Divining an Approach to the Duty of Care: The New Zealand Court of Appeal and Claims for Negligent Misstatement

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I Introduction

One of the recurrent problems in the law of negligence has been how to describe an approach to the duty of care in a case that is not directly covered by previous authority (the "duty question"). It is not a problem the New Zealand Court of Appeal has found easy to resolve.[1] A number of contradictory approaches has been suggested over the years, often by the same judges.[2] Yet since at least 1992, the Court has united behind a unique and indigenous approach to the duty question, described most influentially by Richardson J in *South Pacific Manufacturing Ltd* v *New Zealand Security Consultants & Investigations Ltd*.[3] On this approach, the ultimate question is whether it is just and reasonable to impose a duty of care, a question that is answered by reference to broad inquiries into proximity and policy. Throughout this article I describe this as the "conventional" approach.[4] While some may criticise the utility of this approach in terms of providing an objective standard against which the duty question can be assessed, it has at least had the value of a consistent application to a variety of duty situations, and an apparent widespread acceptance by members of the Court.[5]

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1 New Zealand has not been alone in its problems. The difficulties the English Courts have experienced are well known. The approach originally suggested in *Anns* v *Merton London Borough Council* [1978] AC 728 (HL) was, after a long period of mumbled dissatisfaction, rejected by the House of Lords in *Caparo Industries PLC* v *Dickman* [1990] 2 AC 605. However as cases such as *White* v *Jones* [1995] 2 AC 207 (HL) and *Spring* v *Guardian Assurance PLC* [1995] 2 AC 296 (HL) demonstrate, the substance of the English approach is by no means clear. For a recent discussion of some of the problems encountered in Australia see J Davies, "Liability for Careless Acts or Omissions Causing Purely Economic Loss: *Perre v Apand Pty Ltd*" (2000) 8 Torts Law Journal 123.

2 For example, compare the approach of Richardson P in the following cases: *Gartside* v *Sheffield, Young & Ellis* [1983] NZLR 37; *Takaro Properties Ltd* v *Rowling* [1986] NZLR 22; *First City Corporation Ltd* v *Downsview Nominees Ltd* [1990] 3 NZLR 265; *South Pacific Manufacturing Co Ltd* v *New Zealand Security Consultants & Investigations Ltd* [1992] 2 NZLR 282; *McKay Hill & Co* v *Eksteen & Eksteen* unreported, Court of Appeal, 30 May 2000, CA 161/99.

3 Ibid at 305 - 306 [*South Pacific Manufacturing*].

4 This is the description used in *Price Waterhouse* v *Kwan* [2000] 3 NZLR 39 at 41 per Tipping J. See also *Morrison* v *Upper Hutt City Council* [1998] 2 NZLR 331 at 336 per Richardson P.

5 For example *Connell* v *Odlum* [1993] 2 NZLR 527 at 535 per Thomas J; *Fleming* v *Securities Commission* [1995] 2 NZLR 514 at 526-527 per Richardson J; *Wilson & Horton Ltd* v *AG* [1997] 2 NZLR 513 at 520 per Hammond J; *Morrison* v *Upper Hutt City Council*, ibid at 336 per Richardson P; *AG* v *Prince & Gardner* [1998] 1 NZLR 262 at 268 per Richardson P; *B* v *Attorney-General* [1999] 2 NZLR 296 at 300–301 per Keith and Blanchard JJ.

Or so we thought. In a number of recent decisions involving claims of negligent misstatement,[6] the Court of Appeal has adopted an alternative approach to the duty question based on the decision of the House of Lords in *Hedley Byrne Co Ltd* v *Heller & Pts Ltd*.[7] That case set three necessary requirements for liability – the possession of special skill or knowledge by the defendant, an assumption of responsibility by the defendant in making the statement, and reasonable reliance by the plaintiff on the statement by the defendant. I refer to these as the *Hedley Byrne* criteria.[8] These cases present two problems. First, the *Hedley Byrne* criteria are not treated as simply considerations to be weighed under the inquiries into proximity or policy, but are treated as *exclusive determinates* of the duty question. The necessity of these criteria, and the restricted sense in which they are used, suggest a substantially narrower basis of liability in these cases than that of the conventional approach. Second, these cases have applied the *Hedley Byrne* criteria to the duty question without any reference to the conventional approach. No explanation is given for why the Court prefers the *Hedley Byrne* approach over that of the conventional approach. The result is that there is now real uncertainty as to how the Court of Appeal will deal with a case involving a claim of negligent misstatement. Different approaches seem open to the Court, and the approach adopted seems to make a difference to the result, but there is no apparent way to predict which approach will be taken in any particular case.

In this article I consider this uncertainty. I first consider two recent Court of Appeal decisions on negligent misstatement, *Price Waterhouse* v *Kwan*[9] and *Turton* v *Kerslake*.[10] These two similar cases were resolved by fundamentally different approaches to the duty question. They suggest the possibility of real inconsistency and uncertainty in the approach to the duty question in cases of negligent misstatement. I then consider the broader context of these two decisions, and the lines of authority each case represents. It is clear that the problem apparent in the decisions in *Price Waterhouse* v *Kwan* and *Turton* v *Kerslake* is not simply a conflict in two individual cases, but reflects a deeper and developing inconsistency between two established lines of authority. In the final part of the article I consider and reject some arguments that could be made to explain or minimise this apparent conflict.

As is probably clear, this article has limited aspirations. I do not argue that one approach to the duty question is to be preferred over another. My purpose is to emphasise that there should be only one approach, and to highlight the unacceptable level of uncertainty that now exists in this important area of

6 *Brownie Wills* v *Shrimpton* [1998] 2 NZLR 320; *Boyd Knight* v *Purdue* [1999] 2 NZLR 278; *McKay Hill* v *Eksteen* unreported, Court of Appeal 161/99 30 May 2000; *R M Turton & Co Ltd (in liq)* v *Kerslake &* Pts [2000] 3 NZLR 406.

7 [1964] AC 465 [*Hedley Byrne* v *Heller*].

8 The exact basis of liability under *Hedley Byrne* v *Heller* is not entirely clear from the decision. Perhaps the most widely recognised statement of the requirements of liability is in the judgment of Lord Morris at 502-503. However, regardless of the specifics of the decision, at the very least the case is broadly recognised as raising the three essential elements for liability as suggested above. These are also the general criteria suggested in *Turton* v *Kerslake* [2000] 3 NZLR 406 at 415 per Henry & Keith JJ.

9 [2000] 3 NZLR 39.

10 [2000] 3 NZLR 406.

negligence law. To an extent this article continues the theme explored in the last issue of this review, and the importance of certainty in the law.[11] The criticism I make, however, is more fundamental than the lack of predictability in substantive results; any conception of certainty in the law requires as a minimum consistency in approach.

II A Conflict in Two Cases

Claims of negligent misstatement causing economic loss, involving for the most part allegations of professional negligence, are some of the most widely litigated negligence actions in New Zealand. With the number of Court of Appeal decisions in the area over the last 20 years, one would have thought that the approach to such cases would be reasonably settled. However, in the last two years it has become apparent that this may not be the case. *Price Waterhouse* v *Kwan* and *Turton* v *Kerslake* are two recent cases that seem to suggest that the approach to such cases is anything but clear. In this part of the article I wish to introduce the problem of the inconsistent approaches to the duty question in cases of negligent misstatement by reference to these two decisions.

Price Waterhouse v *Kwan*

Vickerman, Cuttance and Johnston were partners in the law firm Salek Turner & Cuttance (the solicitors).[12] They operated a solicitors' nominee company, through which funds belonging to the plaintiffs and other clients of the firm were invested (the clients). The trust account of the solicitors, which included the accounts of the nominee company, was subject to audit in the manner set out in the *Solicitors Audit Regulations* 1987 (the *Audit Regulations*).[13] That audit report was prepared for the Law Society, which could intervene in the affairs of the solicitor if they thought such action was warranted. The auditor appointed by the Law Society for the purposes of this statutory audit was Price Waterhouse (the auditor). It is not clear what happened to the funds of the nominee company. It would appear that funds were placed into mortgages that subsequently became valueless, and that the solicitors failed to account in full for monies paid to them.[14] It also appears that Cuttance was convicted of charges of theft and the falsification

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11 "Symposium Issue on Certainty and the Law" (2000) 9 OLR no. 4.

12 One of the difficulties with the decision in *Price Waterhouse* v *Kwan* is that neither the judgment of the High Court (*Kwan* v *Price Waterhouse; Hughes* v *Price Waterhouse* unreported, High Court, Wellington, 19 March 1999, CP 214/98 & CP 188/98, Master Thomson) nor that of the Court of Appeal contain a full summary of the facts that gave rise to the claim. In addition to the proceedings in the High Court and Court of Appeal, some information can be gathered from an earlier case arising out of the same events *Johnston* v *The Partnership of Price Waterhouse; Cooper* v *The Partnership of Price Waterhouse* unreported, High Court, Wellington, 26 May 1995, CP 348/93 & CP 331/94, Master Thomson. These proceedings were accepted by Master Thomson as raising no "discernible factual difference" to the proceedings in *Price Waterhouse* v *Kwan*.

13 (SR 1987/33). Now replaced by the *Solicitors' Trust Account Regulations* 1998 (SR 1998/17).

14 See *Johnston* v *Price Waterhouse* unreported, High Court, Wellington, 26 May 1995, CP 348/93 & CP 331/94, Master Thomson at 3.

of records.[15] Regardless of the cause, substantial losses were suffered by the clients, and it was apparent that the solicitors would be unable to meet those losses.[16] A number of clients including the plaintiffs in these proceedings brought claims against Price Waterhouse, arguing that if they had properly audited the accounts of the solicitors, the Law Society would have intervened in the affairs of the solicitor, and the clients' losses would have been recognised and avoided. The auditor applied to strike out the plaintiffs' statements of claim on the basis that it did not owe a duty of care to the clients of the solicitor whose trust account it was auditing. This argument was unsuccessful in the High Court,[17] and the defendant appealed that decision.

The judgment of the Court, comprising Gault, Keith and Tipping JJ, was given by Tipping J. He approached the duty question by what he termed the "conventional inquiry"; that is, whether it was "fair, just and reasonable" to impose a duty of care, an inquiry driven by consideration of the issues of proximity and policy.[18] In this case, the proximity inquiry was resolved largely by his view of the purpose of the statutory audit scheme. That purpose was "to initiate steps both in the interests of the clients of the solicitor and in the interests of the good government of the profession",[19] and later, "to protect the solicitors' clients from loss as a result of improper conduct in relation to the solicitors' trust account".[20] Given his conclusion on the purpose of the audit, he had little difficulty in concluding that there was a proximate relationship in this case.[21]

> In our view, clients of a solicitor are entitled to rely generally on the audit regime, and specifically on the individual auditor to conduct the audit with due care and skill. Reasonable auditors will realise that such reliance is being placed upon them. They must accordingly be deemed to have assumed the responsibility envisaged by such reliance. In these circumstances we consider that the clients have shown, prima facie at least, that the proximity requirement for a duty of care in tort is satisfied.

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15 Ibid at 4.

16 It is not clear whether the solicitors were actually insolvent. In the *Johnston* proceedings, ibid, it appears that an agreement was reached between the solicitors and the clients whereby the solicitors would fund the proceedings against Price Waterhouse in return for them not being sued, or at least not immediately. See the interlocutory decision in *Johnston* v *Price Waterhouse* unreported, High Court, Wellington, 18 June 1996, CP 348/93 & CP 331/94, McGechan J at 2.

17 *Kwan* v *Price Waterhouse* unreported, High Court, Wellington, 19 March 1999, CP 214/98 & CP 188/98, Master Thomson. In the High Court proceedings at least, there was also an application by the Hughes plaintiffs to strike out the defendant's application to strike out the proceedings. It is not clear whether this was pursued in the Court of Appeal.

18 [2000] 3 NZLR 39 at 41.

19 Ibid at 43. The reference to the initiation of steps, one assumes, is to the powers of investigation and intervention of the Law Society under Part V of the Law Practitioners Act 1982.

20 Idem.

21 Idem.

It is important to recognise the use that was made of the concepts of reliance and assumption of responsibility. Knowledge of, or specific reliance on, the audit process by the clients was not necessary. Rather, clients were entitled to rely in a general sense on the existence of the audit regime to ensure that any misuse of funds, or thefts from the trust account, did not take place or was at least quickly detected. Likewise, the assumption of responsibility by the auditor was "deemed" and derived simply from the foreseeability of a general reliance by clients on the audit regime. There was no suggestion of specific knowledge on the part of the auditor of any reliance that might be placed on the audit by the clients.

Having concluded that there was a sufficient relationship of proximity, and a prima facie duty of care, Tipping J considered whether there were any arguments of policy that may negate or support the existence of such a duty. The primary argument by the auditor was that as a matter of policy, recognising a duty of care would circumvent an existing contractual structure between the auditor and the solicitors, and the solicitors and the clients (referred to in the judgment as the "contractual matrix" argument). Justice Tipping rejected this argument. It was based, in his view, on a misconceived notion that there could be no concurrent liability in contract and tort.[22] The plaintiff was not limited to its contractual claim against the solicitor, as it was also entitled to bring a claim in tort. The contractual matrix argument, accordingly, "breaks down at the outset".[23] Nor did he believe that there was any good policy reason to deny a prima facie duty of care on the basis of a prospective remedy that was known to be ineffective due to the insolvency of the solicitor.[24]

> To hold that a party who enjoys sufficient proximity with A to raise a prima facie duty of care in tort should be confined to a contractual remedy against B, when the efficacy of that remedy is dubious, hardly seems a good policy reason for denying the existence of a duty of care in A. There may be circumstances in which the legislative or other environment governing the relationship of the parties supports the view that the presence of a contractual right against B militates against there being a parallel tortious right against A for the same damage. Such a conclusion might rest on general matters of express or implied intention or on matters of policy. Such is not the position in the present case.

In addition to the general unattractiveness of the contractual matrix argument, in circumstances where the contract was unlikely to provide an effective remedy, Tipping J suggested further policy reasons that supported the imposition of a duty of care. Most important was the desire to create an effective and direct remedy for the client, and to ensure that the auditor was not immune from the consequences of its actions. If the client sued the solicitor, any claim by the solicitor against the auditor would likely be subject to substantial reductions for

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22 The decision is a clear recognition of the principle of concurrent liability in tort and contract. The Court describes its earlier decision in *Maclaren Maycroft & Co Ltd* v *Fletcher Developments Co Ltd* [1973] 2 NZLR 100 as "having been overtaken by later developments". Ibid at 44.

23 Idem.

24 Idem.

contributory negligence by the solicitor. The only claim that would ensure that the auditor was fully responsible for the consequences of its action was one brought by the Law Society, but the Court believed that such a claim would only be brought if the Law Society was first sued by the client. Rather than relying on the complexities or vagaries of these possible avenues of recovery, the Court thought it easier to allow the client to make its claim directly against the auditor.

The decision in *Price Waterhouse* v *Kwan*, in terms of the result, does seem remarkable. The conclusion that an auditor owes a duty of care to the client of a solicitor is difficult to reconcile with the approach the Court has taken in analogous situations, particularly those involving audits of financial accounts.[25] Likewise, the description by the Court of the regulatory regime, and its conclusion that the purpose of the audit is to protect clients from loss, is debateable.[26] However the focus of this article is on the approach taken to the duty question in cases of negligent misstatement, and the approach of the Court in this case was to ask itself whether it was fair, just and reasonable to recognise a duty of care, a question it answered by reference to the two inquiries into proximity and policy. The proximity inquiry was satisfied by the statutory purpose of the audit regime, and the foreseeability of harm to the plaintiff. There were no policy reasons to negate this *prima facie* duty, and indeed strong policy reasons to support it. The Court was not constrained in answering either of these questions by a necessary consideration of any particular factor, including the *Hedley Byrne* criteria.

Turton v *Kerslake*

Two weeks after argument in *Price Waterhouse* v *Kwan*, a different panel of the Court of Appeal (although still including Keith J) heard the appeal in *Turton* v

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25 Compare *Boyd Knight* v *Purdue* [1999] 2 NZLR 278. Even the decision in *Scott Group* v *MacFarlane* [1978] 1 NZLR 553 did not recognise a general duty on the part of an auditor to shareholders and investors in a company. On the basis of the judgment of Cooke J, the duty of care was limited to situations where the investor was a potential substantial shareholder, and the accounts showed a clear risk of a takeover bid being made.

26 The review of the regulatory regime by the Court is at times inaccurate, and ignores some of the most important features of that regime. For example, contrary to the Court's conclusion, the fees for an audit cannot be paid by clients of a nominee company. (*Nominee Company Rules*, reg 5.4). They must be met by the directors of the nominee company, who are the partners of the firm of solicitors. (NZLS, "Solicitors Nominee Company Rules and Contributory Mortgages" (1988), "Notes for Guidance of Solicitors", note 7 (a)). Also the report by the auditor is expressly made only to the Law Society, and it is up to the Law Society to decide if any matter raised in that report warrants further investigation or intervention. (*Audit Regulations*, reg. 63). The auditor has no right to disclose any information learned in the course of the audit to any person, including the clients, without the permission of the Law Society. (*Audit Regulations*, reg. 66). To do so is a criminal offence. (*Audit Regulations*, reg. 71). The list goes on. It is certainly arguable that the sole purpose of the audit regime is to assist the Law Society in exercising its powers of investigation and intervention under Part V of the Law Practitioners Act 1982.

Kerslake. Like *Price Waterhouse* v *Kwan*, the claim was one for negligent misstatement where the main argument by the defendant was that imposing a duty of care would be inconsistent with the contractual relations the parties had assumed, but also where confining the plaintiff to its contractual claim was not likely to provide an effective remedy, due to the insolvency of some of the contracting parties. The Southland Area Health Board (the Board) decided to build a new hospital near Queenstown. It employed a firm of architects to design the building, to supervise tendering for the construction project, and also to supervise construction. The architects in turn hired Kerslake, an engineering firm, to provide expert advice on the engineering aspects of the project, including preparation of the mechanical services specification and subcontract. At issue in the case was the specification in the mechanical services section of the contract for the heat pumps to be used in the hospital. That specification provided precise details of the type of heat pump to be used, including componentry, and the level of output they would achieve.

Turton was the successful tenderer for the construction project. Its accepted tender specified George Mechanical as the subcontractor for the mechanical services section of the contract, and the heat pumps to be installed as in the original tender specification prepared by Kerslake. Unfortunately, the heat pumps when installed were unable to achieve the required level of output. Turton was required to spend approximately $74,000 modifying the system so that it could meet the required output. By this time, George Mechanical and the manufacturer of the heat pumps were in liquidation. Turton accordingly brought claims against the Board, the architect, and Kerslake to recover the cost of the remedial work, and interest on progress payments that had been withheld. The issue in this case concerned its claim in negligence against Kerslake. It was unsuccessful in that claim in both the District Court and the High Court,[27] on the basis that Kerslake did not owe Turton a duty of care in preparing the specification. Leave was granted to appeal. By a majority of 2 to 1 (Thomas J dissenting), the Court of Appeal rejected Turton's appeal.

The majority of Henry and Keith JJ delivered a joint judgment. That judgment was concerned with the same two questions that arose in *Price Waterhouse* v *Kwan*, namely the approach to the duty question in cases of negligent misstatement and the relevance of the contractual matrix. The approach of the majority, however, stands in sharp contrast to that in *Price Waterhouse* v *Kwan*. The majority based their approach on the decision in *Hedley Byrne* v *Heller*, and the *Hedley Byrne* criteria. Under that approach, the important questions were "was the defendant possessed of a special skill, did it undertake to apply that skill for the assistance of another person, and did that person rely on it and suffer loss as a result of the defendant's breach of its duty of care in applying that skill?"[28] Applying those factors to the case before them, the Court did not think the plaintiff was able to satisfy these criteria. The majority doubted that as between Turton and Kerslake, Kerslake possessed any special skill. Kerslake relied on the manufacturer of the heat pumps with regard to their ability to achieve certain outputs, as did Turton and its subcontractor. Nor was there any

27 *R M Turton & Co Ltd* v *Southland Area Health Board* unreported, High Court, Invercargill, 16 June 1999, NP 2804-92, Pankhurst J.

28 [2000] 3 NZLR 406 at 415.

assumption of responsibility by Kerslake, or reliance by Turton. Turton did not approach Kerslake regarding the information contained in the specification, nor did it indicate to Kerslake that it was relying on that information. Rather, it relied on its subcontractor, George Mechanical, with regard to the capabilities of the heat pump, who in turn probably relied on the manufacturer of the heat pumps.

The majority also emphasised the importance of the contractual relationships that each party had assumed. Under those contracts, there was a clear allocation of risk between the parties in respect of the accuracy of the specification. As between the Board and Turton, it was clear that Turton was contractually bound to provide the heat pumps as per the specification, an obligation that was not affected by the subcontracting of part of that work to General Mechanical. It was up to Turton, and in particular General Mechanical, to satisfy themselves that they were able to perform the terms of their contract and subcontract. On the other hand, the contract under which Kerslake carried out its work contained a number of specific disclaimers of liability, including liability arising from "any errors in or omissions from data, documents, plans, designs or specifications not prepared by the Consulting Engineer". In addition, any liability that Kerslake did have was limited to "direct loss or damage" and subject to time limits for notification and quantum limitations, while disputes under the contract were to be referred to arbitration. Recognising a duty of care in these circumstances "would cut across and be inconsistent with the overall contractual structure which defines the relationships of the various parties to this work, and in the circumstances of this case would not be fair, just or reasonable to impose the claimed duty of care".[29]

The majority judgment concludes with an important comment on the relevance of policy considerations to the existence of a duty of care in such cases:[30]

> It is necessary to make a further observation. There are, here, no broad policy issues to be considered. In a case such as this, therefore, we would not endorse the concept of a two-stage inquiry, which somehow first considers the general criteria (possession of skill, foreseeability, reasonable reliance) as establishing a prima facie duty of care, and then goes on to consider whether the contractual matrix negates the prima facie duty. There is no prima facie duty in that sense. The imposition of the duty will depend upon a consideration of all the circumstances, which must include the contractual matrix. The criteria cannot properly be considered in its absence.
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> The test is based on broad formulations including fairness, reasonableness and justice. In considering those concepts the Court must examine the whole of the circumstances and the relationship between the parties. This examination is usefully focused on the relevant matters by inquiring into factors such as those mentioned in the preceding paragraph, but in the end the Court must be satisfied that the relation is such that there has been an undertaking of responsibility to the particular plaintiff and the imposition of a duty of care is justified. In a case such as the present this cannot be done without considering the various contractual

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29 Ibid at 417.

30 Ibid at 418. The reference appears to be in response to the Supreme Court of Canada's decision in *Edgeworth Construction Ltd* v *N D Lea & Associates Ltd* (1993) 107 DLR (4th) 169, where an engineer preparing specifications for a tender was held to owe a duty of care to the successful tenderer.

> rights and obligations. In a comprehensive contractual situation such as existed here, the Court should be hesitant to go beyond that relationship. A tortious duty of care outside that framework, but affecting the rights and liabilities of the various separate parties coming within the very contractual setting, should not lightly be imposed.

This comment will be discussed in more detail later,[31] but it suggests that in cases of negligent misstatement, at least where there are existing contractual structures in place, a two stage approach such as that adopted in *Price Waterhouse* v *Kwan* is not appropriate. Also, contrary to the decision in *Price Waterhouse* v *Kwan*, the majority concluded their judgment by emphasising that they did not see any relevance in the fact of the insolvency of many of the parties to the contractual structure. The possibility of insolvency was a known risk that Turton accepted when contracting with its subcontractor.[32]

There is an interesting albeit lengthy dissent by Thomas J. Like the majority, he regarded the case as one of negligent misstatement, to be resolved by reference to the *Hedley Byrne* criteria.[33] But his treatment of those criteria involved some important differences. First, he viewed those criteria as simply a more precise expression of the conventional approach in cases of negligent misstatement. The *Hedley Byrne* criteria had subsumed within them the inquiries necessary under the conventional approach. So, for example, if a defendant with necessary expertise made a negligent representation knowing that the plaintiff is likely to rely on it and the plaintiff did in fact rely on it to his or her detriment, foreseeability and proximity would be established.[34] Likewise, policy considerations were to a significant extent overtaken by the *Hedley Byrne* criteria because it had already been decided, as a matter of policy, that where those factors are established, a cause of action should exist.[35] Second, the existence of a contractual structure was of only minimal relevance, less even than that suggested by the Court in *Price Waterhouse* v *Kwan*. In his view, contract terms would only be relevant if they expressly excluded the alleged tortious relationship between the plaintiff and defendant. Simple inconsistency with the alleged duty of care was not sufficient. Against this background, and disagreeing with the majority on some of the inferences to draw from the facts, he had little difficulty in determining that the *Hedley Byrne* criteria had been satisfied in the case. He also noted broader policy considerations that in his view supported the imposition of a duty of care, in particular the commercial reality of the tendering process for large construction projects. In his view, it was unrealistic in that context to say that the risk of any inaccuracies in the specification should rest with the contractor rather than the person preparing the specification.

Some comment is necessary at this point on the approach taken by the majority in *Turton* v *Kerslake*. Their decision stands in sharp contrast to the approach of the Court in *Price Waterhouse* v *Kwan*. It in fact rejects that approach at almost every level. First, the majority does not endorse the view that the ultimate

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31 Infra notes 36 to 38 and accompanying text.
32 [2000] 3 NZLR 406 at 418
33 Ibid at 419.
34 Ibid at 426.
35 Idem.

question is whether it is fair, just and reasonable to impose a duty of care. For them, the question is whether there has been an undertaking of responsibility to the particular plaintiff and whether the imposition of a duty of care is "justified".[36] Questions of "fairness, reasonableness and justice" are simply "broad formulations on which the test is based".[37] Second, the Court rejects the use of the two broad inquiries into proximity and policy, and in particular the reference to policy factors. The focus of the inquiry, on the approach of the majority, is solely on the relationship between the parties understood by reference to the *Hedley Byrne* criteria.

There is no doubt that the decision represents a narrower approach to the duty question in cases of negligent misstatement than that in *Price Waterhouse* v *Kwan*. While the Court claims that the *Hedley Byrne* criteria are not to be treated as a "test" of liability,[38] ultimately it is an application of those factors that determines the result in the particular case. The clear implication from the judgment is that in the majority of negligent misstatement cases, it will be necessary for the plaintiff to establish the *Hedley Byrne* criteria, and if it is unable to do so, no duty of care will be recognised.

We should also recognise the way in which the *Hedley Byrne* criteria are used. In this case, they reflect a narrow, factual inquiry into the specific relationship between the plaintiff and defendant, and the inferences of fact that can be drawn from their conduct. For example, Kerslake could not have assumed a responsibility to Turton in circumstances where it had dealt with the possibility of any disputes or inaccuracies in the specification in its contract with the architect. Likewise, Turton could not have reasonably relied on Kerslake in circumstances where it had itself assumed responsibility for the accuracy of that specification in its contract with the Board, and had relied on its own subcontractor to ensure the accuracy of the specification. The *Hedley Byrne* criteria in *Turton* v *Kerslake* are used in a narrow and restricted sense, focused solely on the relationship between the parties and the inferences that can be drawn from their conduct.

Summary

Price Waterhouse v *Kwan* and *Turton* v *Kerslake* are cases that appear to take a fundamentally different approach to the same problem. Both were negligent misstatement cases involving similar issues. Yet in one case, adopting what the Court described as the "conventional" approach, the plaintiff was successful in its claim, while in the other, adopting an approach based on the *Hedley Byrne* criteria, the plaintiff failed. Neither decision makes reference to the approach used in the other, nor do they suggest any reason why one approach was preferred over the other. On the face of the decisions, there is clearly an inconsistency in approach, which in the absence of some explanation by the Court, creates real uncertainty as to how any future case involving a claim of negligent misstatement will be resolved.

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36 Ibid at 418.
37 Idem.
38 Ibid at 409.

III Divergent Lines of Authority

In this part of the article I want to demonstrate that the problem apparent in these two cases is illustrative of a deeper problem that exists in the general approach of our Court of Appeal to cases of negligent misstatement. The approach in *Price Waterhouse* v *Kwan* reflects the distinctive approach the Court has taken over the last 20 years to establishing duties of care. It is an approach derived from the House of Lords decision in *Anns* v *Merton Borough Council*,[39] and has developed as a separate and more expansive approach to negligent misstatement cases than that taken in *Hedley Byrne* v *Heller*. *Turton* v *Kerslake*, however, is one of a number of recent decisions of the Court of Appeal that have determined the duty question by an almost exclusive reference to the *Hedley Byrne* criteria, ignoring the conventional New Zealand approach. These cases appear to signal the re-emergence of negligent misstatement as a separate category of negligence claims. Rather than being an isolated example of a division of opinion in our Court of Appeal, *Price Waterhouse* v *Kwan* and *Turton* v *Kerslake* represent a fundamental and ultimately irreconcilable conflict in two established lines of authority.

The conventional New Zealand approach

A duty of care in respect of negligent misstatements originated in the House of Lords decision in *Hedley Byrne* v *Heller*. As noted earlier, liability in that case was based on the plaintiff establishing the *Hedley Byrne* criteria. If a plaintiff were unable to establish these requirements, no duty of care would be recognised. The *Hedley Byrne* criteria were the exclusive determinates of liability. The conventional New Zealand approach to the duty question, however, is derived from the decision in *Anns*. The two stage test suggested by Lord Wilberforce in that case is now so well known that it does not bear repeating, but it should be recognised that it was intended as a general statement of the approach to the duty question. It encompassed all negligence claims including claims for negligent misstatement. Under that test, the *Hedley Byrne* criteria were treated as simply policy reasons that may negate a prima facie duty of care.[40] In contrast to the approach in *Hedley Byrne* v *Heller*, the presence or otherwise of these factors under the two stage test of *Anns* would not finally determine the duty question.

Following the decision in *Anns*, the New Zealand Court of Appeal was initially enthusiastic in adopting this two stage 'test', and in particular in cases involving claims of negligent misstatement.[41] Although there was some support for the idea that proximity was satisfied by mere foreseeability,[42] the Court was generally prepared to consider a range of factors at each stage of the test.[43] But, consistent

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39 [1978] AC 728 [*Anns*].

40 Ibid at 752.

41 For example, *Scott Group* v *MacFarlane* [1978] 1 NZLR 553; *Allied Finance and Investments Ltd* v *Haddow & Co* [1983] NZLR 22; *Meates* v *AG* [1983] NZLR 308.

42 See *Scott Group* v *MacFarlane*, ibid at 574 per Woodhouse J; *Gartside* v *Sheffield, Young & Ellis* [1983] NZLR 37 at 47 per Richardson J; *New Zealand Social Credit Political League* v *O'Brien* [1984] 1 NZLR 84 at 97 per Casey J.

43 *Allied Finance* v *Haddow* [1983] NZLR 22 at 30 per Richardson J, at 34-35 per McMullin J; *Meates* v *AG* [1983] NZLR 308 at 334 per Woodhouse P & Ongley J.

with *Anns*, the *Hedley Byrne* criteria were at best only factors to be considered. While their presence could lead to the recognition of a duty of care,[44] a failure to establish these criteria did not mean that the plaintiff's claim must necessarily fail. They were not necessary elements of liability.[45] The *Anns* two stage test was seen as subsuming within it the *Hedley Byrne* criteria,[46] and was expressly recognised as offering a more general and broader test of liability than the narrower approach of *Hedley Byrne* v *Heller*.[47] The dominant and only necessary consideration for a duty of care was forseeability of harm to the plaintiff.[48]

However, from at least the mid-eighties, the Court of Appeal started to move away from a strict application of this two stage test towards the modified *Anns* approach that we now recognise. Relying on the decision of the House of Lords in *Governors of the Peabody Donation Fund* v *Sir Lindsay Parkinson & Co Ltd*,[49] the Court started to focus on what it saw as the overriding standard of whether it was just and reasonable to impose a duty of care.[50] The 'tests' of proximity and policy came to be treated as simply guides to determining this question. Yet this change in emphasis was neither immediate nor universal. Some members rejected the just and reasonable standard as imposing any limit on the breadth of liability set out in *Anns*.[51] Others simply treated just and reasonable as a factor to be taken into account in assessing the proximity question.[52] Others deliberately chose to avoid the question.[53] It was not until the decision in *South Pacific Manufacturing*, and in particular the judgment of Richardson J, that this approach could claim the general support of the Court of Appeal. That case concerned claims of negligent misstatement against fire investigators who had stated that fires in the insured's premises had been caused by arson. Richardson J described the approach to be taken to the duty of care in the following terms:[54]

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44 For example, *Allied Finance* v *Haddow*, ibid.

45 *Gartside* v *Sheffield, Young & Ellis* [1983] NZLR 37 at 53 per McMullin J.

46 *Allied Finance* v *Haddow* [1983] NZLR 22 at 29 per Richardson J.

47 *Meates* v *AG* [1983] NZLR 308 at 334 per Woodhouse P & Ongley J; *Gartside* v *Sheffield, Young & Ellis* [1983] NZLR 37 at 46 per Richardson J.

48 The best example of this is the decision in *Gartside* v *Sheffield, Young & Ellis*, ibid.

49 [1984] 3 All ER 529.

50 The most important judgment in this regard was that of Cooke P in *Brown* v *Heathcote County Council* [1986] 1 NZLR 76 at 79. This approach was broadly similar to that adopted by Richardson P in the *South Pacific Manufacturing* case. See infra note 54. The judgment of Cooke P was described as "useful" by the Privy Council in the appeal in that case; [1987] 1 NZLR 720 at 725 per Lord Templemann. It was also approved or at least applied in a number of other cases. See *Craig* v *East Coast Bays City Council* [1986] 1 NZLR 99 at 106–107 per Tompkins J; *Williams* v *AG* [1990] 1 NZLR 646 at 687 per Casey J, at 692 per Bisson J. However, it is of note that in the case itself, at 83, the other members of the Court limited their agreement to "the facts of this case and the legal issues involved".

51 *Takaro Properties Ltd* v *Rowling* [1986] 1 NZLR 22 at 57 per Woodhouse J, a judgment with which Richardson J agreed.

52 *Steiller* v *Porirua City Council* [1986] 1 NZLR 84 at 95 per Tompkins J.

53 *Takaro Properties* v *Rowling* [1986] 1 NZLR 22 at 71 per McMullin J, at 73 per Somers J.

54 [1992] 2 NZLR 282 at 305-306.

> The ultimate question is whether in light of all the circumstances of the case it is just and reasonable that a duty of care of broad scope is incumbent on the defendant . . . It is an intensely pragmatic question requiring most careful analysis. It has fallen for consideration in numerous cases in this Court over recent years and, drawing on *Anns* v *Merton London Borough Council*, we have found it helpful to focus on two broad fields of inquiry. The first is the degree of proximity or relationship between the alleged wrongdoer and the person who has suffered damage. This is not of course a simple question of forseeability as between parties. It involves consideration of the degree of analogy with cases in which duties are already established and . . . reflects an assessment of competing moral claims. The second is whether there are other policy considerations which tend to negative or restrict – or strengthen the existence of – a duty in that class of case.

Since that decision, this approach has been consistently approved by the Court of Appeal as the approach in New Zealand to the duty question.[55] In particular, it has been consistently applied to claims of negligent misstatement. Excluding *South Pacific Manufacturing* itself, it has been used in a claim against a solicitor for negligently certifying that the effect of a matrimonial property agreement had been fully explained to his client,[56] to the Comptroller of Customs in respect of the provision of advice regarding tariffs,[57] and in resolving a claim by the birth mother of an adopted child for misrepresentations concerning the adoption process.[58]

Two things must be noted about the conventional approach from this brief review. First, the conventional approach has always claimed to be a general test of liability, one that purports to apply and has been applied to all duty questions including claims for negligent misstatement. Second, in being applied to claims of negligent misstatement, it has always been treated as a potentially broader approach to the duty question than one based on the *Hedley Byrne* criteria. While a plaintiff who is able to satisfy the *Hedley Byrne* criteria will generally be able to establish a duty of care,[59] a failure to satisfy those criteria will not necessarily resolve the duty question. As was the case in *Price Waterhouse* v *Kwan*, plaintiffs have repeatedly succeeded in cases of apparent negligent misstatement where they have been unable to satisfy the *Hedley Byrne* criteria.[60]

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55 For example *Connell* v *Odlum* [1993] 2 NZLR 527 at 535 per Thomas J; *Kavanagh* v *Continental Shelf Company (No 46) Ltd* [1993] 2 NZLR 648 at 654 per Hardie Boys J; *Wilson & Horton* v *AG* [1997] 2 NZLR 513 at 520 per Hammond J; *Morrison* v *Upper Hutt City Council* [1998] 2 NZLR 331 at 336 per Richardson P; *Riddell* v *Porteous* [1999] 1 NZLR 1 at 9 per Blanchard J; *B* v *Attorney General* [1999] 2 NZLR 290 at 300–301 per Keith & Blanchard JJ. Two of the important restatements of this rule are by Richardson J in *Fleming* v *Securities Commission* [1995] 2 NZLR 514 at 526-527 and *AG* v *Prince* [1998] 1 NZLR 262 at 268.

56 *Connell* v *Odlum*, ibid.

57 *Comptroller of Customs* v *Martin Square Motors* [1993] 3 NZLR 289.

58 *AG* v *Prince* [1998] 1 NZLR 262.

59 See for example *Allied Finance* v *Haddow* [1983] NZLR 22; *Matua Finance Ltd* v *KPMG Peat Marwick & Ors* unreported, Court of Appeal, 25 May 1994, CA 179/93.

60 For example *Scott Group* v *MacFarlane* [1978] 1 NZR 553. Even in those cases where the plaintiff has failed to satisfy the *Hedley Byrne* criteria and no duty of care has been recognised, the decisions have referred to the lack of any other considerations to support a duty of care. For example, *Cooper Henderson Finance Ltd* v *Colonial*

Given the context of the decisions in *Price Waterhouse* v *Kwan* and *Turton* v *Kerslake*, we should also consider how the conventional approach to the duty question has dealt with the problem of a "contractual matrix". Generally, this has been considered as a policy reason which may negate the existence of a duty of care.[61] A good illustration of this is the judgment of Richardson J in the *South Pacific Manufacturing* decision itself, where the contractual relations between the insured and insurer, and between the insurer and the investigator were held to negate any duty of care between the investigator and the insured. If the contract did not provide such a remedy, then they should not be allowed "greater recovery through tort than they were prepared to pay for in contract".[62] However, it is clear that a contractual matrix is only a factor to be considered, and is certainly capable of being outweighed by other factors. The important consideration appears to be whether reliance on the contractual relations is likely to provide the plaintiff with an effective remedy, a concern which in a number of cases appears to encompass the inability to recover as a result of insolvency.[63]

Against this background, the decision in *Price Waterhouse* v *Kwan* can be seen as representing and being supported by the conventional approach to the duty question that has developed in New Zealand over the last 20 years. The two stage approach used by the Court, while possibly not entirely consistent with the recent reluctance to talk in terms of prima facie duties and negating considerations of policy, certainly is consistent with the spirit of that approach. Likewise, the fact that the clients' contractual remedy against their solicitor was unlikely to result in any compensation is a consideration that has been taken into account by the Court in determining the relevance of the contractual matrix. While the result in the case may owe more to the period immediately following *Anns*, where foreseeability of harm was the overriding consideration,[64] it is

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Mutual General Insurance Co Ltd [1990] 1 NZLR 1; *Trevor Ivory* v *Anderson* [1992] 2 NZLR 517.

61 See for example *Gartside* v *Sheffield, Young & Ellis* [1983] NZLR 37 at 49 per Richardson J; *Stieller* v *Porirua City Council* [1986] 1 NZLR 84 at 96 per McMullin J; *Cooper Henderson Finance* v *Colonial Mutual General Insurance*, ibid at 3 per Cooke P; *South Pacific Manufacturing* [1992] 2 NZLR 282 at 308 per Richardson J, at 319 per Hardie Boys J; *Kavanagh* v *Continental Shelf Company* [1993] 2 NZLR 648 at 652 per Richardson J, at 654 per Hardie Boys J.

62 Ibid at 308. Other good examples of the Court giving weight to the existence of contractual remedies as a reason not to recognise a duty of care are *Cooper Henderson Finance* v *Colonial Mutual General Insurance*, ibid, and *Kavanagh* v *Continental Shelf Company*, ibid.

63 For example, in cases involving the construction of residential houses, the inability of a small building firm to meet a judgment has been an important consideration in imposing a duty of care on a council. See *Invercargill City Council* v *Hamlin* [1994] 3 NZLR 513. Likewise, in *South Pacific Manufacturing*, [1992] 2 NZLR 282 at 309, Richardson J recognised that if reliance on the contractual structure is likely to leave the loss remaining with the injured party, "it may be reasonable to focus particularly on the respective moral claims of one as against the other". Contrast this, however, with the approach of Hardie Boys J in *Kavanagh* v *Continental Shelf Company*, ibid at 654 where he stated that the addition of a tortious duty of care to an existing contractual duty may give "a greater chance of recovery, but if that be so ... it is a fortuitous matter, hardly relevant to the principle".

64 See supra note 42.

certainly not a decision that could be described as contrary to the established, conventional approach of the New Zealand Court of Appeal to duty questions.

An alternative approach?

The same cannot be said for the decision in *Turton v Kerslake*. As we have seen, the Court in that case expressly rejected any concept of a two stage approach to determining duties of care, and in particular the notion of a prima facie duty cut back by policy considerations. Its focus instead was on the relationship between the two parties, understood almost exclusively by reference to the *Hedley Byrne* criteria. With this focus, the contractual structure the parties had assumed was the very context within which that relationship must be considered, rather than a policy reason that may negate a prima facie duty of care.

Yet *Turton* v *Kerslake* is representative of a growing number of Court of Appeal decisions where the Court has apparently rejected the conventional approach to the duty question set out in *South Pacific Manufacturing*, and adopted a more limited approach focused on the relationship between the parties understood in terms of the *Hedley Byrne* criteria. One important example, with some similarities to the decision in *Price Waterhouse* v *Kwan*, is the decision in *Boyd Knight* v *Purdue*.[65] Boyd Knight was the auditor of a finance company, Burbery. Burbery issued a prospectus for an offer of securities to the public, and that prospectus contained a report by Boyd Knight that the financial statements of the company gave a true and fair view of its affairs. Boyd Knight negligently failed to detect serious frauds that had been committed by a director of the company. Investors in Burbery who had lost money as a result of their investment sued Boyd Knight for their losses. Boyd Knight admitted that had those frauds been detected, the audit report would not have been given and the prospectus would not have been issued. Somewhat unusually, however, the plaintiffs claimed that they had not read the audit report or accounts for the company before making their decision to invest. They argued that they were entitled to rely on the general integrity of the audit regime to ensure that inaccurate prospectuses were not issued. Had the auditor exercised reasonable care, the prospectus would not have been issued, and the plaintiffs would not have had the opportunity to incur the loss.

The Court approached the duty question by an application of the *Hedley Byrne* criteria. The Court held that the auditor could not in the circumstances be taken to have assumed a responsibility to people who did not read the accounts they had certified. For the plaintiffs to establish a duty of care it was necessary for them to show that they specifically relied on the accounts. It was not enough for the plaintiffs to say that they relied in a general way on the statutory scheme for their protection. To emphasise the difference in approach taken by the Court to that of the conventional approach it is of interest to note that Blanchard J approves the *dissent* of Richmond P in *Scott Group* v *MacFarlane*,[66] which involved a strict application of the *Hedley Byrne* criteria, and makes no reference to the approach of the *majority* in that case, which is one of the foundational decisions in the development of the conventional approach.

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65 [1999] 2 NZLR 278.

66 [1978] 1 NZLR 553.

This reliance on the *Hedley Byrne* criteria is also seen in a number of other cases recently decided by the Court of Appeal. In *Brownie Wills* v *Shrimpton*,[67] Gault and Blanchard JJ, delivering a joint judgment, went as far as to state that "[A] plaintiff who sues in tort alleging economic loss arising from negligent advice given to the plaintiff ... needs to prove actual reliance upon the defendant's advice ... Whether that was so in turn depends upon whether the reliance was induced by the conduct of the defendant in assuming or appearing to assume responsibility for advising the plaintiff. Foreseeable reliance is thus an element in proximity."[68] Likewise in *McKay Hill* v *Eksteen*, the claim of a non-client against a solicitor failed simply because the plaintiff was unable to establish an assumption of responsibility.

What is important in these cases is that the *Hedley Byrne* criteria appear to be treated as necessary requirements for the establishment of a duty of care, rather than considerations that help answer the ultimate question of whether it is fair, just and reasonable to recognise a duty. Their presence or otherwise appears to be determinative of the duty question. And in taking this approach, the cases make almost no reference to the conventional approach outlined in *South Pacific Manufacturing*. Indeed, as *Turton* v *Kerslake* makes clear, the cases appear to represent a deliberate decision not to use that two stage approach.

Summary

The two lines of authority represented by the decisions in *Price Waterhouse* v *Kwan* and *Turton* v *Kerslake* create real problems in predicting how the Court of Appeal will respond to a case involving a claim of negligent misstatement. Two approaches seem to be available to the Court, but there is no guidance on which approach will be favoured. Further, it does seem to matter which approach is taken. If the plaintiffs in *Price Waterhouse* v *Kwan* had been required to satisfy the *Hedley Byrne* criteria, and in particular reliance, it seems clear that their claim would have failed. Indeed this was conceded by the plaintiffs in argument at first instance.[69] Likewise, had *Turton* v *Kerslake* been resolved by use of the conventional approach, there was at least the strong possibility of a different result. The dissent of Thomas J illustrates this. For first instance judges, practitioners advising clients, and even academics teaching students, there appears to be a fundamental uncertainty in how the Court will approach such cases.

IV Can the Decisions be Reconciled?

The final question I wish to consider is whether this apparent conflict in approach, represented by the decisions in *Price Waterhouse* v *Kwan* and *Turton* v *Kerslake*, can be reconciled by reference to a principled distinction between the two cases. The difficulty with this is that the Court of Appeal has not clearly recognised this difference in approach, let alone suggested how the difference may be resolved. However, the lines of argument that may be made can be

67 [1998] 2 NZLR 320.

68 Ibid at 324.

69 *Kwan* v *Price Waterhouse* unreported, High Court, Wellington, 19 March 1999, CP 214/98 & CP 188/98, Master Thomson at 9.

detected in the decisions. The first possible claim is that *Price Waterhouse* v *Kwan*, and other similar cases, are not cases of negligent misstatement at all, but rather cases where a defendant failed to exercise a protective power they held for the benefit of the plaintiff. A second possibility is to suggest that *Price Waterhouse* v *Kwan*, unlike *Turton* v *Kerslake*, did not involve a true contractual matrix situation. A third argument is that *Turton* v *Kerslake*, unlike *Price Waterhouse* v *Kwan*, is a case involving sophisticated commercial parties who are able to look after themselves. Ultimately I conclude than none of these arguments fully explains the conflicting approaches taken to the duty question in cases of negligent misstatement. The uncertainty considered in this article is real and can only be resolved by the Court directly confronting the conflict.

Claim 1 - Price Waterhouse *v* Kwan *is not a case of negligent misstatement*

The first argument that might be made is that *Price Waterhouse* v *Kwan* is not a 'true' case of negligent misstatement. 'True' negligent misstatement cases are those where the plaintiff alleges that it suffered loss as a result of relying on a statement (or possibly silence when there was a duty to speak) made by the defendant. Those cases are properly resolved by an application of the *Hedley Byrne* criteria. *Price Waterhouse* v *Kwan*, however, involved a failure by the defendant to exercise powers that it held for the purpose of protecting the interests of the plaintiff. The nature of those powers, and the strong foreseeability of loss to the plaintiff if those powers were not properly exercised, were sufficient to create a relationship of proximity and, in the absence of any countervailing policy considerations, a duty of care. The breach of that duty lay in the negligent conduct of the audit by the auditor, which caused loss to the clients because it meant that the Law Society did not intervene to prevent any further loss. This formulation of the duty, in contrast to one formulated in terms of a negligent misstatement, was expressly adopted by the High Court,[70] and seems largely to underlie the approach in the Court of Appeal.

Similar arguments have been made, and accepted, in other cases.[71] So, for example, in residential building negligence cases, the liability of a local authority to subsequent owners is not based on any implied statement to the owner by the council that the construction of the building complied with the relevant by-laws, a statement on which they relied in purchasing the house.[72] Rather, liability arises from the element of control,[73] the general reliance placed on the local authority by home owners[74] and the foreseeability of the loss to a subsequent purchaser. Likewise in *Christensen* v *Scott*,[75] the Court held that it was arguable that a solicitor and financial adviser owed a duty to protect the personal interests of shareholding directors in a company to which they had provided professional advice. The basis of the duty was that the advisers had over the years acted for

70 Ibid at 10.

71 See J Smillie, "Certainty and Civil Obligation" (2000) 9 OLR 633 at 649.

72 *Mt Albert City* v *NZMC Insurance Co Ltd* [1983] NZLR 190 at 196 per Cooke J.

73 Idem.

74 *Brown* v *Heathcote County Council* [1987] 1 NZLR 720 (PC) at 726 per Lord Templeman; *Invercargill City Council* v *Hamlin* [1994] 3 NZLR 513, aff'd [1996] 1 NZLR 513 (PC).

75 [1996] 1 NZLR 273.

the shareholders in a personal capacity, giving rise to a general duty on their part to look after and protect their interests.[76]

This argument has a number of difficulties when applied to a case like *Price Waterhouse* v *Kwan*, and in particular a case where apart from any other claim that might be brought against the defendant, a 'true' negligent misstatement claim could be made by another party. Regardless of any claim the clients might have, it is clear that the Law Society would have a claim against the auditor either if sued by the client for failing to exercise its powers of intervention, or even if suing on its own behalf to recover the cost of payments made out of the Fidelity Fund,[77] or the cost and expense of an investigation. That claim would probably be for either the auditor's negligence in its report to the Law Society, most likely in certifying that the solicitor had complied with the regulations concerning the operation of a nominee company,[78] or in failing to report "forthwith" to the Law Society any relevant matter.[79] Such a claim would clearly be a 'true' negligent claim, and on this argument resolved by reference to the *Hedley Byrne* criteria. There would then arise the anomalous situation whereby the claim by the Law Society, with whom the auditor had the most proximate relationship (being the party to whom the statement was made), would be resolved by reference to the *Hedley Byrne* criteria, while a claim by the client, with whom there was a more distant proximate relationship, would be resolved by reference to the potentially more beneficial conventional approach.

This anomaly simply illustrates the artificiality of the analysis of the duty which this approach suggests, and which was taken in *Price Waterhouse* v *Kwan*. It is an analysis that attempts to separate the duty question from the question of the loss in respect of which that duty was owed.[80] The auditor did not cause money to be lost from the solicitors' trust account. The fact it has carried out an audit does not change the amount of money that is or is not in that account. All the auditor can do is report the matter to the Law Society who may choose to investigate and intervene to prevent further losses occurring. The only loss that the client can suffer as a result of negligence on the part of the auditor is the loss of an opportunity for the Law Society to intervene, and the only duty of care that corresponds to that loss is a duty on the auditor to promptly and accurately report to the Law Society. That is a 'true' claim of negligent misstatement.

Second, to say that the conventional approach does not apply to 'true' claims of negligent misstatement would require not just a revision of the history of the

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76 See also *Delloitte Haskins & Sells* v *National Mutual Life Nominees* (1991) 3 NZBLC 102,259, rev'd [1993] 3 NZLR 1 (PC); the judgment of Cooke P in *Fleming* v *Securities Commission* [1995] 2 NZLR 514; *Comptroller of Customs* v *Martin Square Motors* [1993] 3 NZLR 289.

77 That is, the Solicitor's Fidelity Guarantee Fund. See Part IX Law Practitioners Act 1982.

78 For the form of the audit report, see the *Audit Regulations*, schedule 2.

79 *Audit Regulations*, reg 54.

80 On the importance of considering the duty question by reference to the type of loss suffered see *The Wagon Mound (No 1)* [1961] AC 388 (PC); *Caparo Industries Plc* v *Dickman* [1990] 2 AC 605 (HL); *South Australian Asset Management Corp* v *York Montague Ltd* [1997] AC 191 (HL); *Bank of New Zealand* v *New Zealand Guardian Trust Co Ltd* [1999] 1 NZLR 664; *Boyd Knight* v *Purdue* [1999] 2 NZLR 278.

development of the duty of care in New Zealand, but a complete rejection of it. The conventional approach has always been used as an approach to 'true' cases of negligent misstatement.[81] In fact, it largely grew out of a concern that the *Hedley Byrne* factors were too narrow an approach to take in such cases.[82] For example, in *Scott Group* v *MacFarlane*, as the minority judgment of Richmond P makes clear, although the plaintiff clearly relied on the audit, it was not able to satisfy the *Hedley Byrne* factors, as the defendant was not aware of the use that would be made of the information and the reliance by the plaintiff. In spite of this, the majority still recognised a duty of care based on an earlier version of the conventional approach. It would be disingenuous in the extreme to suggest that the conventional approach does not apply to cases where a plaintiff relies on a statement by a defendant.

Claim 2 - Price Waterhouse *v* Kwan *did not involve a 'contractual matrix'*

A second argument that might be made is that an approach based on the *Hedley Byrne* factors is only appropriate in cases involving a "contractual matrix" and that *Price Waterhouse* v *Kwan* is not such a case. It may be that this does operate as a point of distinction between the two cases.[83] *Price Waterhouse* v *Kwan* is not the classic situation in which an argument of deference to a contractual matrix is usually made. The auditor carried out the audit under a detailed regulatory scheme and primarily for the benefit of the Law Society, a party with whom it did not have any contractual relationship. The majority of its obligations were derived from that regulatory scheme rather than voluntarily assumed contractual rights. Indeed, the strength of those regulatory obligations are such that it has even been doubted that there is a contractual relationship with the solicitor who pays the auditor.[84] This can be contrasted with the clear contractual structure that existed in *Turton* v *Kerslake.* Each party had to a large extent defined their rights and obligations by contract; the engineer with the architects, the architects with the Board, the Board with the contractor, and the contractor with its subcontractor.

Yet even if this were a legitimate point of distinction between the two cases, it would not provide a comprehensive explanation of the difference in approach in the lines of authority each case represents. As noted above, the conventional approach has always treated the existence of a contractual matrix as simply a factor to be taken into account in the policy inquiry.[85] In cases similar to *Turton* v *Kerslake*, where there was a clear contractual matrix, it has not been used to determine the proximity of the relationship between the parties.[86] Nor has it

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81 See supra notes 41 and 56-58.

82 See supra notes 46-47.

83 Although it would only be a distinction based on the facts of each case. In a situation where there is no allegation of a breach of a statutory duty, it is not clear that a statutory matrix should be treated any differently from a contractual matrix. Both are intended to achieve the same function of assigning responsibilities and allocating risks between the parties.

84 *Stringer* v *Peat Marwick Mitchell & Co* [2000] 1 NZLR 450 (HC) at 460 per Chisholm J.

85 See infra notes 61 to 62 and accompanying text.

86 For example, *South Pacific Manufacturing* [1992] 2 NZLR 282.

been treated as a reason for or against adopting a particular approach to the duty question.[87] Likewise, in decisions which, like *Turton* v *Kerslake,* have applied the *Hedley Byrne* criteria, there have not been arguments that the contractual matrix between the parties negates a duty of care. So while a distinction between cases that do involve a "contractual matrix" and cases that do not may help explain the result in *Price Waterhouse* v *Kwan*, such a distinction does not explain the divergence in the lines of authorities each case represents.

Claim 3 - Turton *v* Kerslake *involved a claim by a sophisticated commercial party*

A third possible argument is that *Turton* v *Kerslake,* and other similar cases, involved claims by sophisticated commercial parties who were able to look after themselves. In those circumstances, it may be appropriate to base their liability on the *Hedley Byrne* criteria. By contrast, it would be argued that the plaintiffs in *Price Waterhouse v Kwan* and other similar cases were not sophisticated commercial parties and require the additional protections and flexibility that may be offered by the conventional approach.

This argument is very much the other side of that considered under claim 1, except that rather than focusing on the nature of the powers of the defendant, it looks to the vulnerability of the plaintiff. And as those cases illustrate, there is no doubt that Courts do intervene to protect those who cannot reasonably be expected to protect themselves. It is also clear that those cases under the conventional approach that have placed the greatest reliance on the *Hedley Byrne* criteria have been cases involving large commercial enterprises. For example, in *Cooper Henderson Finances* v *Colonial General Insurance*[88] a claim by a finance company with security over a car belonging to a third party, against the insurer for failing to advise them that the insurance had lapsed was resolved substantially by reference to the *Hedley Byrne* criteria, although under the framework of the conventional approach.[89]

But this exception again does not explain the difference in the lines of authority we have discussed. Taking the position of the clients in *Price Waterhouse* v *Kwan*, it is not at all clear that investors in a solicitor's nominee company deserve any special treatment or protection from the court. For the large part, one would expect that they are reasonably sophisticated commercial investors, enjoying higher than market rates of return, and assuming some commercial risk in response. But even if they were worthy of some protection, many of the cases that have applied the conventional approach have been cases involving clearly sophisticated commercial parties. For example, in *Scott Group* v *MacFarlane*,[90] the plaintiff was mounting a takeover of a company worth approximately one million dollars. At the same time, many of the cases that have applied the *Hedley Byrne* criteria have involved parties that were clearly not sophisticated

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87 See infra note notes 61 to 62 and accompanying text.

88 [1990] 1 NZLR 1.

89 See also *Trevor Ivory Ltd* v *Anderson* [1992] 2 NZLR 517 (CA); *Matua Finance Ltd* v *KPMG Peat Marwick & Ors*, unreported, Court of Appeal, 25 May 1994, CA 179/93.

90 [1978] 1 NZLR 553.

commercial operators. For example, the plaintiff in *McKay Hill* v *Eksteen*[91] was a new immigrant to the country who did not have the benefit of legal advice in entering into the transaction. Moreover, it was found he had placed some reliance at least on the solicitor. Yet his claim failed because the solicitors had not assumed a responsibility to him. Again, this argument does not explain the difference between these two approaches.

V Conclusion

In this article I have tried to emphasise a serious problem that exists with cases involving claims of negligent misstatement; the Court of Appeal is adopting two different approaches to similar cases in a way that does appear to influence the result. There is no clear basis on which we can predict the approach that will be taken in any particular case. The cynic might say that the approach will depend on the composition of the Court in a particular case, and the justices' enthusiasm for a particular view, although even this does not appear to be a reliable indicator.[92] There is no easy way out of this problem for the Court. As I have tried to argue, it is difficult to see how these two lines of authority can be reconciled. One would hope that if this uncertainty reflects a movement by the Court away from the conventional approach in cases of negligent misstatement, towards one based on the *Hedley Byrne* criteria, then the Court would acknowledge this change in direction and expressly recognise that many of its earlier decisions, so important in forming the conventional approach, are now no longer relevant. That would involve the Court sacrificing some of the flexibility in approach it has for so long championed. One suspects, however, that the response, when forthcoming, will be less clear cut.

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91 Unreported, Court of Appeal, 30 May 2000, CA 161/99.

92 For example Keith J sat in both *Price Waterhouse* v *Kwan*, and in the majority in *Turton* v *Kerslake*. For the differences in approach of Richardson J, see supra note 2. As well, compare the approach of Thomas J in *Connell* v *Odlum* [1993] 2 NZLR 527 to his dissent in *Turton* v *Kerslake*.