



## Tipsheet 3 Proportionate Liability – What is it?

Client version  
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***What is proportionate liability, when does it apply and how does it impact on insurance policies and contracting by you?***

### What is it?

Proportionate liability legislation is applicable in every State and Territory in Australia<sup>1</sup>. It came about in response to the liability insurance crisis in 2001. Unfortunately the legislation is not uniform in every jurisdiction – this means there are slight differences.

Basically it enables the courts to apportion the responsibility for a damages claim amongst each wrongdoer according to the amount the court considers just. When doing this the court examines the extent to which each wrongdoer's actions contributed to the loss or damage.

In the past, each wrongdoer had joint and several liability with each other and a claimant had the option of suing any one person to claim 100% of their loss or damage. It was then up to those who had been sued to cross-claim or seek contribution from others who may have also been responsible for the claimant's loss or damage.

This meant the claimant could pursue the person with the 'deepest pockets' and that person would have to pursue everyone else who was responsible.

If any of the other people responsible were bankrupt or insolvent, the person with the 'deepest pockets' had to wear the loss.

Sometimes, a person might also assume 100% of liability under a contract. This is common in many commercial contracts whereby one party agrees to "indemnify" another for any loss caused by the actions of the first party. It also occurs for 'hold harmless' clauses.

For more information read Tipsheet 1 on "Indemnity Clauses – What are they? (Your broker can send you a copy of this tipsheet on request)

*Example: A construction project may have a number of professional consultants performing services in connection with the project. Before the proportionate liability legislation, developers would often contract with a project manager and pass 100% of the project risk to them in a contract.*

*The outcome was that if a claim for property damage due to negligence/defective work was brought against the developer, the project manager would be 100% accountable for the loss or damage even though the project manager's failure to review the work of the other consultant(s) was only a minor cause of the damage.*

*If an indemnity clause recognises proportionate liability and the court decides the project manager was responsible for only 10% of the loss/damage suffered by a claimant, the project manager will only be liable for 10% of the loss. The claimant has to sue all of the other wrongdoers to recover the share of the damage caused by them.*

### When does it apply?

Proportionate liability can apply in a broad range of commercial contracts for products and services including leases, software licences, service contracts, bills of lading, manufacturing contracts, maintenance agreements, security contracts, advertising agreements, transport contracts etc.

It applies to:

- "Apportionable claims" – which are:
  - A claim for damages relating to economic loss or property damage arising from a failure to take reasonable

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- care<sup>ii</sup>;
- A claim for damages arising from a breach of the State Fair Trading Act (except in Qld); or
- A claim for damages arising from a breach of certain Commonwealth legislation (eg misleading and deceptive conduct, director's duties, parts of the financial services legislation etc.);
- Where there are 2 or more concurrent wrongdoers; and
- The claim is for compensation, an indemnity or liquidated damages (eg a debt).

### When doesn't it apply?

Proportionate liability doesn't apply to:

- Negligence claims involving death or personal injury.
- Intentional or fraudulent damage - in such cases if one of the concurrent wrongdoers has intentionally or fraudulently caused damage, only that person will be liable (except in Victoria).
- Vicarious liability, agency and partnership liability.
- If the person has no duty of care owed to the claimant.
- Absolute or strict warranties or conditions in a contract – eg where one contracting party agrees to do something absolutely and is not agreeing to exercise 'reasonable care' when performing their services or supplying a product.
- 'Consumer transactions' in Qld.
- Claims for contractual liability where the parties to the contract have 'contracted out' of the legislation.

### What is 'contracting out'?

Parties to a contract can agree between them that the proportionate liability legislation will not apply. They can also agree to indemnify one another on a basis does not reflect proportionate liability principles. This is called 'contracting out'.

In NSW, Tasmania and WA, parties can 'contract out' of the legislation and exclude its operation.

However, in SA, ACT, NT, Victoria and the Commonwealth, it is arguable that parties are permitted to 'contract out' but this hasn't been

tested by the courts yet.<sup>iii</sup>

Only in Qld is it unlawful for a person to 'contract out' of proportionate liability. However it is still possible to avoid proportionate liability if the parties agree to an 'exclusion clause' that states that no duty of care is owed to the party being indemnified under the contract.

If the contract contains indemnity clause that does not reflect proportionate liability principles or does not preserve the operation of the legislation, the parties can be 'deemed' to have contracted out of the legislation. This can happen if for example, a party agrees it "*will be liable for the acts or omissions of its subcontractors or agents*".<sup>iv</sup> This type of obligation is very common in a commercial contract.

Other obligations and clauses in a contract where the parties can be taken to have "contracted out" of the legislation include warranties, guarantees, indemnities, releases, "hold harmless" clauses and obligations to maintain insurance.

Proportionate liability may not apply to alternative dispute resolution under a contract unless the parties expressly agree.<sup>v</sup>

Complications can also occur where the parties to a contract containing an indemnity clause are concurrent wrongdoers and one of them tries to recover the share of their liability from the other party.

In NSW, ACT, Queensland, Victoria and the Commonwealth, it is unlawful to seek contribution or indemnity from a concurrent wrongdoer. In NT, Tasmania, WA and SA contribution and indemnity between concurrent wrongdoers is permitted.

Because of the differences between the legislation in each State and Territory and the confusion it causes, the Standing Committee of the Attorney Generals has decided to introduce a Model Law which will apply across Australia. This work is still in progress.<sup>vi</sup>

### Who stands to benefit?

Both insurers and insureds benefit from the proportionate liability legislation. Insurers are in favour of it because it reduces the quantum of liability claims and assists them to more easily price liability insurance.

This is because insurers can take into account an

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insured's claims history and the inherent risks of their profession, business or trade and don't need to load the premium to take account of unknown liability for the incompetence or reckless behavior of others. This also assists to reduce premiums and making liability insurance more affordable.

Insureds benefit because they are only liable for their share of the loss or damage they caused and where some wrongdoers are insolvent or uninsured, the insured need not pay more than they are responsible for.

### What impact does it have on insurance policies?

Usually an insurance policy will exclude a claim where the insured has entered into a contract that changes their legal liability so it is different to what would have applied at law.

This is referred to as a 'contractual liability' or an 'assumed liability' exclusion. It is often found in professional indemnity and other legal liability policies.

Because the proportionate liability legislation is statute law, insurers will not deny a claim where the liability of the insured is apportioned in accordance with the legislation.

If the parties 'contract out' of the proportionate liability legislation, there is an argument that one party has agreed to assume greater liability to indemnify the other party in a way that is not consistent with their liability at law.

It is too early to predict how courts will view contractual indemnities.

A NSW case indicates that even if there is a contractual indemnity between two concurrent wrongdoers, the proportionate liability legislation may still override the indemnity so that a third party claim is treated as an 'apportionable claim'.<sup>vii</sup> This suggests that the contract needs to expressly state that the proportionate liability legislation does not apply (if the parties are allowed to 'contract out').

A more recent Tasmanian case has a completely different outcome. In that case, the contract<sup>viii</sup> did not expressly 'contract out' of the legislation. However the indemnity and other clauses in the contract did not reflect 'proportionate liability' principles so the court concluded the parties had

agreed to 'contract out' of the legislation.

It appears that the outcome depends very much on the clauses contained in the contract and the facts of each case.

If an insured agrees to 'contract out' this may trigger the 'contractual liability' exclusion. Although there have been no cases decided on whether an insurer can deny a claim on this basis, there is a risk that the insurer will not pay a claim if the insured has agreed to 'contract out' and this has extended their legal liability beyond what it would have been at law.

### How do you protect against this?

Until the courts test the operation of contractual liability exclusions and 'contracting out', a cautious approach should be taken.

Contributory negligence principles should be incorporated in any indemnity or 'hold harmless' clauses in contracts, or the contract should state that the liability of the parties is to be determined in accordance with the relevant proportionate liability legislation. Arbitration and alternative dispute resolution clauses should expressly refer to proportionate liability.

It may be necessary to re-negotiate indemnity, 'hold harmless' and other contract clauses for this purpose.<sup>ix</sup> If this is done, you can have greater confidence that your policy will respond to claims involving the liability risk relating to the provision of their work, services or goods.<sup>x</sup>

<sup>i</sup> Queensland – Civil Liability Act 2003 (Qld); New South Wales – Civil Liability Act 2002 (NSW); Victoria - Wrongs Act 1958 (Vic); Western Australia - Civil Liability Act 2002 (WA); Australian Capital Territory - Civil Law (Wrongs) Act 2002 (ACT); Northern Territory – Proportionate Liability Act 2005 (NT); South Australia – Law Reform (Contributory Negligence and Apportionment of Liability) Act 2001 (SA); Tasmania – Civil Liability Act 2002 (Tas); Commonwealth - Corporations Act 2001 (Cth); Trade Practices Act 1974 (Cth) and Australian Securities & Investments Commission (Cth).

<sup>ii</sup> In the Victorian case of *Wood v De Gabriele and Others* handed down on 15 June 2007, Justice Hollingworth found that there is an implied term in every contract for service that the party providing the services will exercise reasonable care and skill so it is arguable that the proportionate liability legislation applies to all claims relating to service contracts.

<sup>iii</sup> The proportionate liability legislation is under review by the Standing Committee of Attorney Generals. The proposal is to enact uniform proportionate liability laws in every State and Territory so the differences are eliminated. Contracting out of the legislation is an area where SCAG will seek consultation with the public once the "Model Law" has been drafted because there are arguments for and against 'contracting out' of the legislation.

<sup>iv</sup> In the Tasmanian case of *Aquagenics Pty Ltd v Break O'Day Council* [2010] TASFC 3, the Federal Court ruled that an indemnity clause

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under which the contractor agreed to be liable for damages suffered by the principal due to the acts or omissions of subcontractors operated as an agreement to 'contract out' of proportionate liability so no subcontractor could be treated as a concurrent wrongdoer.

<sup>v</sup> In the same Tasmanian case of *Aquagenics Pty Ltd v Break O'Day Council* [2010] TASFC 3, the court ruled that proportionate liability legislation did not apply to arbitration. The basis for this decision may have been due to the conclusion that the parties had 'contracted out' of the legislation. The SCAG is reviewing the legislation and is likely to change the laws to ensure that arbitration and alternative dispute resolution is subject to proportionate liability legislation.

<sup>vi</sup> At the meeting of Attorney Generals held in May 2010 they resolved to instruct the Parliamentary Counsel's Committee to draft model proportionate liability provisions and finalise them for public consultation. There no definite publication date yet.

<sup>vii</sup> In the NSW case of *Reinhold v New South Wales Lotteries Corporation* [2008] NSWSC 5, Justice Barrett ruled that the claim of a customer whose winning lottery ticket was cancelled by a newsagent and NSW Lotteries by mistake was an 'apportionable' claim even though NSW Lotteries and the newsagent had entered into an agency agreement which contained a different contractual indemnity.

<sup>viii</sup> The contract in question was an Australian Standard contract (AS4300-1995). Indemnity clauses in Australian Standard contracts are not consistent with proportionate liability legislation.

<sup>ix</sup> Don't assume that Australian Standard contracts are subject to proportionate liability legislation – these contracts need to be re-drafted to incorporate 'proportionate liability' principles.

<sup>x</sup>For an example of an indemnity clause with proportionate liability principles - see Tipsheet 1. Your broker can send you a copy of this tipsheet on request.

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