



Précis Paper

Equitable Contribution

Senior Counsel Marcus Pesman and Barrister Charles Alexander discuss the equitable doctrine of contribution, and a recent case in which the High Court clarified the notion of coordinate liabilities.

Discussion Includes

- What is the equitable doctrine of contribution?
- What happened in this case that led the High Court to consider the doctrine of contribution?
- What are "co-ordinate liabilities" in modern Australian law?
- How can the right to contribution be lost?
- When does the right to contribution arise?
- Joint debtors are sometimes arranged into "camps", where each camp should bear equal liability, rather than each debtor bearing equal liability.
- A deal between one joint debtor and a creditor leaves that joint debtor vulnerable to contribution claims – the only safe settlement with a creditor is one that also includes all other joint debtors.

Précis Paper

Equitable Contribution

1. In this edition of BenchTV, Marcus Pesman SC (Barrister) and Charles Alexander (Barrister) discuss the High Court (French CJ, Kiefel, Bell, Gageler & Keane JJ) decision of *Lavin v Toppi* [2015] HCA 4 which considered the issue of contributions in equity.
2. Mr Pesman SC led Mr Alexander in acting for the successful respondent, Toppi, in the High Court.

Background to the High Court Proceedings

3. Lavin and Toppi were friends and shareholders in a company called Luxe Studios. The company borrowed \$8 million from NAB, with Lavin and Toppi as guarantors, to build photographic studios. The business failed and NAB sought funds to discharge the debt owed.
4. Lavin settled with the bank on payment of part of the guaranteed debt, while the bank covenanted not to sue Lavin on the guarantee. Toppi later discharged the guarantee by paying the larger outstanding balance of the debt and claimed contribution from Lavin for half the difference of the sum each had paid.
5. Lavin resisted the claim for contribution on the basis that the parties were no longer governed by coordinate liabilities given the bank had covenanted not to sue Lavin.

Covenants Not to Sue

6. The utility of a covenant not to sue lies in the fact that it does not release liability, and therefore avoids the problem of the release of one co-surety operating as a release of all co-sureties.

Coordinate Liability

7. Mr Pesman SC argues that where parties have a common obligation and there is a loss, equity says they need to share the burden equally. The liabilities of the parties is said to be coordinate and where one party is required to discharge a disproportional share of the obligation, it may rely on claims of contribution in respect of payment in excess of their proportionate share of the debt.
8. In *Albion Insurance Co Ltd v Government Insurance Office of New South Wales* [1969] HCA 55; (1969) 121 CLR 342, Kitto J explained that it is a rule of natural justice that "persons who under

co-ordinate liabilities to make good the one loss (e.g. sureties liable to make good a failure to pay the one debt) must share the burden pro rata": [12] in *Toppi* NSWSC.

9. Lavin argued that there was no coordinate liability because the parties' obligations were different in that Toppi's liability was enforceable by the bank whereas Lavin's was not.

Toppi v Lavin [2013] NSWSC 1361

10. Rein J in the Supreme Court rejected this argument and ordered Lavin to pay \$750,000 in contribution to Toppi.
11. His Honour stated that he was bound by the earlier decision of the Court of Appeal of *Carr v Thomas* [2009] NSWCA 208. The Court in *Carr* concluded that contribution could be available between company directors who are sued for breaching director's duties and where one of the directors has the benefit of a covenant not to sue.
12. Rein J further observed at [17] that the result would have the benefit "of precluding one surety, with the assistance of the creditor, from being able to saddle other sureties with a disproportionate amount of liability." The principles of equitable contribution demand that creditors should not be able to choose their victim and Mr Pesman SC argues that "equity protects guarantors from the possibly arbitrary and capricious actions of the creditor."

Lavin v Toppi [2014] NSWCA 160

13. Lavin appealed to the Court of Appeal where Leeming JA (Macfarlan and Emmett JJA agreeing) found that the covenant to sue had no effect on the underlying liability and that the liabilities remain coordinate.
14. Leeming JA reconsidered the decision in *Carr v Thomas* by applying first principles and agreed with the court's decision. His Honour observed that a release evaporates a right to sue but a covenant actually confirms it, indicating the right to sue exists but that there is a promise annexed to it.
15. The judgment further explored the possible means of losing a right of contribution. For example, there can be a clause in a guarantee that specifically precludes contribution. Additionally, it is also possible to lose the right by disentitling conduct – for example, if a co-surety engages in conduct that has the effect of leaving the principal debtor with no assets such that it cannot pay its debts.

Lavin v Toppi [2015] HCA 4

16. On appeal, the High Court unanimously rejected Lavin's argument and concluded that a surety who pays more than its share of a guaranteed debt can recover contribution from a co-surety despite that co-surety having the benefit of a covenant not to sue from the creditor.
17. The bank's covenant had not extinguished Lavin's coordinate liability.
18. Further, the right to contribution is an equitable chose in action that vests not in the bank but in the co-sureties.
19. The High Court also explained that a claim for equitable contribution usually arises before the co-surety makes payment to the creditor. In *Lavin v Toppi*, the bank's call on the guarantees gave rise to an entitlement in equity to contribution. No action by Lavin or the bank thereafter could eschew this entitlement to contribution, not even the entry into the covenant not to sue.
20. Mr Alexander noted that Lavin and Toppi were not the only guarantors to the debt owing. He explained that it had been decided earlier in the procedural history that the relevant co-sureties were the Lavin camp and the Toppi camp and not the individual companies and spouses that were linked to each party. Mr Alexander considered this practical result to be an example of the courts in equity looking to substance and not form.

Implications

21. Mr Pesman SC argues that the case did not create any new law but emphasised that a covenant not to sue will not affect the liability of the co-sureties, as well as the essential natural justice requirement that they should share the liabilities equally.
22. The presenters observe that the same principle of contribution will apply in many other contexts including amongst joint tortfeasors and directors who breach director's duties.
23. Finally, the presenters highlight the practical take-away of *Lavin* is that: "when you are acting for one of many guarantors or co-sureties, the only safe settlement is an all in settlement."

BIOGRAPHY

Marcus Pesman SC

Marcus Pesman SC is a senior counsel who practices principally in equity, commercial and competition law at trial and appellate level. He also has significant experience in class actions. He is an occasional member of the Australian veterans fencing team, an activity he characterises as "Epee for the Elderly".

Charles Alexander

Charles Alexander has a general practice, with a background in equity and commercial matters. He also practises family law, specialising in family law matters that contain equitable causes of action. Charles is a lecturer in equity at Sydney University, where he also teaches a number of other law subjects.

BIBLIOGRAPHY

Focus Case

Lavin v Toppi [2015] HCA 4

Benchmark Link

http://benchmarkinc.com.au/newslettercms/webversion/benchmark_18-02-2015_weekly_civil_law_review.html

Judgment Link

<http://www.austlii.edu.au/au/cases/cth/HCA/2015/4.html>

Cases

Albion Insurance Co Ltd v Government Insurance Office of New South Wales [1969] HCA 55; (1969) 121 CLR 342

Burke v Lfot Pty Ltd [2002] HCA 17; 209 CLR 282

Caledonian Railway Co. v Colt (1860) 3 Macq 354

Carr v Thomas [2009] NSWCA 208

Legislation

Contracts Review Act 1980 (NSW)