sup>11</sup> *Cummings v Lewis* (1993) 41 FCR 559

<sup>12</sup> The High Court's analysis in this regard is set out at [67] to [83] of the joint judgment

<sup>13</sup> Beazley JA, Ipp JA and McColl JA in a joint judgment

<sup>14</sup> *Walker v Bowry* [1924] HCA 28

<sup>15</sup> *Carr v Thomas*, [34]-[36]

Appeal's attempt to get around these requirements by relying on a category of contribution based upon 'common design' was rejected.

*Carr v Thomas* highlights an important difference in the uses of either a release of a party from liability or of a covenant not to sue. Those differences can impact not only on the legal position as between the parties to the release or covenant not to sue, but also on the applicability of the doctrine of equitable contribution as between co-defendants, and the liability of co-defendants to the plaintiff. In cases, for example where co-directors are sued, where proceedings against one of the directors are disposed of by means of a covenant not to sue, the remaining directors in the proceedings may still be entitled to equitable contribution from the "released" defendant, subject to satisfying the requirements of the doctrine of equitable contribution. But if the creditor has released one of several directors who are jointly and severally liable, this may operate to release all directors.

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